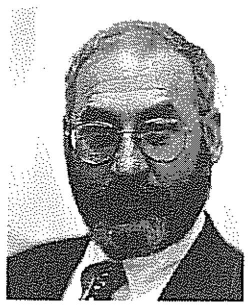
'The whole truth is not on agenda of the 'Knowledge Bank'

FRED HARRISON



JOSEPH E. STIGLITZ has received accolades galore for his cutting-edge economic analysis that was to take him to the White House as chief economic advisor to President Bill Clinton.

He is now chief economist and Senior Vice-President of the World Bank, which proudly claims to be "a Knowledge Bank". Its international corps of top-notch economists hold Stiglitz in awe. He is their guru.

But guru status did not save him from a dressing down on the diplomatic limits to knowledge. Sources inside the World Bank have revealed to *Land & Liberty* that Dr Stiglitz has been "carpeted" for spilling the beans on the defects in "the Washington consensus", and in particular his attacks on the flaws in the financial philosophy of the sister organisation, the International Monetary Fund. The Bank's President, James Wolfensohn, has on several occasions cautioned his Vice President against making embarrassing public statements.

The result, according to World Bank insiders, is that Prof. Stiglitz is now cautious about making public statements. "There is a clamp on what Joe can really do now in public," the source told *Land & Liberty*. For example, said the source, "He is certainly sympathetic with the idea of refocusing Russian taxation on to natural resources and land, and giving business and enterprise a break, but this is not something he can run through the whole machinery of the Bank right now. It would just add gasoline to the fire if he was to do something official as the World Bank chief economist in the Duma" (Russia's parliament).

Professor Stiglitz shoots from the hip. Comments such as the following have not endeared him to the ideologues who shape global economic policy: "If someone says a reform plan has been successful because it has stabilised the exchange rate, I would say he's looking at the wrong indicator because people don't eat foreign exchange".

The problem began when Dr. Stiglitz launched on a critique of Washington wisdom in a lecture at the United Nations University in Helsinki. That was in January last year.(1) He then issued further public statements before stepping beyond the acceptable limits. He was called into Wolfensohn's office.

people to draw on his scholarly writings as an oblique way of hearing what the chief economist has to say on issues like public finance.

THE WITHERING attack on "the Washington consensus" had raised the hopes of critics of the Bank and the IMF. These two institutions have a lock on global financial policies. Governments that borrow money have to relinquish sovereign control to Washington. Critics claim these policies exact an unacceptable price in unemployment and poverty.

Dr. Stiglitz convincingly showed that Washington policies were "not complete, and they are sometimes misguided". Good economic performance, according to this wisdom, required liberalized trade, macroeconomic stability, and "getting prices right". Problems arose when government intervened in the markets. The solution was for government to "get out of the way". Private markets could then allocate resources efficiently and generate robust growth.

Fly in the ointment: the "miracle" of the Asian "tigers". Some of their key policies contradicted the Washington consensus. Yet they "had somehow managed the most successful development in history", Dr. Stiglitz awkwardly pointed out.

The financial crisis that struck Thailand in June 1997 was a god-send. The ideologues condemned the "misguided economic policies" of the tigers. But, countered Dr Stiglitz, "they overlook the successes of the past three decades, to which the government, despite occasional mistakes, has certainly contributed".

WHAT REALLY went wrong in Asia? Dr Stiglitz, a master of the economics of public finance, could not share the triumphant relief of western nations that were losing the war for the wallets of the world's consumers. Nor did he think much of the despatch of western government emissaries to Bangkok, Seoul and Manila to preach the need for less government and more financial "prudence and transparency".

He was to note: "In Thailand the problem was not that the government directed investment … regulators failed to halt it".

In Korea, the problem was not with "the government misdirected credit – the fact the current turmoil was precipitated by loans by so many US, European and Japanese banks suggest that *market* entities may also have seriously misdirected credit. Instead the problem was the government's lack of action..."

RECKLESS credit wrecked Asia. Data in the table below illustrates how South Korea in the 1980s was escalating towards the big fall of the 1990s because money was being systematically shifted into land speculation. Family budgets were squeezed by the cost of housing, the supply and price of which was distorted by the quest for unearned capital gains in the land market.

SOUTH KOREA: economic indicators (1975 = 100)

	1975	1980	1983	1985	1988	Increase
Land Price	100	328	440	533	839	X8.4
House Price	100	355	328	97	466	X4.7
National income	100	142	178	204	287	X2.9
Wholesale price	100	225	284	289	293	X2.9

SOURCE: *The Losses of Nations* (ed: Fred Harrison), Othila Press, London, 1998, p.xxi.

Dr Stiglitz could read the true meaning into these numbers, but for his current views we have to interpolate what he would say in an interview, drawing on his academic writings.

In testing the insights offered by 19th century American social reformer Henry George, Prof. Stiglitz concluded that the efficient way to pay for public services was by drawing revenue from the rent of land. He gave a name to his findings: "the Henry George theorem".(2)

The macro-economic implications of optimum financial policies was not lost on Dr Stiglitz. If government drew its revenue from land-rent to pay for public goods, land speculators would be deprived of capital gains. Their money would have to go into investments that raised productivity and created jobs. No land speculation, no Asian crisis!

Moral from the Stiglitz reading of the economic story: the problem in Asia was not too much government interference in the markets, but the *wrong* kind of interference. Governments that want to avoid booms-and-busts need to treat publicly-created land-rent as public revenue. That would enable them to untax people's wages and savings, the "secret" to long-run equilibrium – the holy grail that eludes the industrial economies. But it is knowledge that Dr. Stiglitz cannot disseminate out of the Knowledge Bank because it exposes the flaw in the Washington consensus.

1 J. Stiglitz, "More Instruments and Broader Goals Moving toward the Post-Washington Consensus", World Institute for Development Economics Research, The UN University, Helsinki, Jan. 1998.

2 J. Stiglitz, "The Theory of Local Public Goods", in *The Economics of Pubic Services* (eds: M.S. Feldstein and R.P. Inman), London: Macmillan,