

16. From liberal economic policies to liberal political institutions? Democracy, development clusters and wellbeing

Tim Besley and Torsten Persson

The period since the Washington Consensus has seen a gradual, though sometimes stuttering, growth in liberal political institutions that support free speech, open contests for power, and constraints on the arbitrary use of power. Meanwhile, economists and other social scientists have studied the interplay of economics and politics along alternative paths of development – paths associated with more or less solid underpinnings for a market economy and more or less peaceful resolutions of domestic conflict. Our chapter explores whether this research supports a consensus around the kind of political institutions, values, and norms that can produce flourishing economies and societies.

By development I mean the movement upward of the entire social system, ... besides the so-called economic factors, ... the distribution of power in society; and more generally economic, social, and political stratification; broadly speaking, institutions and attitudes. The dynamics are determined by ... circular causation, ... if one [endogenous condition] changes, others will change in response, and those secondary changes in their turn cause new changes ...¹

(W)hen people look back at what happened in this century, they will find it difficult not to accord primacy to the emergence of democracy as the preeminently acceptable form of governance.²

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I. Introduction

When the Washington Consensus was formulated in 1989, a great deal was different in both the real and the academic worlds.³ The Consensus advocated a set of liberal economic policies to promote development, but was immediately criticised for not paying enough attention to the institutional foundations of a market economy. In the intervening years, research in the field of political economics has flourished and singled out political institutions – together with the norms and values that sustain them – as fundamental drivers of peace and prosperity. In this chapter, we try to assess whether that body of research, which tries to bring insights from political science into our understanding of economic issues, can support a new consensus that highlights the importance of liberal political institutions rather than liberal economic policies.

In the initial quote, from more than half a century ago, Gunnar Myrdal argues that paying greater attention to institutions and attitudes will foster a more nuanced view of development as a process of circular causation among multiple drivers of economic, social, and political change. Above all, Myrdal understood that economic analysis alone would not suffice to understand development processes and policies. Even if the architects of the Washington Consensus were right in their policy prescriptions, they had a blind spot regarding how these policy prescriptions could be introduced and sustained, given the political and institutional incentives faced by real-world policymakers. On a similar note, the architects paid scant attention to social and political dynamics, contributing to a commonly held critique of economics as a narrow and inward-looking discipline.

These oversights were somewhat paradoxical, as they came at the tail end of a major global debate about economic systems, which juxtaposed (mostly) democratic capitalism and (mostly) authoritarian communism. The ideological rift of the Cold War was thus both political and economic. Moreover, when the Consensus was formulated, the Berlin Wall was falling and China's economic model was seemingly changing. On top of this, the 1990s saw a 'third wave of democratisation' in many parts of the developing world. These events unleashed a new wave of globalisation and a new liberal economic order. In retrospect, it seems impossible to understand these global trends without appealing to the underlying institutional forces that helped reshape policies.

In parallel to these real-world events, academics came to emphasise how institutions could foster more inclusive forms of policymaking.⁴ More specifically, they recognised that state capacities are vital pre-conditions for effective intervention by the state.⁵ We also saw systematic efforts to go beyond formal institutions and incorporate values and norms into dynamic analyses of state effectiveness.⁶

In short, forces that shape politico-institutional change penetrated both the real world and academic thinking over the past few decades. An important question is whether we can use what has been learned to forge insights

into the making of an effective state. We will argue that modern research on the political economics of development provides a useful starting point. In particular, it may help us formulate a consensus around certain liberal principles for building effective states by exploring the institutional and social bases of cohesive policy formation.

II. Background

1. *Why politics is key*

Politics is central because it aggregates conflicting interests and, thereby, affects who gets what when the state exercises its power to tax, spend, and regulate. Generally speaking, the political-economics literature has developed a wide variety of models to study how power is acquired and used.⁷ To understand how political forces shape development, it is essential to study how they impact incentives to invest.⁸

Research in this tradition has stressed how sub-optimal government policies stem from dynamic political failures, most often due to a lack of policy commitment – for example, governments being unable to offer credible long-term investment-friendly policies.⁹ A case in point is the classical time-consistency problem in capital taxation: once it is in place, capital is easily taxed.¹⁰ However, classic redistributive motives in policymaking are also key to recognising how investment incentives are shaped, and to understanding how politics affects development.

2. *Which democratic institutions?*

Debates in political-economics are often framed around the consequences of different constellations of institutions, especially democratic institutions. But ‘democracy’ is an elastic concept, with multiple dimensions.

We and others have previously argued – from first principles – that it is essential to distinguish two distinct dimensions of democratic institutions.¹¹

The first is openness in access to power, particularly in executive recruitment: determining who holds office and whether their position is contestable. Hereditary monarchy lies at one end of the spectrum, and competitive elections at the other. We often refer to the latter end as democracy, as it vests power in the ‘people’ to choose who governs. Indeed, many equate democracy with a wide franchise in mass elections.

The second dimension of democracy concerns constraints on the exercise of power once it has been acquired. This puts the spotlight on the checks and balances that different political and state actors can impose on each other. At one extreme, leaders possess unconstrained powers; at the other, they are subject to strong checks by legislatures and/or independent judiciaries. This aspect of democracy stresses limits on absolute power even if that power is acquired in a (legitimate and competitive) election. Strong executive

constraints also make it more likely that rulers exercise their power in the wider public interest.¹²

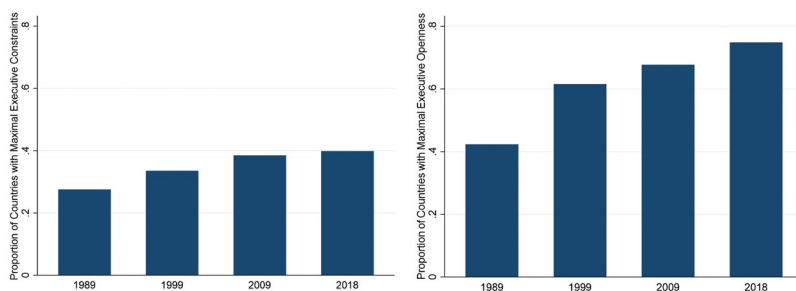
The idea is that openness in recruitment allows different groups to alternate in power – but without strong executive constraints, each group may simply govern in its own interest, which might damage the motives for investing in an efficient state and in physical and human capital. In such a situation, institutions could either impose restrictions on access to power, to induce more stability, or impose some constraints on executives, with the purpose of inducing less self-interested policies. Constraints on power also help preserve democratic institutions, by preventing rulers from watering down political rights as a means of staying in power.

3. Measures of democratic institutions

Well-established data bases, produced by different research consortia, can be used to classify political institutions along the two dimensions discussed. Here, we largely rely on the Polity-IV project, which scores the political institutions of all independent nations with more than half a million people, going back for more than two centuries. Over that period, getting the top Polity score for strong executive constraints has been a good deal rarer than getting the top score for open executive recruitment.¹³ Effective constraints on power may require a stronger political culture, which accepts and enforces such constraints when those in power try to undermine them. Misusing political office in this way may also be less visible to citizens than cancelling or undermining an election.¹⁴

Figure 16.1 offers a birds-eye view of how the two dimensions of democratic institutions have trended since 1989 – the publication year of the Washington Consensus. Over these three decades, the fraction of countries with open executive recruitment and the fraction with strong executive constraints have both increased, reflecting a general trend towards democratisation. But – as in the historical backdrop mentioned – strong executive constraints are clearly lagging behind.

Figure 16.1: Executive constraints and openness over time



Source: authors' calculations based on The Polity Project data (<https://www.systemicpeace.org/polityproject.html>).¹⁵

4. *Development clusters*

We now turn to our central question: how can one build an effective state, all things considered? In the spirit of Myrdal's multidimensional approach, we seek answers guided by theoretical arguments and empirical evidence. However, these will not invoke a single driver but a range of common attributes that underpin clusters of states. We begin by investigating prospective drivers of success or failure in promoting peace, prosperity, and wellbeing. We then show that the data support three distinct 'development clusters', which – in line with the theoretical framework – we label as common-interest, special-interest, and weak states.

5. *Building blocks*

Following on from our previous research, we argue that development clusters are likely to form across two dimensions: the extent of political violence and the build-up of state capacities.¹⁶ These ideas are anchored in two strands of social science research on the history of states, which we trace back to the work of political sociologists Max Weber and Charles Tilly.

6. *The Weber doctrine*

To be effective, a state must limit violence to its own legitimate use of force. This idea goes back, at least, to early social-contract theory, such as Thomas Hobbes's *Leviathan*, but was articulated in a more modern context by Weber.¹⁷ It is now widely accepted that an effective state has a monopoly of coercion in its own territory. Such a monopoly rules out coercion by non-state actors, as in civil wars or in situations where militias contest parts of a territory.

Civil wars where control of the state is at stake remain a common phenomenon.¹⁸ The frequency of such wars increased in the post-World War II period peaked in the 1980s and 1990s, and steadily declined thereafter. The annual prevalence of civil war has now levelled out at around 10% of countries.¹⁹ Of the 172 countries for which both conflict and income data are available, 39 had a violent conflict between 1989 and 2016, of which 24 are classified as low income, 13 as middle income, and only 2 as high income.²⁰ That is, we see a clear pattern when it comes to civil war and level of economic development.

Mainstream research began to emphasise political violence and peace – as a cause as well as a consequence of development – only after the formulation of the Washington Consensus.²¹ But, nowadays, debates about the causes and consequences of internal conflicts underpin a vast body of research in both economics and political science. This work stresses that low income can be both a cause and consequence of conflict. It also studies the role of political institutions, especially legislative and judicial constraints on executive powers. These institutions constrain incumbent behaviours that may provoke conflict, such as encroachments on minority rights. In line with this

observation, Polity IV's measure of strong executive constraints shows that 27 of the 39 countries with a civil war between 1989 and 2016 did not have a single instance of strong executive constraints over that period.

However, focusing on civil war is only a partial approach, as not being in civil war does not necessarily imply a society where political violence is absent. States that stave off outright conflict by repressing their populations – for example, by locking up opposition groups and coercively stamping out protests – still engage in violence, although the violence is closer to being 'one-sided' than 'two-sided'.²²

Throughout human history, coercion and repression have been more common tools for sustaining political power than winning elections. These tools remain prevalent today; even in the third wave of democracy since 1989, 79 countries have sometimes been ruled by regimes classified as repressive. Although the share of countries engaging in repression fell from 30–40% in the 1950s to near zero by the late 1990s/early 2000s, repression has increased since 2006, with close to 10% of states carrying out political purges, including Brazil, the Philippines, Russia, Thailand, Turkey, and Venezuela.²³

7. Peace as a condition for an effective state

Establishing peace is an essential part of establishing social order, which plays an important role in building an effective state. Beyond its direct importance, limiting the use of political violence often improves incentives to invest in physical and human capital. Conversely, civil conflict may hurt incomes through lower earnings, deterred investments, or widespread disruption of vital infrastructures.

Endemic repression may certainly increase political stability – China and the Middle-East monarchies are examples of repressive versions of peace. But unchecked power is also a source of risk that may prevent development. Absence of the rule of law can raise fears of expropriation and deter investment. Repressive regimes often foster corruption, as personal relationships substitute for open access to economic opportunities. This can restrict welfare-enhancing entrepreneurial entry, or entrench welfare-reducing monopolies. Meanwhile, if educational opportunities expand, an aspirational middle class that demands political rights may also pose risks to autocrats. Thus, even stable autocracies face a difficult balancing act, which can result in crackdowns on freedoms with negative economic consequences. When is a state more likely to realise a peaceful and legitimate monopoly on violence? We delineate three conditions.

The first is limited opportunities for using the state to promote the interests of a ruling elite. When state power faces few constraints, it is attractive to capture the state or retain control of the spoils of office. By contrast, when rulers are constrained by courts and parliaments, this reduces the incentives to use violence to acquire or maintain power at all cost. So, executive constraints are key.

The second condition is cross-cutting economic, political, and social cleavages in society. Researchers have stressed how the incentives for conflict, rather than cooperation, go up when groups defined by income, classes, ethnicities, or religions coincide and reinforce each other.²⁴ In such cases, groups that are competing to be in power are more sharply delineated, so using violence to capture the state is more attractive. On the other hand, when political cleavages are cross-cutting, they foster incentives to build alternative broad-based coalitions for cooperation. Such latent coalitions with common interests across groups may weaken the motives for each group to invest in violence to acquire political power. So, cross-cutting cleavages are key.

A third, related, condition is a developing economy that helps pacify the polity. If many citizens perceive strong gains from economic cooperation, this can help underpin a peaceful society, which feeds back to prosperity through stronger investment incentives. This idea – that economic relations provide a civilising force – is often labelled the ‘doux commerce hypothesis’.²⁵ Thus, peaceful political settlements can be reinforced by an economic peace dividend.

8. *The Tilly doctrine*

The term ‘state capacity’ has its roots in historical sociology and was popularised by Charles Tilly, who principally used it to describe the power to tax.²⁶ Nowadays, state capacity is used to describe the general infrastructure that allows a state to deliver a wider range of policies – and to do so at a low cost. The concept of state capacity allows a degree of consensus around public intervention, by cutting through ideologically loaded debates about the size of the state. Thus it appeals to proponents of government intervention, who see building state capacity as a road to wider intervention – say, a greater array of industrial strategies. But the term also appeals to sceptics of state intervention, who see building state capacity as a road to narrower intervention – emphasising more effective regulation but on a smaller scale.²⁷

In a previous paper, we described three key state capacities.²⁸ *Fiscal capacity* refers to the power to tax, which requires investing in systems for compliance with broad-based income taxes and collection of social-security contributions. High fiscal capacity allows the state to raise more tax revenues at lower cost. *Legal capacity* refers to the power to implement laws and regulations, which requires investments in legal institutions, courts, and regulatory bodies to protect property rights and enforce contracts that encourage trade and investment. *Collective capacity* refers to the power to deliver a range of public services, which requires investing in organisational structures to provide infrastructure, and investing in services like health and education.

State capacities can thus be thought of as different forms of public capital – not just physical structures, but digital structures. Such capacities are the bedrock for state intervention: spending money will rarely achieve positive results without the ability to identify and deliver public projects. Moreover,

they are inherently dynamic: states can shift the dial by enhancing capacities in times of need – in order to, say, administer vaccinations in a pandemic, or raise new taxes in a war.

We now argue that the very same forces that help constrain investments in political violence help stimulate investments in state capacity. The incentive to invest in a capable state is strongest when current and future rulers use the state to further common interests. For example, the incentive to invest in a broad-based tax system is greater if the proceeds largely finance universal programmes, and such programmes are most effective when backed by organisations that help raise the returns on public spending. A state intent on raising tax revenues will also have stronger motives to build legal capacity to promote a market economy.

Such motives are sustained by political institutions that constrain rulers from spending on narrowly defined group interests. Furthermore, a sense of common purpose – such as defending a country against a common enemy – will help sustain the working of such institutions. As Tilly argues, external warfare has been a key force in building tax capacity throughout history.²⁹ Similarly, many states reviewed their public-health systems following the pandemic.

Building legal capacity to make the market system work better will provide a boost to productivity and thus stimulate economic development. Indeed, the state can be a source of endogenous growth. With collective capacity, the fruits of growth can also be shared more broadly. This may create a powerful constituency for the development of the state which, in turn, may support the maintenance of peaceful domestic relations.

9. Three kinds of states – development clusters

The motives to create different forms of state capacity are complementary, in the sense that they reinforce each other. Moreover, many drivers of investment in state capacities are helpful in creating a peaceful state. In this way, state capacities and peace tend to become symbiotic, which fits nicely with Myrdal's notion of circular causation. In previous publications, we have stressed precisely how, in theory, economic, political, and social outcomes mutually reinforce each other.³⁰ When operating for a period of time, a process of mutual reinforcement can create three archetypical state structures.

Common-interest states

As the name suggests, taxes raised by such states are largely spent for the common good. Political institutions largely constrain the power of political elites and weaken the motives to use political violence, making common-interest states largely peaceful. Institutions also encourage investments in state capacities. Common-interest states thus tend to have effective systems of revenue collection with broad-based taxation to fund collective provision of universal programmes for health, education, and retirement. They also

have legal and regulatory systems, which lay the foundations for a strong market economy.

Special-interest states

Special-interest states are run to favour political elites that become de facto ruling groups, such as dynasties in stable monarchies, or oligarchic party elites in single-party states. Ruling elites are only weakly constrained by institutions, and often resort to repression to maintain a hold on power. Taxes may be used extractively, and public spending may be used to head off political opposition. Being entrenched in power does, however, allow elites to take a long-term view that can spur them to build certain state capacities. Moreover, elites can benefit from economic development if it does not threaten their hold on power – though the latter constraint may hold back the emergence of an educated middle class. Greater control over the economy, limiting competition, often makes sense to the ruling elite.

Weak states

Weak states are prone to internal conflicts and have limited state capacities. In contrast to special-interest states, no group has found a way to maintain a long-term hold on power. Moreover, such states tend to have weak constraints on the exercise of power, which makes it attractive to use the state to serve the short-term interest of the ruling group at any point in time. This rarely means investing in state effectiveness, as the benefits of such investments are likely to be reaped by future governments. As state capacities are low and conflict is endemic, incentives for private investment are limited, and in the worst cases this may result in a vicious cycle of poverty and conflict.

10. *Taking stock*

Given the complexity of today's world, it is a crude simplification to classify countries into three stylised types. Moreover, even within this, there is heterogeneity within types, not least among special-interest states and weak states. Indeed, some countries – Syria being but one example – have cycled between periods of repressive autocracy and conflict. We have previously described this heterogeneity as the 'Anna-Karenina principle', riffing on the opening lines of Leo Tolstoy's eponymous novel:

'Happy countries are happy in the same way. But unhappy countries are unhappy in different ways'.³¹

Above all, the principle stresses that – as in other syndromes with multiple and interdependent causes – there are no simple remedies.³² Nonetheless, below we try to draw some practical lessons based on the patterns we observe in the data.

While our three-way classification of states draws on a specific analytical frame, it has much in common with a large body of research in political economics that examines the underpinnings of economic success. Thus, our classification parallels the celebrated work of Daron Acemoglu and James A. Robinson, who juxtaposed extractive and inclusive institutions in their analysis of why nations succeed or fail.³³ Their work, in turn, drew on established ideas about institutions as a fundamental cause of development, as stressed in the work by Douglass North.³⁴ Indeed, strong statements about the overall importance of institutions are now widespread in economics.³⁵

Understanding the forces behind political violence also chimes with a great deal of research in economics and political science. Researchers have argued persuasively that limits on violence play a central role in effective states, and that the challenge is to build societies with 'open access orders', where transitions to power are competitive in both political and economic terms.³⁶ In political science, researchers have stressed how survival motives for holding onto power matter crucially for how the state is used.³⁷ Meanwhile, others emphasise that political violence can also be important in high-capacity countries, where governing factions deliberately weaken and collude with non-state violent actors to maintain power.³⁸

The ideas that we have discussed also create a bridge to the extensive research on state failure. The work of Robert Bates is a key reference for problems when it comes to building effective states in Africa.³⁹ Indeed, it is common to use the term 'state fragility' to describe the challenges of development in the poorest parts of the world.⁴⁰ In their practical work, many international organisations and donors look for distinctive ways of engaging with weak and fragile states.

Our notion of building collective capacity is in tune with an extensive literature in recent years on what does and does not work in reducing poverty. Much of this research is associated with the use of randomised controlled trials (RCTs) in development.⁴¹ Increasingly, such field experiments focus on alternative institutions and their consequences, with the aim of learning how government performance can be improved and how complementary investments in state capacities can further enhance this performance.⁴²

Many of the conceptual ideas we have discussed have been around for a while. But the acknowledgement of their central importance has grown since the Washington Consensus was formulated. Any attempt to forge a consensus around the preconditions for development must thus take into account the lessons we have learned about institutional conditions that may simultaneously contain political violence and create more effective states.

III. Evidence

In this subsection, we gauge how the dimensions of state effectiveness suggested by our theoretical discussion match up with the empirical evidence. Thus, we searched for development clusters in the data, based on a statistical classification that draws on some of the key concepts that we have discussed so far, namely state capacities, peacefulness, and income. We compute the resulting classifications in a sample of 64 countries for which we have reliable data for long enough a time period.

1. *Measurement*

Measuring state capacities is not straightforward.⁴³ To capture the main ideas, we use three crude measures, one for each aspect of state capacity. For fiscal capacity, we record the share of total taxes that was raised in the form of income taxes in 2016, using data from the International Centre for Taxation and Development Government Revenue Dataset. The idea is that, compared to, say, border taxes, income taxes require much more extensive bureaucratic infrastructures to be collected. For legal capacity, we collect the 2016 value of the World Bank's contract enforcement index from the Doing Business Project. This is just one, but a key, aspect of supporting market activity by judicial structures. Finally, for collective capacity we construct a basic index that takes the average of educational attainment, from Roberto Barro and Jong Wha Lee's dataset, and life expectancy, from the World Development Indicators.⁴⁴

These three indicators are positively correlated with each other and co-determined with income, rather than causally related to it. The correlation reflects the various feedback loops from economic development to state capacity stressed in our theoretical discussion. One example is when growing formal employment, facilitated by higher legal capacity, enables a state to collect more taxes and firms to produce at a greater scale.

In addition to state capacity measures, we gauge the share of years from 1975 to 2016 that a country was in civil war, according to the UCDP/PRIO Armed Conflict dataset.⁴⁵ We also record the share of years when the country was not in civil war but engaged in acts of repression, according to the data on political purges from the Banks Cross-National Time-Series dataset. Finally, we measure income per capita at real international prices in 2016, as defined in the Maddison Project Database.⁴⁶

2. *Real-world development clusters*

We now look for clusters of these six indicators in the data. Specifically, we let a machine-learning algorithm classify countries into distinct groups.⁴⁷

In a first step, the algorithm identifies two dimensions of heterogeneity. Dimension 1 broadly captures differences in state capacity and income, with positive numbers indicating high values and negative numbers low values.

Dimension 2 captures political violence, with positive numbers indicating frequent civil wars, negative numbers frequent acts of repression, and numbers around zero the absence of both violence types.⁴⁸

In a second step, the algorithm picks out distinct clusters of countries. These are illustrated in Figure 16.2, which plots each country's Dimension-1 value on the x-axis and its Dimension-2 value on the y-axis. We also shade the area behind the countries that belong to each cluster.

Figure 16.2: Three clusters of states



Source: authors' calculations based on the Pillars of Prosperity database (Besley and Persson, 2021).⁴⁹

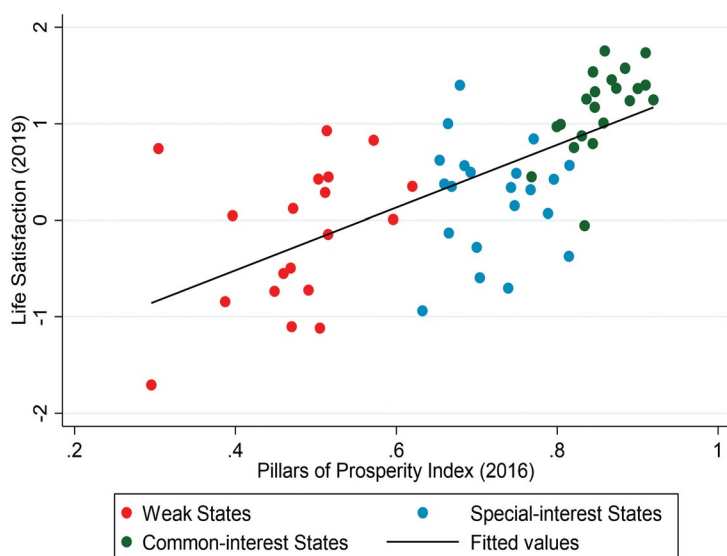
This procedure picks out three groups of countries, which turn out to quite neatly match the three groups predicted by our conceptual approach to state effectiveness. Weak states in the figure are shaded in red and located at negative values in state capacity/income Dimension 1 and positive values in conflict Dimension 2. This echoes the idea that weak states have high levels of civil war and low levels of state capacity and income. Special-interest states are shaded in blue and have middling levels of state capacity and income. Moreover, many have high repression levels (negative y-axis values), China being a notable outlier with its long history of political repression. Finally, common-interest states are shaded in green and form a particularly tight cluster, scoring positively on state capacity/income and around zero on political violence.

Of course, the data is noisy and the boundaries between clusters sensitive to different measures and time periods. But the tight cluster of common-interest states is still remarkable. Arguably, the goal of development efforts is to elevate countries to this cluster, a goal often cheekily referred to as ‘making everyone like Denmark’. In retrospect, one way to interpret the Washington Consensus is thus as a recipe to move all countries into the common-interest state cluster. But it would be hard to argue that the recipe has worked.

3. Subjective wellbeing and development clusters

This discussion – and our analysis more generally – entails a ranking of states, with common-interest states at the top. While this is an explicit normative judgement, there are good reasons to expect higher levels of wellbeing in states where political violence is largely absent and state capacities are generally high. To explore this assertion, we use a common empirical measure of wellbeing. In the Cantril ladder of the Gallup World Poll, a representative sample of individuals in each country is asked to subjectively score their own lives from 0 to 10, where 0 is the worst and 10 the best. Figure 16.3 plots average country-level scores, holding constant the individual characteristics known to shape individual wellbeing, such as age, income, gender, health, employment, and marital status.

Figure 16.3: States and wellbeing



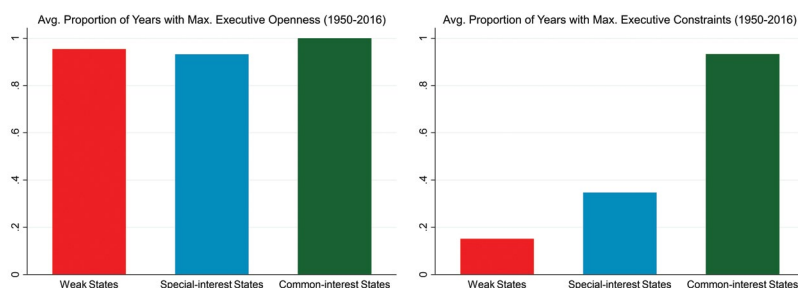
Source: authors' calculations based on the Pillars of Prosperity database (Besley and Persson, 2021) and life satisfaction data from the Gallup World Poll (Gallup, 2019).⁵⁰

The figure relates the national wellbeing scores to an index of state effectiveness, peace, and income, which we constructed and updated several years ago.⁵¹ In Figure 16.3, each dot colours each country according to its cluster in Figure 16.2: red for weak states, blue for special-interest states, and green for common-interest states. The figure shows a tight partial correlation between average subjective wellbeing levels and development clusters, which lends further support to the idea that a set of interrelated country-level factors are an emblem of state effectiveness.⁵²

4. Institutions and development clusters

As a final exploration, it is interesting to consider how development clusters relate to the two measures of democratic political institutions stressed in section II, open executive recruitment and strong executive constraints. Figure 16.4 plots the average Polity IV scores for these two institutional measures against the three state clusters displayed in Figure 16.2.⁵³

Figure 16.4: State types, executive constraints and openness



Source: authors' calculations based on the Pillars of Prosperity database (Besley and Persson, 2021) and The Polity Project data (Centre for Systemic Peace, 2021).⁵⁴

The left panel shows that openness does not correlate with development clusters. A more open process of executive recruitment is thus no guarantee for peace or for high state capacity. However, as we stress in the next section, political freedom is not just a means to an end, but also has an intrinsic value. A way to interpret the null relation in the left panel is that incentives to invest in political violence or in state capacities do not reflect how power is acquired, but rather how it is used. This interpretation is consistent with the right panel, which displays a strong relation between state development clusters and the strength of executive constraints.

Of course, Figure 16.4 does not reflect a simple causal chain. Moreover, each country will have to carve out its own development path. But the correlation still gives a useful backdrop to debates about state effectiveness and peace as preconditions for development.

IV. A liberal political consensus?

We now consider how an approach rooted in political economics may frame a consensus around how to support peace, prosperity, and wellbeing. In the spirit of Myrdal, this approach recognises the dynamics of circular causation. We acknowledge that the task of framing such a consensus could easily be seen as foolhardy, given the abundance of political philosophies and the heterogeneity in existing forms of government, some of which appear extremely stable. That said, [Figure 16.1](#) illustrates that the last 30 years have seen enough institutional change to reject the idea that political institutions are set in stone. We also see value in offering a reasoned defence of certain core principles, that are informed by a logical framework and by patterns in the data.

Our approach draws on a broad ‘liberal’ line of thought that goes back to the enlightenment. It is grounded in a political and social philosophy that emphasises individual rights, civil liberties, and democratic institutions, along with open access to markets that facilitate free enterprise. While these features can be derived from philosophical principles alone, we believe that the evidence also supports the case for a liberal political consensus.

We express our case with three propositions.

1. *Proposition 1 – Intrinsic values*

A liberal society based on principles of basic economic, political, and civil rights has intrinsic value.

The key here is direct ‘intrinsic value’ – as opposed to indirect instrumental benefits like higher incomes. To us, a liberal polity – where it is right for all citizens to exercise control over government, but wrong for a single elite to dominate others – is a valuable arrangement regardless of its consequences. With a few exceptions, this argument is unusual among economists, most of whom have argued for political liberalism based on its consequences.⁵⁵ However, a polity can raise the wellbeing of its citizens and contribute to human flourishing beyond the consumption of material goods. Societies that repress certain freedoms in pursuit of material gains cannot be given the same status as those that both pursue material gains *and* preserve freedoms.

Political equality as a value underpins the idea of a liberal political order where freedom of association and expression, and equality before the law, are central.⁵⁶ As many societies do not adhere to such values, actors who support them should try to work out how the intrinsic value of liberal societies affects evaluations of specific policies. This is a largely unresolved challenge for many international organisations. But the European Bank of Reconstruction and Development (EBRD)⁵⁷ set a precedent for making public such intrinsic values. As stated in Article 1 in the Incorporation of the EBRD:

In contributing to progress and reconstruction, the purpose of the Bank shall be to foster transition towards open market-oriented

economies and to promote private and entrepreneurial initiative in the Central and Eastern European Countries committed to and applying principles of multiparty democracy, pluralism and market economics.

The term 'pluralism' is certainly open to interpretation, even though a standard definition would refer to a setting where people of different beliefs, backgrounds, and lifestyles can co-exist in the same society and participate equally in the political process. Of course, this article is a legacy of the particular circumstances after the fall of the Berlin Wall, but it remains to this day. The EBRD's founders were committed to supporting the transition from communism towards more liberal political ideals. Taken seriously, the article means that policy approaches, project support, and engagement should also promote liberal values where possible.

Whether individual donors and international organisations can and should promote liberal values certainly raises hard choices. Colonial history makes it problematic to externally impose institutions and values. On the one hand, championing certain causes at home and forgetting the same causes abroad can appear hypocritical. But on the other, failing to defend liberal values abroad could end up eroding support for them at home.

2. Proposition 2 – Instrumental benefits

Used with caution, the large evidence base on the economic outcomes associated with alternative institutional arrangements does allow us to draw conclusions about their merits.

Compared to the time when the Washington Consensus was formulated, the research about how and why political institutions might matter is now vast. Moreover, this research is being extended from macro to micro evidence, based on RCTs and investigations of sub-national differences, and draws lessons from both historical experiences and contemporary outcomes.⁵⁸

An active strand of work has explored how democratic governance is related to growth. Making the instrumental case for democracy has had mixed success, although some researchers have claimed to find persuasive causal evidence.⁵⁹ Though it is always challenging to establish causality in the ebb and flow of institutional histories, such analyses are still useful to discuss the instrumental value of different political institutions.

However, for a nuanced discussion it is vital to go beyond one-dimensional measures of success, such as economic growth rates or levels of income per capita, as well as one-dimensional measures of political institutions, such as democracy. Even for standard economic measures, a quick look at the data reveals heterogeneous performance within simple categories. For example, in data since 1989, the average annual growth rate in democracies stands at 2.3%, compared to 2.5% in autocracies.⁶⁰ But the standard deviation of growth is very different: 4.7% in democracies versus 8.9% in autocracies.

This reminds us about issues around different forms of democracy: presidential versus parliamentary forms of government, or majoritarian versus proportional electoral systems.⁶¹ ‘Democracy’ as a common label ignores such differences. Similarly, autocracies display great variation – for example, whether a well-defined ‘selectorate’ can hold a despotic executive to account and/or regulate succession.⁶²

Used judiciously, the accumulated evidence on performance across different institutions can contribute to the debate about the value of liberal political institutions. There are indeed empirical regularities in the data.⁶³ This evidence base has been used to underpin discussions of why nations succeed and fail.⁶⁴ It can also be used as an empirically-based argument in favour of liberal political institutions. This argument, about instrumental benefits, reinforces that of Proposition 1, which was about intrinsic values.

3. Proposition 3 – Practical policymaking

When designing practical policy and development assistance, actors should focus on increasing cohesion in public action to support the building and maintenance of an effective state.

This proposition effectively argues that we ought to discount the common idea that access to finance is the main constraint on development. While public and private capital may be scarce in developing countries, it is even more important to find better ways of deploying any existing resources. In our view, ‘building effective states’ has three related elements.

First, the notion of a ‘state’ refers to a nation state. For practical purposes, centrally determined policies remain vital to the wellbeing of most countries’ inhabitants. Moreover, while support from external actors certainly can make a difference, we see no credible alternative to nations building cohesive states on their own. Only common-interest states can systematically fulfil the needs of their citizens and secure peace within their borders, without one group dominating over others.

Second, the notion of an ‘effective’ state entails expanding fiscal, legal, and collective state capacities. It also means encouraging a market economy. A state incapable of enforcing property rights will discourage private investment, as will a state without the capacity to deploy public capital to areas with high collective benefits. Such states will have limited impact on development.

Unfortunately, there is no silver bullet. Many states inherited systems of bureaucratic selection and control from a colonial past, a heritage that cannot be ignored when deciding how to build cohesive states. Using external actors, even those with local roots, thus creates accountability challenges. More generally, how far non-state actors can contribute to state building is an open issue. Many RCTs rely on collaborations with non-governmental organisations (NGOs), to avoid working with dysfunctional governments. NGOs may thus draw scarce skilled workers away from state employment or generally avoid systems of state accountability and responsiveness. Because of this, temporary

responses to immediate needs by non-state actors may yield immediate collective benefits, but also compromise long-term strategies needed to build effective states. The co-generation of knowledge by researchers working together with governments in evaluating public policies therefore holds more promise for strengthening long-term public service delivery.⁶⁵

Another way that RCTs can help is to shed light on the drivers of state capacity in weakly institutionalised environments.⁶⁶ This is consistent with approaches to investigate sources of trust and legitimacy in state action that have been pursued by political scientists. One idea is to link tax payments to tangible benefits from state action.⁶⁷ The World Bank and other organisations now pay far greater attention to governance issues and building state effectiveness.⁶⁸

Third, 'building' effective states entails more than just getting institutions right. That idea that norms play a key role in shaping social action is key within the social sciences – and one that is gaining acceptance in economics. A related idea is that prosocial behaviour reflects social values, as well as reactions to the behaviour of others. Formal institutions and rules can create strong incentives, but how people act under these institutions also depends on culture and norms.⁶⁹ Social context can thus shape how well people comply with formal rules, whether these rules prescribe that people pay their taxes or abstain from expropriation. While it is not always possible to 'engineer' values, one should be aware of the importance of intrinsic motivation and ways of incorporating it in public organisations.⁷⁰

Furthermore, over the longer term, formal institutions and values may interact as they evolve. In particular, institutions and culture may be complementary and thus reinforce good or bad societal outcomes by gradually strengthening each other. This idea has recently been applied to show how the interplay between democratic electoral institutions and democratic values can help explain the long-run stability of democratic and autocratic societies.⁷¹ Likewise, the interplay between executive constraints and the weight the prevailing culture puts on others in society can help explain the long-run stability of non-corrupt and corrupt societies.⁷²

To put this last point differently: cohesive states are embedded in cohesive societies. In practical terms, policy interactions should be viewed as 'teachable moments', with externalities tied to the norms and values of participants. Policymakers should only attempt to implement new policies – or put in place new institutions – that will succeed under realistic assumptions about these norms and values. This can lead to reinforcement learning that builds further prosocial incentives. How to enforce stronger standards to limit corruption, how to increase transparency about the allocation of public resources, and how to administer sanctions all have to be part of concrete policy discussions.

V. Final comments

Development is increasingly studied with a blend of economic, political, and social considerations. In this chapter, we have tried to articulate a political–economics consensus about the roots of societal success. We have stressed that a liberal polity may enjoy an advantage in securing peace and prosperity. We have also stressed multiple outcomes, as well as multiple drivers of these outcomes. Thus, we have discussed how economic success is built on political and social foundations, a discussion which is quite different from the largely technocratic agenda that motivated the Washington Consensus. Hence our stress on a liberal *political* consensus, rather than a liberal *economic* consensus.

But we have also cautioned against an uncritical mantra of ‘getting institutions right’. Bringing cohesion to the use of state resources may be done in several ways, and which one will work the best likely reflects a country’s heritage, traditions, and history. Put differently, the norms and values that influence policymaking transcend formal institutional rules. A strong civic culture not only helps institutions work for the common good but also makes the institutions more robust in the face of efforts to undermine them. Liberal-governance norms and values are sometimes violated and ultimately citizens must be prepared to stand up and defend democracy against such violations. This, in turn, helps to build strong democratic values.⁷³

Labels like democracy and liberalism may be blunt. However, liberal societies and democracies broadly go hand in hand, with one tradition that sees democracy as a universal value and another that sees liberal political institutions as a means to consensual policymaking. When liberal democratic institutions and values combine with greater cohesion in the population, this creates incentives for political leaders to build a strong state and abstain from violent resolution of conflict. This, in turn, makes it more attractive for private actors to invest in the future, which boosts economic outcomes. In such situations, we are more likely to see cohesive societies – common-interest states, as we call them – and the benefits they bring: high incomes, peace, and a rich menu of government services. A range of common-interest states with these characteristics have indeed emerged over the past two centuries.

So, the crucial question becomes how liberal political values and institutions can be built. Given the complex issues, no manual is available. Where and when critical junctures arise to strengthen institutions, these should certainly be taken.⁷⁴ Outright external interventions – like the Marshall Plan or membership demands from the European Union – may have been important to help sustain democracy in fragile contexts. External influence – as seen in Japan, South Korea, and Taiwan – may also have helped nurture self-sustaining democratic societies in the wake of existential threats. We have seen how the creators of the EBRD statutes were able to include a political mandate, alongside an economic one, at the critical moment after the fall of communism.

We are not formulating a utopian vision. For all their imperfections and limitations, some common-interest states have been created and sustained. They reflect arguments by political philosophers who identified the freedoms of association, expression, and participation as building blocks for better government. Historically, emerging democracies denied political rights to women, but over time this imperfection has largely been resolved within the system through a process of changing values and legal-cum-political change. Thus, we should think about common-interest states as evolving systems that respond to ongoing shocks and challenges. But their resilience should never be taken for granted, and it remains to be seen how robust they will be in the face of attacks on liberal values by left- and right-wing populist groups.

In conclusion, we return to our two opening quotes, on development as a process of circular causation and on democracy as a universal value.⁷⁵ The two visions agree on putting societal values at the heart of the political economics of change. Indeed, when we consider humanity's greatest challenges – climate change, conflict, poverty, and state fragility – it is hard to see solutions that do not involve changing values.⁷⁶ To analyse such issues, we need to combine institutional, cultural, and economic dynamics. Although some building blocks are already in place, this remains a huge challenge, not just for economics but social science more generally.

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Notes

¹ Myrdal (1974).

² Sen (1999).

³ Williamson (1990).

⁴ Acemoglu and Robinson (2012); Bates (2009); North et al. (2009).

⁵ Besley and Persson (2009); Besley and Persson (2011); Levi (1989); Tilly (1990).

⁶ Persson and Tabellini (2009); Acemoglu and Robinson (2019).

⁷ Persson and Tabellini (2000).

⁸ Alesina and Rodrik (1994); Persson and Tabellini (1994).

⁹ Acemoglu (2003); Besley and Coate (1998).

- ¹⁰ Kydland and Prescott (1977); Fischer (1980).
- ¹¹ Besley and Persson (2011); Mukand and Rodrik (2020).
- ¹² Besley and Persson (2011).
- ¹³ This is not unique to data from the Polity Project (Center for Systemic Peace, 2021), but also true for data from the V-Dem project (V-Dem, 2025).
- ¹⁴ Fearon (2011).
- ¹⁵ Center for Systemic Peace (2021).
- ¹⁶ Besley and Persson (2011).
- ¹⁷ Weber (1919).
- ¹⁸ There are large literatures on the determinants of civil war in both economics and political science, see Blattman and Miguel (2009) and Walter (2004).
- ¹⁹ See Figure 9 in Besley et al. (2021).
- ²⁰ The latter two (according to the UCDP/PRIO data) are Israel and the US. UCDP/PRIO (2023).
- ²¹ Key early contributions include Collier (1999) and Fearon and Laitin (2003). Blattman and Miguel (2009) review the early literature.
- ²² For background discussion see, for example, Davenport (2007).
- ²³ See Figure 9 in Besley et al. (2021).
- ²⁴ Lipset and Rokkan (1967).
- ²⁵ Hirschman (1982).
- ²⁶ Common references are Tilly (1985), Tilly (1990). We are unsure when the term 'state capacity' became common currency, but Google Ngrams suggests that its usage took off in the English language in the 1980s. However, in the 1950s the term was used in various US government documents in a way that is consistent with Tilly's definition. Mann (1984) also talks about the capacity of the state but in a wider sense than the power to tax.
- ²⁷ See, for example, Niskanen Center (2023).
- ²⁸ Besley and Persson (2014).
- ²⁹ Tilly (1985); Tilly (1990).
- ³⁰ Besley and Persson (2011).
- ³¹ Besley and Persson (2011).

- ³² Of course, there are differences within states that we classify as common interest. Moreover, many common-interest states face significant challenges, like polarisation and the rise of divisive forms of identity politics, which may lead to a deterioration of norms and institutions.
- ³³ Acemoglu and Robinson (2012).
- ³⁴ North (1990).
- ³⁵ Rodrik et al. (2004).
- ³⁶ North et al. (2009).
- ³⁷ Bueno de Mesquita et al. (2003).
- ³⁸ For example, Kleinfeld and Barham (2018).
- ³⁹ Bates (2009).
- ⁴⁰ International Growth Centre (2018).
- ⁴¹ Duflo and Banerjee (2011).
- ⁴² Callen et al. (2023).
- ⁴³ For an extensive discussion of the measurement challenges see Hanson and Sigman (2021).
- ⁴⁴ Barro and Lee (2013).
- ⁴⁵ UCDP/PRIO (2023).
- ⁴⁶ Banks et al. (2024).
- ⁴⁷ For details see Besley et al. (2021). We use a two-step clustering method based on so-called principal components: (i) use the raw data to create principal components, (ii) use an agglomerative hierarchical clustering algorithm to identify clusters based on these principal components.
- ⁴⁸ By construction, repression is a substitute for civil war. While the positive orthant captures civil war, the negative orthant captures repression, so that zero represents countries without either type of political violence.
- ⁴⁹ Besley and Persson (2021).
- ⁵⁰ Besley and Persson (2021); Gallup (2019).
- ⁵¹ For details see Besley et al. (2021).
- ⁵² For a discussion of the links between state effectiveness and wellbeing, including the dispersion of subjective wellbeing, see Besley et al. (2023).
- ⁵³ It is important to recall that neither of the two institutional measures appear (directly or indirectly) in any of our six measures of state effectiveness.

- ⁵⁴ Besley and Persson (2021); Center for Systemic Peace (2021).
- ⁵⁵ Sen (1999).
- ⁵⁶ See Sen (1999) and Verba (2001). Beramendi et al. (2022) also argue that the essence of political equality is trying to give every citizen equal consideration.
- ⁵⁷ EBRD (2013).
- ⁵⁸ Callen et al. (2023); Cantoni and Yuchtman (2021).
- ⁵⁹ Persson and Tabellini found mixed success, see Persson and Tabellini (2006); Persson and Tabellini (2008). Acemoglu et al. (2019) claimed to find persuasive causal evidence.
- ⁶⁰ As is standard, we define democracies and autocracies as countries with average Polity scores of more or less than 5, on a scale from -10 to 10 between 1989 and 2018. GDP growth data is from the Maddison Project Database. Groningen Growth and Development Centre (2020).
- ⁶¹ See, for example, Taagepera and Shugart (1989); Persson and Tabellini (2003).
- ⁶² See, for example, Besley and Kudamatsu (2008).
- ⁶³ Persson and Tabellini (2003); Acemoglu et al. (2005).
- ⁶⁴ Acemoglu and Robinson (2012).
- ⁶⁵ Ashraf et al. (2020).
- ⁶⁶ Weigel (2020).
- ⁶⁷ Levi and Sacks (2009); Levi et al. (2007).
- ⁶⁸ For example, the World Bank now has a dedicated Bureaucracy Lab and promotes work on Community Driven Development based on social cohesion and social capital.
- ⁶⁹ Levi (1989); Putnam et al. (1993).
- ⁷⁰ Ashraf et al. (2014).
- ⁷¹ Besley and Persson bring together insights from two earlier literatures that tried to understand long-run drivers of stable democracies: one on democratic values in political science, going back to Lipset, and one on democratic institutions in economics, going back to Acemoglu and Robinson. See Besley and Persson (2019); Lipset (1959); Acemoglu and Robinson (2000).
- ⁷² Persson and Tabellini (2021).
- ⁷³ Besley and Persson (2019).

⁷⁴ Acemoglu and Robinson (2012).

⁷⁵ Myrdal (1974); Sen (1999).

⁷⁶ For an articulation of this view in the context of climate change see Besley and Persson (2023).

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Response to Tim Besley and Torsten Persson by Margaret Levi

What I most appreciate about this interesting chapter is its efforts to be a work of *political* economy. Besley and Persson take seriously politics and political institutions, as well as the norms and values that are the oil and glue of such institutions. They deserve applause for recognising the intrinsic value of 'a liberal society based on principles of basic economic, political, and civil rights has intrinsic value'. While going far beyond what most economists do by acknowledging intrinsic value, they also marshal evidence for the instrumental benefits of such a society.

That said, this is still very much an economics chapter, and it would benefit from being even more inclusive of the politics – both the science and the practice. Although Besley and Persson acknowledge the work of political scientists in this chapter, the need for more political analysis becomes most apparent in their argument for focusing '...on increasing cohesion in public action to support the building and maintenance of an effective state'. Cohesion, for them, rests on a society-wide consensus that '...emphasises individual rights, civil liberties, and democratic institutions, along with open access to markets that facilitate free enterprise'. It is this cohesion that allows for institutional reforms to achieve the aims of a liberal society as circumstances change and as countries attempt to attain more inclusive political and economic development. Thus, it is imperative that their theory address the political sources of institutional change.

Besley and Persson are relatively persuasive about the three development clusters and the factors that contribute to them, particularly the role of state capacity. This is hardly surprising, given that they are the authors of the paradigm-shifting *Pillars of Prosperity*. But when it comes to societal cohesion, they tend to assume its existence rather than explain its emergence and maintenance. Although they acknowledge it might not be easy to achieve, they nonetheless proceed as if it is.

Besley and Persson recognise that institutional reform is often a product of changes in incentives that encourage powerful actors to accept reform as the best alternative, and they certainly recognise the threat of violence to both cohesion and stability. It is worth further exploration of the politics of cohesion. One way to start is with the kind of political economics they favour. For example, as Barry Weingast argues in his well-known 1997 paper and Acemoglu and Robinson in their 2005 book, fear of popular reaction is one source of incentive change.¹ It can also be a source of stability if there

is a well-grounded belief that certain moves towards special interest politics or revocation of a cherished reform or benefit might provoke electoral push back and mobilised opposition. This was the case with the National Labor Relations Act in the United States in 1935, the federal legislation that gave workers the right to unionise, engage in collective bargaining, and strike legally. The possibility of violence and even a revolution in the country was one reason corporations and legislators were willing to consider significant labour reform, and the likelihood of union pushback helped keep the reforms in place. On the other hand, as union power waned, Congress enacted amendments that undercut labour's rights.² The same happened with welfare benefits, which expanded and contracted in response to the electoral power and urban rebellions of the relatively poor.³

To get at what sustains 'common-interest states' also requires considering the relationship between citizens and states, or at least their governments. What are the conditions under which people peacefully comply with or withdraw their compliance from governments? Or to put the question another way: what are the conditions under which citizens believe government is trustworthy? This comes up in the chapter but largely in relationship to how RCTs might be used in formulating policy.

The conditions for trustworthiness include:⁴

- That the government uphold the social/fiscal contract to provide promised goods and services to its population.
- That the provision of these goods and services is done in a way that is relatively fair according to the standards of the day.
- That government demonstrate it can and will catch and punish free riders, thus reassuring those who would like to comply with government laws that they are not suckers and that there is good reason to believe there will be sufficient contributions to the public good.

As Pablo Beramendi, Tim Besley, and I argue in our work on political equality,⁵ social cohesion may also require arrangements to mitigate conflicts that create problems for democratic practice and public policies by undermining cohesion. Class, ethnic, religious, racial, ideological, and gender divides are often sources of intense disagreement in a polity, as Besley and Persson note. To inhibit violence and achieve a minimal level of consensus requires institutions that facilitate deliberation and mutual respect. Political scientists have long grappled with these questions, as Besley and Persson note, but a new generation of political theorists and philosophers are suggesting new approaches to citizen engagement and social connectedness.⁶

Another way to think about this issue is in terms of an expanded and inclusive community of fate – those with whom our destinies are entwined. We all have some small community of fate, usually with members of our family and close friends. The question is whether it is possible to develop a broader,

more encompassing community of fate among those with whom there are no close pre-existing relationships or indeed any personal relationships at all. John Ahlquist and I were able to provide a proof of the possible in our investigation of certain American and Australian longshore worker unions.⁷ These are organisations whose primary aims are economic: to improve wages, hours, and working conditions. Yet, their members chose to engage in costly political actions on behalf of distant others who are unlikely to reciprocate directly. They closed ports despite loss of salary and possible loss of jobs and imprisonment.

What we observed was built on but distinctive from the solidarity necessary for a union. It was solidarity, yes, but for prosocial ends. The mechanism for deciding whom to help and how was a form of participatory democracy. There were personal relationships among those making the decision but on behalf of strangers they would probably never meet. Crucial to an expanded and inclusive community of fate is the existence of some mutually shared values and norms. The value these labour actions embodied was the old union motto, 'An injury to one is an injury to all', with the ensuing commitment to prevent and to mitigate those injuries. Besley and Persson argue that policies must be consistent with prevailing norms if they are to succeed, but there is also reason to believe that institutions are a source of norm creation. The abolition of slavery in Britain, the US and elsewhere reflected the norms of some but not all. Yet, over time the illegality of slavery came to also make it largely unthinkable. In other instances, institutions and laws may facilitate the establishment of new norms. The development of welfare states both reflected and created norms about who is deserving of help and under what conditions. Moreover, those norms – and welfare state institutions – vary widely across countries, reflecting differences in the values that form the basis of cohesion in those polities.

Besley and Persson appropriately emphasise the importance of a liberal consensus and cohesive society for political and economic development. Moreover, they provide us the beginnings of an important road map for how to achieve such a society. The next step is to fill in more of the details. This is a mammoth project for political economists that will depend on drawing from the research of multiple disciplines and their plurality of approaches and methods.

Notes

¹ Weingast (1997); Acemoglu and Robinson (2005).

² Levi et al. (2017); Cuéllar et al. (2020).

³ Piven and Cloward (1993 [1971]).

⁴ For a fuller summary of this argument and the literature and evidence that informs it, see Levi (2019).

- ⁵ Beramendi et al. (2022). IFS (February 2022). We also have a book in progress.
- ⁶ See, e.g., Allen (2023); Schwartzberg and Knight (2024).
- ⁷ Ahlquist and Levi (2013).

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Response to Tim Besley and Torsten Persson by Leonard Wantchekon

The chapter by Besley and Persson revisits the evolution of development thinking within academia and policy circles over the past 35 years, starting from the Washington Consensus. This consensus was a blueprint for market-oriented state reforms believed to be essential for helping underdeveloped countries catch up economically with their wealthier counterparts. A notable omission from the Washington Consensus was its lack of focus on the social and political dynamics within nations, which significantly influence the implementation of economic policies. The authors highlight a shift in thinking among policy and academic communities towards recognising institutional and social dynamics as crucial to development. This shift emphasises the importance of institutional foundations, state capacity, and the values and norms that underpin economic growth.

In the theoretical section, Besley and Persson outline the institutional prerequisites for development, including the establishment of a peaceful order through the state's monopoly on legitimate violence. They also emphasise the development of state capacities such as taxation, law enforcement, and public goods provision. These elements are more likely to emerge in nations that impose constraints on rulers, have cross-cutting cleavages, and share economic growth.

The authors categorise countries into three 'development clusters' based on the attributes of effective states. The first cluster, 'common-interest states', features strong constraints on the executive, leading to effective revenue collection and broad-based taxation that supports common good expenditures. The second, 'special-interest states', has weaker executive constraints and some state capacity, allowing for taxation and redistribution to appease opposition and benefit the elite. The third, 'weak states', is marked by unstable leadership, lack of constraints on rulers, ineffective or exploitative taxation, and minimal investment and redistribution.

The empirical section presents evidence supporting these state clusters. Using development indicators from various sources and a clustering algorithm, the authors demonstrate that the data align well with the described development clusters. This classification correlates with an index of state effectiveness, subjective wellbeing, and the strength of executive constraints.

The chapter concludes with a discussion of a new consensus in development thinking that prioritises liberal governance principles. This consensus values liberal institutions both for their intrinsic worth in providing a framework

for individual freedom and for their instrumental value, as research shows a correlation between economic performance and democracy. Additionally, it suggests that reforms should extend beyond market policies to bolster state capacity and foster prosocial values and norms that support state functions, marking a significant evolution from the Washington Consensus.

This review and the London Consensus as a whole are both important and timely. The review captures very well the recent evolution of development research, marked by a renewed focus on political institutions and state capacity.

I find the emphasis on liberal and prosocial values very interesting as it both departs from a more 'technocratic' approach to state capacity and invites a more explicit role for social cohesion, citizen empowerment, and autonomy in building state capacity.

I have three main comments to the authors.

I. A liberal consensus?

Is there truly a consensus on liberal institutions as the 'correct' path towards development? While post-war international bodies like the World Bank and the International Monetary Fund champion political and economic liberal institutions, an alternative model has been gaining traction in developing nations. This model is exemplified by China and Vietnam, politically non-liberal regimes that have achieved significant economic growth and poverty reduction through industrialisation and technological innovation.

China's development strategy is characterised by a 'regionally decentralised authoritarian system', which, despite central political control, fosters regional economic innovations via a blend of experimentation and patronage networks. Unlike the Washington Consensus and the authors' proposed 'liberal democratic consensus', China and its financial institutions offer developing countries new financing avenues without demanding liberal economic or political reforms. This alternative financing avenue has led to stronger economic ties between China and Sub-Saharan Africa, helping China to surpass North American and European countries and become the primary economic partner for many African countries. For instance, China has overtaken France as the main trade partner of Francophone Africa. There are similar trends in East Africa with China being the dominant infrastructure investment partner.

Given China's unique trajectory and developing countries' long-standing reluctance to adopt liberal institutions, it's worth questioning who upholds the authors' proposed consensus and how the liberal model is being challenged with Chinese influence. I would suggest a discussion of the non-liberal development path (e.g., Rwanda, Vietnam, Ethiopia) with large investment in infrastructure and education, a top-down approach building social cohesion, and a one-party state with internal factions.

The authors might find the SCRIPTS project of interest, which conducted a survey on perceptions of liberal models in various countries.¹

II. From a typology of states to institutional diagnostics

Transitioning from a state typology to institutional diagnostics raises another point of contention. While categorising countries by similarities and ideal institutional models is insightful, labelling a country merely as a bundle of undifferentiated institutions is limiting.

Consider the United States, positioned at the right-most corner of the cluster analysis. Despite being labelled a ‘common-interest state’, this designation oversimplifies the complexities of its political and social landscape, marked by a gerontocratic elite, special interest-dominated politics, a highly polarised public, and limited distribution and social welfare.

This critique extends beyond the US; most nations display a mix of liberal and non-liberal institutions. The focus should shift from broad state assessments to detailed diagnostics identifying underperforming institutions, setting normative and empirical benchmarks for their operation, and charting pathways to improvement. This approach, which I term an analysis of ‘political distortions’, delves into the political incentives hindering optimal economic institution performance.²

This perspective is vital, as it not only reveals the current institutional equilibrium but also illuminates potential paths for transition. Encouraging institutional experimentation, as the authors acknowledge, may offer a more feasible route to reform than sweeping state overhauls, which are typically rare in history.

One challenge with the authors’ conceptualisation of development clusters emerges when considering policy interventions. After all, political violence and state capacity co-evolve. Indeed, as they suggest, taxation and the protection of property rights may require peace, yet developing institutions that favour such rights also affect the likelihood of civil wars. Hence, which reforms should one target to affect both dimensions of development, when they are endogenous? One possible approach could target the initial sources of such disparities, including endowments or the prevalence of local information. Both affect local state capacity.³ However, another approach could take the existing frictions (i.e., political distortions due to the historical, institutional and informational past) as given, and then consider which reforms may improve long-run development in this second-best world. These may include bureaucratic reform to merit-based appointments, information provision, or procurement reform.

The discussion above suggests another limitation of the authors’ classification approach: it is based on an *ex-post* labelling. Like any clustering method, it is based on the similarity of observed data along multiple dimensions. However, the meaning of the groups is typically given after the classification, and might not remain if more clusters were considered, or if new data were to arise. Indeed, small changes to the data or measures used could significantly alter the groupings in [Figure 16.1](#). There may even be alternative groupings that would be more useful for both policy purposes and classification.

III. From technocratic power to power to the people

Finally, the chapter's emphasis on the importance of norms and values in shaping effective institutions misses an opportunity to fully explore its implications. If cultural factors are crucial for state capacity, then we must scrutinise the often technocratic nature of capacity-building interventions. Development is unlikely to be a top-down process, akin to the Washington Consensus approach, but rather should incorporate institutional experiments that reflect and utilise local power dynamics, fostering state capacity from the ground up.

To sum up, the chapter by Besley and Persson rightly documents the massive transformation in development thinking across academic and policy circles in the last 35 years. Three main challenges stem from the authors' proposal to move forward. First, while liberalism is one natural candidate, alternative paths like that of China threatens its pre-eminence. Second, the interactions between capacity, the maintenance of order, and constraints to power seem to co-evolve, with very few nations able to advance in each one from a liberal path. Finally, while the fields of development and political economy have followed a micro trend (for example, Institutional Experiments), it remains to be seen how we could integrate results from a collection of studies to broader macro models and to actual state reform. All these topics remain an active field of research – one which the authors contextualise in this chapter.

Notes

¹ Giebler et al. (2023).

² Canen and Wantchekon (2022).

³ See de la Sierra (2020); Balán et al. (2022); Aman-Rana et al. (2023).

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