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The Political Dynamics of Economic Growth

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Abstract

This paper is an assessment of what we know about the political determinants of economic growth. It begins by setting out the stylized facts of economic growth. The paper suggests that there is a need to shift away from much of the previous literature's emphasis on the determinants of long-run *average* economic growth (including political determinants), to an understanding of the determinants of within-country growth patterns. The paper proposes a conceptual framework to understand the political channels of within-country growth. Using this framework, it reviews the theoretical and empirical literature on the political determinants of economic growth. It argues that the theoretical and empirical literature do not provide an adequate understanding as yet of the political dynamics of economic growth, and suggests future directions for research in this area.

Keywords: political dynamics, economic growth, institutions.

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1. Introduction

The process of economic growth and why there are such significant differences in living standards across countries is one of the most important and challenging areas of research in economic development. An early tradition in the very large literature that exists on the determinants of economic growth was mostly focused on understanding the proximate determinants of economic growth, and in particular, the role of human and physical capital accumulation, technological change and productivity growth in explaining economic growth. However, as North and Thomas (1973) noted, such proximate determinants or correlates of economic growth "are not causes of growth; they are growth" (p. 2). A more recent literature has gone beyond these proximate determinants and attempted to understand the *fundamental* causes of economic growth – "the factors potentially affecting why societies make different technology and accumulation choices" (Acemoglu, 2009, p. 20).

Institutions and geography are widely regarded as the two most important fundamental causes of economic growth (Acemoglu, Johnson and Robinson 2005, Sachs 2003). While these two factors are not necessarily mutually exclusive causes of economic growth, a large empirical literature has shown that institutions – understood as the formal and informal rules that constrain economic and social behaviour - trump geography as the dominant cause of long-run improvements in standards of living. While this literature identifies the causal effect of regulations, laws and norms on economic incentives, and in particular, on the incentives to invest in the technology, physical capital and human capital that are proximate determinants of economic growth, it also recognises that these economic institutions are in large part politically determined, and ultimately reflect choices made and decisions taken by society at large or by some powerful groups in the society. A very new literature has been analysing why in certain political contexts, growth-enhancing economic institutions emerge and why we see the persistence of growth-impeding economic institutions in many developing countries for long periods of time.

In this survey article, we assess what we know (and what we do not know) about the role of political factors in explaining why some countries economies grow faster than others. We begin with a fresh look at the “stylized facts” of economic growth. We identify an important limitation in the past literature on economic growth in that their focus on rates of **average** growth of per capita income has obscured the fact that most countries observe dramatic fluctuations in growth of per capita income. Most developing countries tend to observe stop-go growth episodes, with growth accelerations followed by growth decelerations or collapses. We argue that an understanding of the political drivers of economic growth needs an explanation of the political dynamics around the transition from one growth regime to another – that is, the political determinants of growth accelerations, growth maintenance and growth declines/collapses. We then sketch out a simple framework to understand the political channels of economic growth around the transitions from one growth regime to another regime. We then use this framework to review both the theoretical and empirical literature on the political determinants of economic growth. Our specific interest in reviewing this literature is the role political factors play in the establishment and change of economic institutions, and how the dynamics of institutional change and persistence in turn affect economic growth.[1] We argue that neither the theoretical and empirical literature provide an adequate understanding yet of the political dynamics of economic growth, and suggest future directions for research in this area.

The rest of the paper is structured as follows. We first set out the “stylized facts” of economic growth in Section 2. In Section 3, we sketch out a framework by which to understand the political channels of economic growth. The next two sections review the literature on the political and institutional determinants of growth. Section 4 discusses theories of the political determinants of economic growth while Section 5 discusses the empirical literature on the political and institutional determinants of economic growth. Section 6 concludes, with a set of research questions that we suggest should inform future research on the political drivers of economic growth.

2. Stylized facts of economic growth

The standard definition of economic growth is that it is a sustained increase in per capita incomes over a sufficiently long period. The Commission on Growth and Development (CGD, 2008), a multi-donor initiative to study the causes of economic

[1] By political factors, we mean “the processes of conflict, negotiation and cooperation between interest groups” and individuals in the use, production, and distribution of resources (Willams et al. 2011).

growth, identify only thirteen countries which have experienced high, sustained economic growth (defined as an average of 7 per cent growth of per capita income or more over 25 years or more). These thirteen success stories are listed in Table 1. Two of these countries are developed countries (Japan and Malta), and one is oil rich (Oman). This leaves only ten countries from the developing world that have experienced sustained growth in the post- World War II period: Botswana, Brazil, China, Hong Kong, Indonesia, Korea, Malaysia, Singapore, Taiwan and Thailand. Of these examples of growth successes, only two are from outside Asia, these being Botswana and Brazil. Figure 1 provides the plots of per capita GDP (in constant 2005 US PPP dollars) for the ten developing countries from 1960 to 2008. It is clear that the increase in per capita income for most of these countries (with the exception of Brazil) follows a linear growth process, and that income grew more or less continuously for these countries (except for the period of the 1997 financial crisis, which affected economic growth in countries such as Indonesia, Korea and Thailand).

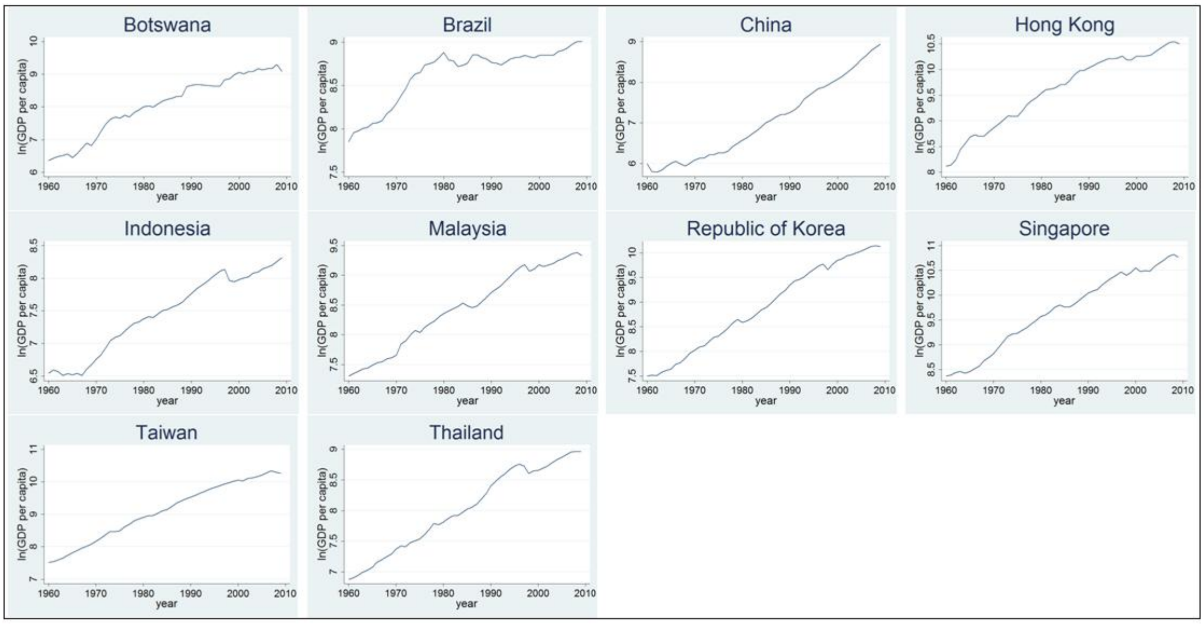
Table 1. Success stories of sustained, high growth, as identified by the Commission on Growth and Development (CGD 2008)

Economy	Period of high growth**	Per capita income at the beginning and 2005***	
Botswana	1960–2005	210	3,800
Brazil	1950–1980	960	4,000
China	1961–2005	105	1,400
Hong Kong, China*	1960–1997	3,100	29,900
Indonesia	1966–1997	200	900
Japan*	1950–1983	3,500	39,600
Korea, Rep. of*	1960–2001	1,100	13,200
Malaysia	1967–1997	790	4,400
Malta*	1963–1994	1,100	9,600
Oman	1960–1999	950	9,000
Singapore*	1967–2002	2,200	25,400
Taiwan, China*	1965–2002	1,500	16,400
Thailand	1960–1997	330	2,400

Source: CGD (2008)

Notes: *Economies that have reached industrialized countries' per capita income levels.
**Period in which GDP growth was 7 percent per year or more.
***In constant US$ of 2000.

Figure 1: The ten growth successes from the developing world, GDP per capita, 1960-2010



Notes: PPP Converted GDP Per Capita (Laspeyres), at 2005 constant prices
Source: Penn World Tables 7.0.

CGD point out five points of resemblance in the thirteen success stories: i) these countries fully exploited the world economy; ii) they maintained macroeconomic stability; iii) they mustered high rates savings and investment; iv) they let markets allocate resources and v) they had confirmed committed, credible and capable governments. Given the wide variation in initial conditions, colonial origin of the state, and resource endowments in these thirteen countries, it is quite striking that the set of factors that CGD hold responsible for the successes of these countries in economic growth does not vary substantially across these countries. However, as with much of the empirical growth literature, several of the factors that CGD hold responsible for growth success can be seen as proximate determinants of economic growth and not the fundamental causes. Whether a country experiences macroeconomic stability or high rates of saving and investment depends very much on the economic institutions that reward high saving and investment and political institutions that limit the discretion of politicians to engage in macroeconomic populism or to tax citizens of the country through seignoriage.

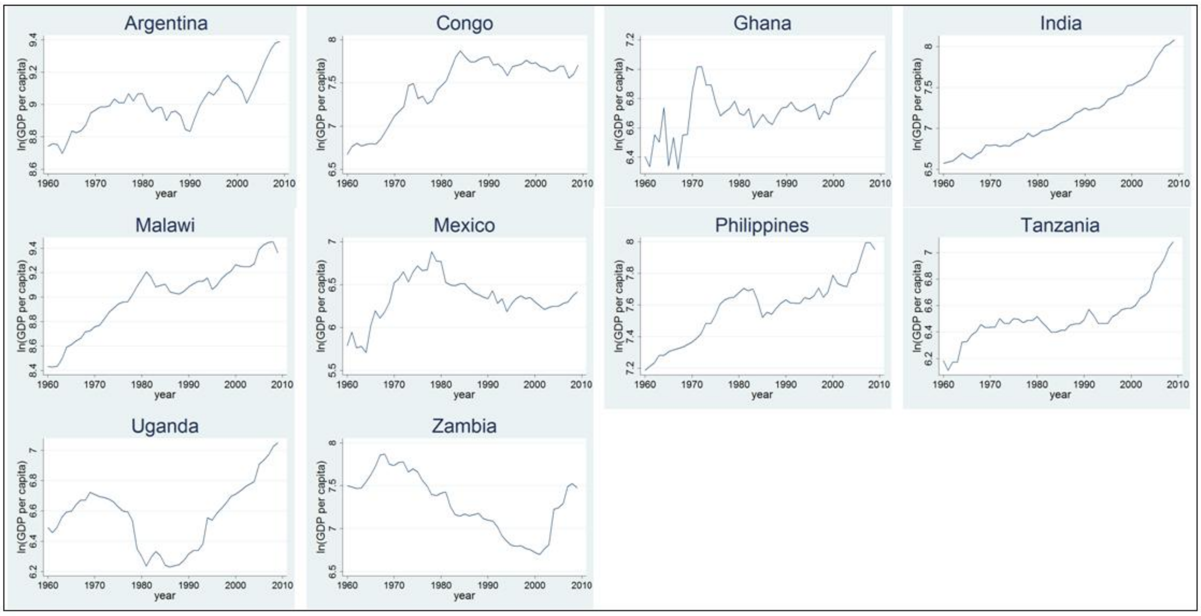
Integration into the world economy in a manner that has been observed by Korea and Singapore, for example, is itself a function of a country's institutional quality and its geography (Rodrik, Subramanian and Trebbi 2004). Capable and committed states are more likely to emerge when incentive structures for politicians and bureaucrats reward long-term behaviour, and CGD do not explicitly address under what conditions such long-term behaviour of the part of states is more likely to occur. Therefore, the key question that remains in CGD's analysis of the success stories of sustained growth is: what are the underlying political determinants of the factors that CGD identify as being central to growth success?

There is one important limitation of CGD's approach in identifying economic growth successes, which is also evident in the wider empirical literature on economic growth. CGD's approach of classifying growth successes by high rates of **average** growth of per capita income misses the point that most countries observe dramatic fluctuations in growth of per capita income. Very few developing countries meet the criterion of sustained high rates of growth – most developing countries tend to observe stop-go growth episodes, with growth accelerations followed by growth decelerations or collapses. As Jones and Olken (2008) point out, "almost all countries in the world have experienced rapid growth lasting a decade or longer, during which they converge towards income levels in the United States. Conversely, nearly all countries have experienced periods of abysmal growth. Circumstances or policies that produce ten years of rapid economic growth appear easily reversed, often leaving countries no better off than they were prior to the expansion" (p. 582). Therefore, long-run growth averages within countries often mask distinct periods of growth success and growth failure, and "the instability of growth rates makes the talk of *the* growth rate almost meaningless" (Pritchett 2000, p. 247). Growth experiences differ over time within a country almost as much as they differ among countries, and identical average growth rates can mask very distinct growth paths (Jerzmanowski 2006).[2]

[2] In the first systematic analysis of growth accelerations, Hausmann, Pritchett and Rodrik (HPR) (2005) study such episodes of growth accelerations for all countries, developed and developing, since the 1950s, and identify an episode of growth acceleration by the following three conditions: i) where the least squares growth rate is greater or equal to 3.5 per cent per annum; ii) where the change in the least squares growth exceeds 2 per cent per annum over a eight year time horizon; and iii) where post-change growth output exceeds the pre-episode peak.[2] Using these criteria, HPR identify 83 episodes of growth accelerations between 1957 and 1992, the starting and ending years of their analysis. They find episodes of growth accelerations in all regions of the world, and the average acceleration in per capita income is 4.7 per cent per annum, implying that in the typical episode, output was almost 40 per cent higher at the end of episode than it would have been without the growth acceleration. The large number of episodes observed by HPR and the magnitude of changes in per capita incomes in the average episode provides a strong justification why it is important to move beyond accounts of long-run growth to within country growth episodes in any examination of the causes of economic growth. HPR observe that a typical country would have about 25 per cent chance of experiencing a growth transition at some point in any given decade. It is also worth noting that the largest number of growth accelerations is in Africa (20 episodes, using the HPR criteria), a continent that is not usually associated with economic growth.

To illustrate our point about the very different growth regimes that may characterise economic growth for a particular country over a period of time, we present plots of GDP per capita for a random sample of ten developing countries drawn from Africa, Asia and Latin America. The evolution of GDP per capita shows distinct patterns across the ten countries, and more importantly, **within** these countries. For example, Argentina has seen both periods of high growth and periods of growth declines. Ghana and Tanzania have seen a prolonged period of stagnation in the 1980s and 1990s, followed by positive growth in the 2000s. Malawi and Zambia have observed prolonged periods of growth collapses. In comparison, Uganda shows a significant growth collapse in the 1970s, followed by rapid growth since the 1980s. It was the reverse in the Congo, with growth accelerating in the 1960 and 1970s, and then stagnating since the mid-1980s. In the case of The Philippines, there were multiple growth regimes - there was steady economic growth in the 1960s and early 1970s, followed by a growth collapse in the late 1970s and then stagnation in the 1980s and early 1990s, with growth recovering in the 2000s. Tanzania witnessed a long period of stagnation for three decades in the 1970s to 1990s, with rapid economic growth in the 2000s. Economic growth was low in India till the late 1970s, with a steady acceleration since the early 1980s.

Figure 2: Growth Regimes in a Sample of Countries (GDP per capita, 1960-2010)[a]



Note: PPP Converted GDP Per Capita (Laspeyres), at 2005 constant prices.
Source: Penn World Tables 7.0).

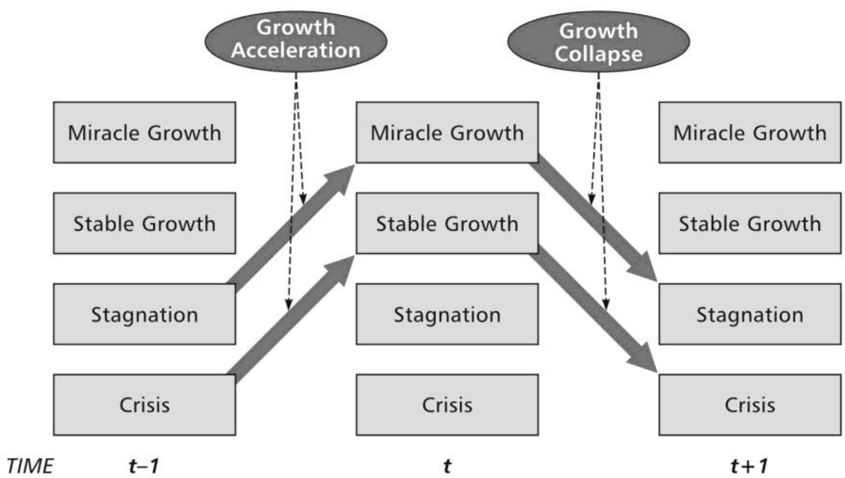
Thus, growth regimes vary across time and space – the same growth regime does not characterise countries in the same region and in the same period, and countries which are similar in some respects (such as Ghana and Uganda) show very different growth regime switches. This tells us that exogenous factors such as oil shocks or terms of trade declines may not be causal to growth regime switches, or at least, that their effects of economic growth may be mediated by within-country variables. The analytical challenge here is to understand what leads to growth accelerations in some countries and not in others, and why do some countries maintain economic growth for extended periods, while in other countries, economic growth declines or collapses after initially accelerating. What explains the likelihood of a country switching from one growth regime to another growth regime, and what is the role of political factors in these growth traverses?

To fix our ideas on transition paths around growth regimes, we provide a simple sketch of these transition paths in Figure 3 below. Using a rough and ready way to demarcate growth regimes, we classify growth regimes into four categories: i) a growth regime which we call 'miracle growth' where the average increase in per capita income is seven per cent per annum or more; ii) a growth regime which we call 'stable growth', where the average increase in per capita income is between two and five per cent per annum; iii) a growth regime which we call 'stagnant growth, where the average increase in per capita income is between zero and two per cent per annum; and iv) a growth regime we call 'growth crisis' where the average change in per capita income is negative. [3]

[3] A more comprehensive classification of growth regimes than the one provided here is offered by Pritchett (2000), who attempts to identify single break-points in the per capita income time-series of developed and developing countries using a simple rule of thumb statistical procedure for the period 1960-1992 (not all countries in Pritchett's sample had data till 1992). He then demarcates six distinct growth regimes, based on the identification of the break-point: i) Steep Hills – where growth rates were 3 per cent or higher in pre and post-break periods; ii) Hills - where growth rates were higher than 1.5 per cent in pre and post-break periods; iii) Plateaus - where growth rates were higher than 1.5 per cent in the pre -break period but fell to less than 1.5 per cent in the post-break period; iv) Mountains - where growth rates were higher than 1.5 per cent in their trend beak but fell to negative rates afterwards; v) Plains - where growth rates were less than 1.5 per cent in pre and post-break periods; and vi) Accelerators – where growth rates were less than 1.5 per cent before the break, and higher than 1.5 per cent after the break. While Pritchett's criteria to identify growth regimes is fairly rudimentary, an emerging literature has begun to identify the exact timing of growth regime switches and the duration that a particular country stays in a particular growth regime using more sophisticated modern time-series methods. Example of the application of such methods are Jones and Olken (2008) and Berg et al. (2012) who use variants of the procedure proposed by Bai and Perron (1998) to identify multiple breaks in the per capita income series when the total number and timing of structural breaks is unknown, and by doing so, allow a country to be in multiple growth regimes over time (in contrast to Pritchett, whose method only allows for two growth regimes – one before and one after the single break in the per capita income series). Jerzmanowski (2006) and Kerekes (2012) use Markov switching regression models to estimate the probability of transition from one growth regime to another for countries with different chararacteristics. More details of these studies are provided in our discussion of the empirical literature on the politics of economic growth.

There are three points to note from Figure 3. Firstly, most, if not all, of the countries that the CGD considers as growth successes will be those in the top half of the figure (miracle growth => miracle growth), where a country is persistently in a miracle growth regime (it is obvious that there would be a point far back in time in the country's history where the country observed a growth acceleration to reach the miracle growth regime). Secondly, in understanding transitions between growth regimes, we should not only be interested in countries which make the move from stagnant/crisis growth to miracle growth but also countries which make the transition from negative growth to stable growth as well. The latter type of growth transition is important and may have significant implications for the country's welfare and its ability to move out of a situation where the living standards of its citizens are declining, to a situation where they are improving. Thirdly, while much of the literature has concentrated on the causes of miracle growth and the maintenance of such growth, Figure 3 makes clear that our understanding of the causes of miracle growth will not be complete if we do not understand why some countries persistently remain in miracle/stable growth regimes while others suffer growth collapses. Clearly, the avoidance of the factors that lead to growth collapses or declines is the reason why some countries see persistent high economic growth over extended periods of time.

Figure 3 Transition Paths between Growth Regimes



If the emphasis in our understanding of economic growth in developing countries should be less on the determinants of long-run *average* economic growth and more on the determinants of within-country growth patterns, it would be necessary for us to understand the political dynamics around the transition from one growth regime to another, and the political economy determinants of growth accelerations, growth maintenance and growth declines/collapses. The overarching research question for us to address would be to understand what determines *political transitional dynamics* around growth regime traverses –the move from one growth regime to another growth regime. In the next section, we sketch out a framework which makes an attempt in this direction and that we will use as a way to embed our review of the theories and empirics of the politics of growth within the context of such an overarching research question.

3. The political channels to economic growth

By definition, economic growth is an outcome of increase in capital accumulation and increases in productivity or technological progress. But what are the political channels by which capital accumulation and/or productivity increases occur? Do these political channels play out differently across the different phases of economic growth – from growth acceleration to maintenance/sustenance? In this section, we sketch out a framework for understanding the political channels of growth, and especially in the transition from one growth regime to another, which we will use to interrogate the theories of politics of growth we review in the next section.

The literature identifies three distinct political channels to growth. The first is **credible commitment** by the state, or agents of the state (Haber, Razo and Maurer 2003). That is, the state needs to credibly commit to potential and current investors that it will not expropriate most or all of the profits that may accrue from the production process or the means of production themselves. By committing to not expropriating rents over and above which may be considered to be 'fair', the state can ensure that investors commit to the investment decision and engage in production, so that rents can be generated through the production process. This commitment needs to be seen as credible by investors in that they believe that the state will not renege on its implicit or explicit promise not to expropriate all or most of the rents accruing from the production process in the future, especially after investment decisions involving sunk costs in fixed capital have been taken. Investors also need to commit to share a part of their rents to the state (or its constituents, such as politicians) and when states raise revenues from taxes, to pay the state the necessary taxes.

Credible commitment can be seen as both a necessary and sufficient condition for capital accumulation to take place or for entrepreneurs to make the necessary investments in productivity enhancing changes in their enterprises. Most investment activities take time and there are lags between the time-period when investment in land and machinery is made, and the time-period when profits can be obtained from the sale of the product in the market. Investment decisions are by their nature lumpy and may have large sunk costs – that is, the costs of certain investments cannot be recovered in full if the investment decision turns out to be less profitable than anticipated. By credibly committing ex ante to not extracting most of the proceeds from the investment decision, the state provides the incentive for the entrepreneur to make the investment and production decision and can extract a part of the proceeds from the investment ex post. In this sense, credible commitment is incentive compatible both for the state and the entrepreneur. However, it follows from the nature of credible commitment that the state has to take a reasonably long view in that reneging on the commitment not to fully extract the rents from investment in one period can lead to a loss in credibility on the part of the state, and for investors not to trust the state when it comes to future investment decisions, leading to a fall in investment, and consequently, in a decline in rent extraction in future periods.

Credible commitment can be obtained through both formal and informal institutions. Formal institutions such as laws which prohibit the expropriation of private property (which investors believe will be implemented), courts that provide sanctions against the firm's customers when there is a non-payment of dues, and bankruptcy procedures which protect financiers such as bondholders when a firm enters into bankruptcy are all examples of formal institutions of credible commitment.

But informal institutions such as kinship structures, social norms and patron-client networks can also act as institutions of credible commitment, especially in environments where formal institutions do not exist or are not well-functioning (Dixit 2009). For example, in a patron-client network, where the patron is the politician and the client is the domestic entrepreneur, the politician may protect the entrepreneur and provide him or her with access to funds and certain privileges (such as licenses for production or imports) in return for the rents that accrue from production which may be used in part for financing the political machinery. Entrepreneurs too will have an incentive to find political patrons who may be keen to protect them, in exchange for economic and political support. Therefore, the existence of informal institutions of credible commitment can be both necessary and sufficient for an episode of growth acceleration, especially in a low income country where formal institutions have not developed or do not function effectively. As long as informal institutions that exist can address at least in part the credible commitment problem in the investment decision, entrepreneurs will be willing to invest, and economic growth will result.

A second political channel to economic growth is **the provision of public goods**.[4]Among the determinants of economic growth that have been identified in the

[4] We take public goods here as being not only pure public goods (in that they are non-excludable and non-rival) but also club goods (in that they are not non-rival but are non-excludable) and quasi-public

empirical growth literature are public goods such as primary and secondary education and provision of health services that are both available to a broad cross-section of the population, and infrastructure such as roads and electricity, that are seen as being crucial enabling factors for economic growth to occur (Barro 1991, Benhabib and Spiegel 1994, Strauss and Thomas 1998, Bloom, Canning and Sevilla 2004, Gyimah-Brempong, Paddison and Mitiku 2006, Pedroni and Canning 2008, Rud 2012) . The literature on the provision of public goods generally see these goods being produced when the state has enough capacity both to raise taxes to finance large scale provision of public goods and to administer the effective delivery of these goods. The dimensions of state capacity that may matter here are bureaucratic and infrastructural power – the capacity of the state to implement decisions and exert its authority over the national territory. Clearly, the more capable the state is in its ability to raise taxes and in its ability to use these taxes to provide high quality 'productive' public goods to the majority of the population, the larger will be the growth-enhancing effects of public goods provision. As Evans and Rauch (1999) find, an increase in half a standard deviation of the "Weberian score" of bureaucratic capacity is worth a 26 per cent increase in GDP from 1970 to 1990.[5] But bureaucratic and infrastructural power need a certain degree of bureaucratic professionalism, and it is more likely that the formal institutions that underpin such bureaucratic professionalism (such as meritocratic recruitment and merit based promotion) will emerge later in the growth process. Therefore, the provision of public goods will be less important as a political channel to growth accelerations and may be more important for growth maintenance. However, not all public goods need a critical level of bureaucratic professionalism for their provision, and it is possible that some local public goods which may be important for growth take-offs such as the creation of an export processing zone or an industrial estate (that allows for pockets of growth to develop in the economy) and the infrastructure associated with these public goods can be provided even when bureaucratic capacity is not well developed, and within clientelist and neopatrimonial contexts (Kelsall et al 2010).

The third political channel to growth **is the overcoming of co-ordination failures in investment decisions**. These co-ordination failures often result from the high costs

goods (in that they are non-rival but are excludable). While education can be both rival and excludable, we take it to be a public good as human capital can have significant positive externalities (Lucas 1988).

[5] Evans and Rauch (1999) measure the Weberian-ness of the bureaucracy by coding responses to 10 questions, collected from a survey of country experts who know the level of bureaucratic capacity in their countries for 35 developing countries. The questions range from those assessing the importance of bureaucracies in generating economic policy, the importance of exams in recruiting civil servants to core economic agencies, the possibilities for career progression and whether there was sufficient rewards to bureaucrats in terms of salaries and prestige.

of collecting and processing information for new products, technologies and industries in low income countries. By investing in new information collection and processing and making information about the relevant new industries freely available to firms, the state can play a facilitating role in the introduction of new products and the move to new industries, and as a consequence, in bringing about structural change and technological upgrading in the economy (Lin and Monga 2010). Co-ordination failures also result from the fact that private returns to investment in sectors that offer the potential of dynamic comparative in low income countries may be less than social returns, as firms need to go through a learning process to build the capabilities to become competitive in new industries (Whitfield and Therkildsen 2011). Since this learning process may involve substantial financial losses at least at the initial stage, the private return to such investment may well be negative, even if the investment may lead to significant positive spillover effects and the building up of social and human capital. Risk averse entrepreneurs with low wealth endowments may not be willing to invest in such investments that have high sunk costs and prefer to invest in activities with a high short-term possibility of profits but which offer less possibilities for technological upgrading.

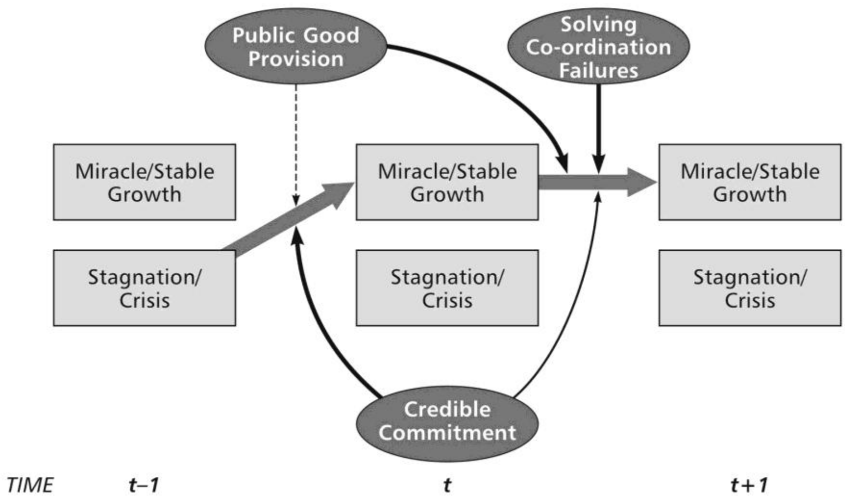
The divergence of the private and social returns to investment may be particularly evident in more modern manufacturing activities or in knowledge-based services as compared to unskilled labour intensive manufacturing or primary commodity production. As the economy moves into these modern sectors, economies of scale and scope become more important, and there is a greater reliance of firms on highly skilled labour and access to long-term finance to make the lumpy investments in equipment, working capital and export financing. Thus, there is a need for the state to play a coordinating role in directing scarce investible funds and limited foreign exchange (to purchase imported capital goods and technology from abroad) to the most productive firms and facilitate the upgrading and diversification of individual firms (Lin and Monga 2010).

But the overcoming of coordination failures needs both a political elite that is committed to a long-term vision of economic development (since the growth payoffs to technological upgrading and industrial diversification may take time to occur) and the presence of an economic bureaucracy that is staffed by relatively competent individuals who are insulated from the pressures of special interests. Such bureaucracies are characterised by a high degree of well institutionalised and organisationally consistent career ladder which bind them to corporate goals while simultaneously allowing them to acquire the expertise necessary to perform effectively (Evans 1995). The relative autonomy of the bureaucracy allows them to intervene selectively in favour of certain firms, sectors and industries in a market-conforming way and to provide both incentives to capitalists and to discipline them (Amsden 1989). Based on the East Asian successes in how governments in these countries successfully overcame coordination failures, Evans (1995, 2011) has argued that another important attribute of bureaucracies in these countries that allowed them to address coordination failures effectively was their 'embeddedness, that is, "the dense set of concrete interpersonal ties that enabled specific agencies and enterprises to construct joint projects at the sectoral level" with local capitalists (Evans 2011, p. 47). Both embeddedness and autonomy were essential features of the state's ability to address coordination failures effectively in the East Asian 'growth successes'. As Evans (2011), argues, "avoiding capture and being able to discipline entrepreneurial elites is a defining feature of the 'embedded autonomy' of East Asian developmental states, distinguishing them from less successful states in Asia and Africa" (p. 47).

How important would the overcoming of coordination failure be as a political channel to growth across different growth regimes? Our discussion of how coordination failures may arise in developing countries indicates that it is more likely to be evident in the later stage of structural transformation when the economy has started the transition from activities that are less human capital intensive and technologically less sophisticated to more complex activities. Thus, the state's role in overcoming coordination failures will be more important when growth has already ignited, than in a context where growth is yet to accelerate. Further, as we have argued earlier, the level of capacity and autonomy of the bureaucracy that may be needed to address the complex interventions necessary for resolving all but the most basic coordination failures would be more likely to emerge at a later stage of the growth process. The ability of the state to resolve coordination failures may play a causal role in why some states cannot successfully transform their economies to more productive and technologically advanced activities. This may also explain why some countries are able to maintain high growth if they are able to successfully transform their economies, while growth dies out in other countries which cannot manage this transformation.

We provide a sketch of how the relative importance of the three political channels in the transition from one growth regime to another in Figure 4 (to simplify the diagram, we collapse the miracle and stable growth regimes into one regime, and stagnation and crisis growth regimes into another regime). As shown in the figure, the first political channel we discuss – institutions of credible commitment – may be a necessary and sufficient channel to growth accelerations while contributing to growth maintenance as well, with informal institutions of credible commitment playing a more important role in growth accelerations, while formal institutions may be more important in growth maintenance. The second political channel we discuss– the provision of public goods – would be more important in growth maintenance and in the avoidance of growth collapse, though it can also play some role in growth accelerations. The thickness of the arrows linking this channel to the different phases of growth shows the relative importance of this channel for the growth maintenance phase as compared to the growth acceleration phase. Finally, as shown in the figure, the third political channel we discuss – the overcoming of coordination failures – would be important in the growth maintenance phase, and would not be expected to play a significant role in growth acceleration.[6]

Figure 4 Political Channels to Growth along Transition Paths



4. Reviewing the Theoretical Literature on the Politics of Economic Growth

[6] Our argument in this section that the political channels to economic growth differ across the different phases of economic growth has also been noted by Rodrik (2004), who has argued that: "igniting economic growth and sustaining it are somewhat different enterprises. The former generally required a limited range of (often unconventional) reforms that need not overly tax the institutional capacity of the economy. The latter challenge is in many ways harder, as it requires constructing a sound institutional underpinning to maintain productive dynamism and endow the economy with resilience to shocks over the longer term."

In this section, we will review the literature on the politics of economic growth, and assess the strengths and weaknesses of the major theoretical and empirical literature on the politics of economic growth. Specifically, we will ask the following two questions of the literature:

i. To what extent can these theories explain the movement between different growth regimes that we set out in Section 2?
ii. To what extent do these theories provide an analytically coherent account of economic growth that address the political channels of growth as discussed in Section 3?

Our literature review is deliberately selective – we review the specific theories that have been influential in the recent literature on economic growth, and that illustrate our arguments around the political dynamics of growth regime switches. The two major theoretical bodies of literature that we discuss are the work of a) Daron Acemoglu and James Robinson (Acemoglu-Robinson), and b) Mushtaq Khan. We begin with a review of the work of Acemoglu-Robinson.[7]

The Politics of Growth Maintenance: Acemoglu-Robinson and Inclusive Institutions

As with much of the recent literature on the politics of economic growth, Acemoglu-Robinson (AR)'s starting point is the premise that institutions, defined as "the rules of the game or more formally, the humanly devised constraints that shape human interaction" (North 1990, p. 3)" are the fundamental cause of economic growth. The set of institutions that matter for broad-based economic growth, according to AR, are inclusive economic institutions and inclusive political institutions (AR 2008, 2012). Inclusive economic institutions are secure property rights for the majority of the population (such as smallholder farmers and small firms), law and order, markets that are open to relative free entry of new businesses, state support for markets (in the form of public goods provision, regulation and enforcement of contracts) and access to education and opportunity for the great majority of citizens. Inclusive political institutions are political institutions that allow broad participation of the citizens of the country and uphold the rule of law, and place constraints and checks on politicians along with the rule of law. AR argue that along with political pluralism, some degree

[7] A recent influential contribution on the causes of different levels of economic and political development across countries is North, Wallis and Weingast (2009). We do not review North, Wallis and Weingast here as the focus of their work is on the long-term historical roots of economic progress, especially in Western societies, and they do not provide a theory of economic growth. It should be noted, however, that there are common elements between their theory of economic development and those of Acemoglu-Robinson and Khan.

of political centralization is also necessary for the states to be able to effectively enforce law and order. In contrast to the growth-enhancing effects of inclusive economic and political institutions, AR argue that extractive economic institutions such as insecure property rights and regulations that limit entry to markets and extractive political institutions that concentrate power in the hands of a few with limited checks and balances are not likely to lead to broad-based and sustained economic growth (that is, growth can occur for some time under these institutions but is not likely to last and will benefit a narrow set of elites rather than the majority of the population).

But what determines the set of economic and political institutions prevailing in the country at a particular point of time? Economic institutions are not distribution neutral: they not only determine the aggregate growth potential of the economy but also the distribution of resources in the country. This implies that economic institutions are **politically determined**, as the prevalent power relations will determine which set of economic institutions are more likely to emerge. A similar argument can be made for political institutions, and AR argue that these are determined by political power of different groups in society. Political power can be both *de jure* and *de facto*. *De jure* political power refers to power that originates from the political institutions in society. *De jure* political institutions determine the constraints on and the incentives of key actors in the political sphere and could be both formal (that is, whether the political system is democratic or autocratic) or informal (that is, the set of informal constraints on politicians and political elites). *De facto* political institutions, on the other hand, originate from the possibility that important social and political groups which hold political power may not find the distributions of benefits allocated by *de jure* political institutions and by economic institutions acceptable to them, and may use both legal and extra-legal means to impose their wishes on society and try to change these institutions (for example, they may revolt, use arms, co-opt the military or undertake protests).

AR argue that the degree of *de facto* political power originates from the ability of some groups to solve their collective action problem and from the economic resources available to the group (which determines their capacity to use force against other groups). In the ultimate analysis, therefore, the initial distribution of economic resources and the nature of *de jure* political institutions determine both *de jure* and *de facto* political power and these in turn determine the set of economic institutions and political institutions that are likely to emerge in the economy, and which in turn determine economic performance and the distribution of resources that are compatible with the distribution of political power. This can be seen in the following schematic representation in Figure 5.

Figure 5: The Evolution of Political and Economic Institutions in Acemoglu and Robinson's Theory of Economic Growth

$$\left.\begin{array}{ccc}
\begin{array}{c}\text{political}\\ \text{institutions}_t\end{array} & \Longrightarrow & \begin{array}{c}\text{de jure}\\ \text{political}\\ \text{power}_t\end{array}\\
 & & \&\\
\begin{array}{c}\text{distribution}\\ \text{of resources}_t\end{array} & \Longrightarrow & \begin{array}{c}\text{de facto}\\ \text{political}\\ \text{power}_t\end{array}
\end{array}\right\}
\begin{array}{ccc}
\Longrightarrow & \begin{array}{c}\text{economic}\\ \text{institutions}_t\end{array} & \Longrightarrow \left\{\begin{array}{c}\text{economic}\\ \text{performance}_t\\ \&\\ \text{distribution}\\ \text{of resources}_{t+1}\end{array}\right.\\
\Longrightarrow & \begin{array}{c}\text{political}\\ \text{institutions}_{t+1}\end{array} &
\end{array}$$

Source: Acemoglu and Robinson (2008)

AR introduce the concept of **political equilibrium** as a way of understanding how political factors determine the form and functioning of economic institutions and by doing so, affect economic growth. A political equilibrium is the the set of political and economic institutions compatible with the balance of *de facto* political power between groups. It is the political equilibrium that determines the institutional arrangements in society and the manner in which economic institutions function. Therefore, AR argue that "making or imposing specific institutional reforms may have little impact on the general structure of economic institutions or performance if they leave untouched the underlying political equilibrium". An example of this was in Argentina during the imposition of Washington Consensus type economic reforms in the late 1980 when Memen and the Peronist party after 1989 recognised that the policies of the Washington Consensus could be bent to function as "politics as usual", and there was little change in the underlying political equilibrium though the instruments that the Peronists used after 1989 were different (AR 2008). AR point out that the reason the reforms failed was not due to the nature of the reforms but that the political equilibrium would have to change if the reforms were to succeed.

An important implication of AR's theory is that bad political equilibrium that leads to poor economic performance may persist over time, and economic growth may stagnate in a country for many years as a consequence. Since the distribution of political power determines the evolution of economic and political institutions, political elites who hold power will always have an incentive to maintain the political institutions that give them political power, and the economic institutions that distribute resources to them. Furthermore, the initial distribution of resources allow elites who have access to these resources to increase their *de facto* political power, allowing them to push for economic and political institutions favourable to their interests, reproducing the initial disparity in political power (Acemoglu, Johnson and Robinson 2005). Therefore, there will be a persistence of extractive economic and political institutions in societies with such institutions, since the elites who benefit from these institutions would not be an incentive to change them. Conversely, inclusive and political institutions will be more likely to prevail, once they emerge, as with the emergence of such institutions (e.g. democratization and secure property rights for the majority of the population), strong economic performance will be likely to result, reinforcing the welfare enhancing effects of these institutions and allowing states to become more credible via greater legitimacy to the commitment of these institutions.

But what explains the switching from one growth regime to another; say, from stagnant growth to miracle growth? AR argue that while bad political equilibrium tends to persist, change is possible. With time, institutional drift may occur, leading to a critical juncture where there may be institutional divergence. This is shown in Figure 6 below.

Figure 6: Institutional Change in Acemoglu-Robinson's Theory of Economic Growth

$$\begin{tikzcd} \text{institutions}_t \arrow[r, "\text{drift}"'] & \text{institutions}_{t+1} \arrow[r] & \begin{matrix}\nearrow \\ \searrow\end{matrix} & \begin{matrix}\text{institutional} \\ \text{divergence}\end{matrix} \\ & & \text{critical juncture} \arrow[ul] & \end{tikzcd}$$

Source: Acemoglu and Robinson (2012)

Many factors can contribute to this divergence. For example, new economic elites may emerge who challenge the existing balance of power and demand change in economic institutions from extractive to more inclusive institutions. There is also the possibility of revolt from citizens excluded from current political institutions, and the elite may respond with greater political pluralism. AR view these critical junctures as 'stochastic' and therefore, to a large extent, exogenous, and they state that it is not clear "under what circumstance political equilibria that lead to economic growth will arise" (AR 2008, p. 10). Therefore, it is not clear how a country will move from a bad political equilibrium associated with growth stagnation/crisis to a good political equilibrium associated with stable or miracle growth, where the political drivers of this move is endogenously determined, and not due to external events or to exogenous factors.

The political channels that are evident in AR's theory of growth are formal institutions of credible commitment (as in the rule of law that leads to the security of property rights) and public good provision. There is less recognition in their theory of the important role the state can play in overcoming coordination failures, and that the emergence of formal institutions of credible commitment and the provision of high quality public goods may not be enough to bring about the structural transformation that has been evident in the successful cases of economic growth in East Asia. Notwithstanding this omission, AR's theory is a more a theory of growth sustenance (and by association, also a theory of long-term growth stagnation) than a theory of growth acceleration or of growth collapse. Once growth has ignited in a country, the emergence of inclusive economic and political institutions may lock in the growth process, and also by implication, broaden the process of growth to make economic growth inclusive. Also, while AR do not directly state that the inclusive economic and political institutions they take to be correlated with sustained economic growth are formal institutions, the specific examples they provide of inclusive economic institutions such as contract enforcement and state regulation of markets and inclusive political institutions such as the rule of law for all citizens suggest that these are more likely to be formal institutions.

This also suggests that AR's theory of growth may be more relevant in the understanding of growth maintenance rather than growth acceleration. The formal institutions that AR take to be crucial to economic growth need a sufficient level of state capacity for enforcement and for their effective functioning, and these enforcement capabilities (and the commitment of the ruling elite to enforce these institutions) are unlikely to be observed in the very early stages of economic growth when growth has begun to accelerate. To understand the political drivers of growth acceleration, we need a theory that can help us understand how economic growth occurs even without the presence of well-functioning formal institutions. We now discuss the work of Mushtaq Khan which, as we will argue, provides such a theory.

The Political Foundations of Growth Accelerations: Mushtaq Khan and Patron-Client Networks

Like AR, Khan starts with the proposition that institutions are the fundamental cause of economic growth (Khan 2010). Like AR, Khan takes institutional performance to be a function of the distribution of power between important groups in society. Khan argues that the political settlement – defined as "the interdependent combination of a structure of power and institutions at the level of a society that is mutually 'compatible' and also 'sustainable' in terms of economic and political viability" is the key determinant of institutional performance and consequently, economic growth. While there are strong similarities here in Khan's notion of political settlement and AR's concept of political equilibrium (both take political power and institutions to be inter-dependent and both take institutional form and functioning to be determined within the political settlement/equilibrium), there are differences as well – Khan's treatment of the way a political settlement emerges suggests a more dynamic view of how elites come to a settlement on the type of institutions that are compatible with the balance of power, and how these institutions may be enforced. In Khan, a political equilibrium which leads to very poor economic performance is not likely to last, and there would necessarily be a move to an equilibrium which is compatible with an institutional configuration that delivers better economic performance. In this sense, Khan truncates the set of AR political equilibria (if ordered continuously from bad to good equilibria from left to right) on the left – bad equilibria, while a theoretical possibility, is not likely to persist, and therefore, not an equilibria in the dynamic sense. Khan does not define what the minimum level of economic viability for a political settlement may be, which suggests that the difference between the two concepts will not differ greatly in empirical terms (and as AR would argue, bad political equilibria have shown a tendency to persist for a very long time in history).

In Khan's notion of political settlements, institutions and the distribution of power have a circular and interdependent relationship. Khan defines power as holding power – that is, "how long a particular organization can hold out in actual or potential conflicts against other organizations or the state" and where holding power is "a function of a number of characteristics of an organization, including its economic capability to sustain itself during conflicts, its capability to mobilize supporters to be able to absorb costs and its ability to mobilize prevalent ideologies and symbols of legitimacy to consolidate its mobilization and keep its members committed" ((Khan 2010, p. 20). The relationship between holding power and institutions is two way. The configuration of holding power at the level of society is supported by a range of formal and informal institutions that reproduce and sustain the specific configuration of relative power between organizations by enabling a consistent set of economic benefits to be created and allocated. In turn, relative power determines which institutions emerge, whether institutions are enforced, and what their effect is on economic performance. If the distribution of benefits by a particular institution is not accepted by groups who have high holding power, there would be opposition to the introduction of the institution or its enforcement would be contested, leading to a possible increase in political instability, even though the institution may be growth-enhancing.

Khan's most important contribution to our understanding of the political dynamics of economic growth is the primacy he accords to informal institutions in the beginning of the growth process. Khan argues that the inherited distributional power cannot be supported by the incomes generated by formal institutions alone, and that "informal institutions play a vitally important role in all developing countries because informal institutions are the only feasible mechanism for sustaining economic benefits for powerful groups who would otherwise have lost out" (Khan 2010, p. 26). The reason why formal institutions play a less important role in developmental transitions is that those with holding power will have few of the capabilities that could benefit from protection of property rights and the rule of law, and would therefore have little interest in enforcing these institutions. It is informal institutions, then, that are compatible with the incentive structure of powerful elites, who can use these institutions to have continued access to incomes through 'political accumulation'.

Khan defines a clientelist political settlement as a political settlement where significant holding power is based on sources outside the incomes generated by formal institutions. Khan contrasts this with a capitalist political settlement, where capitalist profits are the dominant source of holding power, and argues that clientelist political settlements are likely to be the type of political settlement prevailing in developing countries, where the formal sector tends to be small, and much of the holding power of important groups are held outside the formal sector. While capitalist political settlements are more of a heuristic device for Khan since they are not likely to emerge in most developing countries till a late stage of economic development. It is more realistic to see political settlements in developing countries as hybrid in nature, with a combination of elements of both clientelist and capitalist settlements. This is for two reasons – one, in many developing countries, there are already existing productive formal sectors for reasons of history (due to colonization strategies and past import substituting industrialization policies), and two, with some economic growth occurring, there would be demand for formal institutional change (or the enforcement of formal institutions where they exist) originating from many new agents in the productive sectors of the economy.[8]

According to Khan, clientelist political settlements are more likely to characterize growth accelerations. Under these settlements, patron-client networks – informal relationships or organizations that involve individuals with different degrees of power – are likely to provide the institutional context within which credible commitment problems to do with investment can be addressed in an environment where formal institutions of property rights are either not there or are not likely to be enforced. In a typical patron-client network, the patron (who could be a politician or a local mafia, for example) is an organizer of power who organizes group of clients “who offer their organizational support in exchange for the benefits that the patron offers” (Khan 2010, p. 60). Patron-client networks can operate as informal networks or be within formal organizations such as political parties. Khan suggests that patron-client networks can be organized as pyramids, whereby an individual or faction can be a patron of one network and client of another network. The hierarchical structure of these networks and the elements of control exercised in each level of the pyramid allows for patron-client networks to be self-sustaining and therefore, credible to productive entrepreneurs that the rents from the investment process will not be completely expropriated. Therefore, patrons in the network offer local enforcement and dispute resolution activities to their clients – the investors – in return for political support and the rents that accrue from the production process.

But why do patron-client networks not degenerate into predatory networks, where the level of rent extraction is so high, that investors have little incentive to invest, or where patrons expropriate the productive assets of investors (or where investors fear that expropriation will occur at any point in the production process). Khan argues that the structure of the ruling coalition is important in explaining why some patron-client networks have greater enforcement capabilities than others. Two dimensions of power matter in understanding these capabilities. First, the horizontal distribution of power, which is the power of the ruling coalition relative to the power of excluded coalitions. Second, the vertical distribution of power, which is the relative power of

[8] For example, Steer and Sen (2010) show that in the case of Vietnam, as economic growth accelerated and the private sector increased in size, there was an increasing recourse to courts and other formal dispute settlement procedures, even though these institutions did not play an important role in the initial period of economic growth, where informal institutions such as relational contracting through friends and family were more important in the risk management process around economic transactions.

higher compared to lower level factions within the ruling coalition. We show the various possibilities for the horizontal and vertical distribution of power in a 2 X 2 matrix in Table 2.

The most favourable combination in terms of the enforcement capabilities of the ruling coalition is when the ruling coalition faces low opposition from excluded factions and lower level factions of the ruling coalition are weakly organized (the top left cell in the 2 X 2 matrix in the table). In this case, the ruling coalition can take a long-term view on economic growth. With limited power from lower level factions, the ruling coalition is able to exercise control across the entire pyramidical structure of the network to make sure that the network does not turn predatory. In this case, patron-client networks can be self-sustaining and growth focused. A concentrated horizontal distribution of power coupled with dispersed vertical distribution of power leads to a vulnerable authoritarian coalition that is always in the danger of being overthrown (top right cell in Table 2), while a concentrated vertical distribution of power coupled with dispersed horizontal distribution of power leads to a weak dominant party that may be growth oriented, but is unable to obtain 'buy-in' from the different lower level factions in using rents productively for growth (bottom left cell in Table 2). Finally, Khan argues that dispersion in both horizontal and vertical distribution of power can lead to 'competitive clientelism', leading to cycling of factions in power and in the shortening of the time horizon of patrons, leading to possible predation and a lack of economic growth (bottom right cell in Table 2). Therefore, it is only when the distribution of vertical and horizontal power are both concentrated in the ruling coalition that we would expect growth-oriented patron-client networks to emerge and be sustained over time.

Table 2: The distribution of horizontal and vertical power in Khan's theory of economic growth

<table>
<tr><th colspan="2" rowspan="2">Vertical/horizontal distribution of power</th><th colspan="2">Horizontal distribution of power: power of excluded factions</th></tr>
<tr><td>WEAK (Low opposition from excluded factions gives ruling coalition stability and long time horizon)</td><td>STRONG (Interests of Ruling Coalition weakly aligned with growth)</td></tr>
<tr><td rowspan="2">Vertical distribution of power: power of lower level factions</td><td>WEAK (Ruling Coalition has strong implementation capabilities)</td><td>Potential developmental coalition</td><td>Vulnerable authoritarian coalition</td></tr>
<tr><td>STRONG (Ruling Coalition has weak implementation capabilities)</td><td>Weak dominant party</td><td>Competitive clientelism</td></tr>
</table>

Source: Adapted from Khan (2010)

While Khan provides a powerful theory on why patron-client networks can be growth-enhancing, and not degenerate into rent-dissipating entities as often viewed in the literature on economic development (e.g., Krueger 1974), there are also some limitations in Khan's theory of economic growth. Firstly, it is not clear how dominant ruling coalition which has both significant vertical and horizontal power would necessarily be growth oriented. What prevents the coalition not to use its considerable power to use extractive institutions for its own ends and to maintain an optimal rate of rent extraction which may not lead to a growth collapse, but will not lead to stable/miracle growth as well? The sanction mechanisms here are weak in the absence of a third party enforcer and the ability of the ruling coalition to be growth oriented would depend on the coalition's own long-term self-interest to maximize wealth, or in the vision of long-term development among the elites who constitute the coalition (and therefore, exogenous to Khan's theory). Secondly, it is not obvious why competitive clientelism – that is, the cycling of factions in power -would necessarily lead to poor growth outcomes if it is a high expectations political equilibrium, where citizens expect certain critical public goods such as roads, education and health to be provided, regardless of the faction in power. Thirdly, it is not clear how the overcoming of coordination failures can take place in clientelist political settlements when the ability of the state to 'pick winners' and to monitor the performance of firms needs a certain degree of bureaucratic capacity, and a relative autonomy of the state from the investor class (Evans 1995). It is more likely that the character of the political settlement underpinning economic growth changes from a pure clientelist political settlement to hybrid political settlements where formal institutions and formal organizations (both an effective economic bureaucracy and well organized and representative business associations) are increasingly important in resolving coordination failures (Bräutignam, Rakner and Taylor 2002). Finally, Khan downplays the role of high quality public good provision (including a literate and skilled workforce and no infrastructure constraints) that have been seen as important determinants of economic growth in the empirical growth literature, and it is difficult to see how public goods such as education, health and infrastructure can be provided through patron-client networks which by their very nature are exclusionary.

The above discussion suggests that Khan's theory of the politics of growth is a more convincing theory of growth acceleration than it is a theory of growth maintenance. Informal institutions and patron-client networks may be crucial in igniting growth and formal institutional reform may have little growth enhancing effects in clientelist political settlements. But for growth maintenance, it would be necessary for formal institutions to develop, as well as a more effective bureaucracy, as the political channels of the overcoming of co-ordination failures and the provision of high quality public goods become the primary mechanisms by which political factors determine growth sustenance.

5. Reviewing the empirical literature of the politics of economic growth

What does the large and ever-expanding empirical literature on the determinants of economic growth tell us about the political factors that determine the transition from one growth regime to another growth regime? A recent set of papers in the empirical growth literature has tried to go beyond the proximate determinants of economic growth (such as macroeconomic stability and trade open-ness) to study the fundamental causes of economic growth across countries, and in particular, the importance of economic and political institutions. Barro (1997)'s work was seminal in the empirical growth literature, in trying to bring in two measures of institutional quality – political stability and the rule of law index – among the determinants of growth of GDP per capita. In Barro's empirical implementation of the neoclassical growth model, a higher degree of political stability and a greater presence of the rule of law have a positive effect on the investment rate, which leads to higher economic growth. However, a major weakness of Barro's work is the possibility of reverse causality – countries that grow faster will tend to adopt better institutions and be more politically stable. It is only with a landmark paper by Acemoglu, Johnson and Robinson (henceforth, AJR, 2001) that a serious attempt was made to control for the possibility of reverse causality in establishing a causal role for institutions in economic development.

To estimate the impact of institutions on economic performance that does not lend itself to interpretations of reverse causality, AJR need a source of exogenous variation in institutions. To do this, they propose a theory of institutional differences among countries colonised by Europeans, and exploit this theory to derive a possible source of exogenous variation. Their theory rests on three premises. Firstly, there were differences in colonisation policies which created different sets of institutions. At one extreme, European powers set up 'extractive' institutions, exemplified by the Belgian conquest of the Congo. These institutions did not introduce much protection for private property, nor did they provide much checks and balances against government expropriation. The main purpose of these extractive institutions was to transfer as much of the resources from the colony to the coloniser. These institutions were detrimental to investment and economic development. At the other extreme, many Europeans migrated and settled in a number of colonies, where they tried to replicate European institutions, with strong emphasis on private property and checks against government power. These institutions enforced the rule of law and encouraged investment. Primary examples of this include Australia, Canada, New Zealand, and the United States. Secondly, the colonisation strategy was influenced by the feasibility of settlements. In places where the disease environment was not favourable to European settlement, the formation of extractive institutions was more likely. The final premise of AJR's theory was that the colonial state and institutions persisted after independence. This is because the political elite that came to power at independence in the previously colonised countries had a strong self-interest in maintaining the extractive institutions established during colonial times and the access to revenues obtained from the control of these institutions.

AJR validate their theory by regressing current economic performance (log GDP per capita in 1995) against current institutional quality (the average protection against expropriation risk for the period 1985-1995), and by instrumenting the latter by the settler mortality rate during the colonial period compiled by the historian, Philip Curtin. The settler mortality rate is an indirect measure of the disease environment in the colonies, and thus, measures the likelihood of Europeans settling in a particular colony and setting up institutions of private property. AJR find that there is a high correlation between the mortality rates faced by soldiers, bishops and sailors in the colonies and European settlements and early measures of institutions, and between early institutions and current institutions. AJR estimate large effects of institutions on income per capita using this source of variation. They also find that this relationship is not driven by outliers, and is robust to controlling for latitude, climate, current disease environment, religion, natural resources, soil quality, ethnolinguistic fragmentation, and current racial composition.[9]

An important criticism of the quantitative work in the AJR genre comes from Khan (2012) who argues that while measures of institutional or governance quality used in this body of work may be strong, positive correlates of long-run per capita income, they are less important in explaining why some countries experience economic growth and not others. As Khan notes, for the same level of institutional quality, we see very different growth experiences among developing countries. Since the measure of institutional quality used in the AJR genre captures in essence how well formal institutions are functioning, what the cross-country econometric work in the AJR tradition establishes is the strong positive relationship between the quality of

[9] Two more important papers in the AJR genre are Rodrik, Subramanian and Trebbi (2004) and Hall and Jones (1999). The first paper addresses the three standard ‘deep determinants’ of economic prosperity across countries - geography, institutions and integration. find that institutions overwhelmingly trump integration, and do slightly better than geography in explaining cross-country variations in income per capita. The second paper find that differences in institutions and government policies, which the authors call social infrastructure, is the prime determinant of differences in capital accumulation and productivity, and therefore, per capita income across the 127 countries (both developed and developing) in their sample. Hall and Jones measure social infrastructure by the government’s ability to protect against private diversion of economic activity (higher ability being proxied by a higher rule of law, better bureaucratic quality, lower risk of expropriation, less corruption and less risk of government repudiation of contracts) and by the open-ness of the economy (measured by lower trade barriers and lower distortions in the foreign exchange market). Both papers address the endogeneity concerns with institutional quality as an explanatory variable by the use of appropriate instrumental variables strategies.

formal institutions and long-run economic growth. Therefore, well-functioning formal institutions may not be important determinants of growth accelerations, though these institutions may be important in the growth sustenance process, and in the long-run evolution of per capita incomes.

While the previous cross-country econometric literature on the institutional determinants of economic growth has mostly focused on the determinants of long-run per capita income differences and less on within-country growth, there is an emerging quantitative literature on the determinants of growth accelerations, and why some countries maintain high growth while other countries witness growth collapses. With respect to growth accelerations, Hausman, Pritchett and Rodrik (2005) find that standard growth determinants such as major changes in economic policies, institutional arrangements, political circumstances or external conditions “do a very poor job of predicting the turning points” (p. 328). They argue that growth accelerations are caused predominantly by idiosyncratic and often, small-scale changes. Pritchett (2000) points out that slow moving determinants of growth such as improvements in the quality of institutions or time-constant factors such as geography (land-lockedness, distance from the equator), resource endowments (e.g. minerals), ethnic diversity, culture and colonial experience are less likely to explain the frequent shifts from one growth regime to another that we observe in many developing countries and the wide variations in within-country economic growth.[10] Jones and Olken (2008) show that growth accelerations are accompanied by increases in productivity and not investment, and with increases in trade, suggesting that reallocation of resources from less productive to more productive uses are an important part of growth accelerations. Growth declines, on the other hand, are associated with monetary instability and increases in inflation, along with higher frequency of military conflict, and trade does not play an important role in growth declines as it does in growth accelerations. Jones and Olken also find changes in institutions are not associated with either growth accelerations or declines, where institutional quality is measured by a lower level of corruption and better rule of law. However, they find that growth accelerations and declines are more likely to occur in autocracies than democracies. On the other hand, Berg, Ostry and Zettelmeyer (2012) find that growth duration (that is, the avoidance of growth collapses) is positively related to the presence of democratic political institutions in the country,

[10] These findings have been extended in by a recent paper by Kerekes (2012) which shows using modern time-series methods that the level of institutional quality does not differentiate moderately successful countries from failing countries while successful countries are characterised by better initial conditions and institutions.

along with the degree of equality of income distribution, export orientation and macroeconomic stability.[11]

Using Markov switching time-series techniques and calculating the transition probabilities around growth regime switches, Jerzmanowski (2006) finds that better institutional quality improves the possibility that a country will remain in a stable or miracle growth regime and will be less likely to suffer a growth collapse. Thus, a country such as Korea, with a high quality of institutions would have a 74 per cent probability of remaining in a stable or miracle growth regime, and the ability to recover from a crisis to miracle growth is high at 43 per cent probability. On the other hand, for a country with a low quality of institutions such as Nigeria, while the probability of being in stagnation or crisis is high at 82 per cent, there is still a 14 per cent chance that Nigeria can move out of a growth crisis to miracle growth. These findings suggest that while growth accelerations may occur in countries which have weak institutions, the latter may limit the sustainability or maintenance of economic growth.

The large N studies on the institutional determinants of economic growth discussed so far do not address what are the underlying characteristics of the political settlement within which growth-enhancing institutions emerge and growth accelerations occur. Small n country case-studies are more likely to provide a better understanding of the political factors that trigger growth accelerations. For example, Bräutignam, Rakner and Taylor (2002) highlighted the role of 'growth coalitions', which are coalitions of business and political elites that are underpinned by synergistic relations and which mobilise institutions and resources for economic growth, in explaining growth successes of countries such as Mauritius in the African context.[12] Similarly, Abdel-Latif and Schmitz (2010), in their study of the political determinants of sectoral differences in investment and growth outcomes in Egypt, show that informal alliances between business and politicians, built around strong social ties, and based on common interest in the sector's growth and a common

[11] A similar finding is obtained by Goldsmith (1995) who show that democratic institutions are associated with growth in a sample of 59 developing and transitional countries in the 1980s and 1990s.
[12] One important criticism of small n case-studies in the politics of growth literature is that they pay insufficient attention to issues of causality – do growth coalitions cause economic growth, or do they simply growth in that they tend to emerge once economic growth accelerates (Brady and Spence 2009)? Jones and Olken (2005) address this issue by using death of leaders as a source of exogenous variation in leadership and find robust evidence that leadership matter for economic growth. They also find that the effects of leaders are strongest in autocratic settings where there are fewer constraints on a leader's power. Similarly, Poteete (2009) shows that the formation of a stable and inclusive political coalition pre-dated the beginning of the long period of economic growth in Botswana.

understanding of the sector's problems, can explain why there were positive investment and growth outcomes in some sectors in Egypt and not in others. The findings of these studies provide further support for the proposition that informal institutions in the form of loose and informal alliances between politicians and investors, are more important in growth accelerations, as compared to improvements in formal institutions around better rule of law and better developed property rights systems.

6. Concluding observations

This survey article assessed what we know about the role of political factors in explaining why some countries growth faster than others. We began with a fresh look at the "stylized facts" of economic growth, and identified an important limitation in the past literature on the stylized facts of growth in that their focus on rates of **average** growth of per capita income, has obscured the fact most countries observe dramatic fluctuations in growth of per capita income. We suggested that there is a need to shift away from much of the previous literature's emphasis on the determinants of long-run *average* economic growth (including political determinants), to an understanding of the determinants of within-country growth patterns. We proposed that the key question that a research agenda on the political drivers of economic growth must address is an understanding of the political dynamics around the transition from one growth regime to another.

We then developed a simple framework for understanding the political dynamics of growth transitions. We discussed three key political channels to economic growth – institutions of credible commitment, the provision of public goods and the overcoming of coordination failures, We argued that these three channels play out differently across different phases of economic growth. Institutions of credible commitment may be a necessary and sufficient channel to growth accelerations while contributing to growth maintenance as well. Informal institutions of credible commitment may play a more important role in growth accelerations, as opposed to formal institutions which may be more important in growth maintenance. The provision of public goods would be more important in growth maintenance and in the avoidance of growth collapse, though it can also play some role in growth accelerations. The overcoming of coordination failures would be more important in growth maintenance, and can be expected to play an insignificant role in growth acceleration.

We reviewed two dominant theories of the politics of growth – those of Acemoglu and Robinson and of Khan. We argued that there are strong similarities in both theories in their emphasis on the political settlement/equilibrium as the key political driver of economic growth. However, the theory of Acemoglu and Robinson, with its emphasis on inclusive economic and political institutions, may more relevant for growth maintenance, while the theory of Khan, with its emphasis on informal institutions and patron-client networks, is more relevant for growth acceleration. Neither Acemoglu and Robinson nor Khan are able to provide a unified theory of understanding the political drivers of growth acceleration as well of growth maintenance/non-collapse. There is a need for further theoretical development around the explanation of the political transitional dynamics around growth regimes switches that encompass both growth accelerations and growth maintenance.

Our review of the empirical literature on the political and institutional determinants of economic growth complemented the main conclusions that we drew from the review of the theoretical literature. The cross-country econometric literature on institutions and growth suggest that there is a positive relationship between institutional quality and the level of income. However, there is less support for the proposition that better formal economic and political institutions such as a good property rights regime or the prevalence of democracy are either necessary or sufficient to obtain growth accelerations. Our review of the literature on the determinants of growth accelerations and growth maintenance also support this conclusion – these studies find that reforms in formal economic institutions do not seem to be associated with growth accelerations, and that the latter is more likely in a country with a non-inclusive political institution such as autocracy. However, this literature finds that a country which has witnessed growth acceleration is more likely to stay in a high growth regime and not suffer a growth decline if better quality formal institutions were to emerge and develop in the growth process.

Both our review of the theoretical and empirical literature supports the proposition that the political drivers of growth acceleration are different from the political determinants of growth maintenance. But it still leaves open several important unresolved questions in our understanding of the political dynamics of economic growth. What are the political drivers of growth accelerations? Are these more related to informal institutions of credible commitment and patron-client networks? What are the political drivers of growth sustenance and growth collapses? Are these more related to the emergence (or non-emergence) of inclusive economic and political institutions, the provision of public goods and the overcoming of co-ordination failures? What explains the transition from political equilibrium/ settlement characterizing a growth acceleration to an equilibrium/settlement characterizing a growth sustenance? To what extent is the transition endogenous to the political dynamics? And how do economic and political institutions jointly evolve from the set of institutions that are causal to growth accelerations to the set of institutions that allow growth to be maintained?

The literature on the determinants of economic growth has moved a long way from being pre-occupied by proximate determinants of growth such as human capital formation, macroeconomic stability, and trade openness to more fundamental causes such as economic institutions, which in turn are increasingly seen to be shaped by political factors. The task of future research in this area should be to better understand why it is rare to see growth episodes being sustained in the developing world, and how political processes and institutions can explain the differential success that developing countries have, both in igniting economic growth and in transforming growth accelerations to growth sustenance.

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