

Appraising institutional challenges in the early stages of development

Introduction to part 3

March 2022

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About Economic Development & Institutions

Institutions matter for growth and inclusive development. But despite increasing awareness of the importance of institutions on economic outcomes, there is little evidence on how positive institutional change can be achieved. The Economic Development and Institutions – EDI – research programme aims to fill this knowledge gap by working with some of the finest economic thinkers and social scientists across the globe.

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Introduction to Part 3

This last part of the volume puts together the lessons learned from the in-depth case studies undertaken within the Institutional Diagnostic Programme (IDP), and the more cursory analysis of the success development stories of South Korea and Taiwan at about the time when they were at a broadly similar level of development as our four case studies today. In doing so, the objective is to provide a kind of analytical list of potential institutional obstacles to development based on the conclusions reached in our analysis of the case study material at hand, whether those obstacles still prevail nowadays or have been removed in one way or another. We also rely on other development experiences, whenever links to them are suggested by our base material, in terms of either similarities or contrasts. Even though our knowledge of those additional country experiences is more superficial, it may still supply valuable insights that complement or enrich those obtained from our main analysis. In other words, from the institutional diagnostics established on Bangladesh, Benin, Mozambique, and Tanzania, as well as the central messages emerging from an institution-focused approach to the early development experiences of South Korea and Taiwan, we are able to extract a set of summary 'generic institutional issues'. Awareness of these issues should help us to better understand the nature of the most important institutional constraints on economic development in general, and to provide a guide to identifying the most binding constraints in the case of a particular country at a particular point in its development.

This list of critical institutional problem areas should assist experts and analysts in uncovering the factors which slow down the development of a country, and the deep institutional reasons behind them. By perusing these generic issues one by one, experts and analysts will have their attention drawn to *potentially* important impediments to growth and development, and should then reflect on how constraining they actually are in the particular country they are interested in. Even though several items in the list can apply to countries at varying levels of development, it should be borne in mind that the whole research programme on the basis of which these generic institutional issues have been established deals with low-income or lower middle-income countries. Other institutional issues might have to be considered at later stages of development.

The analysis we provide below is nevertheless more ambitious than simply listing generic institutional issues or obstacles. On the basis of our four (plus two) case studies, it also offers an in-depth analysis of their possible causes and economic consequences, and, most importantly, the political economy factors that spark resistance to reforms that could mitigate or remove their adverse effects. Beyond mere identification of institutional weaknesses, we thus aim to supply a framework that will enable analysts to reflect on these weaknesses by placing them in their own specific context and their own set of institutional interactions, including those linking formal and informal rules and organisations.

This last part of the volume is organised into three chapters. The first chapter (Chapter 7) focuses on the nature of the *economic* obstacles to development which may be found in a low-income country, with special attention to those that can only be surmounted if some institutional dysfunction is addressed. A key lesson from the case studies is that this inquiry must imperatively be based on an approach that views development as a process of structural transformation by which the great mass of poor people gets out of poverty by moving into decent formal jobs or accessing modern technology. This approach was

formalised by the fathers of the discipline and is at the heart of the tradition initiated by the seminal works of Arthur Lewis (1955) and Simon Kuznets (1966), in particular. An aggregate approach in the spirit of Hausman, Rodrik, and Velasco (2005) is helpful in revealing problems in the way the economy works and, possibly, in shedding light on their institutional underpinnings. Yet it is bound to miss key sources of blockage located in the structural dimensions of development. Based on what we learned from the four IDP case studies and two East Asian success stories, the first part of our discussion thus summarises the various types of economic factors which may block, slow down, or accelerate the process of structural transformation, as well as the broad institutional domains involved.

The second part of our synthesis work is presented in the next two chapters. It delves into key institutional factors by following a conceptual approach that starts by regrouping them into generic institutional issues, as defined above, and then proceeds by probing each of them methodically. By conceptual approach we imply that, beyond a mere listing of these issues, we provide a framework of analysis that goes into the details of each institutional problem area in an orderly and meaningful manner, using concepts borrowed from the existing social sciences literature, and economics literature more particularly, as reviewed at the beginning of this volume. More fundamentally, in the light of our in-depth case studies, and the comparison between the latter and the successful early development experiences of South Korea and Taiwan, we intend to reflect on the proximate and deep causes of institutional dysfunctions, and on how they can be reformed. Our concern about reforms makes it necessary to examine the political economy environment in which the country operates. Although the deep causes behind the generic institutional issues, and the directions for reform, inevitably include country-specific elements, care is taken to identify what may be of more general relevance for middle-to low-income countries.

The above logic leads us to divide the strictly institutional part of the analysis into two chapters. The first one (Chapter 8) deals precisely with the role of institutional factors of a political nature, as well as politics per se, in interfering with the process of structural transformation. As for the second one (Chapter 9), it addresses the same issue from the more functional perspective of the capacity of the state to efficiently deliver public goods and services, and to regulate the private sector so as to make it compatible with the long-term interests of the country, including through the protection of property rights.