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*Stiglitz discusses the worldwide economic reforms of the past two decades and the imbalance between the more-developed and less-developed countries that has become more pronounced with the spread of globalization and the growth in power of international financial institutions.*

**Shock Therapy in Russia: Was There an Alternative?**

INTERVIEWER: Let's start with the simplest of all questions: What does "shock therapy" mean to you?

JOSEPH STIGLITZ: Well, shock therapy is very rapid change in society. There was a kind of shock therapy that most economists supported, which is rapidly bringing down hyperinflation to reasonable levels. But there was another kind of shock therapy, which was a dramatic change in society, changing from a socialist economy, a communist economy, into a market economy by overnight privatizing, liberalizing, changing the rules of the game overnight rather than the gradual approach of changing one thing after another, so you may develop the prerequisites. So the gradual policy is really a policy that was pursued, for instance, in China as it moved from communism to a market economy. In a way what has happened is it's a race between the tortoise and the hare. In many cases, the gradualist approach wound up being faster than the shock therapy, because the shock therapy tried to push changes in societies before they were ready, before the prerequisites. You privatized before you had appropriate laws; you wound up with what is sometimes called the Wild East. And that Wild East, you didn't have wealth creation from privatization; you had asset stripping. You had the undermining of the basic social fabric of society. You didn't have growth; you had decline. You had increase in poverty rather than the fruits that capitalism was supposed to bring.

INTERVIEWER: So what happened in Russia?

JOSEPH STIGLITZ: In Russia, the people were told that capitalism was going to bring new, unprecedented prosperity. In fact, it brought unprecedented poverty, indicated not only by a fall in living standards, not only by falling GDP, but by decreasing life spans and enormous other social indicators showing a deterioration in the quality of life. The number of people in poverty in Russia, for instance, increased from 2 percent to, depending on the statistics you use, somewhere between 40 and 50 percent, with more than one out of two children living in families below poverty. The market economy was a worse enemy for most of these people than the Communists had said it would be. It brought Gucci bags, Mercedes, the fruits of capitalism to a few. And there were some people who were better off. You did have traffic jams when you didn't have them before. But you had a shrinking [economy]. The GDP in Russia fell by 40 percent. In some [parts] of the former Soviet Union, the GDP, the national income, fell by over 70 percent. And with that smaller pie it was more and more unequally divided, so a few people got bigger and bigger slices, and the majority of people wound up with less and less and less.

INTERVIEWER: So it achieved the opposite of what was intended?

JOSEPH STIGLITZ: Everybody expected that there'd be some increase in inequality, but the way it was done, the shock therapy resulted in a far greater increase in inequality than certainly anybody had wanted and than the advocates of the market had predicted. But what was striking was they got this increase in inequality, but with no benefit in terms of economic growth. The overall GDP, the overall national income, declined. There are only four countries, three or four or five countries, that by the end of 1999 were better off in terms of average GDP than they were at the beginning of the transition. And the declines ranged anywhere from, in some cases, like in Russia, to 40 percent, in some cases 70 percent. And obviously in that context, the political support for market reforms, and in some cases even for democracy, was undermined.

INTERVIEWER: So people like Jeff Sachs would say there was no other option, there was no other road to take [besides] shock therapy, and that the way it was applied was the way to do.

JOSEPH STIGLITZ: That's absolutely wrong. There were countries that were successful, and most of the countries that were successful did not follow the shock-therapy approach. China had a gradualist policy. In retrospect, in 20, 25 years, it actually has moved faster towards creating a market economy. They have a bigger stock market than almost any of the other emerging markets. So they've gone a long way, but it was step by step by step. And as they went on with this gradualist policy, they had enormous support from the people within their country. It wasn't forced on them; it was really something that everybody became convinced was the right way. Slovenia is one other very successful country, one of the countries [whose] GDP today is higher than it was at the beginning of the transition. It, too, followed the gradualist policy.

Poland is one of the most interesting cases, because it did use shock therapy to get inflation down. And some people think, therefore, it is a shock-therapy country, but that's not right. In fact, what it did is, having gotten inflation down to reasonable levels—and by that I mean 15, 20 percent a year, not to the very, very low level—it didn't pursue getting inflation down with a single-mindedness that was the case in some of the other countries. [Poland] then took a gradualist policy of restructuring their economy, restructuring their society. And the result of that was the best performance relative to where they were in the beginning of the transition. So there were alternatives, [and] those who choose the alternatives were more successful than those who choose the shock therapy.

INTERVIEWER: And in Russia's case, what went wrong specifically? Why didn't it work?

JOSEPH STIGLITZ: Well, there were an enormous number of mistakes one after the other. They began with the shock therapy of liberalization, eliminating all price controls for most of the commodities, but not all. The result of that was that there was a massive inflation. So the hyperinflation, the high levels of inflation, were in fact a consequence of the shock-therapy strategy in the beginning. That wiped out the savings of an enormous number of people. You didn't at that point have any basis of people having wealth to have a legitimate privatization process, using people's savings. They then had a privatization process that was corrupt, and in which the rich country's assets were turned over to a few, the oligarchs. So you had the strategy of privatization at any cost. "Do it quickly," is what the IMF kept telling them. They kept a scorecard—how many privatizations had you done? But it's easy to privatise [when you] give away the state assets to your friends. And, in fact, it's not only easy; it's rewarding, because then they give a little bit of money back to you. So that was a strategy that was advocated and pushed. They then had policies like capital market liberalization before they were ready.

So what did that mean? You had an illegitimate privatization. The people then who had been able to use their political influence to get these billions and billions of dollars of natural resources for a pittance were then told, "Well, you have a choice: Keep your money inside Russia, or take it to the United States." The United States was having a boom; Russia, because of the policies, was in a depression. Well, if you were smart enough to persuade Yeltsin to give up these billions of dollars, you were smart enough to figure out it's better to take your money in the United States or, even better, to Cyprus, secret bank accounts, or Switzerland, knowing full well that there will be a change in government. When there's a change of government, there will be a questioning of whether those privatizations were legitimate. If you had your money in Russia, people might say: "We want to do that over again. You effectively stole the country's assets." If they took the money out, you had to protect it. So the experiences in Russia show that in some sense economists are right: Incentives matter. But under the IMF strategy, you put in place incentives that led to asset stripping rather than wealth creation, and incentives that led to the implosion of the economy rather than to its economic growth.

INTERVIEWER: So what was the option then? What would have been a better road?

JOSEPH STIGLITZ: Well, the better roads were the roads that Poland, that other countries—Slovenia, China—have taken. First of all, they focused on creating new enterprises rather than just restructuring the old. They focused on creating jobs and employment so that as you restructured the old, you had new avenues [in which] to use society's resources. Moving resources from low productivity to unemployment doesn't increase society's wealth, doesn't increase anybody's income; moving resources from low productivity to high productivity does. But if you have tight monetary policy that has interest rates at 25, 50, 100, 150 percent, you can't start new businesses. And if you can't start new businesses, how are you going to have the new enterprises that are going to create the new jobs? As you're reorienting the economy you take out the resources from the inefficient sectors to move into the more efficient sectors. In the United States we talk about what raising interest rates by 1 percent or 2 percent does to job creation. In Russia, at one point, their interest rates were over 50, 100, and were up to 150 percent. How could you have job creation?

That was called a stabilization policy, but it wasn't stabilizing the society. It was actually leading to these policies that lead to, in some sense, the implosion of the society and the economy and a destabilization of society.

INTERVIEWER: Give me a better sense of how this affected the poor in Russia and the average person. What exactly happened to their money?

JOSEPH STIGLITZ: Well, a number of things happened that contributed to the increase in poverty. Poverty, as I said before, increased from around 2 percent to 40 percent or more, depending on how you calculate it—you know, one the most rapid increases in poverty that the world had seen in that short a span of time, apart from a natural disaster. What happened was that with the tight monetary policies that were pursued, and the other policies that were pursued, firms didn't have the money to even pay their employees, so while they often didn't fire them, because what good would that do, they didn't pay them. What was tragic about it is while they didn't have enough money to pay their pensioners, to pay their workers, they were giving away the valuable state assets to a few rich people. So in a way there were the resources there, [but] resources were leaving Russia in massive amounts. Billions and billions were leaving with these open capital markets. So they privatized before they had a good tax system in place. It's very easy to tax oil, and you can monitor the amount of oil coming out; you can monitor the amount of oil that's being shipped abroad. It's actually relatively easy. But they privatized it before they put in the means of taxing the most basic resource of the Russian economy.

And so by not getting the sequencing right, by not pacing it right, they led to the impoverization of massive amounts of their people. Then, with the government not having enough revenue, other aspects of life started to deteriorate. They didn't have enough money for hospitals, schools. Russia used to have one of the good school systems in the world; the technical level of education was very high. [But they no longer had] enough money for that. So it just began to affect people in every dimension of their lives.

**Bolivia and Argentina: Stabilization Without Economic Growth**

INTERVIEWER: Surely [the advocates] of this shock therapy [often point to] Bolivia, which overnight managed [almost] to change its hyperinflation from some exorbitant amount to the single digits. How would you classify that experience?

JOSEPH STIGLITZ: Well, as I say, it is important for countries to get hyperinflation down to moderate levels—[otherwise] it's very hard for the economy to grow—and that needs often to be done relatively rapidly. But one can't confuse a policy of stabilization with a policy for economic growth. Stabilization brings inflation down to moderate levels; it's necessary, but it's not sufficient. ... [In Bolivia] they're going through another recession, as is the case in many, many areas in Latin America. The reforms that were ordered which did lead to economic growth at the beginning of the '90s were short-lived. By '97, growth had stopped. We've now had almost a half decade of stagnation, in some cases recession, in some cases depression.... I think that the market reforms were in many cases right. They are important parts of success, but they're only part.

INTERVIEWER: [So in Bolivia], the overall results might not have been as good as people originally thought. Tell me what you saw.

JOSEPH STIGLITZ: I saw a country that was facing recession. I saw a country that was asking questions like, why is it that when the United States faces an economic downturn, everybody says you ought to have a stimulus? But in Latin America, when they have an economic downturn, they're told to tighten their belts, [to] go back to the kinds of policies that were used—we call them Hooverite in the United States—policies that were rejected by the new economics, Keynesian economics, several years ago. The policies that they were taught in their graduate schools and undergraduate standard textbooks, every textbook says that when you have a recession, you're supposed to have expansionary fiscal policy. [But] they're told no, that's not right; you have to cut back your expenditures. And when that happens, the economy goes down.

But more broadly, what we see in countries like Bolivia, they're asking: "Okay, now we felt the pain; we've felt the pain of contraction and austerity. When do we start getting the fruits?" And in retrospect they say: "Well, yes, we had a few years of growth, but those few years of growth exposed us to an enormous amount of volatility. And now we have four, five years of stagnation, recession, depression." And looking at the statistics, if we look at a longer span, our growth record now in this decade doesn't appear particularly impressive.

And, in fact, what growth we had could largely be interpreted as a catch-up from the lost decade of the '80s, a lost decade caused by mismanagement of the last economic crises by the IMF. And they look around, and they say, "Look at the star pupil—Argentina." [In] '91, '92, '93, '94, everybody described it as the best performing economy. They followed the IMF prescriptions; they got rid of hyperinflation. They did succeed, but they didn't get the kind of sustained economic growth that is going to bring benefits to all the people. The result, since 1995: double-digit unemployment. An economic framework that originally worked to bring down inflation became a shackle that did not allow the economy to grow. The wonder in Argentina is not that there were eventual riots; the wonder is that it took so long for them to occur. At the time they occurred, unemployment was approaching 20 percent; open unemployment and disguised unemployment was another 10 or 15 percent. What kind of democracy can sustain that kind of failure of economic policy? And some people will say it's the problem of the Argentineans, [but] the IMF and the policies they imposed have a high degree of culpability. They exposed it to disturbances, interest rate rises around the world, that were not caused by its misperformance, but by a global failure, global problems. They couldn't adjust quickly enough to these, but I'm not sure any country could have, any democratic country could.

INTERVIEWER: But in the case of the Argentinean people, some people would argue they just didn't do enough. What would you say to people who say that?

JOSEPH STIGLITZ: Well, what I say is they went very far towards reform. Prices were not only flexible; they were falling. Wages were falling. People were seeing their incomes decline. Maybe, you know, critics say, "Well, they should have declined faster; they should have gone into poverty quicker." That was what the prescription was saying. But the fact is, you know, I don't want to say that they did everything right, because clearly there were mistakes made all around, but the economic straitjacket of being pegged to the dollar made their life impossible, particularly in an environment where the dollar was overvalued. Their neighbor Brazil devalued enormously; the euro was weak. They were in an impossible situation. And then, with the IMF giving them a good report card for so long, they borrowed too much from the international markets, which just kept pushing more money on them, [saying], "Fine, take it if you want it," until they all of a sudden change their minds, saying, "Oh, no, I'm sorry—now you have to pay us high interest rates." The debt GDP ratio in Argentina was only around 45 percent. In Japan it's around 130 percent. So even in terms of their indebtedness, it was not outrageous. But they were put in this economic straitjacket which the markets rightly recognized would be very difficult for them to get out of.

**The Importance of Sequencing and Pacing to Successful Economic Reform**

INTERVIEWER: Why is there that sort of moral double standard, that when there's recession in North America they say, "Let's expand and spend money, stimulate the economy," but that prescription is opposite for places like Latin America?

JOSEPH STIGLITZ: I think that that's a difficult question. It certainly goes against all standard economics. I think that part of it is that there's greater focus on worry about repaying creditors than what you do to sustain the lives and livelihoods of the people in the country. Even when they were having economic growth, the benefits went mostly to the upper-income people. Mexico had economic growth, but the lower part of the people, the lower 30 percent, saw stagnation and even decline. So they didn't focus on the overall economy within the country. They didn't focus on poverty; they focused on "What can we do to make sure that the creditors get repaid?" And if you cut back on your GDP, you import less. When you import less, your reserves build up, and you have more money to pay back the debts that you owe. And so it became a focus on your reputation and your credibility with the financial markets, not what were the fundamental issues of leading to economic growth and the concerns of the people inside the country.

INTERVIEWER: Looking sort of generally at Latin America, it seems like country after country after country followed Bolivia's example. Do you think they made a mistake?

JOSEPH STIGLITZ: Well, as I said, some of the policies that Bolivia did were right. Getting hyperinflation down was right; privatization of many of the enterprises was right. It wasn't that the policies were, in that sense, wrong policies. The problem was that they weren't accompanied by other policies that would have led to economic growth. To give you an example, in the case of Argentina, the way they went about privatizing, they privatized a lot of utilities and gave the foreign firms that bought the utilities a guarantee of the price that they were able to sell that was indexed to American prices. But meanwhile, prices in the country itself were falling because of the straitjacket they were put in, so you had the utility prices rising relative to the incomes of the people. That was a recipe for disaster. In other countries you privatized before you had in place an effective competition policy, so you created a private monopoly. The private monopolies were better able to exploit the consumers than the government would, because the government was checked by the political process; the private monopolies were not. So it was the way things were done, and the sequencing and the pacing that was done.

Bolivia was quite remarkable. It brought down its tariffs; it opened up its markets. But the North, the United States and the other countries, didn't reciprocate. So the goods that Bolivia could have sold, it couldn't get access to those markets. So the pacing again was wrong. Bolivia could have produced sugar, and that could have increased their income. The United States said: "No, you can't export sugar to us. We believe in free markets, but not for you. You can't sell your goods to us."

**The Chilean Miracle: "Combining Markets with Appropriate Reform"**

INTERVIEWER: Let's look at the one sort of example of the "miracle," I'd say, in Chile, where Milton Friedman once said, you know, you just can't cut the dog's tail little by little; you've got to hack it [off all at once]. And they followed that, and it seems that by all accounts everybody was really impressed with Chile for a long time. What are the lessons?

JOSEPH STIGLITZ: Well, first of all, when they followed Friedman's prescription, Chile had a crisis, the free banking experiment, that was done under the intellectual leadership of that free-market hypothesis. They had the kind of bank boom and bust that we've seen around the world. And Chile, while it grew [and] then fell precipitously, has now recovered from that and has been growing strongly. But that experiment in the real free market was not a success. They went from that to a much more regulated market economy. They imposed capital controls, controls on the inflow of capital, so they wouldn't be inundated in the way that Thailand was, which led to the [1997 Asian] crisis. So it's not an example of free market; it's an example of a success of combining markets with appropriate regulation. Some parts of their achievement were achievements that in retrospect are beginning to be questioned, and are, even to the extent they were successful, unique to the particular circumstances of Chile. For instance, one of the experiments of Chile was privatization of social security. When you privatize social security, you have a set of unfunded contingent liabilities of people in the future. Chile was lucky it had these copper mines that it was able to privatize and use the revenues to fund that unfunded liability associated with the social pensions or public pension program.

Most countries don't have copper mines that they can privatize. And so in the process of trying to privatize or fully fund social security, you have to get the funds somewhere, from taxes or otherwise. And that has been a real problem in many of the other Latin American countries. When the stock market was booming, everybody loved the Chilean system. People invested in the stock market; the prices went up. But after the '97 crisis things didn't work out so well for an awful lot of people. The stock market crashed, came down precipitously, and with that many people's savings were lost. Even in countries where capital markets were better, as we've looked in more detail at what is entailed by this free-market solution, what we see is that things aren't quite what they were cracked up to be. In England, for instance, in the UK they've privatized part of the social security system, the old-age pension system, the public old-age pension, and it's been discovered that pensions are reduced by up to 40 percent as a result of transaction costs. Now transaction costs, while they make the pensioner poorer, that money goes to somebody else, to the people in the financial market. So for [the financial markets] it's a great thing.

**Inequalities of Globalization**

INTERVIEWER: So for Latin America, have free markets been a step in the right direction?

JOSEPH STIGLITZ: Well, I think they made a lot of steps in the right direction. But right now, throughout Latin America, people are asking the question, "Has globalization failed us? Has reform failed us?," because what they're seeing is that they didn't get [what was promised]; [the gains] weren't sustained. In fact, the two questions are not really distinct, because an essential part of the reforms was buying into globalization. My view is that it was important for them to make most of these reforms, but the failure was to recognize that they were only part. They were prerequisites, and done in the wrong way with the wrong pacing, the wrong sequencing, they weren't going to develop benefits for the vast majority of people. Trade liberalization leads countries to face a deluge of imports, in agriculture or subsidized agricultural goods, from the United States. How can a Jamaican milk producer compete with the highly subsidized [producer] from the United States? And so the job destruction then came before the job creation. The tight austerity that was imposed by the IMF meant there was no opportunity for job creation. So part of it worked. You got the not necessarily inefficient [industries], but the industries that could not compete with the American-subsidized agriculture or European-subsidized agriculture; that couldn't go into producing sugar because the United States wouldn't buy it. And you had that happen before you had the opportunities for job creation.

INTERVIEWER: And yet there's still sort of a perception out there that the rich got richer and the poor got richer. And, you know, maybe there was a wide gap between them, but everybody was still better off 15 years on.

JOSEPH STIGLITZ: The number of people in poverty in many of the countries actually increased. In some of the cases it wasn't just that the gap between the poor and rich increased, but the people at the bottom actually went down. You know, the people who had been milk producers, eking out a living, now were unemployed. The people who were producing corn, who saw the price of corn fall, they couldn't compete with the subsidized American corn. So they saw the price of corn fall and with that, their incomes.

Some people were better off. The people in the cities found lower prices for corn and milk, and their standard of living went up. So there were winners, and there were losers. The problem is that there were a few big winners, and many, many people who saw a little gain, but very, very little, and many people who saw significant losses. So when you look at the overall picture, you have to say the net effect was an increase in stress within the society, and in many areas of Latin America, that stress has manifested itself in ways that are very destructive. Urban violence is prevalent in many places. Why? You think people prefer lives of crime rather than gainful employment? The fact is young men don't, can't find jobs, and without jobs, they turn to crime.

In the United States we found that when we got our unemployment rate down, in the '90s, it had an enormous impact on our crime rate. And when you get the unemployment rate up, which was an intrinsic part of the policies that were pushed in these countries, this social stress was inevitable. The implication, of course, is that societies in which there is a high level of violence are not going to be attractive for investment. So in the end it turns out not even to be good economic policy.

INTERVIEWER: So free markets are bad?

JOSEPH STIGLITZ: No, free markets are good, but in the United States and in Europe, we've learned to combine free markets with an important role for government. Markets are the engine of the economy, but we recognize that markets by themselves do not deliver. In the United States, even with its sufficient financial market regulation, we had the savings-and-loan crisis that cost American taxpayers several hundred billions of dollars. The Enron scandal has now exposed the fact that without adequate regulation on the principles of accounting, people can have their life savings wiped out overnight. Since the beginning of capitalism, there have been fluctuations of the market economy, recessions, depressions, and we've learned that active government policy, stimulus, fiscal, monetary can reduce the magnitude of the downturns in their frequency. We know that; the data supports it. And yet, for reasons I do not understand fully, the IMF has been pushing policies that are precisely contrary to that in country after country after country.

INTERVIEWER: What's good about trade?

JOSEPH STIGLITZ: Trade creates the opportunity for small countries to have access to huge markets and to take advantage of their comparative advantage. That means that incomes can rise. Now, in the United States and in advanced industrial countries, we often say that trade is good, but imports are bad. We like to export, but we don't like to import. Why? Because we recognize that sometimes imports lead to job destruction. We recognize that it is the responsibility, though, of those involved in macromanagement, the Central Bank—the Fed in the United States—to ensure the economy remains close to full employment. But even when we had unemployment of 3.9 percent, 4 percent, we worried. We worried about the unemployment that a flood of imports could create, even though these people could get jobs eventually elsewhere in the economy. The current [Bush] administration, for instance, has proposed creating a global cartel in steel to protect American steel producers from the onslaught of less expensive steel. Korea has a far more efficient steel industry than the United States. We don't like that, and it's a threat to our steelworkers, as well as the profits of our steel industry. So we recognize there's a problem.

But just think of what it would be like if you're an economy, like many of the developing economies, with unemployment, not 3.9, 4, 4.5 percent, but unemployment of 10, 15, or 20 percent; not an economy in which interest rates are 3, 4, 5, 6 percent, but an economy in which interest rates are 15, 20, 25, 30 percent. In those situations, if you lose a job, you worry about not being able to get another one. At least in the United States and Europe, when you lose your job, we have an unemployment insurance system and a welfare system. Imagine you're in a less-developed country where there's no unemployment insurance system, or one that really doesn't cover very much, pennies. Imagine that you're in one of these less-developed countries where there's no welfare system. A loss of a job means that your children won't be able to go to school; they'll face malnutrition. These are really life-threatening events; these are not just statistics. You know, unemployment went up from 4 percent to 8 percent. These are things that are going to destroy the lives of these people.

**The North-South Divide: Who Makes the Rules, and Who the Rules Benefit**

INTERVIEWER: The world has sort of swung on this pendulum from accepting command economies to going to free markets. Where is it going to swing next?

JOSEPH STIGLITZ: Well, I think there is now an acceptance of trying to get that balance. We now recognize that there is an important role for government. The exact boundary of where that role is is one [thing] that's hotly debated in all of the Western democracies. ... Some people think there ought to be more privatization of, say, social security. Some people think the current arrangements are appropriate, but we debate these issues; we debate them hotly. The problem is that the IMF has pushed a particular view of these economic policies, the view that says free markets by themselves work, or a view which puts more emphasis on the private markets than many of us, within our own democracies, where markets worked very well, would believe is appropriate. And so they have been pushing what can only be viewed as a particular political agenda, and using international institutions to pursue that particular political and ideological agenda. And there's a recognition that that's no longer going to be acceptable.

There's also a recognition that the international arrangements are not balanced—the trade negotiations of the past where an agenda that was set by the North for the North, and the North benefited. For instance, the great achievement, one of the great achievements lauded by the restraint of trade negotiations during the Uruguay Round [1986-1994] was that we finally got into service, but what services? Financial services, which are the export industry, the comparative advantage of the United States and Europe. Services like construction services and maritime services were not even on the agenda. These are the things that are concerned with developing countries. But the United States still remains protectionist in these areas, but will not even allow these to be brought up.

INTERVIEWER: So who should set the new rules of the game?

JOSEPH STIGLITZ: I think we have to redesign the governance of the international arrangements, the international institutions. We have to recognize that we share one planet and that there are basic principles of fairness and equity that we have to adhere to; that the kind of hypocrisy that has characterized the past really cannot be sustained. It's one of the great things about openness and transparency. ... These things have brought out in the open. One of great achievements of the last five years is that people have seen, become aware of some of the feelings of the way things were done in the past, recognize that excessively strong intellectual-property protection meant that people in countries like South Africa were being condemned to death because they would not be able to get access to AIDS drugs. And that was changed in Doha [site of the 2002 World Trade Organization meeting, in Qatar]. But it took a massive global protest to do it.

When I was in the White House ... [as chairman of President Clinton's] Council of Economic Advisors, discussions of these intellectual-property regimes were going on. We thought that what was being advocated in the Uruguay Round was unbalanced. We thought it didn't pay enough attention to the users, both the users in the developing countries and the users in the academic community, and that as a result, not only would there be these kinds of inequities that people had been talking about, but even the pace of innovation might be slowed down.

But the agreements that were made were dictated by the corporate and financial interests. Those interests who want a stronger protection dominated. There was not a balanced discussion. And the consequences of that have now been made clear. And so the good news is that as we've seen these inequities, there is an outcry around the world, not only from the South, who recognizes, who's lived with this for decades, but also from well-intentioned people in the North who have said, "How can we accept this?"

**Is Capitalism in Crisis?**

INTERVIEWER: Are you familiar with the work of Hernando de Soto?

JOSEPH STIGLITZ: Yes, I am.

INTERVIEWER: And do you feel that his views are too simplistic, that it's all about property rights, or is that the right solution?

JOSEPH STIGLITZ: Well, property rights are important. Property rights are part of a market economy, and you can't have a well-functioning economy without strong property rights. On the other had, to say that that is the solution, I think, is overly simplistic. I'll give you one example. In many countries, a problem is that individuals don't have title to their land. Without title to their land, they can't borrow against their land; without borrowing, they can't get access to, say, the fertilizer or the other things that would improve their productivity. And in that he's right. But in many places titling is only one part. For instance, if there's no land market, you won't be able to borrow against your property even if you are titled, and there will have to be developed other sources of credit. That's why a lot of people have been putting a lot of emphasis on micro-credit, schemes, ways of getting out credit to the poorest of the poor. And there have been a lot of successes in that.

INTERVIEWER: And when Hernando de Soto says that this is the moment of capitalism's greatest crisis, do you see that?

JOSEPH STIGLITZ: Well, capitalism has had a lot of crises. The Great Depression was a great crisis. I think what is true, what is an issue here, is whether globalization, which has the potential to enrich the lives of so many people—it has enriched the lives of so many people—can be spread, if its benefits [can be] spread [to] more countries and to more people. If we don't reform the way globalization works, if we have globalization in the way that it has been working in the past, eventually there'll be opposition to globalization—there already is. And this opposition will become more and more emboldened, and ... in many countries they'll say, "No, we don't want it," or they'll put all kinds of impediments in it.

INTERVIEWER: But is globalization not irreversible?

JOSEPH STIGLITZ: Oh, the overall process of globalization is irreversible. But the real question is, how does it affect different people? It is perfectly clear that we may not have another round of successful trade negotiations. If we don't, the developed countries [will not be living] up to the implicit commitments that were made in Doha. This was supposed to be a development round. There was enormous fighting to put on the agenda issues that were of concern to the developing world. But of course the developing world just doesn't want to have discussion; they want to have real progress. And unless real progress towards a more balanced trade agenda is made, the further steps will not occur.

INTERVIEWER: So the world will move back towards protectionism?

JOSEPH STIGLITZ: That could happen. That could happen. Unless the imbalances of the past are redressed, it will be very difficult to go forward with the continuing progress in opening up markets. And those who want to step back and say we have to at least have some forms of increased protection will increasingly prevail. If the United States is setting bad examples, like starting up steel cartels and aluminum cartels when one of their industries is attacked, that will be imitated. When the United States accuses other countries of dumping simply because they were undercutting American goods, other countries will imitate, and they will charge us with dumping, and a whole variety of not only tariffs, but tariff barriers, will start to arise. This is a real danger. And in that sense, the movement towards globalization can be partly reversed. To put it another way, in the 19th century—the end of the 19th century, trade as a fraction of GDP was actually higher than it is today; it was reversed. The events of World War I, the aftermath, did reverse globalization, and it could happen again.

**The Asian Crisis**

INTERVIEWER: When you look at what happened in the Asian crisis, do you think that globalization will make crises like that more common in the future?

JOSEPH STIGLITZ: The East Asian crisis was, to a large extent, caused by pressure, by policies of excessively rapid capital and financial market liberalization that were pushed on these countries by the IMF [and] the U.S. Treasury. It led to an onslaught of capital into these countries, and then capital [flowed] out. Even countries that were much stronger economies would have been hard pressed to have survived the magnitude of these vacillations in capital flows. Today, even the IMF recognizes the dangers of this kind of opening your markets to speculative hot money, although their policies have not really moved commensurately with the change in this recognition. Over the last 25 years, crises have become more frequent and deeper, even though the IMF's responsibility is to enhance global stability, [but it's some of the IMF's] policies which have led to this increased instability. We are now in a situation where we've come to recognize these problems. We recognize the risks that are associated with these policies of capital market liberalization. Countries are trying to design policies that allow them to manage these risks better. It is too soon to know whether those policies will be fully successful. I'm hopeful that as they recognize the dangers and they engage in strategies to insulate themselves from some of the worst aspects of this, that crises may... that the failures of the last two decades will become less frequent, but I think it's too soon to tell.

**How Have the Economics of Keynes and Friedman Fared Over the Years?**

INTERVIEWER: ... Just one [last question]: What is your verdict on Keynesianism, [after] all you've seen in the last 20 years?

JOSEPH STIGLITZ: There have been enormous changes in thinking about economics over the past 50 years. Adam Smith, 200 years ago, put forward the idea of the invisible hand, that the market automatically takes care of things, [that] the market is self-regulating. In the last 30 years we've recognized that the assumptions required for that conclusion to be true are just not satisfied in more-developed countries let alone less-developed countries.

The work that I did, for which I got the Nobel Prize, focused on the problems associated with imperfections of information and particularly asymmetries of information. We recognize that these imperfections of information, asymmetries of information, are pervasive in every economy, but especially in developing economies, where the market for information doesn't work as well. And the essential result of this research of the last 30 years is to show that Adam Smith's invisible hand is not true, [that] whenever there are these imperfections of information and these other market failures, that markets very frequently fail, and fail massively.

Now, one of the most important market failures has been discussed, of course, for a long time, and those are the great depressions and recessions that have plagued capitalism since the beginning, periods in which 10, 20, 30 percent of the labor force can't get jobs, periods in which a large fraction of the capital stock remains idle, periods in which poverty increases. Those who believe in the free market believe that, while these events may occur, the economy very quickly recovers. That view is simply wrong. [John Maynard] Keynes recognized that. Keynes created a particular model to try to explain why that was the case and, on the basis of that model, to say what policies could resolve these problems, what government could do to reduce the length of recessions, to get the economy out. Those policies have worked. The magnitude of the downturns, the length of the downturns since World War II, under the influence of Keynesian policy, are much shorter than they were before World War I. Keynesian policies work.

Now, at an intellectual level, there were a lot of problems with Keynes. After all, he wrote 70 years ago, and we didn't have the economic theories, like the theories of asymmetry of information, on which to develop what is called the microfoundations of these theories. Over the last 30 years, one of the main things that I've been working on, and a lot of other people were working on, is to create that intellectual foundation. We now have that.

So am I a Keynesian? Well, sometimes people say I'm a new Keynesian; that is to say, the basic lessons are the same, but the intellectual foundations are much stronger than they were 70 years ago, which is what we would hope to be the case. After all, that's the whole point of research, is to try to understand these phenomena better. So the way I would put it is they're building on the foundations of Keynes. In modern microeconomics, we have now created theories of macroeconomics that do far, far better in explaining the kinds of fluctuations that we see in East Asia, in Latin America, and even in the United States. And on the basis of that, we have better policies that can help redress these problems, maintain greater stability, help the economy get out of recessions when they do occur.

INTERVIEWER: What about Milton Friedman?

JOSEPH STIGLITZ: Well, Milton Friedman made very important contributions to economics. But the ideas of free markets are basically more ideologically based than based on sound economic theory. You know, models in which information is assumed perfect just don't make sense in the modern world. You talk about an information economy where so many people are engaged in acquiring, processing, disseminating information, and the models that Friedman grew up in and that he's worked on for most of his life, information was effectively assumed to be perfect, and there wasn't the close study of how this information processing works, how markets handle risk. So he was really in the tradition of Adam Smith, elaborating on those ideas in a very particular intellectual frame, a particularly narrow intellectual frame. And part of that progress is to say, "Well, that was an important contribution. But today we know our economy has changed, and we know more about how the kind of economy that we have today functions, and the kinds of theories that he developed simply don't work well, either in the developed or the less-developed countries."

**Reforming the Rule Makers and the Need for Transparency**

INTERVIEWER: And now my favorite question: Is there something you'd like to say that I haven't asked you?

JOSEPH STIGLITZ: Well, one of the central problems that we face in the international arena is that we've now come to recognize that international economic institutions are important; we need rules of the game. The WTO sets the rules of the game for trade. The IMF sets the rules of the game for finance. The question is, within our own country, when we try to create the rules of the game, we have democratic processes with democratic accountability. When we make those rules, we don't say to the U.S. Treasury, "You go ahead and make the rules for the financial markets that the financial market wants." We don't say to the Department of Commerce, the U.S. trade representative, "When it comes to business, you set the rules; you go talk to the business community and see what they want." You say, "Talk to them, but we want to look at this from the perspective of our whole society." And we have what we call in the United States the National Economic Council, where we all sit around a table and we debate this. We look at it from many different angles—from the perspective of the workers, from the perspective of commerce, perspective of the financial community.

In the international arena we don't do that. And that is why we are running into so many problems in the international arena. The trade ministers get together to set the rules of trade. They don't worry about the environment; that's somebody else's agenda. Trade above all—that's the way they approach it. And as a result of that, we get a trade agenda that puts environmental and other concerns below. The IMF ... is not just making rules like "How do we clear checks?" They're making rules and policies that affect workers, that affect small businesses, that affect everybody in our society. And yet these other people have absolutely no voice. To make matters worse, the representation of the countries in this international arena are often not in accord with any democratic principle. In the UN, five nations have the veto power, largely determined by historical accident of World War II. Some people ask, "Why is France there and not India?" In the IMF, one country alone has the effective veto power. The allocation of voting rights is not by democratic principles. In our own democracies, when we vote on economic issues it, we don't say that if you're Bill Gates you should get many more votes on what kind of antitrust law we should have because you're bigger. No—we have one person, one vote. Yet in the IMF it's the richer countries that have more votes.

But it's not even wealth based [on countries as they are] today. It's wealth based largely on the way things were at the end of World War II, with some adjustments since then. And no wonder that out of this system of governance, where the voices of only some are heard, and the voices of some are heard louder than others, you get international arrangements, economic policies that seem bizarre, seem not in accord with what most of us think conforms with good economics, let alone basic principles of social justice. And unless we change the system of governance, it will be very difficult for us to achieve fundamental reforms in the international economic arrangements.

In some ways things are even worse than I just described in the context of the IMF, because Central Bank governors play a central role in the governance, in the decision making of this institution. But Central Bank governors in most countries, in many countries, are not directly democratically accountable. And the real irony is that the IMF has been pushing an agenda to make them more independent, so the IMF has been pushing an agenda to make itself more accountable to people who are less democratically accountable.

The reforms that I would advocate would be first [to] begin by changing the governance, but that's going to be difficult. The United States is not going to give up its veto power at the IMF. The second thing that is doable, though, is increasing transparency. Much of what goes on goes on behind closed doors. There are even instances where the U.S. government has a hard time, the U.S. Congress has a hard time finding out how the U.S. representative in these institutions has voted. Through transparency others have begun to see what is going on, and as that happens [the institutions] have become subject to greater scrutiny, and that is part of the criticism that has been levelled against them so strongly over the last five years. As they see what's going on, people have been asking questions.

Among the questions is, for instance, that they make predictions of what's going to happen: This policy is going to lead to this consequence. But they won't make their models available, so people can't criticize—you know, how did you come to that conclusion? Within modern science, modern economics, when you do research, you have to make your data and your model available so other people can look at it, to evaluate it: Is it right? Is it wrong? Does it work? Doesn't it work? The IMF still refuses to make its models publicly available in many cases. So transparency is a very, very important reform, and I think one for which there's increasing demand, but in which there is yet to be adequate response. In the United States, when we had these problems in the Nixon era, we passed a Freedom of Information Act, where American citizens have the right to go to their government and say: "What are you doing, and how did you make that decision? Who did you talk to?" There is no such thing in international institutions. We need to have that. So that's a second reform that I would do.

The third set of reforms that I would have are particular reforms for each each of the institutions. As I said, you know, for trade, we need to have a more level playing field. We have to get rid of hypocrisy. As for the IMF, it needs to focus on the one area that it was created for: promoting global stability. Part of that would be moving away from the era of the big bailouts, which actually make things worse, to a focus more on standstills and bankruptcies. The rhetoric is there, but the reality has not yet gotten through. [There is not yet the recognition] that its policies have an impact on poverty. [The IMF] should tell us when it has a program, what it estimates [that program's] impact on poverty will be. Again, the rhetoric is there, [but] we're now waiting to see whether reality will conform to that rhetoric.