

Public Policy Management:

W7. Institutional Foundations of Public Policy

Geetha Rani Prakasam,
ICCR Chair Professor,
DBS, UNITECH, Lae, PNG.

Sl. No	Main Topics	Key words
1	Introduction to Public Policy	Public policy, goals, decisions
2	Fundamental theories in public policy	Theories, Concepts, framework, model
3	The Policymaking Process	policy process, policy cycle
4	Policy Formulation	brainstorming, lobbying
5	Paradoxes, Dilemmas, and Path-Dependence	coalition, advocacy
6	Policy Planning Process	design, structure
7	Institutional Foundations of Public policy	systems required, systems in place

Outline of W7

- Part I and Part II
- Part 1 covers the following:
 - Major Institutions, country examples
 - Significance of Institutions
 - What determines the ability of different polities to undertake the task of producing effective public policies?
 - Political and Economic Institutions
 - Why public policies in Argentina tend to be so dysfunctional?
 - Understanding Institutional Strength: stability, adaptability, coherence and coordination, the quality of implementation and enforcement; public regard and efficiency
 - Characteristics of Political Party Systems
 - Electoral Rules, Party System Fragmentation, & the Partisan Powers of Presidents, etc

Outline of W7

- Part 2 covers the following:
- Comparative Perspectives
- Importance of institutions in the development process
- Political, Economic, Social institutions
- Precolonial institutions – the path dependence
- Post colonial quality of institutions
- Ray of Hope in improving the quality of institutions

Major institutions: courts, bureaucracy, Senate, national media

- Studying political and governmental institutions (president, Congress, courts, etc.) in order to understand the policies that all those institutions have produced.
- Courts: (i) Make decisions that force action by other branches: school desegregation, abortion and (ii) Change the political agenda
- Bureaucracy: (i) Source of political innovation: size and expertise; (ii) Thinks up problems to solve and (iii) Forms alliances with senators and their staffs
- Senate: (i) Once a slow moving, status quo club; (ii) Influx of liberal activist Senators in the 1960s; (iii) Now—contrary to the intent of the Framers—a major source of change
- Media: (i) Help place issues on political agenda and (ii) Publicize those issues raised by others, such as safety standards proposed by Senate

Other Relevant Institutions

- Action by the states
 - a) Sometimes laws are pioneered in states
 - b) State attorneys general can file suits against businesses that result in settlements binding throughout the country
- Evolution of political agenda
 - a) Changes in popular attitudes that result in gradual revision of the agenda
 - b) Critical events, spurring rapid changes in attitudes
 - c) Elite attitudes and government actions, occasioning volatile and interdependent change

Institutional Foundations: Country Example

- Institutional foundations differ across countries.
- Parliament is the supreme legislative body of India.
- The Indian Parliament comprises of the President and the two Houses - Rajya Sabha (Council of States) and Lok Sabha (House of the People).
- The President has the power to summon and prorogue either House of Parliament or to dissolve Lok Sabha.
- The Constitution of India came into force on January 26, 1950.
- The first general elections under the new Constitution were held during the year 1951-52 and the first elected Parliament came into existence in April, 1952.

Institutional Foundations: Country Example

- President of India. Under the Constitution, of the Republic of India, the President replaced the Monarch as ceremonial head of state. The President is elected by the Electoral College for a five-year term. In the event of a vacancy the Vice-President serves as Acting President.. Status Denotes Vice-President acting as President.
- President
- Vice President
- Prime Minister
- Council of Ministers
- Governors
- Lt. Governors and administrators

Institutional Foundations: Country Example

- Chief Ministers
- Judges of Supreme Courts
- Chiefs of Armed Forces
- Members of Parliament
- MLAs / MLCs
- India - characterize the eleven institutions, or institutional clusters
- The Presidency; Parliament; The Supreme Court; Central Bank (Reserve Bank of India); India's Institutions of Public Expenditure Governance; New Regulatory Institutions in Infrastructure; Institutions of Internal Accountability; Financial Accountability in Governance:-Comptroller and Auditor General of India; The Civil Service; Election Commission of India; local governments (LGs)

Civil Servants

- Under the Indian Constitution, the higher civil servants or top echelons of bureaucracy have a Constitutional responsibility to advise on policy options.
- The secretaries to the Government of India, for example, advise the ministers to take decisions that arise within the framework of the existing laws or policy, which otherwise cannot be dealt with by routine procedures.
- Such decisions clarify the scope of a policy and finalize its application in new and special situations.
- Further, they are extensively involved in preparing explanatory material for ministerial use on the operation of existing policies.
- Thus, higher civil servants, particularly the secretaries to the Government of India and the state government play more than an advisory role in the public policy formulation process.

The significance of Institutions

- At the analytical level, some Economists and Political Scientists call for an end to the business of producing universal policy recipes.
- But the political economy of formulating and implementing the policies was basically about finding a way to implement these reforms in political systems stacked with stubborn entrenched special interests that had resisted those policies thus far.
- Once that magical moment of reform was over, the policy makers, political scientists, economists, etc. could just sit back, relax, and enjoy watching the countries embark on a healthy development path.
- But that has been found to be rare across country contexts, more so among the developing countries.

What determines the ability of different polities to undertake the task of producing effective public policies?

- Policymaking is a continuous and ongoing process. Aspects of that very process affect the economic and social impact of the policies themselves.
- Credibility is part of a set of policy characteristics that influence their effect on development outcomes.
- These characteristics, in turn, are derived from the process by which policies are discussed, decided, implemented, evaluated, and modified.
- Public policies are more than their titles and that what really matters for policies to induce good performance and outcomes are **some fundamental state capabilities**, such as the ability to commit to not expropriating, or the ability to enforce compliance.

Policy Framework draws on both economics & political science

- This framework predicts that the extent to which some desirable policy characteristics (such as stability, adaptability, consistency, and public regard) obtain depends on the behavior of political actors in the policymaking process.
- Players in this game include official state actors and professional politicians (for instance, presidents, party leaders, legislators, judges, governors, and bureaucrats), as well as business groups, unions, the media, and other members of civil society.
- The policymaking process is viewed as a series of bargains and exchanges among these actors, whose behavior depends on their interests, incentives, and constraints and on their expectations about the behavior of other actors.
- These interactive patterns of behavior constitute equilibria of the policymaking game. These behaviors and equilibria, in turn, are conditioned by the rules of the policymaking process.

Political and Economic Institutions

- These rules relate to the workings of political institutions such as the legislature, executive-legislative relations, the political party system, the judiciary, and public administration.
- Good institutions (including property rights, equal opportunity for a broad cross-section of the population, rule of law, and constraints on politicians) is crucial for economic development.
- These good institutions, in turn, are derived from geographical, productive, and population-settlement conditions at the time of colonization, and they seem to persist over time.
- Illuminating as those lines of research are, they leave many questions unanswered.
- Effect of institutions, especially political institutions, on the qualities of public policies but the relevant observation period is years or decades, as opposed to centuries.
- In a sense, this represents an intermediate view with respect to the issue of the endogeneity or exogeneity of institutions.

Political and Economic Institutions

- Institutions are clearly endogenous to past arrangements and events and, to some extent, to more recent configurations of political power, socioeconomic structures, and other deep determinants.
- Yet, it is important to understand the impact of particular configurations of political institutions on policymaking processes and thus on policies.
- Understanding those constraints is crucial for the development of policy proposals that are attuned to the institutional realities of each country. At the same time, political institutions are being debated and even reformed in country after country, and these debates are not just smoke screens for blunt exercises of power.
- Rather, they are informed by discussions on the possible effects of reform on political practices and outcomes. By taking a middle path, aiming to increase the awareness of the importance of political practices and institutions in the policymaking process, without falling into a totally deterministic mode in which everything that happens is determined by forces absolutely beyond the control of contemporary actors.

Political and Economic Institutions

- A lot of work in political science and political economy links political institutions with political and economic outcomes.
- To adjust policy recipes to institutional capabilities or even to think about reforms of political institutions that might improve policymaking processes, one needs a country-based approach conveying detailed knowledge of the institutional context and historical background, which facilitates an understanding of the interactions among factors that affect policymakers' incentives.
- Regularities emerging from abstract modeling of political institutions and cross-country empirical analysis are a very important input in this quest, but they need to be complemented by details of the interactions at play in each polity.
- The goal is to look for principles of good policymaking processes and then understand how the details of each country's polity facilitate or impede the operation of such principles. One such principle is political cooperation.

Ability of political actors in consensus building

- Important features of public policies depend on the ability of political actors to reach and enforce intertemporal agreements: that is, to cooperate. In political environments that facilitate such agreements, public policies tend to be higher in quality, less sensitive to political shocks, and more adaptable to changing economic and social conditions.
- In settings that hinder cooperation, policies are either too unstable (subject to political swings) or too inflexible (unable to adapt to socioeconomic shocks). They tend to be poorly coordinated, and investments in state capabilities tend to be lower.
- Under what conditions is cooperation more likely?

Ability of political actors in consensus building

- The theory of repeated games suggests that cooperative outcomes are more likely if there are good aggregation technologies, so that the number of actors with direct impact on the policymaking game is relatively small; if the arenas for political exchange are well institutionalized; if key actors have long time horizons; and if there are good enforcement technologies (such as the presence of impartial and effective arbiters and the possibility of effective delegation of the implementation of agreements).
- Verifying whether such conditions are present in practice requires substantial empirical knowledge about the workings of policymaking and political institutions. These conditions are associated with some incentives and characteristics of key players and arenas such as congress, the party system, the judiciary, and the bureaucracy.
- This approach is heavily demanding in terms of identifying the details of institutions and policymaking in each country. The first phases in the agenda have therefore focused on detailed country studies.

Why public policies in Argentina tend to be so dysfunctional?

- Why public policies in Argentina tend to be so dysfunctional, especially in comparison with the country's level of human development.
- We concluded that the workings of political institutions in Argentina were contrary to the requirements for effective policymaking.
- There does not seem to be a magic bullet in terms of political reforms that will produce good policymaking under all circumstances.
- Understanding the overall workings of the political and policymaking processes in each country, with their specific historical trajectories, is a crucial prerequisite for developing appropriate reform proposals, not only in terms of policies, but also in terms of political institutions.

Public policy features: Proxy for Institutional Strength

- The public policy features we examine include the following:
- stability (the extent to which policies are stable over time);
- adaptability (the extent to which they can be adjusted when they fail or when circumstances change);
- coherence and coordination (the degree to which policies are consistent with related policies and result from well-coordinated actions among the actors who participate in their design and implementation);
- the quality of implementation and enforcement; public regard (the degree to which policies pursue the public interest); and
- efficiency (the extent to which they reflect on allocation of scarce resources that ensures high returns).

Adaptability

- Countries need to be able to adapt policies to changing conditions and to change policies when they are obviously failing.
- Political circumstances, however, might prevent such changes from happening, for instance, in the case of opposition from entrenched veto players or rigidities that were built into the policy mechanisms to prevent political opportunism.
- Countries with low policy adaptability will be unable to respond to shocks adequately, and they may get stuck in bad policies for extended periods.
- **The notion of policy stability is closely linked to the notion of policy credibility.**

Coordination and coherence

- Third measure—namely, coordination and coherence—takes into account the fact that public policies are the outcome of actions taken by multiple actors in the policymaking process.
- Ideally, different agents acting over the same policy domain should coordinate their actions to produce coherent policies.
- This is not always the case, however. Policymaking often involves a large number of agencies and layers of government that do not communicate or cooperate adequately with one another.
- Lack of coordination often reflects the uncooperative nature of political interactions.

Quality of policy implementation and enforcement

- A policy could be very well designed, sail through the approval process unchanged, and yet be completely ineffective if it is not well implemented and enforced.
- Our fourth indicator thus measures the quality of policy implementation and enforcement which is quite poor in many countries in Latin America.

Public regard

- Fifth indicator, public regard, was first suggested by Cox and McCubbins.
- It refers to the extent to which policies produced by a given system promote the general welfare and resemble public goods (that is, they take public well-being into account) or, alternatively, funnel private benefits to certain individuals, factions, or regions in the form of projects with concentrated benefits, subsidies, or tax loopholes.
- Budget Allocation and Spending
- Finally, a key aspect of good policymaking is the state's ability to allocate its scarce resources to those activities in which they have the greatest returns.
- Our index of efficiency has two components: whether the composition of public spending is wasteful, and whether resources are targeted where they will be most effective.

The Policymaking Capabilities of Congress

- National legislatures are the most natural arena for discussing, negotiating, and enforcing political agreements. Since they include broader representation than the executive, they might serve as an arena for forging intertemporal political agreements among broader societal interests.
- A legislature made up of professional legislators, with technical capabilities for discussing and overseeing policies and with adequate organizational structures, could facilitate the development of relatively consensual and consistent (stable) policies over time.

Characteristics of Political Party Systems

- Parties are organizations whose function is to represent and aggregate diverse interests. As such, they are naturally encompassing organizations that may facilitate political bargains in the policymaking process.
- Here, we focus on characteristics of parties and party systems that make parties more encompassing policy players, and it explores the effects of these characteristics on the quality of public policies.
- One important characteristic is their **degree of institutionalization**.
- More institutionalized parties and party systems are more likely to encourage long horizons and to prevent individual politicians from behaving opportunistically, particularly when parties are programmatic.

Characteristics of Political Party Systems

- They can also facilitate intertemporal bargains, both within a party and between parties, since the commitments made by current party leaders are more likely to be respected in the future.
- Another characteristic that might facilitate encompassing parties is their relative focus on national issues, as indicated by measures of party system nationalization.
- How effectively parties play their roles in the policymaking process also depends on the main incentives and orientations of key party actors.
- In well-institutionalized party systems, parties are likely to have longer horizons and more encompassing interests than individual citizens or individual politicians.
- Parties are collective entities, with an interest in maintaining or enhancing their reputation over time.

Party system institutionalization & programmatic orientation

- Well-functioning parties are likely to be able to control the free-rider incentives of individual politicians to engage in activities that give them short-term benefits.
- Long-lasting, well institutionalized parties could be consistent long-term policy players and contribute to generating intertemporal cooperation.
- A relatively small number of parties that are expected to be around for a long time, alternating in government, are likely to respect some basic rules of interaction and to establish somewhat consensual sustained policy stances on crucial issues.

Party system institutionalization & programmatic orientation

- Interactions among institutionalized parties with a focus on national policymaking can also add credibility and predictability to the policymaking system, complementing or even substituting for well institutionalized legislative bargaining arenas.
- The institutionalization of the party system is therefore expected to have positive effects on key features of policies, such as stability.
- Policies are better only when party systems are both institutionalized and programmatic.

Implementation and Enforcement

- Policies with good properties are most likely to emerge in cooperative policymaking environments. Adequate enforcement and implementation facilitate such cooperation and thus strengthen the quality of policies. The judiciary is the most obvious enforcer in the political system.
- The bureaucracy plays a predominant role in policy implementation, so its characteristics and capabilities are likely to have an effect on the quality of implementation.
- The quality of the bureaucracy can also affect the ability of other political actors to bargain and enforce intertemporal policy agreements. In fact, delegation to a competent bureaucracy might in some cases be the way to enforce the intertemporal implementation of political agreements.
- Ministers and, more broadly, cabinets, also play a key role in the design, discussion, and implementation of public policies in Latin America. The discussion that follows explores how characteristics of the judiciary, the cabinet, and the bureaucracy affect the properties of public policies.

The judiciary

- Of all the roles that the judiciary plays in the polity, one is especially important for our framework: the intertemporal enforcement of prior political and policy decisions, as reflected in constitutions and laws.
- A judiciary that plays this role effectively will improve some properties of public policies, such as stability and the quality of enforcement.
- The supreme court or equivalent institution is usually in charge of ensuring that the president does not overstep congress and that neither branch violates the constitution.
- The judiciary will not be able to perform this role adequately if it is not independent of the executive in power.

The judiciary

- Building an independent judiciary is a complex business, which usually takes a long time.
- Clearly, a supreme court whose members change too often is unlikely to establish much independence. Since the president nominates justices in most countries, a short tenure would imply that most of the country's supreme court justices had been nominated by the sitting president.
- Individual justices who owe their position to the sitting president are less likely to show independence from the executive in their rulings.

The cabinet

- Cabinet ministers, in turn, play key roles in every stage of the policy process in Latin America. Characteristics related to the formation, operation, stability, and structure of cabinets are likely to have important effects on the properties of public policies.
- For instance, a certain degree of cabinet stability is likely to be necessary to promote long-term policies and to allow ministers to see programs and policy implementation through to completion.
- Frequent turnover of cabinet ministries is likely to promote a short-term orientation to policy and frequent policy switches. Long tenures are also conducive to improving relationships with permanent bureaucrats, which are essential for implementing policy efficiently.

The cabinet

- Frequent changes in the cabinet can leave leadership vacuums that may contribute to bureaucratic inertia and even corruption. Long tenure allows ministers to accumulate valuable expertise specific to the policy area in which they work and to develop political and managerial skills that should improve the quality of their performance in their different policymaking functions.
- Of the many characteristics of cabinets that might affect the features of policies, we focus on two that are particularly consistent with our emphasis on long horizons and institutionalization: the stability and durability of ministers (the inverse of the number of ministers per portfolio in each administration) and the fraction of the cabinet and the top political appointees that come from a civil service career (an indicator of institutionalization).

The bureaucracy

- Finally, a strong and capable bureaucracy is likely to improve the quality of public policy implementation. It also has positive feedback effects on other stages of the policy process.
- Having a competent and independent bureaucracy to which some policy decision making and implementation may be delegated might facilitate intertemporal agreements, particularly in policy areas that are prone to politicization and political opportunism.
- When there is a choice between rules and discretion, and if discretion may lead to political opportunism, delegation to a technically competent bureaucracy can facilitate adaptability while keeping political opportunism at bay.
- Conversely, policies are more likely to deviate from the public interest in the absence of a competent bureaucracy. For instance, businesses affected by economic regulation or taxation are likely to focus their efforts on evading regulation or taxation at the implementation stage.

Electoral Rules, Party System Fragmentation, and the Partisan Powers of Presidents

- Several characteristics of presidential democracies have received considerable attention because of their potential impact on governability (and thus policymaking).
- the degree of proportionality of representation induced by electoral rules.
- More proportional electoral rules are expected to lead to better representation, but lower policy effectiveness. They are also associated with more fragmented party systems and with presidents that have lower partisan powers.
- Traditional measures of these concepts, the proportionality of the electoral system, the effective number of legislative parties, and the presidential party's lower or single chamber contingent) and their correlation with policy characteristics.

Electoral Rules, Party System Fragmentation, & the Partisan Powers of Presidents

- None of these measures seems to correlate significantly with this study's measures of policy effectiveness. This suggests that it is difficult to generalize about the direct effects of institutional rules and political configurations on the nature of policymaking and the characteristics of policies.
- Several of the institutional variables under analysis, such as having an independent supreme court or a strong congress that is heavily involved in policymaking, reflect the equilibrium behavior of a number of relevant political actors.
- A supreme court is only able to maintain or develop its independence over time if it is in the best interest of other relevant actors (such as the president) not to tinker with the supreme court in pursuit of short-term political benefits.
- Strong congresses and independent judiciaries are not built overnight, but are the outcome of processes of investing in the quality and credibility of such institutions.

Part II: Comparative Perspectives

- Importance of Institutional strength in making, reforming and implementing public policies for the development process.
- Institutions both formal and informal are historically evolved over centuries
- Country's political, economic and social institutions play a larger role in not only successful formulation of policies but also their effective implementation.

Efficacy of Domestic Institutions

- Another difference between most developing countries and most developed countries at the time of their early stages of economic development lies in the efficacy of domestic economic, political, and social institutions.
- By the time of their early industrialization, many developed countries, notably the United Kingdom, the United States, and Canada, had economic rules in place that provided relatively broad access to opportunity for individuals with entrepreneurial drive.
- High inequality and poor institutions facilitating extraction rather than providing incentives for productivity were often established by colonial powers. Today such extraction may be carried out by powerful local interests as well as foreign ones.
- But it is very difficult to change institutions rapidly. As Douglass North stresses, even if the formal rules “may be changed overnight, the informal rules usually change only ever so gradually.” We will return to the question of economic institutions later in this lecture.

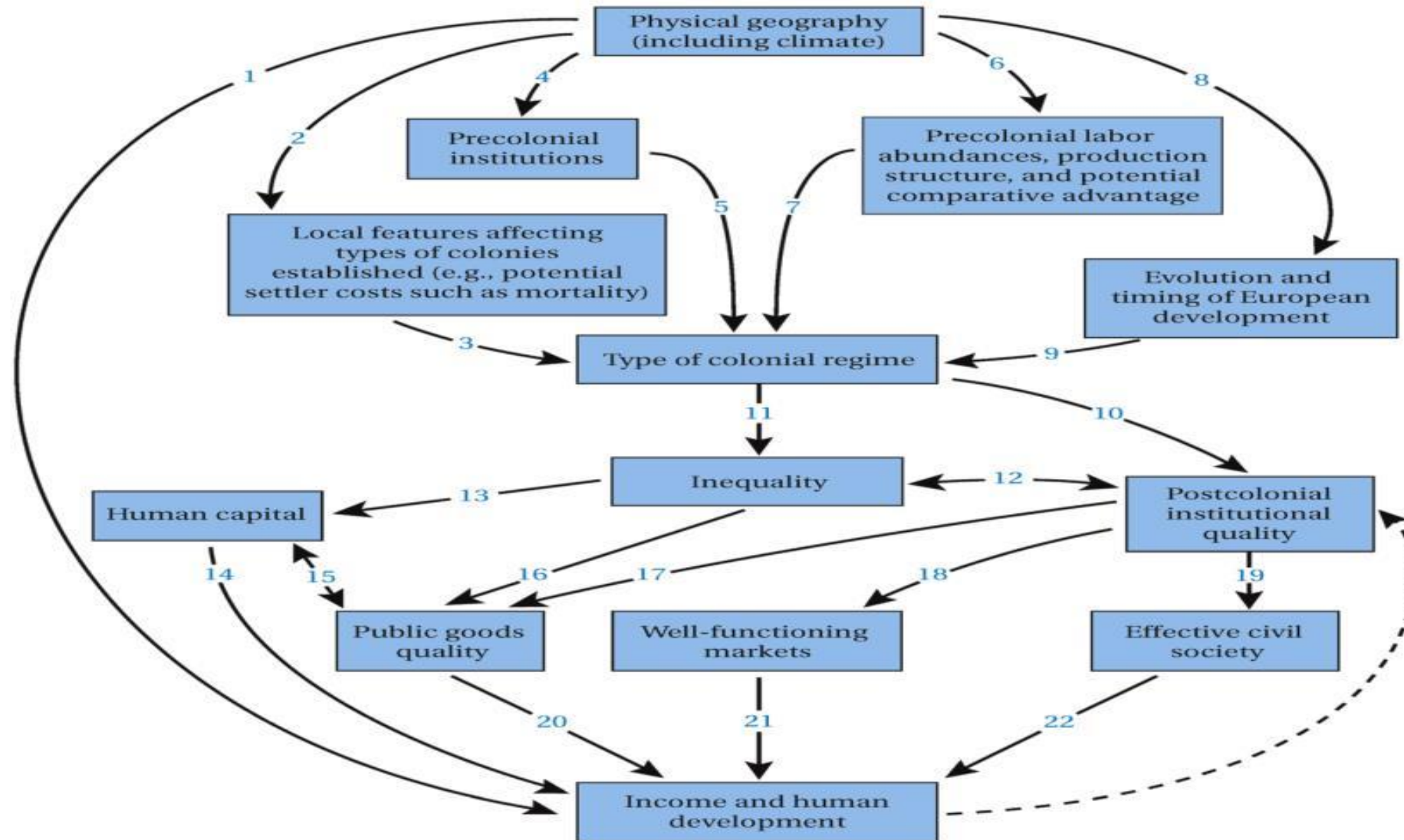
Efficacy of Domestic Institutions

- The developed countries also typically enjoyed relatively stronger political stability and more flexible social institutions with broader access to mobility.
- States typically emerged more organically over a longer period of time in the developed regions, and consolidation as nation-states generally occurred before the industrial era.
- In contrast, particularly in Africa, national boundaries were more arbitrarily dictated by colonial powers. The “failed state,” and states in danger of becoming so, is a phenomenon of the postcolonial period, with roots in imperial and colonial practices.
- Although many developing nations have roots in ancient civilizations, a long hiatus often existed between autonomous regimes.

Economic institutions

- **Economic institutions**, which play an important role in comparative development, are defined by Nobel laureate Douglass North as the “rules of the game” of economic life.
- As such, institutions provide the underpinning of a market economy by establishing the rules of property rights and contract enforcement; improving coordination; restricting coercive, fraudulent, and anticompetitive behavior—providing access to opportunities for the broad population; constraining the power of elites; and managing conflict more generally.
- Moreover, institutions include social insurance (which also serves to legitimize market competition) and the provision of predictable macroeconomic stability.
- Countries with higher incomes can afford better institutions.

Figure 2.11: Schematic Representation of Leading Theories of Comparative Development



Comparative Perspectives

- As noted earlier, most developing countries were once colonies. Geography affected the types of colonies established (**Arrow 2**), with one of the now best known geographic features being settler mortality rates, whose impact was examined in work by Daron Acemoglu, Simon Johnson, and James Robinson.
- In this argument, when potential settlers faced higher mortality rates (or perhaps other high costs), they more often ruled at arm's length and avoided large, long-term settlement. Their interest could be summarized as “steal fast and get out” or “get locals to steal for you.”
- Unfavorable institutions were therefore established, favoring extraction over production incentives. But where mortality was low, populations were not dense, and exploitation of resources required substantial efforts by colonists, institutions broadly encouraging investments, notably constraints on executives and protection from expropriation, were established (sometimes as a result of agitation from settlers who had the bargaining power to demand better treatment).

Precolonial institutions

- The influence of geography on *precolonial institutions* is captured by **Arrow 4**. Precolonial institutions also mattered to the extent that they had influence on the *type of colonial regime* established. This possible effect is reflected by **Arrow 5**.
- *Precolonial comparative advantage* and evolving *labor abundances* in the Americas and its relation to the institutions established have been examined in the pioneering work of Stanley Engerman and Kenneth Sokoloff. When climate was suitable for a *production structure* featuring plantation agriculture (particularly sugarcane in the early history), slavery and other types of mass exploitation of indigenous labor were introduced.
- In other areas, when indigenous peoples survived contact in sufficient numbers and mineral wealth was available, vast land grants that included claims to labor were established (by Spain). Although resulting from different comparative advantage (sugarcane and minerals), economic and political inequality was and remained high in all of these economies (even among freemen), which had long-lasting negative effects on development.

Precolonial institutions

- These effects are reflected by **Arrow 3**. Acemoglu and colleagues present evidence that after accounting for institutional differences, geographic variables (e.g., closeness to the equator) have little influence on incomes today. Their statistical estimates imply large effects of institutions on per capita income
- These links are reflected by **Arrow 6** and **Arrow 7**. Early inequities were perpetuated with limits on the nonelite population's access to land, education, finance, property protection, and voting rights, as well as labor markets.
- This inhibited opportunities to take advantage of industrialization when they emerged in the nineteenth century, a period when broad participation in commercial activity had high social returns.
- The contrast with North American potential *production structure* is striking. Its comparative (emerging) advantage in grain lacked at the time the scale economies of tropical agriculture and of mineral extraction seen elsewhere in the Americas.

Precolonial institutions

- Scarce labor with abundant land inhibited the concentration of power (despite efforts of colonizers to do so). The need to attract more settlers and encourage them to engage the colonial economy led to the evolution of more egalitarian institutions in the North American colonies.
- North Americans enjoyed greater egalitarianism in access to all of the factors so restricted elsewhere.
- This environment facilitated broad-based innovation, entrepreneurship, and investment and gave the United States and Canada a decisive advantage despite their starting out as much poorer societies, which they used to economically surpass societies whose populations were mostly illiterate, disenfranchised, and lacking collateral.

Precolonial institutions

- When local populations were larger and denser and social organization was more advanced, it was easier for colonists to take over existing social structures to gain tribute.
- In such cases, resulting institutional arrangements would tend to favor mechanisms of extraction of existing wealth over the creation of new wealth, often leading to declines in the relative fortunes of these regions.
- This is pointed up by Acemoglu, Johnson, and Robinson, whose influential research on this historical “reversal of fortune” is also reflected by **Arrow 5**.
- These authors stress that if geography were fundamental to development prospects, the most prosperous areas prior to colonization should continue to be relatively prosperous today.
- But the most prosperous formerly colonized areas today tend to have been least prosperous in the past. Past population density and past urbanization, which are positively correlated with past income, are *negatively* correlated with current income.

Precolonial institutions

- There is evidence that Europeans set up more *extractive institutions* (ones designed to extract more surplus from colonized populations) in prosperous areas and that these institutions have often persisted to the contemporary period.
- Geography undoubtedly influenced early economic history in Europe. This is reflected by **Arrow 8** leading to *Evolution and timing of European development*.
- Early development in Europe gave it advantages over most other regions, advantages that were used to colonize much of the world. But the types of colonial regimes implemented varied considerably, depending on conditions prevailing at the time of colonization both in the different parts of the world colonized and within the colonizer's home country.
- The timing of European development influenced the type of colonial regime established, reflected by **Arrow 9**. For example, it has been argued that for various reasons, earlier colonization generally involved more plunder and less active production than later colonization, although both occurred at the expense of the indigenous populations.

Precolonial institutions

- *Precolonial comparative advantage* may also have interacted with the timing of European development in influencing institutions in that settlers in later colonized temperate zones arrived with more knowledge and more advanced technology.
- In particular, Europeans brought better agricultural techniques to the later-settled areas such as North America. As noted by David Fielding and Sebastian Torres, by the eighteenth century, population growth in Europe and technical change had produced a large supply of people with temperate zone agricultural skills in products such as wheat and dairy.
- They were able to gain higher incomes using these skills in temperate colonies and former colonies (the so-called neo-Europes). Thus precolonial (potential) comparative advantage again mattered. This link is reflected in the flow through **Arrow 6** and **Arrow 7**.
- The possible role played by specific skills also points up the importance of human capital investments for development, reflected by **Arrow 14**.

Precolonial institutions

- Thus the types of colonial regimes established, while always designed for the benefit of the colonizers, were influenced by local and European supply and demand factors. The type of regime had enormous influence on postcolonial institutional quality, reflected by **Arrow 10**.
- For example, the depraved rule of Belgium's King Leopold II over the Congo (today's Democratic Republic of Congo) was arguably an ultimate cause of the oppressive Mobutu reign after independence.
- Of course, not all influences of colonialism were necessarily bad. Along with enslavement, subjugation, exploitation, loss of cultural heritage, and repression, colonists also brought modern scientific methods in fields such as medicine and agriculture.
- Note that this can be no apologia for colonialism, because these advances could have been gained without the societies' becoming colonized, as in Japan.

Precolonial institutions

- Still, there is some evidence that countries and territories that spent a longer time as colonies (at least in the case of islands) have higher incomes than those that experienced shorter colonial periods, with this effect greater for entities colonized later (perhaps because earlier colonial activity had more pernicious effects than later ones). Even so, there are strong caveats to this finding.
- Besides creating specific institutions, European colonization created or reinforced differing degrees of *inequality* (often correlated with ethnicity), ultimately leading to diminished prospects for growth and development, notably in Latin America and the Caribbean.
- This is reflected by **Arrow 11**. High inequality often emerged as a result of slavery in regions where crops could be “efficiently” produced on slave plantations. They also emerged where a large, settled indigenous population could be coerced into labor.

Precolonial institutions

- Such histories had long-term consequences, particularly in Latin America. As Engerman and Sokoloff have argued, the degree of inequality itself can shape the evolution of institutions as well as specific policies.
- Where inequality was extreme, there was less investment in human capital (**Arrow 13**) and other public goods (**Arrow 16**) and, as reflected by the bidirectional **Arrow 12**, a tendency of *less* movement toward democratic institutions (which could also have facilitated movement to other constructive institutions).
- Thus extreme inequality is likely to be a long-term factor in explaining comparative development. This is raised in the striking historical contrast between the states of North America and the states of Central and South America.

Precolonial institutions

- There was greater egalitarianism in North America, though the inhuman treatment of Native Americans and of slaves in the southern colonies reflects the fact that this is not because the English settlers were inherently “nicer masters” than the Spanish.
- Still, the North American experience contrasts strongly with the extreme inequality of Central and South America and the Caribbean.
- Engerman and Sokoloff argued that high inequality in Latin America led to low human capital investments, again in contrast to North America; this mechanism is again reflected by **Arrow 13**. Elites in Latin America then loosened their control only when their returns to increased immigration, and thus to creating more attractive conditions for immigrants, were high.

Precolonial institutions

- Besides creating specific institutions, then, European colonization created or reinforced different degrees of inequality, often correlated with ethnicity.
- This history had long-term consequences, particularly in Latin America. In the direction from inequality to postcolonial institutional quality, **Arrow 12** reflects what has been termed the social conflict theory of institutions.
- Cultural factors may also matter in influencing the degree of emphasis on education, postcolonial institutional quality, and the effectiveness of civil society, though the precise roles of culture are not clearly established in relation to the economic factors looked at in this section.
- In addition, institutional quality affects the amount and quality of investments in education and health, via the mediating impact of inequality.

Precolonial institutions

- Clearly, human capital has a direct impact on income and on human development more broadly, as reflected by **Arrow 14**. The depth and breadth of education in the population will help determine the effectiveness of government as a force for development, reflected by **Arrow 15**.
- This is due not only to a better-qualified civil service but also to the understanding of citizens of poor government performance and the knowledge of how to work for a better outcome and capacity to organize.
- Of course, education could also independently affect the organization and functioning of markets per se (arrow omitted), but the literature to date has primarily viewed the productive impact of human capital on market outcomes as a direct one, reflected by **Arrow 14**.

Postcolonial institutional quality

- Postcolonial institutional quality has a strong impact on the effectiveness of the private, public, and citizen (or civil society) sectors. Democratic governance, rule of law, and constraints on elites will encourage more and better quality public goods, reflected by **Arrow 17**.
- Better property rights protections and contract enforcement for ordinary citizens and broad access to economic opportunities will spur private investments, reflected by **Arrow 18**.
- And institutions will affect the ability of civil society to organize and act effectively as a force independent of state and market, reflected by **Arrow 19**.
- Clearly, the activities of the three sectors will each have an influence on productivity and incomes, and on human development more generally, as reflected by **Arrows 20, 21, and 22**, respectively

Postcolonial institutional quality

- It is not yet entirely clear which economic institutions are most important in facilitating development or the degree to which strength in one institution can compensate for weakness in another.
- Clearly, there are multiple paths to economic development (see, for example, the case of China). But a key finding of recent research is that *forces that protect narrow elites in ways that limit access of the broader population to opportunities for advancement are major obstacles to successful economic development.*
- ***If institutions are highly resistant to attempts at reform, this helps clarify why development is so challenging.***
- Nevertheless, in most countries with poor institutions, there is still much that can be done to improve human welfare and to encourage the development of better institutions.

Ray of Hope

- Although the picture of life in much of the developing world painted throughout this section may seem bleak, it should be remembered that most developing nations have succeeded in raising incomes significantly.
- And most developing countries have had notable successes in lowering infant mortality, improving educational access, and narrowing gender disparities.
- By pursuing appropriate economic and social policies both at home and abroad and with effective assistance from developed nations, poor countries do indeed have the means to realize their development aspirations.

Ray of Hope

- But concomitant and complementary human capital, technological, social, and institutional changes must take place if long-term economic growth is to be realized.
- Such transformations must occur not only within individual developing countries but in the international economy as well.
- In other words, unless there is some major structural, attitudinal, and institutional reform in the world economy, one that accommodates the rising aspirations and rewards the outstanding performances of individual developing nations, particularly the least developed countries, internal economic and social transformation within the developing world may be insufficient.

Importance of Institutions

- To appreciate the challenges of resolution and prevention, the critical importance of institutional quality and the deep difficulties of improving them.
- Legal rules and informal norms define and reinforce the ways that interests of different groups, even when strongly opposing, can be resolved at least to the point where development can proceed.
- Good institutions provide a foundation of basic security and rights, to successfully prevent or at least strongly mitigate risks of armed conflict likely to retard and set back progress.
- A good institution in this context facilitates conflict resolution, avoiding violence and doing so in a way that allows capabilities to grow. Without improvements in underlying institutions, purely political agreements come with the danger of relapse or can fail to create conditions for balanced economic development.

References:

- Mariano Tommasi, (2005), The Institutional Foundations of Public Policy, DEPARTAMENTO DE ECONOMÍA, DOCUMENTO DE TRABAJO, University of San Andres , Economia 6(2), 1-49.
- Todaro Michael P. and Stephen C. Smith, (2012), Chapter 2: Comparative Economic Development, in Economic Development, Eleventh Edition.

What next?

- Law Making and its Actors