
Improving Development Assistance in Light of New Institutional Economics

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July 1, 2004

Economics as the study of institutions

- NIE is about paying attention to the exchange relationships that emerge among people and the institutions within which those exchanges take place
 - Institutions are the set of rules which govern social intercourse in a particular context and the enforcement of those rules in that context
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Role of institutions

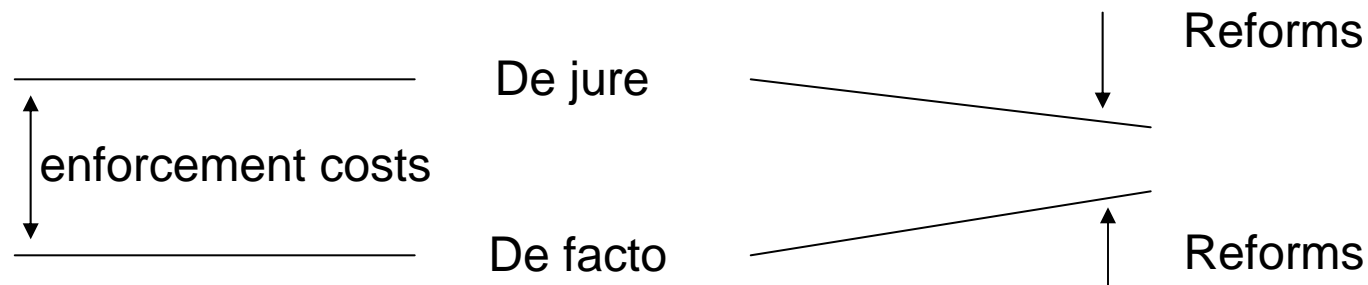
- Institutions provide the incentive structure that individuals face in their social intercourse
 - Three games in development economics:
 - Incentives that actors in developing world face
 - Incentives that the decision makers in both the donor and recipient nation face
 - Incentives that the actors within development agencies face in deciding on development priorities and ideas to utilize in pursuing those priorities
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De jure and de facto

- Distinction between the *de jure* (official) and *de facto* (unofficial) rules that constitute institutions
 - The closer the tie between the *de jure* and the *de facto* rules, the lower the enforcement costs
 - Vice-versa, the looser the tie, the higher the enforcement costs
 - Important to understand the nature of the tie between *de jure* and *de facto*
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Reform process

- Successful reform process will:
 - Strengthen the tie
 - lower the cost of operating within the de jure
 - raise the cost of operating outside it



Crucial issues of the reform process

- Conflicts between the *de jure* and *de facto* often revolve around rules of property:
 - Lead to alternative enforcement devices, and greater costs of realizing gains from exchange
 - Affects entrepreneurial activity
 - Entrepreneurial Environment:
 - “Betting on Ideas” and finding the finance to bring those “bets” to life
 - Need strong tie between *de jure* and *de facto*
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Crucial issues of the reform process

- Political economy mapping:
 - Understand political interests
 - Identify who could benefit and who could be made worse off by the reforms
 - Facilitate local ownership of the reforms
 - Align interests in order to build winning coalitions
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Getting ‘Dirty’ in Order to Address Institutions

- To understand the *de facto* rules which govern social and political intercourse
- One must get “dirty”: on-the-ground data gathering, historical reading, and familiarizing oneself with the culture and way of life of the people



- www.mercatus.org/pdf/materials/435.pdf