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Endogenous institutional change after independence

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Abstract

Independence from colonial rule was a key event for both political and economic reasons. We argue that newly independent countries often inherited sub-optimal institutional arrangements, which the new regimes reacted to in very different ways. We present a model of endogenous changes in property rights institutions where an autocratic post-colonial elite faces a basic trade-off between stronger property rights, which increases the dividends from the modern sector, and weaker property rights that increases the elite's ability to appropriate resource rents. The model predicts that revenue-maximizing regimes in control of an abundance of resource rents and with insignificant interests in the modern sector will rationally install weak institutions of private property, a prediction which we argue is well in line with the experience of several developing countries.

JEL classification: O17; O57; P14

Keywords: Institutions; Property rights; Independence; Resource rents; Rent seeking

1. Introduction

The rules that societies live by have proven to be crucial for all kinds of economic development. A number of recent studies have established links between the general quality of countries' economic institutions and, for instance, income per capita (Hall and Jones, 1999; Acemoglu et al. (AJR), 2001, 2002; Easterly and Levine, 2003; Acemoglu and

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Johnson, 2005; Olsson and Hibbs, 2005). Perhaps more difficult to understand is what explains the wide international variation in measures of institutional quality. Empirical and theoretical efforts in this tradition have typically focused on deep historical explanations such as the various effects of colonialism (Acemoglu et al., 2001, 2002; Sokoloff and Engerman, 2000) or the role of the sovereign in the legal and economic systems of medieval Spain, France, and Britain (North, 1990; Glaeser and Shleifer, 2002). However, although institutions typically display a high degree of persistence, we argue that the institutional configuration of countries is also influenced by more recent circumstances.

The central issue that we address in this article is why more or less equally autocratic regimes installed widely different institutions for private property after independence. In countries like Singapore, the government pursued a strengthening of property rights and of the protection against government expropriation, whereas development was quite the reverse in some initially relatively developed countries like Ghana and Zambia. The major hypothesis advanced in this article is that the relative importance of natural resource rents played a central role for post-independence institutional development. The development literature contains numerous anecdotal accounts of how large inflows of easily appropriable rents from oil and valuable minerals provided rulers in developing countries with strong incentives towards expropriation of private property (Bates, 1981; Bates and Collier, 1993; Ndikumana and Boyce, 1998; Bigsten, 2001, Sala-i-Martin and Subramanian, 2003). Several econometric studies have also confirmed the negative relationship between natural resource abundance and institutional quality (Leite and Weidmann, 1999; Sala-i-Martin and Subramanian, 2003); Dalgaard and Olsson, 2007).

In order to understand this phenomenon, we present a model of endogenous change in property rights institutions and executive constraints. We take 'as given' the deeper historical effects of for instance the disease environment and the identity of the colonizer, and model endogenous institutional choice for a more or less autocratic elite who maximize their own utility in a two-period setting. The first period starts at independence and is typically characterized by sub-optimal property rights institutions from the perspective of the new regime.[1] The ruling elite has economic interests in a modern, formal sector but can also appropriate rents from a natural resource sector. These circumstances imply that the ruling elite faces a basic trade-off between weak and strong institutions of private property. Strong property rights will make the modern sector prosper and raise the ruling elite's incomes from that sector. Weaker property rights, on the other hand, means a poorly functioning modern economy but makes the ruling elite's expropriation of resource rents easier.

Our model predicts that ruling elites are more inclined to weaken property rights if easily appropriable natural resource rents abound, whereas the lack of an 'easy rents-sector' coupled with substantial interests in a modern sector will motivate even an autocratic ruling elite to install stronger private property rights, which in turn results in higher growth. The costs of institutional change also play a central role in our model. In addition, a higher initial level of property rights protection will diminish, in some instances even negate, the negative impact of natural resource abundance on growth, as demonstrated

[1]See Acemoglu et al. (2001, 2002) for possible explanations as to why colonial powers might establish extractive institutions in the colonies. Further, Djankov et al. (2003) argue that the institutions put in place by colonial powers were likely to be inefficient, even when the colonizers attempted to transplant their own institutional arrangements directly.