

Economics focus Roots of development

What matters most for development—geography, institutions or policy?

ECONOMIC growth in poor countries, it seems reasonable to suppose, depends on getting lots of different things right, and probably on a generous measure of good luck as well. Is it possible to say which factor or factors matter most?

For many years economists emphasised the importance of good economic policy (though often disagreeing about which policies were good and which not so good). Lately, it has become orthodox to stress the importance of long-lived "institutions" that are conducive to growth: political stability, property rights, legal systems, patterns of land tenure, and so on. Other economists instead put great weight on geography, especially climate (which affects the incidence of disease, the applicability of some technologies, agricultural opportunities, and more) and access to the sea (which affects the scope for international integration).

Such explanatory factors need not be mutually exclusive. Successful development could depend on all of the above. Rich economies usually combine competent policy (on the whole), sound and stable institutions and favourable geography. Many of the world's poorest countries score badly on all three counts. Still, it would be interesting to discover that policies, say, matter much more than geography—and it would be encouraging too, because policies are easier to change than whether a country is in the tropics or has access to the sea. A new paper* by William Easterly of the Centre for Global Development and Ross Levine of the University of Minnesota tests the importance of these three sets of factors, looking at a sample of 72 rich and poor countries.

The results are intriguing. Institutions turn out to matter most—but that is

putting it mildly. Geography and policy, as influences in their own right, turn out to matter not merely less than institutions but, roughly speaking, not at all.

Take policy first. In this study the quality of policy is measured by inflation, openness to trade, exchange rates and so forth. The finding that policy in these areas does not drive development seems surprising, and at odds with a lot of other work, as the authors acknowledge.

One explanation may be that other studies relate good policies to growth rates, whereas Mr Easterly and Mr Levine relate it to the level of income. Why would that matter? Possibly, bad policies curb growth rates for a spell, but not enough to have a significant effect on incomes in the long term. Or the reason could be that some other studies fail to include institutions alongside policies as a possible explanation for development. If low-income countries with bad policies also have bad institutions, and institutions are not included in the analysis, then bad policies may act as a proxy for bad institutions, and appear to be the true underlying influence.

At any rate, the study finds that countries with good institutions tend to do all right with good or bad policies. In the same way, countries with bad institutions tend to do badly regardless.

Germ of an idea

Other studies say that geography matters a lot. In this case, Mr Easterly and Mr Levine agree, sort of, because they find that geography affects institutions. Favourable geography, they find, promotes good institutions; good institutions then promote development. When the study looks at the economic influence of geog-

raphy in its own right—that is, does geography affect income independently of promoting good institutions?—they find no clear connection.

In itself, in other words, good geography does not seem to count. A country with bad geography and good institutions will do fine. A country with good geography and bad institutions will not. It is only in so far as good geography breeds good institutions that good geography promotes development.

But hang on. Why on earth should good geography favour good institutions? The authors explain that this odd-seeming finding is consistent with a plausible theory set out and defended empirically elsewhere†. The 72 countries in the sample are all former colonies. Europeans followed a variety of colonial strategies. In North America, Australia and New Zealand, Europeans settled in large numbers and created institutions to protect private property and curb the power of the state. In most of Africa and Latin America, Europeans never wished to settle and instead concentrated, to varying degrees, on extracting metals, cash crops and other resources: less democracy, less regard for property rights.

Why did Europeans settle in North America and not in Africa? Because of geography—that is, because of germs. Where settler mortality was low, because geography and climate were conducive to good health, Europeans moved in and planted good institutions. Where settler mortality was high, because of bad geography, they stayed away and planted bad institutions. These institutions, good and bad, put down roots—and the result, broadly speaking, is the pattern of income you see today around the world.

Institutions are more difficult to change than policies, of course. If that were not so, the European colonial legacy emphasised in this account of development would not have been so enduring. But institutions are presumably not as resistant to reform as geography. Spelling out more precisely—or with any precision at all—how to get from bad to good institutions is, on this view, the real challenge for development economics. ■

* "Tropics, Germs and Crops: How endowments influence economic development". NBER Working Paper 9106.

† "The Colonial Origins of Comparative Development: An empirical investigation", by D. Acemoglu, S. Johnson and J. Robinson. *American Economic Review* 91, December 2001.

