An institutional perspective to international development

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Abstract: The purpose of this paper is to develop an alternative scheme and recommendations for international development based on the institutionalist tradition. Such an exercise of contrasting the institutional tradition with the Washington Consensus and the After the Washington Consensus (AWC) has not been endeavoured. Students of international development would benefit from these findings that distinguish between mainstream and institutionalist perspectives on international development programs. A classification strategy is adopted using the WC and AWC as starting points. The alternative institutionalist development program is scrutinised according to how it varies from the WC and AWC features. The original WC and the AWC are both based on the prevailing mainstream discourse on the relationship between institutions and economic development that requires only institutions that maximise market freedom and protect private property rights. As well, the Washington Consensus and the AWC have a poor understanding of evolutionary character of institutional change, habitually being either overly optimistic or pessimistic about the feasibility of institutional change.

Keywords: Washington consensus; economic development; institutionalism; international development.

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Biographical notes: John Marangos is a Professor of Comparative Economic Systems at the Department of Balkan, Slavic and Oriental Studies at the University of Macedonia. Focal points of John's research include transition processes in Russia, Eastern Europe and the former Soviet Union and Asia, international development, and innovative methodologies for teaching economics. The publications or in the process of publication include: 12 books, 17 book chapters, 70 refereed journal articles, nine refereed papers in conference proceedings, 14 entries in encyclopaedias, one report, seven book reviews, four multimedia developments projects and nine research grants. He is among the top 5% authors in the world according to these criteria: number of journal pages and number of journal pages weighted by number of authors.

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1 Introduction

In 1989, John Williamson (1990) presented the term 'Washington Consensus' to describe the consensus and conditionalities imposed by 'Washington' upon Latin America. The Washington-based United States Executive Branch, the International Monetary Fund (IMF), and the World Bank (WB) are main financiers of anguished developing countries. The Washington Consensus evolved as a prescription for international development under the burden of condemnation, assessment, and ever-changing economic conditions. By 2003, the Washington Consensus policy-set for international development was modified. Accordingly, the initiator of the term designated a 'new' set of policy reforms and a new term, the 'After the Washington Consensus' (AWC).

The theoretical underpinnings of the Washington Consensus and the AWC are based on neoclassical economics and imposed by Washington upon debt-stranded developing countries. In contradistinction, there is a need for (original) institutional economists to offer an alternative to the dominant neoclassical model of international development. The purpose of this paper is to develop an alternative scheme and recommendations for international development based on the institutionalist tradition. Institutionalism, which sometimes is named old or original institutional economics, in the tradition of Thorstein Veblen and John Commons, underline the importance of institutions beyond the market for the functioning of the economy and society (Jameson, 2006). To my knowledge, such an exercise of contrasting the institutional tradition with the Washington Consensus and AWC has not been attempted. Students of international development would benefit from these findings that distinguish between neoclassical and institutionalist perspectives on international development programs. Currently, the dominant discourse on international development in a clear and useful way takes the form of the AWC, applied and imposed by the multilateral donor organisations and developed countries. It is true, that 'Washington' has been excessively passionate in promoting the AWC reforms and possesses the ability to coerce developing countries to their adoption because of their financial power. In consequence, the leverage of these lenders has dwindled, as nations strive to circumvent them with whatever means.

Intriguingly, "some of the free market ideologies in developing countries were even more dogmatic than the ones from the rich countries in a manner that the Latin Americans describe as being 'more Catholic than the Pope'" [Chang, (2011a), p.475]. Latin America's unsatisfactory growth performance, the birthplace of the Washington Consensus and later on of the AWC, is a blunt example of the impact the Washington Consensus and the AWC policies in contradistinction to the performance of the region up to 1980s [Ros, (2011), p.567]. The Washington Consensus policies furthermore led to political instability: "The mix was poisonous, and the 1980s was truly a lost decade economically" [Jameson, (2011), p.536]. Overall, even though, 'Washington', multilateral donor organisations, and developed countries have dispensed over two trillion dollars into African, Latin American, and Asian countries, using as a yardstick the AWC, there are very few success stories in terms of growth-enhancing institutions; the headway made does not match the funds dispersed [John and Storr, (2011), p.585]. The 1980s were followed by attempts to instigate a change policy from

about 1998 onward until commodities collapsed. Also, global outsourcing and the internationalisation of capital yielded demand for policy change. But the devil, of course, is in the details, overall, disarray exists in the house of macroeconomics! [Peterson, (1987), p.1588].

The dynamics between institutions and development are numerous and it is very trying to observe across geographic or temporal contexts [Keefer, (2011), p.544]. Cultures are not homogenous and so cannot with certainty be characterised as pro or anti-development [John and Storr, (2011), p.587]. Thus, Williamson (1999, p.2) knowingly restricted the debate only on economic issues using "simple messages, not nuanced and subtle ones" [Wallis, (2011), p.591]. The institutional approach to international development is undoubtedly not the institutionalism adopted by the AWC, 'institutions for markets' based on neoclassical economics. The AWC, while the Washington Consensus ignored institutions, utilises New Institutional Economics (NIE), the application of neoclassical economics to transaction costs, property rights, contract theory, and public choice [Castellano and Garcia-Quero, (2012), p.924; Richter, 2015]. Nevertheless, the market itself is a social institution. Markets are based on complex rules, social norms and customs, exchange relations and information networks. The establishment and preservation of market institutions is culturally complex, fraught with conflict, and psychologically fragile [Strassmann, (1976), p.76].

I employ a classification strategy using the Washington Consensus and AWC as starting points. The alternative institutionalist development program is scrutinised according to how it varies from the Washington Consensus and AWC features. The alternative set of policies, summarised in Table 1, is a grid in which the rows represent various planks of the Washington Consensus and AWC and the columns represent the institutional alternative. The aim of this format is to give structure to the debate by showing precisely which tenets are challenged by institutionalists, who are fundamentally against the practice of international economic development imposed by the AWC guidelines.

The structure of the paper is as follows: the next section presents the AWC and its relationship with the Washington Consensus. The third section examines the institutional perspective. The fourth section compares the distinct programs and concludes.

2 Washington consensus and the 'AWC'

2.1 Washington Consensus

In November 1989, John Williamson convened a conference to investigate the progress of economic reforms in Latin America in reaction to the debt crisis. In this conference, Williamson (1990) found the opportunity to reveal for the first time the now well-known term 'Washington Consensus'. Williamson (1990) identified and debated ten policy instruments whose proper deployment could muster a degree of consensus in Washington. The ten policy endorsements were converted into 'the Ten Commandments' for international development (Williamson, 2004a, 2004b). The Washington Consensus is presented in Table 1.

Table 1 The AWC, Washington Consensus and institutional policies for international development

After the Washington Consensus		*Policies*	*Original Washington Consensus*	*Institutional policies for international development.*
New Agenda I: crisis proofing	Stabilising inflation, sub-national governments subject to hard budget constraints; increase domestic savings.	Fiscal discipline	Small budget deficit financed without resource to inflation tax.	'Crowding-in' is predominant. Public investment in infrastructure and/or industrial subsidies. Indicative planning.
	Stabilise the real economy through Keynesian policies; establish a stabilisation fund	Public expenditure priorities	Redirect expenditure from politically sensitive areas to fields with the potential to improve income distribution, such as primary education, healthcare and infrastructure.	Eliminating poverty, providing universal healthcare, improving the educational system by providing universal access to higher education.
	Monetary policy targeting for a low rate of inflation; strengthening prudential supervision.	Financial liberalisation	Market determined interest rates.	Development of institutions that create conditions conducive to stable long-term finance for productive investment.
	Flexible exchange rates; minimise the use of the dollar.	Exchange rates	A unified competitive exchange rate.	Fixed exchange rate system as a means to combat the destructive behaviour of speculators.

Table 1 The AWC, Washington Consensus and institutional policies for international development (continued)

After the Washington Consensus		*Policies*	*Original Washington Consensus*	*Institutional policies for international development.*
New Agenda II: completing first-generation reforms	As the original Washington Consensus	Fiscal discipline	Small budget; deficit financed without resource to inflation tax	'Crowding-in' is predominant. Public investment in infrastructure and/or industrial subsidies. Indicative planning.
	As the original Washington Consensus.	Public expenditure priorities	Redirect expenditure from politically sensitive areas to fields with the potential to improve income distribution, such as primary education, healthcare and infrastructure.	Eliminating poverty, providing universal healthcare, improving the educational system by providing universal access to higher education
	As the original Washington Consensus.	Tax reform	Broadening tax base and cutting marginal tax rates.	A comprehensive, non-discriminatory, and enforceable taxation system
	Supplementing financial liberalisation by the strengthening of prudential supervision	Financial liberalisation	Market determined interest rates.	Development of institutions that create conditions conducive to stable long term finance for productive investment.
	Flexible exchange rates minimise the use of the dollar.	Exchange rates	A unified competitive exchange rate.	Fixed exchange rate system as a means to combat the destructive behaviour of speculators.
	Complementing import liberalisation with better access to export markets in developed countries.	Trade liberalisation	Replace quantitative trade restrictions with tariffs of around 10–20%.	A tariff being high enough to protect the reasonable value of labour in the economy
	As the original Washington Consensus.	Foreign direct investment	Abolish barriers to entry for foreign firms.	Develop formal institutional structures to encourage FDI without weakening the efficiency enhancing aspects of informal institutions on inward FDI flows
	Continuing the privatisation program, even though in some cases, it was carried out badly.	Privatisation	State enterprises should be privatised.	There is a role for state property in areas where private property does not function efficiently.
	Liberalising the labour market	Deregulation	Abolition of regulations that impede entry of new firms or restrict competition.	No market is 'free'.
	As the original Washington Consensus, provide property rights to the informal sector, land reform	Property Rights	Secure property rights which are also available to the informal sector.	The introduction of the institution of property into the possession-based systems can occur only through a radical change of the governmental and legal structure into establishing independent property law.

Table 1 The AWC, Washington Consensus and institutional policies for international development (continued)

After the Washington Consensus		*Policies*	*Original Washington Consensus*	*Institutional policies for international development.*
New Agenda III: Second-generation reforms:	A role for the state: maintaining effective institutions, in providing public goods, internalising externalities, correcting income distribution, decent infrastructure, a stable and predictable macroeconomic, legal and political environment and a strong human resource base. Reforming the judiciary, education and civil services, building a national innovation system, modernising the market institutional structure and institutional reform in the financial sector	Institution building	Not a concern.	Reverse causation and endogeneity between institutions and development. It is institutions that use and develop technology.
New Agenda IV: income distribution and the social sector	Establishing property taxation as the major source of revenue; elimination of tax loopholes and taxing income earned on flight capital.	Tax reform	Broadening tax base and cutting marginal tax rates	A comprehensive, non-discriminatory, and enforceable taxation system.
	Expanding opportunities for the poor, spending on basic social services, social safety net, education and health, provide property rights to the informal sector, land reform and microcredit.	Public expenditure priorities	Redirect expenditure from politically sensitive areas to fields with the potential to improve income distribution, such as primary education, healthcare and infrastructure.	Eliminating poverty, providing universal healthcare, improving the educational system by providing universal access to higher education.

2.2 The 'AWC'

Due to the stagnation that Latin America was experiencing in fall of 1999 and after a comprehensive reassessment of Latin America's progress, a new set of policy recommendations was established with the name AWC (Kuczynski and Williamson, 2003). This new set of policies attempted to correct the defects in yet maintain the fundamental tenets of the original WC. The AWC is a set of policies with the goal of reviving economic momentum in Latin American [Kuczynski, (2003), p.31] so "as to put them back on the road of catch-up growth that most people thought they had achieved before the debt crisis" [Williamson, (2003), p.305]. While the original goal of the AWC was to accelerate economic growth, the goal was expanded to include improving income distribution. I outline the policies of the AWC in Table 1 in the order presented by the founders of the term, with the addition of how each policy relates to the Washington Consensus. It appears that there is significant but incomplete overlap: some reforms are the same, while other reforms were added, such as income distribution, the social sector, and institution building.

3 The institutional perspective to international development

Institutional transformation and improvement in developing countries and transition economies (after the collapse of centrally administered socialism in the Soviet Union and Eastern Europe) are fundamental for the proper functioning of a market economy (Frydman et al., (1997), pp.45–46; North, (1990), p.134]. Developing countries and transition economies without the heritage of a market economy, had to provide a hospitable foundation for the establishment of institutions for a market economy [North, (1997), p.16]. An institutional arrangement can be formal or informal [Lin, (1989), p.7].

The role of economic institutions is to make individuals responsive to the economic environment and make the economic environment responsive to individual actions. The institutional structure determines the rules of the game in a society, which are humanly devised restrictions that mould human interaction [North, (1990), p.3]. Institutions identify the constraints within which rational economic actors comprehend, plan and use to achieve their goals. Institutions encourage competitive or cooperative behaviour, reduce or increase transaction costs and provide the organisational foundation for production and exchange [Caporaso and Levine, (1993), p.149; North, (1990), p.5]. In addition, each society's interests are embedded in the institutional structure and institutions change in accordance with customs, regulation, and ideology and ad hoc decisions by those who hold power [Nee and Matthews, (1996), pp.908–909]. "Indeed, the market cannot properly be understood separately from the economic, social and political institutions necessary for its functioning and its legitimacy" [Stilwell, (1996), p.95]. Hence, economic actors struggle to establish institutions to facilitate competition, and to serve their interests through both informal arrangements and formal institutions.

The market process requires "complex institutional arrangements" [Frydman et al., (1997), p.46]. The institutional structure embodies property rights and organisational relations. The most important of these are the state, human and civil rights, property laws, habits and other unwritten conventions. Institutions have an important role in reducing uncertainty, as Keynes (1936), Lin (1989, p.3) and North (1990, p.6) stressed. While uncertainty may have a stimulating effect on the one hand, on the other it discourages

action. Institutions introduce, to a certain degree, regularity, predictability and appropriate responses to unforeseeable changes in the economic environment, in this way facilitating individual decision-making especially with respect to investment decisions. Developing an appropriate institutional structure is essential if developing countries and transition economies were to obtain the potential benefits of market relations. This was because "…exchange presupposes clear boundaries which the system must generate. Without clear boundaries exchange communication may lead to socially and economically intolerable consequences" [Dietz, (1992), p.34]. In addition, the purpose of the institutional structure is to minimise transaction costs associated with economic actors controlling and rendering precise their property rights and exercising these associated rights.

Informal constraints such as trust also have an important role to play in a market economy. Informal constraints cannot be as precisely defined as formal rules. They are extensions, elaborations, and qualifications of rules that 'solve' innumerable exchange problems, not completely covered by formal rules and, in consequence, have tenacious survival ability. Routines, customs, traditions and culture are words we use to denote the persistence of informal constraints. Consequently, path dependence is a major factor in constraining our ability to alter performance for the better in the short run [Lin, (1989), p.21; North, (1997), p.17]. For fear of social opprobrium and ostracism, an individual may be reluctant to violate the informal arrangements, even if the material gains from this violation appear to be very large. Thus, informal institutions play a role in shaping the formal rules [North, (1997), p.4, p.14]. Hence, institutional development in developing countries and transition economies did not only involve the development of formal but also informal institutions. The development of informal institutions could only be gradual.

Considering the aforesaid, institutions are the rules of the game in society and shape human interactions. They are systematic patterns including shared expectations, unquestioned assumptions, and accepted norms and routines of interaction that influence the motivations and behaviour of socially interrelated actors; formal and informal institutions share these properties (Castellano and Garcia-Quero, (2012), p.925; Seyoum, (2011), p.920]. Institutions attempt to handle uncertainty and are crucial in formulation of successful economic development theory and policy. The goal of the institutional approach is to define economic priorities and redistribute wealth and income by promoting development through institutional change and democratic processes. Accordingly, institutionalists promote the awareness and significance of institutions, social values, and inherited customs in the process of development. Nevertheless, the goal of institutionalists is a topic calling for significant attention.

Most institutionalists would advocate wealth distribution which is a normative approach, and some may argue that it is not the prime focus of institutionalism. Especially for Veblen, the task was accuracy in describing monopoly capitalism (theory of business enterprise and absentee ownership stand out in this regard) without ignoring normative propositions. The institutionalists are far from homogeneous and so it is hard to say to what degree economic policy is reduceable to such normative proposition such as wealth distribution. Nevertheless, for our purposes we would maintain this goal of institutionalists, keeping in mind that institutionalism ranges far beyond this proposition.

In the following, the Institutional paradigm on international development is presented by reacting to the AWC (Washington Consensus plus institution building) policies in the order originated by John Williamson.[1]

3.1 Fiscal discipline

Empirical work by mainstream economists has the goal to painstakingly demonstrate that crowding out occurs. Cutting public expenditure means that essential programs for development will be eliminated, thereby causing recession. However, a plethora of studies have shown significant crowding in or inconclusive results: "Crowding out has not occurred and it will not" [Waller, (1989), p.1053]. The substantial decline in public investment, due to the Washington Consensus and the AWC, had an adverse effect on investment as 'crowding-in' is more predominant than 'crowding-out' [Neto and Vernengo, (2004), p.341; Saad-Filho, (2007), p.521]. Early writings on economic development stressed the need for spending on long term projects to support private production. Dams, roads, bridges etc. were needed, but the projects were too big and the pay off in the long run for the private sector. Public investment is necessary to support private consumption and profit. Public enterprises shoulder the large costs, but private enterprises reaped the profits. Public investment and private investment are directly linked, as the costs and profits are allocated to different sectors. Hence, private investments are not necessarily superior to public investments [Chang and Grabel, (2004), p.195]. On reflection, the verdict is that government spending crowds-in private investment in infrastructure, education, health, transportation and communications; while government spending crowds-out private investment in military, welfare and subsidies [O'Hara, (2013), p.36]. The objective of fiscal policy it to attend to social goals by supporting public investment, providing industrial subsidies [de Medeiros, (2011), p.296] based on indicative planning [Waller, (1989), pp.1054–1045]. Consequently, institutionalists are interested in fiscal policy because it is a policy instrument that might allow the solving of pressing economic and social problems, while providing full employment and sustaining economic stability.

3.2 Public expenditure priorities

Public expenditure is the means to create social solidarity, a sense of community purpose, both producing a commitment to overcome social problems as eliminating poverty, providing universal healthcare, improving the educational system by providing universal access to higher education and vocational training [Waller, (1989), p.1054]. Ayres's holds that the rate of development is dependent on the educational level of the society, since education is stimulated by technological processes [Street, (1987), p.1868]. Increasing spending on social programs advances higher levels of social welfare [de Medeiros, (2011), p.297]. In this fashion, a satisfactory rate of economic growth and a more equitable distribution of income and wealth are important policy objectives. "If economic analysis theory cannot point out the way to improving the human condition, it has little relevance" [Peterson, (1987), p.1587]. Economic developments through education expenditure, infrastructural investments, or industrial subsidies, also indirectly promote institutional development, which further promotes economic development [Chang, (2011a), p.477]. As incomes of the mass of poor people rise, resistance to public expenditure lessens, as popular demand strongly supports public investment [de Medeiros, (2011), p.296]. In the General Theory, Keynes (1936, p.357) holds that "the outstanding faults of the society in which we live are its failure to provide for full employment and its arbitrary and inequitable distribution of income". It is a very sorry

fact that we are still struggling with the same problems, due to the fact that public expenditure does not play its proper role in the economy defined by institutionalists.

3.3 Tax reform

The state's incapacity in developing countries to implement a comprehensive, non-discriminatory, and enforceable taxation system is a fundamental constraint on economic growth and development. Insufficient collection of taxes in developing countries reflects the lasting power of the agro-mineral export elite. There is a structural reason for the weak state. When the state is too weak to manage taxation it cannot obtain political legitimacy (Chang, 2002). Economic development requires the creation and expansion of state institutions funded by taxation. Public expenditure priorities, state intervention in general and the directing credit towards industrial investment through loan-finance investments or through providing property titles to entrepreneurs in the form of 'venture capital', all require tax money [Castellano and Garcia-Quero, (2012), p.927]. However, due to globalisation there is a loss of tax autonomy since financial deregulation makes it hard to tax international 'homeless' capital due to the competition for foreign savings through tax incentives. Thus, financial globalisation is well recognised to entail genuine costs, risks and hazards [Nissanke and Stein, (2003), p.290], especially regarding tax policy.

3.4 Financial liberalisation

Financial regulation has the goal to spurn moral hazard, so that banks avoid excessive risk, while regulators protect against bank runs [Keefer, (2011), p.544]. But then again, financial liberalisation, by increasing competitiveness and concentration of the banking system, has not led to an improvement in long-term finance. A sharp increase in nominal interest rates following liberalisation tends to worsen the risk composition of banks' loan portfolios [Nissanke and Stein, (2003), p.290]. Instead, institutionalists are most likely to support lower interest rates and expanding public investment, especially in infrastructure and social welfare. Institutions must ensure that savings will flow into the most productive sectors of the economy to enhance development. These institutions, for instance corporate structures, industrial-financial ownership linkages, legal systems, and international trading institutions and regimes, have the capacity to influence financial markets [Nissanke and Stein, (2003), pp.300–301]. However, the debt crisis cannot be solved only by reducing the rate of interest; there is a need for state loans to finance investments or through 'venture capital' by tax-provided funds (Steiger, 2006). Finally, international capital mobility has significantly increased the degree of instability in developing countries, instead of providing steady funds for productive investment. In sum, the goal of institutionalists is the development of institutional arrangements in the financial market at a domestic and international scale, which create conditions conducive to stable long-term finance for productive investment.

3.5 Exchange rates

Skepticism surrounds exchange rate volatility, as it discourages trade and investment. Most importantly, exchange rate volatility encourages speculation by currency dealers, with the goal of outwitting opponents by predicting their collective behaviour. Exchange

rate dealers desire and perpetuate volatility because volatility provides the opportunity for short-term profit. Stated simply, volatility encourages frequent currency sales and purchases, instigating further volatility. This ultimately establishes a vicious cycle with no end, further destabilising the exchange rate. Undoubtedly, currency dealers are not motivated by their desire to raise world welfare through trade and investment, nor to keep exchange rates stable and reliable. They encourage volatility, while their customers seek protection from the same volatility [Harvey, (1993), p.693]. Ultimately, foreign exchange dealers are encouraged both by economic theory and by their subculture's norms, sanctions, rewards and worldview to encourage exchange rate volatility for self-interest and short term profits [Harvey, (1993), p.694]. Thus, fixed exchange rate system is supported by institutionalist as a means to combat the destructive behaviour of speculators.

3.6 Trade liberalisation

Mainstream trade theory is mainly a theory of the location of production, not a theory of international exchange. International trade reform has little to do with Ricardian classical theory, wherein the factors of production were immobile. Nowadays, production is moved most often to take advantage of low wages and lax environmental standards. Corroborating, trade is to a large extent in intermediate products for further production in comparison to final consumer goods that was Ricardian international trade. An institutionalist perspective differs by offering a more holistic, culture-based approach to the international trade, explicating economic relations among nations operating in a largely interlocked global market environment [Adams, (1987), p.1839; Brent, (1988), p.477]. Upon acknowledgement of the importance of facilitative institutional arrangements that influence external trade, comparative advantage theory becomes obsolete. International competition is an instituted process of collective action, a set of working rules of various and conflicting goals, consistent with the needs, culture, politics, technology and physical environment of the society [Adams, (1987), p.1846; Ramstad, (1987), pp.12–13]. Furthermore, societies are forced to impose special controls and constraints on external exchanges so that their influence on domestic life is restricted to what is judged suitable. "When societies are unable to protect themselves against unwanted external connections they be warped, demoralized, colonized, annihilated, or assimilated" [Adams, (1987), p.1842]. In this context, a tariff has a defensive role and should be based on the comparative cost of labour being high enough to protect "the reasonable value of labor" in the economy [Ramstad, (1987), p.19].

3.7 Foreign direct investment

Today, instead of trade, nations, especially developing countries and transition economies, focus mostly on net foreign direct investment (FDI) (incoming FDI minus outgoing FDI), which may cause intense negotiations and as a result disruption, as they related to copyright ownership and the like. A characteristic example of the divergence of perspectives between developing and developed countries is the attempt to incorporate labour and environmental standards in the WTO negotiation agenda. Developing countries argued that these 'standards' are concealed protectionist measures against WTO's principles, while developed countries insisted that these are general 'standards' are consistent [Chang, (2002), p.543]. In addition, the WTO has forced developing

countries to adopt American-style intellectual property rights laws, while NAFTA has completely changed the institutions that governments use to regulate corporations [Chang, (2011a), p.474]. The multinational corporate structure makes it difficult for a developing country to avoid significant constraints on its development choice. Most importantly, the multinational firm and its power make it very hard for developing countries to build autonomous institutions and policies.

However, FDI inflows cannot solely be determined by conventional variables such as availability of natural resources, human capital accumulation, technological progress, or modern infrastructure. Once proper recognition is assigned to institutions, the crucial role of institutions in attracting FDI is founded [Seyoum, (2011), p.917]. Especially, the existence of informal institutions based on culture with high levels of trust and reputation, and reactions to bad practices such as corruption, has greater effect on inward FDI flows than formal institutions. The relationship between informal institutions and FDI is partially mediated by formal institutions [Seyoum, (2011), p.925]. Some nations, Korea and Taiwan for example, have been able to condition FDI and gain technological spillovers and learning. Others are usually passive, such as Latin America. In view of this, institutionalists advocate reconstructing international institutions based on globally shared values in order to attain greater freedom in international exchanges [Adams, (1987), p.1860].

3.8 Privatisation

It is not ownership that determines efficiency, but rather environmental factors. Thus, the development of a regulatory framework should be a goal for developing economies, not a particular ownership regime. The case for privatisation in the developing countries and transition economies becomes even less clear when the underdeveloped markets for capital, corporate control, and managerial labour are considered. The absence of a capital market where take-over could be initiated, the lack of corporate control in the form of institutional norms and the substantial imperfections in the managerial labour market could only promote managerial failure. The issue is that privatisation enables a transfer of public wealth to the 'few'. The transfers have been massive and continue to be so. Due to privatisation efficiency drops, investment drops, wage shares drop as well. Private property rights largely enable income transfers. Far from being something necessarily to be discouraged, a high degree of state ownership may enable strong protection of private property rights [Chang, (2011a), p.481].

3.9 Deregulation

The role of the state as a central planning agency is very important to the institutionalists in understanding the operation of market capitalism [Street, (1987), p.1863]. On the other side of the fence, mainstream international development theory points out that institutional change that strengthens market freedom is a prerequisite for economic development. According to this view, it is necessary to get the 'prices right', but after getting the 'institutions right' [Dutt, (2011), p.529]. In light of this, what is market freedom and what is a free market? Seemingly, the simple exercise of defining the free market is not so simple any more [Chang, (2002), p.544]. The very definition of a free market depends on whether someone accepts the political and ethical values that complement the institutions of the 'free' market. Consequently, people with diverse

values discover different degrees of freedom within the same market. "In other words, depending on various assumptions one makes about human motivation and psychology, technology, institutions and politics, one can draw any conclusion one likes on the appropriate boundary between the market and the state" [Chang, (2002), p.541].

3.10 Property rights

Without property law guaranteeing the right to burden and collateralise assets, there will be no private individual use of resources. Without the use of assets as collateral, uncertainty increases altering the nature of investment, capital formation, division of labour, and specialisation. There from, the incentive for economic actors is to accumulate short-term inventories, invest in mobile assets and there is a tendency to 'mine' the land by maximising its short-run production at the expense of investment in long-term fixed capital and permanent structures [Kerekes and Williamson, (2008), p.301; De Soto, (1993), p.9]. Ipso facto, the foremost aim of the institutional structure is the establishment of a "system of well-defined property rights which forms the basis for the rationality of behaviour of economic agents and, therefore, the basis for affluence and prosperity" [Klaus, (1995), p.45]. "Formal property systems help take the anonymity out of anonymous markets" [Woodruff, (2001), p.1217].

Steiger (2006, p.184) argues that to be able to explain the rise of private property, one needs to distinguish between property and possession. What has existed at all times and everywhere is possession, not property. In most developing economies, property law may exist. However, the majority of the people are excluded from property use. They have no legal property rights to their resources, they remain outside the market and, therefore, remain poor. Any attempt to transform their informal possessions into universally obtainable, standardised instruments of exchange that are registered in a central system governed by legal rules, involves large transaction costs.

This warrants some elaboration, the very notion of 'property', is not merely possession but institutionalised possession, grounded on the presence of governmental and legal structure "that can legitimate, adjudicate and enforce the relevant rights of property owners" [Chang, (2011a), p.480]. The poor in the developing economies are poor not because they lack resources, but because they are excluded from property rights [Steiger, (2006), p.190]. All assets are being 'owned' by a proprietor and a possessor and their rights are different and distinctive [Steiger, (2006), p.194]. For example, "Britain is a property economy, Peru is not" [De Soto, (1993), p.8].

In much the same way, informal institutions are so prevalent in developing countries, especially regarding property rights that affect business firms engaged in international business, inclusive of multinational entities. The ideas of De Soto can provide some guidance along these lines. De Soto (1993, p.8) argues that developing countries should spend their energies ensuring that property rights are in order, formalised, widespread and protected by law, instead of concentrating on macroeconomic policy. On reflection, "modern market economies generate growth because wide-spread, formal property rights permit, low-cost change, thus fostering specialization and greater productivity" [De Soto, (1993), p.8]. Capital markets fail to most of the population in developing countries because they do not own formally titles of property. As the rights to these possessions are not adequately documented, these assets cannot voluntarily be transformed into capital, cannot be traded outside narrow neighbourhood where people recognise and trust each other and cannot be used as collateral for a loan [De Soto, (2001), p.29]. Even though the

majority do own property, ownership of the property is secured only informally. Individuals invent informal institutions, when formal institutions are absent. Elsewhere De Soto (2000, p.59) says: "squatters housing organizations, mafias and even primitive tribes manage to protect their assets quite effectively". The lack of formal titling and mapping prevents from capturing the full value of their investment, the use of property as collateral and the capital embedded in these assets is 'locked' [Woodruff, (2001), pp.1215–1216]. To sum up, informal businesses and precarious homes are essentially 'dead capital' that should be formalised by the official legal system and turned into liquid capital. Therefore, people can gain access to formal credit, invest in their businesses and homes, in consequence, bolstering the economy [Fernandes, (2002), p.6]. In developing countries, states fail to act in creating and enforcing private property rights.

De Soto's influence can be reasoned by the fact that increasing number of countries and cities, in Latin America and elsewhere, have introduced regularisation policies based on his ideas and these programs have already had a significant impact on international and institutional approaches to property reform and good governance [Fernandes, (2002), p.5]. Nevertheless, in tandem, De Soto's ideas have received heavy expression of skepticism. Gilbert (2012, p.v) holds that "I could not understand why a book based on so little real evidence was so much attention by serious professionals and policy-makers". A striking feature is that "from an academic standpoint, De Soto's most irritating tendency is to reinvest the wheel without acknowledgment. He scrupulously avoids mention of prior work by other researchers or of models, ideas, and policy recommendations previously developed by others" [Bromley, (1990), p.334]. In addition, "His work has failed to qualify the discussion of property rights and he seems to assume that there is universal, a-historical, 'natural' legal definition of such rights" [Fernandes, (2002), p.7].

Regularisation, formalisation mapping and titling of property rights is not enough. Capital markets function poorly in developing countries for reasons other than property rights. Unlocking capital will require more than just recognising existing informal property rights. Improving the efficiency of judicial systems, re-writing bankruptcy codes and laws, restructuring financial and banking regulations are a few of the necessary complementary reforms. "These are swept under the rug in the text of *The Mystery of Capital*" [Woodruff, (2001), p.1222]. Without these essential complimentary reforms, registration systems "are likely to have more limited effect than de Soto's (very refreshing) enthusiasm would lead one to believe" [Woodruff, (2001), pp.1222–1223].

To remove the blatant conflict between property with possession we have to drop the assumption that private property on its own creates security and leads to investment, as the Washington Consensus and AWC stipulate, neglecting the problem of insecurity, when property rights are introduced [Steiger, (2006), p.196]. However, "property is not a thing but a social relation" [Lund, (2000), p.17]. The introduction of the institution of property into the possession-based systems of developing economies can occur only through a radical change of the governmental and legal structure toward establishing independent property laws with access to property rights. This includes possession rights also for the poor. Only such a reform would allow transformation of the poor's resources into property, serving both as collateral for credit and as capital for securing loans [Steiger, (2006), p.202]. Once this happens, contracting and enforcing institutions are endogenously created by the members of society in a decentralised manner [Boettke and Fink, (2011), p.500]. At any rate, "regularization programs should be group specific, taking into account the local historical, cultural and political contexts as well as the existing forms of tenure arrangements, both legal and customary and formal and

informal. Public administrators and lawmakers should refuse the pressure to homogenize land and property laws" [Fernandes, (2002), p.8].

3.11 Institutions building

Past failures to incorporate key institutional characteristics of the economy into economic development programs, as reflected in the Washington Consensus, was the cause of the unwelcoming socio-economic outcomes around the developing world. Local, national, and international institutions all impinge on the development and evolutionary institutional change. However, mainstream institutional theory has a highly problematic understanding of the relationship between institutions and economic development. The AWC based on neoclassical institutional theory "wrongly see the relationship between institutions and economic development as linear and uniform across time and space" [Chang, (2011a), p.482]; actually, the relationship is a lot more complex than what the neoclassical theory, and as a result the AWC, assumes [Chang, (2011b), p.597].

Based on original institutional economics, economic development is not only the product of exogenous technological advance and it is not continuous. "Economic development is, therefore, far from obvious and characterizes only a small part of human history. Stagnation is the normal of [sic]mankind" [Brouwer, (2011), p.505]. institutionalists study the impact of institutions on economic development, appreciate institutions to be the 'working rules of the game' adhered when interacting with one another, making institutions evolutionary in nature; working rules evolve as institutions develop. Obviously, 'working rules of the game' exist in every society, however, institutionalists concentrate on identifying the rules that are most conducive to growth and that determine the long-run economic performance of a society [Brouwer, (2011), p.505]. Institutions should not be mistaken with policies pursued within the given institutional structure. Policies influence short-run fluctuations in economic activity, whereas institutions affect long-run economic performance; "Institutions rule, not policies" [Boettke and Fink, (2011), p.501]. The fact that institutional reform is not about short-term fluctuations, makes it difficult to evaluate institutional reforms in the short run to satisfy international financial organisations. Commons (1950, p.21) holds that "an institution is collective action in control, liberation, and expansion of individual action". Institutions are not just constraints and institutional reform is evolutionary.

The term 'institution' is defined for our purposes, as the combination of formal or written laws rules (statutes, bodies of case law and constitutions); informal habits, social norms or conventions widely shared; and formal organisations of people or groups (courts, the police, civil service bureaucracies, firms, trade unions, families and official international organisations). "The need for combining these three aspects of society into one concept comes from the fact that it is impossible to understand each one and its role in the economy without understanding the others" [Dutt, (2011), p.530]. This perception about institutions is in contrast to the AWC, seeing institutions as only 'constraining' human behaviour and political actions, while falling short in that institutions are also 'constitutive', affecting people's motivations, opinions, worldviews, politics and the acquisition of human capital [Brouwer, (2011), p.509; Chang, (2002), p.556].

The impact and character of institutions on development, owing to the nature of human behaviour and the evolutionary process of social change, demonstrates that their creation cannot be only by government dirigisme; development requires changes in individual mentalities, along with changes in social relations. Consequently, institutional

change for development requires a mixture of spontaneous institutional formation and conscious institutional design [Jameson, (2006), p.373]. For institutionalists, development is more than economic growth. Development is an ongoing evolutionary process involving increasing standards of living and quality of life, and enabling people's self-realisation [Greenwood and Holt, (2008), p.446]. Development involves a revolutionary change in many aspects and patterns of life, a fundamental change in the relative power and position of various groups, and resistance by a complex structure of established social interests and values [Kuznets, (1965), p.3; Street, (1987), p.1871]. Development is conceived by institutionalists as a complex cultural process and not just a mechanical addition to the stock of physical capital. Social and historical contexts clearly matter.

The dynamism for economic development is the utilisation of technological knowledge and instruments. The forces inhibiting social advancement and change are entrenched in existing institutional (ceremonial) patterns of behaviour [Street, (1987), p.1861]. It is institutions that use and develop technology [Greenwood and Holt, (2008), p.449]. Subsequently, developing countries are faced with the dominant influence of outmoded institutions and the subsequent failure to utilise progressive technical knowledge and skills. "While technology has universal adaptability, institutions are culture specific" [Street, (1987), p.1861].

4 Conclusions

This paper presents the institutional paradigm on international development. To give structure to the debate, the analysis was concentrated on identifying the reactions of the institutional economic school of thought to the specific policies of the Washington Consensus and the AWC. Undeniably, these policies are not the only preconditions for economic development.

The alternative institutionalist development program is scrutinised according to how it varies from the WC and AWC policies. The alternative set of policies, summarised in Table 1, is a grid in which the rows represent various planks of the Washington Consensus and AWC and the columns represent the institutional riposte. The aim of this format is to give structure to the debate by showing precisely which tenets are challenged by institutionalists who are fundamentally against the practice of international economic development imposed based on the AWC guidelines. The AWC, is founded on neoliberalism which emerged out of the 'unholy alliance' between neoclassical economics supplying the analytical tools and the Austrian-libertarian tradition, offering the political and moral philosophy [Chang, (2002), p.540].

Using Table 1, it appears that there are no common elements between the Washington Consensus and AWC with the institutional approach to international development. This is not surprising. The Washington Consensus and the AWC are both based on the prevailing neoclassical discourse on the relationship between institutions and economic development that requires only institutions that maximise market freedom and protect private property rights. As well, the Washington Consensus and the AWC have a poor understanding of evolutionary character of institutional change, habitually being either overly optimistic or pessimistic about the feasibility of institutional change. Chang

(2002), p.539, (2011b), p.611] concurs that a marginal tinkering with the neoliberal framework is not enough; words are cheap, as long as, neoclassical economics, provide credible theories that are able to explain institutional changes on the basis complex interactions between material conditions, institutions and individuals. Indeed, "Institutions have become politically too important to be left to those who believe in these simplistic and extremist arguments" [Chang, (2011a), p.495].

Pushing this line of thinking one step further, the institutional framework proposed, in contradistinction to the Washington Consensus and the AWC, is beneficial to all (firms, industries and policy makers) in determining an international business strategy. Peng et al. (2008), p.920] opine that an institutional-based view of international business strategy has emerged as one leg in the 'strategy tripod'. The other two legs are the industry-based view and the resource-based view of business strategy, which assume institutions are 'background', effectively ignoring the formal and informal institutions that provides the context of competition among industries and firms [Peng et al., (2008), p.920]. Institutions significantly shape the strategy and performance of firms inasmuch as strategic choices are not only driven by industry conditions and firm capabilities but are also a reflection of the formal and informal constraints of a particular institutional framework. Considering the aforesaid, institutions, dynamic in nature, both enable and constrain international business strategy, complementing, not substituting, the industry and resource-based views. Due to this telling contribution, the institution-based view of an international business strategy "directly connects the firm-level strategy-making processes with both the micro and macro branches of transaction cost research" [Peng et al., (2008), p.930]. The institution-based view of international business can aid firms to enhance their competitiveness, especially when embarking abroad due to the fact that institutions abroad are likely to differ from the familiar home rules. Overall, an institution-based view, in combination with the industry- and resource based views, place the international business strategy tripod on firmer ground [Peng et al., (2008), p.931]. Peng et al. (2008, p.921) make a powerful case that international business research should focus more on the context of institutions; seen in this light, this paper is telling in that respect.

In this context, it is essential to understand the macroeconomic implications of the institutional framework proposed as they relate to recessions, along with the aforementioned microeconomic implications as they relate to firms and industries. The related policy focus of the Washington Consensus and the AWC on economic liberalisation and macroeconomic stabilisation "overlooked the importance of strong over-arching institutions" [Hodgson, (2006), p.890]. Anomalies of deep recession, debt crisis and financial instability are problems associated with a systemic process of institutional decline and reduced growth and investments [O'Hara, (2013), p.19]. Policies supporting austerity fail to address anomalies of rising systemic risk and uncertainty. The institutional response to recessions, as the proposed framework demonstrates, need to be similarly systemic, requires an institutional structure of preventing inadequate global demand by reversing cuts in productive government spending and providing a mechanism of reducing surplus and deficit current account positions. The proposed institutional framework produces a policy program for the world-system to moderate deep recession, debt crises and financial instability, so as to generate a new systems of governance, investments on innovation and numerous socioeconomic public goods which stimulate long term equitable and sustainable performance [O'Hara, (2013), p.45].

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Notes

1 While the paper only concentrates on the institutional approach for international development for competing approaches and systems of institutional development, please see Marangos (2001, 2002, 2005, 2011).