

1-1-2015

## Book Review of: Why nations fail

Ashutosh Mani Dixit

Follow this and additional works at: <https://ir.iba.edu.pk/businessreview>



Part of the Finance Commons, Political Economy Commons, and the Public Economics Commons



This work is licensed under a [Creative Commons Attribution 4.0 International License](https://creativecommons.org/licenses/by/4.0/).

### Recommended Citation

Dixit, A. M. (2015). Book Review of: Why nations fail. *Business Review*, 10(1), 194-200. Retrieved from <https://doi.org/10.54784/1990-6587.1323>

This article is brought to you by *iRepository* for open access under the [Creative Commons Attribution 4.0 License](https://creativecommons.org/licenses/by/4.0/) and is available at <https://ir.iba.edu.pk/businessreview/vol10/iss1/15>. For more information, please contact [irepository@iba.edu.pk](mailto:irepository@iba.edu.pk).

**BOOK REVIEW**

**WHY NATIONS FAIL: A REVIEW ARTICLE**

Ashutosh Mani Dixit

Daron, A & Robinson, J 2012, *Why Nations Fails: The Origins of Power, Prosperity, and Poverty*. 1 st ed. New York: Crown.

From the time of eighteen century economist Adam Smith to contemporary researchers, the question ‘What enables countries for economic success?’ is still an open issue. Policy makers and economic scholars have spent years on research and dedicated themselves into developing path breaking theories and equations, but the question still remains unanswered. Theories started with classical economist claiming ‘capital formation’ as key for economic growth, than Neo classical economist emphasized on technology and production function, than evolved new growth theory claiming the notion of endogenous growth models (Perkins et al. 2012, p.101-103). As theories on economic and development growth evolved, M.I.T. economists Daron Acemoglu and the Harvard political scientist James A. Robinson, published book ‘Why Nations Fail’ in 2012 after ten years of extensive research. In the book, the authors vehemently advocate that the key determinant for economic success and failure of a nation is political and economic ‘institutions’. Authors argue that nations flourish in ‘inclusive’ political and economic institutions, and they fail under ‘extractive’ institutions with power concentrated in the hands of few.

The purpose of this article is to assess the contribution of *Why Nations Fail* about its forefront claim that institution is exclusive determinant of nation’s economic outcome. This paper will examine its findings and put forward arguments and claims of prominent studies about economic development. The paper has been organized in two more section. Immediate section presents chapter wise summary of the book highlighting strengths and key outcomes.

While the third section, which is the purpose of the article, offers a critique, than sums up in final section providing some concluding comments

**The Book**

*Why Nations Fail* is structured in fifteen chapters. Chapter 1 starts with the example of two cities Nogales United States (US)/Mexico, explaining how difference in nature of institutions divergently affects performance of two demographically similar states. Authors traces historical conquest of Spanish and English on South and North America to elaborate the difference, and claims that historical contingencies had significant role in shaping the political landscape and had prolonged effect even centuries later on two nations (Acemoglu and Robinson 2012, p.21). Further they illustrate that sound institutional platform has brought economic progress in the United States, whereas colonial legacy and its authoritarian politics has restricted entrepreneurship; weaken property rights and discouraged ideas in Mexico (Acemoglu and Robinson 2012, p.53). In pursuit of further explaining the role of institutions and governance, authors put forward different theories that exemplifies geography, cultural and ignorance as decisive factor in outcome of nation. Progressively each of these hypothesis is refuted by the authors (Acemoglu and Robinson 2012, p.62-82). They advocate that the difference in economic trajectory of Koreas, Nogales, or East and West Germany can only be explained by quality of political institutions at work. Further Acemoglu and Robinson argues that political hegemony vested on the hands of few lead identical regions to unproductive

economic activity, and ultimately as failed nation. Overall chapter 2 advocates that decentralization of powers in political system are imperative to have an affluent nation; and argues that theories on geography, cultural and ignorance are weak in explaining the difference in economic growth between countries.

Chapter 3 begins with history of political institutions operating in North and South Korea, and claims that economic prosperity in South Korea unlike North is complemented by inclusive economic institutions. However authors acknowledge that some nations prospered under extractive institutions by allocating resources into short lived productive ventures, but render limited social benefits (Acemoglu & Robinson 2012, p.88-98). They argue that economic growth under extractive political institutions are temporary, and are prone to collapse from consequence of infighting generated between themselves. Soviet Russia (USSR), a nation built upon extractive political institution and its collapse is a country case authors put forward to support the argument.

Chapter 4 unfolds key historical events (coined as critical junctures) that shape the path of economic development. It builds up analysis on the critical juncture like Bubonic plague catastrophe (1346 A.D) originated from China, and illustrates political and institutional change that ascended from shortage of labour due to spread of the catastrophe (Acemoglu and Robinson 2012, p.111-12). As a whole, chapter underscores that small institutional change in the historical juncture magnifies over the time, and as a result nation grossed diverse path of development.

Chapter 5 highlights the evolution of USSR under Stalin and Gosplan's Five Year Plans, and advocates that demise of USSR was result of extractive institutions and inefficient allocation of resources (Acemoglu and Robinson 2012, p.141-147). Aligned to the case they make a bold statement that China is on the same trajectory and its fate is no different from USSR. Authors also examines the evolution of tribes Bushongs and Leles (separated by a river), and explains that institutionally weak Lele were poor and disputed whereas the Bushong were rich and had advanced technologies. Overall chapter reiterates the notion of economic growth and extractive institutions, and advocates that economic growth under extractive institution is not sustainable.

Chapter 6 outlines homogenous characteristics that Venice and Ancient Rome, Ethiopia and Mayan city-states shared in their evolution pattern and explains how extractive nature of political institutions led them to failure. However authors acknowledge that there were time when those states had some degree of inclusive institutions that provided incentives for growth. But when authoritarianism shadowed the system and elites illicitly used the power conflicts emerged and the downfall of the societies began (Acemoglu and Robinson 2012, p.168-171). Chapter 7 begins with case projecting regressive thought of ruling elites in England who feared creative destructions. It then highlights the history of England from signing of Magna Carta to failed absolutism of Stuart king. Overall chapter underscores inflection point of England from extractive institution to more inclusive institutions with vivid illustration of glorious and industrial revolution.

Not all nations learned from the industrial revolution of England neither they followed the path of rapid development till distant future. In Chapter 8 authors explain that it is due to the critical juncture in the history which lead minions of Ottoman Empire to be relatively poor for centuries and abstained them from growth. Revolt against influential never grew so strong in the Ottoman Empire and neither there was environment for inclusive

institutions. Ottoman Empire feared the possible uprising from technological adaptation, so instead of embracing the change they restricted it, and same was case with countries akin China, Spain, Russia and Hungary (Acemoglu and Robinson 2012, p.230-236).

Beginning of chapter 9 emphasize exploitation and underdevelopment of the Southeast Asia in seventeenth century, it talks about genocide of Spice Islands, and East India Company's contract of Ambon. Later most part of chapter draws attention on one of the important theory in economics 'Dual economy model' by Sir Arthur Lewis. Authors argue that dual economy is moulded by colonization and it is a channel through which extractive institutions sustains (Acemoglu and Robinson 2012, p.299). Chapter 10 describes variegated evolutions of different countries, from establishment of institutions and political system in Australia, revolution and introduction of inclusive institution in France to westernization of institution in Japan. Authors connect similitude in evolutions of these countries to conclude that they embraced inclusive institutions, progressively invited industrialization and enabled development (Acemoglu and Robinson 2012, p.316). Conversely, author advocates that some countries confined themselves to absolutism and monopoly and suffered repercussion of social inequality and regressive growth for long time.

Chapter 11 is about virtuous circles- chains of events that strengthens itself through feedback loop. Authors advocates that presence of inclusive institutions enables virtuous circle to initiate positive feedback and restrain elites from overpowering. Chapter cites an example of Black Act of 1772 in England (Acemoglu and Robinson 2012, p.345), the case that created a wave of positive cycle forming mechanism for right to vote and warranted level playing ground for prosperity. Similarly author briefs about the negative feedback loop and iron law of oligarchy in chapter 12, with multitude of cases from Sierra Leone, United States, Ethiopia, Guatemala and southern part of United States. Authors claims that these countries had no power checks and thus ruling elite had incentive for larceny. Author advocates that even in the case revolution dethroned the ruling elites, it is implicit from prevailed 'iron law of oligarchy' that a new elite would just replace the ousted and continue the appropriation. This is one of the reason why author doubts on possibility of move towards inclusive institutions even after Arab Spring.

Chapter 13 starts with case of extractivism in Zimbabwe under Robert Mugabe and his cronies, and elaborates the consequence of similar extractive interventions in Steven's Sierra Leone, Karimov's Uzbekistan and Kim Jong's North Korea. In one interesting case of Colombia authors describes that failure of Colombia was due to consequence of failing to set up inclusive institutions, albeit it had democratic elections. Addition to brief country case of US breaking the vicious circle (cited in chapter 12), another example authors cites about 'breaking the mould' is Botswana in Chapter 14. Endowment of natural resources (diamonds) did not create tussle over access of resource extraction and rent appropriation in Botswana. Authors claims that after colonial independence in Botswana, traditional elites and political party did not perform an extractive interventions at the cost of society because there was a perfect 'interplay between a critical juncture and existing institution' (Acemoglu and Robison 2012, p.454).

Initial part of chapter 15 comes back to the changing reforms in China and its probable future analogues to USSR under continued restrictive regime. Authors than focuses on foreign aid and advocates that international institutions cannot engineer prosperity with structural loan and conditional grants, but growth has to come by reforming towards inclusive institutions and empowerment of people. Chapter cites numerous examples on

failure of foreign aid; from funds channelled towards absolute regime in Africa to UN project of shelter restructuring in Afghanistan that unproductively smoked millions of dollars. Overall chapter highlights that nation's success lies in market liberalization, inclusive institutions and understanding of real problem, not in foreign aid and extractive regimes (Acemoglu and Robinson 2012, p.493).

### **Review**

The stated objective of the book is to advocate that 'Countries differ in their economic success because of their different institutions' (p. 88). Why Nations Fail is derived and extended version of Acemoglu and Robinson's academic paper 'The Colonial Origins of Comparative Development' that was co-authored with Professor Simon Johnson of MIT in 2000. Although authors put on ambitious statement with deep facts supporting chronological events that shaped the institutions and trajectory of nation, but it is hard to agree on all of them. However there are some important central themes that are interesting and convinces reader. Foremost, authors advocate that there are critical incidents in history of nation that lead to establishment of inclusive or extractive institutions -or to be specific success or failure. Deep illustration of evolution pattern has enabled this book to make valuable contribution in evolutionary theory and economics. It is interesting to read those small steps towards democracy; when Western Europe landlord competed for services of surviving peasants after Bubonic plague and land lord in Easter Europe cloistered themselves against contagious effect of labour shortage. In similar fashion it is informative to go through the post-journey after discovery of Americas and read how parliament prevented Elizabeth I and royal elites from monopolizing Atlantic trade. While in other side of the map Spanish elites monopolized the trade and ignored the citizen's demand, leading to different institution. Readers go through overwhelming facts to understand the history and diversity of economic growth and comprehend how government's reaction to momentous event can have lasting effect on nation's outcome at longer run. Another important view authors put forward is that passive institution and vested interest of governments is a road block for development. They highlight that government's interest on benefit of few is detrimental for growth of nation, so existence of sound pluralistic political institution is imperative to ensure level playing ground and accountability of government.

The arguments authors put on this book are based on research into hundred years of economic evolution. They have related each circumstances with role of institutions in economic outcome. But the breadth of the facts readers have to go through book is very rigorous and makes it challenging to validate each of them. The scope of coverage can be inferred from MacLeod (2013, p.121) graph which showed that each 100 pages of book takes leap of one century on an average. However there are some studies that are contrary to the claim put forward by book. Authors frequently claim that institutional drift and critical junctures has long run effect even centuries, but conversely study by Shleifer (2004, p.8-10) claims that 'institutions are highly volatile' and there is discontinuity on freedom pattern of the world after 19<sup>th</sup> century. Further there are reports from leading institutions highlighting that freedom in world has been increased by 40 percent in just 18 years and countries are becoming more liberalized despite ethos of the archaic institutions (Freedom House 2013).

However there some shortcomings in the book which deserves more attention , for one authors have ambiguously and repeatedly used inclusive and exclusive addressing economic and political institutions which is hard to comprehend and accept them to be exclusively imperative for economic development of nation. Further authors have confined

the scope of institutions and arguably marginalized weight of culture, informal institution and social characteristics as determinant for economic development by refuting cultural hypothesis. It is apparent from studies (Jutting, p.14) that there are different types of institutions, on basis of formality (formal and Traditional/Indigenous), hierarchy (Levels1-3) and area (Economic, political, law and social), which have a significant role to play in economic system. Jutting (2013) underscores that ‘development outcomes need to take into account the differences between exogenous and endogenous institutions, the local setting, the actor perspective and the existence of different levels of institutions with different time horizons of change’ (Jutting 2013, p.8). Similarly an article from Fukuyama (2006) in *The American Interest* highlights that beliefs, traditions, values and habits are imperative for function of formal institutions; centring formal institutions and failing to account cultural factors to analyse the development outcome is a not exclusively convincing, he claims formal institutions are shaped by informal institutions.

Next, authors bold argument ‘History illustrates that there is no simple or enduring connection between climate or geography and economic success’ is not convincing (p.63). Readers find it hard to comprehend that economic development is insulated from effect of geography and topographical characteristic of nation and challenges it exerts to technological diffusion. Studies have revealed that nation facing of escalating production cost and vicinity to global market (due to geographical constraints) have slow technological diffusion (Veisheh, 2010). Additionally if we look from the perspective of climate change and future development, developing economy which are most vulnerable to climate change (geography factor) has high probability of facing adverse situations on the road towards economic prosperity. In near future developing countries are the first which will face adverse effect of climate change and hit by hard environmental externality such as coastal erosion, floods and droughts (Warner and Gest 2013, p.373). So in the light of this fact it is naïve to ignore the role of climate change and geography in the trajectory of economic development.


Further to support the above argument this paper takes evidence from the work of one of the pioneer advocate of institutions and economic growth Douglas North and relate it to significance of geography theory. Douglas North’s in his paper ‘Ocean Freight Rates and Economic Development 1730-1913’ claims that decline in per unit cost of marine transport was significant factor for reviving interdependence of the world, opening up venue for developing countries and enabling migration and settlement (1958, p.2) . As per North (1958) global interdependence reduced ocean cost efficiently and channelled the raw materials from developing countries towards industrialized ones. If we relate this fact to claim put forward by Levinson (2006) that low freight rates and commercial use of ship containers further reduced the expense of international trade providing greater mileage for global partnership, we will get a picture that land lock countries were isolate from this opportunity. Further it is estimated that cost of containerization is three time less than cost of road transport; this pushed landlocked countries at even more cost disadvantage position (Levinson, 2006). This helps to understand why landlocked Nepal and semi landlocked Paraguay are among the poorest countries of Asia and America respectively, and why they have low volume of international trade. It is also makes vivid why Vietnam (ranking lower in freedom index- not only limited to geography) instead of landlocked Bolivia is preferred place to assembly line for Japanese and South Korean companies. In the light of this fact we can infer that those countries which were in proximity to ocean routes must have clear geography advantage, so Acemoglu and Robinson (2012) claim on direct causal relationship between institution and economic development is not solely convincing.

Acemoglu and Robinson (2012) analysis is based on history, critical junctures, institutional drift and past economic trajectory but it fails to answer what's next after inclusive institution. It is well articulated book on evolutionary economics and history, but the theory cannot provide satisfactory analysis on post revolution stage of movement like Arab Spring. It is well accepted that politics matters, and bad governments can indeed restrict development and bring forward 'Iron law of oligarchy'. But having said that it is equally important to account technological process, cultural, geography, innovations and technological diffusion, and the myriad ways through which these factors flow around the world and module the future events.

Authors pithily advocate that international donor organizations are trying to 'engineer prosperity' by structured aid and unproductive rehabilitation projects, rather than investigating and reforming the institution. But importance of foreign aid has been matter of debate from seemingly conflicting opinions and contours (Perkins 2012, p.499). While scholars like Sachs has been advocating the significance of aid and serially disregarding institutions importance, Easterly hails idea of strengthening institution and provokes notion of discouraging the aid dependency, but both agree on the point that geography position and countries endowment affect the economy through institutions (Easterly & Levin 2003; Sachs 2003). So author's brief introduction on malfunction of foreign aid is informative but not convincing to support the theme of book and refusal of other hypothesis.

Although there are different theories which are for and against the dominant role of institutions in economic development there claims are not yet fully justified. Perkins (2012) convincingly highlights that effective government and institutions along with favourable geography and trade (along with other indicators), are characteristics that shape the economy, and claims that understanding how these factors exclusively affect the economic outcome is far from complete.

### **Concluding comments**

This is rigorously researched and well written book on current area of academic and policy interest. Thorough exploration of economic history and industrial revolution in the book projects ambitious statement that good quality institutions in every aspect are imperative for virtuous performance of nation. Since the book has confined itself within inclusive and exclusive institutions ignoring role of geography, trade and technological factor in determining outcome of nation, readers may not agree with its strict institutional rim. Furthermore it is important to note that geography and other myriad of factors like culture, technology and trade has significant role to play in economic outcome of countries, and if geography is conducive to integrate technology and conduct commerce it will enable economy for higher growth. Overall we can say that this book is full of extensive evolutionary proof and highlights significance of institutions, readers will enjoy the simple read. Authors have tabled a heavy analysis underscoring importance of institution in front of policy architects, which I believe will unquestionably stimulate policy debate about 'sound institutions as determinant for economic development'. 

### **References**

- Daron, A & Robinson, J 2012, *Why Nations Fails: The Origins of Power, Prosperity, and Poverty*. 1 st ed. New York: Crown.
- Daron, A, Johnson, S & Robinson, J 2001, 'The Colonial Origins of Comparative

Development: An Empirical Investigation’, *American Economic Review*, vol.91, no.5, pp.1369–1401.

David, L, Dwight, P & Steven, B 2012, *Economics of Development*, W.W Norton & Company, Harvard University Press.

Easterly, W & Levine, R 2003, ‘Tropics, germs, and crops: how endowments influence economic development’, *Journal of Monetary Economics*, vol.50, no.1, pp. 3-39.

American Interest, Policy Politics & Culture, USA, viewed 16 May 2014, <<http://www.the-american-interest.com/articles/2006/11/01/do-defective-institutions-explain-the-gap-between-the-united-states-and-latin-america>>

Geest, K & Warner, K 2013, ‘Loss and damage from climate change: local level evidence from nine vulnerable countries’, *International Journal of Global Warming*, vol.5, no.4, pp. 367-386.

Freedom House, Freedom in the World 2013, Washington, United States. <<http://www.freedomhouse.org/sites/default/files/FIW%202013%20Booklet.pdf>>

MacLeod, WB 2013, ‘On Economics: a review of why nations fail by D. Acemoglu and J. Robinson and pillars of prosperity by T. Besley and T. Persson’, *Journal of Economic Literature*, vol.51, no.1, pp. 116-143.

North, D 1958, ‘Ocean freights rates and economic development’, *The Journal of Economic History*, vol.18, no.4, pp.537-555.

Sachs, 2003, ‘Institutions don’t rule: Direct effects of geography on per capita income’,

*NBER Working Paper*, no.9490, viewed 20 May 2014, <[http://www.nber.org/papers/w9490.pdf?new\\_window=1](http://www.nber.org/papers/w9490.pdf?new_window=1)>

Glaeser, E, Porta, R, Silanes, F, Shleifer, A 2004, *Do institutions cause growth?*, viewed 20 May 2014, <<http://www.nber.org/papers/w10568.pdf>>

Veiseh, N 2010, ‘Reconciling Acemoglu and Sachs: geography, institutions and technology’, *Journal of International Affairs*, vol.64, no.1, pp. 205-220.

The life of every teacher is partly dedicated to discovering and encouraging those few powerful minds that will influence our future, and the secret of education is never to forget the possibility of greatness.

GilberHight