Development Lessons for Asia from Non-Asian Countries

DANI RODRIK

The disappointments of the Washington Consensus have led to the search for a new paradigm to replace it. The chief failing of the Washington Consensus was that it represented an approach based on "rules of thumb." As such it was not well grounded either in economic theory or in the reality of actual countries. I discuss several strands of new thinking that have appeared following the demise of the Washington Consensus, and argue in favor of an explicitly diagnostic approach.

One always comes with a considerable amount of trepidation when talking about development policy in Asia, a region where development performance over the last two and a half decades has been quite extraordinary with a few exceptions. Perhaps the country that we are in (the Philippines) is one of the important exceptions. Nonetheless this is a region that has done extremely well and it is not entirely clear what an outsider can tell you about what there is to learn about development policy—except to say "well, keep on doing what you've been doing." But as my colleague and co-author Ricardo Hausmann likes to say "Fish don't know they are in water." And sometimes it is helpful to have an outsider with broad comparative experience come and talk about what has worked and (mostly) failed elsewhere to give you a sense of what is it that for the most part seems to have worked here in the Asia and Pacific region, in order that policymakers in this region can keep on the right path.

What I want to talk about is basically the search for a new paradigm. We used to have a paradigm, the Washington Consensus. We are now at a point where I think it is fair to say there is no one who is willing to stand up and defend the Washington Consensus anymore. Even the originator of the term, John Williamson, is willing to defend his version of the original Washington Consensus but not what that term has come to imply and mean these days. The questions now are: what is going to take its place, and what are the new views, new approaches that are coming out.

Dani Rodrik is Professor of International Political Economy at the John F. Kennedy School of Government, Harvard University. This paper was presented in the Asian Development Bank's Distinguished Speakers Program held 31 March 2006 at the ADB Headquarters, Manila, Philippines. The informal style of presentation has been preserved.

Asian Development Review, vol. 23, no. 1, pp. 1–15

Here is an outline of what I want to talk to you about. First, I want to give you a sense of how far we have come from the original Washington Consensus. I think it is important to understand why the Washington Consensus has dissipated and why no one believes in it anymore. Here the fundamental problem is that the Washington Consensus was really a set of rules of thumb, a set of do's and dont's. You liberalize, you stabilize, you privatize. You don't regulate, you don't promote industries, you don't run populist policies and so forth. It is important to understand not simply from the perspective of understanding why the Washington Consensus failed, but also where we will be heading—why rules of thumb of this sort are inevitably doomed to failure. So if our search ends in replacing the original ten commandments with simply a different set of commandments I think we are going to find that the new recipe will prove a disappointment as well. So I want to say a few things about why we need to move away from rules of thumb when we work on prescription.

Next I will survey briefly a set of reactions to the dissipation of the Washington Consensus to see what is out there in terms of post-Washington Consensus ideas. Finally, I will conclude by giving you a flavor—I'm afraid that it will have to be no more than a flavor given the limited time that I have—of some ideas that my colleagues and I at the Kennedy School have been working on to try to develop a much more strategic and much more diagnostic approach to developing growth strategies. This is an approach that says that the new paradigm we need is not one that lists specific prescriptions, but one that helps you think about your problems and how you design approaches and solutions to your specific constraints. Rather than taking an *ex ante* stand on what the problems and their solutions are, this is an approach that helps you diagnose your most pressing problems and corresponding priorities. I hope this will become clearer by the end of my talk.

I. THE COLLAPSE OF THE WASHINGTON CONSENSUS

Let me give you a couple of recent quotes from leading Washington institutions. I think they are important in terms of revealing how far in fact we have moved away from the original Washington Consensus. The first one comes from the introduction to the World Bank's recent book on *Economic Growth in the 1990s: Learning from a Decade of Reform.*

> There is no unique universal set of rules … we need to get away from formulae and the search for elusive "best practices" …. [and] rely on deeper economic analysis to identify the binding constraints on growth… (World Bank 2005, xiii).

This came out late last year and represents as clear an anti-Washington Consensus statement as you can possibly imagine. And you have to bear in mind that this was published in an official report of the World Bank.

Here's another one. This one comes from a regional development bank, the Inter-American Development Bank also based in Washington. The quote is from their *2006 Report on Economic and Social Progress in Latin America*, their flagship publication.

> Whatever the policy area, there is no single formula applicable to all circumstances; policies' effectiveness depends on the manner in which they are discussed, approved, and implemented…. A strictly technocratic approach toward policymaking shortchanges these steps… (Inter-American Development Bank 2005, 3).

This is something that is very similar to the previous quote, and in fact actually cuts a bit deeper. So it is not just that there are no formulas, no single one-size-fits-all approach to development policy, but that you also cannot think about your problems and solve them in a technocratic fashion. You have to be concerned about the manner in which you are thinking about them and the process of developing solutions. And that means that you need to think a lot about the political process within which these solutions are developed.

You are of course familiar with what the Washington Consensus is but I think it is useful to remind you of what it stood for. On the column on the left of Table 1 you have the original Washington Consensus. These were the 10 items that John Williamson included in his list of what countries ought to do—fiscal discipline, reorientation of public expenditures, tax reform, and so on. If you want to summarize those 10 items, it is really about "stabilize, privatize, liberalize."

Table 1. **The Washington Consensus**

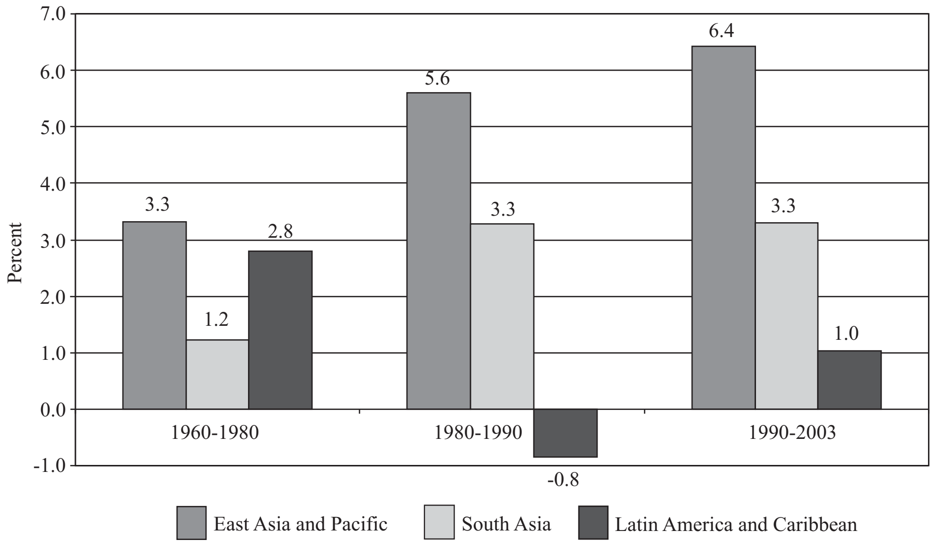
Original Washington Consensus	**"Augmented" Washington Consensus: The previous 10 items plus:**
1. Fiscal discipline	11. Corporate governance
2. Reorientation of public expenditures	12. Anticorruption
3. Tax reform	13. Flexible labor markets
4. Financial liberalization	14. World Trade Organization agreements
5. Unified and competitive exchange rates	15. Financial codes and standards
6. Trade liberalization	16. "Prudent" capital-account opening
7. Openness to foreign direct investment	17. Nonintermediate exchange rate regimes
8. Privatization	18. Independent central banks/inflation targeting
9. Deregulation	19. Social safety nets
10.Secure property rights	20. Targeted poverty reduction

Over time this original Washington Consensus, which was a limited and relatively easy set of policy reforms, has broadened into a much broader agenda of reforms, which I call the *augmented* Washington Consensus. It is important to draw the distinction between the original Washington Consensus and its augmented version because they entail a very different style of reform. The original Washington Consensus was about simple policy levers: to eliminate black market premia, you simply unify the exchange rate, which is something you can do in five seconds. You can eliminate a huge amount of trade restrictions by decree overnight. You can welcome foreign investors by tearing up your old regulations and restrictions. Privatization may take a longer time but it is still mainly an issue of either auctioning off or selling your state-owned enterprises. The one thing on the original list that is institutionally really demanding is item 10, which is secure property rights. In fact the presence of that item in the original Washington Consensus is quite telling about the intellectual climate in which the Washington Consensus developed. John Williamson tells the story of how he listed "secure property rights" almost as an afterthought, to round out the list to 10 items (Williamson 1990). So secure property rights, which in some sense have become the cornerstone of thinking about long-term economic performance, were actually an afterthought in the original Washington Consensus of 1989.

When it comes to the augmented version of the augmented Washington Consensus, everything is about implementing secure property rights and improving institutions and governance. And you might say that is wonderful, in fact I have written papers claiming institutions are fundamental for economic growth and isn't that the end of the story? But I'm going to argue that the augmented Washington Consensus is not a particularly good departure point for thinking about practical development strategies. I'll come back to that at the end of my story.

The facts of the Washington Consensus's failure are fairly clear. Remember that the Washington Consensus originated not in Washington but in Latin America; it was a codification of what those countries were already doing to get growth going. Those countries tried very hard to implement this agenda. From the mid-1980s to the late 1980s onward, these countries did a significant amount of privatization, deregulation, liberalization. They stabilized their economies, brought inflation down, unified currency markets, liberalized trade. In a few years starting from as early as 1985 in Bolivia to as late as perhaps 1994 in Brazil, they did a series of regulatory and trade reforms that were both in context of the history of these countries and comparative economic history quite drastic and quite extensive. What has happened in terms of economic growth? The results were very disappointing. What you can see in Figure 1 is that in the decades prior to 1980, Latin America was lagging behind East Asia and Pacific, but not considerably, and was doing better than South Asia. But then look at what happened in the period since 1990. Since 1990, Latin America has lagged behind both East Asia and now also South Asia—and by a mile. What is especially striking is that Latin America's performance following the adoption of Washington Consensus policies has actually fallen behind the region's own performance pre-1980. By any standard you can imagine, judged by the Washington Consensus (whether it is openness to trade, inflation, regulatory regime, currency regime, or financial liberalization)—in all those dimensions, policies have been far better post-1990 than they were prior to 1980. At the very least, we have a big puzzle.

Figure 1. **Comparative Growth Experience**



In Asia, the countries that have actually done extremely well—for example those that the World Bank has called the "star globalizers" of the last two decades—are countries that have played by very different rules of the game. People's Republic of China (PRC), India, and Viet Nam have maintained throughout the 1980s and 1990s high barriers on imports, in some cases have not even been a member of the World Trade Organization. When they significantly reduced barriers to imports (as for example the PRC did in the mid-1990s and India in 1991), in at least a decade they achieved very rapid economic growth. So it certainly was not the case that import liberalization preceded and ignited growth. It was growth that gave room to the government to actually engage in a much deeper trade liberalization of the sort that Latin American countries were relying on to engineer growth. Neither of course did these countries engage in privatization of state enterprises early in the process of growth.

II. WHY RULES OF THUMBS DON'T WORK

I think it is important to understand what this kind of evidence really means and does not mean. One of the key points that I want to drive home is the idea that we should give up the search for rules of thumb. Let me do this by focusing on perhaps the least controversial area of policy reform: trade liberalization. This is one of the key planks of the Washington Consensus. I want to show that even the simplest, most direct and apparently most uncontroversial policy recommendation is actually contingent on a whole range of other side conditions. In order for us to have a reasonable amount of certainty that the policy is going to work, we need to ensure that a ton of other things are in place as well.

So what does economic theory say about when trade liberalization is actually desirable? Some (but certainly not all) of the conditions are listed in Table 2. As you can see, the list is quite long and involves a complex set of considerations having to do with the extent of liberalization, presence of other market distortions, complementary exchange rate policies, market power in world trade, state of full employment and requisite demand-management policies, distributional effects, fiscal consequences, political economy, and credibility. Even the simplest of policy reforms turns out to hinge on a complex set of prerequisites. An *unconditional* recommendation to liberalize trade implicitly assumes that all the side conditions have been met. But of course the analysis of whether that is indeed so is hardly ever done.

Table 2. **When is Trade Liberalization Desirable (in Theory)?**

The liberalization must be complete or else the reduction in import restrictions must take into account the potentially quite complicated structure of substitutability and complementarity across restricted commodities.
There must be no microeconomic market imperfections other than the trade restrictions in question, or else the second-best interactions that are entailed must not be adverse.
The government must be able to undertake a compensatory devaluation of the currency or else nominal wages must be downwardly flexible.
The home economy must be "small" in world markets or else the liberalization must not put the economy on the wrong side of the "optimum tariff."
The economy must be in reasonably full employment or else the monetary and fiscal authorities must have effective tools of demand management at their disposal.

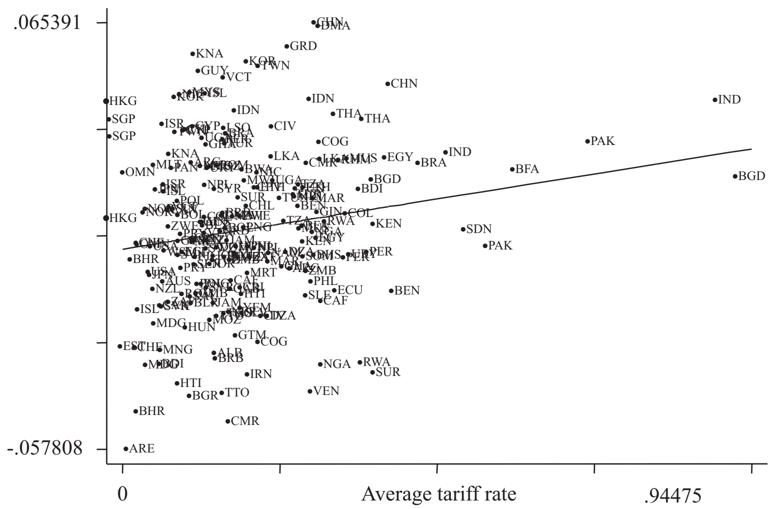
continued.

Table 2. **continued**.

The income redistributive effects of the liberalization should not be judged undesirable by society at large
or else there must be compensatory tax-transfer schemes with low enough excess burden.
There must be no adverse effects on the fiscal balance
or else there must be alternative and expedient ways of making up for the lost fiscal revenues.
The liberalization must be politically sustainable and hence credible
or else the fear of reversal must not lead to too large a consumption boom in imported durables.

You might say that theory is ambiguous (contingent is more correct), but the proof lies with the empirical evidence. But here too it turns out there are no easy answers. Figure 2 shows the (partial) association between average tariff rates and growth rates in the 1980s and 1990s. If anything, the correlation is a positive one, rather than a negative one. Again, this should not be surprising since as I have already pointed out, some of the most rapidly growing Asian countries have had high tariff barriers on trade.

Figure 2. **Relationship between Trade Barriers and Economic Growth**



Notes: The vertical axis is the unexplained component of economic growth. The data are pooled averages for 1980s and 1990s. The additional controls included are initial income, inflation rate, share of government spending in GDP, and a dummy for 1980s.

So what's the point? The point is *not* that trade liberalization is a bad thing or that countries should raise their trade barriers and get out of the World Trade

Organization. The point is that we cannot expect an unambiguously positive response from the typical reform policies—except under specific conditions. That may well be a trite point, but one that the advocates of the Washington Consensus forgot. The Washington Consensus did not say you should undertake trade liberalization only when you have been convinced by extensive analysis or by your knowledge of local conditions that the prerequisites listed in Table 2 are actually in place. It says you go ahead and do trade liberalization, period.

Increasingly, of course, we see in the discussion of trade liberalization (as in other areas), a recognition that reform efforts need to be complementary. Precisely because these reforms have not brought the expected payoffs, their advocates now say "it is not enough to do reform A; you will need to complement it with reforms in areas X, Y, Z." So if you want trade liberalization to work, you need to make sure that labor markets are flexible, that you have a good regulatory structure in place, that you are providing adequate R&D support to firms, that your financial sector is working well, and so on and so forth. This is what intelligent advocates of trade liberalization today are saying. But you have to note that what they are saying is not that you should not do trade liberalization unless you are ensured that those on the side conditions are there. They are saying you should do trade liberalization *and* make sure all those other things are at the same time being done as well. From a policymaker's perspective, this becomes really an unattainable objective: what they have to do in order to make trade liberalization a success is basically all the other reforms that would make them a success regardless of whether they undertake trade liberalization in the first place or not. So one wonders, what's the point of trade liberalization?

There is also something misleading about this kind of recommendation because when people say you should do this and that, there are always three dots ("and so on…") at the end of the statement. The list of complementary reforms is hardly ever a closed list. This way, if the reform fails, policymakers can always be faulted for not having done something that turns out to have been "crucial" *ex post* but not specified *ex ante*.

III. POLICY CREATIVITY INSTEAD OF RULES OF THUMB

All this may sound extremely discouraging because it makes it look highly complicated. How can we possibly know all the prerequisites and take care of all the complementarities entailed in reform? The good news is that once we move away from rules of thumb, we are freed up to design context-specific reforms that can cut across the kind of complicated complementarities I just mentioned. Many successful countries have in fact relied on such short cuts, which often take unconventional forms. So it is not a big surprise that some of the most important ways in which countries have been able to integrate themselves into the world economy have taken the form of unorthodox policies, including special economic zones, export processing zones, export subsidies, two-track reforms of the kind that the PRC has pursued, and so on. The reason that these kinds of reforms have worked where across-the-board import liberalization has not is that the former are more robust to the absence of the standard prerequisites of liberalization.

I usually make this point by going through an extensive counterfactual for the PRC. I start by asking my audience to imagine that they are in the PRC in 1978, just on the eve of the reforms that the PRC undertook to get its economy going. I ask them to think about the kind of reforms they would recommend the PRC to undertake.

The conventional reasoning would go something like this (see Table 3). We need to start from the biggest problem, which is low agriculture productivity in the PRC. So we say the solution is to make rural markets work. We have to liberalize pricing of agricultural crops. Then we recognize that private incentives are not necessarily provided by simply freeing markets in a system where farmers are employed in communes and yet do not have any private property rights. So we recommend privatization of land. The next thing we have to worry about is the fiscal consequences of price liberalization in crops, and therefore we recommend tax reform. In addition, once crop prices are freed up, urban workers will demand higher wages, so we need (at the minimum) to corporatize state enterprises so that they can respond to the demand for higher wages. But of course that raises the problem of monopoly power because these are huge state enterprises. If you give them autonomy to set wages on prices they will maximize their monopoly profits. So we recommend trade liberalization to import price discipline from abroad. But trade liberalization is going to create other problems in turn, and will require restructuring to render enterprises competitive. That requires the financial sector to allocate capital well, so we recommend financial sector reform at the same time. And of course trade liberalization and restructuring may generate unemployment, so we better recommend social safety nets as well.

Table 3. **A People's Republic of China Counterfactual (1978)**

Problem	**Solution**
Low agricultural productivity	Price liberalization
Private incentives	Land privatization
Fiscal revenues	Tax reform
Urban wages	Corporatization
Monopoly	Trade liberalization
Enterprise restructuring	Financial sector reform
Unemployment	Safety nets

By the time we have run through this list and have taken care of all the complementarities entailed in reform, we may feel pretty good about the quality of our advice. But the recipient of our advice would probably think twice about reform. After all, how can all these things be done simultaneously? (Remember that it is crucial for them to be done together; otherwise each on its own will fail.) What kind of government has all the administrative capability, human resources, and political capital needed to undertake such an ambitious reform program? And if this is what is required for successful reform, perhaps it is better to leave reform for another day.

The actual experience of the PRC is instructive because in fact none of the recommendations in the second column of Table 3 was undertaken (at least not quite in the form shown). Instead, what the PRC did was to use two-track pricing, grafting a market track on top of a plan track rather than completely eliminating the plan track, in order to provide supply incentives without generating a public finance crisis at the same time. Rather than tackle the controversial and complicated area of ownership reform head-on, the PRC policymakers implemented innovations like the household responsibility system and township and village enterprises. These were interesting experimental ways of providing incentives both in rural areas and in township industries to generate private entrepreneurship and investment. Rather than opening up their economy to imports in the standard way, with all the restructuring problems that this would entail, they provided incentives for export orientation through special economic zones. And they employed a system that Weingast and Qian have called "Chinese-style federalism" in order to generate incentives for policy competition and institutional innovation among the country's regions. Now most observers with Washington Consensus instincts would have said that these are the wrong ways in which to reform. But in light of the counterfactual story I have just told, it is hard to find fault with the logic of the PRC style of reform.

To be clear, I'm not saying that every country should go and implement two-track pricing and the household responsibility system. I'm just giving this as an example of how context-specific solutions and pragmatic domestic policy responses can overcome some of these complementarities and complications involved in reform. But this is possible only if we move away from ready-made rules of thumb.

IV. POST-WASHINGTON CONSENSUS IDEAS

So where are we now? There have been a number of different reactions to the dissipation of the Washington Consensus, which I briefly review here.

There's one approach that I associate with the International Monetary Fund (or parts of it), which says that the problem is that the Washington Consensus was not really tried. Anne Krueger's title for a speech she gave in 2004 summarizes the basic message: “Meant Well, Tried Little, Failed Much” (Krueger 2004). So governments may have had their hearts in the right place, but they do not get high marks for effort. Much the same evaluation is reflected in a report that the IMF’s Western Hemisphere Department prepared on Latin America, which concludes:

> reforms were uneven and remained incomplete…. More progress was made with measures that had low up-front costs, such as privatization, relative to reforms that promised greater long-term benefits, such as improving macroeconomic and labor market institutions, and strengthening legal and judicial systems (IMF 2005, xiv).

So the problem was that the policymakers took the easy way out and did not complete the reform agenda.

Another related reaction is to look at the same evidence that I briefly reviewed above and conclude that it actually validates the Washington Consensus prescriptions. In the following quote, Larry Summers can be interpreted as arguing that successful countries are those that have done things that are on the Washington Consensus agenda:

> I would suggest that the rate at which countries grow is substantially determined by three things: their *ability* to integrate with the global economy through trade and investment; their *capacity* to maintain sustainable government finances and sound money; and their *ability* to put in place an institutional environment in which contracts can be enforced and property rights can be established. I would challenge anyone to identify a country that has done all three of these things and has not grown at a substantial rate (Summers 2003).

But upon closer reading, it is clear that Summers is saying something quite different. He is talking about the importance of having an *ability* to integrate—but he does not say trade liberalization per se. This leaves room for the PRCs and Indias of the world. He is talking about the *capacity* to maintain sound fiscal and monetary polices—but once again he does not have in mind specific rules (such as low fiscal deficits, independent central bank, inflation targeting, and the like). This leaves room again for the renegades that have done well without any of these (e.g., India). He’s talking about an *ability* to generate an environment in which property rights are established, but not about privatization per se (allowing the PRC and Viet Nam to fit his definition).

So what Summers says defines as successful growth-promoting policy turns out to have very little operational content. It still leaves open the question of what a government is to do.

The third approach, for which I'm partly responsible, is what might be called "institutions fundamentalism." This is actually the position that the augmented Washington Consensus has converged on. Remember that this more recent variant of the Washington Consensus is heavily oriented toward getting governance and institutions and property rights and rule of law right across all sorts of different policy areas. The academic support for this approach comes from the now fairly convincing demonstration that in the long run countries that have attained high levels of income are those with high-quality institutions. This correlation can be interpreted in a causal way as well: the most important way in which you can ensure long-term convergence to the living standards of rich countries is by acquiring high-quality contract enforcement, rule of law, and property rights protection.

Now the bad news here is that just as in my discussion of the Larry Summers quote, the actual policy content of this prescription turns out to be very slim. Much of this line of reasoning deteriorates into a laundry list of institutional prerequisites that all but describe what being developed looks like. By the time you root out corruption, sort out property rights, develop first-world institutions of corporate governance, develop financial market regulation that are best-practice and so on, you are already developed! Which is to say, this is hardly a *strategy* to get there. It does not help policymakers to be told that in order to reach Sweden's income level they need to look more like Sweden.

The good news on this score is that when we look at the evidence of what drives actual instances of growth accelerations, we rarely see large-scale institutional change as the instigator. India doubled its growth rate starting in the early 1980s with no institutional change whatsoever—in any case none that left its mark on paper. In the PRC, there were important policy changes around 1978, as I discussed, but these fell far short of what an institutions fundamentalist would have liked to see. All of which suggests that the ambitious agenda of governance reform that the World Bank often pushes for is not only impractical, but also unnecessary to get growth going. This agenda confuses what needs to happen eventually for long-term income convergence with what can be done now to improve matters.

The *UN Millennium Report* (UN Millennium Project 2005) represents yet another approach. It focuses on the Millennium Development Goals and on attaining them by 2015. It proposes to do so by significantly scaling up investments in human capital, public infrastructure, and public administration, with these investments being financed by a combination of increases in foreign aid and national resources. I will not say much about this except that there is little evidence for generalized poverty traps of the sort that provide the conceptual underpinning of the Millennium Plan approach. As I've said before, when we look at the actual evidence on how growth happens it seems to happen not through wholesale, large-scale, and complementary investments but through a sequence of strategic interventions that seem to relax binding constraints over time.

V. TOWARD A DIAGNOSTIC APPROACH

In my own work, what I am drawn to is precisely that kind of approach that focuses on the binding constraints and on diagnosing them appropriately. This is an approach that allows different fixes for different countries, yet provides a unified way of analyzing their problems and generating policy priorities. It relies crucially on diagnostics—on being able to identify areas with greatest return to reform. Of course poor countries are poor because they have many things that are wrong with them. But the diagnostic approach aims to figure out where the most binding constraints on economic growth are at any particular point in time. The idea is that by focusing administrative and political capital on those areas where the bang for the reform buck is biggest, we might be the most effective. This is also a promising way to identify country-specific programs because it is based on the idea that the binding constraint will differ from setting to setting. Therefore when we do the analysis right we will end up with policy solutions that differ according to setting.

Very briefly, the growth diagnostics approach is based on trying to identify what is the most important constraint blocking private investment (Hausmann et al. 2005). It proceeds in the form of a sequence of questions. Is private investment blocked primarily by low return to economic activity or primarily by high cost of finance? If it is high cost of finance, do the problems lie with domestic financial markets or with the country's poor entry into international financial markets? If it is bad domestic local finance, is the problem with poor intermediation or with low domestic savings? On the other side, if low private investment is due to low returns to economic activity, we ask whether it is social returns that are low, or it is the appropriability of those returns that are low. If it is low appropriability, is that due to government failures or market failures? If it is government failures, what are they? And so on.

I think this will give you an idea of the type of exercise that is entailed in implementing this approach. We basically move down a decision tree, trying to identify the relevant branch to take at each node. So if at the end of the process we identify, say, poor intermediation as the binding constraint on investment, that is going to call for a different kind of policy than if we had instead identified low human capital as the constraint.

Can this type of exercise be done? It is not very easy, and probably there is more craft than science involved in doing it well. But to me, it is not clear what the alternative would be. This seems to be the only way we can sensibly approach and develop country specific programs and priorities.

Let me give you a flavor of how many of these ideas can be operationalized by focusing on one example. Suppose we are trying to decide whether the problem is one of low returns or of high cost of finance. Depending on where the problem is, the economy will throw out very different kinds of diagnostic signals. In a country where the problem is low returns to economic activity, you will have banks running after customers, low interest rates, and current account surpluses. If for whatever reason there is an increased inflow of foreign resources, this is going to raise consumption rather than investment. So in all these respects an economy where the binding constraint is low returns will behave very differently than an economy where the binding constraint is high cost of finance. In the latter economy, interest rates will be high, borrowers will be chasing after banks, and liquidity will be tight. Anytime there is a relaxation of the external constraint the result will be high investment rather than high consumption.

The diagnostic approach is obviously one that needs to be repeated over time. If the diagnosis at time T is the correct one, the resulting growth will make something else the binding constraint at time T+1. In other words, we also need to think of *institutionalizing* the diagnostic process so that this becomes a habit of mind, the natural way in which policymakers think about their problems.

It goes without saying that the diagnostic approach is no panacea. Much thought and hard work needs to go into filling in all the operational details. And often, the answers will not be clear and we will not be able to pin down the binding constraints convincingly. Nonetheless, the approach has the advantage that it is inherently bottom-up: it empowers countries to do their own analyses—search for their own binding constraints and short-cuts to relax them—instead of relying on international financial institutions to present ready-made solutions.

REFERENCES

Hausmann, R., D. Rodrik, and A. Velasco. 2005. "Growth Diagnostics." Kennedy School of Government, Harvard University, Massachusetts. Available: http://ksghome.harvard.edu/~drodrik/barcelonafinalmarch2005.pdf.

Inter-American Development Bank. 2005. *The Politics of Policies: Economic and Social Progress in Latin America, 2006 Report*. Washington, DC.

International Monetary Fund. 2005. Stabilization and Reform in Latin America: A Macroeconomic Perspective on the Experience Since the Early 1990s. IMF Occasional Paper, Washington, DC.

Krueger, A. 2004. "Meant Well, Tried Little, Failed Much." Remarks at the Roundtable Lecture at the Economic Honors Society, 23 March, New York University, New York.

Summers, L. 2003. "Godkin Lectures." John F. Kennedy School of Government, Harvard University, Massachusetts.

UN Millennium Project. 2005. *Investing in Development: A Practical Plan to Achieve the Millennium Development Goals*. New York.

Williamson, J., ed. 1990. *Latin American Adjustment: How Much has Happened?* Institute for International Economics, Washington, DC.

World Bank. 2005. *Economic Growth in the 1990s: Learning from a Decade of Reform*. Washington, DC.