

The Nobel and the Question of Why You Drive Slower When There Are CCTV Cameras

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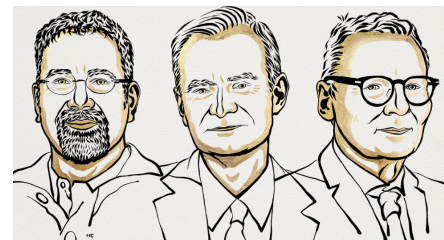
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‘The great divergence’ is a phrase used to describe the chasm in economic and political development between the west and the east. One of the most relevant findings that emerged from this scholarship is the idea that institutions set up during colonialism can have persistent effects many years into decolonisation of a country.

Daron Acemoglu, Simon Johnson and James Robinson are pioneers in emphasising the role of institutions in the direction of development. Institutions are human-made constraints on human behaviour, the rules of the game that prevent the powerful from exploiting the weak, say, the constitutional limits on the powers of a president or prime minister. Institutions have their effect through incentives, like the CCTV cameras on busy streets to nudge you into driving slower.

Acemoglu, Johnson and Robinson's work has highlighted the role of 'extractive institutions' in derailing a country's development path. Extractive institutions concentrate power in the hands of a few while inclusive institutions establish legal authority to rule. Colonialism established extractive institutions in Sub-Saharan Africa, Latin America, the Caribbean and South Asia. On the other hand, there are relatively fewer extractive institutions in the USA, Canada, Australia and New Zealand. In order to establish how these institutions have a causal impact on economic growth, they showed how the colonists settled and thrived in large numbers where inclusive institutions were present while wherever they were wiped out due to tropical disease, more extractive institutions were common. For instance, settler colonists of Australia and the USA settled there in large numbers due to a favourable disease environment. Now while this research highlighted that the mortality of colonists at the time influenced their settlement patterns, it still did not explain how they influenced economic outcomes today.

Economic institutions are collective choices and these in turn are determined by political power. *De jure* political power means there are political institutions that determine constraints and the incentives of key actors in the political sphere. The political power for Joe Biden doesn't come from the person, but the office that he holds, of the president of the USA. On the other hand, you can't say the same for Teodoro Obiang Nguema, the president of Equatorial Guinea for more than 50 years. This would be *de facto* power.



The question of reform of an extractive institution then becomes about the ability to solve a collective action problem through the economic resources available to them. What Acemoglu, Johnson and Robinson's research have shown is that even if we know good institutions can cause good economic outcomes, it is difficult for groups with conflicting interests to agree on what those good institutions look like. That is essentially a problem of politics. Groups with political power cannot commit to not using their power to change the distribution of resources in their favour. These institutions which can have a long-term effect on economic development can take the form of property rights. The various land tenure models introduced by the British rule in the Indian subcontinent have been shown to determine poor economic outcomes until recently due to the absence of widespread land reforms since independence.

Acemoglu, Johnson and Robinson's research signalled a comeback to the importance of institutions in economics. Their research came to prominence at a time when the economics profession was moving away from a presumptive policy framework to

something more diagnostic. This newer approach saw policy experimentation to discover local solutions, and monitoring and evaluation to understand which approaches work. There was a deliberate move away from universal remedies like the erstwhile shock therapy in Latin America or the Washington Consensus. Their research can be read as optimistic if one were inclined to accept the possibility of a progressive politics that can undertake the necessary reforms to build inclusive institutions. This Nobel award for institutions is very well justified.

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