Is development a function of your ethnicity?


Main Findings:

Overwhelming empirical evidence that suggests that the public goods provision is lower in fragmented societies but contentious on whether productivity is positively related to diversity in the population (heterogeneity vs. homogeneity)
This Lecture

Is development a function of the quality of your government?

How did some countries have good government and others did not? How does history influence government performance? Quality of Government (La Porta et al, 2005)

- Using data on government performance from a large sample of countries evaluating 3 theories: economic, political and cultural determinants of government performance.
Quality of Government (La Porta et al)

Method: testing empirical determinants using a large cross-section dataset

Main Findings: Countries that are poor, close to the equator, ethnolinguistically heterogenous, use French or Socialist laws, or have high proportions of Catholics or Muslims exhibit inferior government performance. Large governments tend to be better performing ones. (Look at which countries exhibit this and compare to their economic performance)
What is a good government?

- Institutions good for capitalism

- Security of property rights – lack of intervention by the government, benign regulations, low taxation – as the crucial metric of good performance.

- Other features of good government?
Competing Theories of Determinants of Good Government

Economic theory– institutions are created when it is efficient to create them; when the social benefits of having institutions exceed the transaction costs for doing so

Demzets 1967, North 1981

Political – focus on redistribution rather than efficiency; policies and institutions are shaped by those in power to stay in power and to transfer resources to themselves (class or organized interests); government policies are inefficient because their creators want them so. (examples in history; how important is the design of bureaucracies?) (ability to extract rents)

Marx 1872, North 1990, Olson 1993
Competing Theories...(continued)

Cultural – societies hold beliefs that shape collective action and government; some are distrustful and intolerant that government simply cannot function properly; trust in strangers are essential for distribution of public goods (Why?); Discuss example of Italy and the Catholic Church

Implications and Exogenous Measures of Variation

Economic Theory – scale of economic activity expands, better institutions become more affordable; better government in turn improves economic performance and therefore expands economic activity so the ‘scale of economic activity’ is endogenous. What is the problem with this?

Political Theory – the essence of the theory is political divergence; measured by ethnic heterogeneity and how else? Why are these measures appropriate?

Cultural Theory – use religion as a proxy for work ethic, tolerance, trust and other characteristics
Questions

Why look at 3 different theories?

Isn’t per capital income enough to explain bad governments? Poor country, they can’t afford it, etc
Dimensions of Government performance

- Non-interventionism
- Quality of the bureaucracy
- Public goods provision essential to development (high quality vs. high expense)
- Government expenditure on transfers, consumption and public sector employment
- Democracy and political rights
How do we measure this?

- Look at historical predetermined variables (why?)
- Per capital (reverse causality)
- Political; ethnic heterogeneity (why; how does this variable undermine the production of good governments and ultimately economic performance?);
- Legal origin – socialist, civil, common law (what are the differences between legal traditions? And what do they measure (proxy of)?); how does it effect public goods provision? (endogenous?)
- Cultural: religion particularly Catholic and Muslim as bad for development. Why?
- Simple causal relationships are useful but do not explain properly
Reading the Empirical Results

The Data

Table 1 summarizes the definitions and sources for all variables used in the paper. 152 countries and a combination of large data sets from the 1990’s.

Measuring government intervention – index of property rights protection; index of the quality of business regulations, tax rate.

Measuring government efficiency – survey scores on corruption, bureaucratic delays and tax compliance, relative wages of government officials

Measuring the output of public goods – infant mortality, school attainment, illiteracy and infrastructure quality

Size of the public sector – transfers and subsidies, government consumption, size of the state owned enterprises and public sector employment
Table 2 Results

High correlation between government performance measures

Positive correlation between property rights protection and business regulation (high taxes are not necessarily a sign of an inferior government)

Corruption correlated with bureaucratic delays

Tax compliance positively correlated with bureaucratic delays (what is the explanation of this?) (delays create the opportunities for rents)

Corruption is negatively correlated with relative wages of government officials (contrary to the view that higher pay for bureaucrats will solve the corruption problem)

Measures of public good output are highly correlated with each other

Countries with good public goods are also the ones with efficient government, low relative government wages and less intervention (except for high top tax rate).

Size of government measures are correlated with each other except for SOE index

Countries with bigger government consumption, transfers and labor are less corrupt, have fewer b-delays and better provision of public goods but also higher tax rates

Figure 1 and 2 present the scatter plots show bigger governments perform better. **Larger governments tend to be the high quality ones is one of the key findings.**

Measures of democracy and political rights are highly correlated. Freer governments are larger, more efficient, intervene less and provide better public goods.
Table 3 results

Correlations between the independent variables (3 broad factors that may be related to government performance) (what are their findings?)

- Ethnolinguistical fractionalization (-)
- The origin of commercial laws
- Religious composition of the population (-) with legal
- Latitude (why?) and per capital income as control variables
Results (continued)

- Table 4 – EF and legal origin are independent variables
- Table 5 includes religious affiliation and EF
- Table 6 EF, legal, religious are all together (differences is about correctly specifying the model)
- Table 4: per capita has a strong positive effect on govt performance, richer countries are less interventionist in that they protect property rights and regulate better, high tax rates; richer countries are better at distributing public goods
- Table 5 EF has consistent adverse effect on government performance, captures political theory that EF captures predisposition of ethnic groups in power to redistribute. Explanatory power lessens when you control for latitude and government performance (means its not a driver of underdevelopment)
Legal origins: Table 4: socialist law was predicted by the political theory but they do well on public goods provision, more interventionism, less efficiency, bigger government transfers and less democracy.

Civil law – more interventionism (have higher top rates, less secure property rights and worse regulation); less efficiency by having high b-delays and tax compliance but low on corruption; pay high wages to bureaucrats than common law countries but does not buy them high government efficiency. Fall behind on the provision of public goods and score worse on democracy and rights than common law countries. Predicted by political theory.

Scandinavian origin performs the best.

Table 5 reports religious affiliation on government performance.
Results (continued)

- Reports that Catholic and Muslim countries have the worse performing economies but results become insignificant when latitude is controlled for.
- Catholic countries are generally more interventionist, less efficient, more corrupt but better paid. They do worse on public goods provision, smaller transfers and less democratic.
- The effect of Muslim affiliation is generally same as the Catholic one particularly negative on public goods provision, and misuse their power; poor govt performance and low tax rate.
- Both legal and religion might have lead to hostile market formation.
- Final step, run a complete specification. Table 6 presents results. EF important determinant of government performance. Legal origins exert significant negative influence on government performance, religion becomes insignificant (not a driver). Static laws are a more robust predictor of performance.
- Colonial status? Tackled in the next lecture.
Conclusion

Thoughts on this article?
Next Lecture

Is development a function of your colonial history?

‘The Colonial Origins of Comparative Development’ (June 9, 2011)