

Unlocking Development

A CAGE Policy Report

Stephen Broadberry

Leigh Gardner

Rocco Macchiavello

Anandi Mani

Christopher Woodruff

Foreword by Frances Cairncross

Introduced by Nicholas Crafts

Edited by Mark Harrison

Unlocking Development

A CAGE Policy Report

Stephen Broadberry
Leigh Gardner
Rocco Macchiavello
Anandi Mani
Christopher Woodruff

Foreword by Frances Cairncross

Introduced by Nicholas Crafts

Edited by Mark Harrison



FIRST PUBLISHED BY

The Social Market Foundation, November 2014

ISBN: 978-1-904899-98-3

11 Tufon Street, London SW1P 3QB

Copyright © The Social Market Foundation, 2014

The moral right of the authors has been asserted. All rights reserved. Without limiting the rights under copyright reserved above, no part of this publication may be reproduced, stored or introduced into a retrieval system, or transmitted, in any form or by any means (electronic, mechanical, photocopying, recording, or otherwise), without the prior written permission of both the copyright owner and the publisher of this book.

THE SOCIAL MARKET FOUNDATION

The Foundation's main activity is to commission and publish original papers by independent academic and other experts on key topics in the economic and social fields, with a view to stimulating public discussion on the performance of markets and the social framework within which they operate. The Foundation is a registered charity and a company limited by guarantee. It is independent of any political party or group and is funded predominantly through sponsorship of research and public policy debates. The views expressed in this publication are those of the authors, and these do not necessarily reflect the views of the sponsors or the Social Market Foundation.

CHAIR

Mary Ann Sieghart

DIRECTOR

Emran Mian

MEMBERS OF THE BOARD

Lord Charles Falconer

Daniel Franklin

Baroness Olly Grender MBE

Nicola Horlick

Graham Mather

Sir Brian Pomeroy CBE

Peter Readman

Baroness Gillian Shepherd

Professor Alison Wolf

DESIGN AND PRODUCTION

Pistachio Design

www.pistachiodesign.com

PRINTED BY

Diversified Global Graphics Group

www.dg3.com

CONTENTS

Acknowledgements	4
Foreword	5
Introduction: Unlocking Development	6
Executive Summary	10
Chapter 1. National Economies: Sustaining Growth	13
Chapter 2. The Private Sector: Unlocking Enterprise	47
Chapter 3. Citizenship: Empowering Women	83
About Us	111

ACKNOWLEDGEMENTS

Warwick's Centre for Competitive Advantage in the Global Economy (CAGE) acknowledges funding of this policy report by the Economic and Social Research Council. CAGE is grateful for other support to our home institution, the University of Warwick and its Department of Economics, and to our partner the Social Market Foundation.

Parts of chapters 1 and 3 previously appeared in another format as CAGE-Chatham House briefing papers. CAGE is grateful to Chatham House, and especially to Paola Subacchi, Research Director of International Economics, and André Astrow, research consultant, for their partnership and assistance.

Stephen Broadberry and Leigh Gardner thank their collaborators in the research discussed in chapter 1, especially Bruce Campbell, Alex Klein, Mark Overton, Bas van Leeuwen, and Jan-Luiten van Zanden. Chris Woodruff and Rocco Macchiavello thank their collaborators in the research discussed in chapter 2, especially Arthur Blouin, Pablo Cotler, Suresh de Mel, Marcel Fafchamps, Ameet Morjaria, David McKenzie, and Simon Quinn. Anandi Mani thanks her collaborators in the research discussed in chapter 3, especially Lakshmi Iyer, Prachi Mishra, and Petia Topalova.

Nicholas Crafts and Mark Harrison are grateful to all whose assistance have helped deliver this report to the public, especially Sascha Becker, Karen Brandon, Fiona Brown, Tracy Evans, Emran Mian, Jane Snape, and Amanda Wolthuizen; we also thank John Wallis for advice and Nicolás Lillo Bustos for research assistance.

CAGE POLICY REPORTS

This is the second CAGE Policy Report. The first CAGE Policy Report was published in 2012 as *Reversals of Fortune? A Long-term Perspective on Global Economic Prospects*, by Sascha O. Becker, Stephen Broadberry, Nicholas Crafts, Sayantan Ghosal, Sharun W. Mukand, and Vera E. Troeger. *Reversals of Fortune* is available from <http://goo.gl/wxhYTn>.

FOREWORD

BY FRANCES CAIRNCROSS

As Chair of the Advisory Board of the Centre for Competitive Advantage in the Global Economy at the University of Warwick, it gives me great pleasure to introduce the 2014 CAGE Policy report. It has been produced in partnership with the Social Market Foundation. The report reflects the remarkable way in which CAGE knits together a broad range of perspectives to throw light on some of the most important economic issues of our age.

Thus it looks at what light can be shed on Sub-Saharan development by the experience of thirteenth century Europe. It emphasises the importance of the rule of law, of clear property rights and of a state that aspires to treat citizens equally before the law. 'The rule of law is ... infrastructure,' it explains. 'Arguably it is more important than any power cable or drainage system.'

In a chapter on private enterprise, the report draws attention to the fact that in the poorest countries, half of the labour force is typically self-employed or employed in firms with a handful of employees. To grow, developing countries need larger firms. 'For the mass of people in low-income self-employment....' it argues, 'hope for the future lies in becoming wage workers in larger organizations that someone else has created.' The chapter explores the reasons why so few small firms grow larger, and the ways that policy makers should tackle the issue.

The final chapter explores the connected issues of gender violence, discrimination against women and the impact that women politicians can have on public perceptions. To span such a broad canvas in such a readable and thoughtful way is a tremendous achievement. The report is soundly researched, readable, provocative and essential reading for anyone involved in the development of the world's poorest nations.

Frances Cairncross, CBE, FRSE, is the former head of Exeter College, Oxford, and she is about to become Chair of Court at Heriot-Watt University, Edinburgh. She is also Chair of the CAGE Advisory Board.

INTRODUCTION: UNLOCKING DEVELOPMENT

BY NICHOLAS CRAFTS

There are two fundamental aspects of CAGE research. One is rigorous attention to evidence and context: what is it that can be shown to have worked in its particular place and time? In our view, the key that unlocks development has a different shape in every context. That is, poverty and lack of development are global problems, but the details of the solution are always local. The other is a consistent vision of economic development as a process that expands the control ordinary people can exercise over their own lives.¹ This means that economic development is about much more than just economic growth; it is about a wider concept of living standards which includes escaping from poverty but also entails various other aspects of life such as the ability to participate fully in society. Growth is necessary but not sufficient for development in this broader sense and different growth trajectories vary in the degree to which they are 'pro-poor'. Measures of 'human development' show that income levels do not necessarily predict well other aspects such as life expectancy or educational attainment.²

The design of policies to promote economic development needs to pay attention to the specifics of local conditions. Countries vary greatly in terms of their comparative advantages in international trade, institutions, political structures, and geography. The binding constraints on achieving faster growth which need to be addressed are not necessarily the same. Nevertheless, certain basic requirements for growth do have to be put in place one way or another. Credible incentive structures (which may take a diverse shape – the Chinese economy is clearly 'unorthodox' compared with traditional western designs) that make it worthwhile to undertake productive investment and innovation are a fundamental building block. It is also essential to have a framework for the design and implementation of economic policy which allows market failures to be addressed while at the same time containing the risks of government failure. Sadly, in many poor countries, the first purpose of politics has been to loot the state while you have the power to do so.

All this implies that governance really does matter for success in achieving sustained economic growth. But governance structures also have profound

implications for economic development and well-being. This is quite well-known and has been well documented by World Bank research which found that a range of governance attributes including voice and accountability, governmental effectiveness, political instability and violence and quality of the legal system have powerful impacts on such development outcomes as literacy rates and infant mortality.³ Governance also matters for gender equality, which affects both growth and development outcomes. For example, the extent to which women are educated differs widely across the developing world.⁴

Many people in poor countries – and some people in rich ones – are kept in poverty by multiple shackles and restraints, each of which must be unlocked for them to escape. They are trapped by lack of resources, by lack of education, by discrimination, and by hopelessness and fear, all at the same time. Foreign development assistance alone will not help them escape. In many cases the key can be fashioned out of quite general materials such as ‘market access’, ‘education’, and ‘equal rights’ – and, of course, ‘aid’. But the key must also be fitted to the lock. Unless the key fits the lock, just to allocate more money to schools, or to legislate for equal rights, may have little or no effect on the situation. Foreign aid can facilitate local solutions but our analysis does suggest that development will not generally be promoted by unthinkingly giving large amounts of money to poor countries. Nearly \$5 trillion of development assistance have flowed from richer countries to poorer ones since 1945 but there is little evidence that our world has been transformed as a result.⁵

Why has large-scale foreign aid not produced more clear-cut effects? Several factors appear to be at work. One problem is that an average dollar of productive resources, when transported from a wealthy country to a much poorer one, becomes worth only a few cents in its new setting. Poor countries are poor not so much because they lack capital as because many things do not work well, and much value is dissipated by inactivity, theft, and corruption. Another reason why the average aid dollar does not do a dollar’s worth of good is that average effects do not mean much. Some aid dollars help a lot, and at the same time many others are completely wasted. It is then difficult to disentangle the good uses from the bad ones.

A final reason is that economic growth and development are hard to explain anyway, and in that context it is harder still to identify the marginal effect of an external intervention.

Thus more money for schools will be wasted if the children do not attend because they must work, or if the teachers take higher salaries without improving their delivery of lessons. Laws that prohibit discrimination will have no effect if victims lack confidence in the police or fear further victimisation at the hands of the violators. Exactly what will free the natural energy and enterprise of ordinary people and empower them to participate in development must be understood in its context in every region, country, and village.

Unlocking Development, therefore, does not advocate detailed reforms to which every country must conform. Its approach, rather, is to look at what measures have been shown to work in particular contexts and periods. It draws primarily on experience and history, considering many different countries and many different periods.

REFERENCES

Kaufmann, D., A. Kraay, and P. Zoido-Lobaton (1999), 'Governance matters', World Bank Policy Working Paper no. 2196 (The World Bank, Washington, DC).

Prados de la Escosura, L. (2014), 'Human development as positive freedom: a world view since 1870', CAGE-Chatham House Briefing Paper no. 12.

Tierney, M.J., D.L. Nielson, D.G. Hawkins, J.T. Roberts, M.J. Findley (2011), 'More dollars than sense: refining our knowledge of development finance using AidData', World Development 39(11), pp. 1891-1906.

UNDP (United Nations Development Programme) (2014), Human development report 2014. Sustaining human progress: reducing vulnerabilities and building resilience (New York: UNDP).

ENDNOTES

1. Development as 'a process of expanding freedom' is a central theme of research on human development by CAGE associate Leandro Prados de la Escosura, summarised in Prados de la Escosura (2014).
2. See the data in UNDP (2014). For example, South Africa and Sri Lanka have per capita income levels of \$11,788 and \$9,250 respectively, but in the former life expectancy is 56.9 years and in the latter 74.3 years.
3. World Bank research on governance: a rich literature has grown from Kaufmann et al. (1999).
4. UNDP (2014) reports indices of gender equality which show big variations. For example, India has far greater gender inequality than China and this is reflected in much lower female educational attainment and labour force participation.
5. Nearly \$5 trillion of development assistance: Tierney et al. (2011), who also provide a detailed survey of applied research on the effectiveness of foreign aid of all kinds.

EXECUTIVE SUMMARY

The world's poor are 'trapped' in poverty. How can we unlock development so that poor countries can sustain economic growth over long periods of time? Our report considers this problem on three levels, the national economy, the private sector, and citizenship. At the core of each chapter is new research by CAGE members and associates. Chapter 1 addresses the factors underlying sustainable growth of the national economy. Chapter 2 looks for the sources of business capacity and sustainable growth of the private sector. Chapter 3 links citizenship to economic development, showing how political voice can enable women to participate more freely in society and the economy.

In all three chapters we show how economic development relies on the rule of law, including a framework of laws and their enforcement that is applied to all and accessible by all. We show how, without such a framework, the sustainable growth of national economies and their businesses is threatened when laws fail to resolve conflicts. This failure is often accompanied by corruption or violence. So, we discuss what can be done to promote the rule of law; to make economic growth more stable and sustainable; to enhance the capacity of business organisations that are most likely to attract, grow and create jobs; and to enable women to play a full part in economic development as citizens, providers, and entrepreneurs.

CHAPTER 1. NATIONAL ECONOMIES: SUSTAINING DEVELOPMENT

National economies in Africa have seen many episodes of growth acceleration alternating with reversal. This pattern of growth and reversal is not new; it was typical of most European national economies over 600 years from 1270 to 1870. Growth regularly ran into the sand because commodity bubbles burst or prosperity collapsed into conflict. A vicious circle links poverty, dependence on a few primary export commodities, and lack of diversification with weak rule of law, corruption, and periodic outbreaks of violence.

To overcome this pattern, African economies must undergo institutional changes. This is easier said than done, but policy can make a difference.

Good policy will foster a robust civil society and private sector, the rule of law, and the government's capacity to tax and spend on basic public goods. These are not just technocratic goals; they also require far-sighted political leadership.

CHAPTER 2. THE PRIVATE SECTOR: UNLOCKING ENTERPRISE

If the poorest countries are to become rich, their private sectors must be transformed. To judge from appearances, developing countries are abundantly supplied with one of the most important factors of production: entrepreneurship. Most workers in poor countries are self-employed micro-entrepreneurs working on their own account. Evidence from several Asian and African countries suggests that supporting micro-enterprise can help to combat poverty, but the reality is that it will not lead to sustained growth. More likely, the high-productivity, high-wage jobs that prosperity requires will come from firms that already exist.

We turn to those firms that are already successfully exporting to Western markets where consumers are wealthy and quality standards are high. In these markets an important role is played by Western buyers that seek out reliable, high-quality producers and establish valuable buyer-seller networks. A problem is that such networks inhibit competition, and are required largely to overcome a legal deficit: in some poorer countries it is hard to enforce contracts or resolve disputes non-corruptly. The best remedy would be to improve the economy's legal framework but, as we have already noted, this is easier said than done and takes a long time. Meanwhile, second best is to support buyer-seller networks, alongside industry boards that facilitate cheap and transparent contract enforcement and arbitration.

CHAPTER 3. CITIZENSHIP: EMPOWERING WOMEN

Violence against women is a global issue. It raises moral and legal issues; it is also a development issue. This is because gender violence suppresses women's ability to participate in economic life. Gender crime is typically hidden. It is hidden when women do not have a voice. A social evil that is

hidden cannot be addressed. Any strategy for dealing with gender crime must start from enabling women to be seen and heard in public life and present at the policy-making table.

We use Indian evidence from a local government reform to show that when women have more political representation there is an increase in recorded violence against women, but this is good news: gender crime does not rise, but more of it is reported. When women are 'in charge' locally, more female victims come forward, and the political leaders are more ready to intervene. The biggest effect is from representation at the lowest levels of government where female leaders are closest to female victims. Reporting of crimes against women, including domestic violence, is also a problem in developed countries, where institutional responses also tend to discourage reporting and fail to reduce offending. In fact, low female participation in politics is just as typical of rich countries as of poor ones. Reserved seats for women appear to be the most effective way to encourage more women into politics.

CHAPTER 1. NATIONAL ECONOMIES: SUSTAINING GROWTH

INTRODUCTION

In the first decade of the twenty-first century many African countries have achieved relatively rapid growth. This has raised hopes that Africa is finally on a path to convergence with Asia and Latin America. The patterns that we see in African economic development are not new; we will see that they replicate several centuries of European history. Europe's history suggests that optimism for Africa will be misplaced unless economic growth is accompanied by serious institutional change. What changes are required? This is not an easy question because we will identify a vicious circle that links poverty, dependence on a few export commodities, and lack of diversification with weak rule of law, corruption, and periodic outbreaks of violence. Vicious circles are difficult to break. How can we break this one?

Box 1.1. Setting the scene

Africa rising? 'The shops are stacked six feet high with goods, the streets outside are jammed with customers and salespeople are sweating profusely under the onslaught. But this is not a high street during the Christmas-shopping season in the rich world. It is the Onitsha market in southern Nigeria, every day of the year. Many call it the world's biggest. Up to 3m people go there daily to buy rice and soap, computers and construction equipment. It is a hub for traders from the Gulf of Guinea, a region blighted by corruption, piracy, poverty and disease but also home to millions of highly motivated entrepreneurs and increasingly prosperous consumers. Over the past decade six of the world's ten fastest-growing countries were African. In eight of the past ten years, Africa has grown faster than East Asia, including Japan' (Source: 'The hopeful continent: Africa rising', The Economist, 3 December 2011).

Using annual data from many countries since 1950, and defining a growth acceleration as a period over at least eight years in which the national growth of GDP per head is at least 3.5 per cent, exceeds the previous growth rate by at least 2 per cent, and leaves the level higher than at any time in the past, 'the largest number of growth accelerations is actually in Africa ... a continent that one hardly associates with economic growth. However, this region still has the lowest probability of a growth transition among all the regions: only 1.9 per cent. ... Financial liberalisation and positive external shocks are associated with growth accelerations that eventually fizzle out. Fundamental economic reform and positive political regime change increase the likelihood of sustained accelerations ... [but] the predictability of these different kinds of growth episodes still remains extremely low.' (Source: Hausman, Pritchett, and Rodrik 2005).

Africa's recent growth 'has largely followed rising commodity prices, and commodities make up the overwhelming share of its exports - never a stable prospect. Indeed, the pessimists argue that Africa is simply riding a commodities wave that is bound to crest and fall and that the region has not yet made the kind of fundamental economic changes that would protect it when the downturn arrives. The manufacturing sector in sub-Saharan Africa, for example, currently accounts for the same small share of overall GDP that it did in the 1970s. What's more, despite the overall decline in poverty, some rapidly growing countries, such as Burkina Faso, Mozambique, and Tanzania, have barely managed to reduce their poverty rates. And although most of Africa's civil wars have ended, political instability remains widespread: in the past year alone, Guinea-Bissau and Mali suffered coups d'état, renewed violence rocked the eastern Democratic Republic of the Congo, and fighting flared on the border between South Sudan and Sudan. At present, about a third of sub-Saharan African countries are in the throes of violent conflict' (Source: Devarajan and Fengler 2013).

AFRICA'S FUTURE: SUSTAINABLE GROWTH?

African countries have achieved impressive rates of economic growth since the mid-1990s, second only to those of East Asia. Can Africa's improved economic performance be sustained? Optimists point not only to a boom caused by high prices for primary commodities, but also to improved macroeconomic policies, democratisation, and the transformation of industrial and service firms by information and communications technologies. However, more pessimistic commentators point to continued political instability, corruption and weaknesses in transport and energy infrastructure.¹

Both optimists and pessimists have looked back to the period of rapid growth following the end of World War II and its subsequent reversal in the 1970s. Optimists have argued that this reversal reflected the difficult challenges of decolonisation and that Africa has now moved on. Pessimists have suggested that the export led growth of the current boom is similar to that of the 1950s and 1960s. However, a longer view of Africa's economic history suggests that periods of rapid growth followed by reversals have characterised African economic performance for several centuries. These reversals have limited long run improvements in incomes per head. The periods of growth and the reversals alike have been driven by changes in world demand for primary commodities.²

Recent research has reconstructed GDP figures for Europe since the thirteenth century. It shows the same pattern for Europe up to the mid-nineteenth century as for Africa recently. There were periods of rapid growth and setbacks. These were based on the success and failure of export commodities, particularly wool.

This research also suggests that average incomes in medieval Europe were substantially higher than previously thought, so that the medieval period should be seen as the starting point of the road to sustained growth, not an embodiment of all things backward. The first transition to modern economic growth occurred in the North Sea area. The North Sea economies were the first to escape the pattern of growth reversals. They were allowed to succeed in this transition by fundamental institutional change.

Box 1.2. GDP as a measure of development

What is GDP? A country's gross domestic product measures everything that is produced within the country. The size of a country's GDP can be taken as a measure of its weight in the world economy. Economic size is important where scale matters: for example for national power, or when the existence of an industry depends on a large market. Thus politicians, diplomats, and defence contractors care most about whether America or China is the world's largest economy. But the size of an economy tells us little about its level of development; both the American and Chinese economies are very large, but China's economy is much less developed than America's.

What is development? A developed economy is rich so that its GDP is large relative to its population. A first approximation to the level of development of an economy is its GDP divided by the population, or GDP per head. This is not an infallible measure, but it is always a good place to start. However, a developed economy is usually also diversified, so that its citizens, most of whom live in cities, do many different things that complement each other, and what they do is intensive in knowledge, skills, and capital. Some economies are rich without being highly developed because they have oil, gas, or other mineral wealth. They are rich only because other economies that are rich and developed have valuable uses for their resources.

Does GDP measure social welfare? Having a high GDP per head of the population does not guarantee social welfare. It has been said that a large GDP relative to the population captures the potential for wellbeing rather than wellbeing itself. Still, there is evidence from around the world that GDP and wellbeing are somewhat connected. On average, each doubling of GDP per head does tend to increase psychological wellbeing by about the same amount.

GDP growth or level? It is important to distinguish the level of an economy's development from its rate of growth. From the point of view of how we live at any moment the level of GDP per person is surely more important than its growth. However, poor countries can achieve high levels in the foreseeable future only by means of rapid growth, so growth matters too.

What is sustainable growth? Not all growth is sustainable. When growth that takes the form of producing more by using ever more resources and effort, the result is sustainable only while there are resources lying around that are unused. The evidence is increasingly compelling that our world's resources are finite, especially its atmosphere. To be fully sustained in the long run, growth must take the form of producing more from less.

We will compare Africa's growth patterns since 1950 with those of Europe since the 13th century.³ We will find that most African countries have average real incomes at the same level as in medieval Europe. This suggests grounds for both optimism and caution. Optimism comes from the vastly greater technological possibilities open to African countries today, compared with medieval Europe – mobile phones are just one example. Indeed, China and Russia are now middle-income countries, where 'middle-income' is a multiple of the income levels that were found in medieval Europe. In other words, modern technology has created more room for countries to grow even though they still have corrupt, closed political institutions.

But the same history also suggests the need for caution. European experience shows that the pattern of growth acceleration alternating with reversal can persist for centuries. The transition to modern economic growth is not inevitable. Growth is made sustainable by institutional change. African economies today have achieved levels of development comparable with medieval Europe, but they do not yet have the institutions, such as the rule of law, necessary to eliminate growth reversals and make growth sustainable in the long run. There is a ceiling on what can be achieved without these changes. While African economies are likely to be well below the ceiling, and can continue to grow for a while, their growth is fragile and the ceiling is still there.

AFRICA'S PAST: A LONGER VIEW

What is the evidence from Africa's more distant past? The African story has often been presented as a narrative of unrelenting failure. A good example is the literature inspired by the economist Robert Barro, which sought to explain why African countries grew so slowly between 1960 and 1990.⁴ It is sometimes called the 'Africa dummy' literature. In this context an Africa dummy was an artificial statistical variable, set to 1 for African countries and zero for all others. The literature started from the observation that, when researchers looked for factors explaining country growth in a global sample, most of the lack of growth of African countries was explained, statistically speaking, by the fact that they were in Africa (represented by the large negative coefficient of an Africa dummy).

Recent research in African economic history has revised this story.⁵ Rather than persistent failure, there have been periods of growth, but these were followed by reversals which typically erased the gains made during the previous spurt. Since 1950, in fact, most African countries have followed this pattern of growth and reversal. The two decades after 1950 saw relatively rapid growth, for example, but this ended with the oil crisis of the 1970s. The 1980s and 1990s saw stagnation or even decline. The recent revival of growth dates from the late 1990s, and the first task was to offset the decline of the previous two decades.

International trade is likely to have stimulated African growth far back into the past. The trans-Saharan trade in gold, slaves and ivory from the early medieval period favoured the emergence of large urban centres and elaborate commercial institutions in West Africa and along the edge of the desert. Like Venice and Genoa in Europe, Timbuktu, centre of the once-mighty Kingdom of Mali, prospered by facilitating international trade. Growing trade between Europe and West Africa (including the Atlantic slave trade) also led to increasing commercialisation. But gains at some times were lost in others. None of these developments – and certainly not the slave trade – led to sustainable growth. Again, in the late nineteenth century many African countries benefited from strong growth in the international economy by selling cash crops at favourable international terms of trade. These gains too were lost in the Great Depression of the 1930s.

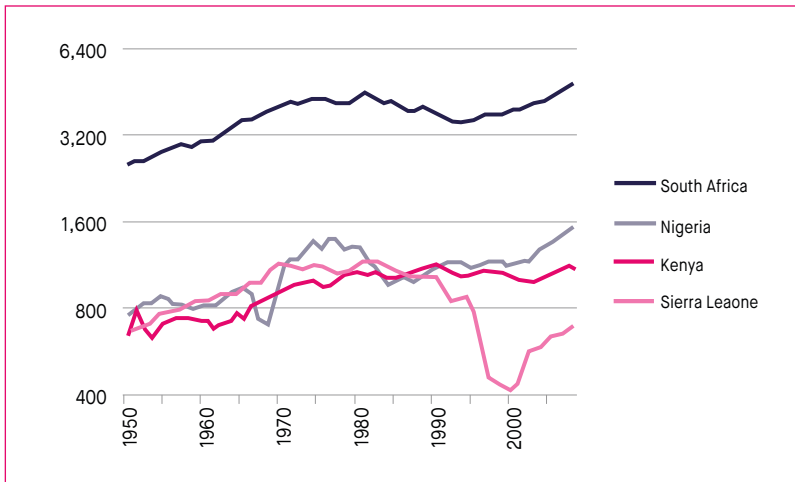
To summarise, the growth that African economies have shown recently has been repeated many times in the past. What are the chances that the outcome anywhere in Africa will be more successful – or more sustainable – than hitherto?

Here it is important to recognise the diversity of Africa's societies. While there are common factors in the growth of African economies, each region has a different physical and cultural endowment, beginning with its own pre-colonial history and culture. Each part of Africa had a different experience of Western colonialism; it is worth noting that Africa's modern borders are largely a legacy of the colonial period. Post-colonial developments also show great variety.

FOUR CASE STUDIES

To simplify, we will focus on four countries: Kenya, Nigeria, Sierra Leone and South Africa.⁷ Figure 1.1 shows the real GDP per head of each country from 1950 through 2008.

Figure 1.1. Real GDP per head in international dollars and 1990 prices, 1950 to 2008: South Africa, Nigeria, Kenya and Sierra Leone



Source: Data from Maddison (2010).

The most striking finding is that today, like other sub-Saharan African countries, they have average incomes on a par with medieval European economies. Indeed, only a handful of African countries have higher incomes than Britain enjoyed at the beginning of the 19th century.

There are differences as well as common patterns. Most obviously, they are not equally poor. South Africa is much richer than Kenya and Nigeria. Sierra Leone used to be close to the others but has fallen behind.

Box 1.3. What are “real GDP” and “international dollars and 1990 prices”

What is real GDP? It is sometimes thought that ‘real’ GDP is an objective measure of the number of things produced. A moment’s thought shows this cannot be the case. It makes no sense to say that an economy that produces nine shirts and one car has made ten things. All the things that are produced must be valued before they are added together. When the values change from year to year (or from one country compared to another), we call it GDP at current prices or ‘nominal GDP’. Real GDP implies the use of a single set of unchanging or constant prices, so that the GDP of all the years (or all the countries) is measured using a common standard.

Constant prices. Figure 1 reports GDP per head in constant prices. The basis of valuation is ‘1990 international dollars’; this is a standard for historical comparisons of economic performance across many years and countries (Maddison, 1995; 2010). Dollars are the unit. ‘International’ dollars mean that the prices used to value output are average international prices rather than U.S. dollar prices. The year these prices are taken from is 1990.

A measure of absolute poverty. This measure gives rise to a useful benchmark. In 1990, the World Bank poverty level for an individual was a dollar per day, or \$365 per year. This suggests that no society can survive for long with average incomes much below \$400 in international prices of 1990, taking into account that even the poorest economies have elite families with income many times higher than the poorest. Thus \$400 in international prices of 1990 is usually taken as the minimum or 'bare bones' level of subsistence of a society.

Sierra Leone

In Sierra Leone average incomes in 2008 were below \$750 (in 1990 prices), making it by far the poorest of the four countries. How did Sierra Leone arrive at this position? The country enjoyed favourable prospects in 1950 owing to its mineral wealth. While it kept pace with other countries until the early 1970s, the transition to an increasingly repressive one-party state in 1973 resulted in GDP per head stagnating at around \$1,100 a year through the 1980s. The major decline came with the outbreak of one of Africa's deadliest civil wars in 1991. This war lasted ten years, killing more than one per cent of the population and turning nearly half into refugees.⁸ After the war the economy recovered, but average incomes in 2008 remained no higher than in 1950.

Sierra Leone shares many of the features prominent in the literature on Africa's failed states, including the extensive use of patronage to maintain an elite coalition in power, limited control over the use of violence, and vulnerability to external shocks. William Reno describes the reliance on patronage systems as a 'shadow state', in which rulers use their ability to intervene in their countries' economies to strengthen their political base.⁹

In Sierra Leone, a poor country with fragile institutions, 'all politics is real politics; people risk death when they make political mistakes'.¹⁰ Sierra Leone's recent civil war is a prime example. With the transition to independence, which gave a greater political voice to groups that were marginalised during the colonial period, the coalition of coastal elites of that

earlier era was no longer sufficient to limit violence. The country's descent into civil war resulted from the combination of this unstable coalition and the effects rippling from conflict in neighbouring Liberia. The 'shadow state' or patronage networks played an important role in state policy, as well as in the promotion of violence in Sierra Leone.

Kenya

In 2008 the average Kenyan had an income of around \$1,000 (in 1990 prices). Kenya's economic performance since 1950 has been less volatile than the other three countries, but it shares many of their features. Its economic success in the 1950s and 1960s was due largely to agricultural exports, but Kenya also benefited from its dominant position in East Africa. However, mismanagement of revenue earned in the coffee boom of the 1970s along with the increasing use of state funds for political patronage led to a poor economic performance during much of the 1980s. A brief recovery in the late 1980s came to an end with outbreaks of ethnic violence in the aftermath of highly contested national elections in 1992 and 1997. This was compounded by droughts and high oil prices due to the Gulf War.

Kenya is wealthier today than Sierra Leone, but it is not long since these two countries were at the same level. Today, Kenya's state institutions are also fragile. Recurrent ethnic violence illustrates that competition between patron-client groups can still lead to violence. As a result of the interconnection between ethnicity and party allegiance in Kenya, competition between parties at election time is to a large extent competition between ethnic groups. The link in Kenya between ethnic violence and elections highlights the risks of political competition when violence is barely contained in normal times.

In Kenya, privileged access to economic resources is one of the 'carrots' that can be used to ensure the support of ethnic coalitions. This is reminiscent of the European historian of the 'freedoms' which, according to the economic historian Larry Epstein, undermined market integration in Europe because they took the form of privileges granted to elites in order to sustain their political support.¹¹

Nigeria

In Nigeria in 2008 average incomes were around \$1,500 (at 1990 prices), substantially higher in Kenya and twice the level of Sierra Leone. In 1958 the World Bank claimed that Nigeria's prospects for growth based on its agricultural exports (including palm oil, cocoa, groundnuts, cotton and rubber) were good, but that they depended on 'Nigerians' success in eliminating tribal or regional antagonisms and maintaining reasonably high standards in public administration'. In fact, post-independence political conflict has resulted in several growth reversals. The Biafran War of the late 1960s reversed earlier gains, and GDP per head fell to below its 1950 level. The oil boom of the 1970s led once again to positive growth, but oil revenue had little lasting impact on per capita GDP, which declined in the 1980s and remained stagnant through the 1990s. Since 2000, oil production and expansions in agriculture and services have led to a period of renewed economic growth, but the country remains overwhelmingly dependent on its energy sector.

A hopeful sign for Nigeria is that politics is not everything. Nigeria is home to many of Africa's largest private corporations, and has a vibrant civil society. As of 2012 the private sector employed 80 per cent of Nigeria's workforce and generated most of its exports.¹² In other words, Nigeria's elite does not fear interests that are organised outside the state as potentially damaging competition that must be suppressed. This is not to say that power and wealth are fully separated, as is needed for an open-access society. Moreover, the state remains vulnerable to factional disputes in which violent religious mobilisations are playing an ominously increasing role.

South Africa

In 2008 average incomes in South Africa stood at nearly \$5,000 (in 1990 prices), three times the level in Nigeria. South Africa's advantage has a long history. As early as 1950, the average South African was wealthier than Nigeria today. South Africa became the continent's economic leader following the mineral discoveries of the nineteenth century. Foreign investment and public revenue generated by the gold mines allowed the South African government

to pursue an aggressive strategy of state-led industrialisation in the 1920s. Since then South Africa has been the most industrialised economy in sub-Saharan Africa. Manufacturing outpaced mining and agriculture as South Africa's leading industry by the 1970s, and later in that decade its GDP per capita peaked just below \$4,500, a level only regained in 2006. During the 1980s, however, protests against the repressive apartheid regime caused Africa to become politically unstable. The gold price fell at the same time. The result was a period of economic contraction. Growth was resumed only with the coming of majority rule in 1994.

Even more than Nigeria, South Africa has a strong corporate sector. While economic growth has been steady since the mid-1990s, high rates of inequality and youth unemployment have limited the benefits of growth to a small proportion of the South African population. In fact the very idea of the 'average' South African is problematic (in a similar way you could well question who is the average Nigerian, Kenyan, or Sierra Leonean). Fault lines in the coalition of the ruling African National Congress and the trade unions threaten to undermine the party's base of political support. Unequal distribution ensures that disputes over ownership and rewards quickly become political and threaten violence.

To summarise, these four countries have shared features as well as differences. One is that economic growth has been significant, but has not been sustained. Growth has been followed by reversal. Another common feature is that an important trigger of reversals has been internal conflict. Nigeria suffered a devastating civil war over the Biafra secession in the late 1960s. South Africa experienced prolonged instability as the apartheid regime disintegrated in the late 1980s. One of Africa's deadliest civil wars broke out in Sierra Leone in 1991, ending only in 2002. And Kenya has seen repeated violence associated with contested election outcomes in 1992, 1997, and 2007.

EUROPE'S PAST: PARALLELS WITH AFRICA TODAY

European history from the thirteenth century to the nineteenth also suggests a pattern of periods of economic growth followed by reversals. The European pattern is consistent with the experience of the African

continent to the present day. We base this judgement on new estimates of real national income per head in Europe since the thirteenth century by ourselves and other CAGE associates. We focus on four major European countries: England (later Great Britain), Holland (later Netherlands), Italy and Spain.¹³

Box 1.4. The measure of poverty

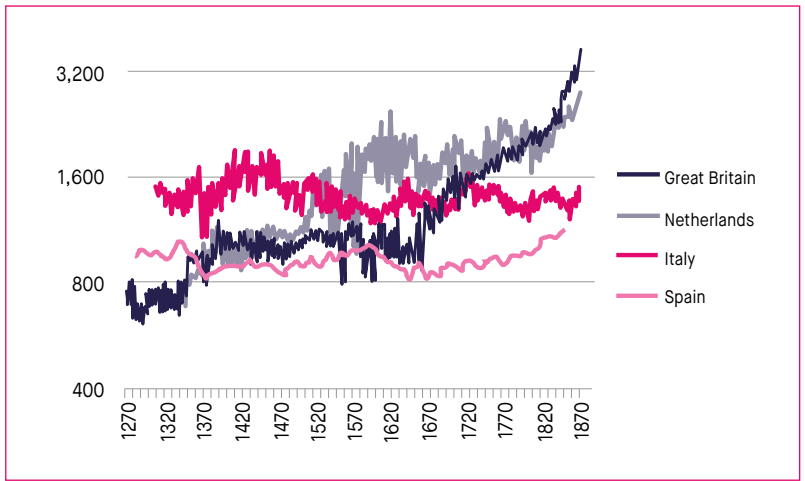
Poverty is not what it used to be. We take \$400 in international prices of 1990 as the annual cost of 'bare bones' subsistence. Is the purchasing power of \$400 dollars the same today as it was in medieval Europe? Not exactly. Today you can buy a smartphone for \$400. The price of a smartphone in thirteenth century London was certainly prohibitive and arguably infinite. More generally, the range and variety of goods and services you can buy today with a dollar at 1990 prices is far wider than in any past period. To be poor today is different from being poor in the past because the poor have more choices, even if they are still poor. This illustrates the problem that measuring historical change in living standards cannot be exact. But many dimensions can be estimated with relative precision, for example nutritional quantity and quality, the availability of clothing, shelter, heat, and light, access to the written word, the time taken for news to travel, and so forth. Our estimates of GDP per head reflect what can be measured and this provides the basis of meaningful comparisons over time.

Today's poor live longer. Because of advances in health care and disease control, poor people have many more years of active life and health than in the past. In Sierra Leone in 1960, for example, average life expectancy was 30 years, and this was comparable to life expectancy in medieval Europe. Today average incomes in Sierra Leone are no higher than in 1960, but life expectancy has risen from 30 years to 45 years. Poverty means that disease control remains fragile, as the recent Ebola outbreak reminds us. (Source: World Bank, World Development Indicators 2014). Whether it is better to live longer in acute poverty is a matter for debate.

Figure 1.2 shows six centuries of economic growth in Western Europe. By the late Middle Ages Western Europe was already well above bare-bones subsistence, which we take to be \$400 (see Box 1.4). On the eve of the Black Death in 1348, average incomes were around \$750 in England and Holland and substantially more than this in Italy and Spain. At this point economic growth had already taken place, bringing Western Europe to a level of development similar to that found today in much of sub-Saharan Africa. Despite this, several more centuries would go by before the first of these countries made its breakout to modernity.

The figure underscores the fact that low standards of living in pre-industrial economies are not due to persistent failure. Rather, they are due to inconsistency; the economy succeeds from time to time, but then the gains are lost. Long-term stagnation results from alternating periods of growth and decline. This is illustrated in Figure 1.2 by Italy and Spain.

Figure 1.2. Real GDP per head in international dollars and 1990 prices, 1270 to 1870 Britain, Netherlands, Italy, and Spain



Source: Data from Malanima (2011); Álvarez-Nogal and Prados de la Escosura (2012); Broadberry et al. (2012). Note that the apparent drop of incomes in Holland in the early 19th century is the result of a break in the territorial basis of the estimates, with the pre-1807 data referring to Holland, the richest part of the Netherlands, and the post-1807 data covering the whole of the Netherlands.

Violence contributed to growth reversals. There was hardly any time during this period when two or more of the European powers were not engaged in conflict somewhere.¹⁴ Borders changed frequently, and this also brought discontinuity of the political and legal framework of the disputed territories. Most wars were small and short, but a clear exception was the Thirty Years' War, fought bloodily on the continent of Europe from 1618 to 1648. Although the sea offered protection from external attack, England experienced bouts of internal violence; power struggles within the dominant coalition led to the Wars of the Roses in the fifteenth century and the Civil War of the seventeenth century. The revolt of the Dutch against the Habsburg rule of the Low Countries, which led to the foundation of the Dutch Republic in the late sixteenth century, also illustrates the instability of the Spanish state.

In the eighteenth century, as Figure 1.2 shows, a small part of Europe in the North Sea region broke the mould and made the transition to modern economic growth. The result was a long-term reversal of fortunes. In the early fourteenth century Italy and Spain were richer in average incomes than Britain and Holland. The second half of the fourteenth century was marked by the Black Death and further outbreaks of plague. The first growth spurt in the North Sea region followed the Black Death, after which average incomes remained on a relatively high plateau rather than falling back to their pre-1348 level. This was followed by further waves of growth: first in Holland, during its Golden Age (1500-1650), and then in Britain from the mid-seventeenth century. By the nineteenth century, Britain and Holland had clearly outpaced Italy and Spain. This is sometimes called the Little Divergence.

To what extent are the growth booms and reversals experienced by African countries since 1950 comparable to those that occurred in medieval Europe? Because the European data in Figure 1 cover a much longer period than the African data in Figure 2, European growth may at first sight look smoother than African growth. In fact, however, the scale of reversals is actually quite comparable.

Box 1.5. The Great and Little Divergences

The Great and Little Divergences took place between 1300 and 1800.

In the Great Divergence, Europe became much wealthier than China. The Great Divergence is often also associated with eighteenth-century developments such as the European Enlightenment and the Industrial Revolution, and the first era of globalisation in the nineteenth century. In fact, these came very late in the Great Divergence. The roots of the Great Divergence lie far back in the Middle Ages and so well before these events.

The Little Divergence took place within Europe, and was reflected in the emergence of the North Sea region, England and Holland, as the most prosperous part of the continent. Again, the Little Divergence became obvious in the eighteenth century but its roots can be traced much earlier.

Table 1.1. Real GDP per head: the variability of annual growth in Africa and Europe compared, standard deviations in percentage points

	1270 to 1870	1950 to 2008
Europe:		
UK	6.4	1.8
Netherlands	8.2	2.1
Italy	5.2	2.5
Africa:		
South Africa	...	2.3
Nigeria	...	6.7
Kenya	...	4.2
Sierra Leone	...	6.6

Sources: Africa, as Figure 1.1. Europe, 1270–1879, as Figure 1.2; 1950 to 2008, from Maddison (2010).

Notes: UK is England until 1700 and Great Britain thereafter; Netherlands is Holland until 1807. Spain is excluded, although the same calculations could be done for Spain using the sources cited above. These would suggest an opposite pattern: higher variability since 1950 than before 1870. The reason for this is technical: Spanish GDP in the medieval period is estimated by a methodology that smoothes year-on-year variation, artificially reducing the standard deviation of the annual growth rate.

The variability of economic growth can be measured by the standard deviation of a country's annual growth rate. This reflects the average distance of the growth rate in each year above or below the average over a longer period. Table 1.1 shows that, as European societies have become more developed, the variability of annual growth of their economies has declined. Before 1870 the standard deviation of annual growth was 6 to 8 percentage points for Britain and Holland, and more than 5 percentage points for Italy. Since 1950, in contrast, European economies have grown relatively smoothly, with variation in annual growth rates of less than 3 percentage points.

When we compare our four African economies, we see that economic growth in Nigeria, Kenya, and Sierra Leone has been as variable as economic growth in medieval Europe. Only South Africa has achieved a growth pattern as smooth as that of Western European economies.

HOW DID EUROPE ACHIEVE THE TRANSITION TO MODERN ECONOMIC GROWTH?

From 'limited access' to 'open access'

The Little Divergence culminated in a transition to sustained long-run growth first in Great Britain during the Industrial Revolution, then in other countries of northern Europe with similar institutional frameworks.

The sources of this divergence have been much debated. There are convincing reasons to think that this transition depended on a balancing act: the emergence of a new kind of government that balanced the building of state capacity with constraints on the executive.

England's Glorious Revolution of 1688 illustrates this balancing act.¹⁵ By confirming the supremacy of Parliament, the Glorious Revolution placed effective constraints on the executive powers of the Crown. At the same time, it unified the domestic market by ending local monopolies, and made the tax raising powers of Parliament legitimate; this led the British state to become better funded and more centralised than ever before, giving the government much greater capacity to intervene, particularly in foreign affairs.

It is important to realise, however, that the emergence of a powerful state subject to the rule of law was a lengthy process, not a single event. It is wrong to place all the emphasis on 1688. The Glorious Revolution was just one moment in a lengthy series of institutional developments, the origins of which can be traced as far back as the Magna Carta of 1215 which first limited the rights of the Crown. In between there were movements backward as well as forward. The economic effects of these movements were not felt overnight. A moment's reflection suggests that it takes a long time for people to gain confidence in the law and secure property rights.

Economists Douglas North, John Wallis, and Barry Weingast have written about the balancing act involved in a state that is both powerful enough to be effective, yet also restrained by the rule of law. In their framework the state is not a single actor to be controlled or enabled; rather, how the state works depends on how a society organises itself to limit violence. They classify all societies in two major types of organisation. Access to power is either 'open' or 'limited'. In this view the wealthy democracies are based on open access. With open access, rights are impersonal and belong to everyone equally. The state has a monopoly on violence. States in open access orders are constrained by highly developed civil societies. Civil society is made up of networks and organisations that have legal existence independent of the life of any private person and do not depend on the ruler's political favour. There can be many examples but in economic life the incorporated private enterprise is one of the most important.¹⁶

Limited-access societies come in many varieties. This is not surprising, since they have dominated through most of human history. But all limited-access societies have common features. One feature of limited-access societies is the everyday experience of violence and threats of violence. Another feature is that under limited access it is men's access to power that is limited; with rare exceptions, women have been excluded altogether (we return to this in Chapter 3). These two features can be linked by the historical fact that men have shown a greater capacity for violence than women.

Limited-access societies, it is argued, evolved to suppress the universal violence of continual banditry and clan warfare. The historian Christopher

Wickham, for example, emphasises the importance of patronage networks in maintaining the small, fragmented states that emerged following the collapse of the Roman Empire.¹⁷ Elite coalitions emerged that had the capacity to monopolise land and resources, subjugate the workers, capture the rents that they created, and agree to share them. Business was politics, and politics was also business. To preserve their wealth, they kept out competitors from outside their ranks, defined by kin, clan, or ethnic group. Thus access was limited. Men like Thomas Cromwell or Dick Whittington could rise to wealth and power from outside only through special personal favour.

A limited-access order could thus suppress conflict, and under peaceful rule the result would be a degree of prosperity. In the right conditions the degree of prosperity might be considerable. Russia and China today provide examples of countries where GDP per head stands at around \$10,000 (in international prices of 1990) although they retain limited-access orders. Arguably, this might suggest that all African countries can double or triple their average incomes without much further institutional development. Today, however, both Russia and China face the existential problem of maintaining internal and external stability. Their problems are growing: both countries are increasingly troubled by confrontational ethnic politics and disputed borders. Under these circumstances continued peaceful development is just a hypothesis.

In Europe's limited-access societies, peace was maintained only as long as those making up the elite could deter each other from grabbing bigger shares. These coalitions were vulnerable to disruption by economic and political shocks, ranging from famine, plague, and external attack to changes in the relative value of resources. If the shock was large enough, the result would be foreign war or a collapse into civil conflict.

The 'doorstep conditions' for change

Today's societies based on open access have evolved from limited-access orders. How has this come about? Slowly, in the North-Wallis-Weingast view, European societies began to move across a doorstep from limited access into open access.

This movement was permitted, but not guaranteed, by meeting three 'doorstep conditions'. First, the elite allowed the rule of law to govern the behaviour of its own members, so that no one person was above the law, however wealthy or powerful. Second, civil society grew stronger and both civil society and the state evolved forms of organisation that were impersonal and perpetually-lived, such as bureaucracies and corporations, so that they did not depend on the physical existence of powerful sponsors such as aristocrats or oligarchs. Third, the government consolidated its control of the military, so that armed force did not belong to factions or warlords. Meeting these conditions would eventually support open access to power and resources: everyone could have property rights and everyone had the same political rights. Business and politics could be separate. You could still mix business and politics by choice, but the links would be relatively transparent and open to scrutiny. The links would also be voluntary: you could lose wealth and retain political rights, and you could lose office and keep your wealth.

Many other things happened at the same time, contributing to the virtuous circle of economic growth. Violence diminished in society. To lose one's place in the elite ceased to be a death sentence. Under the rule of law it became advantageous to invest and work with others, which meant waiting to earn a productive return on investment, rather than to seize the moment to rob or cheat. As the returns to enterprise and learning increased, the economy diversified and ceased to rely on single-commodity exports. Growth became more resilient.

The open-access society did not lie at the end of a one-way street, however. To meet the doorstep conditions for movement to open access did not guarantee that the move would actually be made. Movement could also go backwards. By 1913 Russia had taken some first steps along this path but the First World War pushed it sideways into communism. In the 1920s Germany was well on the way to a liberal democracy but the Great Depression caused it to relapse into fascism. At best, meeting the doorstep conditions improved the chances of a successful transition in the long run.

These ideas have deep implications for the sources of economic growth. It seems that European countries made their transition to modern economic

growth by building up the conditions for open access; it seems likely that open-access social orders are less vulnerable to breaks in progress that throw the economy back. Recent research has confirmed this idea empirically by demonstrating that open access societies show fewer growth reversals.¹⁸ In other words, institutional changes allowed European economies to invest, grow, and diversify. Growth was spread across a widening range of activities, resulting in less dependence on staple commodities that were vulnerable to periodic market setbacks.

WHAT ARE AFRICA'S OBSTACLES TO SUSTAINED GROWTH?

In similar fashion to the literature on Europe, studies of obstacles to growth in Africa have explored the tension between the need to increase the capacity of the state and the importance of constraining its ability to violate property rights.¹⁹ As two Africa specialists have written, the challenge

...that every society faces is to provide the state with the means to fulfil its legitimate duties, while at the same time preventing it from misusing these means to suppress dissent and expropriate private wealth.²⁰

In a recent survey, Daron Acemoglu and James Robinson bring these strands of thinking together, arguing that:

To generate sustained economic development requires not just the formation of centralised polities, but also the removal of [their] absolutist and patrimonial tendencies.²¹

They argue that it was the late formation of centralised states, together with their absolutist nature, that provided the foundation for Africa's relative poverty today. African states are too often endowed with too little power to collect taxes, enforce property rights, and regulate violence, combined with too much power to extract bribes and confiscate the fruits of enterprise.

The idea of a 'gatekeeper state' links limited capacity to govern with predatory tendencies. A gatekeeper state maintains its authority by controlling access

to external markets. The result is that those who need access to external markets in order to import goods and make trading profits have no choice but to cooperate with government officials and recognise official authority.

While Sierra Leone provides one illustration, the idea of a gatekeeper state can be applied more widely to pre-colonial, colonial and post-independence states in Africa.²² Colonial institutions had many deficiencies, and this is one reason why the expansion of the franchise and political competition that came with independence gave rise to optimism about Africa's future in the 1950s and 1960s. Unfortunately, the democratic institutions introduced at independence came under almost immediate threat in many of these countries, as public funds were used for patronage projects and democratic governments were replaced by military dictatorships and one-party states. The return of many African countries to democracy since the 1990s, like the Arab Spring of more recent years, has again revived optimism, but the underlying fault lines that make democracy unstable are still visible.

To summarise, African economies face shared obstacles to economic growth. Table 1.2 offers some simple measures of these obstacles.

First, as already shown in Table 1.2, in most African countries economic growth is not sustained; growth is followed after a time by reversal. When future prosperity is unreliable, the incentive to invest in the future and work together for the future is weakened by comparison with incentives to grab something now at others' expense.

Second, growth is unstable in part because African economies tend to show reliance on a narrow range of activities, usually based in agriculture and resource extraction. Farmers produce a few crops and export commodities. Table 1.2 shows that in recent years Nigeria still retained two out of every five workers in agriculture, and Kenya three out of five. This level of dependence on agriculture was last seen in England in the eighteenth century and elsewhere in Western Europe in the nineteenth century. Only South Africa is significantly more industrialised.

Table 1.2. Development indicators: South Africa, Nigeria, Kenya and Sierra Leone

	South Africa	Nigeria	Kenya	Sierra Leone
GDP/head in 2008 ^a	4,793	1,524	1,098	686
Standard deviation of annual GDP/head growth rate, 1950 to 2008, in percentage points ^b	2.3	6.7	4.2	6.6
Agriculture, per cent of labour force ^c	15.0	58.9	48.3	...
Tax revenues, per cent of GDP ^d	27.8	14.8	25.7	13.8
Firms expecting to give gifts when meeting tax officials, per cent ^e	3.1	22.9	32.3	8.6
Intentional homicides per 100,000 people in 2012 ^e	31.0	20.0	6.4	1.9

Sources:

a As Figure 1.1.

b As Table 1.1.

c World Bank, *World Development Indicators 2014*, available at <http://data.worldbank.org/data-catalog/world-development-indicators/> (accessed 15 September 2014). Figures are for 2012 or the nearest available year.

d *African Economic Outlook*, available at <http://www.africaneconomicoutlook.org/en/statistics/> (accessed 15 September 2014).

e United Nations Office on Drugs and Crime, *'Homicide Counts and Rates 2000-2012'*, available at <https://www.unodc.org/gsh/en/data.html> (accessed 15 September 2014). Figures are for 2012.

Third, African growth is unstable because violence is poorly suppressed. In 2012, as Table 1.2 reports, Kenya reported 6.4 intentional homicides per 100,000, Nigeria 20, and South Africa 31 (Sierra Leone reported only 1.9;

it is unclear whether the latter figure reflects genuine war weariness or just deficient reporting). In Northwestern Europe, by comparison, homicide rates have been below 3 per 100,000 for more than 300 years (Eisner 2003).²³ Of course there are many kinds of violence and Europe has also experienced violent wars and imposed warfare on others. On one estimate, from 1960 to 2002 more than one and a half million people were killed in battles in Africa, about 40 per cent of the global total. This made Africa the deadliest of the world's regions over that period. More than that, because Africa contains around only around 13 per cent of the world's population, the probability of death in armed conflict in that region was more than four times that in the rest of the world.²⁴

Finally, just as they lack capacity to control violence in a lawful way, many African states show limited capacity to tax, spend, and regulate within the law. A state that cannot raise taxes cannot supply public goods, including protection against violence and clean law enforcement. When protection is granted only in return for gifts and bribes, there is a vicious circle: security is privatised, justice is replaced by privilege (literally, 'private law'), and no one wants to pay the tax on top of a bribe. In the seventeenth century growing fiscal capacity was an important signal of the superior quality of the institutions of governance emerging in the North Sea region.

As economists we are particularly interested in learning about a state's fiscal capacity. Where revenues are raised in Africa, they tend to come either from resource rents such as Nigeria's oil revenues, or from taxes on agriculture and trade that significantly worsen the efficiency with which resources are allocated across the economy. Naturally, scholars have debated whether such deficiencies have their roots in the colonial and even pre-colonial past.

Some recent research has stressed that colonial rule shaped the modern tax capacity of African states. But other research has stressed the greater influence of post-independence political imperatives.²⁵ In practice, neither distant history nor the recent past can be ignored. The importance of history is shown by the relative positions of our four case studies, shown in Table 1.2, which are of long standing. While benefiting from tax reforms since

1995, South Africa already raised considerably more revenue per capita in the first half of the twentieth century. Nigeria, on the other hand, has underperformed relative to expectations both during the colonial period and since 1960, while Kenya has done substantially better, even during the colonial period. One possible explanation is that settler regimes such as those in South Africa and Kenya developed more effective tax systems that were less dependent on trade taxes, because they needed coercive strength.²⁶

But history cannot explain everything. Sierra Leone's revenue collections dipped very low during the civil war. Until this time, however, Sierra Leone raised considerably more revenue per capita than Nigeria, illustrating how violence can undermine fiscal capacity.

The direct link from violence to poor fiscal capacity is not the only one that is possible. Deficient fiscal capacity causes the government to lose tax revenues partly because its agents want more income than their salaries provide. Underpaid officials become corrupt and steal revenues before they reach the exchequer. Deprived of revenues, the government cannot redistribute resources legitimately to its political base, so politicians instead resort to secret patronage, which hollows out the state's legitimate functions.²⁷ In that setting efforts to clean things up disrupt established interests and expectations, and provoke resistance, which can turn violent. The result is to make corruption and violence alternatives: if you try to have less corruption, you may get more violence. And the converse may be true as well.

MOVING TOWARDS THE RULE OF LAW

The rule of law as infrastructure

This chapter implies that one of the most important projects that any society can embark on is to build the rule of law. The rule of law is part of a society's infrastructure. What is infrastructure? Usually we think of infrastructure as physical systems. Infrastructure is the systems that deliver goods, electric power, clean water, and other essential services. When the infrastructure works well we rely on it and we expect it to be there. We press the switch

and a light comes on. We flush the toilet and the sewage flows away, out of sight. We don't even think about it.

The rule of law is also infrastructure. Arguably it is more important than any power cable or drainage system. This is because the ability of any society to lay cables and sewers rests in part on the expectation of officials that the primary purpose of the contract is to build the network, not to pay off supporters. It also relies on the expectation of the contractor that the equipment will not be stolen, the manager will not be abducted and held to ransom, and the contract will be paid on completion. When the rule of law is in place, the contract is turned into a switch you press so that capital is created.²⁸

Good policy will invest, first and foremost, in the rule of law. This means establishing simple laws that favour fair dealing, a police force that is professionally trained and equipped, courts that deliver justice openly and without favour, salaries that enable officials to live without bribes, and a culture that stigmatises backhanders and malfeasance.

On one interpretation, the implied policy advice to government would be: Enforce the law. But enforcing the law is not the same as accepting the rule of law. We reject the view that any government can simply coerce society into accepting the rule of law. That is not where the rule of law comes from. Rather, the first step is for the elite members of a society to organise themselves in such a way that they can give up private violence and allow the state to monopolise violence. The rule of law comes first from its social acceptance, and only then from its imposition.

Policy matters

The question then becomes: What can policy do to promote acceptance of the rule of law? A key to this is 'organisation': the elite members of a society must organise themselves in such a way as to reduce the resort to violence and agree to subject themselves to the rule of law. Here better organisation is organisation that is more coherent and capable, above all more durable. The more durable are the state and private organisations such as incorporated enterprises, the easier it will be for all society's members

to cooperate for the sake of future gains from investment and education, rather than fight each other for immediate spoils.

An issue for policy makers is that the organisations that need this investment are often under attack in the public arena – sometimes violently. In public life government bureaucracies and private corporations are often seen as the property of the privileged – and indeed they generally are. When children are malnourished and disease stalks the shanty towns, why is it a priority to pay lawyers and law enforcers and so give more to those that already have?

In fact, this issue replicates a more familiar problem on a wider scale. How much should a poor society pay a policeman? Precisely because the police have the power to extort bribes, they must be paid enough that they are not too easily tempted. When everyone else is desperate, it is important that the police are not desperate too, even if the result is unfair.

What difference can good policies make in this direction? Institutions cannot change quickly. A society's institutions are rooted in the daily lives, actions, beliefs, and expectations of all its citizens. Attempts to change them will encounter resistance. There is reason to think that large, abrupt changes in a society's legal regime can promote law-breaking. If gift exchange is customary when meeting government officials, for example, it is probably reflected in lower government salaries. Faced with a refusal to offer gifts, the official might retaliate in some other direction: for example, if law-breaking was previously widespread, by threatening to expose some other illegal behaviour by the reluctant giver.²⁹ Either the law is ignored or everyone is threatened by exposure. This is the case for gradualism.

A case for gradualism is not a case for doing nothing. Policy matters. While history, geography, and institutions provide a legacy that cannot be changed, good policies can still make a measurable difference.³⁰ If change is slow and if repeated failure is also possible, all the more reason to start now.

Good political leadership can also load the dice in favour of change. This is because many of the events that disrupt growth are political acts. The decision to rig an election, or contest a fair election result, can trigger violence. Thus, by their behaviour leaders influence the behaviour of

others through their expectations and the incentives they perceive. Good leadership enabled a peaceful transition from apartheid in South Africa, just as good leadership gave most European countries a peaceful transition from communism. It was easy to envisage much worse outcomes. Thus, good leaders made a clear difference.

IMPLICATIONS FOR POLICY MAKERS

Africa's growth performance in the first decade of the twenty-first century has led to speculation that the continent is entering a new century of sustained economic growth. Such a view, however, raises a number of question marks when the current boom is put into historical context. As was the case in previous boom periods, high external demand for natural resources — particularly oil, but also land and cash crops — is at the heart of this rapid growth. Without institutional change, therefore, further growth reversals can be expected. Indeed, the multi-party democracies established in the 1990s are already showing considerable strain in several countries across the continent, with military coups and ethnic violence hindering what is already a fragile electoral process.

Our research on European economic history highlights the fact that the pattern of rapid economic growth followed by reversals can be repeated over a very long period of time — in Europe's case, half a millennium. With average incomes in many African countries today comparable to Europe in the Middle Ages, such a comparison suggests that it will be difficult for Africa to break free from this historical pattern without significant institutional change. The main reason is that institutions in many African countries still have many of the features of a 'limited-access' social order. In this context, policy should focus on:

- Good policy will foster a robust civil society that can thrive outside of state control. This must include nongovernment organisations that have permanent legal status and do not depend on strong leaders and patronage, or on informal ties to power.
- While such organisations have many varieties, one is particularly important: the sphere of corporate enterprise. Thus fostering the private sector is part of good policy. We will see in chapter 2 that sustainable

economic development and job creation are inconceivable without larger firms. Incorporated private business is an ultimate expression of a society's willingness to allow its members to invest in the future and wait patiently for productive returns. Fostering the private sector does not mean treating rich people favourably. It begins with making it easy to start and register a business and protecting business property against theft and confiscation.

- Good policy will invest in the legal framework of the economy, and also in the apparatus of the law and impartial law enforcement. This means courts that are open to the press, non-political appointment of court officers, security of tenure for judges, decent salaries for police officers, and a social consensus that it is normal to punish senior political and business leaders if they break the law.
- Finally, good policy will foster the government's fiscal capacity. This means paying tax officers a decent salary, encouraging a diverse tax base, easing the conditions for starting and registering a business, setting taxes that are simple and transparent with few loopholes and concessions, and taxing many activities and many people lightly.

Reading these recommendations, anyone might be forgiven for thinking that here is a recipe for apple pie. But there is more. These items are not randomly chosen from a longer list of desirables: they really deserve priority. Attempting them does not guarantee that apple pie will be the result. Most societies that have succeeded at them have done so only after repeated attempts. There is only a chance of success. But there can never be success if we do not try. Good leadership is also vital. In other words, these are not just lessons for specialists and technocrats. They are lessons for all who hold or aspire to office, including the highest offices of all: presidents, prime ministers, and their political advisers.

REFERENCES

- Acemoglu, D. and M. Jackson (2014), 'Social norms and the enforcement of laws', NBER Working Paper no. 20369 (National Bureau of Economic Research, Cambridge, Mass.).
- Acemoglu, D. and J. A. Robinson (2011), 'Why is Africa poor?' *Economic History of Developing Regions*, 25 (1), 21-50.
- Acemoglu, D., S. Johnson, and J. Robinson (2005), 'The rise of Europe: Atlantic trade, institutional change, and economic growth', *American Economic Review*, 95, 546-579.
- Álvarez-Nogal, C. and L. Prados de la Escosura (2013), 'The rise and fall of Spain, 1270-1850', *Economic History Review*, 37(1), pp. 1-41.
- Arbache, J.S. and J. Page (2009), 'How fragile is Africa's recent growth?', *Journal of African Economies*, 19, 1-24.
- Arrow, K.J. (1972). 'Gifts and exchanges', *Philosophy and Public Affairs*, 1(4), 343-362.
- Barro, R. (1991), 'Economic growth in a cross section of countries', *Quarterly Journal of Economics*, 106 (2), 407-443.
- Baskaran, T. and A. Bigsten (2013), 'Fiscal capacity and the quality of government in sub-Saharan Africa', *World Development* 45, 92-107.
- Bates, R.H. (2010), *Prosperity and Violence: The Political Economy of Development* (New York: Norton).
- Bates, R.H., J.H. Coatsworth, and J.G. Williamson (2007), 'Lost decades: post-independence performance in Latin America and Africa', *Journal of Economic History*, 67: 917-943.
- Broadberry, S., B. Campbell, and B. van Leeuwen, 2013. 'When did Britain industrialise? The sectoral distribution of the labour force and labour productivity in Britain, 1381-1851', *Explorations in Economic History*, 50(1), pp. 16-27.
- Broadberry, S., B. Campbell, A. Klein, M. Overton, and B. van Leeuwen (2011), 'British economic growth, 1270-1870: an output-based approach' (London School of Economics).
- Broadberry, S., B. Campbell, B. van Leeuwen, and J.L. van Zanden (2012), 'Reversals of fortune: Holland, Britain and the rise of the North Sea area, 1270-1870' (London School of Economics).
- Broadberry, S., and L. Gardner (2014). 'African economic growth in a European mirror: a historical perspective'. *The Economic History working papers*, 202/201 (London School of Economics).
- Cameron, R. (1967), 'England, 1750-1844', in R. Cameron, O.A. Crisp, H.T. Patrick, and R. Tilly (eds.), *Banking in the early stages of industrialisation: a study in comparative economic history* (New York: Oxford University Press).
- Chenery, H.B. and M. Syrquin. (1975), *Patterns of development, 1950-1970* (Oxford: Oxford University Press).
- Clapham, C. (1976), *Liberia and Sierra Leone: an essay in comparative politics* (Cambridge: Cambridge University Press).
- Collier, P. and J.W. Gunning (2008), 'Sacrificing the future: intertemporal strategies and their implications for growth', in B.J. Ndulu, S.A. O'Connell, R.H. Bates, P. Collier, and C.C. Soludo (eds.), *The political economy of economic growth in Africa, 1960-2000, Volume I* (Cambridge: Cambridge University Press).
- Cooper, F. (2002), *Africa since 1940: the past of the present* (Cambridge: Cambridge University Press).

- Crafts, N.F.R. (1984), 'Patterns of development in nineteenth century Europe', Oxford Economic Papers, 36, 438-458.
- Cuberes, D. and M. Jerzmanowski (2009), 'Democracy, diversification and growth reversals', Economic Journal, 119, 1270-1302.
- Delgado, M, C. Ketels, M. Porter, and S. Stern (2012), 'The determinants of national competitiveness', NBER Working Paper no. 18249 (National Bureau of Economic Research, Cambridge, Mass.).
- Devarajan, S., and W. Fengler (2013). 'Africa's economic boom: why the pessimists and the optimists are both right'. Foreign Affairs, 3 April 2013. Available at <http://www.foreignaffairs.com/articles/139109/shantayanan-devarajan-and-wolfgang-fengler/africas-economic-boom> (accessed 23 June 2014).
- Elischer, S. (2010), 'Political parties, elections and ethnicity in Kenya', in Branch, D., Cheeseman, N. and Gardner, L.A. (eds.), *Our turn to eat: politics in Kenya since 1950* (Berlin: Lit Verlag).
- Epstein, S.R. (2000), *Freedom and growth: the rise of states and markets in Europe, 1300-1750* (London: Routledge).
- Fedderke, J. and C. Simkins (2012), 'Economic growth in South Africa', *Economic History of Developing Regions*, 27, (1): 176-208.
- Feinstein, C. H. (2005), *An economic history of South Africa: conquest, discrimination and development* (Cambridge: Cambridge University Press).
- Fenoaltea, S. (1999), 'Europe in the African mirror: the slave trade and the rise of feudalism', *Rivista di Storia Economica*, 15, 123-165.
- Frye, T. (2010). *Building states and markets after communism: the perils of polarized democracy* (Cambridge: Cambridge University Press).
- Harris, R. (2000), *Industrializing English law: entrepreneurship and business organisation, 1720-1844* (Cambridge: Cambridge University Press).
- Hayek, F.A. (1960). *The constitution of liberty* (London: Routledge & Kegan Paul).
- Herbst, J. (2000), *States and power in Africa: comparative lessons in authority and control* (Princeton: Princeton University Press).
- Hoeffler, A. (2008). 'Dealing with the consequences of violent conflicts in Africa'. Background Paper for the African Development Bank Report 2008. Available from <http://users.ox.ac.uk/~ball0144/consequences.pdf> (accessed 15 September 2014).
- Iyoha, M.A. and D.E. Orioaki (2008), 'Explaining African economic growth performance: the case of Nigeria', in B.J. Ndulu, S.A. O'Connell, R.H. Bates, P. Collier, and C.C. Soludo (eds.), *Political economy of economic growth in Africa, 1960-2000, Volume 1* (Cambridge: Cambridge University Press).
- Jerven, M. (2010) 'African growth recurring: an economic history perspective on African growth episodes, 1690-2010', *Economic History of Developing Regions* 25 (2), 127-54.
- Kalema, V. (2011), 'Sub-Saharan Africa: outlook and challenges', *World Economics*, 12, 105-115.
- Kishtainy, N. (2011), 'Social orders and growth fragility' (Department of Economic History, London School of Economics).
- Lynch, G. and G. Crawford (2011), 'Democratisation in Africa 1990-2010: an assessment', *Democratisation*, 18 (2): 275-310.
- MacLeod, C. (1988), *Inventing the Industrial Revolution: the English patent system, 1660-1800* (Cambridge: Cambridge University Press).

- Maddison, A. (2010), 'Statistics on world population, GDP and per capita GDP, 1-2008 AD', Groningen Growth and Development Centre, <http://www.ggdcc.net/MADDISON/oriindex.htm> (accessed 23 June 2014).
- Malanima, P. (2011), 'The long decline of a leading economy: GDP in Central and Northern Italy, 1300-1913', *European Review of Economic History*, 15: 169-219.
- McMillan, M. S., and K. Harttgen (2014), What is driving the 'Africa growth miracle'? NBER Working Paper no. 20077 (National Bureau of Economic Research, Cambridge, Mass.).
- Mwega, F.M., and N.S. Ndung'u (2008), 'Explaining African economic growth performance: the case of Kenya', in B.J. Ndulu, S.A. O'Connell, R.H. Bates, P. Collier, and C.C. Soludo (eds.), *Political economy of economic growth in Africa, 1960-2000*, vol. 2 (Cambridge: Cambridge University Press).
- Ndulu, B.J., and S.A. O'Connell (2008), 'Policy plus: African growth performance, 1960-2000', in B.J. Ndulu, S.A. O'Connell, R.H. Bates, P. Collier, and C.C. Soludo (eds.), *Political economy of economic growth in Africa, 1960-2000*, vol. 1 (Cambridge: Cambridge University Press).
- North, D.C. (1990). *Institutions, institutional change and economic performance* (Cambridge: Cambridge University Press).
- North, D.C., and B.R. Weingast (1989), 'Constitutions and commitment: the evolution of institutions governing public choice in seventeenth-century England', *Journal of Economic History*, 49: 803-832.
- North, D.C., J.J. Wallis, and B.R. Weingast (2009), *Violence and social orders: a conceptual framework for interpreting recorded human history* (Cambridge: Cambridge University Press).
- O'Brien, P.K. (2011), 'The nature and historical evolution of an exceptional fiscal state and its possible significance for the precocious commercialisation and industrialisation of the British economy from Cromwell to Nelson', *Economic History Review*, 64: 408-446.
- Organisation for Economic Co-operation and Development (2012), *African economic outlook 2012* (Paris: OECD).
- Ostrom, E. (1998). 'A behavioral approach to the rational choice theory of collective action', *American Political Science Review*, 92(1), 1-22.
- Radelet, S. (2010), 'Success stories for "emerging Africa"', *Journal of Democracy*, 21, 87-101.
- Reno, W. (1998), *Warlord politics and African states* (London: Lynne Rienner).
- Reno, W. (2000), 'Clandestine economies, violence and states in Africa', *Journal of International Affairs* 53 (2): 433-59.
- UNODC (United Nations Office on Drugs and Crime). 2013. *Global study on homicide 2013*.
- van Zanden, J.L. and van Leeuwen, B. (2012), 'Persistent but not consistent: the growth of national income in Holland, 1347-1807', *Explorations in Economic History*, 49: 119-130.
- Wickham, C. (2006), *Framing the early Middle Ages: Europe and the Mediterranean, 400-800* (Oxford: Oxford University Press).
- World Bank (1958), *The economy of Nigeria* (Washington, D.C.: The World Bank).

ENDNOTES TO CHAPTER 1

This chapter sums up research listed in the references under Broadberry, and van Leeuwen (2011), Broadberry, Campbell, Klein, Overton, and van Leeuwen (2011), Broadberry, Campbell, van Leeuwen, and van Zanden (2012), and Broadberry and Gardner (2014). Two of the researchers, Stephen Broadberry and Leigh Gardner, are also authors of this policy report. We also draw extensively on the conceptual framework of North, Wallis, and Weingast (2009). The authors thank John Wallis personally for advice.

1. Optimists: Radelet (2010); McMillan and Harttgen (2014). More pessimistic views: Kalema (2011); Arbache and Page (2009). See also Devarajan and Fengler (2013).
2. A longer view of Africa's economic history: Jerven (2010).
3. This is not the first attempt to compare African economic development in the recent past and European development during the medieval and early modern periods. However, previous studies (Bates, 2010; Fenoaltea, 1999) have been limited to a qualitative approach.
4. Inspired by the economist Robert Barro: Barro (1991).
5. See for example Jerven (2010) and Ndulu and O'Connell (2008).
6. Trans-Saharan trade: Lydon (2009). Gains at some times, lost in others: Jerven (2010). The boom of the late nineteenth century: Havinden and Meredith (1996); Hopkins (1973). Prados de la Escosura (2012) gives growth estimates for eight African countries (Sierra Leone, Ghana, Nigeria, the Gambia, Kenya, Uganda, Tanzania, and Mauritius) from around 1880 to 1960.
7. In our four case studies we draw on the work of others as follows: on Sierra Leone, Clapham (1976), Herbst (2000), and Reno (1998, 2000); on Kenya, Mwega and Ndung'u (2008) and Elischer (2010); on Nigeria, World Bank (1958), Iyoha and Orioaki (2008), Collier and Gunning (2008), and OECD (2012); on South Africa, Feinstein (2005), Fedderke and Simkins (2012), and OECD (2012).
8. One of Africa's deadliest civil wars: UNODC (2013: 85).
9. Shadow state: Reno (2000).
10. Real politics: North et al. (2009: 42).
11. Privileges granted to elites: Epstein (2000).
12. Nigeria's private sector: OECD (2012).
13. New estimates: Broadberry, and van Leeuwen (2011), Broadberry, Campbell, Klein, Overton, and van Leeuwen (2011), Broadberry, Campbell, van Leeuwen, and van Zanden (2012), and Broadberry and Gardner (2014). We also draw on related research by Malanima (2011); Álvarez-Nogal and Prados de la Escosura (2012); Leandro Prados de la Escosura is also a CAGE associate.
14. Hardly any time: Pinker (2011: 224-229).
15. The nature of this balancing act has been fiercely debated. The temperature of debate has been raised in part because some scholars have emphasised one side of the balance over another. Our view draws on the work of a wide range of contributors, especially North and Weingast (1989), Epstein (2000), Açemoğlu et al. (2005), and O'Brien (2011). As already mentioned, our interpretation owes much to the most recent stage of this debate, represented by North et al. (2009), Cuberes and Jerzmanowski (2009) and Kishtainy (2011).
16. Access to power is either 'open' or 'limited': North et al. (2009).

17. Following the collapse of the Roman Empire: Wickham (2006).
18. Recent research: Kishtainy (2011).
19. Jerven (2010) identifies two generations of literature on African economic growth since the 1960s. In the first generation, there was a focus on 'too much power': Africa's disappointing economic performance was explained largely by the policies pursued by African governments after independence. For this first generation a major source of growth failures was African rulers' interference in their countries' economies for largely political purposes, in order to seize rents and use them to reward supporters. The result of this analysis was a series of 'structural adjustment' reform programmes in the 1980s and 1990s, which aimed to set limits on the capacity of African rulers and ruling parties to interfere in their economies. The second generation emphasised other factors besides policy failure, and looked further into history to understand the origins of Africa's failed institutions. Among the factors that emerged was deficient state capacity, or 'too little power'. The second generation therefore sought to explain why African states have relied on political structures dependent on rent-seeking and patron-client networks. The problem is that these structures do not amount to a 'capable' state. Explanations have included geographical endowments, such as low labour-land ratios and the legacies of colonial rule.
20. Baskaran and Bigsten (2013: 92).
21. Açemoglu and James Robinson (2011).
22. The 'gatekeeper' state in Africa: Cooper (2002); in post-colonial African states: Lynch and Crawford (2011).
23. Homicide rates in Northwestern Europe: Eisner (2003).
24. On one estimate: Hoeffler (2006).
25. Legacies of colonial rule: Gardner (2012); Mkandawire (2005); Olsson (2009). Post-independence political imperatives: Block (2002); Kasara (2007)
26. South Africa: Ajam and Aron (2007). Settler states: Mkandawire (2010).
27. Frye (2010) describes this process in relation to Eastern European transition economies.
28. The rule of law: nearly all economists would see the rule of law and trust in the key institutions of the state and their proper functioning as critical factors enabling people to cooperate (in groups) and compete (in markets) to achieve mutually productive outcomes. Kenneth Arrow, Friedrich von Hayek, Douglas North, and Elinor Ostrom are four Nobel prize winners who would agree on this, even though they would disagree on many other things. See for example Hayek (1960), Arrow (1972), North (1990), and Ostrom (1998).
29. There is reason to think: Acemoglu and Jackson (2014).
30. Good policies can still make a measurable difference: Delgado et al. (2012).

CHAPTER 2. THE PRIVATE SECTOR: UNLOCKING ENTERPRISE

INTRODUCTION

If the poorest countries are to become rich, their business sectors must be transformed. To judge from appearances, developing countries are abundantly supplied with one of the most important factors of production: entrepreneurship. Most workers in poor countries are self-employed or one step away from self-employment. What does this mean for development? What is the potential that waits to be unlocked – and where is it, exactly? How much of that locked potential belongs to women? How can government and non-government agencies and corporate actors contribute to unlocking enterprise and its capacity for development?

Box 2.1. Setting the scene

The market for cut flowers in Aalsmeer, Netherlands. ‘Flowers in all their colors covering an area the size of 125 soccer fields are what you see if you visit the world’s largest flower market, in the Dutch village of Aalsmeer. The scale is astounding. Seven million roses, three million tulips, two million chrysanthemums, and eight million other flowers and potted plants pass through on a typical morning. Some two thousand buyers bid US \$5 million for them.

‘The flowers are flown in from as far away as Colombia, Kenya, and Zimbabwe. While shipping flowers to the Netherlands might seem akin to taking coals to Newcastle, the Dutch today are in the business of running the global flower trade. The marketplace is organised so expeditiously that the flowers are still fresh when they reach their ultimate destinations all around the world.

‘A worldwide market in cut flowers, delicate and perishable as they are, could not exist without modern technology. It was not until the late 1980s that countries like Kenya became significant suppliers. Efficient air transportation and telecommunications are needed to move roses from a grower near Nairobi to Aalsmeer and then on to a buyer, say, in Seoul, all in less than a day. Electronic devices keep track of the flowers as they move through the auction house.

The “Dutch clock” method of bidding allows the thousands of auctions to run in a few hours. A gigantic clock, to which every bidder is wired, dominates the front of each auction hall. As each lot of flowers is towed by, the clock’s hand starts at a high price and rotates through lower prices until one of the bidders stops it with a push of a button. Computers then automatically organise the flowers’ delivery to the buyer’s address.

‘Sophisticated as its processes are, the core of the global flower market – competitive buying and selling – is as old as civilisation. The Aalsmeer market marries high technology to the time-honored practices of the bazaar’. (Source: *McMillan 2002*: 3-4.)

The bazaar in Sefrou, Morocco. ‘To start with a dictum: in the bazaar information is poor, scarce, maldistributed, inefficiently communicated, and intensely valued... The level of ignorance about everything from product quality and going prices to market possibilities and production costs is very high, and much of the way in which the bazaar functions can be interpreted as an attempt to reduce such ignorance for someone, increase it for someone, or defend someone against it.

‘The search for information – laborious, uncertain, complex, and irregular – is the central experience of life in the bazaar. Every aspect of the bazaar economy reflects the fact that the primary problem facing its participants (that is, “bazaaris”) is not balancing options but finding out what they are.’ (Source: *Geertz 1978*: 28-30.)

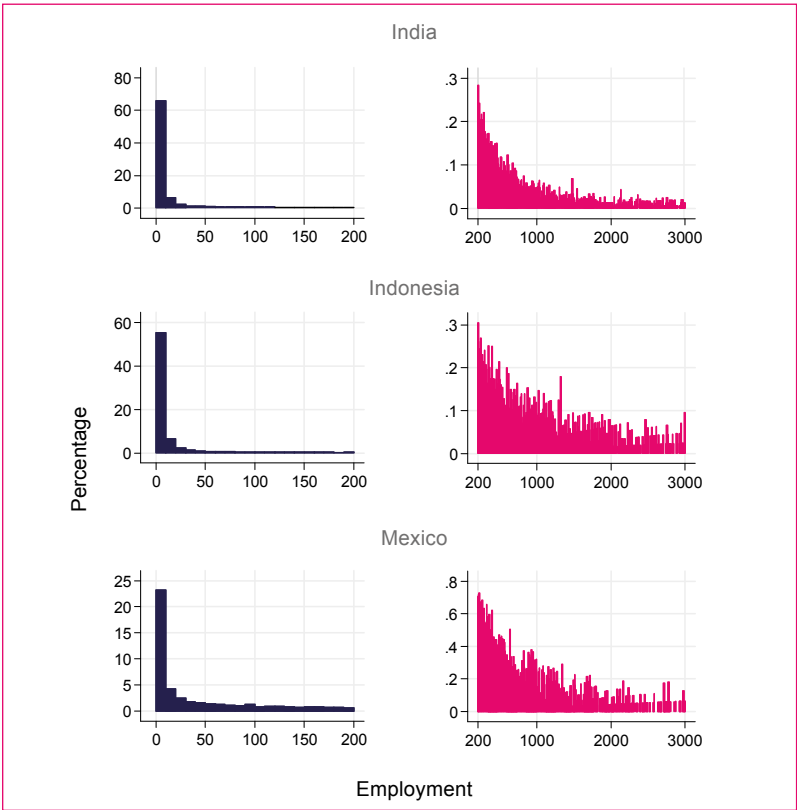
WHERE DOES GROWTH COME FROM?

Half of the labour force in a typical low- or lower-middle income country is self-employed or employed in firms with a handful of employees. A collective term for these firms is ‘micro-enterprise’.

If most people in poor countries are to become moderately rich, micro-enterprise employment must give way to employment in larger, more productive firms. We can think about the role that micro-enterprise can play

in this transition in two ways. On an optimistic view, micro-enterprise can be a source of job creation and a breeding ground for entrepreneurship. A more pessimistic interpretation is that the prevalence of micro-enterprise reflects the failure of larger firms to displace them; the self-employed will escape poverty only when they find jobs in larger firms, led by entrepreneurs that come from elsewhere.¹

Figure 2.1. Distribution of employees by firm size in India, Indonesia, and Mexico, 2011

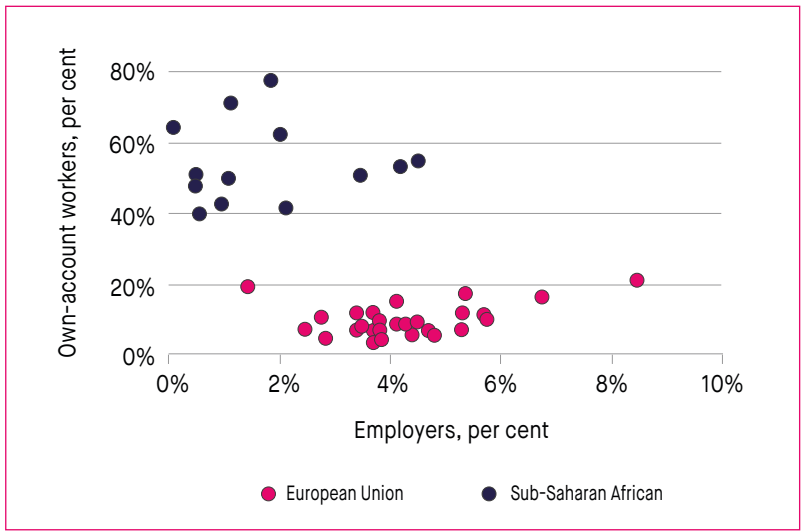


Source: Hsieh and Olken (2014: 105).

Figure 2.1 shows how employees are distributed by firm size in India, Indonesia, and Mexico in a recent year, 2011. For each country the left hand panel shows the proportion of employees in firms or establishments of 10

employees or less. This is two thirds of the workforce in low-income India, more than half in low-income Indonesia, and still nearly a quarter in middle-income Mexico. The right hand panel shows that India and Indonesia do have medium and large firms, and Mexico has more in proportion, but in all these countries the shares of each group of large firms in total employment are measured in fractions of a percentage. This pattern is general for less developed countries. Taken together, in fact, the three countries that are shown account for nearly one quarter of the world’s population.

Figure 2.2. Employers and own-account workers in the European Union and sub-Saharan Africa: shares of total employment, recent years



Source: International Labour Organisation (2010).

Another way of measuring highlights the difference between less developed and more developed countries. Figure 2.2 compares the employment shares of two groups of the population: those that employ others (‘employers’) and those that employ only themselves (‘own-account workers’). Data are shown for a group of wealthy countries and a group of poor countries: European Union member states and sub-Saharan Africa. The figure shows that in the average EU member state employers make up more than 4 per cent of the workforce, but less than 2 per cent in sub-Saharan Africa. In EU

countries around 10 per cent of the workforce is self-employed; in sub-Saharan Africa this figure jumps to more than half. In each region there is some variation around the mean, but the two groups are completely separated, without any overlap.

In poor countries, most people who are able to work pursue low-productivity, low-income occupations. An outcome of successful economic development must be to change these for high-productivity, high-income jobs. If these countries' future is to be one of development, where will the high-productivity, high-income jobs come from?

Consider the firm sizes shown in Figure 2.1. Will these future jobs be created by the firms that today have 2 to 3, 20 to 30, 200 to 300, or 2,000 to 3,000 employees? Where among today's firms are the entrepreneurs hiding who can emerge to make tomorrow more prosperous? Research that is now available helps us to see some of the answers and understand some of the implications.

CAN MICRO-ENTERPRISES GROW?

A first question is: can micro-entrepreneurs increase profits, and hence the household incomes of their owners? When given money to invest, do they make more money? A closely related question naturally follows: when they make more money, can they use that money to grow and create jobs? If the answer is 'No', what other obstacles do micro-entrepreneurs face when they try to scale up? Our research addresses both of these questions.

Are micro-enterprises profitable?

Our research has looked to a number of field experiments in different countries to answer these questions. The first set of projects that we have undertaken asks: when more capital is added to the enterprise, by how much do profits increase? We carefully measure returns to marginal investments in micro-enterprises in Mexico, Sri Lanka, and Ghana. Typically the projects involve a 'treatment' group that receives extra capital (or other material assistance) compared with a 'control' group that is untreated. In all of the projects, the data indicate that profits earned by micro-entrepreneurs

increase substantially when the entrepreneurs invest a bit more capital in their business. In other words, the marginal returns to capital in these enterprises appear to be very high, on average.

Box 2.2. Experimental research in economics

How economic research is done. Economics was once thought of as a non-experimental science. How could any researcher ethically carry out an experiment with other people's fortunes, or even with an entire economy? Yet, in today's understanding, much empirical work in economics is based on experiments of different kinds.

What is an experiment? An experiment requires a treatment group that is subjected to some kind of external stimulus and a control group that is unaffected. By comparing the subsequent behaviour of the two groups, the researcher tries to identify cause and effect. This can happen in three settings – in the lab, in the field, and in nature, so, corresponding to this we have lab experiments, field experiments, and natural experiments. In a lab experiment the researcher usually plays various kinds of game with volunteer subjects, but there are no lab experiments in this report so we focus on explaining the other kinds of experiment.

What is a natural experiment? Does vocational training improve economic growth? A traditional approach would observe that there has been more emphasis on vocational training in Germany than in Britain, and also higher productivity. A sceptic would object that there are many differences between the two economies that are not taken into account. To avoid this problem the inventive researcher might look for a natural experiment: two settings that differ as little as possible, except in the amount of training that has been supplied. In that case no experiment was intended, but one might have accidentally come about. The result would be to enable measurement of the change in productivity associated with the additional training (the 'treatment').

What is a field experiment? Faced with a natural experiment, the sceptic would worry that the higher level of training in one setting might reflect some previously hidden advantage that would also explain the higher productivity that resulted. In a field experiment, this problem is overcome by allocating training to different settings randomly, and then looking for a productivity effect. Because it might be unethical to experiment on people without their consent, this usually requires the cooperation of others. It is also difficult to run field experiments where the focus of interest is on very long term processes – and sustainable development certainly takes a long time.

Our first study examines a large cross-section of micro-enterprises in Mexico with around 200 US dollars of capital. We found returns to incremental investments of 10 to 15 per cent per month. On a smaller sample of male-owned enterprises in Mexico where grants were the source of the increased capital, we found even higher returns of 20 to 33 per cent per month. In this study, the micro-enterprises made highly profitable use of extra capital when it was made available to them.²

A related study of enterprises in Sri Lanka with less than 1,000 US dollars of capital (de Mel, McKenzie, and Woodruff 2008) found returns of 5 to 6 per cent per month for owners who received grants of 100 or 200 US dollars. But these average returns mask an important difference. Male-owned businesses realised increases in monthly profits of around 10 per cent of the amount granted, while female owners did not receive any return on the additional capital. Why men did better than women is a troubling question to which we will return.³

The high returns are puzzling in the following sense. Most of the grants are invested in additional inventories. Why do micro-entrepreneurs not build their business incrementally so that they capture the additional income from these investments? One possibility is that they face a lot of unexpected events that require them to spend resources – sick children, death of parents, and so forth. We see additional profits shortly after the grants are provided, but we might wonder if the additional profits are sustained in the longer term.

Here, a follow-up study (de Mel et al. 2012) gives the answer ‘Yes’. We find that five years later the male owners who received additional capital have had better survival rates and monthly profits which are higher by around 12 per cent of the original grant.⁴ In this study, in other words, the male-run micro-enterprises that received extra capital were able to keep the additional capital in the business and make higher profits in the long run as well as in the short run.

Why are female micro-entrepreneurs disadvantaged?

We return to the question of why some studies show women micro-entrepreneurs at a disadvantage. Where women do worse than men, it might be thought that there is some hidden difference of skills or attitudes, but the evidence does not support this. Instead, our research on female owners in Sri Lanka suggests that a key obstacle for women entrepreneurs is lack of autonomy in disposing of credit and appropriating profits within their families.⁵ Put more bluntly, it is likely that when women receive additional capital male family members either divert the resources when they are received or they divert the profits that are made.

Related research on male and female micro-entrepreneurs that we carried out in Ghana (Fafchamps et al. 2014) echoes these results. Consistently with other studies, the marginal returns are high: 20 to 30 per cent a month. But women entrepreneurs obtain lower returns, especially from assistance given in money; assistance given in kind is more likely to find a productive use.⁶ It is reasonable to imagine a story that goes like this: when a female businesswoman is given access to cash, relatives can divert it for their own use, so that her business does not benefit. But they are less likely to interfere if she is given a sewing machine.

To summarise, our results have an optimistic implication – up to a point. Our optimism concerns the scope for alleviating poverty in developing countries. The evidence suggests that incomes of micro-entrepreneurs can be increased if we can channel capital to them. The micro-entrepreneurs in our samples are among the poorer households in urban areas of Sri Lanka and Ghana. But they also highlight some unexpected obstacles – for example, those facing women who might want to develop their business.

Now we turn to a more demanding question: the goal of sustained development implies a need for job creation. Can micro-enterprises also scale up to a point where they can create additional jobs? Will micro-business be the source of tomorrow's high-wage, high-productivity jobs?

Can micro-enterprises grow and create new jobs?

Here we ask various questions. One of them is obvious: for micro-entrepreneurs, is self-employment an opportunity or just a way to survive? In other words, is it more reasonable to think of the vast reservoir of the self-employed as future businessmen, or as future wage workers? An important consideration is that there are so many millions of micro-businesses in poor countries that even a small proportion of emergent entrepreneurs could still transform the economy and society. In the United States, for example, it is found that only about 3 per cent of non-employers ever move up to hire a paid employee, but their vast number means that these expansions account for 20 per cent of new employees.⁷

Suppose it turned out to be the case that many or most micro-entrepreneurs do not have business talent or opportunities, but a minority does. A next question is: can we work out which are the ones with more potential? Suppose we decide to fund a scheme to help kickstart business growth. An example would be the Start and Improve Your Business programme offered by the International Labour Office. Up to the present this programme has given subsidised training to around 100 million candidates in 95 countries. But it is hardly efficient to fund 90 (or 99) hopeless businesses in order to reach the 10 (or 1) that might succeed. It would be more cost-effective to focus scarce resources on the few with real potential.

Finally, suppose we find that we can identify the micro-businesses that have a chance to take off. What is stopping them now? Is it credit, training, or experience?

One way of trying to sort the types of micro-entrepreneur is to ask which have characteristics and attitudes more like wage workers and which more like larger firm owners. We ask this question of our data from Sri Lanka.⁸ We find some interesting differences. On average, own-account workers

are more willing than wage workers to take control and to juggle tasks. But they are less motivated and less tenacious than firm owners. For the most part, in other words, they have attributes that are necessary to maintain a business but not those that would help to grow it.

In cognitive ability, competitive attitudes, and motivation, therefore, the great majority of self-employed looks more like wage workers. A minority, however, turns out to have attributes more comparable with those of larger business owners. Within the 30 months of our study, moreover, a minority of own-account workers did succeed in growing their business to the point of taking on at least one paid employee. We looked at the attributes of those that did so and found that three attributes were associated with this: the micro-entrepreneurs who experienced growth were more focused on achievement, less focused on taking control (because a large business requires control to be shared), and, discouragingly but predictably, less likely to be female.

Where are the few entrepreneurs?

The idea that a small minority of the self-employed has real entrepreneurial potential is echoed by another project that we carried out in Sri Lanka.⁹ It is important that we worked with a sample of firms with more than one and less than 10 employees. We took the fact that they had already hired at least one employee to indicate some ability and desire to expand by becoming an employer. We used an experiment that induced some firms to become formally registered with the authorities. Our underlying idea was that formalising a business so that it becomes a legally recognised entity has clear costs, such as the cost of registering and after that the liability to pay taxes. But formal registration also brings benefits such as access to a bank account and perhaps bank credit. We wanted to see whether helping micro-enterprises with the up-front costs of formalisation would remove barriers to growth. Nevertheless, it turns out that the answer for the typical enterprise was 'No'. But the answer changed to 'Yes' for a small minority of enterprises where we found a very large effect.

A similar result emerges from a study in which we provided capital, incentives to hire workers, and management training simultaneously to a group of micro-

enterprises in Sri Lanka. This project studied 1,525 enterprises with two or fewer paid employees.¹⁰ In a field experiment, enterprises were randomly allocated to a control group or to treatment groups that offered incentives to save and build capital, or to hire new employees, or to undertake management training. Some enterprises received two of the treatments. They were followed up over time. Four years later, the most consistent effects on employment and profits came from the saving incentive. Wage subsidies alone led to faster employment growth in the short-run, but the differences in the average enterprise went away in the longer term and there was no increase in profits.

Table 2.1. Saving and wage incentives and the distribution of firm size by employment four years later: A field experiment in Sri Lanka

	Control group	Treatment group: wage incentives	Treatment group: savings incentives
Number of firms	197	628	394
By number of paid employees after four years, per cent:			
0	71.1	67.3	68
1	16.3	18.7	17
2 or 3	9.8	9.4	9.3
4 or more	2.8	4.5	5.7
Difference from control group by number of paid employees, per cent:			
0	...	-3.8	-3.1
1	...	+2.4 ←	+0.7
2 or 3	...	-0.4	-0.5
4 or more	...	+1.7 ←	+2.9 ←

Source: De Mel et al. (2014b). The highlighted figures are the findings of most interest. For explanation see text.

Table 2.1 shows the changing distribution of firms in our study by size. They are grouped in three columns: the control group, a group of firms treated by wage subsidies, and another group treated by savings incentives. In the top half of the table, we can see the distribution of firms in each group by size after four years. Initially, none had more than two employees, and most had none, so the firms that now have three or more have grown under the course of treatment during the study.

The bottom half of the table highlights the differences in the distributions of the two treatment groups compared with that of the control group. Here it can be seen that the treatments were associated with three to four per cent fewer firms without any employees. In the case of wage subsidies, about half of that difference is found in firms with exactly one employee – perhaps the one that the wage subsidy induced them to hire. But the remaining two percentage points of the gap are found in enterprises that have grown to four or more employees. In the savings treatment group, moreover, essentially all of the reduction in firms without employees is now found in the group with four or more employees. Here is more evidence for the argument that, with the right initial stimulus, a few micro-businesses can expand.

Can we predict who will succeed?

Can the entrepreneurs of the future be picked out from the mass in advance? We asked this question, looking at micro-businesses in Ghana.¹¹ We considered two different ways of predicting business expansion. One is to measure the competence of micro-entrepreneurs based on years of schooling and performance in tests of numeracy, non-verbal reasoning, and financial literacy. The other is to put them through a competition familiar to British and American audiences as a ‘Dragon’s Den’ where business consultants and successful employers evaluate a business plan. Finally, we surveyed the same businesses one and two years later to see which businesses had succeeded in expanding. This study produced several answers. One is that both objective tests and expert judgements could predict expansion. Another is that these techniques could be seen as complementary: when objective tests had done their bit, expert judgement still improved the quality of prediction.

Our story from Ghana has one more dimension. Part of the reward for success in the Dragons' Den was a chance to be entered for management training. Here the results were disappointing. Access to training had no positive effect. If anything, those that received training were less likely to still be in business when results were followed up.

MICRO-ENTERPRISE: THE STORY SO FAR

To summarise, findings from many studies present us with an inconsistency. Capital invested in micro-enterprise brings high returns. Yet most micro-entrepreneurs seem to lack the capability to grow the firm. That capability is found only amongst a small minority.

Various reasons for this can be eliminated. It is not the lack of opportunity, because the evidence is that returns to additional capital are high. But it is not just a lack of credit, because, given additional credit nearly all micro-businesses do not expand. Nor is it a lack of training, at least as it is most commonly provided, because additional training does not support business expansion.

There is some evidence for the idea that most own-account workers cannot envisage the relentless task of growing their businesses into larger organisations, or shouldering the burdens of responsibility for others and accountability to others in the same organisation. This is hardly surprising. Most citizens of modern Western societies are unique in world history in spending their lives in large bureaucratically regulated organisations from nursery class, school, and college and through employment to retirement. Most citizens of poor countries can acquire this experience only by entering military or public service.

The limited growth possibilities open to micro-entrepreneurs does not take away a role for micro-credit and similar supportive programmes, but it does diminish their significance. These programmes can contribute to poverty alleviation by increasing the incomes of the self-employed and small entrepreneurs. But they are unlikely to unleash sustained economic growth on a wide scale.

It is true that, hidden in the mass of self-employed and small entrepreneurs, are small minorities that have the capability to reap larger profits and sustain growth of production and employment. It is possible, although hardly easy, to identify these future entrepreneurs and support them selectively.

One reason they may need initial support is to overcome residual psychological barriers to business expansion. Another possible reason may be that, while returns to capital are high, they are also variable. In other words, borrowing and investment are risky. Most micro-finance schemes involve lending to own-account workers and micro-businesses at fixed interest, and require repayment beginning within a few weeks of the loan being disbursed. The effect is to place the burden of risk on the borrower, who has to service the debt at a fixed rate regardless of whether or not profits are made. Moreover, the borrower needs either to use part of the loan to make initial repayments, or to invest only in projects that bring an exceptionally rapid return.

Other research indicates that a grace period as short as two months before repayments begin may dramatically increase the profits businesses realise from investing loans.¹² Unfortunately, by inducing the entrepreneurs to make riskier but higher-return investments, the grace period also leads to higher default rates. Hence, micro-lenders will not find it profitable.

The problem is that when a risky investment fails it is the lender who bears the entire loss. When the investment succeeds, in contrast, the entrepreneur takes all the profit above the loan repayments. The solution is that more micro-finance should take the form of equity, where the lender does not expect a fixed schedule of repayment but takes a share of the profit. This allows the lender to share the risks with the borrower.

Even with more suitable financial products, however, employment growth from scaling up of smaller enterprises is likely to be very modest. For the mass of people in low-income self-employment, hope for the future lies in becoming wage workers in larger organisations that someone else has created. We now turn to look at research that identifies ways in which larger firms can be encouraged to grow and create more jobs. In particular, it turns out that globalisation has been a positive factor for exporting firms in poor countries.

FIRM GROWTH AND GLOBALISATION

Another place to look for forces that can unlock development is in the responses of larger firms in developing countries to globalisation. Globalisation means the cheaper and faster movement of goods, services, people, and ideas. These improvements have given developing-country producers the opportunity to serve wider, richer, and more demanding foreign markets.

The firms that are of interest to us from this perspective are not micro-enterprises. They are likely to have dozens or hundreds of employees, making them large enough to be found in the far right tail of their home country's size distribution of firms, and in the right-hand panels of Figure 2.1. They generate substantial incomes. They are not large by Western standards, for in developing countries such true giants are exceptionally rare: Tata Steel in India or Desh Garments in Bangladesh. But they are certainly large by developing-country standards.

Most of these firms are domestically owned, but some will have foreign participants. And most of them have not mushroomed organically out of a micro-enterprise. Their origins often lie in patronage and connections to power, or in early links to exporting and external partners. But here is another reason why we should pay attention to larger businesses that have been formally incorporated. This is because formal incorporation is a step towards the separation of business interests from power structures. Here, as argued in Chapter 1, is one of the basic 'doorstep conditions' for moving to an open-access society where rewards are distributed by the market rather than by force.

You may not have heard of these firms, but you will have heard of their export-market distributors. Between developing-country producers and Western consumers sit large buyers such as Walmart, Carrefour, Tesco, and H&M. These buyers are typically much larger than their suppliers, with stronger bargaining and financial power.

The rich-country distributors often get a negative press: for example, they are often accused of imposing low wages and poor conditions on poor-country suppliers to keep prices low in Western markets. In this chapter

we show another side. Collaborative relationships between Western buyers and producers in developing countries can also promote development by relaxing institutional constraints, unleashing entrepreneurial activity, and pushing up productivity and wages.

Box 2.3. The value of a relationship

When does a relationship have value? First of all, a valuable relationship is more than just an acquaintance. Each of us knows lots of people on a nodding basis. We say ‘hello’ to them every day. But merely to be familiar with someone is not enough for the relationship to have value. A valuable relationship is one that requires initial investment: you have to put something into the relationship, for example by getting to know the other person, learning what they might want from you, and providing something that they need. In due course, the investment will bring a return: something you want, and cannot get more cheaply elsewhere.

Your friend the pharmacist. Here are two examples that are relevant to the arguments in this chapter. First, imagine you live in a world where distribution is unreliable and there are frequent supply breakdowns. You go to buy medicine and there is a shortage. You stand and wait in line with others. Many of the people whom you greet every day will do nothing to help you, but ‘a friend in need is a friend in deed’. If the pharmacist is a good enough friend to take you behind the counter, then that friendship has value. The value is two-sided: in due course, you will need to maintain the friendship by repaying the favour in some way.

Building a business is costly. Here is the second example. Imagine you run a business in a world where written agreements have no value because the courts do not work and the law is ineffective. How can you gain clients? Only through personal contact: you must help your clients get to know you well enough that they appreciate you are a reliable person. One way to show this is to do business with them even when you could make a quicker profit elsewhere. Here the lost profit is your investment in a long-term relationship with your client.

Relationships and markets. A common feature of these two examples is that they both describe a world where things the citizens of rich countries often take for granted don't work well. In the first case, supply failed. In the second case, the law failed. Personal relationships become less important in economic life when the market economy is flexible and the rules of the market are firmly established. This is roughly as it should be: most of us would see economic outcomes as more fair if they depend on what we know, not whom we know.

Relationships and quality. Even in the best organised world, some problems will not go away. In today's market economies the quality of service is often a key aspect of what is delivered. No written agreement can be enforced that guarantees a wine that everyone will like, or service with a smile, or care with compassion and respect. Such dimensions of a relationship can be thought of as 'non-contractable': that is, you cannot write a contract for 'service with a smile' because it would generally be impossible to prove a breach of contract in court. In transactions of this kind the relationship between buyer and seller will always come before a written agreement, and such transactions may become more common as incomes rise.

How does this come about? It is not apparent from the model of a market presented in an Economics 101 textbook. In this model the market is perfectly competitive, information is freely available to buyers and sellers alike, and it is costless to enforce a contract or a promise. In this model relationships are irrelevant and have no value. If that is the case, the market will take care of everything. But this is not the reality facing many producers, especially in developing countries. There the environment is difficult for several reasons:

- Excessive regulation weakens competition and encourages corruption, raising significant barriers to profitable investments.
- Contracts are weakly enforced, so that firms have difficulty in expanding to seize profitable investment opportunities.
- Domestic consumer markets are relatively underdeveloped because most households have low incomes.

In this setting, poor-country suppliers can gain from collaborative relationships with foreign buyers because these relationships can yield solutions to some (though not all) of the problems they face. For example, foreign buyers can offer access to much wider markets; they can provide business finance; and they can enhance suppliers' capabilities.

At the same time, valuable relationships are hard to initiate and hard to sustain. This is true in general, and particularly so in the context of international trade. When trade crosses borders there are higher costs of monitoring and enforcing contracts. Cultural differences can also increase the costs of reaching agreement and resolving problems.

THREE CASE STUDIES

To get an idea of the costs of establishing buyer-seller relationships and the gains from maintaining them, we carried out three case studies: wine (exported from Chile to the UK); flowers (from Kenya to Europe), and specialty coffee (from around the world to the United States). In each case we aim to measure the value obtained by the exporter in the poorer country from establishing a relationship with a rich-country buyer.

Chilean wines

Many countries have the climate, terrain, and soil types that are suitable for making wine, but few of these have made successful wine exporters. With a climate somewhere between that of California and France, forty years ago Chile was one of the many without a significant presence in world markets. Since then the Chilean wine trade has been revolutionised. Today Chile exports around 90 per cent of its wine production, worth nearly \$2 billion, and is the tenth largest wine producer worldwide. Chilean wines account for around one tenth of British 'off' sales (licensed for consumption off the premises). The number of employees in Chilean wineries is uncertain but is numbered in the thousands or more ten thousand.¹³

The situation of Chilean vineyards forty years ago was typical of the problem facing many potential exporters from less developed countries: how to become known as reliable suppliers of a good quality product.

The international wine trade is managed by distributors based in the importing market economies. Typically, a distributor will 'match' with an exporting vineyard on a one-to-one basis; for example, each distributor will sell one Chilean wine label in the UK market and each Chilean vineyard will sell through one distributor. This makes sense from the distributor's perspective because most Chilean wines are seen as intrinsically similar so that they are competitive with each other. A distributor that already has to compete with other distributors in the UK market would wish to avoid the additional complexity of having to manage competition within its own portfolio of wine labels.

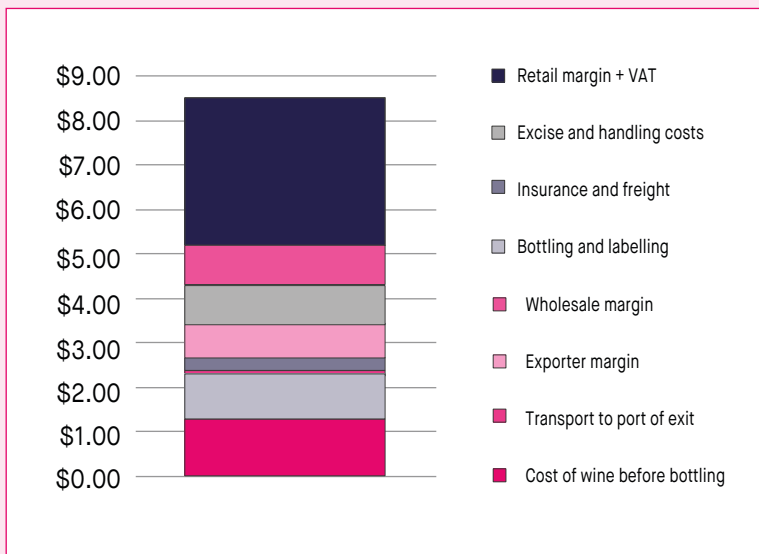
Two aspects of quality are crucial to the buyer-seller relationship. One is the quality of the wine itself. The other is the quality of the supplier in the sense of reliable delivery of the quantity and quality promised. Both of these qualities are summed up in the reputation of the wine label. Here we are fortunate that data on wine quality such as reviews, ratings, and competition medals are widely available, so that we can separate the two dimensions.

In our research, we collected and studied all the 288 agreements made between Chilean vineyards and wine distributors between 1983 and 2006. We wanted to understand how Chilean wine producers have broken into world markets and improved their terms of trade.

We found evidence that the key to success lay in gaining experience. What mattered was not experience of the overseas market gained by the exporting vineyard; the important thing was the distributor's acquisition of experience of the wine maker. Chilean vineyards have broken into the export market by first matching with a subset of distributors: those that have a relative advantage in discovering new, unknown wineries and pioneering their sales in the Western market. This is a high cost activity, so the 'pioneer' distributors have relatively high marketing costs. At the outset, therefore, the distributor buys the wine of the new label at a relatively low price.

Box 2.4. The value of a bottle of wine

Who gains in the wine trade? According to data supplied by Wines of Chile, a typical bottle of Chilean wine retails in international markets for \$8.54 per litre. This sum is passed down the value chain as follows:



Source: Wines of Chile at <http://http:winesofchile.org> (accessed on 1 July 2014).

In our study we focus on the wine price at the port of exit, sometimes called the price FOB ('free on board' the ship). The price of wine FOB in the Wines of Chile data is \$2.35 per litre.

How is value distributed? The fact that the poor-country producer receives only a fraction, in this case less than one third, of the final retail price in rich-country markets is sometimes considered to be an issue of international distributive justice. To us, this approach is oversimplified. Chilean wine is valuable mainly because Western consumers value it and can afford to pay for it. (The same is true of the Kenyan roses and specialty coffees also considered in our chapter.) They value it so much that intermediaries find

it worth their while to bear the considerable costs of searching for it, identifying it, buying it, and shipping it across the world; they also have to pay wages to expensive European workers to distribute it and rent costly European city-centre premises to market it. This explains the other two thirds of the retail price of a bottle of Chilean wine.

How will the distribution of value change? Three things might change this pattern. As global distribution technologies improve, the resources eaten up by intermediaries will fall. And, as the Chilean economy becomes richer and more diversified, Chilean land rents will rise and vineyard workers will become more expensive. Because of these trends, a rising share of the value chain is likely to flow to Chilean wine producers. However, as the world becomes more efficient at producing and distributing Chilean wines it is also possible that the retail price per bottle will fall. This will not benefit Chilean wine producers, but it will benefit the much larger number of Chilean wine consumers.

The loss the vineyard makes initially by selling at a low price is, in effect, an investment in the relationship with the distributor for the sake of future business. Over time, as the distributor learns that the vineyard is a reliable partner, the vineyard's price increases. More than that, as time passes the vineyard can exploit its improving reputation to end its agreement with the pioneer distributor and shift up to other distributors that deal with established labels, have lower costs, and will pay a better price. As a result the vineyard can further improve its terms of trade (see Box 2.5).

Unpredictable fluctuations in exchange rates in the world market also suggest a kind of natural experiment. How much was the price received by the exporting vineyard affected by external shocks such as exchange rate fluctuations? We find that the effect was smaller, the longer the vineyard had been in a relationship with its distributor.

Of course, one can imagine alternative explanations of these patterns. Changes in the vineyard's selling price could also be explained by obvious confounding factors such as changing wine production costs and qualities.

There could also be other, more subtle mechanisms at work: for example the vineyard might improve its bargaining power by acquiring experience in selling a given wine. But our data are rich enough that we can rule these other explanations out.

Box 2.5. Chilean wine: becoming known

Eduardo Guilisasti, CEO of Concha y Toro, a leading Chilean wine exporter.

Q: 'What are your greatest strengths?'

A: 'First, we produce quality at very different price levels. People all over the world recognise that fact. Second, we have developed long-term, solid relations to our distributors. Third, we have been investing a lot in building our brands'. (Source: Interview for Meininger's Wine Business International by Anamaria Barahona and Jürgen Mathäß on 10 April 2007, available at <http://goo.gl/tdhekA>, accessed 1 November 2014.)

Finally, the effects are large. As a result of gaining reputation, the price paid for the same bottle of Chilean wine at the point of export increases relatively by 2 to 3 per cent a year over the course of a relationship with their distributor.

Kenyan roses

Globalisation has not only brought developing-country wines to European homes, it has also brought their flowers and vegetables. With its location on the equator, perpetual sunshine and variations of altitude, Kenya is endowed with many of the natural conditions necessary for growing flowers. Its farmers have succeeded in growing roses to be cut and flown to Europe where consumers buy them to give to each other, especially on Valentine's Day and Mothers' Day. In slightly more than a decade, the country has become one of the world's largest flower exporters, overtaking such traditional leaders as Israel, Colombia, and Ecuador. The flower industry now ranks alongside tourism and tea as one of Kenya's largest foreign currency earners, worth nearly half a billion US dollars a year, which represents five-

fold growth over the end of the 1990s.¹⁴

The industry is labour-intensive and mostly employs less-educated women in rural areas. Flowers are fragile and highly perishable, so that care is a key determinant of quality. Workers receive significant training in harvesting, handling, grading and packing, and this makes them hard to replace quickly.

There are two channels for the export trade in Kenya's roses. Through one channel, intermediaries work the Kenyan flower market in the same way as wine distributors in Chile. In this channel, rose growers and distributors form long-term relationships. Why should we expect to find that durable relationships matter in the market for flowers? For flowers, as with wines, quality matters. Suppose a farmer sends a consignment to a buyer: it is all too easy for the buyer to refuse to pay on the grounds that the flowers were dead when they arrived. Equally, it is all too easy for the farmer to send dead flowers and deny it. The evidence will have withered by the time the case might go to court. It is advantageous, therefore, to have a reputation for reliability based on past experience.

In the market for Kenyan roses, nonetheless, there is also another channel based in Netherlands, where farmers sell directly to buyers in a descending price ('Dutch') auction (Box 2.1 above). In the auction channel there is no long-term relationship, only an immediate connection that dissolves as soon as flowers and money have changed hands. Importantly for our study, nearly all Kenyan flower exporters maintain accounts at the Dutch auction, even if they rarely use it, and it is inexpensive to do so. Thus, the option of sending flowers to auction is always available.

Again, we collected data on 189 relationships between farmers and flower distributors between the summers of 2004 and 2008. The importance of this period is that it includes a period of intense and widespread violence in January 2008, arising from the contested outcome of a presidential election held in December 2007. In its wake, an estimated 1,200 people were killed and more than 300,000 others were displaced. This was a human tragedy; added to the human cost are the economic losses, put at £145 million, or 1 per cent of GDP.

Some features of the violence allow it to be seen as the trigger for a natural experiment (Box 2.2 above). First, the violence was unforeseen, so no one was able to prepare for it or insure against it; not one of the 74 growers we interviewed claimed to have foreseen the turn of events and prepared for it. Second, the violence came just before the peak of European demand for roses associated with Valentine's Day (14 February). Third, in the places where violence was concentrated it seriously affected the activity of rose growing and harvesting because workers failed to report for work: farms located in the affected regions reported an average of 50 per cent of their employees missing in that period. Finally, the violence was focused on tribal boundaries and, as a result, localised: not all farms were affected to the same degree, and some were unaffected.

A difficulty facing empirical research in such a situation is to provide a valid assessment of what would have happened to affected firms if the violence had not taken place. By accident rather than design, the geography of the Kenyan violence pointed the way. In fact, in two weeks of particularly intense violence, export volumes and revenues of firms in affected regions dropped by 38 per cent relative to comparable firms in regions not affected.

At this time Kenya's rose farmers were faced with exceptionally hard choices. If they were menaced by violence, they faced losing production unless they went to special lengths to guarantee the safety of farm workers; for example, they would have to hire extra security, and provide temporary accommodation for workers so that the workers could live safely on site. These efforts would be costly. Also, with roses suddenly in short supply, farmers had to choose which buyers to prioritise. If the farmers' efforts paid off, so that they had roses available despite the troubles, they could choose between satisfying their regular buyers and letting them down by sending their crop to the Dutch auctions to take advantage of high prices.

In our 'model' of the buyer-seller relationship, it is important for the poor-country seller to invest in a relationship with the rich-country buyer over time by working to build up a reputation for reliable delivery. If this is the right model, then we would expect that some sellers would make more efforts than others to maintain that reputation by prioritising their regular buyers and delivering roses to them at all costs.

At any given moment, such as in January 2008, we should find relationships in existence at several different stages of development. Some would be new, some old, and some in between. We should expect sellers in new relationships not to try so hard to maintain deliveries; they would not have had much time to build a reputation, and so would have little to lose by falling short. We should expect sellers in old relationships also not to try so hard, because their reputation would be well established and their reliability in normal times is proven; they could expect their regular buyers to cut them some slack. It is the sellers in the middle who ought to try harder, because they have most to lose: a reputation that is partly established but still fragile.

We test these ideas against the data, which allow us to calculate the value of costs and opportunities foregone in order to maintain deliveries to regular buyers. Sales by farms in the affected regions fell sharply in the crisis, compared with farms that were unaffected. We show first that not all affected firms responded in the same way. As predicted, sales fell most short where firms were in very new or very established buyer relationships. Next, during the crisis Dutch auction prices were substantially above prices in most direct relationships. We show that, despite the profits on offer at the auctions, affected farmers cut back the volume of auction sales by around half, which is much more than the 16 per cent cutback in sales to their regular buyers. Thus, farmers prioritised buyers with whom they had more valuable long-term relationships, rather than taking a quick profit where prices were higher. Additionally we find that the same firms, that is, those with most at risk in stable contractual relationships with buyers, went to special lengths to protect their reputations. Measures to safeguard their workers and crops put up their operating costs, on average, by 16 per cent.

These findings all point in the same direction: rose farmers, who make up one of Kenya's most important export industries, have also cultivated a valuable asset, their reputation for reliability with Western buyers. This asset has enabled their industry to grow, create jobs, and raise incomes.

At the end we reached an encouraging conclusion: the jobs created by flower firms are not only valuable in themselves, but seemingly discouraged participation in the violence. Kenya is an ethnically fragmented country, and the violence in the wake of the elections pitted members of some

tribes against others. Most flower firms have ethnically diverse workforces, composed of labourers from tribes that were in conflict with one another. Yet no violence was directed against flower firms, and no episode of violence was recorded on these firms' premises.

The export-oriented nature of the industry further contributed to stabilising the situation, because firms sought to find ways to fulfil contractual obligations with foreign buyers. As a result, policies directed at upgrading agricultural products towards commercial exports might have beneficial side effects in mitigating the risks and consequences of political instability.

Specialty coffees

Our research for this case study is based on the records of an international lender that provides working capital loans to coffee washing stations. The data cover all 756 loans disbursed by the lender between 2000 and 2012 to 197 coffee washing stations in eighteen countries, mainly in Peru, Mexico, Nicaragua, Rwanda, and Guatemala.¹⁵

Washing is a stage in the production of high-grade, high-value specialty coffee beans. Coffee washing stations are medium enterprises; the average firm in our study turned over nearly \$2½ million a year, although 85 per cent of this was the cost of goods sold. The average firm had 135 workers, mainly seasonal employees. So, by the developing-country standards illustrated by Figure 2.1, these would be in the top fraction of a percentage of firms by size.

Credit in this business can be viewed from the standpoint of both borrower and lender. The borrower's problem is that credit is valuable and hard to get. Credit is valuable because coffee-washing firms can use it to buy additional coffee from farmers; in this way, like the micro-enterprises studied in the early part of this chapter, they can make profitable use of additional capital. But credit is hard to get because of the lender's problem. Lenders would like to extend credit on terms that benefit both sides – the borrower can make a profitable investment and the lender can receive a return. But lenders do not fully trust borrowers to repay loans and, if borrowers turn out to be unwilling, lenders have few weapons to enforce repayment.

The main way that the lender secures repayment from coffee washing firms is as follows. The coffee washer makes a contract for a future sale of washed coffee to a buyer, whom the lender knows. The lender then makes a loan to the coffee washer based on a share of the contract. When the coffee is sold on, the buyer remits the share of the sale to the lender to pay off the washer's loan.

At first sight the lender's system is fail-safe. It breaks down, however, if the coffee washer breaks the contract with the buyer. Moreover, sometimes the washer can profit by doing so. This is because the market price of washed coffee can rise unpredictably between the date the contract price was fixed and the date the washed coffee is available for delivery to the buyer. Moreover, if the coffee washer sells the product to an outside buyer different from the one contracted, there is no obvious way for the lender to recover the loan.

Bad borrowers come in two varieties, corresponding to the economic concepts of adverse selection and moral hazard. Moral hazard means that, having obtained a loan, the borrower is tempted to divert the money outside the debt contract. Adverse selection means that in the first place less good borrowers will be more attracted to the loan that is offered. Either way, there is the possibility of a bad outcome for the lender: the loan will not be repaid.

If legal remedies do not suffice, the only way around this problem is for the lender to form a relationship with the borrower in order to learn about the coffee washing business. This takes time. Over time, the lender can learn whether the coffee washer can fulfil contracts and repay debts. Here, again, is the value of relationships, which filters right down to the individual growers (Box 2.6).

Our data allow us to study the influence of market price fluctuations on debt repayment. A particular feature of the coffee market makes for a natural experiment. The market for washed coffee is global, so coffee washers in all countries see the same variation in washed coffee prices. But coffee harvests are gathered, and contract prices are set, in different months in different countries. This means that although a period of rising market

prices would seem to create a temptation for all coffee washers to break sale contracts and default on debts, only some can act on it: those that happen at that moment both to be locked in to an unfavourable contract price and have washed coffee ready to deliver.

Box 2.6. Rwandan coffee: investing in relationships

Bertha Nzabanita, a Rwandan coffee grower and one of 1,800 members of the Dukundekawa coffee cooperative:

'The cooperative invests in us. You could sell another buyer ten sacks of coffee, but you'll lose him. You may never meet again. But the cooperative invests in us, and it makes a difference ... Today, I have four fields, and I have paid school fees for my child. Now he is finishing studies at the university this August.' (Source: Root Capital, 'Building better futures for women in Rwanda', available at <http://www.rootcapital.org/portfolio/stories/building-better-futures-women-rwanda>, accessed 1 November 2014.)

On this basis, we find that a 10 per cent increase in the market price of washed coffee above expectations written into contracts is associated with an increase in the probability of debt default by around 5 percentage points.

At the same time, not all coffee washers break contracts and default on debts. Why not? Because it is profitable for some of them to stick to the agreements they have made. In other words, these suppliers gain more in the long run from maintaining a good relationship with the lender than by foregoing it for a quick profit made by becoming a bad borrower. Our data allow us to work out that the good borrowers tend to be the coffee washers with well established relationships to lenders. These are the firms that have invested in a reputation for reliability and stand to lose most if they let the lender down. In contrast, the lack of a prior relationship with the lender raises the probability of a default by 7.5 percentage points.

Our data also allow us to estimate the value of the coffee washer's relationship with the lender. We find this separately for the compliant

lenders that meet contracts and pay off debts, and for the defaulters. When borrowers are compliant, we find the gain amounts to 54 per cent of the nominal value of the sale contract. In other words, borrowers forego monetary gains worth half the sale contract to preserve a good relationship with the buyer and the lender. Conversely, the additional gain from going outside the contract must be worth at least 20 per cent of the sale contract to trigger a default.

One more time, we find that being able to form a long-term relationship with a rich-country client is a source of substantial benefit for poor-country suppliers.

A generalisation

A coherent picture emerges from our three studies. For the poor-country exporters we have studied, relationships are valuable: they are worth at least 15 per cent of Chilean wine sales, 15 per cent of Kenyan flower sales, and a still higher proportion of specialty coffee sales. There are two kinds of implications for understanding what works in promoting sustainable economic development.

One implication is the importance of time. It takes time to build a relationship. Relationships are valuable precisely because learning about an exporter's reliability takes time. In this setting, there are no quick results. Progress is inevitably slow at first, and its further advance depends very much on the quality of the early pioneers: the first Kenyan flower growers or Rwandan coffee washers to enter the external market. Early disappointments can shape negative perceptions, stopping many valuable relationships from forming.

This leads directly to another implication: the large returns to long term engagement with Western buyers and lenders are not available in the open market. They are restricted to specific firms that persevere in building up specific relationships with specific buyers or lenders over time. The facts are that the returns are large and are not available to all; these are direct evidence of the market inefficiency of the developing economy. It shows that many profitable opportunities cannot be realised because something is missing.

What is the missing factor? Superficially, it is the relationships we have analysed. But these relationships are only necessary because of the context, which is one of incomplete information, low trust, and poor contract enforcement. In fact, Western buyers entering poor-country markets for flowers, wine, and coffee are like Western tourists entering the bazaar in Sefrou, Morocco that Clifford Geertz described (Box 2.1 above): their first problem is 'not balancing options but finding out what they are'.

The options available to Western buyers are framed by their legal setting. Will legal processes be transparent, will judgements be independent, and will courts provide low-cost enforcement of contracts? If Western buyers could be confident in the legal setting, they would be willing to take more risks and offer sellers higher prices today, not after years of trial, error, and relationship building.

IMPLICATIONS FOR POLICY MAKERS

In poor countries, most people's experience of work is through self-employment or family-based micro-enterprise. Relatively few people work in large firms. If poor countries are to become rich, the number of jobs with high productivity and high wages must rise dramatically. Who will create these jobs? Will the entrepreneurs come from the millions of self-employed, or from the relatively few larger firms that already exist? Our research shows that capital invested in micro-enterprise often brings high returns. Despite this most micro-enterprises do not grow. Female family entrepreneurs appear to be systemically disadvantaged when male family members have access to their business.

In poor countries, only small minorities are employed in larger businesses that are formally incorporated. Although that sector is relatively small, it is the most likely source of sustainable growth in the number of highly productive jobs. For the mass of people in low-income self-employment, in other words, hope for the future lies in becoming wage workers in larger organisations that someone else has created.

In that context, our research turns to factors that have hindered the growth of larger firms. In some developing countries an obstacle is the lack of a

developed legal framework. When contracts are poorly enforced, firms that receive contracts or trade credit from Western buyers may fail to stick to agreements. Because buyers are uncertain that contracts will be enforced, they are reluctant to make contracts with sellers or lend to them. Our evidence of this comes from the lengths to which rich-country buyers go in order to identify which buyer-seller relationships will be profitable – and the lengths to which poor-country sellers go to protect their relationship with rich-country buyers, once they have formed. Some of this evidence is produced by responses in Kenya to an unexpected community conflict – just the situation in which growth can experience a permanent setback.

This leads us to identify two channels for the promotion of larger exporting enterprises in poor countries. One channel is provided by rich-country buyers. Firms that buy poor-country exports and distribute them in rich-country markets are playing a developmental role by providing trade credit, by enabling sellers to learn about the requirements of rich-country markets, and by encouraging them to improve quality standards and business practices.

Every relationship is different in the sources of value and relative amounts that they yield. Given that ‘the devil is in the detail’, what general lessons can help the making of policy? We divide our recommendations into implications for micro-enterprises and for larger exporting businesses.

- For micro-enterprises, an implication is that their role in generating sustained growth may be limited. There is evidence from several countries that a small minority of micro-entrepreneurs has the capacity to grow the business, and that many or most larger businesses start large. Because micro-entrepreneurs face high risks, they would be helped by equity-based micro-finance, which would share risks between the borrower and the lender. For the mass of micro-businesses, traditional micro-finance may still have a role to play but it is to combat poverty, not to spark sustainable growth.
- When we turn to larger businesses, most episodes of rapid growth are driven by exporting firms. Our research has implications for exporters, particularly in markets where quality matters. There, buyer-

seller networks are valuable – but their value arises mainly because something else is missing. Such networks would form and re-form more easily, and could become wider, more fluid, and more open, if buyer-seller contracts and debt contracts were more readily enforceable. Thus, a complementary channel for the improvement of poor-country exporters' business capacity is the legal and information systems that support cheap and transparent contract enforcement and arbitration. This is not only a general requirement of sustainable development; it will also specifically improve export performance by raising rates of formation of profitable buyer-seller relationships.

- Government policies to promote exports are not just a matter of advertising one's national brands in foreign markets or subsidising export credits. An essential element is to improve the domestic 'infrastructure' of business governance, including contract enforcement and dispute resolution. In the same spirit, contract enforcement is more than just a matter of cheap and timely access to the legal system. In addition, industry boards and associations can disseminate information on contract breaches and also deliver transparent, low-cost arbitration. ICAFÉ is an example of a government agency that helps to organise Costa Rica's coffee market in this way.
- One implication of our research that is highly problematic concerns competition. Markets in which relationships matter are not fully competitive. In a competitive market it does not matter who you know and buyers can switch smoothly to the cheapest seller. This does not allow relationships to form. There has to be profit in who you know to allow both sides to invest in a relationship. Once a relationship has formed, it has to be more profitable to stay with the partner you know than to leave them, and this weakens competition. As far as rich countries are concerned there is ample evidence that product-market regulation impedes competition and that deregulation promotes economic growth. The same evidence finds a benefit for poor countries but identifies the size of the benefit as smaller.¹⁶ In the cases we have considered, the rich-country market for poor-country products would not exist or would be severely restricted without long-term relationships that weaken competition. If so, enforcing

competition without making good the legal deficit around contract enforcement would destroy the market along with the relationships. In other words, remedying the legal deficit must come first.

REFERENCES

- Blouin, A., and R. Macchiavello (2014), 'Tropical lending: international prices, strategic default and credit constraints among coffee washing stations', CAGE Working Paper no. 211 (University of Warwick).
- Cotler, P., and C. Woodruff (2008), 'The impact of short-term credit on microenterprises: evidence from the Bimbo Program in Mexico', *Economic Development and Cultural Change*, 56(4): 829-849.
- Crafts, N. (2006), 'Regulation and productivity performance', *Oxford Review of Economic Policy*, 22(2), 186-201.
- Davis, Steven J., John Haltiwanger, Ron S. Jarmin, C.J. Krizan, Javier Miranda, Alfred Nucci, and Kristin Sandusky, 2007 'Measuring the dynamics of young and small businesses: integrating the employer and nonemployer universes', NBER Working Paper no. 13226 (National Bureau of Economic Research, Cambridge, Mass.).
- De Mel, Suresh, David McKenzie, and Christopher Woodruff (2008), 'Returns to capital: results from a randomized experiment'. *Quarterly Journal of Economics* 123(4): 1329-72.
- De Mel, Suresh, David McKenzie, and Christopher Woodruff (2009), 'Are women more credit constrained? Experimental evidence on gender and microenterprise returns'. *American Economic Journal: Applied Economics*, 1(3): 1-32.
- De Mel, Suresh, David McKenzie, and Christopher Woodruff (2010). 'Who are the microenterprise owners? evidence from Sri Lanka on Tokman v. de Soto', in *International Differences in Entrepreneurship*, edited by J. Lerner and A. Schoar (Chicago: University of Chicago Press).
- De Mel, Suresh, David McKenzie, and Christopher Woodruff (2012), 'One-time transfers of cash or capital have long-lasting effects on microenterprises in Sri Lanka', *Science* 335 (6071): 962-966.
- De Mel, Suresh, David McKenzie, and Christopher Woodruff (2013) 'The demand for, and consequences of, formalisation among informal firms in Sri Lanka', *American Economic Journal: Applied Economics* 5(2): 122-150.
- De Mel, Suresh, David McKenzie, and Christopher Woodruff (2014a). 'Business training and female enterprise start-up, growth, and dynamics: experimental evidence from Sri Lanka', *Journal of Development Economics* 106(1): 199-210.
- De Mel, S. D. McKenzie, and C. Woodruff (2014b), 'What generates growth in microenterprises? Experimental evidence on capital, labor and training', CAGE Working Paper no. 212 (University of Warwick).
- De Soto, Hernando (1989), *The other path*. New York: Harper & Row.
- Fafchamps, M., and C. Woodruff (2014), 'Identifying gazelles: expert panels vs. surveys as a means to identify firms with rapid growth potential', CAGE Working Paper no. 213 (University of Warwick).
- Fafchamps, Marcel, David McKenzie, Simon Quinn, and Christopher Woodruff (2014), 'Microenterprise growth and the flypaper effect: evidence from a randomized experiment in Ghana', *Journal of Development Economics* 106(1), pp. 211-226.
- Field, Erica, Rohini Pande, John Papp, and Natalia Rigol (2013). 'Does the classic microfinance model discourage entrepreneurship among the poor? Experimental evidence from India', *American Economic Review* 103(6): 2196-2226.
- Frontier Economics (2012). *The impact of regulation on growth*. A report prepared for the Department of Business, Innovation and Skills (London: Frontier Economics).

- Geertz, Clifford (1978), 'The bazaar economy: information and search in peasant marketing', *American Economic Review*, 68(2), pp. 28-32.
- Hsieh, Chang-Tai, and Benjamin A. Olken (2014), 'The missing "missing middle"', *Journal of Economic Perspectives* 28(3): 89-108.
- ILO (International Labour Organisation) (2010), *Key indicators of the labour market (KILM)* (Sixth edition, Geneva: ILO).
- Macchiavello, R. (2010), 'Development uncorked: reputation acquisition in the new market for Chilean wines in the UK', CEPR Discussion Papers no. 7698 (Centre for Economic Policy Research).
- Macchiavello, R., and A. Morjaria (2013), 'The value of relationships: evidence from a supply shock to Kenyan rose exports', *Warwick Economics Research Papers* no. 1032 (University of Warwick).
- McKenzie, David, and Christopher Woodruff (2008), 'Experimental evidence on returns to capital and access to finance in Mexico', *World Bank Economic Review* 22(3), pp. 457-482.
- McMillan, John. (2002), *Reinventing the bazaar: a natural history of markets*. New York: Norton.
- Schiantarelli, F. (2010). 'Product market regulation and macroeconomic performance: A review of cross-country evidence'. In N. V. Loayza and L. Servén (eds), *Business regulation and economic performance*, pp. 23-65 (Washington, DC: The International Bank for Reconstruction and Development / The World Bank).
- Tokman, Victor (2007) 'Modernizing the informal sector', UN/DESA Working Paper no. 42.

ENDNOTES TO CHAPTER 2

This chapter sums up field research listed in the references under Blouin and Macchiavello (2014), Cotler and Woodruff (2008); De Mel, McKenzie, and Woodruff (2008, 2009, 2010, 2012, 2013, 2014a, b); Fafchamps and Woodruff (2014); Fafchamps, McKenzie, Quinn, and Woodruff (2014); Macchiavello (2010), Macchiavello and Morjaria (2013); and McKenzie and Woodruff (2008). Two of the researchers, Rocco Macchiavello and Christopher Woodruff, are also authors of this policy report. The authors thank Nicolás Lillo Bustos for research assistance.

1. An optimistic view: de Soto (1992); a more pessimistic interpretation: Tokman (2007).
2. A large cross-section: Cotler and Woodruff (2008); a smaller sample: Mckenzie and Woodruff (2008).
3. A study of enterprises in Sri Lanka: de Mel, McKenzie, and Woodruff (2008).
4. A follow-up study: de Mel et al. (2012).
5. More research on female owners in Sri Lanka: de Mel et al. (2009).
6. Related research in Ghana: Fafchamps et al. (2014).
7. The United States: Davis et al (2007).
8. We ask this question: de Mel et al. (2010).
9. Another project based in Sri Lanka: De Mel et al. (2013).
10. This project studied 1,525 enterprises: De Mel et al. (2014b).
11. Micro-businesses in Ghana: Fafchamps and Woodruff (2014).
12. Grace periods on loans: Field, Pande, Papp, and Rigol (2013).
13. The Chilean wine trade: this section is based on Macchiavello (2010). Nicolás Lillo Bustos collected supplementary data on the value and volume of Chilean wine exports and employment in wineries from the United Nations Statistics Division at <http://unstats.un.org/> and the United Nations Commodity Trade Statistics Database at <http://comtrade.un.org/> (both accessed 17 October 2014). Recorded employment in Chilean wineries appears uncertain and is highly variable; some of the variation may be sampling error but the Chilean economy is also subject to real volatility from changes in the price of copper, its major export.
14. One of Kenya's largest foreign currency earners: this section is based on Macchiavello and Morjaria (2013). Nicolás Lillo Bustos collected supplementary data on the value and volume of Kenyan exports from the United Nations Commodity Trade Statistics Database at <http://comtrade.un.org/> (accessed 17 October 2014).
15. The research for this case study: Blouin and Macchiavello (2014).
16. As far as rich countries are concerned: Crafts (2012); Frontier Economics (2012). Less benefit for poor countries: Schiantarelli (2010).

CHAPTER 3. CITIZENSHIP: EMPOWERING WOMEN

INTRODUCTION

Violence against women is a global issue. Women suffer discrimination and violence in all parts of the world, rich and poor. Any society that seeks equal rights and equal opportunities for all citizens must extend those rights and opportunities to women. This raises moral and legal issues that should be of concern to all citizens of the world. At the same time, violence against women is a critical issue for social and economic development. When violence is directed against women, some of the issues raised are specifically economic. In this chapter we will first outline why violence against women is a problem for economic development. After that we will introduce our research, which shows how women's access to politics can be part of the solution.

Box 3.1. Setting the scene

Intimate partner violence, according to the World Health Organization 'occurs in all countries, irrespective of social, economic, religious or cultural group'. Findings from population-based surveys of women from 35 countries around the world suggest that at least 10 and up to 69 per cent of women have been physically assaulted by an intimate male partner at some point in their lives, with at least 3 and up to 27 per cent assaulted in the last year. (Source: WHO 2002.)

Grief and rage in India. 'Yes, the gender gap in education in India is closing. Yes, many more women are now in the labour force than ever before. And yes, political quotas and reservations have increased the percentage of women in elected office. But blocking the transformative potential of this evidence of progress is an age-old patriarchal system which regards women as inferior to men and its toxic interaction with the new global culture of consumerism and its relentless sexualisation of women's bodies.'

'The young woman who was raped had been one of the few from her village who had made it into college, she had a promising professional career ahead of her and she was the citizen of a country with a long track record of democracy and increasing numbers of women elected into office. None of this was sufficient to protect her from a sexual assault the sheer ugly brutality of which has brought thousands of horrified and grieving protestors onto the streets across the country.

'Named "Nirbhaya" ("without fear") by some of the press who, in an unusual show of sensitivity have not revealed her real name, the woman was returning home from the cinema with a male friend at 9 o'clock in the evening. They boarded a bus in the belief that it would take them closer to home. Instead her companion was beaten badly and she was subjected to an extended period of rape and violence that left her brutalised and unconscious. Their naked bodies were thrown out of the moving bus to be found by passersby. Nirbhaya recovered sufficiently to give a statement to the police but died on the 29th December. She was named "fearless" because of the fight she put up against her attackers (she left teeth marks on at least one of their bodies), because of her determination that her attackers be brought to justice and because of her struggle to live, despite horrific injuries to her internal organs'. (Source: 'Grief and rage in India: making violence against women history?' by Naila Kabeer on openDemocracy, 12 June 2014, at <http://www.opendemocracy.net/5050/naila-kabeer/grief-and-rage-in-india-making-violence-against-women-history>, accessed 1 July 2014.)

In Scotland 'the recent rise in recorded rapes may be viewed to some extent as a positive trend reflecting greater awareness and lower tolerance of rape, coupled with increased confidence in the police response to rape rather than simply an actual increase in rape'. (Source: 'Rising rape figures in Scotland could actually be a step forward', by Oona Brooks on The Conversation, 14 July 2014, at <https://theconversation.com/rising-rape-figures-in-scotland-could-actually-be-a-step-forward-29109>, accessed 16 July 2014.)

VIOLENCE AND ECONOMIC DEVELOPMENT

Why is violence against women a development problem?

Violence, including the expectation, threat, and fear of violence was introduced as a theme of Unlocking Development in Chapter 1. In that chapter, our focus was primarily on setbacks to growth from outbreaks of community violence associated with ethnic conflict and civil war. Just such an episode of community violence framed one of the case studies in Chapter 2: organised violence around a contested election in Kenya threatened to disrupt the flower exports around which farmers and flower distributors had carefully built up networks over many years.

In this chapter we address everyday violence against women as an issue in economic development. The focus of our report is on how to bring about long-run growth, and one of the risks to growth that we have already emphasised is the frequent setbacks arising from organised conflict. Wars in Africa and elsewhere often claim the media headlines. Yet the immediate costs of everyday violence against women around the world may be many times larger than the costs of warfare.

Anke Hoeffler and James Fearon, two of the world's experts on conflict, have noted:

For each battlefield death in civil war, about nine times as many people are killed in interpersonal disputes, including many killings related to drug-trafficking, intimate partner violence (of all homicides, 7 per cent female and 5 per cent male), and killing of children (7 per cent). About 43 per cent of all female homicide victims were killed by a current or former intimate partner.¹

According to the same estimate, the global cost of violence against women (including 'intimate partner' homicides and assaults, and other sexual violence) is around half the total human costs of all violence. It exceeds the human costs of organised violence by 20 to 30 times. The annual sum involved is thought to be more than \$4.5 trillion per year. How much is that? It is more than 5 per cent of global GDP. It is as much in one

year as the total value of all development assistance to poor countries over all the years since 1945.²

What are the channels through which violence against women affects economic development? Societies that suppress women's rights by law, stealth, or violence pay a very large price for male supremacy. This price is paid in the moment and through many future periods. Relevant research is summarised in a recent World Bank report.³ Some of the immediate effects emerge from studies that show women who suffer intimate partner violence are unable to work while they recover (Nagpur, India; Vietnam), and are substantially less productive and earn less when they return to work (Nagpur, India; Tanzania). Other studies show that the effects of violence are persistent. Not surprisingly, when women suffer violence they are more likely to suffer long-term health problems. These go beyond the consequences of injury and include raised incidence of sexually transmitted diseases and depression. The children of violent relationships are more likely to be abused themselves, and their health, education, and life chances are also impaired. Perhaps the most persistent damage is revealed by the finding that, when women suffer domestic violence, their children are much more likely to be involved in violent relationships when they grow up.

Thus, violence against women does lasting harm to women and their families, and this harm is passed on to the next generation. Violence against women also makes economic development less sustainable. In other words, the whole of society is impoverished – and remains poor.

The damage to development arises because violence and the fear of violence stand in the way of women's market access and limit their capacity to realise entrepreneurial potential. Chapter 2 showed, for example, that when women engage in developmental activities such as business formation, they face multiple obstacles. Some of these obstacles appear to be laid in their paths by men. When family relations threaten their autonomy, women are less effective entrepreneurs. Violence is one factor that keeps women 'in their place', that is out of the market and out of business leadership. In order to play their full part in economic development, women must be free of violence directed against them because of their gender.

More generally, the suppression of women's rights and opportunities is one aspect of a limited-access society, as discussed in Chapter 1. In limited-access societies nearly all women are excluded from business and politics, and they are also silenced in the public arena so that their exclusion goes unremarked. If an open-access society rests on the rule of law, then it is undermined by violence and the fear of violence, including violence against women. If the purpose of economic development is to expand the control that ordinary people can exercise over their own lives, then this purpose is confounded as long as women fear violence and are afraid to participate fully as citizens, providers, and entrepreneurs.

In short, an open-access society is not only essential if economic development is to be sustained, but it must specifically include women's access to power as well as wealth.

The problem of violence against women begins with silence

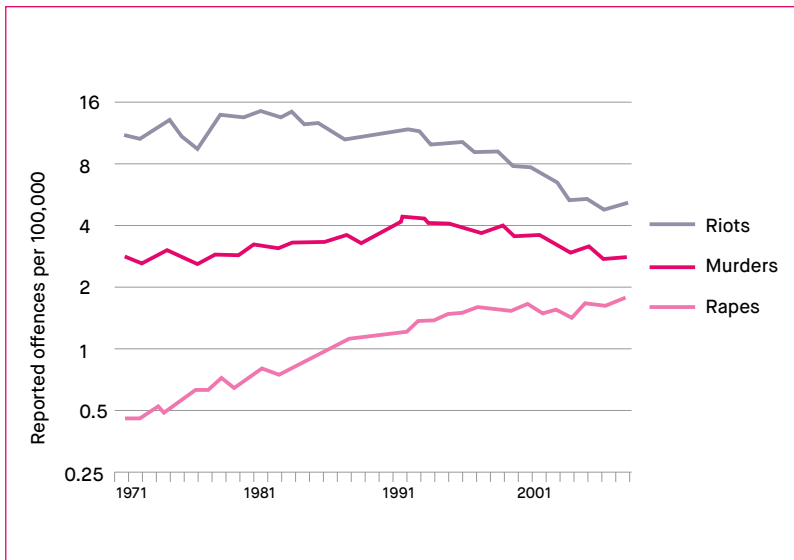
In many parts of the world, violence against women is considered to be normal or is thought to bring shame upon the victim. The result is that much violence against women is hidden by silence. A problem that is hidden cannot be addressed. In this chapter we will show that, when women have greater access to politics, gender violence is better managed. The main reason for this is that it is exposed and brought out into the open.

Violence against women is an acute problem in many developing countries. But this is not always apparent from crime records. In 2010, for example, 79 countries reported the number of rapes to the United Nations. According to these figures the median incidence of rapes per 100,000 people in all those countries in that year was just over 20. The world's most dangerous country was apparently Botswana, with more than 90 rapes per 100,000; second most dangerous was Sweden with more than 60. At the other extreme, India reported less than 2 per 100,000; safest in the world was apparently Egypt, with only one per million.⁴ From these figures we do not learn much about the real distribution of sexual violence around the world, but we can reasonably infer quite a lot about the willingness to report and record sexual violence. In other words, it is likely that Swedish women

report a higher proportion of assaults, while most Indian women who are assaulted suffer in silence.

India provides the evidence base of the present chapter. Figure 3.1 allows us to describe trends in three categories of violent crime in India over more than three decades. Homicide and riotous assembly are forms of violence that are less affected by under-recording. India’s homicide rate rose, then fell; it was never high by the standards set by the African countries discussed in chapter 1. Rates of collective violence expressed in riotous assembly have halved. But reported rapes, less than one per 100,000 in 1971 (the year that these records begin), have quadrupled.

Figure 3.1. Violent crime rates in India, 1971 to 2007



Source: *Numbers of offences in India: National Crime Records Bureau (2007)*. India’s population: *Maddison (2010)*.

A recent incident drew worldwide media attention to India. In New Delhi on the night of 16 December 2012, a 23-year old girl and a male friend returning from a movie boarded what appeared to be a passenger bus.⁵ In the following days the world learned about the savage gang rape of the girl

and her eventual death. As one observer noted, the incident was unusual for India, but not for its brutality. What was unusual was that, instead of apathy, the attack elicited public outrage at home and abroad. Thus it served to bring to light India's hidden burden of violence against women.

After heated debate over how to deter gender violence, the Indian government has placed its bet on a law that calls for stringent punishment of perpetrators of rape and violence against women, including the option of the death penalty. Others are demanding fast-track courts, with increased policing and CCTV surveillance on the streets. In this charged atmosphere, a less dramatic but still effective agency has been overlooked: women's political representation.

HOW DO FEMALE POLITICIANS AFFECT CRIME OUTCOMES AGAINST WOMEN?

The problem of cause and effect

Our research shows that more women in elected political office can have a surprisingly powerful impact on the outcomes of crimes against women.⁶

How do we reach this conclusion? In normal circumstances it would be difficult if not impossible to identify cause and effect. Suppose we see a change in crime outcomes and, associated with it, a change in women's political representation. These changes might be seen over time in a region, or they might be seen comparing two regions. We could then make up a plausible story that links women's political representation (the cause) to crime outcomes (the effect). But should we believe that story? The problem is that changes in women's representation are commonly a result of changes in preferences and attitudes more generally in society. These attitudes include the way that people think about women – including crimes against women. Under these circumstances it is impossible to know what is driving the effect. Was it the women representatives who caused the change in criminal behaviour? Or was it the underlying changes in society that caused the change in behaviour – and also got the women elected? Usually, it's impossible to tell.

Indeed, many would give credence to an opposite story. There is widespread scepticism that female leaders in developing countries have made any difference at all to their constituents' welfare.⁷

Our research overcomes the problem of inferring causation by means of a large-scale natural experiment (see Box 2.2 on page 52). This experiment was made possible by a legal reform to the Indian system of local government, called Panchayati Raj (see Box 3.2). The reform was introduced in 1993. It required that one third of all seats would be reserved for female candidates; the other two thirds would continue to be available to both male and female candidates, but in practice they would continue to be contested largely by men. Thus one-third of all seats in these councils, and also one-third of all chairperson positions across councils, were now reserved for women. The result was a dramatic increase in the number and proportion of women in political office.

The effect of the reform is confirmed by a comparison with assemblies that continue to lack quotas for women. In the legislatures of India's federal states over the past three decades, for example, only 5.4 per cent of members have been women.

Box 3.2. The reform of Panchayati Raj

India is a federal state of 36 states and territories. Each state has its own government and state-level legislature. Panchayati Raj concerns local government below the state-level.

Panchayati Raj is the name that India's first prime minister Jawaharlal Nehru gave to the Indian system of local government. The word raj means 'rule' and a panchayat is literally an assembly of village elders. In fact, Panchayati Raj institutions now comprise elected councils in villages (panchayats), an intermediate level (panchayat samitis), and the district level (zila parishads).

The reform of Panchayati Raj was enacted in 1993, but implemented across India's states at different times. This was for several reasons; it is important to the design of our research that none of these reasons had any relationship to trends in violent crimes against women.

Another reason was lawsuits that challenged specific aspects of the reform and led to different delays in different states. Bihar, for instance, conducted its first Panchayati Raj election only in 2001, because of a lawsuit over representation of 'other backward castes' in Panchayati Raj institutions.

In our research, we examine the effects of the resulting increase in women's local political representation on documented crimes against women. How does the reform help us to identify cause and effect? At first sight a national reform would not seem like a promising case to study, because the effect of the reform might be expected to be the same everywhere. What creates the opportunity for researchers is that the reform, although enacted in 1993, was implemented at varying times across different states of the country. Just as important, as explained in Box 3.2, the reasons why the reform was implemented more rapidly in some states than in others had nothing to do with pre-existing levels of gender crime, and they also had nothing to do with any attitudes and preferences in society that would have made gender crime more or less acceptable.

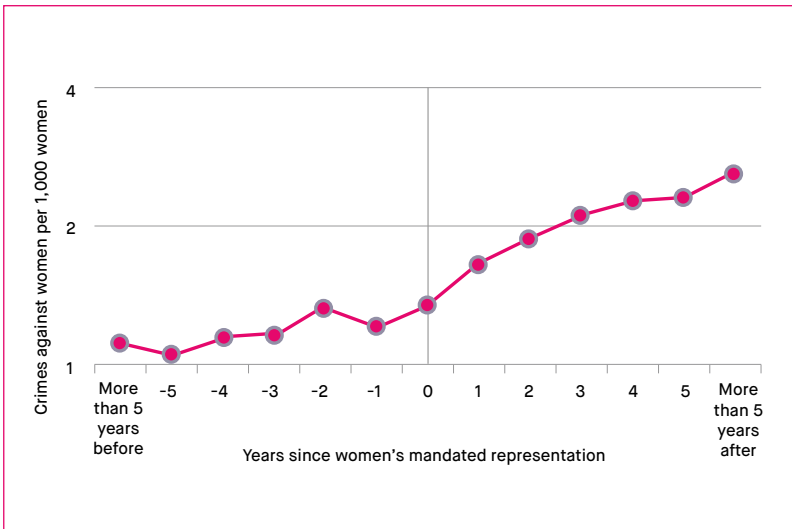
In other words, even if attitudes to women in Indian society were changing, the changes were unrelated to the size and timing of the increases in women's local political representation. At any given moment, many districts were being 'treated' by a sudden, exogenous increase in the number and proportion of women in political office, while other districts were not being treated in the same way. The untreated districts make up a control group. By observing many such moments from start to finish of the reform, and pooling all the information, we can cleanly identify the effects on crime of the cause: women's representation.

To summarise, unique features of India's reform make it the single largest natural experiment worldwide in the effects of increasing the number and proportion of women in political office. It is not surprising, therefore, that it has been a focus of many studies on how women leaders affect citizen outcomes. Our research is one of these studies.

A rise in gender crimes: bad news or good?

When we compare rates of offending before and after the implementation of the reform across states we find that more women political representatives led to an increase in documented crimes against women. We illustrate this from country-wide crime data in two ways. Figure 3.2 shows that in each district offences against women rose steeply following the increase in women’s representation. Figure 3.3 shows the same numbers in another way, indicating that a 23 per cent increase in reported gender crimes can be attributed specifically to implementation of the 1993 reform. This included an 11 per cent rise in the number of reported rapes and a 12 per cent increase in kidnappings of women.

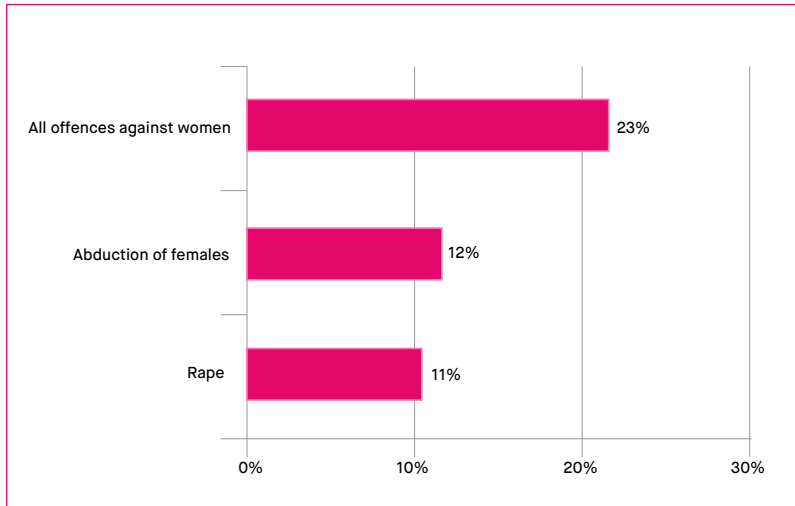
Figure 3.2. Year-by-year effects of women’s empowerment on reported crimes against women



Source: Iyer et al. (2012).

Notes: Each data point represents the impact of women’s representation on the total of reported crimes against women after a given number of years. The vertical line at year zero on the horizontal axis represents the time the reform was implemented in each of India’s federal states. The actual date varied across the states as explained in Box 3.2.

Figure 3.3. Estimated changes in reported offences against women following implementation of the Panchayati Raj reform



Source: Iyer et al. (2012).

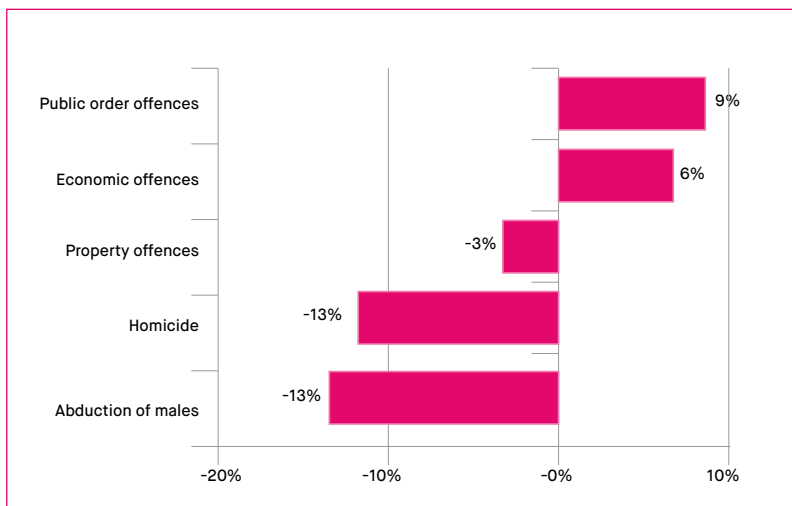
Notes: Crime variables are the number of offences per 1,000 women. Results control for demographic characteristics, real per capita state GDP, policy strength per capita, state and year fixed effects and state-specific time trends. Statistically, not all results shown are significantly different from zero.

At first sight this is disheartening. Indian opponents of mandated representation for women warned that women were inexperienced in governance; they predicted that pushing women into leadership roles would worsen outcomes for everyone. An alternative interpretation is also possible: perhaps rising gender crime statistics were driven by a backlash against women in political office. Either way, one might wonder whether the data are telling us the critics were right.

Several other pieces of evidence encourage optimism. First, it is not true that female leadership has led to worse outcomes for everyone. Figure 3.4 shows clearly that there was no surge in reported crime outcomes unrelated to women. As women moved into legislative seats, public order offences and economic offences rose modestly, but property offences, homicides, and male abductions fell. We attach particular significance to

the evidence on homicides. It is not easy to hide a body; homicides are much harder to conceal than other crimes, and it should go without saying that homicide statistics are unaffected by the willingness of the victim to report the offence. From this evidence, it is more or less certain that we are looking at a decline in underlying violent crime.

Figure 3.4. Estimated changes in other reported offences following implementation of the Panchayati Raj reform



Notes: Crime variables are the number of offences per 1,000 population, except abduction of males which is measured per 1,000 males. Results control for demographic characteristics, real per capita state GDP, policy strength per capita, state and year fixed effects and state-specific time trends.

As for violence against women, other evidence shows clearly what happened. There was no increase in underlying rates of offending but there was an increase in the proportion of offences against women that victims were willing to report and document. In other words, the increase in recorded crimes against women is actually good news. The mechanism driving this seems to be that where women moved into political office the police became more responsive to gender crimes; this encouraged women victims to step forward and speak out, so that reported crimes rose.

A lack of police responsiveness has long been identified as a major problem in India. A study in the state of Rajasthan found that on average the police registered only half of all cases of sexual harassment and domestic violence.⁸ Typically they did this only when a male relative reported it on behalf of a female victim. In contrast, our survey data show that when village councils have female leaders, women are significantly more likely to say that they will lodge a complaint with the police should they become victims of a crime. Men's responses, in contrast, are unaffected.

Our data also refutes the idea that higher rates of reported gender crime reflected a male backlash against women in politics. Women from villages with female leaders were not targets for gender-based abuse at a higher rate than women from other villages. This supports the contention that higher rates of documented gender crime under women political representatives have not been driven by an increase in underlying crime.

Another nationwide survey has looked directly at how women and men interact with the local police. Women in villages with female council heads reported greater satisfaction in their contacts with the police as well as a lower likelihood of being asked to pay bribes.⁹ In contrast the experience of men was neither better nor worse if the village council head was a woman.

Finally, we can consider direct evidence on police actions. In the average state, our evidence shows, arrests for crimes against women increased by 31 per cent after the state implemented political representation for women.

Taken together, our evidence shows clearly that, where women have raised their profile in local government, female victims have benefited from greater responsiveness and willingness to act on the part of the police.

WHAT DO WOMEN ACTUALLY DO IN POLITICS?

Women's voice

What is it that female political representatives do that leads to these effects? It is important to be aware that the local government reform did not suddenly give women direct authority over the courts or the police. Law

and order are not a local government subject, and local representatives cannot change police priorities or redirect resources to fight or prevent crime. Whatever women leaders have done to change crime outcomes has happened in some other way.

A study of village meetings gives a clue: women are 25 per cent more likely to speak up if the village council leader is a woman.¹⁰ To be heard, one must first speak – and female council members and council heads seem to give women more confidence to do so.

Another clue is found by asking at what level women's participation in politics has made the greatest difference. There are three levels of local government at which India's 1993 reform increased the participation of women: the district, sub-district and village level. We made use of the fact that during any election cycle only a third of district council headships within any state are randomly assigned to women (whereas a third of the members across all these councils are women). This allows us to calculate the marginal impact of a female district council head, over and above the impact of women leaders and council members at sub-district level. This marginal impact is small. What this means is that the greater effect of female political representation on crime reporting is at lower levels. In other words, for victimized women to find a voice, the proximity of women leaders does matter. Our conclusion can be linked to the finding that women are more empowered to speak up in village meetings where the council is led by a woman.

The idea that women's voice is the critical factor is consistent with what women say when they are asked what would make the police be more responsive to them. In the State of the Nation Survey, women victims strongly believe that the police are 10 percentage points more likely to listen to them sympathetically and to take action if they go to the police station accompanied by a locally influential person. Nearly half of respondents identified their village council member as the locally influential person they would turn to in case of difficulty.¹¹

As U.S. Supreme Court Justice Sonia Sotomayor has put it,

Our experiences as women or people of colour affect our decisions ... Hence, one must accept the proposition that a difference there will be [made] by the presence of women or people of colour on the bench. Personal experiences affect the facts that judges choose to see.¹²

In the Indian context, it is clear that the gender of our leaders matters. It is not that women have captured the courts or the police. Rather, the female identity of their political leader has changed how women – and policemen and policewomen – are responding to gender crimes.

Women's political representation brings other benefits

What else can female political representatives achieve? With good reason, the primary focus of this chapter is on gender-based crime. The assurance of personal safety and fair treatment under the law are two of the most fundamental aspects of civil society. At the same time, having more women in politics can make other differences too.

Two recent studies examine this issue, adopting a different approach to the problem of cause and effect. They compare post-election outcomes when female candidates are winners, compared with male winners. Again, the challenge is to avoid attributing outcomes to a female politician that might be driven by underlying attitudes or preference among the voters that elected her. Both studies solve this problem by looking only at constituencies with closely contested outcomes. When the election is close (with less than a 5 per cent margin between votes for the winner and runner-up), it is plausible to think that the election could have gone either way. In other words, the gender of the winner was decided to a large extent by chance. Hence, average differences in outcomes after the election that are associated with the gender of the winner were probably caused by the winner's gender difference, not by something else that the research failed to measure.

One of these studies shows that having more female politicians in Indian state-level legislatures results in lower rates of neo-natal mortality. This effect arises through better access to information, better health infrastructure, and

more use of health care facilities and antenatal care visits. The other study shows that Brazilian cities with female mayors have better health outcomes, show fewer irregularities in public procurement practices, and also receive more discretionary federal transfers. Meanwhile, women mayors hire fewer temporary staff members to achieve their objectives. In other words, they achieve better outcomes with fewer resources.¹³

In the Indian local-government context, objectors to mandated women political representatives held strong preconceptions about how effective women leaders would be. They maintained that politically inexperienced and otherwise disadvantaged women would be overruled or manipulated by their spouses or other powerful local interests. An influential study refutes these fears. In providing public goods under Panchayati Raj, it shows, female village leaders have provided a better match with women voters' preferences, for example more water and more roads in West Bengal, and more water but fewer roads in Rajasthan. This is despite the fact that women leaders began with low literacy levels and socio-economic status, and had little experience, ambition or political prospects until they assumed leadership positions.¹⁴

POLITICAL PARTICIPATION: ANOTHER CASE OF MISSING WOMEN?

A global perspective

Despite the advantages that women politicians have been found to bring to the table, they remain underrepresented in government in most countries. Indeed, the worldwide average for the proportion of women legislators (based on 187 countries) today stands at 20 per cent, clearly far short of women's share in the population.

While the 1993 law in India has mandated that the minimum proportion of women representatives locally should be one third (higher in some recent cases), women constitute just 11 per cent of political representatives in the national parliament and 14 per cent at the state level.

It might be supposed that women are likely to play a larger role in the political systems of more developed economies. A few examples suggest

that this intuition might be misleading, however. Female legislators account for only 8 per cent of the national parliament of wealthy Japan. The wealthier United States does somewhat better with 18 per cent, and the United Kingdom beats that with 23 per cent. But Senegal reaches 43 per cent and yet is one of the poorest countries in the world. Among European countries the highest share, 45 per cent, belongs to Sweden, but the highest figure in the world is reported by Rwanda at 64 per cent.

Figure 3.5. Women representatives in the national legislature, 117 countries



Sources: Shares of women in the lower (or single) house of the national legislature are taken from the *Women in National Parliaments* dataset of the Inter-Parliamentary Union at <http://www.ipu.org/wmn-e/classif.htm> (accessed 1 July 2014). GDP per head in 2013 is from *The Conference Board Total Economy Database, January 2014*, available at <http://www.conference-board.org/data/economydatabase/> (accessed 1 July 2014).

As a further check, Figure 3.5 plots rates of female representation in the lower house of parliament against GDP per head of each country in a large selection of developed and developing countries. A striking result is that women's political participation does not show any kind of significant pattern with respect to a country's level of economic development. There is somewhat wider variation among poorer countries than among richer ones, as can be seen by comparing Senegal and South Africa (both over 40 per cent) with Yemen and Qatar (zero or close to zero).

So – what keeps women out of politics?

Women's participation in politics could lag behind their population share for several reasons. In democracies voters, both male and female, may be prejudiced against female candidates. In multi-party democracies, even if voters are unbiased, political parties may avoid selecting women for winnable seats. Finally, women themselves may not aspire to hold office, and this could be because they are deterred by biased voters or biased parties, or because they carry a double burden of duties at work and in the home, or for still other reasons.

Research on closely contested elections to the state legislatures in India can show which of these factors is keeping women out of politics.¹⁵ In state elections, political parties must decide on the pool of candidates they will field across different constituencies. This is unlike local government elections, where political parties are not involved. The researchers find that having a female winner in a particular constituency does not induce major political parties to put forward new female candidates from the same or other constituencies. Female winners are 9.2 per cent more likely to be fielded as their party's candidate for the next election compared with male winners – an important consideration in India where many incumbent representatives do not seek re-election. At the election after that, however, when the female candidate has won twice, their reselection advantage drops off to 4.3 per cent. So, one factor in women's poor political prospects seems to be political parties' lack of enthusiasm. In contrast voter turnout, male or female, is not affected by a candidate being female. This suggests that voter bias is not the key factor that is keeping women out in this context.

This is not to deny that some voter bias is at work. In India, villages with female local government leaders have lower levels of corruption. They provide more public goods, and the quality of the public goods they provide is at least equal to that found in male-headed villages. Despite this, female village leaders are rated below their male counterparts. In Brazil, despite achieving comparable or better outcomes for health and education, with lower levels of corruption, female city mayors are 20 per cent less likely to be re-elected than male mayors.¹⁶

However, unfamiliarity with female candidates seems to play a role in this regard. Indeed, greater exposure to women leaders tends to reduce voter bias against them. In West Bengal, male village voters with prolonged exposure to women as local council leaders (10 years, or two election cycles) have been found to be more likely to associate women with political roles in implicit association tests; in fact, they ranked political campaign speeches delivered in a female voice higher than those with identical content delivered in a male voice. The end result was that villages in West Bengal with longer (10-year) exposure to women leaders had a significantly larger share of women council leaders than those with no exposure (18.5 versus 11 per cent).¹⁷

Finally, do Indian women have an interest in seeking office and confidence in their capabilities comparable to those of men? On the evidence they are not shrinking violets. In West Bengal women reported feeling as competent as their male counterparts in executing their duties after a couple of years of experience. Constituencies with one round of reservation in Mumbai saw a 7.5 per cent increase in the proportion of female candidates contesting open seats the next time around. This was already building on a 10-fold increase in the number of female candidates in the first round of reservation itself. Even in the villages of West Bengal, twice reserved constituencies were found to have doubled the proportion of female candidates in those with no reservation (10.1 per cent vs. 4.8 per cent).¹⁸

The case for quotas

Earlier we offered three possible reasons for women's absence from politics: voter bias, party bias, and women's lack of interest. The Indian experience of mandated reservation suggests that voter bias and women's lack of interest cannot be the whole story. If anything, mandating women's political representation appears to draw more women into the political sphere, especially in comparison to selection processes that can be manipulated by political parties and incumbent male politicians. Just as importantly, women's lack of extensive political experience does not seem to handicap their interest or performance either.

This is consistent with the international picture. Over the last twenty years, the world has seen a push for political quotas for women in many countries. These have taken various forms. Most common have been voluntary quotas, sometimes in combination with other methods. The next most common method has been to legislate a minimum proportion of female candidates. Least popular is the reservation of seats, the method used in India. A study of women's participation in politics confirms that, while the proportion of women among elected representatives bears no relation to a country's income level, it is dramatically affected by political quotas. There are clear differences among types of quota, however. Imposing a quota for female candidates raises the share of women in the national parliament by around 20 per cent of the initial level, whereas reserving seats for women raises their representation by around 60 per cent.¹⁹

WHAT ABOUT GENDER CRIME IN DEVELOPED COUNTRIES?

Similar, but also different

Whatever the crime statistics say, there is not much doubt that the status of women in developed countries is considerably better than in most developing nations, including India. Even in developed countries, however, the recording of crimes against women is fraught with complications.

A good starting point is domestic violence, the most common form of violence against women in developed countries. In the United States, about 75 per cent of all violence against women is perpetrated by domestic partners, with poor women disproportionately affected. In 2001, women in the United States reported 590 thousand incidents of rape, sexual and other assaults at the hands of intimate partners. However, survey data suggest that in the US only 20-50 per cent of cases of such violence are actually reported to the police.²⁰ And even more seriously, on average, four women are killed each day by a partner. Typically the investigation then exposes a history of previous incidents that were not reported or did not trigger intervention.

One measure that has been widely implemented across US states over the past 20 years is mandatory arrest laws. The District of Columbia and 22 states have laws that mandate or at least strongly recommend that when domestic violence is reported everyone accused of abusive behaviour is arrested. Ironically, this seems to have resulted in 'too much' police responsiveness: According to one recent study homicide rates are about 50 per cent higher today in US states with mandatory arrest laws than those without.²¹ These measures appear to have backfired in tackling gender violence because they have reduced the likelihood that victims report incidents to the police. In other words, the certainty of a partner's immediate arrest, weighed against the possibility of continued abuse in future, might persuade a woman not to report violence. As a result, abuse would go unreported until it escalated to homicide.

Other evidence shows that women who do report domestic violence, leading to their partner's arrest, often drop charges. Studies in the 1970s and 1980s found that this happened in at least 50 and up to 90 per cent of cases. However, women who drop charges are four times more likely to suffer future violence than those who do not.²² Women often return to the same partner as well. In a national survey, victims of physical assault suffered an average of 4.5 years of victimisation by the same partner, enduring seven assaults in that time period.²³ 'No-drop laws' that require prosecution of a person charged with assault to proceed, even when the victim wishes to drop charges subsequently, have induced a 14 per cent increase in calls reporting domestic violence, but they have not had any effect on violence against women measured by homicide and hospitalisation rates.²⁴

On a related note, in the US military, female victims who are typically lower level officials were said to be widely discouraged from reporting abuse. Either on their own, or due to active discouragement by their peers and seniors, victims often choose not to report abuse due to emotional distress and the potentially adverse impact on their careers.

Meanwhile, a new and vicious form of gender crime that has recently drawn considerable attention and discussion is abuse using social media

online. The lack of official understanding of this new form of crime and the associated lack of police responsiveness has been a source of frustration for women victims.²⁵

Overall, it seems that institutional responses to gender violence in developed countries have also not been very effective. As in much poorer countries, there is under-reporting. Public awareness, in contrast, is often greater. Police responses are sometimes too little and sometimes too much. In short, Western societies are also in need of a more holistic and nuanced discussion of how to encourage reporting and intervene more effectively to reduce violence against women.

Women's political representation in developed countries

In the absence of good research evidence, one can only speculate as to whether the presence of more women in the political domain will lead to the more nuanced approach that is needed. Perhaps it is not a coincidence that in the numerous sexual harassment cases that arose in the US military in 2012/13, the key politicians who initiated legislative action were all women: US senators Kirsten Gillibrand, Claire McCaskill and Barbara Boxer.²⁶

As Figure 3.5 demonstrates, most developed countries do no better than others in women's representation in the legislature. If a developed country operates a quota system it is typically limited to requiring the inclusion of women in party candidate lists. Some countries, such as the United States and the United Kingdom, have no quotas at all.²⁷ Not surprisingly, and in contrast to the Indian experience in local government, the proportion of women who enter politics or express an interest in doing so has risen little in the US over time.²⁸

Some other developed countries, such as Spain and France, operate candidate quota systems, but the evidence suggests that these can be manipulated by political parties.²⁹ Male politicians who might lose out to female competitors seem to play a role in keeping down the proportion of female politicians that succeed in winning seats. Both countries have fixed deadlines for achieving set proportions of women in the legislature,

so there is hope that women's participation will rise over time. Other developed countries should seriously consider initiatives to expand women's political participation.

IMPLICATIONS FOR POLICY MAKERS

Gender-based violence is prominent among the constraints that bind women into a subordinate position in the family and in society. Lacking autonomy, women are prevented from emerging in society and in the economy.

Crimes against women remain a stubborn concern in developing countries, and to a lesser extent, in developed countries. A significant factor everywhere is that reporting such crimes is challenging for women. The result is that gender crime is severely under-reported.

The reasons range from a lack of nuanced police responsiveness to a host of other psychological, emotional and economic costs. In India, our research shows, police indifference is a major factor. In the United States an opposite factor seems to be involved: police responses may sometimes be too aggressive, as with mandatory arrest laws.

In the short term we need to encourage the reporting of gender crimes. In the long term we need to reduce their true incidence. In today's changing social terrain, gender relations are often under strain because enabling women to speak out against violence and the capacity for police to intervene appropriately may defy long standing social norms that govern men and women's behaviour.³⁰ To avoid violent fallouts from these social stresses demands nuanced responses.

Where is the nuance to come from? An essential element in any strategy for dealing with gender crime should enable women to be seen and heard in public life and present at the policy-making table. Specifically:

- Our research in India has shown that more women in political office raise the number of documented crime against women. This sounds bad, but actually the news is good. There is no increase in underlying gender crime, but more gender crimes are being reported.

- Police activism in documenting and dealing with gender crimes is higher in areas with more female political representatives. Associated with this is increased willingness of female victims to report the crime. Victims are more willing to come forward because they anticipate the police are more likely to hear them when women leaders are in charge.
- Women politicians have the biggest impact on giving a voice to female victims when they are present at the local government level, where they are closest to female victims.
- Reporting of crimes against women, including domestic violence, is also a problem in developed countries. There too, institutional responses often discourage reporting and fail to reduce offending.
- Political participation rates for women are low in many countries across the world. The typical developed country is no better than a developing country in this respect. Reserved seats for women, followed by legislative candidate quotas, may be the most effective way to encourage more women into politics.

REFERENCES

- Aizer, A. and P. Dal Bo (2009), 'Love, hate and murder: commitment devices in violent relationships', *Journal of Public Economics*, 93 (3-4): 412-28.
- Banerjee, A., R. Chattopadhyay, E. Duflo, D. Keniston, and N. Singh (2012), 'Can institutions be reformed from within? Evidence from a randomized experiment with the Rajasthan police', NBER Working Paper No. 17912 (National Bureau of Economic Research, Cambridge, Mass.).
- Beaman, L., R. Chattopadhyay, E. Duflo, R. Pande, and P. Topalova (2009), 'Powerful women: does exposure reduce bias?', *Quarterly Journal of Economics*, 124 (4): 1497-1540.
- Beaman, L., E. Duflo, R. Pande, and P. Topalova (2010), 'Political reservation and substantive representation: evidence from Indian village councils', in S. Bery, B. Bosworth and A. Panagariya (eds), *India Policy Forum* (Brookings Institution Press and the National Council of Applied Economic Research: Washington, DC and New Delhi), vol. 7, 159-91.
- Bertrand, M., E. Kamenica, and J. Pan. (2013). 'Gender identity and relative income within households', Working Paper, University of Chicago. Available from <http://faculty.chicagobooth.edu/marianne.bertrand/research/papers/identity.pdf> (accessed 15 October 2014).
- Bhalotra, S., and I. Clots-Figueras (2014). 'Health and the political agency of women.' *American Economic Journal: Economic Policy*, 6(2): 164-97.
- Bhalotra, S., I. Clots-Figueras, and L. Iyer (2013). 'Path-breakers: How does women's political participation respond to electoral success?' *Harvard Business School Working Papers* 14-035 (Harvard Business School).
- Bhavnani, R. (2009), 'Do electoral quotas work after they are withdrawn? Evidence from a natural experiment in India', *American Political Science Review*, 103 (1): 23-35.
- Brollo, F. and U. Troiano (2013): 'What happens when a woman wins an election? Evidence from close races in Brazil', CAGE Working Paper no. 160 (CAGE, University of Warwick).
- Chattopadhyay, R., and E. Duflo (2004). 'Women as policy makers: evidence from a randomized policy experiment in India', *Econometrica*, 72:5, 1409-1443.
- Citron, D. (2014). *Hate crimes in cyberspace* (Cambridge, MA: Harvard University Press).
- Duflo, E., and P. Topalova (2004), 'Unappreciated service: performance, perceptions, and women leaders in India', *Framed Field Experiments* 00233, available at <http://karlan.yale.edu/fieldexperiments/papers/00233.pdf> (accessed 3 July 2014).
- Esteve-Volart, B. and M. Bagues (2012), 'Are women pawns in the political game? Evidence from elections to the Spanish Senate', *Journal of Public Economics* 96(3): 387-99.
- Field, M.H., and H.F. Field (1973), 'Marital violence and the criminal process: neither justice nor peace', *Social Service Review* 47: 221-40
- Ford, D.A. and M.J. Regoli (1992), 'The preventive impacts of policies for prosecuting wife batterers', in E.S. Buzawa and C.G. Buzawa (eds), *Domestic violence: the changing criminal justice response* (Westport, CT: Auburn House).
- Frechette, G., F. Maniquet, and M. Morelli (2008), 'Incumbents' interests and gender quotas', *American Journal of Political Science*, 52 (4): 891-909.
- Hoeffler, A., and J. Fearon (2014). 'Benefits and costs of the conflict and violence targets for the post-2015 development agenda', Working Paper (Copenhagen Consensus Center), available at <http://www.copenhagenconsensus.com/> (accessed 22 September 2014).
- Iyengar, R. (2009) 'Does the certainty of arrest reduce domestic violence? Evidence from mandatory and recommended arrest laws', *Journal of Public Economics*, 93 (1): 85-93

Iyer, L., A. Mani, P. Mishra, and P. Topalova (2012), 'The power of political voice: women's political representation and crime outcomes in India', *American Economic Journal: Applied Economics*, 4 (4): 165-93.

Klugman, J., L. Hanmer, S. Twigg, T. Hasan, J. McCleary-Sills, and J. Santamaria (2014), *Voice and agency: empowering women and girls for shared prosperity* (Washington, DC: The World Bank).

Lawless, J.L., and R. L. Fox (2010). *It takes a candidate: Why women don't run for office*. Revised edition. Cambridge: Cambridge University Press.

Millennial Survey (2002), *Millennial survey* (Public Affairs Centre: Bangalore).

Minnesota Crime Survey (2003). *Minnesota crime survey 2002: safe at home* (Minnesota Planning – Criminal Justice Statistics Center).

National Crime Records Bureau (2007). 'Incidence of cognizable crimes (IPC) under different crime heads during 1953 to 2007', available at <http://ncrb.nic.in/cii2007/cii-2007/1953-2007.pdf> (accessed 3 July 2014).

Pande, R., and D. Ford (2011), 'Gender quotas and female leadership: A review' (background paper for the World Development Report on Gender), available at <http://www.hks.harvard.edu/fs/rpande/papers/> (accessed 3 July 2014).

Parnas, R.I. (1973), 'Prosecutorial and judicial handling of family violence', *Criminal Law Bulletin*, 9: 733-69.

Sotomayor, S. (2002), 'A Latina judge's voice', *Berkeley-La Raza Law Journal*, 13: 87-93.

State of the Nation (2009). *State of the nation survey, Wave VII*, Centre for the Study of Developing Societies, New Delhi.

Tierney, M.J., D.L. Nielson, D.G. Hawkins, J.T. Roberts, M.J. Findley (2011), 'More dollars than sense: Refining our knowledge of development finance using AidData', *World Development* 39(11), pp. 1891-1906.

Tjaden, P. and N. Thoennes (2000a), 'Full report of the prevalence, incidence and consequences of violence against women: findings from the National Survey on Violence Against Women', National Criminal Justice 183781 (Washington DC: Department of Justice).

Tjaden, P. and N. Thoennes (2000b), 'Extent, nature, and consequences of intimate partner violence: findings from the National Survey on Violence Against Women', National Criminal Justice 181867 (Washington DC: Department of Justice).

WHO (2002), *World report on violence and health* (Geneva: World Health Organisation).

ENDNOTES TO CHAPTER 3

This chapter sums up research listed in the references under Iyer, Mani, Mishra, and Topalova (2012). One of the researchers, Anandi Mani, is also an author of this policy report.

1. Two of the world's experts on conflict: Hoeffler and Fearon (2014).
2. Nearly \$5 trillion of development assistance to poor countries SINCE 1945: Tierney et al. (2011).
3. A recent World Bank report: Klugman et al. (2014: 74-75).
4. A sample of 79 countries: as reported by the United Nations Office on Drugs and Crime at <http://www.unodc.org/unodc/en/data-and-analysis/statistics/data.html> (accessed 15 October 2014).
5. The events of 16 December 2013 and reactions to them: 'The unspeakable truth about rape in India', by S. Faleiro, *The New York Times*, 1 January 2013; 'Rape protests spread beyond India', by J. Burk, *The Guardian*, January 4, 2013; 'Notorious attack spurs India to approve new rape laws', by J. Yardley and N. T. Bagri, *The New York Times*, 3 February 2013.
6. Our research: Iyer, Mani, Mishra, and Topalova (2012).
7. Skepticism: 'Women hurting women', by N. D. Kristof, *The New York Times*, September 29, 2012.
8. Lack of police responsiveness: 'For rape victims in India, police are often part of the problem', by G. Harris, *The New York Times*, January 22, 2013. A study in Rajasthan: Banerjee et al. (2012).
9. Data are from the Millennial Survey (2002), which covers 36,542 households in 2,304 randomly selected villages in India.
10. A study of village meetings: Beaman et al. (2010).
11. The State of the Nation (2009) survey includes 14,404 respondents from 17 major states of India.
12. The words quoted are from Sotomayor (2002).
13. One of these studies: Bhalotra and Clots-Figueras (2014). The other study: Brollo and Troiano (2013).
14. An influential study: Chattopadhyay and Duflo (2004).
15. Research on closely contested elections: Bhalotra et al. (2013).
16. In India: Duflo and Topalova (2004). In Brazil: Brollo and Troiano (2013).
17. In West Bengal: Beaman et al. (2009).
18. In West Bengal: Beaman et al. (2009). In Mumbai: Bhavnani et al. CHECK (2009).
19. A study of women's participation in politics: Pande and Ford (2011).
20. Survey data: Bureau of Justice Statistics (1998); Minnesota Crime Survey (2003); and Tjaden and Thoennes (2000a), using data from the National Criminal Victimization Survey.
21. According to one recent study: Iyengar (2009).
22. Studies in the 1970s and 1980s: Parnas (1973); Field and Field (1973); and Ford and Regoli (1992).
23. In a national survey: Tjaden and Thoennes (2000a; 2000b).

24. No-drop laws: Aizer and Dal Bo (2009).
25. Lack of official understanding: 'Why women aren't welcome on the Internet', by A. Hess, The Pacific Standard, January 6, 2014 available at <http://www.psmag.com/navigation/health-and-behavior/women-arent-welcome-internet-72170/>; see also Citron (forthcoming).
26. According to 'Reports of military sexual assault rise sharply', by J. Steinhauer, The New York Times, 7 November 2013.
27. No quotas at all: Pande and Ford (2011).
28. Proportion of women who enter politics: Lawless and Fox (2010).
29. Evidence on Spain: Esteve-Volart and Bagues (2012); on France: Frechette et al. (2008).
30. Gender relations are often under strain: Bertrand et al. (2013).

ABOUT THE AUTHORS

STEPHEN BROADBERRY

Stephen Broadberry is Professor of Economic History at the London School of Economics and a research associate and theme leader of Warwick's ESRC Centre on Competitive Advantage in the Global Economy (CAGE). He is an editor of the *Economic History Review* and a past editor of the *European Review of Economic History*. A past president of the European Historical Economics Society, he is currently a trustee of the Economic History Association and the Asian Historical Economics Society, and an executive committee member of the Economic History Society. His research interests include the development of the world economy from 1000AD to the present; historical national accounts for Britain since 1086; the Great Divergence of productivity and living standards between Europe and Asia; sectoral aspects of comparative growth and productivity performance during the nineteenth and twentieth centuries; productivity in services; wars and economic performance. His books include *The British Economy Between the Wars: A Macroeconomic Survey* (Blackwell, 1986); *The Productivity Race, 1850-1990: British Manufacturing in International Perspective, 1850-1990* (Cambridge University Press, 1997); *Market Services and the Productivity Race, 1850-2000: British Performance in International Perspective* (Cambridge University Press, 2006), the two-volume *Cambridge Economic History of Europe*, edited with Kevin O'Rourke (Cambridge University Press, 2010) and *British Economic Growth, 1270-1870*, co-authored with Bruce Campbell, Alexander Klein, Mark Overton and Bas van Leeuwen (Cambridge University Press, forthcoming). He has held previous positions at the Universities of Warwick, Oxford, Cardiff, and British Columbia and visiting positions at the University of California, Berkeley, Humboldt University, Berlin, and UPF Barcelona.

NICHOLAS CRAFTS

Nicholas Crafts FBA, CBE is Professor of Economic History and Director of Warwick's ESRC Research Centre for Competitive Advantage in the Global Economy. His research interests include Britain's Industrial Revolution and relative economic decline, the history of general purpose technologies, and why growth rates differ. He recently published *The Great Depression of the*

1930s: Lessons for Today (Oxford University Press, 2013, edited with Peter Fearon). His career has included posts at the London School of Economics, Stanford University, the University of California at Berkeley, and the University of Oxford. He is a past president of the Economic History Society. Among many editorial responsibilities he is a past editor of the Economic History Review. He has also been a consultant to BIS, HM Treasury, the IMF and the World Bank.

LEIGH GARDNER

Leigh Gardner is Assistant Professor of Economic History at the London School of Economics. Her research focuses on the economic history of Africa and the British Empire. She is the author of *Taxing Colonial Africa: The Political Economy of British Imperialism* (Oxford University Press, 2012). Her current work compares the development of independent countries in Africa with their colonised neighbours in order to distinguish the effects of colonialism from more general constraints on development faced by peripheral countries before World War II. She is co-editor of the journal *Economic History of Developing Regions* and a book reviews editor of the *Economic History Review*.

MARK HARRISON

Mark Harrison is Professor of Economics at the University of Warwick and Associate Director for Impact of Warwick's ESRC Centre on Competitive Advantage in the Global Economy (CAGE). He is a research fellow of the Centre for Russian and East European Studies at the University of Birmingham and of the Hoover Institution on War, Revolution, and Peace at Stanford University. His research interests lie in the history of Russia, communism, conflict, and security, and the economics of fighting, cheating, stealing, lying, and spying. His books include *The Economics of World War II* (Cambridge University Press, 1998), *The Economics of World War I*, edited with Stephen Broadberry (Cambridge University Press, 2005), *Guns and Rubles: the Defence Industry in the Stalinist State* (Yale University Press, 2008), and *The Economics of Coercion and Conflict* (World Scientific, 2014).

ROCCO MACCHIAVELLO

Rocco Macchiavello is Associate Professor of Economics at the University of Warwick and a research associate of Warwick's ESRC Centre on Competitive

Advantage in the Global Economy (CAGE). He is an associate editor of the *Journal of Development Economics*. Rocco's research interests mainly focus on the microeconomics of development. His recent projects investigate how exporters from developing countries acquire valuable reputations in foreign markets, and the upgrading of production process linked with international trade and agricultural value chains. He has done extensive field work in Bangladesh, Kenya and Rwanda. Before joining Warwick Rocco was a Post-Doctoral Research Fellow at Nuffield College, Oxford. He holds a PhD from the London School of Economics.

ANANDI MANI

Anandi Mani is Associate Professor of Economics at the University of Warwick and a research associate and capacity-building fellow of Warwick's ESRC Centre on Competitive Advantage in the Global Economy (CAGE). She is also a research affiliate at Ideas42, a think tank for behavioural economics at Harvard University. Her research interests are in development economics, with a focus on the behavioural economics of poverty and social exclusion, gender issues and public good provision.

CHRIS WOODRUFF

Chris Woodruff is Professor of Economics at the University of Warwick and a research associate of Warwick's ESRC Centre on Competitive Advantage in the Global Economy (CAGE). He is also a research associate of the National Bureau of Economic Research (NBER), a senior fellow of the Bureau of Research on Economic Analysis and Development (BREAD), and a research fellow of the Centre for Economic Policy Research (CEPR) and the Institute for the Study of Labour (IZA). He directs the Firm Capabilities group at the International Growth Centre and is Scientific Coordinator of the DFID-CEPR joint research venture on Private Enterprise Development in Low Income Countries (PEDL). He is a member of the editorial boards of the *Journal of Development Economics*, the *World Bank Economic Review*, the *Journal of Comparative Economics*, and the *Journal of African Economies*. He is a leading expert on enterprises in developing countries and a pioneer in the use of field experiments in understanding enterprise dynamics. His recent work includes measuring rates of return to capital investments in micro-enterprises, the effect of formal registration on enterprise performance, the

use of business plan competitions to identify small enterprises with potential for rapid growth and the use of temporary wage subsidies to understand the willingness of micro-enterprises to expand employment. His previous work examined the ability of informal contracting and private institutions, such as trade associations to govern trading relations in the absence of functioning state institutions. Geographically, his research spans a broad area of the developing world, including Mexico, Vietnam, Sri Lanka, Ghana and Eastern Europe. Before Warwick he was Professor of Economics at the University of California, San Diego, where he also served as Director of the Center for US-Mexican Studies from 2003 to 2008.

ABOUT CAGE

Established in January 2010, the Centre for Competitive Advantage in the Global Economy (CAGE) is a research centre in the Department of Economics at the University of Warwick. Funded by the Economic and Social Research Council (ESRC), CAGE is carrying out a 10 year programme of innovative research.

Research at CAGE examines how and why different countries achieve economic success. CAGE defines success in terms of personal well-being as well as productivity and competitiveness. We consider the reasons for economic outcomes in developed economies like the UK and also in the emerging economies of Africa and Asia. We aim to develop a better understanding of how to promote institutions and policies which are conducive to successful economic performance and we endeavour to draw lessons for policy makers from economic history as well as the contemporary world.

CAGE research uses economic analysis to address real-world policy issues. Our economic analysis considers the experience of countries at many different stages of economic development; it draws on insights from many disciplines, especially history, as well as economic theory. In the coming years, CAGE's research will be organised under four themes:

- What explains comparative long-run growth performance?
- How do culture and institutions help to explain development and divergence in a globalising world?
- How do we improve the measurement of well-being and what are the implications for policy?
- What are the implications of globalisation and global crises for policy making and for economic and political outcomes in western democracies?

Copyright © The Social Market Foundation, 2014

Unlocking Development

A CAGE Policy Report

'Unlocking Development' argues that the world's poor are 'trapped' in poverty and investigates how best to promote the rule of law in order to make economic growth more stable and sustainable; to enhance the capacity of the business organizations that are most likely to attract investment and create jobs; and to enable women to play a full part in economic development as citizens, providers, and entrepreneurs.



Social Market Foundation

11 Tufton Street
London SW1P 3QB

020 7222 7060
www.smf.co.uk