# Why Larry Summers Drove Joseph Stiglitz Out of the World Bank

by William Engdahl

Within days of his being sworn in a year ago as U.S. Treasury Secretary, Larry Summers put all his considerable weight behind a drive to have World Bank Chief Economist Joseph Stiglitz ousted from that post. The background to what might seem to be just another case of Washington political infighting, demonstrates what is wrong with much of current U.S. Treasury Department policy, and why earlier calls for a major shakeup of the International Monetary Fund (IMF), for founding a New Bretton Woods system, or even the far milder call by President Clinton in 1998 for creation of a "new architecture" for international finance, have totally disappeared from Administration discussion. Summers, as Stiglitz recently pointed out, is little more than a proxy in government for the traditional interest of Wall Street financial houses and major banks. For them, return on investment comes first, even at the expense of the standard of living of hundreds of millions of innocent victims.

Stiglitz's criticism of Treasury's support for Wall Street policy interests, as well of the IMF role in developing country financial emergencies, comes a full quarter-century after *EIR* founder Lyndon LaRouche launched a campaign to end the role of the IMF as "debt enforcer" for London and Wall Street interests in developing countries, charging that IMF policies were "100 times worse than Hitler."

Despite the lateness of his conversion to the ranks of IMF opponents, however, Stiglitz's campaign is highly useful, in that it reinforces LaRouche's call for a New Bretton Woods conference to replace the bankrupt IMF system.

## Serving Wall Street 'Special Interests'

In an interview with the May 25 *Australian Financial Review,* the American Stiglitz accused the Summers Treasury of acting as the battering ram for Wall Street. He charged that the problems arising from the recent Asia crisis are the result of "broad economic policy being determined by special interests. When the Treasury pushes for Wall Street, people sometimes think it's the high-minded, good policy, and they don't see it for what it is, which is financial markets' interests, which may or may not be good policy."

The background to Stiglitz's remarks sheds light on why, as one of his first priorities upon taking over Treasury in July 1999, Summers set out to drive Stiglitz as far from the public stage as possible. Indications are that Summers has failed badly, given Stiglitz's numerous public comments since leaving the World Bank.

The policy fights between Stiglitz and Summers go back to the early days of the Clinton Administration. Stiglitz was a prominent academic economist who came to the Clinton White House to serve as chairman of the President's Council of Economic Advisors (CEA). Summers was brought to Washington as Harvard's youngest tenured economics professor, to serve as Assistant Treasury Secretary for International Economic Affairs.

In late 1993, for example, Summers and Treasury were pressing within the Clinton Administration to force South Korea to accelerate liberalizing its domestic financial and economic markets, including lifting capital controls. CEA chairman Stiglitz opposed Summers's move, arguing that gradual liberalization was needed. Summers and Wall Street won out. "Most people now agree," Stiglitz said, that "it was rapid capital-market liberalization that was at the root of the [Asian economic] problem, and Larry and I had a very big fight in 1993 when I was in the White House." Stiglitz argued that it was not in U.S. national interest to push Korea to open up its markets faster. "This was not number one on our priorities. . . . This was not going to create a lot of jobs for Americans," Stiglitz said. "Second, it was simply bad policy. This is pursuing special interests over national interests. And Larry pushed this through, reflecting the interests of Wall Street."

In 1996, President Clinton nominated Stiglitz as Chief Economist and Vice President of the World Bank. Whether the assignment was part of Summers's covert effort to get Stiglitz out of the White House, any thought Summers may have entertained that that would have ended Stiglitz's role in Administration policy, was shattered during the 1997 Asian crisis. By 1998, Stiglitz began writing signed newspaper commentaries, including in the *Wall Street Journal,* opposing the IMF role in the Asian events. In the April 17 *New Republic* magazine, Stiglitz wrote, "I was chief economist at the World Bank from 1996 until last November, during the gravest global economic crisis in half a century. I saw how the IMF, in tandem with the U.S. Treasury Department, responded. And I was appalled."

Noting that the crisis had been made possible as a result of Summers's earlier efforts to force Asian countries to lift capital controls, leaving them vulnerable to a sudden flight of



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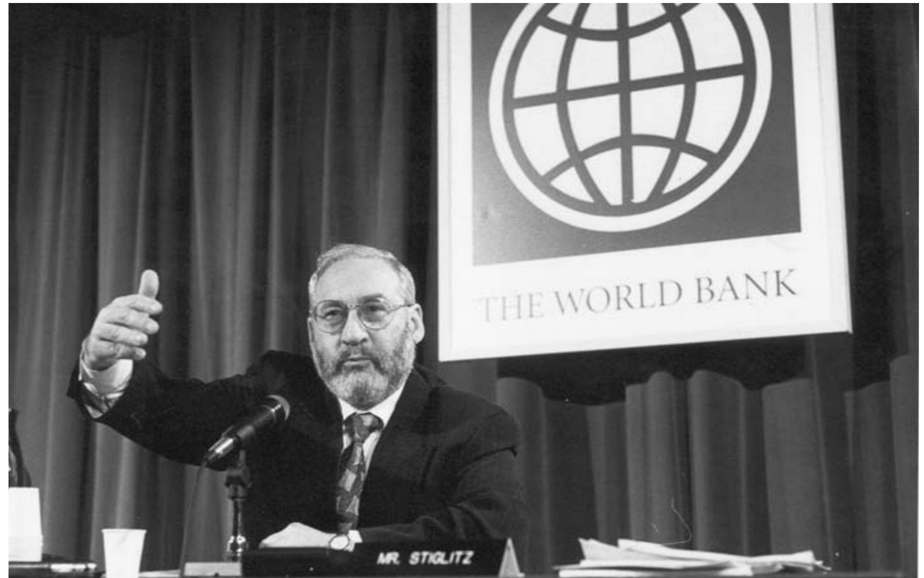


*Joseph Stiglitz (right), former chairman of the President's Council of Economic Advisers, was forced out as Chief Economist of the World Bank by Treasury Secretary Lawrence Summers (left). The policy championed by Summers, compelling Asian nations to liberalize their markets, "was simply bad policy. This is pursuing special interests over national interests. And Larry pushed this through, reflecting the interests of Wall Street," said Stiglitz.*

short-term capital, Stiglitz recounted that Summers called for using the IMF to deal with the Thai currency crisis, much as the IMF had dealt with Ibero-America in the 1980s. "So in 1997," he recalled, "the IMF imposed the same demands on Thailand. Austerity, the Fund's leaders said, would restore confidence in the Thai economy. As the crisis spread to other East Asian nations—and even as evidence of the policy's failure mounted—the IMF barely blinked, delivering the same medicine to each ailing nation that showed up on its doorstep. I thought this was a mistake."

Stiglitz recounted how he tried to press for a policy change. "I talked to Stanley Fischer . . . the IMF's first deputy managing director. I met with fellow economists at the World Bank who might have influence within the IMF. . . . Changing minds at the IMF was virtually impossible." He said that, when he pressed IMF officials as to why they refused to change, they only replied, "pressure coming from the IMF board of executive directors." The largest voting director on the IMF board is the U.S. government, with 18% of the vote. It is represented by the U.S. Treasury.

"By January 1998," Stiglitz continued, "things had gotten so bad that the World Bank's vice president for East Asia, Jean Michel Severino, invoked the dreaded r-word ('recession') and d-word ('depression') in describing the economic calamity in Asia. Lawrence Summers, then Deputy Treasury Secretary, railed against Severino for making things seem worse than they were, but what other way was there to describe what was happening? Output in some of the affected countries fell 16% or more. Half the businesses in Indonesia were in virtual bankruptcy or close to it. . . . Unemployment soared as much as tenfold and real wages plummeted."

He added, "Not only was the IMF not restoring economic confidence in East Asia, it was undermining the region's social fabric. Then, in spring and summer of 1998, the crisis spread beyond East Asia to the most explosive country of all—Russia."

Stiglitz directly blames Treasury, going back to the early Clinton years, for manipulating what at the time was a genuine debate over what economic policy should be urged upon the former Soviet Union. Stiglitz and economist Kenneth Arrow were part of one group of regional experts. "This group emphasized the importance of the institutional infrastructure of a market economy—from legal structures that enforce contracts to regulatory structures. . . . Arrow and I had both been part of a National Academy of Sciences group that had, a decade earlier, discussed with the Chinese their transition strategy. . . . We favored a more gradual transition to a market economy."

Unfortunately, a second group won the policy debate over Russia. "The second group consisted largely of macroeconomists whose faith in the market was unmatched by an appreciation of the subtleties of its underpinnings—that is, of the conditions required for it to work effectively. These economists typically had little knowledge of the history or details of the Russian economy, and didn't believe they needed any. . . . Shock therapy works for countries in transition to a market economy: The stronger the medicine, so the argument goes, the quicker the recovery."

Stiglitz said, "The Treasury Department and the IMF made sure there was no open debate. . . . The IMF and Treasury had rejiggered Russia's economic incentives—but the wrong way. By paying insufficient attention to the institu-

tional infrastructure that would allow a market economy to flourish—and by easing the flow of capital in and out of Russia—the IMF and Treasury had laid the groundwork for the oligarchs' plundering. While the government lacked the money to pay pensioners, the oligarchs were sending money obtained by stripping assets and selling the country's precious national resources into Cypriot and Swiss bank accounts."

He added, "The United States was implicated in these awful developments. In mid-1998, Summers, soon to be named Robert Rubin's successor as Secretary of the Treasury, actually made a public display of appearing with Anatoli Chubais, the chief architect of Russia's privatization. In so doing, the United States seemed to be aligning itself with the very forces impoverishing the Russian people. No wonder anti-Americanism spread like wildfire."

## Ending the 'Washington Consensus'

It is no secret in Washington that Summers's campaign was behind Stiglitz's resignation from the World Bank in November of that year. Stiglitz has subsequently identified Summers's personal role, as has *New York Times* senior journalist Louis Uchitelle, who wrote that Summers forced Stiglitz to resign. The accusations made by Stiglitz explicitly citing the pernicious policy role of Summers since 1993, all were made after Stiglitz had left public service and resumed a tenured teaching post and part-time position with the Brookings Institution. Ironically, since leaving the World Bank, in many respects Stiglitz appears freer to launch pointed attacks on Treasury's wrong-headed policy under Summers.

Yet, the reason why Summers moved obsessively to force Stiglitz out of the Bank, was the fact that Stiglitz, in speeches delivered around the world, repeatedly assailed the IMF's fundamental policy flaws in the handling crisis since 1997.

Stiglitz's attack on the IMF role was centered around the so-called "Washington Consensus." While most of the general public has never even heard of such a concept, it is known in official IMF and international economic policy circles as the Magna Carta of IMF policy.

In 1990, John Williamson, an economist at the Washington Institute for International Economics, and who was involved in the disastrous 1980s Ibero-American debt crisis, published for the annual IMF/World Bank Washington meeting, a menu of ten "idiot simple" policy reforms that should be the basis of IMF and World Bank policy toward Ibero-American debtor nations. This Washington Consensus, which subsequently became official IMF policy, mandated that a victim-country impose ten measures in order to receive IMF help: fiscal discipline (i.e., slash public spending, even on food subsidies for the poor); redirect public spending for high economic return; broaden the tax base; liberalize interest rates; let the exchange rate be "competitive"; liberalize trade; permit free foreign investment flows; privatize state companies; deregulate, especially to foreign entry of capital; and secure property rights.

## 'Still Waiting for Development'

Such medicine, Stiglitz indicated, was worse than the disease. In a speech to a conference of the Ministry of Land Reform in Brasilia, Brazil in July 1998, in the midst of the Asian crisis, yet before the August eruption of the Russia default and the early-1999 Brazil crisis, Stiglitz, still in the World Bank Chief Economist post, declared, in reference to the economies of Ibero-America during the 1980s and early 1990s: "These countries have followed the dictums of the Washington Consensus—bringing down inflation and budget deficits, liberalizing trade, privatizing state-owned enterprises, and 'getting the prices right'—but are still waiting for development. If it is coming at all, it is coming too slowly. The reason for the failure of the Washington Consensus to fulfill its promises is that it not only pursued too narrow a set of objectives—an increase in GDP per capita—but that it saw development from too narrow a perspective in two senses.

"First, the instruments it chose to focus on—trade liberalization, privatization, and macroeconomic stability—although important, sometimes confused means with ends, and in any case ignored other equally important instruments." Stiglitz contrasted the negative Ibero-American experience in implementing the IMF Washington Consensus, the so-called IMF "conditionalities," with the example of China. "China accounts for two-thirds of the increase in the total income of low-income countries over the last 20 years," Stiglitz said. "Yet China did not follow the dictums of the Washington Consensus. It emphasized competition over privatization: Standard economic theory says both are required for an effective market economy. The Washington Consensus emphasized one; China the other. We see the track record. It should not be surprising. . . . Privatizing a government monopoly is often likely to create a private monopoly with high prices and continued inefficiency. . . . Topics left out by the Washington Consensus are perhaps even more telling: financial markets, competition and regulation, transfer of technology, development of institutions—to name but a few whose importance has been increasingly recognized."

However useful Stiglitz's public campaign over the past several years to foster a genuine public policy debate over the failure of the IMF might be, it is far from sufficient. At least in his public pronouncements to date, he has stopped short of the most fundamental critique of the IMF and Summers's Treasury policies, namely, their failure to recognize the urgent necessity for a comprehensive new global monetary order, as Lyndon LaRouche has put forward in his proposal for a New Bretton Woods system. That is now the next step required to secure a sane, moral global economic framework that would ensure real per-capita, per-hectare rising standards of living and longevity. To take that on, as Japan, Malaysia, and other nations well know, means taking on the power behind the IMF: the power of a global financial oligarchy centered in London and New York, which has backing from every major bank and insurance group in continental Europe and Japan.