Beijing Consensus versus Washington Consensus

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Ever since I suggested that there was a useful measure of consensus at the end of the 1980s about the policies that Latin American countries needed to adopt in order to end the debt crisis and start building a brighter future, a vast number of consensi have been proclaimed. Apart from my own Washington Consensus, there is the augmented Washington Consensus (with parts of which I differ profoundly), the Barcelona Agenda (which was almost called a Consensus), the Beijing Consensus, the Beijing-Seoul-Tokyo Consensus (the “BeST Consensus”), the Buenos Aires Consensus, the Copenhagen Consensus (though this dealt with different issues and was not aimed at replacing the Washington Consensus), the London Consensus, the post-Washington Consensus, the Santiago Consensus, the Seoul Consensus, and the Singapore Consensus. Doubtless other cities have had consensi named after them.

Let me state at the outset that I do not believe that listing desirable policies solves all of the profound problems of economic development. I agree with Dani Rodrik (2007) in believing that there are also issues of priority and implementation that agreement on the objectives does not address. I nevertheless do believe that a clear view of the proximate objectives is valuable. I also believe that there are major differences between alternative statements of what commands a consensus. Accordingly I take the view that I have a topic worth discussing.

Since I do not propose to inflict on the reader a summary of a dozen or so different policy agendas that have been claimed to be relevant, I have a first problem of deciding which of the several candidate consensi I wish to discuss. In view of the widespread interest in the subject, it is natural to include the Beijing Consensus. In view of the widespread use of the term, plus its pioneering role in initiating the debate, it is also natural to include the Washington Consensus. But the latter confronts a major problem: The term has been used in at least two major senses, and the present author has no sympathy for the one that has reached the most widespread status. To describe the Washington Consensus as embodying neoliberal, minimalist-state views (as the popular view of the Washington Consensus does) implies that these doctrines command, or commanded, a consensus in Washington, which is not factually correct. In my view this version of the Washington Consensus was invented only to be a whipping boy. Accordingly I shall use the term in my original sense, which bears little relationship to the popular, or populist, version, although I make occasional references to major differences. (Among the consensi listed above, the one that comes closest to my original sense, though it is expressed less clearly, is the Seoul Consensus.)

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1 A paper prepared for the Handbook of Emerging Economies, edited by Robert Looney. The author is indebted to Nicholas Lardy for helpful comments, but he is absolved of all responsibility for views expressed.
The Beijing Consensus

An immediate problem in discussing the Beijing Consensus is to know what it means. The term was introduced by Joshua Cooper Ramo (2004), but he offered no list of the recommended policies. I concluded in a prior discussion that the Beijing Consensus should be defined as the policies pursued by China (Williamson 2012a). This has the virtue of being what most of the enthusiasts appear to mean by their use of the term, and it is also the sense in which Stefan Halper (2010) uses the term in his book with that title.

Hence in this paper we shall contrast the policies pursued by China with those called for by the Washington Consensus.

My version (as opposed to the popular version mentioned above) of the Washington Consensus may be summarized as follows (Williamson 1990):

1. Fiscal discipline. Governments should aim to restrict budget deficits to a level that can be financed in a non-inflationary manner. (I should have added that if interpreted as a medium-run objective this can be a corollary to, rather than competitive with, fiscal policy being conducted in a counter-cyclical manner.) NO VIEW WAS TAKEN, OR IS IMPLIED, ABOUT THE RIGHT COMBINATION OF EXPENDITURE RESTRAINT AND TAX POLICY TO ACHIEVE FISCAL DISCIPLINE.

2. Public spending. Governments should redirect public expenditure from low-priority expenditures like general subsidies to education, health, and infrastructure.

3. In re-designing tax policy, governments should aim to raise revenue by a broad tax base combined with moderate marginal tax rates.

4. Governments should aim for domestic financial liberalization. (I initially focused only on interest-rate liberalization, which is too narrow a focus; I failed to acknowledge the importance of accompanying liberalization by the establishment of effective financial supervision; and I did not make it clear that I regarded the liberalization of capital flows as a low-priority objective.)

5. The exchange rate should be unified and set at a level that is competitive. (I define a competitive rate as one that is not overvalued, i.e. is either correctly valued or undervalued.)

6. Governments should liberalize trade, initially by tarrifying import restrictions and subsequently by reducing tariffs. It was admitted that views differ about both the...

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2 He tells us that the Beijing Consensus consists of three theorems, but these are not sufficiently well-defined to identify the Beijing Consensus.
speed with which tariffs should ideally be reduced and the expediency of allowing the process to be interrupted by adverse economic developments.

7. Inward foreign direct investment should be allowed without restriction.

8. State enterprises should be privatized. (The statement is somewhat bald, but was intended to imply that every Latin American country had state enterprises that would be better off privatized rather than that there is never a justification for state enterprise.)

9. Entry and exit to industries should be de-regulated.

10. Secure property rights should be extended to the informal sector.

Having thus specified the competing frameworks, our remaining task is to ask which of them provides a better guide to successful development.

Gradualism versus Shock Treatment

Many adherents of the Beijing Consensus (henceforth BC) explicitly favored gradualism (based on Deng’s calling for feeling the stones when crossing a river) whereas the subject is not broached by the Washington Consensus (henceforth the WC), because I did not perceive it to be a major issue facing Latin America in 1989. When I have been forced to face the issue subsequently, I have argued that gradualism has merits when there is a society that has not already fallen apart and a leader who is confident of remaining long enough to effect his/her reforms. But often those conditions are unrealistic: the economies in question have already broken down, or else a leader feels that s/he has to act quickly before s/he loses office. I certainly do not believe that many of the former Communist societies had the opportunity to effect gradual and effective reform in 1989-91.

Encouraging Innovation

This has again been explicitly favored by many adherents of the BC, while the WC is silent on the topic. One could make a case similar to that offered above for not including this topic in the WC, but in this case there is an argument for regarding the omission more seriously. A popular recent development has been the tendency to assert the existence of a “middle-income trap” (see, for example, World Bank and Development Research Center of China’s State Council 2012), and one antidote suggested is to change the mix of industries in which a country specializes to more technology-intensive, or innovation-intensive, ones. I am concerned that the notion of a “middle-income trap” has never been properly demonstrated and that it may well be an illusion (Williamson 2012b). But I did not claim to prove the converse,
and the possibility should be taken seriously. The Beijing Consensus, unlike the WC, mentions a possible antidote.

There is also a possible downside. The key to catch-up growth is imitation, not innovation, and it is possible to waste resources re-inventing the wheel (as Brazil used to do in the days when it prohibited the importation of computers).

**Macroeconomic Stability**

This was a major theme in the WC (items 1-3, though monetary policy was not mentioned, betraying the historic origins of the WC). Beijing has maintained something close to price stability ever since 1949, even during the Great Leap Forward and associated famine, when there was a massive increase in food prices. When necessary, notably during the world recession starting in 2008, it has employed Keynesian policies of demand stimulation in order to keep the economy near full capacity operation. In giving a high priority to maintaining macroeconomic balance, China has proved typically Asian. This part of the WC has received has never been problematic in Asia.

Other countries have now followed the Asian and WC lead: rapid inflation has been essentially eliminated from Africa and Latin America. Item 1 of the WC is not controversial. There have of course been innumerable fights (not least in Washington) about the mix of expenditure cuts and tax rises used to achieve fiscal discipline, but the goal is no longer seriously contested. As I emphasized in the preceding presentation of the WC, the mix that should be used was not a part of my version of the WC, although the populist version of the WC called for this to be achieved by expenditure reduction.

**An Open Economy**

Points 5, 6, and 7 of the WC deal with this topic, calling for a competitive exchange rate, trade liberalization, and opening toward inward FDI. (My version of the WC, unlike the popular version, specifically did NOT call for countries to engage in general capital account opening.) Beijing liberalized inflows of FDI very early in the reform era and beginning in the mid-1990s reduced protection substantially as a condition for joining the WTO, so there is no contradiction on points 6 and 7. Exchange rate policy is less clear. By a “competitive” exchange rate I understand one that is not overvalued, so that technically Beijing (which has in practice used an undervalued exchange rate as the main tool for achieving its occasionally large and certainly consistent current account surpluses) satisfied this one too. Moreover, if one measures the openness of the economy in the traditional way, by the ratio of exports to GDP, then the Chinese economy is the most open large economy in the world.
I nonetheless feel some qualms about declaring China guiltless in terms of its external relations. This is primarily because it remains opposed to any attempt to impose an international discipline on exchange rates\(^3\), and certainly has not abandoned the practice of running an undervalued exchange rate and the resulting current account surplus.

The contradiction between Beijing and Washington centers on the question of currency valuation. There are two separate issues in contention: one is the method of determining the exchange rate, the other concerns the level of the exchange rate. The two are often confused. China for long fixed its exchange rate in terms of the US dollar, and then after announcing that it was going to start floating it in fact moved to a crawling appreciation against the dollar. Holding its exchange rate at an undervalued level involved large intervention, and many US economists objected to the intervention per se (and argued that the renminbi should instead float) rather than to the level at which the intervention occurred. My own objection is centered unambiguously on the level, and I have no objection to the fact of intervention: in fact I favor a managed exchange rate, which implies a need for regular intervention. (Those who demand that China floats seem to have great faith that the RMB would be better behaved than many other floating rates have proved, and float to a level at which the current account and/or the basic balance would be in equilibrium, so that the two demands would have similar results.)

I do not think the central issue on which Beijing and Washington differ is well caught by the WC (primarily because this was written for Latin America at a time when there was on prospect of the region developing current account surpluses). The fundamental issue is whether surplus countries have a duty as a member of the international community to take action to curb their surpluses. Even though I believe the demands coming from Washington have confused this message by expressing it as a demand for floating, the basic demand seems to me entirely reasonable, and I would like to see it codified as an IMF duty to avoid large surpluses. The fact that Beijing resists the notion of placing a limit on the surpluses that countries should pursue is a dis-service to far more than the United States: it also makes life far more difficult for most other developing countries, as well as to the cause of building a robust international system, and to the Immediate prospects of restoring prosperity in the advanced world.

Market Liberalization

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\(^3\) It has argued that setting an exchange rate is an inherent feature of national sovereignty. Since an exchange rate is by definition the ratio permitting one currency to be converted into another, this is not true. In international monetary economics this is known as the “n-1 problem”, which was resolved by the passivity of the United States in the Bretton Woods system. China appears to have taken this passivity as an inherent fact of life rather than a policy choice.
The demand for market liberalization is expressed in #4, 6, 8, 9, and perhaps 10 of the WC. This is surely the most basic difference between Beijing and the WC: the fact that even stripped of the absurdities of demands for a minimal state and a belief in the ubiquity of perfect competition (characteristics of the popular version of the WC but emphatically not my version), the WC is basically pro-market while Beijing allows a far larger role for the state. Indeed, since macro-stabilization and opening up to international trade (globalization) are nowadays uncontroversial in most of the developing world, one infers that it was this aspect of the WC which provoked the strong reactions to it.

On the general topic of market liberalization, I would offer two reactions. The first is that Beijing has in fact undertaken a fair measure of market liberalization, and that it is this that prompted the impressive growth of the Chinese economy, rather than the continuing existence of SOEs. By the end of the 1990s China had already liberalized most commodity (though not factor) prices. In 1978 three-quarters of manufactures in China were produced by SOEs, while this figure had fallen to under one-quarter by 2010. (And this decline is not an artifact of changing definitions: SOEs include those that have listed on national or foreign stock exchanges but still have major government participation.) Desire to proclaim a BC is more a characteristic of Western than of Chinese economists.

The second is that there are different forms of market economy, and it is far from obvious that the only way, let alone the right way, to define a market economy is by the absence of the state. This is shown most clearly by the fact that many countries have developed an anti-monopoly (anti-trust) policy. If the maintenance of vigorous competition is dependent upon state action, and one regards a market economy as characterized by competition, than a market economy depends on state action. Of course, it is state action of a particular kind, and does not suggest that all state actions (such as nationalization or the institution of an industrial policy) are to be welcomed. The point is that one cannot judge a market-oriented policy by the test that was often used in the aftermath of the crisis, the minimization of the role of the state.

Four, maybe five, forms of market liberalization were included in my statement of the WC. The first is financial liberalization. In the light of subsequent history, it is quite clear that a liberalization of the financial system needs to be accompanied by adequate prudential supervision. Without this, there is a serious danger of the financial system being abused as a conduit for transferring wealth to the particular individuals who control the financial institutions. Provided this is done, the logic of financial liberalization is that investment decisions are best made on a decentralized basis by individual credit managers considering whether the prospective risk/return characteristics of particular investment projects appear sufficiently attractive to merit support. Presumably there are those who do not accept this logic and envision countervailing advantages in investment decisions being made centrally by "the planners", which would justify opposition to this element of the WC.
The second element of market liberalization included in the WC is trade liberalization. Opponents of liberalization have often pointed out that most presently developed countries went through a phase of protecting their infant industries when they were developing, and therefore accuse those who argue that presently developing countries should liberalize trade of hypocrisy. There are several answers to this critique. First, past levels of protection were modest compared to the barriers that many hopefully developing countries erected in the postwar period. Second, it may be that protection was a bow to sectional interests that impeded overall development in the now-developed countries, rather than the boon to development that is portrayed. It is certainly not true that every presently developed country embraced protection at some stage: Hong Kong provides the most vivid counter-example. Third, while it is difficult to refute the argument that some protection of infant industries may help to establish new industries, it is easy to point to examples of industries that have failed to grow up and continued to need protection for many years.

One should also note that the WC is to be judged as a whole rather than by its independent parts. It is absurd to blame Argentina’s trade liberalization for its economic collapse and ignore Argentina’s failure to maintain a competitive exchange rate; trade liberalization only makes sense if there are thriving export industries into which the resources displaced from import-competing industries can flow.

The third policy favored by the WC that furthers market liberalization is privatization. China showed no hurry to privatize, and many of the remaining state industries proved useful in one capacity that had largely been overlooked during the long period of world prosperity that preceded the world crisis. Specifically, they provided a direct means of rapidly injecting additional demand into the economy at the start of the recession, which enabled China to recover from the world recession far more quickly than other countries. Small companies and private individuals also benefited from the rapid credit expansion by the state-owned banks, but the majority of the additional spending was done by SOEs.

It is, however, wrong to regard this as the only factor at stake in choosing the size of the state sector. Most analyses, including comparisons of the performance of various sectors in China, favor privately-owned over state-owned companies. For example, the study by the World Bank and the Development Research Center of China’s State Council (2012, p.211) calculated the return on equity in state and private companies over the years 1998-2009 and showed that the return was always greater in private enterprises, approaching being double by 2009. Similarly, the National Bureau of Statistics has found the return on equity was always greater in the private sector, and was most recently over 14% (versus under 6% for the state sector). Despite this, privatization probably heads the list of the unpopular elements of the WC. One reason for this is without much doubt the manner in which privatization has often been undertaken: corruptly, so as to channel rents to cronies.
Clearly privatization needs to be handled transparently and in a manner that can be expected to have no first order effects on income distribution, and this should have been added to the WC to have any hope of producing a statement of consensus views.

The fourth element of the WC that was intended to promote a market economy was deregulation. I was careful to specify that by this I meant the abolition of restrictions on entry and exit; I did not make the mistake of calling for the wholesale abolition of regulations intended to promote such causes as consumer safety, financial probity, worker welfare, and environmental sustainability. The model was the spate of deregulation in the United States of things like airlines and trucking that had been started by the Carter Administration. Most countries, both developed and developing, maintain quite unnecessarily many restrictions on entry to certain industries, including the liberal professions.

The final element of the WC that has often been taken to be pro-market was the furthering of property rights, with the emphasis on extending these to the informal sector reflecting specifically (though not exclusively) Latin America. Secure property rights are usually reckoned to be of fundamental importance to growth in a market economy, since no one has an incentive to take care of the future unless they expect to be the major beneficiary. Dani Rodrik has often remarked on the paradox of China’s fast growth rate in view of its dubious property rights.

I never claimed that the WC contained all the elements needed for fast growth. If one asks what the East Asian countries that enjoyed fast growth had in common, the answer is a demographic transition; competitive exchange rates; good education; high savings; and macroeconomic stability. If one excepts Hong Kong, one can add an active state role, typically taking the form of an industrial policy. Demographic factors are exogenous. A competitive exchange rate was applauded (explicitly) in the WC. Education made it only parenthetically, in #2, but there would seem no contradiction. High savings were not mentioned at all, because this was not perceived as an obstacle to Latin American countries escaping from the debt crisis in 1989, but it is difficult to envisage a coherent objection. Macro stability was certainly emphasized by the WC. In any event, the element on which opponents of the WC have seized (notwithstanding the embarrassment of Hong Kong, which was simply declared a city-state and therefore irrelevant) is industrial policy.

A lot seems to hang on exactly what is understood by “industrial policy”. If one interprets it in the traditional sense of “picking winners”, there is little reason to think that the state is particularly good at it, and the serious counter-objection that investment projects should be decided by those who stand to win or lose, depending on the outcome. But if it is interpreted in the sense that Dani Rodrik (2008) does, of government recognizing that it has a responsibility for compensating firms for the main external effects to which they are subject (i.e., for internalizing externalities), then only a rabid believer in the popular version of the WC would be likely to object.
Authoritarianism

A conspicuous feature of Chinese policy is the hostility evident to any sort of democratic ideal. Despite the recent revelations about the wealth accumulated by some of the leaders, it is not clear that the Chinese leadership wants to hang on to power for the sake of material advantages, in which case one is faced by the conundrum of explaining just why they oppose democracy. One possible motivation is the fear that populists would win a democratic election, which has been known to happen in the West. Another possible explanation is a genuine belief that democracy is a Western rather than a universal value, coupled with a belief that it is their mission to oppose all things Western. Whatever the explanation, it is a fact that they act in an authoritarian way.

Not only do they refuse to countenance democracy at home, but they always oppose efforts to use the international organizations to spread any sort of democratic (or, for that matter, human rights) notions. This is done in the name of national sovereignty, which means that it is often popular with the public of the affected state as well as (naturally) with their rulers.

The WC contained no reference to democracy either, essentially taking the view that recovery from the debt crisis was possible whatever the political system (both in a newly-restored democracy like Brazil and in a country like Mexico, which was still an autocracy in 1989). I am firmly convinced that this is right (for reasons that I explain in Williamson 2012, based on Doucouliagos and Ulubaşıoğlu 2008): that there is no relation (or only a very weak relation) from the form of government to the rapidity of growth. Admittedly there are some economists who argue that growth is dependent on having “inclusive” institutions (Acemoglu and Robinson 2012). Now inclusive institutions are not quite the same as democratic institutions, and it is possible that China has developed an inclusive form of non-democracy. It would be interesting to know what this is. (This argument, which seems essential to their thesis, is nowhere made in Acemoglu and Robinson 2012.)

Concluding Remarks

There are two reasons why following the WC might not induce rapid growth, quite apart from the possibility embraced by the critics that the policies are basically wrong. The first is that it was not constructed for that purpose, and therefore it omits certain policies that are essential. The second is that it was designed to be an expression of consensus views, and if some essential policies were espoused only by a minority then they would not appear. In practice I would judge the first factor to
be the overwhelmingly important one. The examination of the individual policies recommended by the WC did not reveal any to be inappropriate, let alone harmful.4

If growth is essentially replicable, i.e. if following the same policies achieves similar results (because growth is not heavily dependent on natural features of the economy), then one knows that adopting the BC will result in fast growth. The problem (since in practice one cannot exactly adopt all the policies) is in knowing which are the essential features of Beijing’s policies that merit adoption. For example, I would doubt whether China’s resistance to democracy or its friendship to dubious regimes has speeded growth, though it is possible (some would argue that democracy complicates the problem of acquiring the resources needed for investment projects). As regards the essential features responsible for China’s fast growth, I would personally plump for the list offered earlier of the five or six commonalities between East Asian fast growers: demographic transition, competitive exchange rate, good education, high savings, macro stability, and perhaps a government that actively aims to internalize externalities. As argued earlier, there is some, but not much, overlap between these policies and those in the WC. This does not make the policies listed in the WC silly or inappropriate or harmful, it simply means that they need supplementing to have a list of the objectives which should be pursued by a country interested in achieving rapid growth. And then, as admitted at the beginning, there are also issues of priority and implementation that have to be addressed.

4 I reached a similar conclusion when I was invited by the World Bank to consider the appropriateness of the Washington Consensus as a formula for development (see Williamson 2005).
References


