



Political Economy Analysis

Selected Readings

Political economy analysis covers an expanding area of development theory and practice drawing on an extensive and dispersed body of literature. As an aid to navigating this wide-ranging subject area [The Policy Practice](#) has prepared the following annotated bibliography of key readings. The aim has been to keep the list short and selective, and to prioritise texts that are written in accessible language, synthesise latest thinking and are freely available on the web. The bibliography is divided into four hyperlinked sections: (1) [conceptual underpinnings](#), (2) [political economy analysis tools](#), (3) [noteworthy case studies](#), and (4) [practical guidance on using political economy analysis](#).

Additional references may be found on the [capacity4dev working group on political economy](#), the [GSDRC political economy analysis topic guide](#) and the [World Bank Political Economy Community of Practice](#). If you have comments on this bibliography or additional suggestions on papers to include please write to contact@thepolicypractice.com.

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1) Conceptual underpinnings

Political economy analysis is not based on a single theory. However, it does embody a coherent set of ideas that underpin analysis about how economic political and economic development occurs. The central contention is that the public authority and public goods required for development arise through domestic political processes and contestation between interest groups. This can be seen as a process of **bargaining between state and society actors** and through the interaction of formal and informal institutions ([IDS 2010](#)). Such explanations of development are in marked contrast to the traditional 'good governance' agenda, which is based on normative assumptions that improved governance and institutional models can simply to be transferred to the developing world.

The recent literature critiquing the '**good governance**' agenda provides a useful summary of many of the key ideas that have been taken forward in political economy analysis ([IDS 2005](#); [IDS 2010](#); [Grindle 2011a](#)). All of these argue for an approach to governance based not on imposing 'good practice', but in looking for the 'best fit' to the local social and political context ([Levy 2011](#), [Grindle 2011b](#)). A proponent of this approach is the [Africa Power and Politics Programme](#), which sets out to examine

structures and institutions rooted in the African socio-cultural context that work better for development (Booth 2011a; Kelsall 2008).

Political economy analysis provides a set of explanations of how societies establish order and subsequently develop. The literature on **statebuilding and fragility** highlights the requirements for establishing basic political authority and limiting conflict by establishing the legitimacy of the state (OECD 2010) and creating a political settlement or bargain amongst elites (Parks and Cole 2010). An influential paper (North *et al.* 2007) categorises the governance situation observed in many developing countries as a '*limited access order*'. Under these conditions access to economic and political opportunities are tightly controlled so as to create economic rents whose benefits can be shared amongst powerful elites in order to ensure their cooperation. The **management of economic rents** is thus a key part of the political settlement and the development challenge. While uncontrolled rent-seeking can be damaging to growth, some forms of rent management may be essential to maintain social stability. Khan (2006) has also argued that rents can be managed in a way that is growth enhancing where this enables resources to be transferred to more productive sectors and creates incentives for achieving rapid technology acquisition and productivity enhancement. Williams *et al.* (2009) attempt to synthesise these ideas in an analytical framework that examines the incentives facing the holders of political and economic power, and analyses the conditions under which they would act in ways that generate sustained growth.

Political economy analysis draws attention to the importance of **formal and informal institutions** - or the **rules of the game** – which mediate political and economic interaction. While there is broad support for the notion that 'institutions rule', there is a great deal of variability in the different institutional forms that can support development (Booth 2011b; IPPG 2010; Rodrik *et al.* 2002). Political economy analysis has emphasised the need to consider both formal institutions (codified laws and officially sanctioned rules) and informal institutions (rules that are created, communicated, and enforced outside of officially sanctioned channels and often through personal, social and ethnic ties). Helmke and Levitsky (2004) provide an analytical framework examining the interaction between formal and informal institutions.

Political competition and its effects on development outcomes has been another important focus of political economy analysis. Khan (2005) finds that there is no difference globally between democracies and autocracies in their development outcomes. Other studies find significant variation between different types of democratic system with young democracies tending to act in less developmental ways that well established democracies (Keefer 2005). In seeking to understand better the mechanisms by which political competition affects development outcomes, analysts have pointed to the effects of entrenched **patron-client relationships** in many developing countries. Kitschelt and Wilkinson (2009) explore different forms of clientelism, which they collectively define as "a transaction involving the direct exchange of a citizen's vote in return for direct payments or continuing access to employment, goods, and services." Keefer and Khemani (2005) identify mechanisms by which electoral competition can reinforce patronage politics. They analyse this in

terms of '*political market imperfections*' (incomplete information, social divisions and credibility gaps) that create incentives for politicians to deliver narrowly targeted private goods rather than public goods that are required for development and whose benefits are more widely shared.

2) Analytical tools

A useful overview of available political economy analysis tools is contained in DFID's how-to note (DFID 2009). Most recently the EC has commissioned a draft background paper on '*Using Political Economy Analysis to Improve Development Effectiveness*' (Unsworth and Williams 2011). There are two annexes to the paper, which provide a tool for country level political economy analysis (EC 2011) and sectoral political economy analysis (EC forthcoming).

The EC framework is a development of the *Strategic Governance and Corruption Assessment* (SGACA) tool used by The Netherlands Ministry of Foreign Affairs (CRU 2008). Other donor tools for country level political economy analysis include DFID's *Drivers of Change* analysis (DFID 2004) and SIDA's *Power Analysis* (SIDA 2006). The World Bank's approach to political economy analysis draws on a wide range of tools to address specific operational problems at country, sector and project level. This '*problem-driven*' approach is described in Fritz et al. (2009) and recently summarised in Poole (2011). The World Bank previously published a tool to assess the political economy of particular reforms (World Bank 2008).

The OECD has recently published a political economy framework examining the *international drivers of corruption* that analyses how international processes interact with domestic political processes (OECD 2011).

3) Noteworthy case studies

Development agencies have often been reluctant to publish political economy studies because of their political sensitivity. However, there are some useful studies available on the web:

Most of the DFID Drivers of Change country studies are published on the GSDRC website. Some noteworthy examples include the Drivers of Change Studies for Ghana (Booth et al. 2005) and Malawi (Booth et al. 2006).

Examples of sectoral political economy analysis include a study of the roads sector in Uganda (Booth and Golooba-Mutebi 2009), infrastructure sectors in Zambia (Beuran

et al. 2011), urban bus transport in Bangladesh (World Bank 2008) and the water sector in Kenya (Rampa 2011).

For an illustration of Keefer's approach to analysing the effects of electoral competition and clientelist politics on public expenditure see this chapter from the World Bank Ghana Country Economic Memorandum (Keefer 2007).

For an analysis of the political economy of economic reforms in Nigeria see Utomi *et al.* (2007).

4) Practical Guidance on Using Political Economy Analysis

Practice guidance on using political economy analysis can be found in DFID's how to note (DFID 2009) and the EC background paper on '*Using Political Economy Analysis to Improve Development Effectiveness*' (Unsworth and Williams 2011). For a discussion on how the findings of political economy analysis has influenced donor engagement in Nigeria and Bangladesh see Duncan and Williams (2010). A recent World Bank paper also discusses the challenges of making political economy analysis operational (Beuran *et al.* 2011). These issues are further explored in critical evaluation of the World Bank's use of political economy analysis (Desai 2011). For a review of the Dutch experience of using the SGACA tool see Hazenberg (2009). Schakel *et al.* (2010) provide a useful guide to the main political economy analysis tools with guidance on practice considerations for implementing studies and using results.

Davis (2011) provides an overview of how private sector development professionals can apply political economy analysis to business environment reform.

A recent paper by Copestake and Williams (2012) suggests that a more interactive approach to political economy analysis is needed to unlock its practical potential.

References and summaries

1) Conceptual Underpinnings

IDS (2010) Upside down view of governance, Centre for the Future State

<http://www2.ids.ac.uk/gdr/cfs/pdfs/AnUpside-downViewofGovernance.pdf>

Many governance programmes fail because they focus solely on strengthening formal, rules-based institutions and ignore the connections between the public and private spheres of life. Research evidence reviewed in this paper suggests that public authority is created in more complex ways through processes of bargaining between state and society actors and the interaction of formal and informal institutions. This requires policymakers to rethink their assumptions about governance and development. While in the longer term it is desirable to build rules-based, inclusive institutions, progress in the short- to medium-term will depend more on indirect strategies that aim to influence the incentives and interests of local actors in the context of informal institutions and personalised relationships.

The following questions can help to understand better the causes of bad governance and to identify ways of supporting more constructive bargaining between public and private actors:

- What is shaping the interests of political elites? (e.g. sources of revenue)
- What is shaping relations between politicians and investors—might they have common interests in supporting productive investment?
- What might stimulate and sustain collective action by social groups to demand better services?
- What informal local institutions are at work, and how are they shaping development outcomes?
- Where does government get its revenue from, and how is that shaping its relationships with citizens?

IDS (2005) Signposts to More Effective States: Responding to Governance Challenges in Developing Countries, Centre for the Future State, Institute of Development Studies: Brighton.

<http://www2.ids.ac.uk/gdr/cfs/pdfs/SignpoststoMoreEffectiveStates.pdf>

This report joins in the criticism of the 'good governance' agenda, stressing that donor prescriptions for institutional change have been unrealistic in their excessive

expectations of poor countries and have failed to examine the deep-seated causes for bad governance. On the basis of a series of separate research projects, the report draws conclusions on: (a) taxation and state-society relations, (b) civil society organisations and their relationship to the state, and (c) new forms of public-private relations. The conclusion is that the development community cannot create good governance, but it can nurture useful, if less bold, changes, such as:

- **Regarding taxation:** restricting access of political elites in poor countries to rents, and stimulating "public debate about the links between revenue-raising and spending";
- **Regarding civil society:** focusing on "the iterative relationship, over time, between state and society, rather than on 'strengthening' civil society vis-à-vis the state";
- **Regarding public-private partnerships:** Building on those informal relationships that are working, rather than trying to impose "purer", imported solutions.

Grindle, M.S. (2011a) Good Enough Governance Revisited, Development Policy Review, Volume 29, Issue Supplement s1, pages s223–s251,
<http://www.gsdr.org/docs/open/RET283.pdf>

'Good enough governance' refers to the minimal conditions of governance necessary to allow political and economic development to occur, contrasting with the long and growing list of normative requirements included in the traditional good governance agenda. Given the fact that there remain major unresolved debates about the relationship between governance and development, how can practitioners take decisions on concrete interventions to achieve 'good enough governance'? The following analytical frameworks can help to improve decision making about what governance interventions should be undertaken in particular country contexts:

- ***Assessing the context for governance interventions: What is there to build upon?*** Priorities for governance interventions should match the characteristics of the state, its strengths and capacities. A typology of state characteristics and respective priorities for intervention is presented in the paper.
- ***Assessing the content of governance interventions: What are the characteristics of specific interventions?*** Practitioners need to anticipate the ease or difficulty of alternative measures based on factors such as their potential to ignite conflict, time requirements, administrative complexity and the need for behavioural change.
- ***Content and context in the process of reform: Is there room for manoeuvre in the process of change?*** Good political economy analysis combines analysis of both context and content and seeks ways of bringing that analysis to bear on the practice of reform. It should recognise that the reform

process is dynamic and may be subject to different influences, public exposure and processes of negotiation unfolding over time.

The paper concludes that where most is needed in terms of improved governance, the more difficult good enough governance is to achieve. Change is not always possible and there are no magic bullets. But, research and practice can help to find opportunities for moving in a positive direction.

Levy, B. (2011) Getting beyond the 'every country is unique' mantra,
<http://blogs.worldbank.org/governance/getting-beyond-the-every-country-is-unique-mantra>

This and other entries on Brian Levy's World Bank blog argue strongly for an approach to supporting governance based on 'best fit' to local conditions rather than 'best practice'. However, in insisting on the importance of recognising the specificity of the country context, practitioners need specific guidance on what types of intervention will be suited to different types of state. Levy distinguishes between five conditions that broadly depict a trajectory in state building and political competition:

- Category 1: The "founding" political settlement. 'Political settlements' – bargains among elites (and sometimes their non-elite allies as well) that end violent conflict – are key to enabling conflict-affected countries to begin a new chapter in their development histories.
- Category 2: Early-stage state dominance incorporates countries where dominant political leadership (perhaps military, perhaps civilian; perhaps organized around a political party, perhaps a charismatic individual) has successfully consolidated its grip on power.
- Category 3: Later-stage state dominance. Countries that successfully traverse the earlier-stages of the 'dominant state' trajectory will over time increasingly confront a new generation of governance-related challenges.
- Category 4: Early-stage competitive clientelism is likely to be the prevalent pattern in those settings where the initial political settlement centred around a 'founding' election.
- Category 5: Later-stage competitive polities.

Grindle, M.S. (2011b) Governance Reform: The New Analytics of Next Steps, Commentary in Governance: An International Journal of Policy, Administration, and Institutions, Vol. 24, No. 3, July 2011 (pp. 415–418)
<http://onlinelibrary.wiley.com/doi/10.1111/j.1468-0491.2011.01540.x/pdf>

In this recent commentary Merilee Grindle highlights the recent shift away from prescriptive, 'one size fits all', best practice modes of development intervention towards more context specific and situationally determined responses to specific

problems. In this new thinking the emphasis on next steps, good enough governance, bottlenecks, contextualized diagnosis, and binding constraints. New analytic approaches and frameworks have been developed focusing on arriving at localised and informed solutions to specific constraints and needs. The question raised by Grindle is whether these approaches in fact lead to effective knowledge of how to resolve real problems. Do they provide effective guidance on what is likely to work and what is not likely to result in policy or institutional reform? Do they distinguish between aspects of a context that can be changed and those that are resistant to change? Where they have been applied, have they led to good results?

Booth, D. (2011a) Introduction: Working with the Grain? The Africa Power and Politics Programme IDS Bulletin 42.2

<http://onlinelibrary.wiley.com/doi/10.1111/j.1759-5436.2011.00206.x/pdf>

This article introduces a new research venture, the **Africa Power and Politics Programme**. The APPP starts from the assumption that the "forms of governance that might work better for development under the specific conditions yielded by African history and geography are not known." The research goal is to examine structures and institutions rooted in the African socio-cultural context that work better for development.

The focus is not only the apex of state power, but also on "the full range of functions performed more or less badly by organs of the central or local state". Methodologically, the project uses systematic comparisons, steering a middle course between multivariate statistical analysis and single case studies.

The two basic hypotheses underpinning the research are:

- Public goods are delivered better when institutions are shaped in such a way as to address the prevailing collective-action problems, and worse when they are imported from outside this local reality.
- The institutions that will work best for public goods provision and development in the African context are ones that, by design or otherwise, have a local problem-solving character and build on relevant components of the available cultural repertoire.

Kelsall, T. (2008) Going with the Grain in African Development? Development Policy Review, Volume 29, Issue Supplement s1, pages s223–s251,

<http://onlinelibrary.wiley.com/doi/10.1111/j.1467-7679.2011.00527.x/pdf>

http://www.dfid.gov.uk/R4D/PDF/Outputs/APPP/APPP_Discussion_Paper_1_Kelsall.pdf

This article examines what -- in contrast to development through the good governance agenda informed by Western practices -- development processes based on shared habits and widely understood practices in Africa means, i.e. development "going with the grain of African ways of doing things". In Africa, the extended family remains the primary locus of political obligation and moral imperative, according to the author. The other effective development institutions are religious (churches, mosques etc.) and community and ethnically based forms of organization. Such organizations are based on some constant socio-political variables: face-to-face accountability, "big men", clientelism (patronage), and (in the case of larger structures) political largesse. Going with the grain at a local level implies utilizing the authority of leaders who already enjoy local legitimacy even if it is based on 'Father-Family-Food' neo-patrimonialism. Thus, "the question for developers wanting to work with the grain of African society -- is not how to transform neo-patrimonialism, since that is an impossible or at least very long-term project, but rather how to restrain or mitigate its worst effects: how to ensure that despotism is always enlightened".

OECD (2010) The State's Legitimacy in Fragile Situations: Unpacking Complexity, OECD, Paris

<http://www.oecd.org/dataoecd/45/6/44794487.pdf>

Four main sources of legitimacy are identified in this report:

- Input/process legitimacy (linked to agreed rules of procedure);
- Output/performance legitimacy (effectiveness and quality of public goods and services);
- Shared beliefs/sense of political community;
- International legitimacy (recognition of the state's external sovereignty).

No state relies on a single source of legitimacy. Different sources of legitimacy interact: harmoniously, uneasily or clashing. Legitimacy in fragile states often differs from region to region and community to community.

Following this analysis, the paper provides a series of recommendations for donors:

- Seek a clear understanding of local people's multiple and conflicting beliefs about what constitutes legitimate political authority.
- Understand how legitimate donors themselves are perceived to be and how this influences their effectiveness.
- Be aware that their actions (project design, providing resources and international legitimacy, demanding accountability etc.) have an impact on internal sources of legitimacy and local state–society relations.
- Facilitate debate and interaction between groups representing different interests and perceptions of legitimacy.
- Focus on how the global environment affects the incentives of political and economic elites to engage in state building.

- Be open to political arrangements that encompass traditional aspects of legitimacy.

Parks, T. and Cole, W. (2010) Political Settlements: Implications for International Development Policy and Practice, The Asia Foundation, Occasional paper 2.

<http://asiafoundation.org/publications/pdf/745>

This paper aims to clarify the key concepts related to "political settlements" thinking and provide ideas on how to operationalise this line of thought at the policy and programme level.

The political settlements framework is a new approach for international development organizations to better understand political power dynamics in developing countries, in particular in countries affected by protracted conflict or fragile conditions. The key elements of a political settlement are actors, interests, and institutions and their alignment in informal, ever-evolving power arrangements.

In many contexts, donor assistance has a significant influence on political settlements, at times entrenching settlements that are exclusionary, destabilizing, or not conducive to development. Thus, it is legitimate for international actors to use the political settlements framework to make sure this does not happen.

This paper creates a framework for donors to:

- Conduct political settlement mapping.
- Realign country strategy based on an analysis of key tradeoffs and plausible best-case scenarios.
- Better understand local politics writ large.
- Engage in entrepreneurial programming, flexibility in project design, implementation and the selection of partners.

North, D. et al, 2007, 'Limited Access Orders in the Developing World: A New Approach to the Problems of Development', Policy Research working paper, WPS 4359, World Bank, Washington, D.C.

<http://go.worldbank.org/775JAU9CB1>

This paper distinguishes between two basic types of political and economic systems:

- **Limited access orders.** These are most common type of social order and the norm in the developing world. A common feature of limited access orders is that political elites divide up control of the economy, each getting some share of the

rents. Since outbreaks of violence reduce the rents, the elite factions have incentives to be peaceable most of the time.

- **Open access orders.** These exist in countries with competitive market economies and democratic political systems. Peace within such societies is maintained through state monopoly on violence and the rule of law. These systems are restricted to a limited set of countries in the developed world.

Economic and political development requires a long-term shift towards open access orders. However, there are risks inherent in this transition where political and economic reforms can disrupt the processes of rent-creation and sharing that are instrumental to peace and social stability.

Khan, M. (2006) Governance and Economic Growth Since the 1960s: Background Paper for the World Economic and Social Survey

http://www.un.org/esa/policy/backgroundpapers/khan_background_paper.pdf

This article distinguishes between 'market-enhancing' and 'growth-enhancing' governance approaches to achieving development in poor countries.

The good governance agenda, based on liberal economics, is of the first type. It focuses on those aspects of governance (such as property rights, rule of law, reducing corruption and banishing expropriation) that are necessary for ensuring the efficiency of markets. The assumption is that if states can ensure efficient markets, private investment will drive economic development.

Growth enhancing governance stresses a different set of different governance capacities for achieving market and non-market transfers of resources to more productive sectors, managing incentives for achieving rapid technology acquisition and productivity enhancement, and maintaining political stability.

Growth-enhancing governance has some effects that appear to contradict the requirements of market enhancing governance. For instance, growth-enhancing governance can increase the chances of corruption and other forms of rent seeking.

The analysis points to the limitations of the current governance agenda that focuses almost exclusively on market-enhancing governance. This is very difficult to achieve in developing countries where markets are inherently inefficient. Moreover, an exclusive focus on market-enhancing governance can often diminish the capacity of states to enhance growth.

Williams, G, Duncan, D., Landell-Mills, P. and Unsworth, S. (2008) Politics and Growth, Development Policy Review 29(s1)299-321

<http://onlinelibrary.wiley.com/doi/10.1111/j.1467-7679.2009.00433.x/pdf>

<http://www3.interscience.wiley.com/cgi-bin/fulltext/121557141/PDFSTART>

This article presents an analytical framework to answer the question: 'What drives the holders of power to act in ways that generate sustained growth?'

Three conditions for growth and associated obstacles are identified:

Condition for growth	Obstacle arising from specific kinds of public-private interaction	Sub-types
Freedom from expropriation	Predation	Private predation State predation Looting
Competitive markets	Rent seeking	Extractive rent-seeking Dividend collection
Adequate investment in public and semi-public goods	Patronage spending on private goods	e.g. subsidies, public-sector wages and pork-barrel projects

Factors influencing the extent of predation, rent seeking, and patronage spending include:

- The structure of the economy and source of government revenues (resource extraction vs. production; agriculture based vs. service-based economy)
- The nature of the political system (extent of political competition and ways politicians gain and hold on to power)
- The use of violence (rent-seeking and patronage are seen as a means to buy off groups which can threaten the regime)
- Collective action generating bargaining around issues of broader public interest
- Public expectations of government (vicious circle of low public expectations of government, weak policy-making and non-delivery)
- Attitudes of political leaders towards business
- Nature of the bureaucracy

The authors conclude by pointing to three main points of entry for development agencies: (i) external pressures influencing political incentives; (ii) strengthening

internal incentives for collective action; and (iii) supporting more constructive forms of state-society interaction.

Booth, D. (2011b) Aid, Institutions and Governance: What Have We Learned? Overseas Development Institute (ODI) Development Policy Review, Vol. 29, pp. S5-S26, 2010

<http://onlinelibrary.wiley.com/doi/10.1111/j.1467-7679.2011.00518.x/pdf>

This summary of latest thinking on the role of institutions in development highlights the following points:

- Institutions 'rule' – the relationship between institutions and development outcomes is stronger than most other development relationships. However, we don't yet know which institutions are the right ones to support in order to trigger development.
- Institutions promoted by the good governance agenda and best practice are a misleading guide to the kind of institutions needed to create growth in very poor countries trying to get less poor.
- Institutions are rarely the result of conscious design, but rather a spin-off from politics, borrowing from previous, culturally recognised structures and processes.
- Institutions frame policy choices in two important ways: by generating a gulf between real policies and declared policies; and by shaping regimes that have an interest in growing the national economy (and which therefore adopt good policies), as well as regimes that are predatory, with little interest in good policies.

The article links these ideas to debates about country ownership and aid effectiveness. It finds that:

- The evidence on the impact of aid is not very encouraging, whereas the evidence on country ownership remains compelling. This leads to the question: can aid help at the margin?
- Poverty Reduction Strategy Papers (PRSPs) did not seem to work, as they engineered a kind of ownership but with new conditions attached.
- Development practitioners need to become much more sophisticated in their understanding of local ownership.
- It will be critical to understand how political systems work and how promising systems can be 'nudged along' towards improved development.

IPPG (2010) Beyond Institutions: Institutions and Organisations in the Politics and Economics of Growth and Poverty Reduction – A Thematic Synthesis of Research Evidence. Manchester: Improving Institutions for Pro-Poor Growth Programme, University of Manchester.

[http://www.ippg.org.uk/8933_Beyond%20Institutions.final%20\(1\).pdf](http://www.ippg.org.uk/8933_Beyond%20Institutions.final%20(1).pdf)

The Research Consortium on Improving Institutions for Pro-Poor Growth (IPPG) summarizes findings from a broad range of research projects on institutions writ large (state-business relations, land reform, contract labour, contract farming, territorial development etc.).

Key findings include the following:

- While it is true that 'institutions matter', individuals and organizations matter too, for it is they who forge, maintain, implement and change institutions.
- It follows that for donors to encourage legitimate and effective institutions which sustain a stable and inclusive environment for growth and poverty reduction, they will need to:
 - Think beyond institutional design and form.
 - Recognise the importance of the distinction and interaction between institutions and organisations and embed this in policy and operational thinking.
 - Learn how to 'think politically' and to 'work politically'; and in particular how to help build up the players – especially the economic, social and political organizations -which will both shape and make institutions work.
 - Get smarter at identifying and understanding stakeholder interests and their relationships, and in discriminating between the developmental, the collusive and the predatory.
 - Appreciate that recognising where the obstacles are, and devising strategies to negotiate them, requires deep knowledge and understanding.

Rodrik, D. and Subramanian, A. and Trebbi, F. (2002) Institutions Rule: The Primacy of Institutions over Geography and Integration in Economic Development," NBER Working Paper 9305, Summary available at:

<http://www.imf.org/external/pubs/ft/fandd/2003/06/pdf/rodrik.pdf>

Why are there huge differences in average incomes between the world's richest and poorest countries?

In this paper the authors test three alternative explanations for varying development performance between countries using regression analysis:

- Geography (i.e. climate, natural resource endowments, disease burden, transport costs, and extent of diffusion of technology from more advanced areas)
- International trade (integration into the global economy)
- Institutions (in particular the role of property rights and the rule of law)

The analysis uses instrumental variable techniques to distinguish the effects of two-way causality and interactions between variables in order which effects are exogenous. The quality of institutions appears to override all else as the determining factor.

The authors stress that while economic analysis can help by identifying the incentive effects of different institutional set-ups, public deliberation and collective choice within societies should be at the core of making institutional choices.

They stress that their findings should raise serious questions about IMF and World Bank conditionality. As institutional change is slow, the time horizons for structural adjustment programs cannot be 3-5 years. Also, the focus in conditionality on getting policies right needs to be rethought, because policy changes are driven by institutional processes.

Helmke, G. and S. Levitsky (2004) 'Informal Institutions and Comparative Politics: A Research Agenda', *Perspectives on Politics* 2 (4): 725–740.

http://www.wcfia.harvard.edu/sites/default/files/883__informal-institutions.pdf

This paper presents a framework for studying informal institutions (defined as socially shared rules, usually unwritten, that are created, communicated, and enforced outside of officially sanctioned channels).

It introduces a typology of four patterns of formal/informal institutional interaction:

Degree to which formal and informal institutional outcomes converge	Effective formal institutions	Ineffective formal institutions
Convergent	Complementary	Substitutive
Divergent	Accommodating	Competing

The article then discusses the mechanisms behind the emergence of informal institutions, stressing the importance of non-functionalist explanations that: a) identify the relevant actors and interests behind informal institutions, b) specify the

process by which informal rules are created, and c) show how rules are communicated to other actors so that they become socially shared.

The article provides a typology of how informal institutions change:

Source of change	Mechanism of change	Pace of change
Formal institutional change	Change in design of formal institution	Often relatively rapid
Formal institutional change	Change in effectiveness of formal institution	Variable
Cultural evolution	Change in societal values	Very slow
Change in distribution of power, resources	New rounds of bargaining	Often slow, incremental
Updating of beliefs/mechanism for coordination	Tipping	Rapid

Khan, M.H. (2005) Markets, States and Democracy: Patron-Client Networks and the Case for Democracy in Developing Countries, Democratization;12 (5): 705-25 December 2005.

<http://mercury.soas.ac.uk/users/mk17/Docs/Khan%20Markets,%20States%20and%20Democracy.pdf>

This article examines whether democracy is necessary for development (as opposed to being preferable for a host of other reasons), and hence the relationship between markets, states, and democracies in developing countries. It concludes that the evidence is inconclusive: it seems that neither democracy nor authoritarianism is a precondition for development.

A main reason why democracy does not necessarily lead to development is the role and entrenchment of patron-client networks in many poor countries, even those that are formally democratic. The resilience of patronage, in turn, is linked to structural features of the economies in developing countries that make welfare-driven redistributive politics unviable.

An implication of this is that the donor emphasis on democratization in recent years "may be diverting us from more important priorities that may be necessary to achieve the prosperity required for making democracy both more sustainable and capable of delivering real decision-making powers to societies." Instead, "If accelerating the transformation was our objective, these patterns of factional politics should have been the target of analysis".

Keefer, P. (2005) Democratization and Clientelism: Why Are Young Democracies Badly Governed? World Bank Policy Research Working Paper No. 3594

<http://go.worldbank.org/UUEKSYBAN0>

This paper identifies and explains systematic performance differences between younger and older democracies: younger democracies are more corrupt; exhibit less rule of law, lower levels of bureaucratic quality and lower secondary school enrollment; and spend more on public investment and government workers. One explanation for this is that politicians in young democracies are less able to make credible promises to citizens leading them to underprovide public goods, overprovide transfers to narrow groups of voters, and engage in excessive rent-seeking. A variety of tests suggest that this is the only theory that explains the performance of young democracies. The effect of democratic age remains large even after controlling for the possibilities that voters are less well-informed in young democracies, that young democracies have systematically different political and electoral institutions, or that young democracies exhibit more polarized societies.

Kitschelt and Wilkinson (2009), "Patrons, Clients and Policies: patterns of democratic accountability and political competition", Cambridge University Press.

http://www.cambridge.org/servlet/file/store6/item2334066/version1/item_9780521690041

[_excerpt.pdf](#)

http://books.google.com/books?id=oKs6oahqfjoC&lpg=PA295&ots=wsS39_27M4&dq=kitschelt%20wilkinson&pg=PP1#v=onepage&q&f=false

This edited volume describes and explains different forms of clientelistic politics. Its observations are in direct contrast to the usual assumptions of programmatic political competition whereby parties compete for citizen's votes by offering alternative policy platforms. This model ignores the quite different type of patronage-based, party–voter linkage that exists in many developing countries and some advanced democracies. In these systems citizen–politician linkages are based on direct material inducements targeted to individuals and small groups of citizens. Democratic accountability in such a system does not result primarily from politicians' success in delivering collective goods such as economic growth, jobs, monetary stability, or national health care, nor does it rest on improving overall distributive outcomes along the lines favoured by broad categories of citizens. Instead, clientelistic accountability represents a transaction, the direct exchange of a citizen's vote in return for direct payments or continuing access to employment, goods, and services.

The volume comprises a diverse collection of chapters covering different systems of clientelism operating across the world. It argues for more serious study of clientelist

politics and its effects, pointing to the important implications for how international financial institutions should deal with a given country.

Keefer, P. and Khemani, S. (2003) Democracy, Public Expenditures and the Poor, World Bank Policy Research working paper 3164

<http://go.worldbank.org/P32N4L76R0>

The central question addressed by this paper is why competitive political systems often fail to adequately provide the public goods needed for growth and poverty reduction. Politicians often have incentives to divert resources to political rents and to private transfers that benefit a few citizens at the expense of the many. These incentives arise because:

- **Voters have incomplete information.** Voters (especially the poor) are not well informed on politicians' performance. They are more likely to notice expenditure on narrowly targeted goods than the widely spread effects of investment in public goods. Political advertising funded by special interests further distorts voter perceptions.
- **Voting patterns are affected by social divisions.** In countries with sharp ethnic and religious divisions voters identify with politician's from their own group, and will tend to distrust the electoral promises of politicians from other groups.
- **Politicians' promises are often viewed by the electorate as lacking credibility.** Voters tend to regard promises to deliver public goods as lacking credibility because: (1) public goods provision requires greater administrative capacity than delivering narrowly targeted private goods, (2) investment in public goods is hard to observe and politician's can easily back out of commitments, and (3) voters know that politicians may not be in power long enough to deliver on their public goods commitments.

The authors refer to these effects as political market imperfections. They argue that a better understanding of these imperfections needs to be reflected in the design of policy reforms aimed at improving public good provision and reducing poverty.

Analytical Frameworks

DFID, 2009, 'Political Economy Analysis How to Note', A Practice Paper, Department for International Development, London

<http://www.gsdr.org/docs/open/PO58.pdf>

DFID's how to note aims to bring together the diverse literature and tools on political economy analysis within a short and accessible document. It covers the following questions: what is political economy analysis? how and why does political economy analysis add value to development agencies' work? What political economy tools are available? how does political economy analysis relate to other tools? and how should political economy analysis be prepared, undertaken and applied? It includes case studies on how political economy analysis has been used by DFID offices.

Unsworth, S. and Williams, G. (2011) Using Political Economy Analysis to Improve Development Effectiveness, A DEVCO Concept Paper

<http://capacity4dev.ec.europa.eu/political-economy/blog/using-political-economy-analysis-improve-eu-development-effectivenessdraft>

This draft concept paper explains what is meant by political economy analysis, why it matters fundamentally for understanding development challenges and outcomes, and the implications for donors. It also offers practical guidance on how to undertake political economy analysis at country and sector level, and suggests how to draw on the analysis to inform every aspect of EU development activity, including programming, identification and formulation of specific interventions, risk management and policy dialogue. The background paper is complemented with two annexes that present political economy analysis tools to be used at country and sector level.

EC (2011) Draft Country Level Political Economy Analysis, Annex 1 to Unsworth and Williams (op cit)

<http://capacity4dev.ec.europa.eu/political-economy/document/draft-country-level-political-economy-analysis-annex-1>

This annex to the draft concept paper presents an analytical framework for undertaking political economy analysis at the country Level. The framework consists of a list of structured questions to help the analyst investigate key aspects of the political and economic processes at work in a given country context, and to understand relationships as well as assess how they influence incentives and capacity for

collective action, and therefore development outcomes. The framework is intended to deepen EC staff's understanding of the country context and to promote discussion of how EC development assistance can best interact with national political economy dynamics. It is intended to fulfil several operational purposes:

- Providing a better understanding of the countries where the EC works, improving the knowledge of existing staff in country and providing a detailed induction tool for new staff.
- Contributing to the drafting of a more grounded and realistic National/Multiannual Indicative Programme.
- Informing choices about priorities, objectives and expected results for EC support as well as implementation arrangements, and better define linkages between EC interventions and modalities.
- Enabling better assessment and management of country programme level risks and opportunities.
- Informing EC's strategy on country level policy dialogue.

Unsworth, S., Conflict Research Institute (CRU) (2008) 'Framework for Strategic Governance and Corruption Analysis (SGACA): Designing strategic responses towards good governance', Prepared by the Clingendael Institute for the Netherlands Ministry of Foreign Affairs

<http://capacity4dev.ec.europa.eu/document/framework-strategic-governance-and-corruption-analysis-sgaca>

DFID (2004) Drivers of Change, Public Information Note'

<http://www.gsdrc.org/docs/open/DOC59.pdf>

SIDA (2006) Power analysis – experience and challenges,' concept

http://www.sida.se/sida/jsp/sida.jsp?d=118&a=24300&language=en_US&searchWords=power%20analysis%202005

Poole A., (2011) Political Economy Assessments at Sector and Project Levels', How-To Note, World Bank, Washington DC

<http://www.gsdrc.org/docs/open/PE1.pdf>

This how-to note provides a summary of the World Bank's approach to Problem-Driven Governance and Political Economy Analysis. The approach draws on multiple

analytical tools (e.g. stakeholder analysis, analysis of winners and losers, institutional and governance analysis, historical analysis, analysis of rents and risk assessments) and can be applied at different levels (e.g. macro level country assessment, thematic analysis, sectors and sub.sectors, development projects and single operational decisions). The common feature is that the analysis should be centred on a clear problem encountered in the World Bank's work. The analysis typically takes place in four stages:

- Step 1 - Identify the problem or opportunity to be addressed through the analysis
- Step 2 - Map out the institutional and governance arrangements and capacities
- Step 3 - Drill down to the political economy drivers
- Step 4 - Propose recommendations on the way forward (an action framework)

The following reference provides a more comprehensive presentation of the problem-driven approach:

Fritz, V., Kaiser, K. and Levy, B. (2009) Problem-driven governance and political economy analysis: Good practice framework, World Bank
<http://siteresources.worldbank.org/EXTPUBLICSECTORANDGOVERNANCE/Resources/PGPEbook121509.pdf?resourceurlname=PGPEbook121509.pdf>

World Bank (2008) The Political Economy of Policy Reform: Issues and Implications for Policy Dialogue and Development Operations, Report No. – 44288-GLB, Social Development Department
http://siteresources.worldbank.org/EXTSOCIALDEVELOPMENT/Resources/244362-1217517341604/PE_Reform.pdf

The World Bank has also recently published a framework for assessing the political economy of reform that looks at: (a) the reform context (referring to the deeper social and ethnic cleavages, national political and historical institutions affecting the reform under consideration), (b) the reform arena shaped by stakeholders, institutions, and their economic and political interests, (c) the reform process consisting of dialogue and decision-making, champions or coalitions of change, and influence of external actors and (d) a framework for possible actions.

OECD (2011) International Drivers of Corruption: A tool for analysis

<http://www.oecd.org/dataoecd/54/1/49263997.pdf>

This report introduces an analytical tool intended to help users understand how factors in the global economy and international relations, affect governance and corruption at the country level. It provides a means for identifying those factors that matter most for domestic governance, as well as opportunities for international actors to work more effectively to improve governance in specific country contexts.

The analysis follows 4 steps:

Step 1: Understanding the domestic political economy

This first step consists of an assessment of the country situation and domestic political economy. This seeks to explain corruption and other governance failures in terms of the political processes of contestation and bargaining between interest groups with competing claims over rights and resources. The analysis focuses particularly on the behaviour of the ruling elite and other factions who are in a position to challenge the power of the ruling elite.

Step 2: Identifying the international drivers

A list of potential drivers and a set of diagnostic questions help to identify which are likely to be relevant in a particular country context. The seven categories of international drivers are as follows: 1) Sources of rents and unearned income, 2) Opportunities and constraints to conceal and move illicit assets, 3) Foreign investment, 4) Global and regional security threats and responses, 5) International legal measures and sanctions against domestic elites, 6) Reputational pressures on political elites from regional and international actors, and 7) External ideas and skills.

Step 3: Tracking the effects of the international drivers

The core part of the analysis examines the mechanisms and pathways by which each driver affects the domestic political economy and the outcomes for governance and corruption. This analysis distinguishes between the immediate effects of the international driver on domestic political processes (primary effects), knock-on effects on institutions and structural factors (secondary effects) and feedback effects.

Step 4: Drawing conclusions and assessing the scope for action

The final step draws together the preceding analysis with the aim of identifying opportunities for specific programmes and applications of international instruments. The tool has been tested around four country examples (Cameroon, Sierra Leone, Uganda and Zambia) for illustrative purposes.

Noteworthy case studies

Booth, D., Crook, R., Gyimah-Boadi, E., Killick, K., Luckham, R. and Boateng, N. (2005) What are the drivers of change in Ghana? Policy Briefings on Drivers of Change in Ghana 1-5, Centre for Democratic Development/ Overseas Development Institute

<http://www.odi.org.uk/resources/details.asp?id=1322&title=drivers-change-ghana>

Booth, D., Cammack, D., Harrigan, J., Kanyongolo, E., Mataure, M. Ngwira, N. (2006) Drivers of Change and Development in Malawi, ODI Working Paper 261

<http://www.odi.org.uk/resources/download/1318.pdf>

Booth, D. and Golooba-Mutebi, F. (2009) Aiding economic growth in Africa: The political economy of roads reform in Uganda, ODI Working Papers 307, September 2009

to download the paper see

<http://www.odi.org.uk/resources/details.asp?id=3829&title=political-economy-roads-uganda-growth>

For an audio interview/ powerpoint presentation see

<http://capacity4dev.ec.europa.eu/political-economy/blog/political-economy-roads-sector-uganda>

An ODI/DFID study of the political economy of the roads sector in Uganda considered the impact of reforms that took place in 2008, including the establishment of a semi-autonomous National Roads Authority (UNRA) and the creation of a ring fenced road fund. The study concluded that the reforms had not fundamentally changed the nature of incentives in the sector. These remain part of the patronage system for distributing rents and ensuring political support and financing. However, while the overall balance of power and incentives are not favourable to reform, there are many actors with an interest in the improved performance of the sector. The study concluded that the reform process has created some additional room for manoeuvre where development agencies can operate to promote change. A particular challenge is to work to solve collective action problems that prevent individual actors breaking out of established patterns of behaviour. In this respect the study concluded that development agencies can play a vital role acting as a third party to broker meetings and agreements, and help the main players to overcome what would otherwise be situations of stalemate or logjam. It suggested donor action should be focussed on the following roles:

communication about performance in the sector, brokering otherwise missing dialogue among key players, facilitation of countervailing networks of influence, lowering barriers to collective action by private actors, facilitating appropriate forms of 'infant industry' support to local firms, and mobilising influence to enable otherwise blocked organisational transformations.

World Bank (2008) Political Economy Analyses of Two Key Industry Sectors in Dhaka, Part A: Urban Bus Operations, report for the South Asia Social, Environment, and Water Resources Department.

Summary available at: <http://go.worldbank.org/GE377Y6840>

Rampa, F. (2011) Applying the EC's "Governance Analysis Framework" to the water sector in Kenya, Draft, European Centre of Development Policy Management,
www.ecdpm.org/dp124

Keefer, P., 2007, 'Political Economy', Section 4 in: Ghana: Meeting the Challenge of Accelerated and Shared Growth, Country Economic Memorandum Ghana, Volume III: Background Papers, World Bank, Washington
<http://go.worldbank.org/SRAJRXUHV0>

This extract from the World Bank's Country Economic Memorandum of Ghana provides an illustration of Philip Keefer's approach to analysing the effects of electoral competition and clientelist politics on public expenditure allocation.

Utomi, P., Duncan, A. and Williams, G. (2007) Nigeria - The Political Economy of Reform - Strengthening incentives for economic growth, The Policy Practice Ltd
<http://www.thepolicypractice.com/papersdetails.asp?code=10>

Growth and competitiveness in Nigeria have been held back by poor policy choices and weak government. This paper argues that these failures are fundamentally linked to problems of incentives rooted in institutions and the political economy. Most importantly these include the lack of public accountability arising from the use of oil revenues, weak state-society relations, patronage politics, a personalised rather than institutionalised policy process, the ever present threat of conflict, and value systems that have promoted short-term behaviour and opportunism. All of these conditions have created a disabling environment for private sector led growth. Against this background the purpose of this paper is to enhance understanding of: (a) the impact of ineffective state institutions on Nigeria's growth performance, (b) the political economy

of growth and the factors that drive economic policy making in the country, and how robust the process is; and (c) how the country can move from patronage and individual-based policy making to robust institution-based reform to facilitate sustainability.

Using Political Economy Analysis

Duncan, A. and Williams, G. (2010) Making development assistance more effective by using political economy analysis: what has been done and what have we learned? The Policy Practice Ltd

<http://www.thepolicypractice.com/papersdetails.asp?code=16>

Politics often explains where development assistance has been effective and where it has not. Yet, until the 2000s there has been little focus by development agencies on political issues. This has begun to change with political economy analysis now being more systematically used by development agencies to understand the real world. Much valuable work has been done in recent years in developing new analytical frameworks, generating fresh insights and applying these to problem-solving. Nigeria and Bangladesh are two positive examples where PEA has demonstrated its analytical and operational usefulness. Much remains to be done in these countries and more widely, to ensure stronger uptake of political economy analysis. On the supply side this includes getting the 'product' right, and better communicating the message. On the demand side, there is a need to take more account of the incentives facing development agencies and to gather more systematic evidence on the operational impact of political economy analysis to date.

Beuran, M., Raballand, G. and Kapoor, K. (2011) Political Economy Studies: Are They Actionable? Some Lessons from Zambia, World Bank Policy Research Working Paper 5656

<http://go.worldbank.org/GDNDNORQH0>

In recent years, the number of studies looking at the effect of politics on economic outcomes has flourished. For developing economies, these studies are useful to better understand why long overdue reforms are not implemented. The studies analyze the overall context within which reforms are being implemented and the underlying incentive framework. However, it seems difficult to make such studies actionable, especially in sectors where donors have a heavy presence that can sometimes distort incentives in addition to the reluctance from some governments to amend the existing systems in place. This paper focuses on some conclusions emerging from the political economy diagnostics carried out in Zambia in various sectors in recent years. Based on interviews of World Bank task managers, the paper attempts to assess the relevance of these studies for the implementation of projects and the policy dialogue and draws lessons on how they have influenced the implementation of the World Bank's support to programs in various sectors in Zambia as well as the main challenges for this type of exercise.

Desai, R.M. (2011) An Evaluation of Political-Economic Analysis in Support of the World Bank's Governance and Anti-Corruption Strategy

http://ieg.worldbank.org/content/dam/ieg/gac/backgroundpapers/gac_eval_political_ec_on_analysis.pdf

This critical evaluation of the World Bank's use of political economy analysis draws the following conclusions:

- Political analysis was and is thinly and inconsistently applied [in Bank operations].
- The rigour and quality of political analysis was uneven, partly as a result of the lack of a common definition of what constituted "political economy".
- Better operational, sector- and project-level political-economy guidelines are needed.
- The demand for free-standing, political-economy assessments by country teams is likely to be low.
- Far more promising is the practice of providing political-economy "inputs" to Economic and Sector Work (or Country Assistance Strategies).
- The gap between the perspectives of political-economy experts and of operational staff remains wide.
- The recommendations of existing political analyses tend to be highly conventional.
- [Most of the Bank's] political analyses ignored the role of donors.
- There is little downstream political-economy support [during programme implementation].

Hazenberg, J. (2009) The SGACA experience: incentives, interests and raw power - Making development aid more realistic and less technical

<http://e-mdf.nl/projects/dprn/backgrounddocuments/The%20SGACA%20experience%20Goed%20Bestuur.pdf>

Schakel, L., Hout, W., Slob, A., and Smith, D. (2010) The Use of Political Economy Analyses in the Governance Sphere - ECORYS Research Programme (ERP)

www.ecorys.com/rapporten/research-programme-2010/the-use-of-political-economic-analysis-in-the-government-sphere/download.html

Davis, P. (2011) The Political Economy of Business Environment Reform: An Introduction for Practitioners, Donor Committee on Enterprise Development DCED

<http://www.enterprise-development.org/download.aspx?id=1715>

This overview discusses the relevance of political economy analysis to private sector development issues, and identifies with the aid of case studies the typical ways in which political processes affect the business environment and conditions for reform. It describes the main political economy analytical tools available to private sector development specialists and offers practical guidance on their use.

Copestake, J. and Williams, R. (2012) The evolving art of political economy analysis: Unlocking its practical potential through a more interactive approach, Oxford Policy Management Development Futures paper.

http://www.opml.co.uk/sites/opml/files/OPM_DF_political%20economy%20analysis.pdf

Development practice entails operating in increasingly complex and uncertain contexts to build and sustain relationships between stakeholders who often have sharp differences in commitment, capacity and outlook. Increasingly, political economy analysis (PEA) is being used by development agencies to respond to this challenge. However, the potential of PEA to inform more radical reform has yet to be realised in full. Doing so entails converting detailed analysis into concrete action at the same time as being more open about the political economy of how development agencies and practitioners themselves operate. This paper sets out a framework to address this challenge. This means shifting from an ‘intervention’ to an ‘interaction’ model of action that builds on the micro-politics of Machiavelli as much as the macro-politics of Marx. It entails using PEA in ways that are more problem specific, reflexive and agile.