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BOOK REVIEW

Timothy Besley, Torsten Person: Pillars of prosperity: the political economics of development clusters

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Claudia R. Williamson

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What determines prosperity? Countless social scientists have pondered this question offering possible answers that range from complete public planning to self-governance to an infinite combination of both public and private provision of governance.

Inspired by the famous Adam Smith quote, "Little else is required to carry a state to the highest degree of opulence from the lowest barbarism, but peace, easy taxes, and a tolerable administration of justice, all else being brought about by the natural course of things" (1755), Besley and Person describe three pillars of prosperity—fiscal capacity, legal capacity, and lack of conflict. These three pillars provide the foundation to explain within country (not necessarily across country) development clusters—strong correlations between types of government institutions, political repression or violence, and a country's level of income. For example, poor countries tend to suffer internal conflict, political repression and weak state institutions.

Understanding what creates a strong effective state is the key ingredient in the framework. The core model is a symmetric two group, two period model with a macroeconomic focus. The ability for a government to easily tax its people (fiscal capacity) and to limit public and private predation (legal capacity) is the basic framework for the analysis. The authors emphasize institution building as opposed to policymaking where current policies are limited by past investments in fiscal and legal institutions. In addition, the idea of complementarities is also a key point. Investment in fiscal capacity, for example, reinforces and incentivizes subsequent investment in legal capacity. The core model illustrates this complementarity between the extractive or taxation aspect and the productive or market supporting role of the state. Two main forces determining the effectiveness of government includes political institutions and natural resources (including foreign aid).

Once the basic setup is derived (Chapters 2 and 3), the authors proceed by extending the core model to include the determinants of political violence—the third pillar. The transition

C.R. Williamson (✉)
Development Research Institute, Department of Economics, New York University, 19 W. 4th St, 6th floor, New York, NY 10012, USA
e-mail: claudiawilliamson@gmail.com

of political power is endogenously determined by the potential for conflict, which depends on the level of investment in violence by the incumbent and opposition. In turn, these investments depend on the cohesiveness of existing political institutions and the demand for public goods. As before, the level of natural resources and foreign aid can alter the pay off to these investments.

Chapter 5 completes the analysis by endogenizing all three pillars to derive a 3×3 state space matrix combining state capacity with determinants of conflict: common-interest, redistributive or weak states with peaceful, repressive, or civil-war states. A country's location in this matrix describes its development cluster explaining the level of income, conflict, and type of government. Chapter 6 extends the role of external rents by further analyzing the role of foreign development assistance. While the authors maintain that aid could have some positive impact such as increasing fiscal capacity, most of the results point to a destructive role. For example, foreign aid can decreases investment in state capacities and increases the likelihood of political violence as the return to maintaining power is increased. Chapter 7 offers a variety of avenues for political reform including constitutional rules and the importance of trust and social capital for effective governance. Chapter 8 summarizes the findings and includes a Pillars of Prosperity Index derived for each country.

The book is an outgrowth from a series of lectures sponsored by the Yrjö Jahnsson Foundation in Finland. The target audience of the book is graduate students and advanced researchers interested in the political economy of development. The approach is highly technical and lacks conceptual, intuitive support for the model and many of the subsequent assumptions. Each chapter is designed to be a stand alone chapter and follows the same set up where the core model is derived, some extensions are applied, data and empirics are used to provide basic support for the theory, and a summary of the existing literature is provided.

Given the aim and structure of the book, its contribution can be interpreted as narrow. Graduate students interested in the intersection of politics, economics and conflict can benefit from having the book as a resource as the authors provide a core model that can be extended in a variety of new ways. Also, the summary of the existing literature provided at the end of each chapter is especially valuable for researchers.

While I appreciate the mentioning of relevant literature, I find it a bit odd and frustrating at times that the authors do not include many of these key findings into their own analysis. The most glaring oversight, from my perspective, is the role and importance of self-governance, or Adam Smith's 'natural course of things.' Private provision of key institutions such as legal and property rights institutions and private provision of public goods is well documented (see Powell and Stringham 2009 for a summary of the anarchy literature).

The first sentence of page 1 states, "Almost all economic analyses presume the existence of an effective state." However, that does not mean that it is the appropriate starting point. Rajan (2004) argues that, especially in the context of development, our starting point should be to assume anarchy, as this is a more accurate depiction. By doing so, it also becomes apparent that many aspects of governance that gets attributed to state institutions may perhaps stem from private governance.

A subset of the self-governance literature is the role of culture and development, a subject the authors acknowledge that they ignore. However, the importance of norms and values is becoming increasingly important, as many scholars have identified possible mechanisms through which culture matters. This includes direct economic effects and indirect effects such as altering the effectiveness of both political and economic institutions and affecting labor market participation rates (see Guiso et al. 2006 and Licht et al. 2007). This implies that before an effective state could possibly exist certain cultural norms may be a necessary prerequisite providing the bedrock for the other pillars to stand.

Secondly, the model does derive conclusions based on the assumption that political leaders face their own incentives that may not align with public interest and include the possibility of a predatory state; however, this viewpoint can be extended by incorporating insights from the literature that typically falls under the umbrella of public choice. For example, state institutions may be designed to maximize political and not economic return. This could lead to efficient administration or to inefficient, entrenched, budget maximizing bureaucracies depending on the context. As a consequence, the extractive aspect of the state (taxation) may increase, as it is politically beneficial to ensure efficient fiscal capacity, while the productive capacity could decrease (poor property rights and contracting institutions). This suggests the possibility of a substitution effect instead of a complementary relationship between state capacities.

This leads to my final area of criticism. Behind each model and explanation of the findings is an implicit assumption that we have the necessary knowledge to design an effective state and subsequent policy as long as we can overcome the incentive problems (which alone is a tremendous task). This oversight is disheartening as Hayek (1945) illustrated how government planning inherently suffers from lack of knowledge. More recently, Easterly (2006) applies Hayek's insights to international development. Easterly's development paradox illustrates that development is not a technical problem with technical solutions—it is a process involving unpredictable bottom-up successes and failures that is achieved without any one person having a comprehensive plan.

Overall, I appreciate how the authors endogenize many key development components that are typically assumed to be exogenous or completely dismissed. The most interesting conclusion is the emphasis that foreign aid will more than likely lead to destructive (not benign or welfare enhancing) consequences. Future researchers in the aid community can benefit tremendously from this aspect of the analysis.

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