Working Paper

TOWARDS EFFECTIVE MANAGEMENT OF ECONOMIC RESTRUCTURING

By

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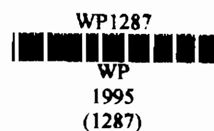

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TOWARDS EFFECTIVE MANAGEMENT OF ECONOMIC RESTRUCTURING

Abstract

Among developing countries there has been a widespread shift during the past decade from state control of the economy to deregulation and liberalisation. The World Bank has played a leading role in promoting this change. Evidence suggests that nearly as many developing countries have experienced a decline in growth rate as the number that has experienced improvement. There is, however, some evidence that substantial deregulation by relatively statist economies improves the growth rate, though there is no evidence of a monotonic relationship, positive or negative, between deregulation and improvement in growth rate. There is a wide variation in the economic response (as measured by growth rate) to liberalisation, not only overall but also in every major region. This suggests that not just the content of economic restructuring but its phasing and management may critically determine whether liberalisation yields positive or negative economic consequences. Several country cases indicate alternative modes of restructuring, and a critique is offered of the World Bank's structural adjustment programme in the light of these case studies and other research findings. The role of the state in economic liberalization is discussed and it is argued that appropriate phasing of economic restructuring and its management by the state may significantly improve the growth rate of the coconomy. It is argued that economic structuring is not just an economic but also a political and social process and must be anchored in a wider range of motives besides the economic motive, and attention must be paid to the effective management of not only the macro but also micro aspects of economic restructuring. In particular, the benefits of having dynamic professional managers head various organizational instrumentalities of restructuring are highlighted, as also the benefits of various innovations in governance. Several hypotheses on the successful decontrol of highly controlled developing economies are offered.

Introduction

This century has seen global swings from free market to state controlled economies and back again to free market economies. The Great Depression of 1929 was a major impetus to state interventionism in the Western economies. The devastation wrought by the second world war, the example of the rapid growth of the Soviet economic and military power in the forties and fifties, and the liberation from colonial rule or foreign hegemony of scores of poor countries with primitive infrastructures and industrial bases also in the forties and the fifties was the spur to central economic planning and an entrepreneurial and regulatory role of the state in fostering socio-economic development. But statism, too, did not work well. In the eighties the Soviet system collapsed and many developing countries experienced stagnation, high inflation, chronic balance of payments difficulties and the debt trap (World Bank, 1991, chapters 6 and 7). These economies had to resort to international funding agencies, most notably the World Bank and IMF, and also to financial assistance by the developed market economies, and these in turn pressured the beleaguered governments to deregulate and resile from statism. The questions explored by the paper are : Does deregulation work in lifting material living standards in poor, developing economies? If it does in the case of some economies but not in the case of some others, is this because the effective management of economic restructuring is a critical but neglected variable that determines whether deregulation works or not? What can be some dimensions of the effective management of deregulation oriented restructuring in developing countries?

The "Liberty" Agenda

The failure of the Soviet system has emboldened the proponents of the free market system. A "liberty" agenda has emerged that represents a wholesale retreat from most forms of state regulation (Heritage Foundation, 1995; Saran, 1995). It seems to take its inspiration from the tenets of conservative capitalism and neoclassical economic theory (Hoover and Plant, 1989). The governing principle seems to be that the state is a necessary evil, statism has messed up economic efficiency and lowered growth rates and therefore the less of state ownership or intervention the better. Further, a deregulated competitive market economy with the dominance of private ownership is a productive and efficient economy, so goes the argument, because private initiative in a competitive, free market economy would unleash the productive power of businessmen in producing efficiently the goods people want. Although not fully laissez-faire in its tenets, it does call for creating an enabling environment for free enterprise, decontrol of wages and prices, financial market liberalization, a fiscal policy that minimises fiscal deficits, keeps taxation at a moderate level, and eliminates subsidies except for the poorest, foreign exchange liberalization, free foreign investment, free flow of information, an anti-inflationary monetary policy, extensive privatization, and trade liberalization (see Table 1). If only the developing countries adopt the "liberty" agenda, all apparently would be well with their economies and they would grow prosperous in the shortest possible time. Besides, rapidly growing and accessible markets in the poor countries would catalyse exports of capital, technology, goods and services of the developed countries and boost their sluggish growth rates. The whole world would presumably become a better place.

(Table 1 about here)

This "liberty" agenda seems in part to be motivating the World Bank and International Monetary Fund in their efforts at restructuring statist economies that had earlier chosen the path of centrally planned and heavily state-controlled and "socialistic" economic development. Many of these economies did show fairly healthy growth rates during their experiment with central planning. For instance, Eastern Europe's economy grew at about 5% per year during 1965-1980 (World Bank, 1990, p.11, Table 1.2). But statist economies also ran into serious macro-economic problems such as persistent trade deficits, debt-trap, runaway inflation, a rampant and inefficient public sector, and looming or actual default in paying international dues (World Bank, 1991). Under financial duress many in the eighties and early nineties accepted the World Bank variety of "structural adjustment". The latter's principal mechanisms seem to be devaluation to decrease foreign trade deficit, a tight money policy and cuts in government subsidies and government expenditure to reduce the fiscal deficit and thereby rein in inflation, deregulation and trade liberalization, lowering of excessively high taxes to reduce tax evasion and stimulate savings and investment, better tax and financial administration, privatisation, easier entry for foreign private investment, increased investment in human capital (health and education) and in "infrastructure" (transport, communications, power), stronger institutions in financial and capital markets, a safety net for those adversely affected by structural adjustment, and land reforms aimed at giving ownership or tenancy rights to land tillers (Country Economics Department of World Bank, 1991). There is thus a substantial overlap between the structural adjustment promoted by the World Bank for developing countries and the "liberty" agenda, except that the liberty agenda represents a conservative face of capitalism and the Bank's structural adjustment a more caring one with greater concern for investment in human capital and safety net for those marginalized by a free market economy.

There has been an attempt to measure how far different economies are from the "liberty" recipe of economic restructuring for a free market economy (Heritage Foundation, 1995; Saran, 1995). Table 2 shows the Heritage Foundation assessment of how controlled several economies were around the mid-nineties in terms of some ten indicators of governmental control that could be measured or judged with some precision. These ten indicators were trade barriers, taxation, state intervention in the economy, monetary control, barriers to foreign investment, restrictions on banking, wage-price controls, restrictions on property rights, business regulations, and black market activities. For each of these, concrete measures were used to the extent possible (such as average import tariff or tax rate or inflation rate), or informed judgement, for scoring each indicator on a 5-point scale that went from one being very low government control in the country to 5 being very high control. The sample of 20 countries shown in Table 2 (Saran, 1995) consists of several major developing countries, the main newly industrialised countries, Russia as the chief representative of the former Soviet socialist empire, and leading developed economies.

(Table 2 about here)

The developed countries and the newly industrialised countries showed the greatest economic regulation related similarities not only within the group, but except for taxation, also between these two groups. In the group of developing countries, however, there was considerable variation along almost every one of the ten indicators of economic control. For example, while Mexico, Malaysia, and Thailand had moderate trade barriers, China, Indonesia, Pakistan, and India had very high trade barriers. The variation was even greater along the indicators of state intervention in the economy, monetary control, restrictions on property

rights, and black market operations. Thus, among developing countries there still seemed to be serious misgivings about economic decontrol and wholesale retreat from statism.

Economic growth rate, although not a be all and end all of economic development, remains a widely used measure of economic development for poor economies (World Bank, 1991). Besides, economic growth may yield a number of other bonuses, such as success of social projects (Kaufmann and Wang, 1995), less social disintegration (Klitgaard and Fedderke, 1995) and more civil liberties and political rights (Klitgaard and Fedderke, 1995; Savivides, 1995). A point of great interest for developing economies is therefore whether there is a monotonic relationship between how regulated the economy is and its growth rate, and whether it is positive or negative. If indeed there is a strong negative relationship, it would strengthen the arguments of free market economists within and outside the World Bank that statist economies must deregulate to attain greater economic development. If there is a positive relationship, their arguments would lose much force vis-a-vis poor countries in which rapid growth of output holds promise for lifting abysmally low living standards. At first blush there seems to be no correlation. Table 3 shows the overall government regulation score for an economy (computed by aggregating for each country its scores on 5-point scales for the 10 indicators of control mentioned earlier) and the annual average GDP growth rate of the economy during the 5 years 1989-1993 (World Bank, 1995). The freest of the economies (that is, with the lowest regulatory scores) were Hong Kong and Singapore, and indeed they had high growth rates. But China and Indonesia were amongst the most regulated economies and they also had high growth rates! Among the moderately controlled economies (scores in the twenties) too, some, like Malaysia and Thailand had very high growth rates while the US, Japan, and the OECD countries had rather low growth rates.

Even among the group of developing countries, the least regulated economy, Malaysia, had about the same growth rate as China, the second most regulated economy. And among the newly industrialised countries, despite a substantial difference in state control between Hong Kong and Singapore on the one hand and South Korea and Taiwan on the other, the growth rates were just about equal. It is clear, therefore, that across the full spectrum of economies in terms of levels of development, there is no relationship, positive or negative, between how deregulated an economy is and its growth rate.

(Table 3 about here)

A cross-sectional study, that too of economies at different levels of development, can, however, be misleading. A clearer picture may emerge if we look at the growth rate when an economy is at one level of state regulation and the growth rate when it moves to another level of state regulation. In the eighties, under Western and World Bank prodding a number of developing economies in Africa, Latin America, the former Soviet empire, and Asia undertook "structural adjustment", many of whose features were strikingly similar to the broad "liberty" agenda. In a 1990-1 study by the Centre for International Private Enterprise the pre-reform and post-reform degrees of freedom from state regulation were estimated by expert panels (Economic Reform Today, 1992). Nine key policy categories were used as indicators of deregulation. These were: trade liberalization, foreign exchange management, financial market liberalization, deregulation of wages and prices, prudent fiscal and monetary policy, privatization, free flow of foreign investment, free flow of information, and the existence of an "enabling" environment (for private enterprise). The overlaps with the "liberty" agenda and several of the World Bank's structural adjustment dimensions are

palpable. The nine policy categories were further disaggregated into 23 policy options, with greater weights to "powerful" policy options. The higher the aggregated score for an economy the closer was it judged to be to the "reform" ideal of a "free" economy. Column 1 in Table 4 shows the decile score (for scores ranging from 0 to 100) of economic deregulation of each economy before economic deregulation began (a decile score of 1 means score of up to 10, 2 means a score of 11-20, 3 means a score of 21-30 etc). Column 3 shows the economic deregulation decile score in 1990-1.

(Table 4 about here)

Market friendly economic restructuring in developing countries seems to have picked up sharply in the eighties. In a study of 93 developing countries, just about 80% of the structural adjustment loans given by the World bank to these countries during 1980 to 1986 were after 1982 (Faini, de Melo, Senhadji, and Stanton, 1991). These loans were given with conditionalities attached to them requiring deregulation. Thus, it is very likely that on the whole developing countries were more deregulated after 1982 than before it, and certainly after the mid-eighties. World Bank ordained economic restructuring was in full cry in many countries during the second half of the eighties, and even the great bastions of statism such as the countries of Eastern Europe and the erstwhile Soviet Union, as well as India, had embarked on it by the late eighties and early nineties. It can therefore be safely assumed that as a group, the developing countries during 1989 to 1993 were substantially more market friendly and had deregulated and opened up their economies substantially more compared to the period 1978 to 1982. A comparison of the growth rates during these two periods may therefore provide a useful indication of whether market friendly restructuring improves the

growth rate or not. Incidentally, the average annual growth rate for the world as a whole was 2.3% for 1978-1982, only slightly higher than the 1.8% per annum for 1989-1993 (the difference was even smaller for the high income countries which are the principal markets for many developing countries) (World Bank, 1995). Thus, any changes in the growth rates of the developing countries as a group between 1978-1982 and 1989-93 may only marginally have been influenced by changes in the global growth rates or in the growth rates of developed economies.

These estimates of economic freedom and growth rates were available for a sample of 29 developing countries (see Table 4). For each country, column 5 in Table 4 provides an estimate of the extent of movement towards economic liberalization from the pre-"reform" to the "reform" period (column 3 score minus column 1 score), and column 6 provides the percentage points change in average annual GDP rate between 1978-82 and 1989-93 (column 4 score minus column 2 score).

Column 6 of Table 4 indicates that out of 29 developing countries, 15 improved their growth rate during 1989-93 compared to 1978-82 while the growth rate deteriorated in 14 countries. In the 27 (out of 29) countries that had deregulated (score of at least 1 in column 5), the scores were 14-13, not very encouraging for those who swear by deregulation as an economic cure-all. If Peru, with an increase in market regulation and a deterioration in growth rate is considered as an example of the positive effect of deregulation, the score rises to 15-13. The picture is somewhat better if the 12 relatively high deregulators (scores of 3 and over in column 5) are compared with the 15 relatively low deregulators (scores of 1 and 2 in column 5). The average increase in growth rate for the dozen high deregulators was 1.2 percentage

points, while for the 15 low deregulators it was -1.2 percentage points. The difference is even less marked if Russia, a deregulator, with its huge decline in growth rate by 13 percentage points, is excluded. Nonetheless, eight out of 12 high deregulators improved their growth rate while only 6 out of 15 low deregulators increased theirs. Thus, while deregulation per se is just as likely to improve a developing country's growth rate as not, substantial deregulation is more likely to do so.

An interesting question is whether substantial deregulation in relatively statist economies yields better results than little deregulation in such economies. Out of a dozen economies with pre-"reform" deregulation scores of 4 or less (column 1 in Table 4) and increase in market deregulation score of 3 and above (column 5 in Table 4), 8 showed improvements in growth rate (column 6) while out of 7 economies with pre-reform scores of 4 or less and increase in market deregulation score of 2 or 1 only 3 showed an improved growth rate. Thus it is likely that substantial deregulation by relatively statist developing economies may more likely improve the growth rate than depress it. At the same time, further deregulation by already substantially deregulated developing economies may not yield much improvement in the growth rate. There were 7 economies that had pre-"reform" scores of 5 and over and had deregulated further. Only 3 improved their growth rate. Thus deregulation does not sustain growth monotonically. It is likely to catalyse growth under fairly restricted circumstances : substantial deregulation of relatively statist economies.

What is particularly striking about the data in Table 4 is the enormous variation in the growth rate response to "reform". As was noted earlier, in response to deregulation, roughly half showed improvement in growth rate and the other half deterioration. Even among the dozen

"high" deregulators, the change in growth rate ranged from -3.8 percentage points to 6.0 percentage points. Within regions also there was a lot of variation. The picture seemed clearest for the ex-socialist countries (decline in growth rate during or following deregulation), but even among these the decline ranged from -2.8 to -13.0 percentage points. For Asian countries also the picture was relatively clear - 6 out of 8 countries showed an improvement in growth rate along with or following deregulation; but here also the variation was not negligible, ranging from -2.4 to 3.2 percentage points. In the case of both Africa and Latin America the picture was very mixed. In Africa 5 out of 9 countries showed a decline in growth rate following deregulation, with a range of -4.7 to 6.0 percentage points, while in Latin America, excluding Peru, 5 economies showed improved growth rate and 3 decline, with a range of -3.8 to 4.6 percentage points. Such variation in the growth rate's response to deregulation begs probing.

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Country Cases on Economic Restructuring

Two economic restructuring attempts of recent years are worth comparing because both involved economic liberalization, both were attempted by very large countries and that too at about the same time, both were strongly influenced by the World Bank and the West, but the economic consequences of the two attempts, so far at least, have been dramatically different. These two are the Russian and the Indian ones, evolving during the eighties but begun in a big way in 1991. Table 5 summarises the Russian attempt at economic restructuring from a largely command economy to a relatively deregulated market economy. It also lists some of the observed economic consequences of this liberalisation (Amsden, 1993; Borodachev, 1993; Maital and Milner 1993). Table 6 shows in some detail (because more information was available) the Indian liberalization effort (Ministry of Finance, undated)

and Table 7 shows some of the economic consequences of Indian economic restructuring (Business India, 1995; Mani, 1995).

(Table 5 about here)

The contrasts in the economic consequences of economic restructuring away from a command economy and towards a deregulated market economy could not be sharper. The Russian economy has all but collapsed: there have been hyper inflation, negative growth rate, growing inequalities of income and social unrest, vast smuggling out of funds, and a catastrophic devaluation. The Indian economy, after a stall in 1991-2 and 1992-3, has bounced back to a healthy growth rate, exports have risen sharply, inflation has been contained, and after an initial significant devaluation of about 25% in 1991, further fall in the rupee has been modest despite the currency having substantially been converted into a floating exchange rate currency. The corporate economy is booming, both in the private and the public sector, and private foreign investment, a mere trickle earlier, is building towards a flood situation.

Why should the two attempts have fared so differently? Part of the reason may be that the Russian economy, in its earlier Soviet parentage, simply did not have the institutional infrastructure for a rapid conversion from a command economy to a market economy (Maital and Milner, 1993). It did not have modern banking, insurance, or telecommunications facilities in an appreciable degree, while India had developed it. It had a large class of bureaucrats, administrators, and technocrats, which India also had. But India had in addition an army of professional managers used to operating in at least a partially marketised economy, and a 2 million plus army of small, medium, and big entrepreneurs who could seize opportunities afforded by liberalization.

A second reason may be that for Russia liberalization, particularly privatization, became an ideological imperative in Russia's haste to dump its authoritarian and socialistic past and to get closer to its new found democratic Western allies (Maital and Milner, 1993). For India liberalization was a pragmatic adjustment to World Bank - IMF pressures, which it achieved without significant privatisation. Russian decision makers appear to have been egged on by their Western advisers to confound democracy with deregulation and privatisation, while India was already a democracy and had a strong public sector and there was no significant confounding of democracy with a privatised economy.

More importantly perhaps, the Russian effort seems, at least in hindsight, to have been impulsive, unplanned, and helter-skelter while the Indian effort, again in hindsight, appears to have been far better planned and phased. For instance Russia lifted wage and price controls too quickly, thus unleashing hyperinflation. It precipitously cut down defence production (thus badly hitting its industries and incomes of employees), embarked on a foolish form of privatisation that involved the distribution of vouchers to its citizens that entitled them to own worthless shares of public enterprises, did precious little to improve the quality of management of its enterprises by replacing bureaucrats and technocrats at their helm by professional managers, exposed 80000-odd Russian enterprises too quickly to greater international competition by removing or reducing foreign trade barriers when their managements had no clue how to operate in foreign markets or indeed to compete even in domestic markets, gave too little attention to modernising its infrastructure, devalued wildly, and on and on. The Russian government appears to have been naive in its faith in deregulation, the play of market forces, and the efficacy of privatisation, and wholly seems

to have mismanaged its liberalization adventure. What might have been fairly sensible decisions in due course turned out to have nightmarish consequences because of lack of proper timing or planning and phasing.

By contrast the Indian effort appears to have been far better managed and phased. There was virtually no privatization, and the limited divestiture of the shares of public enterprises was primarily to test waters and generate some funds to reduce the fiscal deficit. The devaluation of the rupee and its floating also was paced rather than precipitous. Industrial licensing, various reservations of industries in favour of the public sector and the small scale sector were dismantled gradually and this process is still going on. Inefficient public sector enterprises have been denied subsidies for their losses but again in a phased manner. The possibility of their being closed down if they do not improve their performance has also been made palpable in a phased manner. At the same time public enterprises have been given greater operating autonomy and freedom to raise equity or debt from the capital market. The government opened the gates to foreign private investment also in a phased manner. Most important, reduction in import tariffs has been gradual. In 1991, when economic restructuring began in a big way, the average import tariff was 150% and Indian industry thrived under this protective umbrella. This percentage was progressively brought down to an average tariff of 50% in 1995, thus giving Indian industry time to modernise, train its workforce, improve the quality of its products, improve its competitiveness, and so forth. Despite fairly large reduction in tariff protection, the Indian corporate sector increased its sales in 1995 over 1993 by over 40% and virtually doubled its profits (Business India, 1995; Chakravorty, 1995; Economic Times, 1995).

(Table 6 and 7 about here)

Several other country cases indicate that there is no single royal road to successful economic restructuring. Table 8 shows the economic restructuring efforts of three countries, Ghana (Economic Reform Today, 1992, p.21; Werlin, 1991), South Korea (Amsden, 1989; Economic Reform Today, 1992, p.12; Ranis, 1989), and China (Caiden, 1991, ch.10; Chow, 1991; Pei, 1994; Sandesara, 1995), along with some of the economic consequences of these efforts. The Ghana effort seems strongly to reflect the World Bank approach to economic restructuring. The South Korean effort, begun in the sixties, was built around rapid exports growth of manufactured goods led economic growth, an industrial policy that gave priority to the growth and development of select industries in which South Korea believed it had or could have an international competitive advantage, very close working relationship between the chaebol -Korean big business houses - and the government, starting of many public enterprises, and massive efforts at improving the infrastructure to support industrial growth (World Bank, 1993). Removal of import barriers was, by and large, a low priority, and so was privatisation and trade balance. It was only in the eighties, after nearly two decades of the restructuring effort, that South Korea began to open up its protected economy, privatise its public enterprises, deregulate its financial sector, etc. China did its economic restructuring also in a distinctive way. It first abandoned collectivization in agriculture and introduced a partially free market economy for agricultural products, invested heavily in industrial and technological modernization, local infrastructure development, training, and production growth. It experimented with the market economy and with small-scale private enterprises for several years as a learning strategy before opening its economy to massive foreign investment. Only after nearly a decade of experimentation with a market system did China instal such institutions of capitalism as stock exchanges, privately-owned enterprises, and the entry of foreign private investment. But the Chinese economy remains a highly statist,

protected economy. The effort seems to be to improve the management of public enterprises rather than privatize them. Rapid production increase, despite the inefficiencies this may entail in resource allocation, seems to remain a key goal of the Chinese economic strategy. Nor is there any deliberate strategy of fostering competition. But there is increasing resort to market mechanisms and enterprise autonomy for achieving growth.

(Table 8 about here)

Thus, Ghana, South Korea, and China represent three different and yet relatively successful attempts at restructuring. There is, therefore, no single recipe for successful economic restructuring for developing societies. A recipe approach is unlikely to work. Economic restructuring in developing countries has to be "managed", that is, choices have to be made about the pace and direction of economic restructuring, and about effective options in administering policy changes. Economic restructuring is a fairly lengthy process (Van der Hoeven, 1991). It requires large mind set changes initially in the political and economic elite and later in the masses. It requires the learning of very many relatively scarce competencies in developing societies, such as effective growth and competition management, effective management of technology, exports, and internationalisation. It requires the protection of infant industries until they mature and can hold their own against global competition. It requires the building up of infrastructure with strong externalities - transport, communications, energy, health, education, civic amenities and so forth - so that business initiatives can be successful. It requires at least some concessions to history, culture, ideology and sociology. It requires the careful management of a time of transition when expectations about achieving the sweet life far outrun the harsh realities of nation building. To ignore all these factors and simply rush into devaluation, privatization, reduction of tariff barriers, "tax reform", and deregulation, to satisfy the conditionalities imposed by

international financial institutions, is to raise the chances of failure of economic restructuring, as in the case of several countries in Eastern Europe, Africa, and Latin America.

The World Bank's Management of Economic Restructuring of Developing Societies

The World Bank and the International Monetary Fund are the most potent external forces today in the economic restructuring of developing economies. The World Bank has been involved during the past fifteen years or so in nearly fifty restructuring attempts which it likes to call structural adjustment programmes (Country Economics Department of World Bank, 1991). While it does not necessarily follow a recipe approach, it does tend to impose conditionalities upon its client states that reflect certain assumptions about effective restructuring. Table 9 shows in brief outline what appears to be the World Bank's core model of structural adjustment for bankrupt statist developing economies. In content and assumptions it resembles in several aspects the "liberty" agenda outlined in Table 1.

(Table 9 about here)

One key assumption on which the World Bank's structural adjustment model rests seems to be that private ownership is inherently more efficient than public ownership, in part because of the strength of the profit motive under private ownership (Country Economics Department of World Bank, 1992). The second, largely unstated assumption, seems to be that economic efficiency is what really matters given the paucity of resources in poor societies, and should get precedence, if there is a conflict, over such alternative goals as production growth, economic self-reliance, employment, or greater equality. Thirdly, competition in the market place is the most effective means for increasing efficiency. The threat of loss, or closure,

given the strength of the profit motive, would compel entrepreneurs to strive for greater productivity and efficiency. Given these premises the World Bank structural adjustment programme follows - deregulate wages and prices to give more elbow room to market forces, privatise public enterprises so that they would become more efficient, lower tariff barriers to increase foreign competition, deregulate domestic industry to increase competition among indigenous players, improve infrastructure to reduce private costs, facilitate foreign private investment both to supplement domestic investment and to bring new technologies and new management competencies to a relatively closed, backward society, devalue currency to make exports more profitable, reduce fiscal deficit so that the inefficient state pre-empts less of the society's scarce savings and this enables greater flow of savings into the more efficient private sector, lower taxes and rationalise them to promote savings and investment, give ownership or tenure to the tillers of the soil because then they would try to be more productive, invest in human capital to increase productivity, and if the structural adjustment results in large scale unemployment, have a safety net to mitigate hardship.

Indeed, the World Bank has indicated its world view quite clearly (World Bank, 1991, p.148): "It is the particular responsibility of the industrial countries and the finance agencies to

* Defend and extend the liberal order of international trade established after 1945
* Ease the flow of capital across borders
* Pursue domestic economic policies that promote global saving and steady, noninflationary growth
* Support the transfer of technology
* Protect the environment and conserve energy".

It has also clarified its view regarding what the developing countries should be doing (World Bank 1991, pp.148-149): "The right strategy for the developing countries, whether external conditions are supportive or not, is to

* Invest in people, including education, health, and population control
* Help domestic markets to work well by fostering competition and investing in infrastructure
* Liberalize trade and foreign investment
* Avoid excessive fiscal deficits and high inflation".

What the World Bank does not explicitly espouse is to ease the flow of labour (not only capital) across borders and for developing countries to pursue an industrial policy aimed at rapid exports-led growth in manufacturing, so successful in the ASEAN countries, which is based not just on competition but also cooperation within industry and cooperation between industry and government.

The World Bank structural adjustment model seems to represent a Western world view vis-a-vis economic management. The World Bank - and the IMF - are headquartered in Washington, D.C. Their heads are appointed by the President of the United States. They are staffed by economists of different nationalities who have, however, been predominantly trained in the West, especially the US. The World Bank therefore tends to work with assumptions that have worked reasonably well in the West, especially in the US.
Being dominated by economists and bankers it gives primacy to economic incentives, on the usually unstated premise that man is primarily motivated by money. The efficacy of social

cooperation (rather than competition), nurturing (rather than economic insecurity), national identity, patriotism, unity, effort at national self-reliance, sense of social responsibility, commitment to social justice and equality, liberation from oppressive systems, democratisation, and so forth, factors that in various combinations seem to have played so large a role in the economic development of Japan, China, South Korea, several other ASEAN countries, and India do not find a significant place in the economic restructuring agenda of the World Bank. No wonder the World Bank structural adjustment model has worked almost as often as it has not worked, and the great success stories of the seventies, eighties and nineties have been of those countries that retained a powerful directive role for the state, retained independence in economic policy making, had a strong public welfare, paternalistic orientation, but allowed market forces an increasingly freer play in a phased manner.

World Bank's Agenda for the Phasing of Economic Restructuring

The World Bank has advocated a phased programme of structural adjustment for centrally planned economies in a 3 to 5 years time frame (World Bank, 1991 p.145) : "A preferred sequencing ...would include early steps to stabilise the macro economy and deregulate domestic ... and external-sector prices to give clear, accurate signals for economic activity and for the valuation of enterprises. These steps would be accompanied and followed by intense efforts to rationalise enterprises, improve economic decision making, reform trade policy, and build managerial skills and a strong financial sector. Privatization of large state enterprises would become the next priority. Protection would be cut and the economy would be opened to foreign competition on a firm, preannounced schedule - first in goods and later in capital markets. Institution building would be a basic theme from the start and at all levels

: the legal contractual system, the structure of ownership, and the roles of key organizations in the economy would require reform and restructuring".

The Bank has provided no evidence to show that its preferred phasing of structural adjustment is more effective than alternative phasings, such as those pursued by South Korea, China, or India (Rana, 1995). Nor has it indicated the logic for its phasing. Why should macro economic stabilization be the first priority, especially when it can be economically so painful in the short-run in terms of slowing of growth and increase in unemployment? After all, there is evidence that this sort of stabilization through tighter credit control, devaluation, budget cuts to reduce fiscal deficit and so forth affects most those least equipped to take a beating, namely the poor and the women (Grootaert, 1994; Singh, 1994; Tanski, 1994). Too quick a deregulation of wages and prices may have pushed Russia and Eastern Europe into hyperinflation, uncontrolled devaluation, and economic collapse. Rationalization of enterprises may imply downsizing in many overmanned public enterprises, and this may not only increase poverty but also cause severe social backlash.
If rationalization is done precipitously it could jeoparadise economic reform itself. Thus, not only is the World Rank's agenda for restructuring problematic, its phasing is questionable.

A Critique of World Bank Promoted Structural Adjustment

Assessment studies of economic restructuring efforts promoted by the World Bank do not point to any striking success. The World Bank itself has conceded that while in many cases balance of payments difficulties eased, the impact on economic growth and inflation seemed to be inconclusive (World Bank, 1991, p.114). Others have found many deleterious consequences of World Bank promoted and financed structural adjustment. The poor seemed

to become poorer (Grootaert, 1994), the disadvantaged such as women were hit hard (Singh, 1994; Tanski, 1994), several countries, particularly in Eastern Europe, experienced negative growth rate (Solimans, 1993), in a study of 93 developing countries that had received structural adjustment loans in the eighties there was fairly sharp reduction in the rate of investment, sharp increase in debt, and a substantial depreciation in the real exchange rate of the currency resulting in a substantial loss of purchasing power (Faini, de Melo, Senhadji, and Stanton, 1991), etc. The World Bank brand of structural adjustment seems to be a hit or miss affair, with misses alarmingly close in frequency to hits (Mosley and Weeks, 1993; Solimans, 1993). This may be so because the World Bank, dominated as it seems to be by Western neoclassical economic ideology (Stein, 1994), has ignored or underplayed some of the realities of successful economic management.

The great success stories of economic restructuring in the seventies, eighties, and nineties have been of China and the ASEAN countries (Amsden, 1994; World Bank, 1993), in which the World Bank played generally a marginal rather than a decisive role in restructuring. These countries generally beat their own path to economic change, and while they incorporated many of the features of a market economy and invested heavily in infrastructure and human capital, they retained a strong interventionist role for the state, pursued an industrial policy aiming at rapid increase in the output of manufactured goods, often by setting up state-owned enterprises, pursued not just an exports-led growth strategy but one that involved selective focus on a few industries that through technological and infrastructure development could have an international comparative advantage in the future, were protective of their industries for long periods, were selective in permitting the entry of foreign investment, helped big business houses to grow bigger rather than break them up (Lee, 1992),

and stressed not only competition between producers but also cooperation between them and with the government in pursuing national economic goals (Amsden, 1994; Freeman, 1989; *Kohli, 1994*; Singh 1994; Yaghmaian, 1994). These policies deviate markedly from the policies advocated by the World Bank (Kwon, 1994; Lall, 1994), and its express prescription that government interventions should be reluctant, and that it is a mistake for the state to engage in physical production, or to protect the domestic production of a good that can be imported more cheaply or has few local externalities (World Bank, 1991, ch.1).

The obsession with privatization illustrates well the limitations of the World Bank's approach to economic restructuring. Although the World Bank does not regard it as an end in itself, it does assert that privatization is necessary and highly desirable (World Bank, 1991, p.144). This assertion rests on the dubious assumption that ownership "matters"* and that private ownership is inherently more efficient than public ownership (Country Economics Department, 1992, chapter 2). In support it cites the loss making record of public enterprises round the world without establishing that the losses have mostly been on account of inefficiency rather than because of public policy objectives. It has underplayed the record of profitable public enterprises. In India, for instance, of the 250-odd public enterprises owned by the Government of india, well over half are profitable, and of the loss making units nearly half are former terminally ill private enterprises nationalised to maintain employment or for other public policy reasons (Government of India, 1995). Nor has the World Bank cared to highlight that the growth of Japan's or Korea's or India's great business houses would not have been possible without strong state support, subsidies, financial investment, and protection from foreign competition for long periods (Singh, 1994). Nor has the Bank highlighted the magnitude of sickness in the private sector. Around 1990 in India alone there

were 2000 medium and large private enterprises that were sick and around a quarter million sick small enterprises (Khandwalla, 1991). In Poland, after economic liberalization, half of several thousand private enterprises seem to have folded (Amsden, 1993).

The Bank seems to be supporting privatization on a mass scale, almost as a panacea for all ills. By 1992, the World Bank had supported privatization in over 180 operations in 67 countries with International Finance Corporation, its affiliate, providing advisory and investment support to 50 privatized firms (Country Economics Department, 1992, pp.iii-iv). Since then the tempo seems to have picked up, especially in Eastern Europe, Latin America, and Africa. The research base for supporting this massive effort seems woeful. A study of 12 cases of privatization in Chile, Malaysia, Mexico, and the UK commissioned by the World Bank has been highlighted by the Bank in support of the benefits of privatization (Country Economics Department, 1992, p.10). But when (by 1991) nearly 7000 public enterprises had been privatised, of which over 2000 were in developing countries (Country Economics Department, 1992, p.7), a sample of 12 cases, however carefully chosen, can hardly reveal anything definitive. Even in this study, price rises were effected by half the companies after privatisation (justified by the World Bank as a necessary response to resource scarcity), there were no productivity gains in 5 cases, while the consumers gained in 2 cases they were worse off in 3 others, and layoffs were resorted to in an unspecified number of companies. In poor countries without a welfare state, price increases of essential goods and services and layoffs both represent calamities, not just "unavoidable" social costs. And of course there was no "control" sample to determine whether the observed improvements in productivity, customer service, scale up in investment, or diversification were special to privatized enterprises.

On the other hand there is persuasive evidence that what matters is the quality of management, not ownership. In studies of corporate sickness in the U.S., the U.K., Europe, and India, the major cause of sickness in the private sector has been found to be poor quality of management - too much conservatism or too much reckless growth or too much looseness or too much corruption and shady practices or slow-footedness, and so forth (Hegde, 1982; Khandwalla, 1989, ch.1). In studies of turnaround from sickness, the evidence from a large number of cases is highly persuasive that when an inappropriate management is replaced by a dynamic, professionalist management, striking performance improvements take place (Khandwalla, 1992, especially chapters 1, 3 and 4). There are several examples of sick public enterprises being dramatically revived (see Table 10), not after privatization, but after a change in top management (Khandwalla, 1992, especially chapters 1 and 5). In six ASEAN countries (Hong Kong, Indonesia, Malaysia, Philippines, Taiwan, and Thailand) in which there have been (for developing countries) relatively high standards in the delivery of utilities and public services, the degree of public ownership, as of 1992, was as Table 11 shows, quite high (MacMurray, 1993). In India, after economic restructuring began in earnest in 1991, there was a performance decline in both the public and the private sectors for the first two years and striking improvement in the next two, despite much lower tariff barriers and deregulation (Economic Times, 1995; Chakravorty, 1995; Rekhi, 1995). Thus, the assumption that public ownership is inherently less efficient than private ownership, however valid it may be in the West, has dubious validity in many other parts of the world. This does not imply abandonment of privatization as a policy tool; simply its selective, much more discriminating usage. In situations in which public enterprises are badly managed and no substitute effective public management is readily available, privatization may be a useful alternative to consider provided effective management is available in the private sector. And

equally, if a private enterprise has become sick because of inappropriate management, and an appropriate replacement is available in the public sector but not in the private sector, there can be a case for either nationalization or of placing management in public hands. Thus neither privatization nor nationalization are panaceas. They are best seen as tools for improving the quality of management in appropriate circumstances. Besides, there are many options in the form of privatization, ranging from transfer of ownership to contracting out, partial divestiture, joint ownership of government and private parties, franchising, and transfer of management control. There is a similar diversity of options in nationalization ranging from transfer of ownership to public control through various means. A discriminating use of these options in privatization as well as nationalization may better serve economic development than wholesale transfer of ownership.

(Table 10 and 11 about here)

Equally questionable is the insistence of the Bank and its affiliates on reducing tariff barriers in developing economies. To-day's developed economies, notably the US, Japan, and most of the OECD countries, resorted to protective tariffs to facilitate the setting up and development of infant industries during the decades to-day's advanced economies were in their developmental stage. For instance, tariffs on imported manufactures in the UK and the US in 1820 were 40% or over, and as late as in 1930 the average tariff on manufactured imports was 32% for 12 industrialised countries (World Bank, 1991, p.97). Japanese industry was heavily protected by tariff and non-tariff barriers in the 1950s through 1970s, its years of fastest industrial growth, and imported manufactures were 2.4% of Japan's GDP versus 14% - 15% for UK and leading Western countries (Singh, 1994). Most of the fastest growth economies of the eighties and nineties - China and the ASEAN countries - are still substantially protected by tariff and other barriers, and only slowly they are reducing these

barriers. In 1987 the tariffs on imported manufactures in East Asian countries averaged 22% (World Bank, 1991, p.98). And yet the Bank and its affiliates impose conditionalities on many client states from the developing world that include sharp reductions in tariff barriers. Without tariff protection how can indigenous industry develop when entrepreneurial traditions, as in Russia, Eastern Europe, many Latin American and African states are weak, and many industries are on the learning curve so that it would take some years before they can become globally competitive? A better strategy for the World Bank may be to encourage rapid increase in production through tariff protection, SOEs, and/or subsidies for manufactured goods, even if it is "inefficient" for the moment, and then foster domestic competition through deregulation so that costs come down fairly quickly through enforced learning. Massive investments in infrastructure and technical and managerial training would serve as positive externalities for reducing costs (Stewart and Ghani, 1991), as also speedy strengthening of institutions like banking and capital markets that support industry. A strongly supported drive for non-traditional exports (Hamilton and Thompson, 1994; Yaghmaian, 1994), selective entry of foreign private investment, especially in infrastructure, and then, when the industrial base has become diversified and strong, phased reduction in tariff barriers, would, in the light of available evidence, lead to fast economic growth. Dynamic external economies may well convert what at one point of time look like inefficient industries without international competitive advantage into internationally highly competitive industries a decade or two later (Singh, 1994; Stewart and Ghani, 1991).

The Role of the State in Economic Restructuring

After decades of statism it is clear that it does not work beyond a point. The costs of centralization far outweigh the benefits. The market economy has a resilience and a learning

capacity that an over-extended, often rigid, corrupt, and bureaucratic state does not have. It is equally clear that a market economy without a guiding, steadying, and orchestrating role of the state also does not work, for there are serious negative externalities of uncontrolled private enterprise such as pollution and harmful exploitation of natural and human resources that are unacceptable in any civilized society. Then there is the necessity of some form of macro-economic management to dampen business cycle fluctuations, and the need for some form of a welfare state or safety net to cushion the pains of capitalism. In the developing societies there is the additional overwhelming need to alleviate poverty as quickly as possible, partly through rapid economic development, partly through investment in health, education, and skills (Psachazepoulos, 1994; World Bank, 1991, pp.148-149), and partly through various transfer payments. The state also needs to invest heavily in physical infrastructure - roads, transportation, ports, power, telecommunications etc - without which rapid industrial development is infeasible. Finally, the state needs to ensure that sophisticated, long gestation, "high tech" industries get established either through SOEs or through subsidies to the private sector to serve as engines of future growth.

The lesson of the fastest growth economies of the century - Japan until the eighties, South Korea, China, and Taiwan in the seventies, eighties and nineties - is the need to combine a market economy with an entrepreneurial and interventionist state that, however, steers clear of excessive regulation and bureaucracy (Amsden, 1994; Kohli, 1994; Singh, 1994). In the world's poor societies, capitalism in the past has often been synonymous with colonialism and exploitation. That image is fading but still lurks in the subconscious. The autonomous and powerful state is seen as a useful countervailing power to exploitation by business, domestic or foreign. The challenge in designing government in developing societies is to preserve an

activist, social welfare oriented, and nation building state, foster a market economy, nurture its growth through an industrial policy that promotes a rapid growth of non-traditional exports through government - industry collaboration, gradually diminishing tariff barriers and massive investments in infrastructure without, however, the state becoming an octopus of pervasive control. The challenge also is to ensure that the state itself is not captured by vested interests who convert it into a spoils system. The need is not for an authoritarian state but for a broadly democratic state accountable to the people that, however, is well managed, growth oriented, and strong. Indeed, there is evidence that political liberty is associated with greater investment in human capital (Habibi, 1994) and less protectionism (Bates, Brock, and Tiefenthaler, 1991) and increasing democratisation of several East Asian countries has not dampened their high growth rates. Nor is political repression necessary for implementing sustainable stabilization policies over a 3 to 4 year period (Ball and Rausser, 1995).

Effective Management of Government

Effective management of government in developing societies offers an incalculably large potential for growth and improvement in the quality of life of the people. The government is not an undifferentiated blob. It is a system highly differentiated by function (executive, legislative, judicial), sub-function (various departments and agencies and ministries), hierarchical levels, etc. It is a huge, relatively loosely coupled system (Weick, 1976) of systems. Better management relates not just to macro economic management (excessively emphasised by most economists), but to the management of these myriad systems. There is overwhelming evidence that one competent manager at the top can make a vast difference to the performance of an organization, even a government-owned organization (Bennis and Nanus, 1985; Khandwalla, 1992; Singh and Bhandarkar, 1990). The implication is that in

any economic restructuring the highest priority needs to be given to replacing incompetent heads of governmental organizations by competent heads. Without this change no macro economic stabilisation is likely to work, and indeed may backfire badly, as in Russia and other East European countries. If there is one conditionality the World Bank must impose, it is this. The problem is not as formidable as it may appear. The number of dynamic professional managers required to be emplaced is not large. In the case of India, for example, the initial requirement may be new heads for the 100-odd loss making central government owned public enterprises, professional heads recruited through open selection for about 200-odd major government departments, and such heads for the malfunctioning departmental undertakings, financial institutions, agencies, etc. The total may not exceed a thousand for even a huge nation like India. In a country with perhaps 3 million entrepreneurs and managers, this number is not in principle hard to find. But it does mean open selection, lateral entry, emphasis on professionalism as well as a venturing spirit, willingness to give autonomy to the selected heads, etc., conditionalities well worth imposing by the World Bank.

A second major way of improving government is through administrative and managerial innovations. In Britain, two-thirds of the half-a-million strong civil service has been reorganised into executive agencies that are broadly similar to corporate divisions or responsibility centres in the way they work, with promising results in terms of efficiency and service quality (Caiden, 1991; Commonwealth Secretariat, 1995a; Falcon, 1992). Other innovations that have worked, as in Malaysia, are massive training for civil servants, the use of consultants, telecommunications technology, reorganization of government services, use of financial incentives in governance, and various tools of effective personnel management

such as human resource development and organization development (Commonwealth Secretariat, 1995b; Karim, 1992), and the extensive use of information technology and decision support systems as in Egypt (El Sherif, 1988). Indeed there is evidence that economic growth is in part powered by information technology (Kraemer, 1994). The World Bank can use its clout to force badly managed states to restructure in the way the UK and Malaysia have reorganised their civil services, invest heavily in the human resource development and training of administrators, provide financial incentives, and use information and communications technology, decision support systems, and management information systems more extensively in governmental decision making. There is every possibility that these conditionalities, along with the insistence on bringing in dynamic professional managers into administration and state-owned enterprises may give far greater economic benefits than the present insistence on macroeconomic stabilization, deregulation of wages and prices, reduction in tariff barriers, and privatization.

Concluding Comments

Economic control and decontrol are not just matters of economics. These have political and social antecedents, concurrences, and consequences. There are no simple keys to economic development. Although broad approaches help, economic development is substantially a matter of each society choosing and learning and innovating. In this process government, as a massed power that is broadly representative of the aspirations and wishes of the people, must inevitably play a major managerial role. True, many decisions can be decentralised, and such decentralization greatly helps social learning because of the great variety of approaches to problems it catalyses. But many decisions must also be taken collectively, and for this there is no substitute for some sort of government. But the dilemma is that

governments tend to malfunction because of their size and other reasons. The solution is not to dispense with government but to redefine its priorities, revitalise it, restructure it, and manage its parts effectively (World Bank, 1991, ch.7).

There is a great deal of psychological research that suggests that the economic motive is not the only, or even the most important, of human motives (Maslow, 1954; McClelland, 1961; Vroom, 1964). Even on the basis of casual empiricism it is evident that other motives can, in certain circumstances, be even more powerful. After all, the economic motive plays only a modest role in governing relations between close family members, and great social movements are powered by idealism and caring, and/or revulsion with the status quo rather than by economic incentives (Pareek, 1968; Sorokin, 1950). Some social scientists have argued that a strong work ethic plays a central role in economic development (McClelland, 1961). A good deal of art and science and technology is driven by the need to actualise one's potential (Maslow, 1954) or to create or to discover or to pioneer (Khandwalla, 1994), not just by the lure of money. The need for status may be a powerful motivator of a good deal of social behaviour, just as the need for power shapes much of political behaviour (Krech, Crutchfield, and Ballachey, 1962, pp.94-97; McClelland and Burnham, 1976). Even in the setting up, running, and growth of business enterprises, where one would expect the economic motive to be dominant, research suggests businessmen pursue many different goals, not just profit maximization (Dent, 1959; England and Mee, 1971; Khandwalla and Jain, 1984; Perrow, 1970, ch.5) and the achievement motive possibly plays as significant a role as the economic motive (McClelland, 1961). To try and redesign complete societies on the institutionalization of just the economic motive (competition, property rights, profit maximization) is to court failure, because individuals, groups, and institutions in many

situations will often subordinate the economic motive to other motives. At best the economic motive can only tap a part of human energies and potential. Excessively emphasised, the economic motive can pervert human sensibility and lead it to a mindless sort of selfishness. The need in the poor societies of the world is to anchor economic restructuring in a wider range of human motives and to strengthen or build institutions, including governance systems, that tap all of these motives.

A second point in the economic structuring of developing societies towards greater market friendliness is that both the macro and the micro aspects must be managed well. First of all economic structuring must be properly phased keeping in mind the industrial structure of the economy. Too fast a pace of "reform" is likely to boomerang. In particular, both privatization and reduction of tariff barriers must be phased with great care. If there is to be large scale privatization it is essential that public assets are handed over to capable managerial hands, for it cannot be assumed that private ownership, regardless of the quality of management, will improve performance. Tariff barriers should be progressively lowered, but in a phased manner and selectively, so that industry as a whole, as well its different constituents, get time to adjust to global competition. But it is not enough to design well the policy structure and the way "reforms" are to be phased. The effective management of the implementation of policy reform is possibly as important as the reform itself (Commonwealth Secretariat, 1994, 1995a,b,c,d; Prokopenko, 1989). Nor is effective management synonymous with better costing, pricing, and accounting, useful as these are. High quality dynamic, professional managers must be found and installed in key positions to get the best results out of "reforms". Similarly, the various agencies and departments of the government, particularly the strategic ones with long term and/or large multiplier effects must be manned

by high quality managers. The positive multiplier effects of the more effective management of a state's strategic instrumentalities can be extremely large (Khandwalla, 1988). As the data in Table 10 show, it is possible to improve drammatically the performance of public sector enterprises without privatisation, and primarily by providing them with dynamic chief executives. There is also growing evidence of what personal initiative can do in government bureaucracies (Ramachandran, 1984), governmental institutions (Bhatt, 1984), other public sector organizations (Bennis and Nanus, 1985), and indeed, for the nation as a whole (Woycke, 1990). Further, there is now a substantial body of empirical literature on good government practices and innovations round the world that can be resorted to for improving greatly the performance of governance systems (Caiden, 1991; Commonwealth Secretariat, 1994; Commonwealth Secretariat, 1995 a,b,c,d; El Sheriff, 1988; Prokopenko, 1989).

Some hypotheses are suggested for the successful decontrol and economic restructuring of highly controlled economies:

1. The more participatively designed the economic restructuring strategy, the faster and greater would be the improvement in the economy's growth rate.
2. The less precipitous the reduction in tariff barriers, and the more phased the opening up to foreign private investment, the faster and greater would be the improvement in the economy's growth rate.
3. The greater the investment in infrastructure (energy, transport, communications, financial services, etc.) and its improvement, and in human capital (especially in primary, technical, and management education), the faster and greater would be the improvement in the country's growth rate.

4. The more carefully designed the industrial policy of the country, with emphasis on export-led growth in selected non-traditional items, and the greater the collaboration between the government and industry and within industry in effectively implementing it, the faster and greater would be the improvement in the economy's growth rate.

5. The more selective and phased the privatization of non-strategic public enterprises, and the greater the care in ensuring that they are handed over to private dynamic professional managements, the faster and greater would be the improvement in the economy's growth rate.

6. The greater the attention to the effective management of the implementation of economic reform, the faster and greater would be the improvement in the country's growth rate.

7. The greater the induction of dynamic professional managers to head those strategic organizations and institutions that have large, long term, multiplier effects, the faster and greater would be the improvement in the economy's growth rate.

8. The more extensive the structural reorganization of bureaucratic governance systems into relatively autonomous, modest sized responsibility centers headed by competent professional managers, and the greater the use of information techology based decision support systems for the managers of these responsibility centers, the faster and greater would be the improvement in the economy's growth rate.

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Table 1

ECONOMIC RESTRUCTURING AGENDA FOR A FREE MARKET ECONOMY

1. **Creation of an Enabling Environment for Free Enterprise**

   Removal of controls for starting, expanding, diversifying, selling, or closing an enterprise
   Rapid improvement of infrastructure (transport, communications, energy, banking and insurance facilities, education and health)
   Protection of private property rights
   Efficient legal system, enforceable laws
   Development of accounting standards

2. **Decontrol of Wages and Prices**

   Wages and prices to be set purely by market forces

3. **Financial Market Liberalization**

   Minimal restrictions on interest rates charged by banks
   Minimal restrictions on the use of financial instruments
   Minimal restrictions on entry into the financial services sector
   Minimal restriction on financial services offered

4. **Fiscal Policy**

   Balanced budget, moderate deficits during recessions
   Development expenditure to be met out of tax revenues rather than state borrowings

   Low to moderate income and corporate taxes
   Elimination of subsidies except for the poorest

5. **Foreign Exchange Management Liberalization**

   No restrictions on foreign currency transactions
   Fully convertible currency
   Market-based exchange rate

6. **Foreign Investment**

   Full freedom to foreign investors to invest in any sector or industry or enterprise
   Tax incentives and concessions to attract foreign private capital
   Full freedom to foreign investors to repatriate capital and income

7. **Free Flow of Information**

Free access to all economic information
Freedom of the press and other media

8. **Monetary Policy**

Anti-inflationary monetary policy
Elimination of differential interest rates for different sectors

9. **Privatization**

Except for crucial or highly strategic public services, transfer of publicly managed assets to private hands
Disposal of state owned enterprises

10. **Trade Liberalization**

No restrictions on imports and exports and domestic trade
Low import, export, excise tariffs

Table 2

Heritage Foundation Assessment of How Controlled Various Economies Are

	Trade Barriers	Tax-ation	State intervent-ion in economy	Monetary control	Barriers to foreign invest-ments	Restric-tions on banking	Wage and price controls	Restric-tions on property rights	Business regula-tions	Black market activi-ties
Developing Countries										
1 Brazil	H	M	L	VL	M	M	M	M	H	M
2 Mexico	M	H	VL	VL	L	H	M	L	H	M
3 China	VH	H	VH	M	M	M	M	H	H	H
4 Indonesia	VH	H	L	H	M	M	M	M	H	VH
5 Malaysia	M	M	L	VH	L	M	L	L	L	L
6 Pakistan	VH	VH	L	H	L	L	M	L	H	VH
7 Thailand	M	M	VL	VH	M	M	M	VL	M	L
8 India	VH	VH	M	H	M	H	M	M	H	VH
NICs										
9 Hongkong	VL	VL	VL	H	VL	L	VL	VL	VL	VL
10 Singapore	VL	M	VL	VH	VL	L	VL	VL	VL	VL
11 South Korea	M	H	VL	VH	M	L	L	VL	M	L
12 Taiwan	L	M	L	VH	M	M	L	VL	L	VL
Ex-Socialist										
13 Russia	H	H	M	VL	L	M	M	M	L	VH
Developed Countries										
14 Canada	L	H	L	VH	M	L	L	VL	L	VL
15 US	L	H	L	VH	L	L	L	VL	L	VL
16 UK	L	VH	M	VH	L	L	L	VL	VL	VL
17 France	L	H	L	VH	M	M	M	L	L	VL
18 Germany	L	VH	L	VH	L	L	L	L	L	VL
19 Italy	L	VH	M	H	L	M	L	L	L	L
20 Japan	L	VH	VL	VH	M	L	L	VL	L	VL

Source : Rohit Saran, "The liberty agenda", Business Today, Jan.22-Feb.6, 1995, based on Index of Economic Freedom Developed by Hertiage Foundation, US, for a study of 101 economies.

Note : VL = very low; L = low; M = moderate; H = high; VH = very high

Table 3

Overall Regulation of Economy and
GDP Growth Rate of Different Economies

	Overall Regulatory Score for Economy[a]	Annual GDP Growth Rate 1989-1993[d]
Developing Countries		
1. Brazil	29	0.7
2. Mexico	27	3.0
3. China	38	9.0
4. Indonesia	36	6.8
5. Malaysia	26	8.8
6. Pakistan	34	4.9
7. Thailand	27	9.5
8. India	39	4.0
Newly Industrialised Countries		
9. Hongkong	14	6.9[b]
10. Singapore	17	6.6[b]
11. South Korea	26	7.2
12. Taiwan	24	7.6[b]
Ex-Socialist		
13. Russia	30	-9.3
Developed Countries		
14. Canada	24	NA
15. U.S.	23	1.8
16. U.K.	24	1.9[c]
17. France	27	1.9[c]
18. Germany	25	1.9[c]
19. Italy	27	1.9[c]
20. Japan	24	3.0

a: The index of overall regulation of economy was based on assessment of regulation vis-a-vis 10 economic dimensions by the Heritage Foundation, Washington, D.C., U.S. Regulation score for each dimension was computed by giving a score of 1 to Very Low, 2 to Low, 3 to Moderate, 4 to High, and 5 to Very High, and then overall regulation score was computed by summing across the ten dimensions.

b: For 1980-1991

c: For OECD Countries

d: Based on data given in World Bank's World Tables 1995 (Baltimore : Johns Hopkins University Press, 1995).

Table 4

MOVEMENT TOWARDS MARKET ECONOMY IN DEVELOPING COUNTRIES IN RECENT YEARS AND GDP RATES

Sample : 29 Developing Countries

	Pre-reform Economic Deregulation Decile Score	Annual GDP Growth Rate 1978-82	Economic Deregulation Decile Score 1990-1	Annual GDP Growth Rate 1989-93	Change Towards Economic Deregulation (Col.3 - Col.1)	Change in Annual GDP Rate (4-2)
	1	2	3	4	5	6
Africa						
Algeria	3	5.4	5	0.7	2	-4.7
Cote d'Ivoire	5	1.3	6	-1.0	1	-2.3
Ghana	3	-0.1	8	4.3	5	4.4
Kenya	4	5.1	7	2.2	3	-2.9
Madagascar	3	-0.7	5	0.7	2	1.4
Nigeria	4	-1.0	7	5.0	3	6.0
Senegal	3	2.8	5	0.9	2	-1.9
Tanzania	4	1.2	6	4.2	2	3.0
Zambia	4	0.8	6	0.7	2	-0.1
Asia						
India	3	3.5	5	4.0	2	0.5
Indonesia	4	5.8	8	6.8	4	1.0
Malaysia	7	7.3	8	8.8	1	1.5
Philippines	4	4.6	7	2.2	3	-2.4
South Korea	4	6.2	9	7.2	5	1.0
Sri Lanka	6	6.1	7	4.8	1	-1.3
Thailand	7	6.3	7	9.5	0	3.2
Turkey	3	2.1	8	4.7	5	2.6
Ex-Socialist						
Hungary	5	3.1	6	-3.9	1	-7.0
Poland	3	0.5[a]	7	-2.3	4	-2.8
Soviet Union/Russia	2	3.7[b]	4	-9.3[b]	2	-13.0
Latin America						
Argentina	4	-0.2	8	3.5	4	3.7
Bolivia	4	-0.2	7	3.7	3	3.9
Brazil	4	3.1	5	0.7	1	-2.4

Chile	8	3.8	9	7.5	1	3.7
Colombia	6	4.2	7	3.7	1	-0.5
Costa Rica	6	0.5	8	5.1	2	4.6
Jamaica	4	-0.5	7	3.1	3	3.6
Mexico	4	6.8	8	3.0	4	-3.8
Peru	6	3.2	4	-1.7	-2	-4.9

In columns 1 and 3, 1 = score of upto 10, 2 - score of 11 to 20, 3 = score of 21-30, etc. Based on data compiled by Centre for International Private Enterprise, U.S. and published in "The Economic Reform Survey", Economic Reform Today, Summer 1992. Growth rates are from World Tables 1995 published by the World Bank.

a : Data not available before 1981. Average based on 1981-1985 GDP rates.

b : 1978-82 and 1989-93 growth estimates for the Russian Federation.

Table 5

RUSSIAN STRUCTURAL ADJUSTMENT 1991-1995

* Begun in the former Soviet Union in the late eighties. Picked up momentum in Russia in the early nineties.

* Legislation to enable enterprises and cooperatives freedom to operate.

* Swift removal of price controls.

* Liberalization of labour markets.

* Liberalization of foreign trade. 80,000 Russian enterprises exposed for the first time to foreign markets and foreign competition.

* Budget cuts to reduce fiscal deficit, especially steep reduction in defence expenditure and defence production.

* Tax reform.

* Privatization, especially via the distribution of vouchers to people entitling them to ownership of shares in public enterprises.

* Establishment of a capital market.

* Tight monetary policy to cut inflation.

Consequences

* In 1992 GDP declined by 20% and inflation was 25% per month.

* Continuing fall in GDP in 1993, 1994, and 1995 and continuing high inflation.

* Sharp increase in inequality. Inequality index rose from 5 in 1991 to 8 in 1992.

* Widespread emergence of small scale entrepreneurship.

* Catastrophic devaluation of the rouble.

* Huge smuggling out of money estimated at $ 25 billion a year.

* Growing unemployment, corruption, crime.

Table 6

INDIAN STRUCTURAL ADJUSTMENT 1991-1995

* Liberalization process initiated in the mid-eighties.

* Structural adjustment begun in earnest in 1991 following balance of payments crisis and a bail out on the basis of World Bank-IMF conditionalities.

* Initial currency devaluation by about 25%. Progressively greater convertibility of the currency. Exchange rate increasingly based on market forces.

* Attempt to reduce the fiscal deficit by reducing the rate of increase in government expenditure and reducing some subsidies.

* Reduction in the rate of increase in money supply.

* Substantial but phased elimination of licensing for setting up industries, expansion.

* Drastic reduction in industries reserved for the public sector and limited access of private sector even to the reserved list.

* Liberalization of access to foreign technology.

* Phased elimination of import control except for consumer goods.

* Phased reduction in import duties - from an average of 150% in 1991-92 to 110% in 1992-93 to 85% in 1993-94 to 65% in 1994-95 to 50% in 1995-96.

* Liberalization of foreign private investment. Quicker clearance of such proposals.

* Liberalization of import of gold and silver to reduce smuggling.

* Reduction in export restrictions and in export subsidies.

* Liberalization of overseas investments by Indian firms.

* Reduction in income tax, wealth tax, and corporate tax on profits.

* Selective and phased lowering of excise duties.

* Enforcement of new accounting norms to bring reporting of income by banks to international standards.

* Nationalised banks permitted to raise equity from the market and controls reduced on private sector banks. Interest rates charged by banks permitted to vary subject to a ceiling.

* Abolition of Office of Controller of Capital issues to make it easier for enterprises to raise money but simultaneously Stock Exchange Board of India came up with comprehensive rules and regulations for healthy functioning of stock markets. A national stock exchange set up with electronic operations.
* Private sector mutual funds permitted and foreign institutional investors permitted to invest in capital markets.

* Some attempt to phase out budgetary support to loss making public enterprises; disinvestment of some of their equity; freedom to them to raise capital from the market; some risk of closure; more pricing freedom.

* National Renewal Fund set up to fund voluntary retirement schemes and worker retraining schemes. About 70, 000 public enterprise employees have availed of this scheme.

* Significant expansion in backward areas of public distribution system for distributing essential commodities at subsidised rates.

* Sharp increase in expenditure on rural development, health, and education.

Table 7

RESULTS OF INDIA'S STRUCTURAL ADJUSTMENT 1991-1995

* Economy grew at less than 1% in 1991-92; about 4.5% in 1992-93 and 1993-94; 6.2% in 1994-95 and may grow at 7% in 1995-96.

* Industrial growth was virtually zero in 1991-92; 2.5% in 1992-93; 4.2% in 1993-94; 8% in 1994-95, and may top 10% in 1995-96.

* Inflation rate declined from over 12% in 1991-92 to around 8.5% in 1995-96.

* Exports grew from about 18 billion dollars in 1990-91 to 30 billion dollars in 1995-96.

* Foreign exchange reserves climbed from about 1 billion dollars in 1991 to around 19 billion dollars in 1995.

* Foreign private investment climbed from below a billion dollars a year in 1991 to about 5 billion dollars for 1995.

* Corporate sales increased by 20% in 1993-94, by 30% in 1994-95 and corporate profits in 1994-95 were over 70% higher than in 1993-94. Further rise in corporate sales of about 30% was expected in 1995-6.

* Profits and sales of public enterprises were also up sharply in 1994-5 and 1995-6.

Table 8

VARIATION IN ECONOMIC RESTRUCTURING

	Ghana 1983-1994		South Korea 1965-1979-1994		China 1978-1985-1994
	Stabilization Phase		Sixties and Seventies		Late Seventies Early Eighties
1	Elimination of subsidies, cuts in public employment.	1	Significant currency devaluations.	1	Collectivization in agriculture abandoned; replaced by a household farm economy of partially controlled, partially free markets.
2	Tax reforms, lowering of taxes.	2	Powerful export incentives for non-traditional goods.	2	Emphasis on technological modernization, production increase, streamlining of administrative apparatus.
3	Tight money policy	3	Priority to rapid growth of exports, not to foreign trade balance	3	Downplaying of statism and socialist dogma. Greater decentralization to local governments led to considerable local development of infrastructure.
4	Currency devaluation	4	Large investments by state in priority sectors to stimulate industrial development	4	Priority to market economy, enterprise autonomy, decentralization, economic incentives, efficiency, and productivity.
5	Trade liberalization.	5	Large investments by state in infrastructure to support export drive.	5	Profit sharing by state enterprises, central and provincial governments. Dual pricing - part of output sold to the state at a fixed price, the remaining at free market prices. Replacement of physical targets by financial targets for state enterprises.

6	Raised salaries of public officials	6	Support to large business houses - chaebol - and massive entrepreneurial ventures by them.	6	Emphasis on rule of law. Subordination of Party to law.
7.	increased investment in infrastructure	7	Starting of many SOEs.	7	Attempts to stem corruption.
8	Increased spending on vulnerable sectors.			8	Huge effort to train officials.
				9	Modest effort to provide training in modern management methods.
				10	Attempt to reform civil service through training, open competition, merit-based promotion.
				11	Creation of special economic zones to attract foreign investment.
				12	Separation of central banking from commercial banking. Starting of more commercial banks.
	Consolidation Phase		**Eighties**		**Mid-Eighties Onwards**
1	Relaxed import control	1	Attempt to reduce public sector deficits	1	Opening up to foreign private investment in a big way
2	Price deregulation, promotion of greater competition between SOEs	2	Revamping of SOE operations	2	Some deregulation in setting up private enterprises.
3	Abolished two-tier exchange rate	3	Elimination of preferential interest rates for exports and industrial development	3	Setting up of stock exchanges
4	Drastically cut income and property taxes	4	Reduction of import barriers and barriers to foreign investment	4	Some privatization of large state owned enterprises begun

5	Deregulated interest	5	Initiation of privatization and financial sector deregulation	5	Starting of many new foreign trade corporations, with freedom to provinces to retain foreign exchange to fund imports.
6	Started financial sector reforms			6	Some freedom to state enterprises to employ contract labour and some easing of restructions on labour movement
7	Started privatization of SOEs				
8	Greater fiscal incentives for private sector savings and investments				

RESULTS

Ghana	South Korea	China
Reversal of pre-reform decline in GNP, large negative trade balance, high inflation. Still growth rate relatively modest, partly sustained by large foreign aid.	Rapid exports-led, high savings and investments fuelled economic growth. Exports nearly 40% of GNP; long term per capita income growth of 6% per annum. Large foreign exchange reserves	Very rapid economic growth of 9% per annum, with modest inflation, rapid growth in exports of 15% per annum. Large foreign exchange reserves. Attracts huge amounts of foreign investments. Life expectancy has gone up from 64 to 70, infant mortality has nearly halved. Rapid increase in per capita consumption of consumer goods.

Table 9

WORLD BANK'S MODEL OF STRUCTURAL ADJUSTMENT FOR STATIST ECONOMIES

Assumptions

* Ownership matters - private ownership is inherently more efficient than public ownership

* Economic efficiency is the predominantly important economic goal rather than growth, self-reliance, employment, or economic equality.

* Competition is the most effective means of promoting efficiency

* Political leaders and powerful bureaucrats would willingly give up power for the sake of economic efficiency

* If there is large-scale privatization, there would be an adequate supply of professional managers and dynamic entrepreneurs in the private sector who can effectively replace political executives and bureaucratic administrators

* The country has a reasonably good infrastructure or it can be developed quickly to enable a competitive market economy to yield high dividends

Major Elements

* Deregulation, removal of wage-price controls, and market liberalization

* Devaluation to stimulate exports and reduce foreign trade deficit

* Reduction of fiscal deficit to curtail inflation

* Lowering of taxes and their rationalization to reduce tax evasion and improve tax collection

* Greater investment in infrastructure

* Better tax and financial administration

* Removal of domestic barriers to entry as well as barriers to entry of foreign investors

* Privatization of public enterprises and of publicly owned non-strategic assets

* Greater investment in human capital

* Land reforms aimed at distributing ownership or tenure to cultivators

* Safety net for those made redundant by structural adjustment in the form of voluntary retirement, retrenchment, and retraining schemes

Macro-economic stabilization (control over balance of payments deficit, inflation and budget deficit) and deregulation of prices

Rationalization of enterprises, reform of trade policy, improvement in economic decision making, building of managerial skills and a strong financial sector

Privatization of large state enterprises

Progressive reduction in protection to domestic industry

Progressive strengthening of the legal contractual system, the structure of ownership, and the roles of key organizations in the economy

TABLE 10

TURNAROUNDS OF PUBLIC ENTERPRISES UNDER PUBLIC MANAGEMENT

Sl.No.	Organization	Products	Turnaround
1.	Jaguar Motors, U.K. Nationalized loss making company owned by the British Government. £ 500 m. sales	Luxury cars	Lost an average of 24% on sales in 1980 and 1981. Broke even in 1982. Earned 10% on sales in 1983. 1983 sales three times those of 1980.
2.	Southern Petrochemicals and Industries, India. Owned by the State of Tamil Nadu. Rs.5000 m. sales	Fertilisers, chemicals, electronics.	Lost about 45% on sales in 1976-77. Turned profitable in 1978-79. 1981-82 profit 3 times the 1978-79 profit.
3.	Travancore Cochin Chemicals, India. Owned by the State of Kerala. Rs.150 m sales	Miscellaneous chemicals	Lost 43% on sales in 1976. Broke even in 1976. Earned 17% on sales in 1980.
4.	Italtel, Italy. Owned by the Govt. of Italy. L 1200 b. sales	Telecommunications equipment	Lost 46% on sales in 1980. Broke even in 1983. Earned L 25 b. in 1984.
5.	Epe Plywood, Nigeria. Owned by the Govt. of Nigeria. N 7 m. sales	Plywood doors, furniture, etc.	Lost 7% on sales in 1984 and 1985. Broke even in 1986. Earned N 1.3 m on sales of N 6.7 m. Sales more than doubled in 1987 over 1985.
6.	Bharat Heavy Electricals, India. Owned by the Govt. of India. $ 450 m. sales	Power plants and allied equipments	Lost 11% on sales in 1972-73; broke even in 1974-75; profit of 8% on sales in 1975-76. Sales more than doubled over 1972-73.
7.	Bharat Heavy Plate and Vessels, India. Owned by the Govt. of India. Rs.600 m. sales	Sophisticated heavy engineering products like pressure vessels and heat exchangers	Losses for 10 years until 1979-80. Broke even in 1979-80. Net profit rose from 1% on sales in 1979-80 to 14% in 1984-85 and sales doubled.

8.	Jaipur Metals, India, sick private unit taken over by the State of Rajasthan. Rs.120 m. sales	Electrical meters, conductors, wire products	Losses by 1984 3 times equity. Lost 12% on sales in 1983-84, earned 10% on sales in 1984-85 and 16% in 1986-87. Sales more than doubled by 1986-87.
9.	British Steel, UK, owned by the British Government. 14 m. ton capacity	Steel	Lost £ 530 m. in 1979-80 and loss making until 1984-85. Profits £ 76 m. in 1985-86, £ 206 m. in 1986-87.
10.	Steel Authority of India, India, owned by Govt. of India. Sales of Rs.6000 m., 10 m ton capacity	Steel	Lost Rs.2000 m. during 1980-84. Broke even in 1984-85. Profit of Rs.1500 m. in 1985-86, of Rs.3600 m. in 1988-89.
11.	Canadian Cellulose Company, Canada, owned by the Province of British Columbia. Sales C $160 m.	Timber and pulp products	Lost C $70 m. during 1968-72 under private ownership. Lost 20% on sales in 1971. Profit making after take over by government. Earned 27% on sales in 1974, sales climbed 60% above 1972 sales.
12.	State Timber Corporation, Sri Lanka, owned by the Govt. of Sri Lanka, sales Rs.350 m.	Timber and pulp products	Lost SL Rs.5 m. on sales during 1977 and 1978 on sales of around Rs.40 m. Earned Rs.15 m. in 1979 and Rs.84 m. in 1981, and sales increased 9 times by 1981 over the 1977 level.
13.	Zambia Railways, Zambia, owned by Govt. of Zambia. K 400 m. revenues	Railways	Losses upto 1985. Lost K 2.4 m. in 1986. Profit of K 4.3 m. in 1986, profit of K 11.1 m. in 1987.

Note : The above examples are taken from Table 1.1 of ch.1 of Pradip N. Khandwalla's book Innovative Corporate Turnarounds (New Delhi, etc.: Sage, 1992).

Table 11

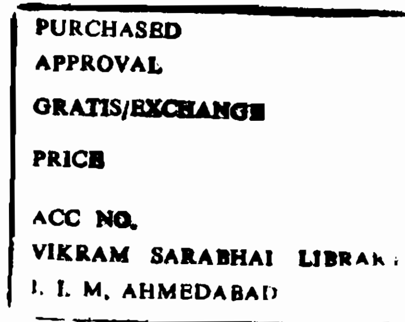
DEGREE OF PRIVATIZATION IN SOME EAST ASIAN COUNTRIES IN KEY INFRASTRUCTURE INDUSTRIES (1992)

	Hong Kong	Indonesia	Malaysia	Philippines	Taiwan	Thailand
Electricity	Over 50%	PSE	Upto 50%	PSE*	PSE	Upto 50%
Water	G	PSE	Over 50%	G	PSE	PSE
Post	G	G	PSE	G	G	G
Airlines	Over 50%	PSE	Upto 50%	Over 50%	PSE	Upto 50%
Telecom	Over 50%	PSE	Upto 50%	Over 50%	G	PSE
Ports	G	PSE	G	G	G	PSE
Airports	G	G	PSE	G	G	PSE
Railroads	PSE	PSE	PSE	PSE	G	PSE
Petroleum	Over 50%	PSE	PSE	PSE	PSE	PSE

PSE = Public sector enterprise run; G = Run by a government department

* PSE was responsible for electricity generation and for national grid; private parties owned local transmission networks.

Source : Trevor MacMurray, "Rethinking privatization" The McKinsey Quarterly, No.1, 1993, pp.35-46.



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