ESSAY

LAW AND NEOCLASSICAL ECONOMIC DEVELOPMENT IN THEORY AND PRACTICE: TOWARD AN INSTITUTIONALIST CRITIQUE OF INSTITUTIONALISM

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INTRODUCTION

In his 1993 Nobel Laureate lecture, the leading theorist of institutional economics, Douglass North, emphasized the relevance of his life's work for economic development policy.[1] Twenty years prior, in his book with Robert Thomas entitled *The Rise of the Western World*, North had laid out the theoretical connection between institutional economics and development: economic growth could not occur without efficient institutional arrangements and property rights, and the "rise of the West" could be explained in these terms.[2] In another influential book, *Institutions, Institutional Change and Economic Performance*, published just a few years before he received the Nobel Prize, North had again argued that his view of institutional economics had primary significance for economic development.[3]

By the time North accepted the Nobel Prize two decades after his original exposition in *The Rise of the Western World*, his hypothesis about the relationship between law and economic growth had won extraordinary recognition in development policy. North's neoclassical theory of the state, in which appropriate laws and institutions supported the market ideal of efficient transactions among private actors,[4] provided the conceptual basis for a new era of development programming in which principles of "good governance"—in particu-

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1 Douglass C. North, Economic Performance Through Time, Nobel Lecture (Dec. 9, 1993), *in* NOBEL LECTURES IN ECONOMIC SCIENCES 1991–1995, at 112 (Torsten Persson ed., 1997) (emphasis added):

> Economic history is about the performance of economies through time. The objective of research in the field is not only to shed new light on the economic past but also to contribute to economic theory by providing an analytical framework that will enable us to understand economic change. A theory of economic dynamics comparable in precision to general equilibrium theory would be the ideal tool of analysis. . . . *A theory of economic dynamics is also crucial for the field of economic development.*

2 *See* DOUGLASS C. NORTH & ROBERT PAUL THOMAS, THE RISE OF THE WESTERN WORLD: A NEW ECONOMIC HISTORY 1 (1973) ("Our arguments central to this book are straightforward. Efficient economic organization is the key to growth; the development of an efficient economic organization in Western Europe accounts for the rise of the West.").

3 *See* DOUGLASS C. NORTH, INSTITUTIONS, INSTITUTIONAL CHANGE AND ECONOMIC PERFORMANCE 9 (1990) ("[I]f I describe an institutional framework with a reverse set of incentives to those [that are efficient and conducive to economic growth], I will approximate the conditions in many Third World countries today as well as those that have characterized much of the world's economic history.").

4 *See* DOUGLASS C. NORTH, STRUCTURE AND CHANGE IN ECONOMIC HISTORY 20, 23 (1981).

lar, the establishment of the "rule of law" and the implementation of property rights—became key focal points of policy reform efforts.[5]

In the 1990s, the goals of legal and institutional reform modified the menu[6] for the transformation of the developing-country macroeconomic regimes that had come to be known as the "Washington Consensus."[7] Beginning in the 1980s,[8] the Washington Consensus was a blueprint for the implementation of the neoclassical economic policies[9] of the Chicago School:[10] liberalization of trade, privatization of investment, fiscal austerity, and monetary stabilization.[11] These

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[5] For a discussion of how these law and development programs emerged, see *infra* Part I.B. For a critical evaluation of these programs, see *infra* Part II.B.

[6] For a discussion of this development, see *infra* Part I.B.

[7] This term arose because the three most influential actors in setting the global development policy agenda endorsed it. Those actors were the World Bank, the U.S. Treasury, and the International Monetary Fund. *See* Narcís Serra et al., *Introduction* to THE WASHINGTON CONSENSUS RECONSIDERED: TOWARDS A NEW GLOBAL GOVERNANCE 3, 3–4 (Narcís Serra & Joseph E. Stiglitz eds., 2008) (defining the Washington Consensus as "the set of views about effective development strategies that have come to be associated with the Washington-based institutions: the IMF, the World Bank, and the US Treasury").

[8] The economist John Williamson coined the term "Washington Consensus" in 1989. *See* John Williamson, *A Short History of the Washington Consensus*, *in* THE WASHINGTON CONSENSUS RECONSIDERED: TOWARDS A NEW GLOBAL GOVERNANCE, *supra* note 7, at 14. By the time he coined the term, however, the policy reforms it described had been in place for several years; indeed, this was the very meaning of the term *consensus*, denoting an observation of agreement on policy reforms arising over a period of time.

[9] Williamson himself has repeatedly objected to using this term to denote the neoclassical economic theory associated with the rise of the conservative Reagan and Thatcher governments of the 1980s. *See id.* at 22. Williamson's original conceptualization of the term denoted a more moderate set of beliefs. *See id.* at 16–17; *see also* Yoram Margalioth, *Intellectual History as Legal Analysis*, 96 CORNELL L. REV. 1025 (2011). Williamson has acknowledged that a sense of personal ownership over the term fueled his objections. *See* John Williamson, *What Should the World Bank Think About the Washington Consensus?*, 15 WORLD BANK RES. OBSERVER 251, 251–52 (2000) ("I find that the term has been invested with a meaning that is significantly different from that which I had intended . . . . I had naïvely imagined that just because I had invented the expression, I had some sort of intellectual property rights that entitled me to dictate its meaning, but in fact the concept had become public property."). Despite those objections, the association of the Washington Consensus with neoclassicism has prevailed, and in using the term in this way, I join the ranks of, among others, Nobel Laureate Joseph Stiglitz, who attracted Williamson's ire for the same reason. *See* Williamson, *supra* note 8, at 22 & n.6 (objecting to the use of the term "as a synonym for neoliberalism or market fundamentalism" and citing as an example JOSEPH E. STIGLITZ, GLOBALIZATION AND ITS DISCONTENTS 74 (2002)).

[10] *See* STIGLITZ, *supra* note 9.

[11] For a discussion of the Washington Consensus, see STIGLITZ, *supra* note 9, at 67. Stiglitz groups the concepts of fiscal austerity and monetary stabilization into the term *macrostability*. *See id.* High inflation and fiscal deficits were viewed as the two major threats to such stability; prevention of inflation through both monetary policies, including high interest rates and through reduced public spending was viewed as paramount to stabilization. *See* José Antonio Ocampo, *A Broad View of Macroeconomic Stability*, *in* THE WASHINGTON CONSENSUS RECONSIDERED: TOWARDS A NEW GLOBAL GOVERNANCE, *supra* note 7, at 63 (critically contrasting this view with the earlier Keynesian view). Though Williamson did not identify monetary stabilization in his original list of Washington Consensus policies, the focus of many developing-country reform programs of this era, particularly in Latin America, was on curbing inflation. *See* Andreas Freytag, *The Credibility of Monetary Reform—*

"structural adjustment" reforms of the 1980s, which focused on pure macroeconomics,[12] were theoretical relatives of the later "turn to institutions" of the 1990s.[13] In the former era, laws figured primarily as instruments to achieve economic policy reform, whereas in the latter, legal reform was to serve as an end in itself towards economic growth.

Part I.A demonstrates the genealogical connection between these two eras of law and development, beginning from the Coase Theorem, through rent-seeking analysis and public choice theory, to the institutional economics of North and others.[14] Neoclassical understandings of the market informed both models, and each constituted progeny of neoclassical theories of the relationship between markets and institutions.[15] Although legal and institutional development programs have been portrayed as the result of a learning process in which development practitioners realized that the desired macroeconomic policy reforms were ineffective without appropriate institutions and laws,[16] that learning process has been bounded by the theoretical constraints of neoclassicism.

More recently, as Part I.A.5 suggests, human rights and other justice concerns have played an explicit role in shaping law and development priorities, although the impact of those concerns on underlying neoclassical priorities remains indeterminate and a subject for further study. This Essay, part of a larger intellectual history project, concerns itself with delineating (in Part I) the bedrock of the neoclassical law and development paradigm, those aspects of it which persist despite more recent modifications, and the ways (in Parts II and III) in which those aspects could be improved.

New Evidence, 124 PUB. CHOICE 391, 398–99 (2005); *see also* Chantal Thomas, *Labour Migration as an Unintended Consequence of Globalization in Mexico, 1980–2000*, *in* SOCIAL REGIONALISM IN THE GLOBAL ECONOMY 273, 277–79 (Adelle Blackett & Christian Lévesque eds., 2011) (describing Mexico's stabilization programs of the era). The focus on monetary stabilization was induced not only by the devastating impact of inflation on the domestic populations of these countries but also by the theoretical focus of the neoclassical Chicago School on supply-side economics and monetary policy.

12 *See* YVES DEZALAY & BRYANT G. GARTH, THE INTERNATIONALIZATION OF PALACE WARS: LAWYERS, ECONOMISTS, AND THE CONTEST TO TRANSFORM LATIN AMERICAN STATES 172 (2002).

13 Kerry Rittich, *The Future of Law and Development: Second-Generation Reforms and the Incorporation of the Social*, *in* THE NEW LAW AND ECONOMIC DEVELOPMENT: A CRITICAL APPRAISAL 203, 210 (David M. Trubek & Alvaro Santos eds., 2006).

14 *See infra* Appendix.

15 *See also infra* notes 221–32 and accompanying text.

16 *See* KENNETH W. DAM, THE LAW-GROWTH NEXUS: THE RULE OF LAW AND ECONOMIC DEVELOPMENT 4–5 (2006) (describing the rise of "neoclassical economic policy" as a "second stage of economic development thinking," which challenged and reversed the heavily statist approach of the earlier postwar era and then describing how this "search for new solutions led to an increasing focus on how poorly many developing country governments functioned and especially on widespread inadequacies, even corruption, of public regulatory bodies and of the legal system").

Part I.B argues that a key opportunity to move beyond macroeconomics to laws and institutions arose out of a crucial shift in the legal interpretation of the World Bank charter's prohibition against interference in the "political affairs" of borrower states.[17] The redistribution of power among members of the international community that occurred at the end of the 1980s[18] supported a reinterpretation of that provision that in turn enabled the adoption of programs which previously would have been considered impermissible interferences in sovereignty.[19] As a consequence of these events, the New Institutional Economics (NIE) could and did join the New Political Economy (NPE) as a basis for international development policy.[20] What followed was an explosion of programs for the reform of legal institutions in developing countries that has been termed "rule-of-law revival."[21] This paradigm for thinking about law, economic development, and institutions implemented programmatically the neoclassical "revolution" in economic theory,[22] which was carried out in particular corridors of the economic and legal academies.

The neoclassical institutionalist paradigm in law and development, however, has proved resistant to some forms and sources of knowledge. Part II takes up some of these challenges, as identified by

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17 *See* INT'L BANK FOR RECONSTRUCTION & DEV., ARTICLES OF AGREEMENT art. IV, § 10 (1989), *available at* http://siteresources.worldbank.org/EXTABOUTUS/Resources/ibrd-articlesofagreement.pdf [hereinafter IBRD ARTICLES] ("The Bank and its officers shall not interfere in the political affairs of any member . . . .").

18 *See* DAM, *supra* note 16, at 4–5, 22 (discussing neoclassical movement's development policy leadership).

19 *See* IBRAHIM SHIHATA, *The World Bank and "Governance" Issues in Its Borrowing Members*, *in* THE WORLD BANK IN A CHANGING WORLD: SELECTED ESSAYS 53, 58 (Fransizka Tschofen & Antonio R. Parra eds., 1991); *see also infra* Part I.B.

20 *See* DEZALAY & GARTH, *supra* note 12, at 164.

21 *See* Thomas Carothers, *The Rule-of-Law Revival*, *in* PROMOTING THE RULE OF LAW ABROAD: IN SEARCH OF KNOWLEDGE 3, 3–4 (2006). Popular programs focused on the judiciary and on property rights. This was consistent with the idea that an independent and well-functioning judiciary was necessary for the effective enforcement of law in general, for the support of stable and predictable legal rules, and for the enforcement of property and contract law in particular. *See id.* at 17, 20. Programs for the improvement of property law through land-titling systems have also been popular. *See generally* Stephen Golub, *The Legal Empowerment Alternative*, *in* PROMOTING THE RULE OF LAW ABROAD: IN SEARCH OF KNOWLEDGE, *supra*, at 181 (discussing land-titling systems in Ecuador).

22 Part I is influenced by the Kuhnian argument that scientific knowledge arises through key historical moments—"scientific revolutions"—that establish theoretical paradigms. *See infra* text accompanying notes 25–27. In adopting a Kuhnian approach, I am influenced by David Scott. *See* DAVID SCOTT, REFASHIONING FUTURES: CRITICISM AFTER POSTCOLONIALITY 8–10, 124–29 (1999). For a discussion of knowledge practices in law, see Annelise Riles, *Legal Knowledge* 1–4 (Cornell Law Sch., Research Paper No. 05-034), *available at* http://ssrn.com/abstract=851885. This approach is consistent with constructivist and discursive analyses, which I have employed in other work. *See, e.g.*, Chantal Thomas, *Democratic Governance, Distributive Justice and Development* 4, *in* DISTRIBUTIVE JUSTICE IN INTERNATIONAL ECONOMIC LAW (Chi Carmody, Frank Garcia & John Linarelli eds., forthcoming 2011) (manuscript at 4) (on file with author).

a growing body of contemporary scholarship on law and development.[23] Some of these critiques are particular to neoclassical law and development, but others are generalizable to the field more broadly. Some point to theoretical inconsistencies; others point to difficulties in application.[24] One serious drawback, which the legal literature has not yet sufficiently discussed, stems from the difficulties proponents have encountered in showing that the causal relationship defining the hypothesis—that better institutions lead to stronger economic growth—can be demonstrated empirically.

Part III considers the implications of Part I and II for contemporary law and development discourse. The theoretical and practical challenges described in Part II suggest the need for a framework that would improve the quality of information available to law and development analysts and provide strategies for correcting the influence of powerful interests in donor and beneficiary countries on development policy, as well as the powerful effects of ideational constructs. As such, this Essay suggests that law and development discourse should be more responsive to its conceptual and empirical limitations. Part III identifies specific areas for analytical improvements in theoretical and practical law and development frameworks premised on institutionalism.

Institutionalism propounds a particular set of theoretical assumptions about the role of law in economic growth. In unpacking the development of those assumptions, this Essay adopts a model of intellectual history based on the Kuhnian argument that scientific knowledge evolves through key historical moments—"scientific revolutions"—that establish theoretical paradigms.[25] These paradigms are replaced only when awareness in the field of anomalies—problems that the existing theoretical paradigm cannot solve—presents a crisis for that paradigm that coincides with the emergence of an "alternate candidate."[26]

The paradigm shift in law and development was enabled by dynamics in both the academy and the field. In the academy, the emer-

23 *See, e.g.*, DAM, *supra* note 16, at 2–6; MICHAEL J. TREBILCOCK & RONALD J. DANIELS, RULE OF LAW REFORM AND DEVELOPMENT: CHARTING THE FRAGILE PATH OF PROGRESS 1–7 (2008); Thomas Carothers, *The Problem of Knowledge*, *in* PROMOTING THE RULE OF LAW ABROAD: IN SEARCH OF KNOWLEDGE, *supra* note 21, at 15, 15–28; José Juan Toharia, *Evaluating Systems of Justice Through Public Opinion: Why, What, Who, How, and What For?*, *in* BEYOND COMMON KNOWLEDGE: EMPIRICAL APPROACHES TO THE RULE OF LAW 21, 21–62 (Erik G. Jensen & Thomas C. Heller eds., 2003); David M. Trubek, *The "Rule of Law" in Development Assistance: Past, Present, and Future*, *in* THE NEW LAW AND ECONOMIC DEVELOPMENT: A CRITICAL APPRAISAL, *supra* note 13, at 74, 74–94.

24 *See infra* Part II.

25 THOMAS S. KUHN, THE STRUCTURE OF SCIENTIFIC REVOLUTIONS 77 (3d ed. 1996).

26 *See id.* at 77. Scientific activity within a paradigm assimilates information not in a "neutral" way but in a way that reflects paradigmatic tenets.

gence of neoclassicism as an alternate candidate coincided with an internal intellectual crisis arising from the limitations of Keynesianism and, in development economics, statism.[27] This shift was mirrored in the field by the emergence of neoclassicism as a political movement that engendered accompanying changes in the personnel and policy of the development institutions. As such, theory and practice in law and development were linked and mutually reinforcing in describing the arc from modernization to neoclassicism.

In adapting a historiographic method to its purposes, this Essay seeks to contribute to economic as well as legal histories of neoclassicism. In doing so, it seeks to specify how influential theories of law in development grew out of a highly idealized conceptual framework wedded to a particular economic policy agenda. Improving law and development discourse will require addressing the theoretical and practical particularities stemming from the field's genealogical origins.

I
CONSTRUCTION

A. The Theorists

1. *The Theoretical Transition in Law and Development Discourse from Modernization to Neoclassicism*

Law and development policy first came into its own with the rise of modernization theory in the mid-twentieth century.[28] Modernization theory promulgated the intuition, later reincarnated by North and Thomas in *The Rise of the Western World*, that "'formal rationality' in governance [was] central to the rise of Western capitalist democ-

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27 First, a great deal of internal pressure in the field stemmed from the fact that Keynesian macroeconomics insufficiently synthesized and incorporated classical economic precepts related to the microeconomic behavior of individuals and firms. WILLEM H. BUITER, MACROECONOMIC THEORY AND STABILIZATION POLICY 5 (1989) (describing "intellectual developments within macroeconomics where there was an intensifying search for 'deep structure' and microfoundations for aggregate economic relationships"). Second, the "stagflation" economic contractions of the industrialized world during the 1970s meant that Keynesian economics no longer appeared to be working in the real world and that Keynesian models could not explain the most pressing contemporary problems. *See id.* In a Keynesian model, increasing money supply should increase real economic output, but in these stagflation economies, monetary inflation was accompanied instead by economic downturns. Externally to the economics academy, economic woes also propelled dissatisfaction with traditional Keynesian policies in public policy circles and the electorate at large. All of these pressures were brought to bear on development economics, causing one of its most illustrious proponents to declare: "Development economics is dead." Luiz Carlos Bresser Pereira, *Development Economics and the World Bank's Identity Crisis*, 2 REV. INT'L POL. ECON. 211, 220 & n.11 (1995) (quoting Arthur Lewis).

28 *See* Chantal Thomas, *Max Weber, Talcott Parsons and the Sociology of Legal Reform: A Reassessment with Implications for Law and Development*, 15 MINN. J. INT'L L. 383, 424 (2006).

racy."[29] This Weberian account provided a foundation for law and development in its first, postwar "moment"[30] of the 1950s and 1960s, influenced by the structural functionalism of Talcott Parsons and the evolutionist political economy of writers such as W.W. Rostow.[31]

Neoclassical law and development discourse built upon this earlier foundation laid by the modernization theorists.[32] While both the mid-twentieth century modernization and the late twentieth century neoclassical versions of law and development discourse shared this intellectual debt to Weber in the conceptualization of law's relationship to economic growth, the economic policy orientation of the later discourse shifted significantly.[33] The vision of ideal governance in the earlier era was consistent with a Keynesian welfare state, in which liberalism was "embedded" in a regime of benign regulation and redistribution.[34] By contrast, the ideal governance of the later era expressed skepticism about the Keynesian vision, instead calling for a "minimalist" state.[35]

If Weberian thought provided a foundation for the neoclassical theorists on the nature of law's impact on economics, a more proximate antecedent was Friedrich Hayek.[36] Hayek's influence over the rise of neoclassicism stemmed not from his economic theory but from his political and legal theory expounding a conception of liberty necessitating a minimal government defined by the rule of law. This work, beginning with the pre–World War II *The Road to Serfdom* and continuing with 1960's *The Constitution of Liberty* and the later three-volume *Law, Legislation and Liberty*, set forth a forceful denunciation of centralized economic regulation as connected to totalitarianism. Hayek endorsed a vision of ideal society which maximized individual liberty and the fulfillment of individual creative freedom with minimal

29 Chantal Thomas, *Re-Reading Weber in Law and Development: A Critical Intellectual History of "Good Governance" Reform* 3 (Cornell Law Sch. Research Paper No. 08-034, 2008), *available at* http://ssrn.com/abstract=1313718; *see* NORTH & THOMAS, *supra* note 2, at 1.

30 *See* David M. Trubek & Alvaro Santos, *Introduction* to THE NEW LAW AND ECONOMIC DEVELOPMENT: A CRITICAL APPRAISAL, *supra* note 13, at 1, 1–3.

31 *See* Thomas, *supra* note 28, at 383–93.

32 *See* DAM, *supra* note 16, at 1–5. Neoclassical law and development practitioners of the latter-twentieth century referenced the Weberian concept of "logically formal rationality." *See* SHIHATA, *supra* note 19, at 53–54, 87 n.99.

33 *See* SHIHATA, *supra* note 19, at 53–54, 85–87.

34 John Gerard Ruggie, *International Regimes, Transactions, and Change: Embedded Liberalism in the Postwar Economic Order*, 36 INT'L ORG. 379, 396–98 (1982).

35 *See* STIGLITZ, *supra* note 9, at 92.

36 *See* NORTH, *supra* note 4, at 36 n.4 ("The original contributions were those of Hayek . . . ."(citation omitted)); James R. Hackney, Jr., *Law and Neoclassical Economics: Science, Politics, and the Reconfiguration of American Tort Law Theory*, 15 LAW & HIST. REV. 275 (1997).

regulatory planning or design.[37] Political liberty depended on formal rules and the protection of property rights.[38]

When Hayek received the Nobel Prize in 1974, his academic position was rather marginal, and the general view is that the primary objective of the award was to create balance with the left-leaning politics of the other recipient that year, Gunnar Myrdal.[39] The sudden visibility of his Nobel Prize and the nontechnical accessibility of his legal and political writings helped Hayek's work to become incredibly influential as a scholarly underpinning for the burgeoning conservative political movement.[40] Hayek's other connection to the rise of neoclassical theories of law was personal: he advocated early on for the adoption of the topic as a serious focus of study at the University of Chicago.[41] Ultimately joining that faculty,[42] Hayek participated in and supported the same scholarly networks as the neoclassicists, building an academic infrastructure that would be mobilized for influence on political and legal reform.[43]

Hayek's own brand of economics, however, varied in key ways from standard neoclassical economic thought. The emphasis of the Austrian economists on "imperfect knowledge, decision making under uncertainty, and the possibility of error"[44] presaged the emergence of the NIE focus on the inefficiencies of institutions, though the latter remained faithful to standard neoclassicism in its basic methodological and normative commitments.[45] Substantively, Hayek emphasized the limitations of human knowledge, rather than the

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37 *See* F.A. HAYEK, THE CONSTITUTION OF LIBERTY 22–38 (1960).

38 *See* F.A. HAYEK, THE ROAD TO SERFDOM 72–87, 103–07 (1944).

39 ALAN EBENSTEIN, FRIEDRICH HAYEK: A BIOGRAPHY 261–63 (2003).

40 *See* JOHN RANELAGH, THATCHER'S PEOPLE: AN INSIDER'S ACCOUNT OF THE POLITICS, THE POWER AND THE PERSONALITIES ix (1992) (asserting that Margaret Thatcher, during her tenure as Prime Minister, asserted that "this . . . is what we believe" while holding up Hayek's *The Constitution of Liberty*).

41 R.H. Coase, *Law and Economics at Chicago*, 36 J.L. & ECON. 239, 246 (1993).

42 *See* Peter G. Klein, *Introduction* to 4 THE COLLECTED WORKS OF F.A. HAYEK 1–5 (Peter G. Klein ed., 1992) (describing Hayek's literal and intellectual journey from Austria to the faculty of the University of Chicago).

43 *See* Dieter Plehwe, *Introduction* to THE ROAD FROM MONT PÈLERIN: THE MAKING OF THE NEOLIBERAL THOUGHT COLLECTIVE 1, 15–20 (Philip Mirowski & Dieter Plehwe eds., 2009) (describing Hayek's role in the establishment of the Mont Pèlerin Society and the various roles played therein by Hayek, Friedman, and others); *see also* Karen Fischer, *The Influence of Neoliberals in Chile Before, During, and After Pinochet*, *in* THE ROAD FROM MONT PÈLERIN: THE MAKING OF THE NEOLIBERAL THOUGHT COLLECTIVE, *supra*, at 305, 305–416 (focusing on the "historical trajectories of neoliberal knowledge in Chile" as influenced by the Chicago Boys, among others).

44 RICHARD M. EBELING, AUSTRIAN ECONOMICS AND THE POLITICAL ECONOMY OF FREEDOM 7 (2003).

45 *See* Giulio Palermo, *The Convergence of Austrian Economics and New Institutional Economics: Methodological Inconsistency and Political Motivations*, 33 J. ECON. ISSUES 277, 279–81 (1999) (ultimately discounting the convergence due to the fidelity of NIE to orthodox neoclassical methods).

perfection of the market, as the primary argument against central economic planning.[46] Whereas the neoclassicists conceptualized the market as an efficient aggregator of the rational preferences of self-interested individuals, Hayek's endorsement of the market stemmed from the imperfections and difficulties inherent in knowledge, which could only multiply the more centralized and detached economic decisions became.[47] This same skepticism towards knowledge also influenced the methodology of Hayek and other Austrian economists, who eschewed the quantitative, data-driven techniques of the neoclassicists in favor of a "market process" theory that attempted to reconstruct market decisions from the subjective point of view of market actors.[48]

Thus, even though Hayek's theoretical and methodological specifics were at odds with neoclassicism,[49] his ultimate political conclusions—minimal government, the rule of law, and strong property rights—were consistent with them. As a consequence, Hayek was able to contribute to the rise of neoclassicism in important ways, namely his support for the study of law by economists within the academy and his influence on political actors who ultimately would look to neoclassical economics as the basis for large-scale, deregulatory government

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46 HAYEK, *supra* note 37, at 22–29; 1 F.A. HAYEK, LAW, LEGISLATION AND LIBERTY 12–15 (1973).

47 HAYEK, *supra* note 38, at 88–118.

48 *See* EBELING, *supra* note 44, at 43–56.

49 *Cf.* Francis Fukuyama, *Hayek's Incomplete Victory*, 28 WILSON Q. 111, 111 (2004) (reviewing BRUCE CALDWELL, HAYEK'S CHALLENGE: AN INTELLECTUAL BIOGRAPHY OF F.A. HAYEK (2005)) ("Today, . . . Hayek . . . is rightly seen as the intellectual godfather of the pro-market revolution that swept the West with Margaret Thatcher and Ronald Reagan."). Though Hayek constituted an important influence on Chicago School economists, some key theoretical differences distinguish the Hayekian argument against market regulation from that of many neoclassical economists. One neoclassical view depends on the premises that individuals are rational, self-interested actors and that markets are efficient organizers of actor-generated information; by contrast, the Hayekian view emphasizes the open-ended quality of both individual economic decisions and markets as aggregators of those decisions. *See* Israel M. Kirzner, *Entrepreneurial Discovery and the Competitive Market Process: An Austrian Approach*, 35 J. ECON. LIT. 60, 64 (1997). Markets, as an aspect of society, work through a process of "spontaneous order" that could never be captured or reproduced by a central planner. *See* HAYEK, *supra* note 46, at 2. Though both views conclude that markets are superior to government regulators as organizers of economic activity, the underlying attitude towards knowledge differs fundamentally. *See* HAYEK, *supra* note 46, at 8–34 (criticizing the Cartesian conception of rationality as based on perfect knowledge). In this way, Hayek shares more with the NIE branch of neoclassical theory, which also recognizes the importance of incomplete information in affecting the rationality of individual market actors. *See* Douglass C. North, *What Do We Mean by Rationality?*, 77 PUB. CHOICE 159, 159–60 (1993) ("In the world of instrumental rationality institutions are unnecessary . . . . But in the real world the actors have incomplete information and limited mental capacity . . . . In consequence they develop regularized rules and norms to structure exchange."). North and other NIE scholars distanced themselves from NPE and public choice theory, which they thought carried the same erroneous assumption. *See id.* at 159. This Essay advocates closer attention to the tenet of imperfect information within NIE. *See infra* Part III.

reform. Hayek's deep dissatisfaction with the modern welfare state extended to dismay at the dissemination of that ideal to the developing world.[50]

2. *The Rise of Neoclassical Economics in Law and Development*

While Keynesianism reigned in the field during the 1960s, a radically alternative theoretical approach was germinating[51] in the academy that would take root some decades later in the second "moment" of law and development discourse in the late 1980s and early 1990s.[52]

Chicago School economists such as Milton Friedman[53] embraced the Hayekian constitutional vision as defined by the rule of law and property rights.[54] The "Chicago boys" decried the Keynesian model of governmental intervention in the economy,[55] though governmental control was required to ensure law and order, protection of property, and monetary stability.[56] As such, the Chicago School established the key components of what would become the Washington Consensus in development policy.[57]

As with the earlier law and development discourse, which modernization theory shaped, the era shaped by the Chicago School required a social science vocabulary and discipline to translate theoretical commitments into applied policy directives. In that vein, Ronald Coase could be viewed as the founding social scientist of the second law and development moment.[58] Introduced by Coase in his 1960 essay *The Problem of Social Cost*,[59] the Coase Theorem argued that

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50 *See* HAYEK, *supra* note 37, at 2 ("A large part of the people of the world borrowed from Western civilization and adopted Western ideals at a time when the West had become unsure of itself and had largely lost faith in the traditions that have made it what it is.").

51 *See* DEZALAY & GARTH, *supra* note 12, at 79–80 (noting that James Buchanan, a Nobel Prize winner, member of the Chicago School, and founder of public choice theory, "described his position of outsider, hostile to the [Keynesian] establishment, as the source of his application of neoclassical economics to the analysis of political choices"); *infra* text accompanying notes 87–92.

52 *See* DEZALAY & GARTH, *supra* note 12, at 80–83.

53 *See id.* at 81 (explaining how Friedman published regular opinions in print and broadcast media such as *Newsweek*, the *Wall Street Journal*, and a television program called *Free to Choose*).

54 *See* MILTON FRIEDMAN, CAPITALISM AND FREEDOM 34 (1962) (describing the neoclassical vision of a "government which maintained law and order, defined property rights, served as a means whereby we could modify property rights and other rules of the economic game, [and] adjudicated disputes about the interpretation of the rules").

55 *See id.* at 37–38 ("'Full employment' and 'economic growth' have in the past few decades become primary excuses for widening the extent of government intervention in economic affairs. . . . These arguments are thoroughly misleading.").

56 *See id.* at 38.

57 *See id.* at 34–38; STIGLITZ, *supra* note 9, at 53–54.

58 *See* KERRY RITTICH, RECHARACTERIZING RESTRUCTURING: LAW, DISTRIBUTION AND GENDER IN MARKET REFORM 115 & n.73 (2002).

59 R.H. Coase, *The Problem of Social Cost*, 3 J.L. & ECON. 1 (1960).

"if the pricing system is assumed to work without cost,"[60] then contract ("bargains between the parties"[61]) could prevent social harms arising from negative externalities created by particular market actors equally as well as regulation.[62] In addition to not reducing harmful effects of the market (which private bargains would reduce in the absence of regulation), the introduction of legal liability to control such effects could produce unintended consequences that would increase overall social harm.[63] Thus, the Coase Theorem provided an argument for refraining from governmental regulation and for not responding to every social harm with a regulatory solution, not only because the market could generate its own solutions and because regulatory solutions might not solve the problem and might only create new ones.[64]

The Coase Theorem engendered many intellectual descendants, most visibly the law and economics movement in the United States.[65] Whereas Keynes concerned himself with macroeconomic aggregates and with the state as their arbiter,[66] Coase suggested a microeconomic view.[67] The role of the state was not assumed in the microeconomic lens—the idea was to measure the efficiency of microeconomic activity *independently* of regulation and *then* to determine how regulation affected that activity.[68] The microeconomic methodological orientation was consistent with, but did not necessitate, a dramatically different default position—that regulation was an encumbrance on otherwise efficient market activity.[69]

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60 *Id.* at 8.

61 *Id.* at 12.

62 *See id.* at 17–18, 44.

63 *See id.* at 30–33. For example, imposing legal liability on a railroad for damage to neighboring farmers' crops might induce farmers to increase crop production. Such increases would adversely affect overall social welfare because the overall number of crop fires would increase and the penalties imposed on the railroad might ultimately cause it to cease operations due to lack of profitability. *See id.* Coase focused on this hypothetical because it was provided by the economist Arthur Pigou, see A.C. PIGOU, THE ECONOMICS OF WELFARE 134 (Transaction Publishers 2002). Pigou is credited with the welfare-economics tenet that government intervention is necessary to prevent negative externalities. *See* Coase, *supra* note 59, at 28–39. Alfred Marchal developed the concept of externalities. *See* A.C. Pigou, Book Review, 17 ECON. J. 532, 532–35 (1907) (reviewing ALFRED MARSHALL, THE PRINCIPLES OF ECONOMICS (5th ed. 1907)).

64 *See* Coase, *supra* note 59, at 1–2, 26–28.

65 *See, e.g.*, RICHARD A. POSNER, ECONOMIC ANALYSIS OF LAW 1–28 (7th ed. 2007) (referencing Coase in a discussion of the interaction between law and economics).

66 *See* Anand Chandavarkar, *Keynes and the Role of the State in Developing Countries*, *in* KEYNES AND THE ROLE OF THE STATE 136–37 (Derek Crabtree & A.P. Thirlwall eds., 1993).

67 *See* Coase, *supra* note 59, at 28–44.

68 *See id.*

69 *Cf.* David Kennedy, *The "Rule of Law," Political Choices, and Development Common Sense*, *in* THE NEW LAW AND ECONOMIC DEVELOPMENT: A CRITICAL APPRAISAL, *supra* note 13, at 95, 95–98 & 129 (describing how, for "neoliberal development policy[,] . . . . [t]he lead passed from macroeconomics to microeconomics" so that "[a]n economy was no longer imagined

The conclusion of the Coase Theorem, that the legal environment could impose effects and costs on market actors that would become variables determining economic output,[70] became an important part of the intellectual heritage of the New Institutional Economics[71] and the New Political Economy,[72] both of which in turn formed theoretical components of the Washington Consensus. NIE focused on the role of the state in affecting property and contract transactions and in particular the importance of private property rights.[73] NPE focused on the role of the state in trade and investment, particularly across borders.[74] The relationship between NIE and NPE was a close one: North described the NPE movement as simply NIE applied to political economy.[75]

These theoretical descendants would transform the field of economic development. NPE became the basis for structural adjustment macroeconomic programs.[76] NIE, of which North was a leading proponent, became the basis for good governance legal and institutional reform programs. Although these perspectives have been recognized as interrelated, there are more systematic connections (graphically represented in the Appendix) than suggested in existing scholarship.[77]

3. *The New Institutional Economics (NIE)*

> Transaction costs . . . become the factor upon which the productivity of the economic system depends.

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primarily as an input-output production cycle open to macroeconomic strategies" but "as a 'market'").

70 *See* Coase, *supra* note 59, at 28–44.

71 *See, e.g.*, Oliver E. Williamson, *The New Institutional Economics: Taking Stock, Looking Ahead*, 38 J. ECON. LIT. 595, 599 (2000) (citing Coase, *supra* note 59, for the key NIE proposition that "easy" or "costless" enforcement of property rights should not be assumed in economic calculations).

72 *See, e.g.*, Amiya Kumar Bagchi, *'Rent-Seeking', New Political Economy and Negation of Politics*, 28 ECON. & POL. WKLY. 1729, 1730 (1993) (noting critically that the "proponents of the new political economy have tried to upset . . . the agenda of the state with the so-called Coase theorem").

73 *See supra* text accompanying notes 2–3; *infra* text accompanying notes 93–100; *see also* MICHAEL P. TODARO & STEPHEN C. SMITH, ECONOMIC DEVELOPMENT 133 n.16 (9th ed. 2006).

74 *See infra* text accompanying notes 102–14.

75 *See* North, *supra* note 1, at 121. North's 1990 book, *Institutions, Institutional Change and Economic Performance*, was part of a series that he created on NPE, further evidencing his belief in the intellectual link. *See* NORTH, *supra* note 3, at 3–10.

76 *See infra* text accompanying notes 138–39.

77 *See infra* Part I.B; Appendix.

> However, transaction costs depend, as we learned from the new institutional economics, on the working of the legal system (the system of property rights, the enforcement of property rights, the ability to foresee what the legal decisions will be, and so on).
>
> — Ronald Coase[78]

In his earlier influential essay, *The Nature of the Firm*, Coase had introduced the concept of transaction costs to explain why firms emerge in a market environment.[79] Together with *The Problem of Social Cost*, Coase's insights provided the foundation for the New Institutional Economics—that the legal and institutional environment could either be conducive to, or impede, market activity and economic growth.[80]

If "[e]fficient economic organization is the key to growth,"[81] the NIE argument held, institutions are key in determining efficient—or inefficient—economic organization.[82] NIE challenged the assumption of some neoclassical theorists that the competitive market would lead to efficient institutions. "The implication [of that assumption] is not only that institutions are designed to achieve efficient outcomes, but that they can be ignored in economic analysis because they play no independent role in economic performance."[83] By contrast, North argued, institutions can be erroneously designed due to transaction costs including "incomplete information and . . . subjectively derived models" of behavior.[84] Nevertheless, such institutions could and did take hold, often serving those in power even where these ruling interests failed to serve the economic welfare of society at large.[85]

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78 Ronald Coase, *Why Economics Will Change*, ISNIE NEWSL. (Int'l Soc'y for New Institutional Econ., St. Louis, Mo.), Summer 2002, at 1, 5.

79 *See* R.H. Coase, *The Nature of the Firm*, 4 ECONOMICA 386, 390–94 (1937). In a completely efficient economic environment, where pricing is always accurate and transacting is costless, market actors have no incentive to establish firms rather than meeting their needs on the "open market." *See id.* Consequently, firms must exist because "there is a cost of using the price mechanism" of the open market. *Id.* at 390.

80 *See id.* at 386–87, 403–05; Ronald Coase, *The New Institutional Economics*, 88 AM. ECON. REV. 72, 72 (1998) ("It is commonly said, and it may be true, that the new institutional economics started with my article, 'The Nature of the Firm' (1937) with its explicit introduction of transaction costs into economic analysis."); Coase, *supra* note 59, 1–2, 42–44.

81 *See* NORTH & THOMAS, *supra* note 2.

82 *See* William M. Dugger, *Douglass C. North's New Institutionalism*, 29 J. ECON. ISSUES 453, 453–56 (1995); *see also* TODARO & SMITH, *supra* note 73 ("The basic message of the new institutionalism is that even in a neoclassical world, the success or failure of development efforts will depend on the nature, existence, and proper functioning of a country's fundamental institutions.").

83 NORTH, *supra* note 3, at 16.

84 *Id.*

85 *Id.* ("Institutions are not necessarily or even usually created to be socially efficient; rather they, or at least the formal rules, are created to serve the interests of those with the bargaining power to devise new rules. In a zero-transaction-cost world, bargaining strength does not affect the efficiency of outcomes, but in a world of positive transaction costs it

Through a process of negative feedback loops in which individual actors conformed their behavior to these initial institutional distortions, inefficiencies would become entrenched and lead aggregate economies down an impoverished historical path.[86] Thus, NIE stood both for the point that efficient institutional arrangements could not be assumed and for the thesis as to how institutional inefficiencies could persist over time through path dependence.

An important part of the NIE argument was the thesis that institutions could become dominated by powerful actors whose interests did not serve the larger economic welfare.[87] The theoretical exposition for this part of NIE was provided by the concept of the collective action problem in public choice theory, a perspective that had powerfully emerged in *The Calculus of Consent*, published by James Buchanan and Gordon Tullock a decade before North and Thomas published *The Rise of the Western World*.[88]

A direct challenge to the idea of the benign welfare state, public choice theory saw decisions by political institutions as merely the aggregate of individual self-interested choices and further asserted that these could be subject to a variety of flaws.[89] In the 1970s and 1980s, these insights became highly influential as "rent-seeking analysis."[90] Collective action problems explained how institutional arrangements could tend towards inefficiency.[91] If this was true, institutions could not be taken for granted as supporting economic growth but would need to be assessed on that basis. In domestic law, this insight became hugely influential and would define a whole field—the study of law and economics—for the next several decades.[92]

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does and given the lumpy indivisibilities that characterize institutions, it shapes the direction of long-run economic change." (emphasis omitted)).

86 *See id.* at 112 ("Path dependence is the key to an analytical understanding of long-run economic change.").

87 *See infra* note 325 and accompanying text.

88 *See* JAMES M. BUCHANAN & GORDON TULLOCK, THE CALCULUS OF CONSENT: LOGICAL FOUNDATIONS OF CONSTITUTIONAL DEMOCRACY (1962). North cited this work as contributing to the "intellectual origins" of his theory. *See* NORTH & THOMAS, *supra* note 2, at 159. North also cited it as an early example of interest analysis in institutional contexts. *See* NORTH, *supra* note 3, at 50.

89 *See* TODARO & SMITH, *supra* note 73, at 121 ("[P]ublic-choice theory assumes that politicians, bureaucrats, citizens, and states act solely from a self-interested perspective, using their power and the authority of government for their own selfish ends.").

90 *See, e.g.*, JAMES M. BUCHANAN ET AL., TOWARD A THEORY OF THE RENT-SEEKING SOCIETY (1980). For a discussion of the impact of public choice theory and rent-seeking analysis on development policy, see RITTICH, *supra* note 58, at 115–25.

91 *See* NORTH & THOMAS, *supra* note 2, at 5 (noting that "[t]he costs of creating or enforcing property rights may exceed the benefits to any group or individual" and that "[t]echnique [sic] may be lacking to counteract the free-rider and/or to compel third parties to bear their share of the costs of a transaction").

92 *See, e.g.*, ROBERT COOTER & THOMAS ULEN, LAW & ECONOMICS 108–10 (5th ed. 2008); POSNER, *supra* note 65, at 36 n.4.

NIE's ambitions extended beyond domestic law, however, and sought to provide a basis for assessing governmental and legal orders across space and time. To explain "the performance of economies through time,"[93] North offered a "neoclassical theory of the state" that would explain "the widespread tendency of states to produce inefficient property rights and hence fail to achieve sustained growth."[94] In this way, he offered institutional economics as a means of understanding the reason that states did not fulfill the ideal set out by the Chicago School.

Indeed, the focus of North's particular brand of economic history was to explain how it was that "efficient" systems arose in the West and not elsewhere.[95] "Efficient economic organization is the key to growth; the development of an efficient economic organization in Western Europe accounts for the rise of the West."[96] From here, the basis for institutional analysis of economies over time—the objective of *The Rise of Western World*—becomes clear. Transaction costs and institutional constraints prevented some economies from reaching the most efficient system of property rights, which included exclusiveness and enforcement.[97]

This thesis echoed the Weberian typology asserting the relationship among law, capitalism, and the West's economic rise.[98] Where NIE departed from Weber and hewed to the neoclassical line was the central importance of property rights in this account. It was not just legal rationality, as in Weber, that induced capitalistic growth—it was the protection and enforcement of property rights which were required for efficient economic production.[99] According to insights from Coase and public choice theory, however, the protection of property rights could not be assumed to evolve simply because it was objectively the most efficient, because "there is no guarantee that the government will find it to be in its interest to protect those property rights which encourage efficiency."[100] Hence the study and correction

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93 *See* North, *supra* note 1.

94 NORTH, *supra* note 4, at 20–23.

95 *See* NORTH & THOMAS, *supra* note 2.

96 *See id.*

97 *See id.* at 5 ("If exclusiveness and the enforcement of accompanying property rights could be freely assured—that is, in the absence of transaction costs—the achievement of growth would be simple indeed. . . . Property rights [however] are always embedded in the institutional structure of a society, and the creation of new property rights demands new institutional arrangements to define and specify the way by which economic units can cooperate and compete.").

98 *See supra* notes 28–35 and accompanying text.

99 *See* NORTH & THOMAS, *supra* note 2, at 8 ("[E]conomic growth will occur if property rights make it worthwhile to undertake socially productive activity.").

100 *See id.* at 7.

of inefficiencies in institutions and legal arrangements could contribute to improving efficiencies in markets.

4. *The New Political Economy (NPE)*

> The practitioners of the "New Political Economy" believe that the state should be a maximizer, rationally finding the right combination of minimalist policies which free the "natural" development forces in an economy.
>
> — James M. Cypher and James L. Dietz[101]

The New Political Economy could be viewed, per Douglass North, as an extension of NIE to political economy. In any case, NPE was certainly a direct application of NIE's shared intellectual influence, public choice theory.[102] NPE scholarship was heavily influenced by the work of Buchanan and his coauthors as well as by Mancur Olson's *The Logic of Collective Action.*[103] In that 1965 study, Olson showed how protectionist trade tariffs could be adopted as governmental policy even though they did not increase economic efficiency or social welfare.[104]

NPE focused substantially on international trade law policy, whereas NIE was focused on mostly on property and contract regimes. Trade was, after all, the intended activity resulting from a market secured by property and contract rights that NIE studied. From Adam Smith down to modern neoclassical theorists, trade was the genesis of national wealth.[105] As such, trade occupied a central place in the neoclassical theory of economic growth, and therefore, trade policy was a subject of economic and development policy, though the insights of NPE applied equally to investment and other economic sectors.

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101 *See* James M. Cypher & James L. Dietz, The Process of Economic Development 220 (3d ed. 2009).

102 *See generally* Rittich, *supra* note 58, at 115–25 (discussing the origins and influence of public choice theory); Todaro & Smith, *supra* note 73, at 121 (describing public choice theory as synonymous with the "new political economy approach").

103 *See* Buchanan & Tullock, *supra* note 90; Buchanan et al., *supra* note 92; Mancur Olson, The Logic of Collective Action: Public Goods and the Theory of Groups (1965).

104 *See* Olson, *supra* note 105, at 10.

105 *See* Adam Smith, The Wealth of Nations *passim* (Edwin Cannan ed., Random House, Inc. 1937) (1776) (discussing the importance of trade in generating national wealth). For an example of this rationale, see Jeffrey D. Sachs & Andrew Warner, *Economic Reform and the Process of Global Integration*, 1 Brookings Papers on Econ. Activity 3, 3 (1995) ("The power of trade to promote economic convergence is perhaps the most venerable tenet of classical and neoclassical economics, dating back to Adam Smith. As Smith's followers have stressed for generations, trade promotes growth through a myriad [of] channels: increased specialization, efficient resource allocation according to comparative advantage, diffusion of international knowledge through trade, and heightened domestic competition as a result of international competition.").

The economists Anne Krueger and Jagdish Bhagwati, among others,[106] propounded NPE as a basis for policy reform both in the United States and in developing countries. In *The Political Economy of the Rent-Seeking Society*, Krueger expanded on the public choice insights of Buchanan and his coauthors and of Olson in arguing that governmental controls, particularly on international trade, reduced economic growth and welfare and reflected capture of economic regulation by harmful minority economic interests.[107] Bhagwati's article, *Directly Unproductive Profit-Seeking (DUP) Activities*, was a widely read application of rent-seeking analysis to international trade.[108]

Both Bhagwati and Krueger applied the critique of trade protectionism to development strategies for poor countries seeking growth but also to the economic giants of the West.[109] Such writings were politically relevant in the late 1970s and early 1980s when stagnating U.S. industries began to decry unfair trade practices in the rising economies of East Asia.[110] As much as their writings were directed towards the "New Protectionism" in the West, however, these theorists were adamant that the state-led growth strategies of the developing world were responsible for choking off growth before it could start and for ensuring that it never would.[111]

NPE's most noteworthy contribution to development economics, then, was providing support for the neoclassical assertion that "trade openness" was the best determinant of economic growth.[112] Another

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106 *See* TODARO & SMITH, *supra* note 73, at 120 (naming Bhagwati and Krueger among other economists such as Lord Peter Bauer, Harry Johnson, Deepak La, and Bela Belassa).

107 *See* Anne O. Krueger, *The Political Economy of the Rent-Seeking Society*, 64 AM. ECON. REV. 291, 291, 302–03 (1974).

108 Jagdish N. Bhagwati, *Directly Unproductive Profit-Seeking (DUP) Activities*, 90 J. POL. ECON. 988, 988–1001 (1982).

109 *See, e.g.*, JAGDISH BHAGWATI, PROTECTIONISM (1988); Anne O. Krueger, *The Political Economy of Controls: American Sugar* 34–55 (Nat'l Bureau of Econ. Research, Working Paper No. 2504, 1988).

110 *See, e.g.*, ELHANAN HELPMAN & PAUL R. KRUGMAN, MARKET STRUCTURE AND FOREIGN TRADE: INCREASING RETURNS, IMPERFECT COMPETITION, AND THE INTERNATIONAL ECONOMY (1985).

111 *See, e.g.*, Anne O. Krueger, *Government Failures in Development*, 4 J. ECON. PERSP. 9, 20–21 (1990). Bhagwati has continued to be a staunch defender of trade openness. *See* JAGDISH BHAGWATI, IN DEFENSE OF GLOBALIZATION (2004).

112 *See supra* notes 109–11, 113 and accompanying text (describing the works of Krueger and Bhagwati, which focus on criticizing trade protectionism). The neoclassical support for trade openness rested on many pillars, only one of which was rent-seeking analysis. *See, e.g.*, TODARO & SMITH, *supra* note 73, at 120–21 (dividing neoclassical approaches into "free-market analysis," which argues that "markets alone are efficient," the "new political economy approach," which "goes even further to argue that governments can do nothing right," and the "market-friendly approach," which describes more more "recent variant[s]" that acknowledge some role for government regulation). The analysis in the text is somewhat stylized for heuristic purposes, streamlining a broad range of overlapping contributions in theory and policy.

prominent advocate of this view was Harvard economist Jeffrey Sachs. As Sachs explained:

> [T]rade liberalization is usually just one part of a government's overall [structural adjustment] reform plan for integrating an economy with the world system. Other aspects of such a program almost always include price liberalization, budget restructuring, privatization, [and] deregulation . . . . Nonetheless, the international opening of the economy is the sine qua non of the overall reform process.[113]

Though most of the NPE scholars were from economics, the movement also included some legal scholars. Robert Hudec was the most prominent of these, and in 1987, he published a valuable book, *Developing Countries in the GATT Legal System*, which provided an institutional history, as well as an economic critique, of trade controls as exercised to promote development in poor countries.[114]

5. *The Moderate Institutionalists*

Embracing the concept of transaction costs and transaction costs' relationship to the institutional environment and economic growth does not require a commitment to the neoclassical view that regulation should be minimized. Possibly, a market *without* regulatory intervention would be subject to internal "failures" based on transaction costs, and active governance might be necessary to correct those failures. In the context of domestic legal scholarship on private law, for example, this argument could justify legal disclosure requirements and remedies designed to correct for unequal bargaining power between contracting parties. Such inequality, the argument goes, would make access to information for the weaker party prohibitively expensive and, without governmental intervention, produce inefficient transactional outcomes.

Similarly, applying the market-failure concept to the problem of the developing economy writ large could lead to the conclusion that active governmental intervention would be necessary to support efficient outcomes and avoid inefficient ones. In this way, the institutionalist orientation, with its focus on institutional quality supporting economic growth and the minimization of transaction costs, could support a regulatory state as well as a deregulatory state. In doing so, it would come much closer to the Keynesian ideal of the mid-twentieth-century moderate interventionists.

Dani Rodrik, one of the more visible moderate institutionalists, explicitly styled his policy analyses as taking such a dialectical turn:

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113 Sachs & Warner, *supra* note 105, at 2.

114 *See* ROBERT E. HUDEC, DEVELOPING COUNTRIES IN THE GATT LEGAL SYSTEM (1987).

> Once upon a time, economists believed the developing world was full of market failures, and the only way in which poor countries could escape from their poverty traps was through forceful government interventions. Then there came a time when economists started to believe government failure was by far the bigger evil, and that the best thing that government could do was to give up any pretense of steering the economy. Reality has not been kind to either set of expectations. . . .
>
> . . . .
>
> . . . [W]e now confront a rare historic opportunity. The softening of convictions on both sides presents an opening to fashion an agenda for economic policies that takes an intelligent intermediate stand between the two extremes cited above.[115]

Rodrik's reconciliatory view does not constitute a departure from institutionalist commitments. Rodrik clearly holds to institutionalist "first-order economic principles—protection of property rights, market-based competition, appropriate incentives, sound money, and so on."[116] He does, however, insist that such commitments "do not map into unique policy packages."[117]

In *One Economics, Many Recipes,* Rodrik extends this moderate approach both to NPE concerns, such as macroeconomic policy on trade and investment, and NIE concerns, such as legal and judiciary reform.[118] On the NIE side, Rodrik states that the protection of property rights need not take conventional form: "Formal property rights do not count for much if they do not confer control rights. By the same token, sufficiently strong control rights may do the trick even in the absence of formal property rights."[119] Thus, even in the absence of a "private-property-rights legal regime," China's economic growth might be consistent with the institutionalist outlook because "property rights were effectively more secure under direct local government ownership."[120]

Similarly, on the NPE side, Rodrik states that the neoclassical macroeconomic program is not the sole path to economic growth: "Scratch the surface of nontraditional export success stories from anywhere around the world, and you will more often than not find industrial policies, public R&D, sectoral support, export subsidies,

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115 DANI RODRIK, ONE ECONOMICS, MANY RECIPES: GLOBALIZATION, INSTITUTIONS, AND ECONOMIC GROWTH 99–100 (2007).

116 *Id.* at 6.

117 *Id.*

118 *See id.* at 109–11, 155–57.

119 *Id.* at 156.

120 *Id.* at 24.

preferential tariff arrangements, and other similar interventions lurking beneath the surface."[121]

Moderate institutionalism also characterizes the "embedded autonomy" perspective of Peter Evans.[122] According to this outlook, the basic dynamism of the private sector should be acknowledged and respected, and safeguards should guard against thoroughgoing and centralized economic planning.[123] Moreover, the susceptibility of the public sector to rent seeking and corruption must be factored into industrial policy design.[124] Nevertheless, the state should "embed" market activity by providing strategic support and intervention.[125]

Robert Lucas, who won the Nobel Prize in 1995, highlighted

> the importance of interactions between individuals and the potential positive role of institutions and models of organization that favored the concentration of knowledge and expertise. With respect to the question of the role of governmental intervention in the economy, he appeared much more open to that possibility than those identified with the dominant orthodoxy, who had been content to denounce affirmative practices by state actors as forms of rent seeking.[126]

Lucas's lecture showed how institutionalism and governance had "become the new frontiers of economic theory"[127] by providing a common language for those whose theories could accommodate greater strategic intervention of governments into economic growth strategies, as well as for those advocating less intervention.[128]

Within that frontier, by the late 1990s and early 2000s, the moderate institutionalism derived from the "first principles" of neoclassical economics began to be joined by other voices questioning the more extreme forms of neoclassicism and offering alternative bases for conceptualizing the law and development ideal. On the macroeconomics side, Joseph Stiglitz, who won the Nobel Prize in 2001,[129] was perhaps

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121 *Id.* at 109. The bulk of these "success stories" have occurred in Asia. *See, e.g.*, ALICE H. AMSDEN & WAN-WEN CHU, BEYOND LATE DEVELOPMENT: TAIWAN'S UPGRADING POLICIES (2003); ALICE H. AMSDEN, THE RISE OF "THE REST": CHALLENGES TO THE WEST FROM LATE-INDUSTRIALIZING ECONOMIES (2001).

122 *See* PETER EVANS, EMBEDDED AUTONOMY: STATES AND INDUSTRIAL TRANSFORMATION (1995).

123 *See id.* at 3–4.

124 *See id.*

125 *See id.* at 41–42. For more discussion of moderate institutionalist perspectives, see CYPHER & DIETZ, *supra* note 101, at 180–85 (discussing the institutionalism of Clarence Ayres and Gunnar Myrdal); RITTICH, *supra* note 58, at 143–51 (discussing the institutional economics of Warren Samuels, Nicholas Mercuro, and Steven Medema).

126 DEZALAY & GARTH, *supra* note 12, at 167–68.

127 *Id.* at 169.

128 *See id.*

129 *See* Louis Uchitelle, *3 Americans Awarded Nobel for Economics*, N.Y. TIMES, Oct. 11, 2001, at C1.

the most visible of the mainstream development economists to acknowledge that the neoclassical program had failed in many cases and had produced a great deal of discontent worldwide.[130] Critiques by Stiglitz and others of the dynamics of globalization as envisioned by neoclassical theory provided a basis for a "chastened" style of economic policy consistent with Rodrik's approach, in which "market" values were balanced with "social" values.[131]

At the same time, Amartya Sen, who won the Nobel Prize in 1998,[132] had articulated a theory of governance that espoused human rights, rather than neoclassical economics, as the basis for first principles of development policy.[133] In Sen's rendition, development was intimately interlinked with human "capabilities"—with human capabilities representing both the means and the ends of development policy.[134] Aggregate social development could not occur without a fully developed population who could provide the dynamism to fuel economic transformation; at the same time, the whole point of economic transformation was to increase aggregate social welfare.[135] Consequently, development needed to attend both to the protection of civil and political human rights, which are necessary to protect individual innovation and expression, and to social and economic human rights, which are necessary to provide for basic needs and thereby preserve capabilities.[136]

Sen's theory broke the impasse that had previously existed in which development economists had suggested that social and political protections were luxuries that government could not provide until after some level of economic development had already been reached. Rather, Sen suggested, economic growth was internally dependent on the protection of human rights. This theory of development also supported a different vision of good governance and the rule of law. Whereas the neoclassical vision of good governance focused on the enforcement of property rights and the stability of private commercial law, the vision informed by Sen's theory of capabilities focused on respect for human rights.[137] In this way, Sen offered an approach to law and development, consistent with that of the moderate institutionalists, that suggested a broader and more social focus.

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130 *See, e.g.*, STIGLITZ, *supra* note 9.

131 *See* Kennedy, *supra* note 69, at 150.

132 *See* Sylvia Nasar, *Indian Wins Nobel Award in Economics*, N.Y. TIMES, Oct. 15, 1998, at C1.

133 *See* AMARTYA SEN, DEVELOPMENT AS FREEDOM 3–4 (1999).

134 *See id.* at 35–40.

135 *See id.* at 87–96.

136 *See id.* at 54–72.

137 *See id.* at 282–91.

Moderate institutionalism, then, allows for variation from the neoclassical baseline on both the macroeconomics side (where the baseline is NPE) and the governance side (where the baseline is NIE). On the macroeconomics side, the moderate institutionalism of Rodrik and others allows a greater role for the state in regulating and directing economic activity.[138] On the governance side, a focus on human rights is consistent with and even constitutive of the rule of law.[139] Development discourse has accommodated both perspectives, and in recent years, the influence of these more moderate views has gained such visibility as to suggest that development discourse has entered into a new era.[140] As of yet, the practical influence of these more moderate approaches, and their theoretical distinctness from neoclassicism, still appears debatable.[141]

Based on an interview he gave late in life, the grandfather of the neoclassical movement himself, Ronald Coase, appeared to espouse the moderate institutionalist approach and to admonish the hardline neoclassicists.[142] In that interview, Coase pointed out that much of the work based on the Coase Theorem erroneously assumed an ideally efficient economic environment.[143] Coase had explicitly flagged this important qualification in his original statement of the Theorem,[144] and in any case, it was implicit from his earlier work on transaction costs.[145] That is, while the Coase Theorem demonstrated "the type of contracts that would have to be made in order to have an efficient economic system," the immediate next step for any meaningful analysis of real-world problems would be to identify the obstacles to efficiency.[146]

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138 *See supra* Part I.A.

139 *See supra* Part I.A.

140 *See* Trubek & Santos, *supra* note 30, at 1–3; David M. Trubek, *supra* note 23, at 74.

141 *See* Rittich, *supra* note 13, at 252; Trubek & Santos, *supra* note 30, at 3. Some analysts see the more recent approaches of the World Bank as simply "variants" of neoclassicism. *See* TODARO & SMITH, *supra* note 73, at 121 (describing a shift in the World Bank from strict free-market and public-choice approaches towards a view that "governments do have a key role to play in facilitating the operation of markets through . . . investing in physical and social infrastructure, health care facilities, and educational institutions"); Ben Fine, *The New Development Economics*, *in* THE NEW DEVELOPMENT ECONOMICS: AFTER THE WASHINGTON CONSENSUS 1, 2 (Jomo K.S. & Ben Fine eds., 2006) ("[T]he newer development economics, in the form of the post-Washington Consensus, looks much more like the Washington Consensus than the old development economics that the Washington Consensus sought to displace.").

142 *See An Interview with Ronald Coase*, ISNIE NEWSL. (Int'l Soc'y for New Institutional Econ., St. Louis, Mo.), Spring 1999, at 3–5.

143 *See id.*

144 Coase, *supra* note 59, at 8 ("[T]he ultimate result (which maximizes the value of production) is independent . . . if the pricing system is assumed to work without cost.").

145 *See* Coase, *supra* note 79, at 390–98.

146 *An Interview with Ronald Coase*, *supra* note 142, at 4.

Because many Coase Theorem adherents had argued for the inefficiency of legal liability rules and other regulation on the erroneous assumption that transactions were costless, in Coase's opinion his Theorem has "been very successful for the wrong reasons," providing an "illustration of what's wrong with economics."[147] For this reason, Coase strongly endorsed the NIE focus on the effect of existing institutions and laws on transactional processes and dismissed prevailing modes of law and economics scholarship as using abstracted economic analyses to theorize about effects of the legal system on the market.[148] As a corollary to this insistence on attention to actual contexts, Coase surmised, "[T]here is no 'one way' better economic system, because everything depends on the society you're in."[149] Thus, Coase appears to be more supportive of a moderate approach than much of the law and economics scholarship begotten from his work.[150]

6. *Conclusion*

Neoclassical economics developed during the 1960s and 1970s as a response to Keynesian welfare economics.[151] As the foregoing sections demonstrate, neoclassicism included key ideas about the relationship of laws and institutions to market efficiency and economic growth. Though the economic policy orientation shifted from a regulatory to a deregulatory tendency under neoclassicism, the belief in legal rules as potential instruments in development remained continuous with the previous era of modernization theory.

The neoclassical movement extended to thinking about international development.[152] Whereas the modernization theorists of the

147 *Id.*

148 *See id.* at 3–5.

149 *Id.* at 5.

150 For a notable elucidation of the relationship between Coase's *The Problem of Social Cost* and *The Nature of the Firm*, see Stewart J. Schwab, *Coase's Twin Towers: The Relation between* The Nature of the Firm *and* The Problem of Social Cost, 18 J. CORP. L. 359, 359–60, 367–70 (1993).

151 *See supra* text accompanying notes 51–57; *see also* TODARO & SMITH, *supra* note 73, at 123 ("[T]he neoclassical counterrevolution of the 1980s had its origin in an economics-cum-ideological view of the developing world and its problems."); Pereira, *supra* note 27, at 218–19 (describing a process whereby the "Keynesian consensus broke down" and opened the way for "the rise of a New Right intellectually well equipped for fighting the state").

152 *See* Sonali Deraniyagala & Ben Fine, *Kicking Away the Logic: Free Trade Is Neither the Question Nor the Answer for Development*, *in* THE NEW DEVELOPMENT ECONOMICS: AFTER THE WASHINGTON CONSENSUS, *supra* note 141, at 46, 46 ("Since the 1980s, neoliberal belief in free trade has come to be the orthodoxy in international economics. This orthodoxy has been translated into policy advice, particularly for developing countries, for which trade liberalization has become a major policy objective."); TODARO & SMITH, *supra* note 73, at 122 (explaining how traditional neoclassical growth theory was applied to criticize statist economic policies whose "heavy-handedness . . . retard[s] growth in the economies of the developing world").

earlier era envisioned an ideal of governance which espoused a regulatory and interventionist state, the neoclassicists embraced deregulation and minimalism as the preferred ideals of governance.[153] It was not until the early 1980s that political events created the opportunity for neoclassical ideas to rise to power and for these ideas to affect international development in practice.[154]

Thus, the key contours of legal reform in development theory were designed not by lawyers or legal scholars, but by economists. The next section describes neoclassical law and development as it emerged in practice in the 1980s and 1990s. Here, though economists continued to lead the charge, lawyers played an important role in the conceptualization of good governance and in its justification within existing international development law and policy.

B. The Practitioners

In 1982, NPE scholar Anne Krueger was appointed to the World Bank as Chief Economist.[155] This was a watershed moment in the transformation of law and development discourse: Krueger's appointment consolidated the influence of neoclassicism, through rent-seeking analysis and trade theory as described above, in development economics.[156] This influence, aided by the ascendancy of the "Reagan

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153 *See* text accompanying notes 28–77; *see also* TODARO & SMITH, *supra* note 73, at 121; Paul Cammack, *Neoliberalism, the World Bank, and the New Politics of Development*, *in* DEVELOPMENT THEORY AND PRACTICE: CRITICAL PERSPECTIVES 157, 163 (Uma Kothari & Martin Minogue eds., 2002) (describing how "the neoliberal revolution has thrown the . . . components of postwar political economy . . . into reverse"); Ben Fine, *supra* note 141, at 4–5 ("[P]rior to the emergence of neoliberalism in the 1980s, development was understood primarily in terms of modernization . . . . Moreover, the influence of Keynesianism . . . suggested that the state should be significant as an economic agent as part of and in achieving modernization. . . . But this was to change, and dramatically, with the rise of neoliberalism. . . . The neoliberal shift against state economic intervention of any sort was then carried over to development . . . .").

154 *See infra* text accompanying notes 155–60; *see also* TODARO & SMITH, *supra* note 73, at 119–20 ("In the 1980s, the political ascendancy of conservative governments in the United States, Canada, Britain and [West] Germany came with a neoclassical counterrevolution in economic theory and policy. . . . Neoclassicists obtained controlling votes on the boards of the world's two most powerful international financial agencies—the World Bank and the International Monetary Fund. . . . [I]t was inevitable that the neoconservative, free-market challenge . . . would gather momentum."). Michael Todaro and Steven Smith identify dependency theory, rather than modernization theory, as an organizing influence for shaping development economics prior to the "neoclassical counterrevolution." *See* TODARO & SMITH, *supra* note 73, at 119–20.

155 *See* CYPHER & DIETZ, *supra* note 101, at 216.

156 *See* STIGLITZ, *supra* note 9, at 13–14 ("The most dramatic change in [the IMF and the World Bank] occurred in the 1980s, the era when Ronald Reagan and Margaret Thatcher preached free market ideology . . . . The IMF and the World Bank became the new missionary institutions, through which these ideas were pushed on the reluctant poor countries that often badly needed their loans and grants. . . . In the early 1980s, a purge occurred inside the World Bank . . . . [W]ith the changing of the guard came . . . a new chief economist, Ann[e] Krueger, an international trade specialist, best known for her

Revolution," had already been signaled by the introduction of the policy of conditionality by both the World Bank[157] and the International Monetary Fund[158] in 1979 and the adoption of structural adjustment lending by the World Bank in 1980.[159]

With the Ronald Reagan and Margaret Thatcher revolutions providing political momentum, development agencies now sought broad-based changes in the basic commitments of economic policy by the beneficiary government, a position consistent with neoclassicism. The influence of Krueger and the general shift that her appointment embodied, shaped by NPE and rent-seeking analysis, was heavily imprinted in the structural adjustment programs that the World Bank increasingly emphasized during the 1980s.[160]

Structural adjustment programs emphasized the need for dramatic NPE-based reforms to macroeconomic policy to improve the "underlying conditions"[161] that would improve growth in developing countries. In trade policy, protective trade regimes influenced by import-substitution industrialization strategies had to be converted to

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work on 'rent seeking' . . . . Krueger saw government as the problem."); Robin Broad, *Research, Knowledge, and the Art of 'Paradigm Maintenance': The World Bank's Development Economics Vice-Presidency (DEC)*, 13 REV. INT'L POL. ECON. 387, 393 (2006) (noting that Krueger's appointment signaled a "key reorganization," which generated a "pronounced 'shift toward macroeconomic and trade issues'" (citations omitted)); Pereira, *supra* note 27, at 223 ("Anne Krueger should probably be particularly credited for [the turn to neoliberalism] at the Bank, where her intellectual influence was decisive."). For other discussions of Krueger's influence on development economics, see, for example, T.N. Srinivasan & Jagdish Bhagwati, *Outward-Orientation and Development: Are Revisionists Right?*, *in* TRADE, DEVELOPMENT AND POLITICAL ECONOMY: ESSAYS IN HONOUR OF ANNE O. KRUEGER 3, 3 (Deepak Lal & Richard H. Snape eds., 2001) ("Anne Krueger has been an influential thinker, researcher and policy adviser on economic development and its relations hip with openness to international trade, investment and technology flows.").

157 *See* Broad, *supra* note 156, at 391.

158 *See* Chantal Thomas, *Does the "Good Governance Policy" of the International Financial Institutions Privilege Markets at the Expense of Democracy?*, 14 CONN. J. INT'L L. 551, 553 n.13 (1999).

159 *See* SHIHATA, *supra* note 19, at 58. The World Bank contains numerous subunits, each with distinctive twists and perspectives on policy. For a discussion of variation among World Bank sub-units, see Alvaro Santos, *The World Bank's Uses of the "Rule of Law" Promise in Economic Development*, *in* THE NEW LAW AND ECONOMIC DEVELOPMENT: A CRITICAL APPRAISAL, *supra* note 13, at 253, 253–300. The World Bank's adoption of structural adjustment lending occurred under the leadership of the Bank by Robert McNamara. *See* Broad, *supra* note 156, at 391.

160 *See* SHIHATA, *supra* note 19, at 58 (describing how structural adjustment lending was introduced in 1980 and "expanded and deepened" over the course of the 1980s); *see also* Howard Stein, *Structural Adjustment*, *in* THE ELGAR COMPANION TO DEVELOPMENT STUDIES 596, 598 (David Alexander Clark ed., 2007) ("A series of events rapidly put structural adjustment policies at the centre of the new World Bank agenda including . . . the elections of the conservatives Margaret Thatcher (May 1979) and Ronald Reagan (November 1980) . . . and the appointment of the ultraconservative and dogmatic neoliberal Anne Krueger (in 1982) as chief economist who systematically replaced most of the development research department with economists holding views similar to her own." (citations omitted)).

161 Thomas, *supra* nóte 158.

trade-liberalization programs.[162] In investment policy, state-led capital investment had to be stopped, state-owned investment enterprises needed to be privatized, and foreign investors needed to be welcomed.[163] In fiscal policy, government spending informed by Keynesian demand-side economics needed to be replaced by fiscal austerity measures to reduce deficits and inflation.[164] In monetary policy, inflation needed to be further controlled through currency "stabilization" programs.[165]

The World Bank first consolidated these two strains of neoclassical economics in its structural adjustment policies in sub-Saharan Africa.[166] By late 1989, the neoclassical program that originally focused on these macroeconomic reforms had explicitly identified "'governance' as a basic issue in the development strategy" of borrower countries in sub-Saharan Africa.[167] The time lag between the early Washington Consensus, which did not explicitly include governance, and the post-1989 Washington Consensus, which increasingly did,[168] is best explained against the backdrop of global geopolitics as it bore on the mandate of the World Bank.

In its Articles of Agreement, the World Bank explicitly prohibited its own interference in "political affairs."[169] For most of the postwar era, Article IV was interpreted consistently with a policy of deference

162 *See* David Simon, *Neoliberalism, Structural Adjustment and Poverty Reduction Strategies*, *in* THE COMPANION TO DEVELOPMENT STUDIES 86, 86–91 (Vandana Desai & Robert B. Potter eds., 2d ed. 2008); *see also* Dipak R. Basu, *Structural Adjustment Program and Public Fiscal Policy in India, 1990–1995*, *in* ADVANCES IN DEVELOPMENT ECONOMICS 155, 156 (Dipak Basu ed., 2009) (describing India's adoption of a structural adjustment program that required liberalization of import policies). The causes of economic reform are often multifaceted and stem from internal shifts in policy as well as from the external pressure of international financial institutions. *See* Basu, *supra*, at 156 (describing earlier shifts in India's policies); *see also* Thomas, *supra* note 11, at 275–77 (describing the influence of the Washington Consensus as one among several factors influencing economic regulatory reform in Mexico).

163 *See* Simon, *supra* note 162, at 86–91.

164 *See id.*

165 *See id.*

166 *See* Rohinton Medhora, *The Political Economy of Debt and Structural Adjustment in Africa*, 28 CAN. J. AFR. STUD. 300, 302 (1994) (reviewing E. WAYNE NAFZIGER, THE DEBT CRISIS IN AFRICA (1993) and BEYOND STRUCTURAL ADJUSTMENT IN AFRICA: THE POLITICAL ECONOMY OF SUSTAINABLE AND DEMOCRATIC DEVELOPMENT (Julius E. Nyang'oro & Timothy M. Shaw eds., 1992)) (citing the "apposite literature on rent-seeking behaviour or institutions" (citations omitted)); *supra* Part I.A.

167 SHIHATA, *supra* note 19, at 54 (citing WORLD BANK, SUB-SAHARAN AFRICA—FROM CRISIS TO SUSTAINABLE GROWTH: A LONG-TERM PERSPECTIVE STUDY (1989)); *see also* Rittich, *supra* note 13("[The] legal reforms that have been a feature of the development of agenda [sic] since the mid-1990s . . . gained force from . . . the conclusion that . . . governance failures lay at the root of the ongoing dilemmas of development, particularly in Sub-Saharan Africa.").

168 *See supra* notes 12–13 and accompanying text.

169 *See supra* note 17.

to regulatory goals set by the borrowing state.[170] Over the course of the 1980s, however, the neoclassical program became increasingly emboldened,[171] and the bulwark for Third World sovereignty, created by the Cold War and the West's competition with the Soviet bloc for the allegiance of developing countries, continued to erode.[172] Soviet leader Mikhail Gorbachev introduced perestroika in the late 1980s,[173] and Reagan's 1987 imperative to tear down the Berlin Wall[174] was realized in late 1989: the existence of the Soviet bloc crumbled along with its effect on the leverage of developing countries.[175] In the wake of these events, geopolitical impediments to the enshrinement of Western values in the global development policy dissolved. Instead, the existence of neoclassical[176] and neoinstitutional[177] perspectives that specifically envisioned institutional qualities as requirements for economic growth fueled this enshrinement.

Thus, by March 1990, the World Bank had introduced a vision of economic reform that explicitly integrated NPE and NIE perspectives and expanded from the regional focus on sub-Saharan Africa to a global lending policy.[178] The establishment of the European Bank for Reconstruction and Development (EBRD) later in the same year[179] explicitly reflected this consolidation of the macroeconomic and institutional dimensions of neoclassical economics.

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170 The policy of deference arose partially out of pragmatic considerations and partially out of a model of development informed by early postwar theoretical influences: Keynesianism and, more specifically, models of development economics which concluded that large-scale industrialization could not occur in poor countries without concerted intervention by the state. For a discussion of these influences, see Pereira, *supra* note 27, at 217–18.

171 *See* SHIHATA, *supra* note 19, at 58.

172 For a discussion of the Non-Aligned Movement in which Third World countries sought to leverage the Cold War, see generally THE PRINCIPLES OF NON-ALIGNMENT: THE NON-ALIGNED COUNTRIES IN THE EIGHTIES: RESULTS AND PERSPECTIVES (Hans Köchler ed., 1982); *see also* K. P. Misra, *Ideological Bases of Non-Alignment (An Overview)*, *in* THE PRINCIPLES OF NON-ALIGNMENT, *supra*, at 62, 73 ("[N]on-alignment has evolved over the years [a] multidimensional ideological framework responsive to the dynamic metamorphosis in post-war international relations.").

173 *See generally* MIKHAIL GORBACHEV, PERESTROIKA: NEW THINKING FOR OUR COUNTRY AND THE WORLD (1987).

174 *See* NATIONAL REVIEW, TEAR DOWN THIS WALL: THE REAGAN REVOLUTION—A *National Review* History (2004).

175 *See generally* PETER WILLETTS, THE NON-ALIGNED MOVEMENT: THE ORIGINS OF A THIRD WORLD ALLIANCE (1978).

176 *See supra* notes 155–65 and accompanying text.

177 *See infra* notes 191–225 and accompanying text.

178 *See* SHIHATA, *supra* note 19, at 58 & n.25, 59.

179 *See* EUROPEAN BANK FOR RESONSTSRUCTION & DEV., AGREEMENT ESTABLISHING THE EUROPEAN BANK FOR RECONSTRUCTION AND DEVELOPMENT 3, 5 (1990), *available at* http://www.ebrd.com/downloads/research/guides/basics.pdf [hereinafter EBRD AGREEMENT].

The EBRD preamble reflected the newly candid "political orientation"[180] of the development community in its emphasis on "the fundamental principles of multiparty democracy, the rule of law, respect for human rights and market economics."[181] Thus, this preamble not only encapsulated the full law and development formula[182] and represented the culmination of the theoretical project that academia had articulated decades before, but it also joined forces with domestic politics in the U.S. and Britain and ultimately influenced international affairs.

The EBRD was a reflection of forces that were also sweeping through the World Bank. Although the EBRD worked closely with the International Bank for Reconstruction and Development (IBRD), it was established by a separate charter.[183] Moreover, reflecting the "context of the historic political and economic changes" of the moment,[184] the EBRD Agreement did not contain the same prohibition on political interference contained in the World Bank charter.[185]

By contrast, the Bank's explicit turn to governance sparked "considerable debate, both within and outside the Bank,"[186] and even at the highest level of the World Bank's own internal governance structure—that is, at the Board of Directors, comprised of twenty-five Executive Directors representing all of the member countries.[187] At that moment, Ibrahim Shihata, who had been appointed General Counsel for the Bank in 1983,[188] shortly after Krueger's appointment as Chief Economist,[189] provided a "clarification" in response to this controversy and began to articulate the concept of good governance that would define the Bank's lending policy in the future.[190]

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180 SHIHATA, *supra* note 19, at 57.

181 EBRD AGREEMENT, *supra* note 179, at 4.

182 *See id.*

183 *See* SHIHATA, *supra* note 19, at 57; *see also About Us—Multilateral Development Banks*, WORLD BANK, http://www.worldbank.org/ (follow "About" hyperlink") (last updated June 30, 2003) ("Each bank has its own its own independent legal and operational status—but with a similar mandate and a considerable number of joint owners, the [multilateral development banks] maintain a high level of cooperation.").

184 SHIHATA, *supra* note 19, at 57.

185 *Id.* at 58.

186 *Id.* at 54.

187 *Id.* at 53, 54 & n.4. For the World Bank's description of its composition, see *Composition of the Board*, THE WORLD BANK, http://www.worldbank.org/(follow "About" hyperlink; then follow "Boards of Executive Directors" hyperlink; then follow "Composition of the Board" hyperlink) (last updated Nov. 1, 2010). The increase from twenty-four to twenty-five Executive Directors occurred in late 2010. *See id.*

188 IBRAHIM F.I. SHIHATA, THE WORLD BANK LEGAL PAPERS xxxvii (2000).

189 *See* CYPHER & DIETZ, *supra* note 101, at 216.

190 *See id.* at 53–54; *see also* Robert C. Effros, *The World Bank in a Changing World: The Role of Legal Construction*, 35 INT'L LAW. 1341, 1346 (2001) (quoting Shihata's remarks to the American Bar Association in 1994 that "[r]ecognizing that *good governance is central to fostering strong and equitable development* and is an essential complement to sound economic