

THE POLITICAL ECONOMY OF GROWTH: INSTITUTIONS AND INCENTIVES FOR INVESTMENT



POLICY LESSONS FROM THE iiG PROGRAMME

Many of the most significant and durable barriers to economic growth – conflict, instability and poor economic governance – are the product of particular political economies in which leaders and ordinary people face incentives to focus on short-term personal gain and security rather than long-term investments in stability, national infrastructure, and sustainable development. Removing these barriers requires us to understand the way in which institutions and information shape the decisions made by individuals at all levels of the political game. This paper summarizes the contribution of Phase 1 of the iiG research programme on the political economy of growth in three specific dimensions: electoral accountability, conflict and instability, and public services.

KEY FINDINGS

- Societies that are small, low-income and resource-rich have little chance of holding free and fair elections, but this can be mitigated by a free press, strong institutional checks and balances and international pressure.
- Low quality elections increase the prospects for political unrest and ethnic violence, while reducing the incentives for governments to deliver good economic performance.
- Ethnic voting and violence often occurs because individuals who do not wish to act ethnically or irresponsibly feel compelled to do so because there is a lack of credible institutions to safeguard their interests.
- Violence intensifies mistrust between rival communities and undermines domestic accountability, investment in the local economy, and export performance.
- The provision of public goods can rapidly increase the willingness of individuals to pay taxation and the legitimacy of the government and encourages citizens to demand more responsive government.
- Decentralizing responsibility for development expenditure while increasing the information available to local residents can strengthen accountability mechanisms.

ELECTIONS AND ECONOMIC PERFORMANCE

Political leaders in new democracies frequently use dirty tricks such as electoral violence and bribery. Almost a third of the respondents we interviewed around the 2007 election in Kenya reported that politicians in their area had openly advocated some degree of violence in the previous year. Our research also found that political violence and bribery was widespread in Nigeria and São Tomé and Príncipe. Perhaps unsurprisingly, when it comes to elections cheats prosper. Incumbents that use dirty politics stay in power 2.5 times longer than those who don't. In turn, dirty politics, and the lack of electoral turnover, reduce trust in institutions and among people.

This process is well demonstrated by events in Kenya, where electoral violence erupted following disputed polls in late 2007. The instrumental use of violence by the government of Daniel arap Moi in the 1990s created a fear within most communities that they would be targeted this time around. Before the election, more than half of the Kenyans we interviewed expressed fear of political violence, while only 16 per cent of respondents stated that they were unconcerned about becoming a victim of violence or intimidation during the election. These fears encouraged groups to arm themselves prior to the polls, which in turn contributed to the rapid escalation of the violence once the official results had been announced. This vicious cycle keeps turning: those affected by electoral violence in 2007 now report that they are more willing to resort to violence to solve their problems, to ignore the law, and to disagree with the holding of elections as a way to elect leaders.

Violence and political instability has major economic consequences. The post-election violence in Kenya had a detrimental effect on regional economic growth and significantly undermined the performance of key sectors of the economy. In the wake of the violence, flower exports fell by nearly one quarter on average and by 40 per cent for firms located in conflict areas. Moreover, iiG research in Nigeria suggests that individuals in more insecure areas become more likely to save rather than to make business investments, dampening local entrepreneurialism. Thus, security and stability shapes the prospects for economic growth.

Cheating is also significant because it enables incumbents to cling on to power even when they are unpopular, and so helps to insulate poorly performing leaders from popular frustrations. This has a dramatic effect on the incentives facing leaders to successfully manage the economy. Cross-national research reveals that incumbents standing in clean elections are penalized if they do not deliver economic growth. Indeed, their time in office is about 40 per cent shorter compared to incumbents that achieve economic growth. But presidents standing in dirty elections face a much smaller penalty: economic stagnation shortens their time in office by only 23 per cent. They therefore face significantly less pressure to get the economy right.

The iiG research projects on elections and economic growth therefore demonstrate that elections in undemocratic contexts make civil unrest and low levels of economic growth more likely. So how can this bleak situation be avoided? Our research suggests two main solutions. Stronger democratic institutions can prevent dirty politics in the first place. Term-limits, a free press, an autonomous electoral

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commission, and constitutional checks and balances, are the most effective instruments to protect free and fair elections and must be put in place if electoral competition is to promote accountability. International pressure has an important role to play in this struggle. However, the provision of aid may be as much of a problem as it is a solution, because aid funds are often diverted to fund the campaigns of leaders employing dirty politics. Policy makers should therefore target their efforts towards improving the effectiveness of checks and balances before making aid freely available.

The provision of information is just as important as the strengthening of institutions. For accountability to take place, voters must have the necessary education and information to evaluate candidates critically. An experiment that provided anti-vote buying and anti-violence education to citizens in a selected number of areas during Nigeria's 2007 general election found that where the education was provided there was less violence, fewer votes for violent politicians, and higher voter turnout. More comprehensive voter education programmes are therefore likely to contribute to more peaceful polls.

ETHNIC VOTING AND ACCOUNTABILITY

Perceptions of past violence and cheating, along with a history of winner-takes-all politics, and deep inequality between different communities, increase the likelihood that individuals will vote 'ethnically'. Where ethnic voting is pronounced, citizens do not support a candidate because he has demonstrated the qualities needed to effectively manage the economy, but because they can be relied upon to look after a particular ethnic community. In the Kenyan context, the vast majority of Kikuyu, Embu and Meru votes supported one candidate, while most Luo and the Kalenjin voters sided with another. Although some Kenyans did vote on the basis of the previous performance of the incumbent, the salience of ethnicity made it less likely that individuals would vote on these grounds; leaders therefore faced fewer incentives to govern responsibly.

The impact of ethnic voting is illustrated by our survey data. While policy considerations were not an important factor in determining political support for Kenyans who self-identify in 'ethnic' terms, policy issues trump ethnic politics for Kenyans who identify in 'non-ethnic' terms (for example, by identifying themselves first and foremost by their profession). Among more civically minded Kenyans, the most important factor shaping vote choice is the performance of the president on the economy and on corruption.

This suggests that if we want to see elections in which presidents are evaluated on the basis of their policies, rather than their identities, we need to find ways to persuade people to opt-out of 'ethnic' identification. The critical question is therefore: what leads to a non-ethnic outlook? Our research reveals that a range of social factors are important. Kenyans whose parents came from different ethnic groups are more likely to report a 'Kenyan' identity than an 'ethnic' identity, while those Kenyans that no longer reside in the province in which they were born are more likely to identify themselves in non-ethnic terms. There is also evidence that individuals that work in certain professions that are associated with working away from home such as being an artisan in the formal sector, businessperson, or

teacher, are more likely to be 'non-ethnic'. The abandonment of ethnic identities and the emergence of policy voting should therefore be understood as twin products of geographical and economic mobility.

Policies that promote the integration of different communities are therefore likely to reduce the salience of ethnic identities over time. This is particularly significant in post-conflict countries, because ethnic violence is often followed by the balkanization of the country, with people of different ethnic groups returning to their 'home' areas. Our research suggests that this is only likely to increase the significance of ethnic identities and to undermine the prospects for policy based politics.

A second important factor influencing the willingness of people to leave behind old ethnic logics is the fear that others will continue to play by the old rules of the game - and that as a result, those who act 'non-ethnically' will be disadvantaged. When asked, Kenyans resist defining themselves in ethnic terms and do not say that they want their candidates to be of the same ethnicity. However, they also fear that other Kenyans do think and act 'ethnically'. Less than one in ten Kenyans expressed high levels of trust in people from other ethnic groups. And half of all respondents reported that the ethnicity of candidates was an important factor in determining the outcome of the 2007 polls. After decades of winner-takes-all politics, feelings of ethnic discrimination run deep: in Kenya, 64 per cent of the Luo community think that their group's economic conditions are worse than others as a result of government discrimination. But citizens that do not favour ethnic politics are therefore reluctant to cease voting ethnically because they believe that if others continue to do so they will be further discriminated against.

Overcoming such a profound lack of trust is not easy and may be dependent on long-term processes of social and economic change. But institutional reform can also help. Stronger political institutions that can be relied upon to deliver fair outcomes and prevent exploitation reduce the danger of acting 'non-ethnically' and so free citizens to act on the basis of other considerations.

PUBLIC SERVICES AND THE SOCIAL CONTRACT

In many countries in which politics has historically been characterized by neo-patrimonial or winner-takes-all politics, governments have rarely sought to provide services for all of their citizens. Rather, they have used their positions to reward their own support base, while excluding opposition supporters from access to resources. As a result, voters do not expect leaders to provide public goods and are reluctant to pay taxes because they do not believe that they will be spent productively, or in a way that will benefit them. But research on Nigeria demonstrates the potential for public goods provision to transform the relationship between voters and the government.

In the case of Lagos State, Governor Babatunde Fashola launched a reform agenda that involved asking citizens and businesses to pay more tax in return for improved public services and a better, cleaner, state. The popularity of these reforms – despite the fact that they significantly increased the tax burden – demonstrates that African leaders can build a cross-ethnic support base by providing public

goods. Most strikingly, the provision of basic public services dramatically increases the willingness of individuals living in recipient communities to pay higher levels of taxation. In other words, ordinary people can be persuaded to buy into the notion of the state remarkably quickly once effective and visible action is taken with regards to public services.

The provision of public services is therefore critical to the evolution of social contracts in which citizens invest in their states and subsequently seek to hold leaders accountable. The provision of effective public services not only benefits the very poor who cannot afford to pay for education and health care, it is also critical to generate public willingness to pay taxes and public support for future reform agendas. Extending new services can also help to boost government legitimacy among marginalized and disgruntled communities and can therefore help to reduce the risks of civil or political conflict. But public goods need to be visible – the more tangible and visible services are, the bigger the impact on public attitudes.

Decentralization is one way to render such changes more visible. It is no coincidence that in Nigeria the evolution of a social contract has occurred at the level of the State, rather than at the national level. In Kenya, control over local development expenditure was decentralized to the constituency level through the introduction of a Constituency Development Fund (CDF) in 2003, which is managed by a committee selected by the Member of Parliament. CDF funds are usually spent on projects of importance to local communities, such as the construction of schools, hospitals, clinics and other local services. iiG research carried out in Kenya found that how MPs were perceived to have performed on the CDF was one of the key factors that shaped whether or not individuals supported their re-election. By moving decision-making power over local development expenditure closer to voters, ordinary Kenyans were empowered to reward or punish their representatives for their performance.

But in line with the findings from Nigeria, the iiG project in Kenya also found that in order for decentralization efforts to have a positive impact on poverty and accountability, voters need to have, and to use, information about the quality of locally provided public goods in making their voting decisions in local elections. One of the virtues of the CDF was that some of the details of CDF activities are made publicly available via the internet and by their nature CDF projects are high profile and are therefore susceptible to monitoring by local communities. But the low quality of information made available to citizens means that their judgment about when an MP has performed well or badly with regards to CDF projects may not always be based on reliable data. Where this is the case, MPs have far less incentive to invest time and energy into improving their CDF schemes.

Similarly, research in India has demonstrated that properly designed public information campaigns can significantly increase knowledge and take-up of public health insurance and other health services among the poor. This is significant, because it helps to overcome problems of traditionally low uptake of welfare schemes by the poor. But for information to be effectively disseminated, individuals must be incentivized to get the message out. Campaigns are most effective if information providers are employed on the basis of performance related pay schemes – in other words, if state agents or

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civil society activists get more wages the higher the knowledge about the programme among the target population. Such awareness programmes are also more effective if the information provider comes from the same social group as the targeted villagers – in this way, strong communal identities may actually facilitate the provision of pro-poor services.

Taken together, iiG research has revealed the capacity for the provision of public services to improve the lives of the very poor and strengthen accountability mechanisms. But this only holds if systems are put in place to communicate the existence of services to the wider population and if sufficient information is available so that people know when services are not performing well - and can identify who is responsible.

IMPLICATIONS FOR POLICY: THE POLITICAL ECONOMY OF GROWTH

- Maintain international pressure for free and fair elections and be more critical of poor quality elections.
- Encourage governments to allow a free and vibrant media.
- Focus on building strong and autonomous institutions.
- Invest more in conflict detection and prevention.
- Empower poor governments to provide public goods.
- Provide further training and support to tax revenue authorities.
- Decentralize some development expenditure, but make sure to simultaneously promote open access to government information.

FOR MORE INFORMATION

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