Introduction

José María Fanelli and Lyn Squire

Imagine that you have recently assumed the position in your government which has full responsibility for the implementation of your country's ambitious program of reform. Imagine further that at your very first press conference you are asked to list the three most crucial points that must be kept in mind when managing reform. What would you say?

This is not an easy question to handle at any time, and it is especially awkward at an initial press conference and when posed in such a precise form. On the other hand, we have all probably pondered at least some aspects of this question and can draw on experience of one kind or another to fashion a reply. Thus, the economists among us may well stress the importance of macroeconomic stability as their first and foremost point, followed by liberalization of key markets including trade and then by more complex reforms, including privatization, to improve incentives in key executing agencies. The economist, therefore, may worry about the key elements of policy and also about their appropriate sequencing. Of course, for every economist there may well be a different set of policies and a different sequence, but the focus will be very much on measures.

A political scientist confronted by the same question will take a different route. He may well give pride of place to forging a consensus within society prior to reform. His second point may be the importance of managing the distribution of costs and benefits of reform in relation to the distribution of political voice. And his third point may have to do with efforts to lock-in reform and prevent reversals. In other words, the points appearing in the political scientist's reply may be more process-oriented. If we next consult an institutional expert, we may learn that the first point to keep in mind is the fundamental importance of the rule of law, closely followed by the effectiveness and transparency of the agencies of central government and then their local and sectoral counterparts which will have much of the responsibility for implementing reform. In short, the emphasis would now be on, predictably, institutions in their various manifestations.

We could continue in this vein and garner more views from other disciplines and perspectives. All of the points emerging in this fashion are important in some sense and at some level, and yet none easily emerges as one of the three most crucial. The identification of three such points which would command a broad consensus is not to be found by sifting through the many plausible responses generated in this way. Instead, they must be sought at a more fundamental level, one that cuts across the different perspectives and identifies more basic points which should command the attention of the would-be reformer without question. In a speech to open the Fifth Annual Global Development Conference held in New Delhi in January 2004, Nobel Laureate Amartya Sen probed this question at such a deeper level. The three points emerging from his analysis are the subject of this volume.

Denoted the ‘Three Rs’, Sen identified Reach, Range and Reason as the key dimensions of reform. As its name suggests, *Reach* refers to the requirement that reform be inclusive. Sen emphasized two dimensions of inclusiveness: across all facets of society – not just economic, but political and social as well – and across all individuals in society, especially those at the ‘bottom of the pyramid’. *Range* is to instruments as *Reach* is to ends. Consequently, the means to pursue the ends of reform inevitably involve many institutions and policies. Finally, *Reason*, which Sen considers to be the most important of the Three Rs, captures the absolute necessity of systematically and continuously asking why a particular reform has been selected or why a particular reform is being implemented.

While the Three Rs have been introduced separately (and will be treated separately in this volume for presentational reasons), they should be considered in unison to fully appreciate Sen’s contribution. Thus, when illustrating how to use the Three Rs as criteria to assess reforms in the ‘battlefield’, Sen underlines two points: social changes create *interdependencies* among different political, economic and social dimensions, and the performance of the economy and society largely depend on the reasoned assessment of *details*. These points have two consequences: One, the reach and range of reforms cannot be defined independently of the context; and two, the constant scrutiny of the reason for reform must take into account the precise way in which specific reforms influence living standards and human capabilities. Therefore it is important to flesh out Sen’s principles with empirical evidence concerning particular reform experiences. This volume undertakes that task.

Each chapter addresses particular aspects of the Three Rs in specific reform contexts. We have used Sen’s construct as the organizing principle to group the chapters under three headings: Reach, Range and Reason. The ten chapters include cross-country studies of developing countries, as well as country-specific studies for Egypt, Ethiopia, Hungary, Kenya, Mexico and Peru. They

also cover a diverse range of reforms including broad reforms, such as trade liberalization, privatization and even the transition process itself, in addition to far more narrowly defined ones dealing with rural roads, primary school enrolment, child labor, property rights and poverty traps. An important and distinctive characteristic of this volume, and indeed of all activities sponsored by the Global Development Network, is that the chapters are written primarily by researchers from the developing and transition worlds, yielding two advantages. First, the research is the work of those with genuine local knowledge of reform. Second, the research provides a perspective on reform from the developing and transition world. Their contributions are organized under the three headings as follows.

REACH: PERSON-CENTERED, EVENHANDED

Sen's notion of reach stresses the importance of the ethical foundations of any reform program. Reach refers to the coverage or breadth of the goals of reform and has two distinct but related elements. First, reform must be 'person-related' or people-centered. His basic example draws and builds on much of his previous work (Sen 1999). He notes that it is not sufficient to focus on economic growth, important though that may be. Other aspects of life – health, educational attainment, political rights and social inclusion – are also important both in their own right and, in many cases, as significant contributors to future growth in incomes (Stern, Dethier and Rogers 2005). Second, if reform is concerned with improving the lives and well-being of people, then it is only natural that the scope of reform should encompass all people: reform must also be inclusive. Inclusiveness obviously extends to all people, but it implies a particular emphasis on the poor since their needs are the greatest and often the most neglected. Reforms must, therefore, be designed and implemented in a manner that explicitly accounts for the poor.

Part One of the volume uses specific examples to explore Sen's two elements of reach. The chapters in this part establish two key points. First, reforms do indeed touch the lives of all people and do so in diverse and varied ways. This broad scope is patently obvious when the reform involves a major restructuring of society as has occurred in the transition economies and as illustrated in Chapter 1. This chapter, however, also reveals the many channels through which reform affects people's lives and in particular, the way in which human capital and demographic characteristics combine to influence outcomes. Furthermore, more specific reforms also have wide influence as the examples of trade liberalization (Chapter 2) and education (Chapter 3) reveal.

The chapters of Part One also reinforce Sen's concern with the poor in the context of reform. The poor may suffer disproportionately during systemic reform and may face barriers to their full participation in more specific reforms. Thus, during the course of major restructurings, societies may become more unequal (Chapter 1). Similarly, the major changes in relative prices and labor-market conditions which trade liberalization usually induces can have disproportionately negative effects on the well-being of the more vulnerable groups. The research findings presented in Chapter 2 suggest that this can create path-dependence to the extent that the harmful effects of trade liberalization can hinder the lower-income groups' ability to accumulate human capital. In other cases, poverty traps may prevent the poor from participating fully in programs designed to build human capital, thereby compromising their future prospects relative to those of richer members of society and limiting the success of reform (Chapter 3).

THE CASES

Sen uses relatively long periods of history, drawing on Chinese and Indian experiences to illustrate why it is important to be clear about the ethical foundations of reform. The point is simple: reforms inevitably have implications for many if not all members of society.

Inequality

In Chapter 1 István György Tóth continues in a similar vein, exploring the changes in inequality during the 'Great Transformation' in Hungary. He uses a decomposition analysis to examine the impact of three phases of transition (1987–92, 1992–96 and 1996–2001) on inequality. The analysis reveals that inequality increased especially during the first period; incomes became more dispersed at the top of the distribution mostly at the expense of a shrinking middle class and in contrast to a relatively stagnant position for the poorest. It also reveals the main factors influencing individual outcomes: labor market participation, location and human capital. Thus, a young individual with a higher education degree enjoyed many new opportunities in the labor market; but his older colleague, long-employed in one of the now-declining heavy industries, faced prolonged unemployment. Similarly, prospects for younger workers with low levels of education deteriorated. The chapter not only illustrates that reform affects all members of society, but also identifies the main channels, especially the important role of human capital, through which that effect is manifested.

Uncertainty

Chapter 2 introduces a factor which may have a significant influence on the reach of reform: uncertainty. The authors, Pierluigi Montalbano, Alessandro Federici, Carlo Pietrobelli and Umberto Triulzi focus on trade liberalization and underline that the economy has a very limited ability to cope with trade shocks, particularly ‘extreme’ shocks when financial markets are incomplete and institutions weak. Relying on an analysis of the experiences of Central and Eastern European countries with trade reform, the authors demonstrate that shocks arising from changes in the terms of trade and trade openness (proxied by their ‘extreme volatility’) reduce the resources which are available for private investment and consumption and disproportionately affect the poor. They argue that one important factor explaining this is the lack of appropriate policy tools to cope with or at least mitigate trade shocks and their repercussions on the domestic economy. The poor are particularly vulnerable, because they cannot access instruments to cope adequately with shocks. Vulnerability thus emerges as an important ingredient or dimension of Sen’s concept of reach.

Their analysis also illustrates the importance of interdependencies in the reform process and has the following implications for the range of policies, a topic discussed in more detail in Part Two. First, trade reforms should be accompanied by policies which can cope with or mitigate any resulting negative impacts. Second, the ‘coping mechanisms’ which are available to the population should be improved. In particular, explicit or implicit insurance should be considered an important form of pro-poor expenditure. Third, the institutions which govern globalization should consider the need to limit the size and frequency of macroeconomic shocks. In this regard, the authors call for a new ‘culture of prevention’ at the international level.

Poverty Trap

Chapter 3, by David Mayer-Foulkes, provides one of the few empirical demonstrations available in the literature of the existence of a poverty trap which limits the accumulation of human capital by the poor. It then shows that the consequent low level of human capital among the poor has diminished the success of Mexico’s reforms, including trade liberalization. The chapter demonstrates that increasing returns to education go untapped by many children in the population whose human capital decisions depend on their family situation and parental assets. As a result, the population classifies itself by educational status into two groups: one with completed lower secondary school or less; and one with 15 or more years of schooling. Since only the

latter group realizes the benefits of increasing returns, the evidence supports the existence of a poverty trap in Mexico. The bulk of the population is unable to invest enough in nutrition and early schooling to benefit from the higher returns to higher education. While Sen's emphasis on reach tells us that reforms must embrace all, especially the poor, Mayer-Foulkes shows that this has not happened in an important sphere of person-centered development in Mexico. Indeed, he argues that past reforms have not had the range (see also Part Two) necessary to achieve the desired level of reach and that future reforms, if they are to reach the lower-income groups, will probably have to rely on public funds to break the poverty trap.

In sum, the chapters in Part One show that when reforms are assessed using Sen's criteria of being person-centered and inclusive, both the details of the context and the interdependence associated with social change matter. Pervasive financial market failures and policy-induced worsening in income distribution and in macroeconomic volatility can severely affect the reach of reform. They can perpetuate rather than weaken poverty traps and social vulnerability. The same interdependencies also become important when considering the range of reforms, the second of his Three Rs.

RANGE: INSTITUTIONAL REFORM, POLICY CHANGE

Range refers to the ways and means which are used to implement reform. Sen's approach to this issue has two distinctive features. First, reform should not be means-centered. Rather, reformers must take into account the way in which policies influence the lives of the people involved. This implies that, as with ends, means must also be people-related and evenhanded. Second, means are complex. They typically involve policy bundles and a cluster of institutions. This is a direct consequence of the fact that social changes are diverse and interrelate with each other in many different ways. From these two features it follows that interdependency and details will play a critical role not only in the design and selection of the range of instruments but also in their implementation. The three chapters in Part Two discuss a number of issues which must be considered when deciding the appropriate range of policies and show how failure to do so can lead to problems during implementation which can be critical in determining whether or not the expected results materialize.

All three chapters illustrate the central point that the range of reform almost always involves a combination of policies to deal with the interdependencies. Each chapter, however, illustrates a different aspect of this basic point. Thus, the range of policies may have to be different depending on the groups whose behavior the policy is meant to influence. One illustration of this is provided in

Chapter 4, that shows that there must be an appropriate combination of policies in order to influence the behavior of foreign investors (the basic point) but that the package must be tailored to meet the needs of different agents (in this case investors from developed countries and investors from developing ones). The appropriate combination of policies will also depend on the presence or absence of other policies or institutions as shown in Chapter 5. Also dealing with foreign direct investment, it illustrates the way in which trade agreements can offset the absence of secure property rights. The final chapter in this part illustrates how the interdependence between two different social spheres has important implications for the range of reform. In this case, the interaction between the social spheres of work and education jointly determines the outcome of reform designed to increase the participation of children in school: reforms are required in both spheres.

Foreign Investment

In Chapter 4, Rashmi Banga analyzes the range of policies that host governments in Asia are adopting to attract investors, as well as the role of regional investment agreements. The chapter addresses first the question of the effectiveness of selective government policies and investment agreements in attracting FDI into developing countries of Asia. It then explores whether investors from developed countries and developing ones respond similarly to the host governments' policies. Drawing on data on FDI inflows into 15 developing countries of Asia for between 1980–81 and 1999–2000, separate analyses are undertaken for FDI from developed countries and from developing ones.

The results highlight the importance of ensuring the mutual consistency of the policies implemented and of considering agents' diversity in order to ensure successful implementation. With regard to policy consistency, the authors show that to attract foreign investors, initiatives which improve economic fundamentals must be complemented with those which facilitate the operations of foreign firms. And with regard to the tailoring of policies to take into account investors' heterogeneity, the study finds that policies with respect to cost factors, e.g., lower tariff rates, tax concessions and tax holidays play an important role in attracting FDI from the developing countries, but these same policies may not attract FDI from developed ones. What matters more to FDI coming from developed countries are the policies which facilitate the business of foreign firms in the host country.

Trade Agreements

Lorenza Martínez Trigueros and Roberto Romero Hidalgo investigate how the appropriate range of policy has to be adjusted to fit the presence or absence of key institutions. In Chapter 5 they tackle this issue in the specific context of the interactions between secure property rights and investment, investigating the hypothesis that, beyond the effects on trade, the signing of a multilateral trade agreement can enhance FDI when property rights are not adequately protected. The study examines treaties which include the option of going through an international panel to resolve disputes under the hypothesis that this provides protection which might otherwise be missing or inadequate. After analyzing a 38-country panel, the authors conclude that signing a treaty has a positive overall effect on FDI flows and that the effect is greater in countries with weak property rights. The authors show how this has unfolded in the specific case of NAFTA, where the study finds that foreign investors make considerable use of the mechanism for dispute resolution and frequently win. They also note the possibility of positive spillover effects on domestic institutions.

Multiple Interventions

In Chapter 6 Admassie and Bedi argue that more than one intervention in different social spheres may be required to realize a particular goal. In their case, the goal is to encourage school participation by children, but the authors show that an exclusive focus on reforms relating to school cost and quality, the obvious and most direct points of intervention, may not be sufficient for the task at hand. They identify other policies, especially agricultural modernization, which exert an indirect effect on school participation by influencing the returns to child labor.

Using household data from Ethiopia, Admassie and Bedi provide fascinating insight into the beneficial and the harmful effects of child labor in the field and in the home. They show that beyond a certain threshold, 16 to 22 hours a week, child participation in the labor force, especially for herding, reduces school participation. They note that 60 per cent of the children in their sample work more than 16 hours a week. Policy changes with respect to school cost and quality do indeed affect school participation but do not influence child participation in the labor force. Other policies, however, particularly different types of agricultural modernization and the availability of agricultural machinery, do reduce the use of child labor. The authors conclude that efforts to improve educational outcomes must embrace not only educational reforms but also the effect of agricultural modernization, since the latter exerts a powerful influence on child labor force participation.

This chapter also illustrates a point to be developed further in Part Three. Sen emphasized the importance of reason, the need to constantly analyze and thoroughly assess what is being done. The Ethiopian example demonstrates this point. Admassie and Bedi show that a superficial examination of school participation and child labor suggests no trade-off. A more thorough analysis which specifically incorporates a non-linear relationship, however, demonstrates the presence of a trade-off after a certain threshold of hours worked. Had the analysis not been so thorough, this point would not have emerged and the negative consequence of labor force participation beyond the threshold on 60 per cent of Ethiopian children would have been missed. The importance of questioning the reason for reform systematically, as this example reveals, is examined further in Part Three.

REASON: STRATEGIES, NOT SLOGANS

Reason is Sen's most important dimension of reform and justifiably so. It refers to the need to constantly analyze and assess what is being done and what needs to be done. This involves understanding the intended reach or aim of reform, and it involves evaluating the range of instruments and policies. This evaluation, nonetheless, is not a task which a reform team can do in isolation. Evaluation must be conceived of as a complex process of social learning and the process must consider political factors. Complexity, in turn, requires – as Sen puts it – detailed reasoning about policy packages rather than slogans. The chapters in the last part of the volume address these dimensions of reason.

The reason for reform can be considered in both an *ex-ante* and an *ex-post* sense. Research can play a key role in the design of reform programs in several ways. It can provide a theoretical rationale for reform. It can provide important factual information which grounds the reform in the realities of local circumstances. And it can offer more sophisticated empirical analysis to establish the likely impact of reform in a statistically rigorous manner. Arguably, reform has the most convincing reason for its implementation when all three – appropriate theory, local information and empirical analysis – are brought to bear on the issue and point to the same conclusion.

In principle, assessing the impact of a reform involves comparing the well-being of individuals or households following the reform with their well-being had the reform not been implemented. Since the latter circumstance is never observed, any attempt to justify the reform is fraught with difficulty. In the physical sciences researchers identify two randomly selected groups – the control group and the treatment group. The latter is exposed to the new medicine, or whatever the experiment involves, while the control group is not.

A comparison between the two groups after the treatment provides an estimate of the impact of the treatment, because all other factors which could possibly affect the outcome have been held constant through the random selection of the members of each group. Conducting such experiments in the social sciences is rarely possible for both practical and ethical reasons. Social scientists, therefore, are obliged to develop innovative ways to ‘construct’ a control group that hopefully matches the target group in all respects other than impact of the treatment or reform.

None of the chapters in Part Three deals with the ‘ex-ante’ concept of reason in a strict sense, since all of them examine reforms which have already been implemented. Nevertheless, Chapter 7 illustrates the combined use of appropriate theory, local knowledge and empirical analysis – the principle of triangulation – in the context of ongoing educational reform in Kenya. Chapter 8 focuses on the experience of transition economies and sheds light on key initial conditions and the quality of institutions which should have been at the forefront of reform design. The final two chapters demonstrate the use of control groups to assess the reason for reform ex post. Thus, Chapter 9 provides an excellent example of such an effort applied to the evaluation of reforms in the rehabilitation of rural roads in Peru and Chapter 10, in an original analysis of privatization in Egypt, constructs a control group of state-owned enterprises (SOEs) against which to assess the performance of privatized firms.

In Chapter 7, Bedi, Kimalu, Manda and Nafula explore the reasoning behind recent educational reforms in Kenya. The chapter illustrates well the three key ingredients of a thorough assessment of the reason for reform: it provides a theoretical framework for analyzing the issue, it is grounded in local knowledge and it conducts a careful empirical investigation. In particular, it shows that the use of cross-section data suggests that school costs, a key element of the reforms, do not play a large role in determining enrollment. Had the analysts stopped here, the policymaker would conclude that the reforms had been well designed and that there was indeed good reason to continue them. But the authors extend the analysis in two important respects.

First, they switch to panel data (or more accurately pseudo-panel data comprising repeated cross-section data) which enables them to control for unobserved fixed effects. This adjustment reveals that school costs are in fact a significant deterrent to enrollment. Second, they extend the analysis to look at the effect of school costs for five per capita expenditure groups. Now it is evident that school costs have no impact on the richest quintile but affect enrollment in the other quintiles and especially the poorest. On the basis of this evidence, the Kenyan educational authorities may well be persuaded to reconsider the level of school costs, especially for the poor, or else devise ways of offsetting their negative impact on the ability of the poor to enroll

their children in school. Education is one of the central elements of people-related reform but, to realize Sen's notion of reach, it also has to be inclusive. Extending the analysis to embrace the distributional effects of reform, as shown in this chapter, is essential for a thorough assessment of the reason for continuing a particular program or policy.

Looking at the outcome of reform in the transition economies, Popov (Chapter 8) calls attention to the fact that, following the collapse of the Berlin Wall in 1989 and the initiation of market reforms, economic performance in the post-communist states was disappointing. In Eastern Europe and the former Soviet Union output collapsed, inequality and the crime rate increased and life expectancy fell. He argues that it is not surprising that the question of the 'reason' to reform has been at center stage in the policy discussions in the post-reform period. His chapter tries to clarify why institutional and policy reforms in transition countries were unable to achieve their goals and provides a fresh perspective on the shock-versus-therapy dimension of the debate.

The chapter makes three contributions to the debate. First, differences in performance during the initial stage of transition (transformational recession) depend strongly on initial conditions – pre-transition levels of GDP per capita and distortions in industrial structure and external trade patterns. Second, the institutional capability of the state is a key determinant of post-reform performance. Market liberalization alone, when it is not complemented with strong institutions and macroeconomic stability, cannot ensure good performance. Hence, the evidence indicates that the conventional wisdom's emphasis on macroeconomic stability is justified, but its insistence on rapid liberalization is not. It follows that the debate about the speed of liberalization (shock therapy versus gradualism) was to a large extent misfocused, whereas the crucial importance of initial conditions and strong institutions for good performance was overlooked.

The third contribution relates to the interactions between institution building and the political regime. According to Popov's findings, institutional capability depends to a large extent on the combination of the rule of law and democracy. While the optimal combination is liberal democracy and firm rule of law, the illiberal democracies which appeared in a number of transition countries created an environment which was not conducive to building institutional capabilities and to enforcing government regulations. These conclusions are in line with Sen's view of the role of democracy in the process of reform. A multiparty democracy and a free press are central to guaranteeing transparency and public scrutiny. In this sense, democracy and political participation have become instrumental to the process of social learning, a process which is essential for the proper assessment of the reasons and outcomes of reform and, therefore, for ensuring that policymakers take into account the provisions that reforms

must be people-related and evenhanded. That said, the chapter shows that democratization without a strong rule of law more often than not undermines institutions and contributes to disorder and poor economic performance.

Chapter 9, by Javier Escobal and Carmen Ponce, addresses directly the difficult question of ‘constructing’ a control group as a means of isolating the impact of a public intervention from other factors. This is a key instrument for analyzing the ‘reason’ for a particular intervention. Such careful evaluation can also be used to broadcast the benefits of particular programs to garner public support. Escobal and Ponce examine the benefits of a reform program intended to rehabilitate motorized and non-motorized rural roads in Peru. They use a technique known as propensity score matching in order to construct an appropriate control group of households.

The main result is that the rehabilitation of motorized roads increases household income but not consumption, because the increased income is invested in livestock. The results are smaller and not statistically significant for the rehabilitation of non-motorized roads. For those living near motorized roads, there was an increase in non-agricultural and agricultural wage income whereas the increase in non-agricultural wage income for those living by non-motorized roads was offset by a decline in non-agricultural self-employment (handicrafts, commerce). The difference may reflect the greater ownership of assets (education, land, public services) of households living near motorized roads. The chapter demonstrates how this approach to questioning the reason for a reform program can lead to clear signals for at least some redesign. While the analysis provides strong evidence that the rehabilitation of rural roads improves the welfare of the beneficiary population, the authors argue that the tendency of households living by motorized roads to increase savings rather than consumption suggests that they view the benefits as temporary. This is an implicit message to the authorities to provide adequate assurance that the roads will be maintained and to act on this. And the fact that households near non-motorized roads did not benefit to the same degree points to the need for complementary investments in education and other forms of public infrastructure. As always, the range of reforms plays a critical role.

Omran, in Chapter 10, also constructs a ‘control’ group to use in his assessment of privatization outcomes in Egypt. Unlike many studies which do not directly test the performance of privatized firms relative to SOEs, he compares the performance of Egyptian privatized and non-privatized firms using industry and firm size as the criteria to construct the two groups. The study examines the performance of 54 newly privatized Egyptian firms against a matching number of SOEs during the period 1994–98. The results of the test do not show a significant improvement in the performance of privatized firms relative to SOEs but rather an improvement in *both* the privatized firms and

SOEs relative to previous performance. The failure to detect an improvement in the privatized firms relative to the SOEs in the Egyptian case does not lead the author to conclude that policymakers should abandon privatization as a vehicle for economic development. Instead, Omran argues that the overall improvement in performance of both privatized firms and SOEs following privatization, appropriately managed, can increase competition and motivate private and public firms alike to better face future changes in the economic system. The study also suggests that interdependence matters to successful divestiture: A number of dimensions must be considered and reformers might need to shift their thinking away from an exclusive focus on ownership to consider the effects of market structure or the power of competition as well.

REFORM AND THE THREE Rs

The varied reform experiences analyzed in this volume constitute a representative sample of the complex problems that policymakers face on the ‘battlefield’ of reform in developing countries. One particularly important point to emerge is that the outcomes of reforms concerning reach and range can differ substantially from what countries expect because of the influence of initial conditions, idiosyncratic path-dependence effects, the institutional setting and political economy factors. Hence, if we take into account Sen’s emphasis on the importance of details and interdependence, we should not be surprised by the frequently observed fact that similar reform initiatives taken in disparate contexts lead to widely different outcomes.

Indeed, this conclusion is in line with the research findings of a related project of the Global Development Network centered on ‘Understanding Reform’ (Fanelli and McMahon 2005). The main goal of this project is to improve our understanding of the market reforms undertaken by developing and transition countries in the last quarter century. Although the project focused on the market reform process as a whole rather than on specific reforms – as the cases analyzed in this volume mainly do – the conclusions are similar regarding the relevance of the details and the interdependencies associated with the national context, the institutional setting and the political economy. It is worth taking a brief look at such conclusions. To the extent that they refer to the process of market reform as a whole, they will help complement our concluding thoughts on the Three Rs, as well as situate them within a more comprehensive framework.

According to the Understanding Reform Project, the most relevant factors associated with the ability to undertake, sustain and achieve the reform goals have to do with:

1. The ability to deal with the uncertainty concerning policy outcomes. This means that the implementation stage is crucial. Typically important are macroeconomic disequilibria, political unrest and 'technical' problems such as bad sequencing, wrong speed, lobbying at the implementation stage or the lack of an efficient bureaucracy.
2. The intensity of distributional conflicts and social cleavages. Reforms have consequences for the distribution of wealth and political power; hence social, ethnic, regional and cultural cleavages matter in different ways in different contexts.
3. The quality of the state and the institutional setting. Successful states show greater ability to react rapidly and correctly to shocks, to make transfers so as to manage distributional conflicts, and to design and enforce the rules of the game. Unsatisfactory reforms frequently relate to phenomena such as state capture, patrimonialism, and poor regulatory frameworks.
4. The quality of the political system and civil society. This impinges on the ability to solve collective action problems and distributional conflicts, to build institutions, to foster collective learning and to undertake political transactions to insure the legitimacy of reforms.

When viewed in light of Sen's Three Rs, these conclusions have important implications. First, if details are essential, the blueprints for specific reforms cannot be mass-produced. The reach and the range of reforms must be carefully tailored to take into account initial conditions, the characteristics of the institutional setting and stakeholders and the constraints posed by political economy issues. To be sure, this does not mean that the design of reforms can overlook the 'sound' principles of economics and political science. It does, however, suggest that reforms should be context-informed in an essential way.

Second, if social and institutional changes are inherent to reforms and this creates interdependencies, the approach to reform must necessarily be interdisciplinary. From this point of view, the stylized answers about the crucial points of reforms given by economists, political scientists and institutional experts mentioned at the beginning of this introduction are all relevant. But this naturally raises the question of how to integrate these different approaches productively to design, implement and reform the reforms. Some of the most brilliant social scientists have closely scrutinized and analyzed the processes of reforms implemented during the last decades, and our knowledge has substantially improved as a result. We have new analytical tools and a number of context-informed stylized facts about reforms. However, a good part of this knowledge has been produced within the narrow boundaries of each discipline without much cross-fertilization. As a consequence, we still lack a unified view

of the social change process. This suggests that investing in multidisciplinary cross-fertilization could pay off well in terms of improving our understanding of reform; reform which should be conceived of as a process of social change in which institutional, political and economic factors interact in complex and sometimes surprising ways.

Third, if reform outcomes can substantially differ from expectations concerning reach and range, it is crucial that we are prepared to 'reform the reforms'. This raises two further questions: How does society learn from experience and manage to put the lessons into practice? What should the criteria for reform of the reforms be?

Although the first question obviously seems urgent, there is scant literature which tackles the issue of how society 'learns'. The papers which analyze reform processes (including the ones in this volume) are full of sensible lessons, and there has been a remarkable analytical effort to model new phenomena, such as those associated with the political economy of reforms. Indeed, given that many countries have made highly visible design and implementation mistakes, one could argue that reformers could even learn from other countries' errors at no cost. However, more often than not, this has not been the case. Many countries have repeated the same mistakes. Hence, it seems that more research is needed on the mechanisms of social learning and, more specifically, on the way in which social consensus on values and norms is built and on the manner by which institutions and organizations of state 'learn'. Since civil society and state organizations do not read papers on reforms, we can hypothesize that learning will take the shape of transformations in social practices and values; changes in the rules of the game and governance structures; and in the allocation of society's resources to improve the functioning of institutions (understood as both players and the rules of the game).

Sen's approach is clear concerning the second question. The reform of reforms should be inherent to the process, because policymakers should constantly scrutinize the reasons for reform in light of the results concerning reach and range. We can take it for granted that technical economic questions – such as whether the reform process is macro-economically sustainable – as well as specific institutional or political issues – such as whether property rights and contracts are firmly enforced – will be part and parcel of the evaluation of the reason dimension. However, in Sen's view all these questions would be instrumental, rather than constitutive. The key question concerning reason is whether reforms are inclusive and person-related. This implies that to assess the reason to reform, policymakers must take into account a number of social facets, especially the consequences of reforms for those individuals that are at the 'bottom of the pyramid'. In this way, while Sen's Three Rs do not deny

the importance of technical considerations, evenhandedness and person-relatedness naturally become organizing principles to reform the reforms.

The Three Rs approach to reforms is, of course, very demanding from the analytical point of view. The analysis of the reason dimension naturally calls for an interdisciplinary approach to the extent that evenhandedness and person-relatedness require an analysis which integrates the technical aspects associated with economics and institutions with the study of the effects in several 'domains' of the economy, society and polity. We may have a long way to go before we can confidently articulate reform technologies which do justice to the richness of Sen's approach. We believe, however, that the chapters in this volume have demonstrated convincingly that researchers and policymakers alike have nothing to gain by shirking this task, no matter how demanding.

BIBLIOGRAPHY

- Fanelli, José M. and McMahon, Gary (eds) (2005), *Understanding Market Reforms*, New York: Palgrave Macmillan.
- Sen, Amartya (1999), *Development as Freedom*, New York: Oxford University Press.
- Stern, Nicholas, Jean-Jacques Dethier and F. Halsey Rogers (eds) (2005), *Making Development Happen*, Cambridge, MA: MIT Press.