Background

- At the aggregate level - an impressive growth rate of over 6% over the last decade on the back of the “commodity boom” - a “growth” story spreading from resource rich economies to a SSA region-wide condition
- Emerging from ‘a fragile continent cursed by economic and political malaise’ to a hope of the “African Renaissance”
- The surge in activities of new investors and actors from emerging market economies
- An acceleration in private investment flows – A shift in “perceptions”
- FDI and remittance have surpassed ODA flows in Africa since the mid 2000s
- Little structural transformation and tangible secondary, economy-wide spill-over effects yet
- With the initial conditions of endemic poverty and high inequality at independence, the growth patterns against the poor over 50 years: due to 1) the low and volatile growth; and 2) the absence of conduits and channels from growth translating into broad-based development.
Background

- Persistent poverty – Between 1980s and 2005- no change in headcount ratio -over 50 % in extreme poor
- Africa is one of the most inequitable regions. Inequalities have not diminished over time. In 2010, six out of the 10 most unequal countries worldwide were in Sub-Saharan Africa
- Rural poor and urban poor absorbed into fragile informal activities with little basic facilities
- 72-80% of the youth population in Africa lives with less than US$2 per day
- Rising inequality in assets and income with some extreme polarisation worldwide under globalisation since the 1980s
- Social cohesion is threatened and social tension raising in the world
- A quest by policy makers for “inclusive” or “shared” growth, turning to the issue of the pattern of economic growth
- A wide recognition: institutional environments exert significant influence on both the rates and pattern of growth and socio-economic development
- Institutions are critical not only for efficiency gains but also in distributional outcomes.
Definitions and Objectives

- Two mechanisms for shared growth: 1) gains from growth are shared ex-post through retrospective fiscal tax-cum-subsidies/transfers policies for redistribution. 2) shared growth as inclusive process of growth with sharing opportunities ex-ante, all-encompassing and inclusive of the poor.

- Ex-ante processes: growth to be accompanied by the process of asset/income equalisation, i.e. the growth path becomes equitable: equity and efficiency interacting ex-ante leading to the development process with a virtuous circle of growth and equity/equality.

- Discuss creating institutions for ‘inclusive development’ as processes.

- Inequality and poverty as the outcome of economic, social and political processes which are mediated through institutions. Then, institutional transformation is required to address the root cause of inequality.

- Objectives: Explore the paths of building institutional foundations for inclusive development in SSA with reference to the concept of endogenous institutions and institutional changes (Greif, 2006 & Aoki 2001, 2007) in their framework of comparative institutional analysis.
Outline of the Paper

1. Introduction

2. Institutions and Institutional changes for Inclusive Development
   2.1 Institutional Configurations as a System for Development
   2.2. Institutions and Inclusive Development
   2.3. Endogenous Institutions and Institutional Changes for Inclusive Development in Comparative Institutional Analysis

3. Domestic and International Conditions that have shaped Institution-Development Nexus in Sub-Saharan Africa
   3.1. Domestic Institutions in the Early Post-independence Years
   3.2. Interface of International and Domestic Conditions under the IFI-sponsored Reform Process
   3.3 Emerging Conditions in the New Millennium

5. Concluding Remarks- Policy Implications
2.1 Institutional Configurations as a System for Development

- Institutions matter for growth and development in the mainstream growth literature (e.g. Rodrik et al, 2004-5; Acemoglu et al, 2001-12 among others).
- *neo-institutionalism* vs *old institutionalism*
- Within *neo-institutionalism*: 1) “institutions-as-rules-of-the-game” and 2) “transaction-cost-economics”
- Institutions-as-rules-of-the game”:
  - North (1981-1995) - the humanly devised (political, social and economic) constraints through incentives and sanctions, shaping human interaction and exchanges and structure opportunities - consisting of formal rules (constitutional, property-rights rules and contracts) and informal ones (social norms and customs).
  - Aoki (2001 and 2007): institutional configurations as a system - complex and diverse (formal and informal) with multiple equilibria
  - Greif (2006): as a system of rules, beliefs, norms, and organizations that together generate a regularity of social behaviour, and social rules to guide and motivate individuals
  - Yet, individuals act and interact as members of different organisations.
2.1 Institutional Configurations as a System for Development
(Cont’d)

- Institutions vs Organisations:
  - **Institutions** create the framework, but **collective action** takes place within **organisations**, bounded by common purpose (North).
  - **Institutions** - the rules of the game: **Organisations**- the players of the game, who can act as agents of institutional change (Aoki).

- Dynamic Interplays between institutions and organisations:
  - **Organisations** as units or channels through which the rule of games are refined, structured and administered at different levels
  - The rule is set through **collective actions/ political processes**. – interface between economic and political institutions;

- Hierarchical order of two perspectives (Aoki):
  - Rules- exogenously per-determined outside the domain of economic transactions, e.g. legal and social norms (“rules-of-the game”)
  - economic institutions e.g. contracts, markets, organisations, and their hybrids are rational transaction-cost-saving responses within these constrains/rules (“transaction-cost-economics”)
2.1 Institutional Configurations as a System for Development (Cont’d)


- Both perspectives of Neo-institutionalism are characterised: by the ‘functional’ view on the role of institutions, with focus on efficiency gains “by: i) protect property rights and ii) minimising transaction and information costs (in contrast the structural view taken by Old (evolutionary) institutionalism)

- Aoki and Greif: use of an equilibrium analysis and agency theory and a strategic game theory as analytical tool and taking institutional configurations as a system either switching around different equilibria, or settling in a specific equilibrium as an outcome of political processes, often dominated by shared believes.

- Comparative institutional analysis emphasises institutional and organisational diversity as a system for development outcomes in efficiency and distribution (Aoki and Hayami, 2001, Greif, 2006, Aoki 2001 & 2007)) - combining Neo and Old institutionalisms
2.2. Institutions and Inclusive Development

- **Bowles (2004)**: "institutional poverty traps" - institutions that implement unequal division of the social product, but not offering any efficiency advantages over more egalitarian arrangements; the persistence due to the self-enforcing nature of existing arrangements and due to the difficulty for the poor in coordinating the collective action to ‘tip’ from an unequal to a more equal set of institutions; Bowles, Durlauf and Hoff (2004) “institutions -especially political and social norms-may entrap entire countries in poverty”

- **Acemoglu and Robinson (2012)**: How institutions matter for Nations’ prosperity and poverty:
  - two institutional regimes - **inclusive** economic and political institutions and **extractive** ones: 1) economic institutions: **inclusive** ones -“enforce property rights, create a level playing field, and encourage investment in new technologies and skills”- vs **extractive** ones -structured to extract resources from the many by the few. 2) political institutions; **Inclusive** ones- distributing political power in a pluralistic manner with some political centralisation vs **extractive** ones concentrating power in the hands of a few.
2.2. Institutions and Inclusive Development (A&R Thesis)

- A& R (2012)-cont’d
  - Powerful synergies between contrasting economic and political institutions- narratives of the historical origin of inclusive institutions and institutional trajectories of different nations as well as their consequences for different development experiences (virtuous vs vicious circle);
  - Extractive institutions can spur sometimes but cannot sustain growth due to being fearful of innovation and creative destruction as well as by engendering political instability;
  - Constant institutional drift resulting from conflict over income, power and institutions; Institutional changes are endogenous!
  - Major institutional changes taking place resulting from interactions between existing institutions and critical junctures (e.g. the Black Death, the opening of Atlantic trade routes or the Industrial Revolutions).

- Little disagreement on; 1) the joint determination of economic and political institutions and 2) the superiority of inclusive regimes over extractive ones
2.2. Institutions and Inclusive Development (Real Challenges)

- Real challenges remaining:
  - Accepting the desirable general form of institutions and their formal establishment by itself does not build those institutions due to both the contingent nature and the path dependence of institutions and institutional changes; they should be underpinned by shared belief and norms;
  - Inclusive institutions may be achieved through different transition paths or may take different forms of institutional configuration
  - Inclusive institutions a la A &R per se do not necessarily lead to more equitable distributional outcome in economic policy making: They are a necessary but not a sufficient condition to ensure inclusive development;
  - Settled institutional arrangements are dictated and determined by political power relationships and conflict resolution mechanisms over distributional outcomes (US and British history);
  - Institution development is not a simple convergence towards, or emulation of, the “best practice” somewhere else as often assumed;
2.3. *Endogenous Institutions and Institutional Changes (Institutional Diversity and innovation)*

- The need for meeting these challenges:
  - Institutions should be *endogenously* developed in a specific local context, so that they are viable and sustainable, backed up by expectations and calculations;
  - Formal institutions simply supplanted from outside without a careful adaptation to local environments are not enforceable as well as functionally ineffective,
  - As inter-dynamics between institutions and organisations are critical forces for social change, institutional changes should be initiated and sustained by local organisations and agents;
  - socially and politically sustainable development involves institutional innovation for a local setting with clearly defined developmental objectives
- institutions are not monolithic; more diversity in organisational and institutional structures in history of institution development and configuration → *comparative institutional analysis* for endogenous institutions and institutional dynamics as a historical process
2.3. **Endogenous Institutions and Institutional Changes**

- **Greif (2006)**
  - **Endogenous institutions**- institutions that are *self-enforcing*, in which all motivation, including that for changes, is endogenously provided.
  - Institutions can change due to endogenous processes, exogenous shocks (institutions become no longer self-enforcing in face of exogenous shocks) or combination of both;
  - endogenous institution can *reinforce* or *undermine* itself. Q: why institutions sometime persist even in a changing environment while endogenous change may occur in a rather stable environment.

- **Aoki (2006 and 2007):** institutions as a *self-sustaining system of shard beliefs*
  - Changes are *endogenously* generated resulting from an interface of formal and informal institutions, and they become self-enforcing through strategic interactions of the agents:
  - an integrative game-theoretic approach - a shift from one institutional equilibrium to another- resulting from combinations of social norms, political states, economic contracts and organisational architecture- ,i.e. dynamic processes of institutional complementarities, social embeddedness and institutional linkages.
2.3. *Endogenous Institutions and Institutional Changes*  
(prototypes of the ‘state’ in the polity domain)  

- prototypes of the ‘state’ in the polity domain (Aoki, 2001)
  - **Government** as an organisation (a player of the game in the political domain) *vs* **State** as “a stable order of relationships between the government and private agents”
  - **Government** is a strategic player that may pursue its own objective but be constrained by strategic interactions with private agents.
  - The emergence of the ‘nation state’ is linked to *market development* for an effective **third party mechanism** to protect property rights and enforce contracts → the extent of market development and demand for third party mechanism are interdependent
  - evolving interface between the **public-private** relationships that engender different outcomes in the institutions-development nexus
  - 3 prototypes of the state (**democratic, collusive** and **predatory**) as a possible stable equilibrium, contingent on strategic interplays between a government and private agents through **taxation** *vs* **public goods** provision → requirements for further market enhancement and development
2.3. Endogenous Institutions and Institutional Changes (an application to SSA under globalisation)

- Globalisation as an epoch-making critical juncture → powerful exogenous shocks to shake up existing, insular, institutions- no longer self-enforcing

- Globalisation → diverse forces for institutional changes (technological and non-technological nature with different distributional outcomes:
  - A previously stable institutional equilibrium has been forced to change in exposure to new environments (new technology - ICTs or mobile technology-, faster flows of information, new production and market arrangements, or scientific knowledge spill-overs: with “right” institution changes. Potential of moving towards inclusive development
  - However, market driven, corporation-led and finance-dominated globalisation increases inequality, in particular functional income distribution against unskilled labour and the poor. The need for counteracting institutional innovation/intervention- which is self-enforcing, so that inclusive development is fostered than hindered under globalisation - requiring a strong nation state

- Need to understand both endogenous institutions, organisations and agents for changes on the ground in SSA in light of path dependent nature of institutional changes
3.1 Institutional Traps in the early years: difficulties in nation-state building

- Institutions at independence- inherited highly extractive political and economic institutions from the colonial regime;
- A huge gap between the leaders’ high vision/aspiration for socio-economic advancement, and the state capacity, institutional configurations and governance structures for implementation of development agenda;
- Autocratic governance structures—justified on the basis of the ethno-linguistically complexity within an artificially created ‘nation-state’; the rulers relied upon pre-existing social institutions, e.g. kinship affiliations.
- State-centred development vision without impersonal state institutions to deliver— with little accountability/ transparency in governance : State engaging in fiscal profligacy, while politically-connected private agents forged a covenant with the state: pervasive client-patron relationships and prone to corruption (extractive political and economics Institutions)
- Use of rationing of subsidies and preferential credits to buy political support— little efforts in broadening tax base, with resource rents available
- The failure to undertake pro-poor public investment in economic and social infrastructures in rural areas – the majority disenfranchised
- Cumulative Institutional Traps with negative private-public interfaces
### 3.2. Interface of International and Domestic Conditions under the IFI-sponsored Reform

- IFI-sponsored reform were supposed to address government failure, seen at the root of negative private-public interactions at the onset of commodity-cum-debt crises in the 1980s&1990s;
- At the macroeconomic stabilization front, the demand management of commodity-dependent economies governed by external shocks should be *counter-cyclical* to the commodity price movements.
- In the absence of a global contingent facility - quick, *unconditional* disbursement upon large shocks, CDDCs dealt with commodity shocks, *pro-cyclical* demand management was imposed by the IFIs.
- The *low-equilibrium trap* of high debt and low growth in the 1980s &1990s.
- Unhealthy recipient-donor relationships developed: → with ex-ante and ex-post policy conditionality, recipient governments and donors can lock into an ‘aid power’ game, resulting in an *inferior non-cooperative equilibrium*.
- Superimposition of the development model with policy conditionality does not work → a *self-sustaining system of shard beliefs* or *endogenous institutions* is not nurtured to emerge → recipient governments little accountable to domestic stakeholders, while donors have to police recipient governments over the adherence to reform packages.
3.2. Interface of International and Domestic Conditions under the IFI-sponsored Reform (cont’d)

- IFIs’ solution for government failure → economic liberalisation/deregulation and keeping the size of governments to minimum in exchange for aid and debt restructuring
- With fiscal retrenchment, governments left with little capacity and resources to undertake public investment on a sustained basis
- The resulting under-provision of public goods (both economic and social infrastructures) with little crowd-in private investment - very high transaction costs to engage in productive activities
- Disenfranchised private agents and rural farmers deterred from making forward-looking productive investments - a powerful deterrent effect both on the rate and composition of investment - away from the "official" economy
- The rural poor left behind, while a largely informal economy with a weak and narrow tax base reinforces the fiscal fragility
- There was a sharp reduction of share of aid towards econ. Infrastructure in total aid and in relation to social infrastructure
- Incidences of fragile states – detrimental to nation-state building
- Poor public goods provision and the fragile fiscal condition developed its own loop of a vicious circle for condemning to a low development trap - a serious impediment to structural transformation
3.3. Emerging conditions in the New Millennium

- The MDRI, and recognition/call for a surge in infrastructure investment
- The revival of growth in the 2000s - associated with the commodity boom, driven by EMs’ rapid demand for resources
- China, along other EMs, has increased aid and investment on the basis of a “coalition” engagement, i.e. a collaborative state-business approach through aid-trade-investment as a package – High hope for South-South cooperation to make a difference despite many new issues
- Focus on infrastructure development and agriculture - critical bottlenecks in Africa - the “resources for infrastructure” model
- Depends on whether new investment deliver real development-growth dividend with higher investment productivity and social returns
- other tangible spillovers - private investors – Africa as one of key destinations of their direct and portfolio investment
- New technology with less sunk costs (e.g. mobile technology)
- FDI increased from from $1.2 billion in 1990 to US$ 40 billion in 2010
- Yet, not much skill transfers and other linkages to local producers yet
- new issues/challenges emerging such as problematic “land grab” by many Ems and others; environmental degradation and climate changes
3.3 Institutional conditions facing producers under globalisation

- Imperative to understand institutional configurations facing private entrepreneurs and rural farmers under - not much market and production network deepened internally and region-wide yet

- TNCs dictate the terms of international trade through intra-firm trade under globally integrated production and marketing strategy- Governance structures of GVCs have become buyer-driven

- Institutional changes affecting agricultural producers in input provisions, access to technology, extension services and marketing → institutional/organisational vacuum

- Farmers: marginalized with little institutional support and the loss of the bargaining power, as vertically integrated TNCs had consolidated their positions over GVCs (production, processing and marketing); Institutional vacuum, leading to fragmentation of marketing activities, and placed small-holders in a weaker position viz private traders and TNCs

- In mineral producing countries- unfavourable outcomes in taxes and royalties negotiated between TNCs and governments in post privatisation

- Imperative for a strong nation state working for interests of domestic stakeholders
4. Concluding Remarks - Policy Implications

- The challenge of overcoming institutional traps that has kept the poor from benefiting from growth - a shift from low institutional equilibrium to a new one with consolidating formal and informal institutions and building institutional configurations as a self-sustained system of shared belief.

- Endogenous institutions and institutional changes through intermediate organisations of collective action and conflict resolution; Aid should be handmaiden for development of endogenous institutions conducive to inclusive development.

- Forging productive functional coalition through better fiscal dialogue (broadening tax nets in return for improved public service and sustained public goods provision) and advancing socio-economic agenda. Leading to productive activities and broader engagement in official economy away from fragile informal activities (mainstreaming informal economy).

- Negotiate better deals for domestic stakeholders with TNCs and investors from both traditional and emerging countries to facilitate knowledge-technology-skill transfers and to protect rights of farmers and employees.

- Building pro-development institutions, including strong nation-states with a realistic development strategy, capable for mobilising aspiration of domestic stakeholders.