

# Good governance agenda: theory analysis



**ASSIGN  
BUSTER**

- Henil Yatin Shah

## Introduction

Khan (2011) defines governance as how the state and society interact. He mentions that there are two views regarding governance: ‘market-enhancing’ governance (often referred to as a ‘good governance’ agenda) and ‘growth-enhancing’ governance. The good governance agenda is the dominant view and is promoted by the World Bank and other international development institutions. The good governance agenda links poor governance attributes directly to low economic growth. At the heart of the good governance agenda is the argument that Africa’s growth depends on strengthening the institutional structures that underpin efficient markets. As well as low corruption, this includes property rights stability, a transparent and accountable public sector, democratic government, rule of law and competitive, rent free, markets. However, significant questions remain in terms of both the theoretical and empirical evidence behind the idea that these institutions are the most important ones for the improvement of economic development in Africa. This is where the alternate view of ‘growth-enhancing’ governance comes in. In this answer, we will now look at the theory behind good governance, discuss the counter argument to the good governance theory by looking at the evidence on governance in Africa and the problems with that evidence, identifying the features of governance that are problematic for economic development, compare African governance to that of East Asian countries and conclude whether or not the growth prospects of Sub-Saharan Africa are dependent on the adoption of good governance practices based on what we have discussed in this answer.

### Good Governance Agenda: Theory

African states were perceived in the 1980s as particularly weak, with high levels of corruption and mismanagement as well as suffering from a lack of democratic accountability and rule of law. The good governance theory is based on two theoretical approaches: New Institutional Economics (NIE) and theories of rent seeking. NIE applies mainstream economic theory to the study of institutions (defined by NIE's founder as 'the rules of the game' – covering formal institutions such as political parties or judicial systems as well as informal institutions such as cultural attitudes towards trust and exchange) and argues that institutions improve economic outcomes to the extent that they lower transaction costs between individuals and groups. Transaction costs are the costs of bargaining, enforcing and monitoring – the activities without which exchange could not take place. The rules that guide these aspects of transacting are established by institutions. NIE argues that the lower the transaction costs, the more transactions will take place and society will achieve greater efficiency and hence better economic performance. The second theory of rents and rent seeking is also vital for the good governance agenda. The concepts of rent and rent seeking are used by economists to think about the impact of the state on the economy, both through its legal activities and through the illegal or 'grey' activities of state officials involved in corruption. The good governance agenda assumes that the creation of rents is bad for economic performance because it leads to distorted resource allocation and policies. However, this overlooks the many other useful roles that rents can and do play in an economy. Not all rents are socially or economically damaging, for example subsidies given to firms

investing in training staff to use new production techniques, but these potentially beneficial aspects of rents are largely overlooked in the good governance agenda.

The general insight of NIE and rent seeking theories is that governance systems that lower transaction costs and minimise state interventions are better for promoting economic growth because they permit greater market efficiency. These economic theories were translated into a concrete set of proposals on governance and the role of the state in the economy that, in broad terms, involved: minimising state interventions in the economy, strengthening the rule of law, securing the property rights of individuals and businesses and lowering corruption and rent seeking through greater democratic accountability. These ‘good governance’ institutions are the ones most normally associated with rich industrialised countries, but are often absent to varying extents in developing countries. The good governance agenda has had a particularly large impact on the policy agenda in Africa – evident from numerous policy documents the extent to which good governance reforms have been integrated within conditionally placed on loans by the World Bank and the IMF, and the formal acceptance of the good governance agenda by many African leaders.

#### Good Governance Agenda: Counter Argument

There is, however, an important counter argument to this consensus that suggests that governance may not be important for explaining African economic performance. Prominent economists such as Jeffrey Sachs have argued that other factors, such as geography and the burden of infectious

diseases, are much more important for explaining poor economic performance than systems of governance in Africa. They suggest that even if good governance could be implemented in Africa, this would not lead to better outcomes for economic growth without massive increases in infrastructure investment to overcome the costs associated with geography and disease. In a related argument, Glaeser and his colleagues (2004) suggest that much higher investments in education and human capital development would trigger better economic performance than improved governance. An alternative to both the good governance agenda and those that deny the importance of governance has been gaining prominence in recent years, associated with Dani Rodrik, Mushtaq Khan and Ha-Joon Chang. These scholars question the theoretical and empirical basis of the good governance agenda and argue that while governance is critical to economic performance, the most important institutions for economic development are not those identified by the good governance agenda. Khan (2011) calls these institutions the ‘market-enhancing’ governance agenda. Khan (2011) says that ‘no country achieved significant good governance capabilities *before* they developed’. He goes on to say that successful countries achieved better governance as described by good governance characteristics by having other governance capabilities that allowed them to grow and then sequentially developed aspects of good governance as the growth process generated resources to pay for the public good that good governance represents. The growth-enhancing governance agenda, according to Khan (2011), is ‘about identifying significant market failures country by country, and developing the capabilities to respond to them in ways that limit the risk of government failures.

### Governance Data

The creation of measurements of institutional quality since the 1990s has supported the rise of the good governance agenda. Given the difficulties in directly measuring governance, quantifying governance has involved identifying proxy indicators for governance attributes based on both ‘ objective’ and ‘ subjective’ measures. Examples of objective measures of governance include counting the number of civil wars, coups, or political assassinations or the number of political parties to assess the quality of the democratic institutions or counting the number of corruption cases taken to court to assess the level of corruption. The problem with these types of objective measurements is that they may be a poor proxy for the underlying governance characteristic that we are trying to capture. The frequency of elections and the number of parties may be a poor proxy for the essence of democracy in terms of the government’s accountability to the people, and the number of corruption cases that actually end up in court may be very few compared to the level of corruption in a country. On the other hand, subjective measures are based on surveys of business people to assess their perceptions of the quality of governance. In addition, surveys of individuals and households such as the ‘ Afrobarometer’, have been a relatively new growth area in the study of governance. These large surveys of citizens are important in terms of assessing people’s normative attitudes to institutions but are much less useful in terms of providing direct information about the relationship between different institutions and economic growth.

The empirical field of governance analysis is now dominated by composite indices of data that involve aggregating different objective and subjective

proxy measures of governance from various sources. The best known of these data sets are the ‘Corruption Perceptions Index’ produced by Transparency International and the ‘World Wide Governance Indicators’ produced by the World Bank. The World Governance Indicators are composite indicators covering six aspects of governance: voice and accountability, political stability, government effectiveness, regulatory quality, rule of law and control of corruption. In terms of these governance measurement tools, most countries in Africa perform badly on all of the key areas of the good governance agenda in comparison to other regions. Governance data has been used extensively in econometric studies of governance. Econometrics uses statistical techniques to investigate relations between different variables. Literally thousands of papers have been produced over the last fifteen years that engage in this type of analysis of governance, and the vast majority of them come up with the same conclusions – that good governance is necessary for economic growth.

### Governance Data: Problems

On first appearances, therefore, the evidence for the good governance agenda appears to be conclusive, and this helps to explain why it has achieved the status of ‘conventional wisdom’ in debates on economic growth in Africa. Yet, on further investigation, there are a number of serious problems with the data on governance that suggest that what we know about the relationship between governance and growth may not be as clear-cut as the econometric studies imply. There are four problematic areas to focus on regarding governance data most relevant for the debates on governance in Africa: subjectivity, causality, the fact that many African

countries are not poorly governed given their level of income and poor governance characteristics are shared by both rapid and slow developers.

### Subjectivity

We looked at some of the problems of using ‘objective’ measurements of governance above; similarly subjective data risks the possibility that ratings are affected by the expert’s knowledge of recent economic performance. For example, when a country is performing well economically, business people are more likely to perceive lower corruption than in a country where the economy is stagnating. Subjective indexes may also be biased in favour of the interests of foreign investors who pay for the studies.

### Causality

Probably the most important problem with the quantitative evidence is that econometric studies have proven inconclusive about the direction of causation between good governance and growth – does good governance *cause* higher incomes or does higher income *cause* good governance? The types of institutions recommended by the good governance agenda, such as a well performing legal system or well protected property rights, are expensive to construct and maintain – it is clear that richer countries have been able to afford these institutions but the evidence that these institutions were necessary for their economic growth in the first place is much weaker. This is a very fundamental problem with the econometric evidence, and economists have tried to deal with this problem through various econometric techniques. Even with more rigorous data tests, however, causality remains uncertain.



### Many African countries are not poorly governed, given their level of income

Many African countries may be as well governed as we could expect for their level of income and that others are actually better governed than the average for their level of income.

### Poor governance characteristics are shared by rapid and slow developers

Many developing countries, mainly from Asia, achieved rapid economic growth with similar governance characteristics to SSA. This means that there may be other characteristics of governance that are important for growth that are not reflected in the recommendations of the good governance agenda.

### Problematic African Governance Features

Economists often argue that there are a number of specific features of governance in African countries that are particularly problematic for economic development. One of these features is Neo-Patrimonialism. A patrimonial state, according to Max Weber, is where authority is based on personal loyalty to the leader. Authority is maintained through personal connections, favours and promises between the patron, who holds a position of power within the state, and clients in society. The patron will give state resources to clients in order to maintain loyalty. However, this feature according to many economists is not problematic to economic development rather it is a step towards economic development and becoming a bureaucratic state. Moreover, they argue that growth still occurs with Neo-Patrimonialism, for example in Nigeria. Another problematic feature is that of ethnic conflict. Ethnic fragmentation is seen to weaken state capacity and, in

its worst form, to lead to civil war and long-running violent conflicts, for example in Democratic Republic of Congo, Uganda, Sudan etc. The last problematic feature we look at is that which focuses on the role of natural resources in African countries. Economists believe that countries in Africa with abundant natural resources bring in large revenues to the economy, but these revenues lead to corruption and rent-seeking. Moreover, it is argued that natural resources make civil wars more likely in a country. However, the evidence on this topic tells us that Africa's deadliest conflicts occurred in countries that were not dependent on natural resources, for example Rwanda.

### Conclusion

When we look at how East Asia has progressed over the years and compare it to Sub-Saharan African countries, we can safely assume that East Asian countries had similar challenges to Sub-Saharan African countries in terms of Neo-Patrimonialism, ethnic conflict and natural resources. But they have proved that going to the good governance agenda might not be the quick answer to economic development. They used Khan's (2011) market-enhancing governance to first establish themselves in the world market and then implemented good governance agenda. The same can be said for highly industrialised countries. Moreover, looking at the above theories and discussions, understanding the role of governance in Africa's economic development has been interpreted through the lens of often conflicting economic theories. These differing accounts of the role of governance and economic development in Africa relate to fundamental divergences in approaches between economists to questions of the causes of economic

growth and the relationship between the state and markets. The comparative and historical record suggests that improving governance is not necessary or sufficient for achieving higher economic growth. Yet issues of governance cannot simply be reduced to a debate on economic outcomes. The political and ethical aspects of governance are also critical. In this respect, there are many Africans working, often under dangerous circumstances, to hold their leaders to account for corruption and mismanagement and to raise awareness of the global systemic drivers of bad governance. Unfortunately, the ‘good governance’ agenda, with its overriding focus on strengthening market institutions and reducing the economic policy interventions of the state, does not necessarily strengthen these domestic political initiatives to improve governance.

### References

Baland J, Moene K, Robinson J (2010) ‘Governance and Development’, Chapter 69 of Rodrik D and Rosenzweig M (Eds) *Handbook of Development Economics*, Vol 5, Amsterdam: North-Holland

Chang H (2006) ‘How Important were the “Initial Conditions” for Economic Development – East Asia vs. Sub-Saharan Africa’, Chapter 4 of *The East Asian Development Experience: The Miracle, the Crisis, and the Future*, London: Zed Press.

Khan M (2011) ‘Governance and Growth: History, Ideology, and Methods of Proof’ in *Good Growth and Governance in Africa*, eds Akbar Noman, ch 2, Oxford: Oxford University Press.