

**PHD THESIS SUMMARY:
Informal institutions and economic development.**

THOMAS DOMJAHN

PhD in philosophy and economics, December 2011

University of Bayreuth

My PhD thesis looks at the relationship between informal institutions (e.g., morals, customs, traditions, norms, ideologies, and religion) and economic development. The perspective is conceptual as well as empirical. The conceptual part critically compares the theories of Aristotle, Montesquieu, Alexis de Tocqueville, Karl Marx, Max Weber, Friedrich A. von Hayek, Douglass North, James Coleman, Robert Putnam, and Francis Fukuyama. The empirical part relates and analyses three country-level case studies: Mexico, South Korea, and Morocco

The PhD thesis is motivated by the observation that institutions are getting more and more important in the debate about the determinants of long-term economic development. However, most economic studies still analyse the role of formal institutions exclusively (e.g., the rule of law, property rights, or patent law) while informal institutions are neglected. Daron Acemoglu (et al. 2004) and Hernando de Soto (2000) can be cited as two prominent examples of this tendency. The disregard of informal institutions in development economics is surprising as Nobel Prize winner Douglass North underlined the importance of formal *and* informal institutions and their interplay throughout his path-breaking book *Institutions, institutional change and economic performance* (1990).

As most, economists have traditionally neglected informal institutions, culture, and social capital,¹ the most innovative approaches in this field have come from non-economists, like the political scientist Robert Putnam (1993), the historian David Landes (1998) and, to go back even further in the history of ideas, from the sociologist Max Weber, such as in *The protestant ethic and the spirit of capitalism* ([1904-1905]). The problem with these works is that they take formal institutions as

¹ Informal institutions, culture, and social capital are slightly different concepts, but all of them have in common that they can be interpreted as complements to formal institutions.

given and just analyse the role of informal institutions, thereby overstating the role of religion, social capital, and culture in general. For example, Landes writes: “If we can learn anything from the history of economic development, it is that culture makes almost all the difference” (2000, 2).

In contrast to many other works dealing with culture and economic development, my PhD thesis does not analyse the role of culture for economic development per se. Rather its main claim is that only a dynamic analysis of the interplay of formal *and* informal institutions can help to understand the process of economic development. I conclude that informal institutions can slow down as well as accelerate the process of economic development. This result has an important implication for development policies: Formal institutions that have been well-proven in one country cannot be transferred easily to another country with different informal institutions. Therefore, it is essential that reforms of formal institutions be compatible with local informal institutions, which change more slowly.

This finding is illustrated and endorsed by the three case studies. Mexico is presented as a country where the imposition of formal institutions that have worked well in other countries—such as democracy, federalism, a market economy, and secularism—did not succeed because they were not sufficiently supported by domestic informal institutions. South Korea, on the other hand, profited from its informal institutions. Confucian ethics in South Korea and other East Asian countries (sometimes also labelled “Asian values”) proved to be more flexible, pragmatic, secular, and adaptive than other non-Western ideologies, such as Buddhism, Hinduism, or Islam. Consequently, they facilitated rapid political and economic reforms, and especially human capital accumulation as Confucianism places a high value on education.

In contrast to South Korea, important political reforms such as the separation of the church and the state have been impeded in Morocco by its informal institutions, shaped by the Islamic religion. Moreover, these informal institutions hinder the socio-economic integration of women and girls (60 percent of all females in Morocco are still illiterate). Nevertheless, formal as well as informal institutions are dynamic entities that evolve in the course of years and decades. Changes of formal institutions can cause changes of informal institutions and vice versa. For example in Morocco, the reform of the family code (*Moudawana*) in 2004 and constitutional changes during the Arab Spring

put into effect by King Mohammed VI show that at least slow institutional change is possible even in countries that are thought to be locked-in to a disadvantaged institutional framework.

The results of my empirical analysis confirm central arguments of Aristotle, Montesquieu, and Tocqueville. All of these, as social scientists, stressed the importance of formal *and* informal institutions and argued that importing institutions is always problematic. For example, in his *Politics* (book IV, section 5), Aristotle argues that a democratic constitution can become oligarchic by non-democratic customs and vice versa. So informal institutions (e.g., customs) can influence the functioning of formal institutions (e.g., the constitution). In *The spirit of the laws* (book XIX, chapter 14), Montesquieu develops the thesis that the state can change formal institutions but that informal institutions cannot and should not be changed by a central authority. In *Democracy in America* (book II, chapter 5), Tocqueville highlights and admires the contemporary (1830s) political culture of the USA because it generates grassroots movements and voluntary associations which can solve social problems more efficiently than the state. On the other hand, he is realistic enough not to advise the introduction of American political institutions in his home country, France, which has a completely different political culture. These three authors are rarely considered in the current debate about institutions and development. So my thesis provides some new (and at the same time classical) perspectives to contemporary debates in development economics and institutional economics.

Apart from their specific arguments, I think that we can also learn methodological lessons from philosophically orientated social scientists like Aristotle, Montesquieu, Tocqueville, and Weber. While today's statistical studies try to reduce the concept of informal institutions, social capital or culture to a minimal definition in order to measure it, these scholars keep a broader concept in their mind. For example, in *Economy and society* ([1922]), Weber coined the term 'comprehensive social science' (*verstehende*) meaning that we should look more at the interaction of social variables and try to understand the underlying mechanisms. As I argue in this thesis, contemporary econometric studies (e.g., Knack and Keefer 1997) do indeed deliver partial results about the relationship between informal institutions (narrowly defined) and development (also narrowly defined as long-term growth of GDP). But these studies have to be complemented by a more dynamic and

evolutionary perspective that takes into account the complexity of social values.

REFERENCES

- Acemoglu, Daron, Simon Johnson, and James Robinson. 2004. Institutions as the fundamental cause of long-run growth. *NBER Working Paper* No. 10481. National Bureau of Economic Research, Cambridge, MA.
- Aristotle. 1995 [ca. 345-325 BC]. *Politics*, translated by Ernest Barker. Oxford: Oxford University Press.
- de Soto, Hernando. 2000. *The mystery of capital: why capitalism triumphs in the west and fails everywhere else*. New York: Basic Books.
- Knack, Stephen, and Philip Keefer. 1997. Does social capital have an economic payoff? a cross-country investigation. *Quarterly Journal of Economics*, 112 (4): 1251-1288.
- Landes, David. 1998. *The wealth and poverty of nations: why some are so rich and some so poor*. New York: Norton.
- Landes, David. 2000. Culture makes almost all the difference. In *Culture matters: how values shape human progress*, eds. Lawrence Harrison, and Samuel Huntington. New York: Basic Books, 2-13.
- Montesquieu. 1989 [1748]. *The spirit of the laws*, eds. Anne Cohler, Basia Carolyn Miller, and Harold Samuel Stone. Cambridge: Cambridge University Press.
- Putnam, Robert. 1993. *Making democracy work*. Princeton: Princeton University Press.
- North, Douglass. 1990. *Institutions, institutional change, and economic performance*. Cambridge: Cambridge University Press.
- Tocqueville, Alexis de. 2000 [1835-1840]. *Democracy in America*, translated by Harvey Mansfield, and Delba Winthrop. Chicago: University of Chicago Press.
- Weber, Max. 2010 [1904-1905]. *The protestant ethic and the spirit of capitalism*. Translated by Talcott Parsons. London: Routledge.
- Weber, Max. 1978 [1922]. *Economy and society: an outline of interpretive sociology*, eds. Guenther Roth, and Claus Wittich. California: University of California Press.

Thomas Domjahn obtained his PhD from the faculty of philosophy and economics at the University of Bayreuth (Germany) supervised by professors Martin Leschke, Peter Oberender, and Bernhard Herz. His thesis was written in German under the title *Informelle Institutionen und wirtschaftliche Entwicklung. Eine empirische und konzeptionelle Analyse unter besonderer Berücksichtigung der Entwicklungspfade von Mexiko, Südkorea und Marokko*, and was published by Verlag für Nationalökonomie, Management und Politikberatung. His main academic interests are development economics, institutional economics, and theories of the state and society. He is presently working as a journalist and as a lecturer.

Contact e-mail: <Thomas.Domjahn@gmx.de>