

The Micro-Dynamics of State Formation
An Exploratory Workshop
on
Strategies for Thinking about Effective & Accountable Institutions in Fragile States

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Summary of Proceedings

selections

(List of Contributors appears at the end of the proceedings.)

The purpose of this workshop is to engage university scholars in thinking about the tough challenge of building effective and accountable institutions in fragile states. Practitioners have often taken the lead in this subject matter. The question at this meeting is whether scholars have observations that might lead to new understandings or approaches and possibly to innovative policies. Princeton has brought together a small group of people who have already made some intellectual contributions and will continue to do so. The Bobst Center has also included a number of younger researchers who are just beginning to develop research agendas and will become the next generation of leaders in this area.

[The meeting proceeded through memoranda and conversations. Some of the memoranda appear in a separate consolidated document. This note offers a summary of insights drawn from the discussion.]

Background

Philip Keefer launched the conversation. He observed that most of the discussion would focus on micro-interventions in fragile states, but he urged the group to begin by stepping back and talking about the macro picture. Fragile states are like many other developing countries in that the political incentives for good government are weak and capacity is constrained. However, in fragile states these

problems are especially severe. There are many unknowns, including the characteristics accountable states must have, strategies for delivering services and generating growth when capacity and accountability are extremely low, and the connection, if any between short-term service delivery fixes and long-term accountability.

Aid donors have not performed especially well in designing responses to the challenges fragile state governance poses. East Timor had a legacy of civil war, along with oil and a history of inter-clan violence. The main political grouping was not an institutionalized political party. Donors relied on the new government for service delivery, relied on elections for delivering legitimacy, and focused on institution-building in the public sector. The outcome? Corruption and no services, unemployment and a collapse in GDP. The country came close to a relapse. In Southern Sudan, similarly, the donors pondered what to do in a post-conflict setting with a history of violence and proximity to significant natural resource rents—oil, again. As in East Timor, the donors emphasized creation of government institutions, such as a judiciary, and sought to build roads. The result was no roads and a lot of corruption. The point is that a strong of well-delivered donor projects may not lead to accountable states.

Countries vary in the information people have to judge political performance, in political credibility and political incentives to invest in credibility, and in the degree to which partly exogenous issues, such as ethnic strife, nationalism, etc. shape incentives and strategies.

It is possible to think about the problem as one of political market failure. We tend to think about elections as devices for building accountability: Politicians make promises to voters. However, poor democracies can be less responsive to non-elite interests than poor autocracies. Why? Information is scarce in both settings. But where politicians need to make promises only to a narrow group of voters they tend to privilege private goods instead of public goods and engage in rent seeking. Young democracies are especially prone to credibility problems. They have had less time to build up trust. Countries with more continuous years of competitive elections tend to have lower deficits as politicians spend less on patronage or corruption.

Second, where a country has programmatic political parties, we are more likely to observe politicians making broad promises, as well as submitting to legislative discipline. These kinds of parties are particularly absent in fragile states.

Third, in some instances autocrats may make credible promises to publics too. They may allow potential investors to coordinate by sharing information and acting on their own initiative. They may permit other ways for members of society to coordinate against the ruling party. We have seen this pattern in China recently. Arguably the military in Indonesia and Chile did the same for a period, and the bureaucracy did so in Singapore. For a time the donors thought they had another case in Uganda, where President Museveni initially championed reform, but as the government increasingly limited competing parties and other points of coordination, rent seeking increased and economic indicators started to fall.

What are the consequences of ignoring accountability? These are obvious. Projects and policy reform are less effective and long-term development slows.

How is it possible to secure better service delivery or more accountability in these contexts? There are three broad possibilities. The first is to by-pass the government. The rationale is that the demand for services is huge in fragile states but the political interest in delivering services is low. Second, where political market imperfections are not extreme, it might be possible to build the capacity of the government. However, this approach slows the roll-out of critical services and there is no evidence that it works when the political market imperfections are huge. Finally, consider “second best” approaches, such as direct distribution to citizens.

State-building is fundamental to medium-term success, of course. But a focus on public administration is not enough and may not be possible. Elections are not enough, either. Focusing on the government in power is not enough. Focus instead on the credibility of political actors and how to design an approach that provides incentives for the right kinds of promises. Political organizations must be associated with promises to deliver public goods and with fulfillment of those promises. What does this mean? My speculation is that the answer is information, information, information. People need more information in order to monitor performance. But further, political systems need third parties to limit clientelism. In two recent cases, the World Bank or other bi-lateral donors have played the third party role: donor-run adjudication of disputes about the use of money in KDP Indonesia and Australian assistance in New Guinea.

Questions and comments focused on several issues. 1) Is there a difference between making credible promises and having credibility? 2) Outsiders want these processes to happen quickly but sometimes these changes just take a long time. Shortcuts aren't always possible. 3) Is the challenge, figuratively, to get the mafia to pass out turkeys or is it to transform the mafia into something else?

Politician-friendly strategies? Behavioral economics

In a recent and much-cited article, James Robinson suggested that the strategies for improving service delivery outlined in the 2004 *World Development Report* were ultimately futile efforts to engage in “politician-proofing.” He pushed policy makers and scholars to consider what kinds of “political equilibria deliver services to the poor.”ⁱ

Chuck Cameron offered a twist on this critique. He suggested it may make more sense to explore politician-friendly strategies for improving service delivery and responsiveness—to link service delivery to things that are valuable to politicians. This approach may require ways to enable easy and credible credit-claiming by politicians, along the lines of patronage. Design of such systems requires a lot of local knowledge. The politics of service delivery varies across jurisdictions because the characteristics of service vary. There won't be magic bullets.

An example of a politician-friendly system that worked is the early postal system in the United States, 1820-1830. At the time the largest employer was the U.S. postal system. 70-80 percent of federal employees were employed in the postal service. The U.S. had some of the characteristics of a fragile state today. But by 1860, most of the U.S. population was covered. Why? This is a case of the transformational impact of information, perhaps. There was an interlocking relationship between the USPS, the stage coach service, and the press at the time. Politicians wanted to send mail to constituents, since they couldn't communicate by phone or email at the time. They acquired franking privileges. They wanted the post to work. But this was a huge subsidy to independent newspapers too, and this was the critical bit. More information began to flow. De Tocqueville observed the access to news in 1831 when he visited. The system was politician-friendly but it also made accountable government a feasible prospect, by improving the availability of information. Its existence changed the environment of politics in a way that eventually produced stronger incentives for accountable performance. By the way, contractees the delivered the mail and secured their contracts through an elaborate and competitive bidding—for example, if you lost you had to sell all your equipment to the winning bidder.

The basic idea in the literature on institutional design is to think very hard about incentives. Organizations are systems of incentives. People within the organizations respond vigorously to incentives that are put to them. The literature also uses the metaphor of contracts. Think of a contract as being design of a standard institution. There have to be incentives such that the person who is supposed to sign the contract will actually do it. This gets back to politician friendly part of my claim. Politicians won't enter into contracts that don't serve their interests. A successful institution is one that aligns these interests through auditing and monitoring schemes, bonuses, etc. The literature on these kinds of things offers no major policy bullet points, but does provide tools for thinking about incentive systems.

Avinash Dixit picked up Cameron's challenge, suggesting a kind of conceptual framework in which a number of these issues can be analyzed. Incentives are crucial in designing institutions. "What I want to suggest is that the framework should be a merger of political economy. Different kinds of regimes--democratic, authoritarian, etc.—shape the way incentives translate into political success or failure for the top level leaders. The idea of incentive theory is that you have to give some resources to the agent in order for the agent to take the right actions, and how far you compromise from the ideal depends on your willingness to provide rents or premia. For an autocrat, the rent given to an agent is out-of-pocket; for a democrat, the rents come from somewhere else. Therefore one might suggest that autocrats would be willing to accept the worse outcome. Democracies are more likely to be constrained by ideas of social welfare. Accountable rulers are better at providing public goods, more willing to sacrifice rent.

It is important to build on organization theory. However, one caution deserves mention. In economics we used to assume everyone was selfish. Now economics contemplates altruism and political science doesn't. Political scientists assume everyone is selfish and the only thing stopping them

from going astray is institutional design. Yet it is clear that some leaders are genuinely concerned. We need to take these differences into account and we need to allow for behavioral considerations to enter analysis. It is also important to take into account organizations or networks that may provide incentives for “doing good,” including professions and even universities (for example, Princeton in the Nation’s Service). The assumptions underlying incentive systems don’t always hold. Self interest may not always prevail. There must be room for other kinds of calculations (including envy).

Finally, Dixit offered comments on the direct provision of services. We may also have to face up to the fact that there will always be a certain level of corruption. There are lots of cases where it will be necessary to give money to ‘the embodiment of empowerment,’ even they steal. We may have to accept that there will be some ‘carrying charges.’ This fits in with more general idea of making politics, politician-friendly (and business and media friendly). Finally, in distributing aid, how do you select the cases you work on? Contractors might not be corruption free. Is it better to deal with local providers on the take --- or Haliburton?

Anne Swidler offered two additional remarks. Patron-client ties are important as a solution to an insurance problem. In fragile states life is characterized by unpredictability. If something goes bad it is vital to draw on the social obligations that patronage helps to create. Everyone has to generate those ties and sustain them.

In terms of culture, in places where incentive structures keep people behaving well, there is a sense that the structures or rules embody sacred meetings, cultural meetings. One of the fascinating intellectual questions is what the cultural stuff is doing there. Chiefs who behave responsibly believe it’s incompatible with their culture to behave inappropriately. In Joseph Kalt’s study of American Indian communities, the conclusion was that if the government system looked like the community’s historical system of governance, then it worked well – if it didn’t, it didn’t work well. The shamans also ran a successful system. Ask the shaman ‘why didn’t you appoint your son to run key service?’ and he will say, ‘I’m ashamed, I couldn’t do that.’ Trying to get ways that cultural meanings sustain incentive systems.

Other participants offered a variety of examples, observations, and questions.

1. Constituency development funds in Kenya and Tanzania are possible examples of a politician-friendly strategy. MP’s passed a law creating constituency development funds. These are wildly popular both for MP’s and among locals. Basically 2.5% of the budget is allocated to constituencies. In each constituency, the money is distributed by a committee headed by an MP. In theory the politician whose committee allocates money to projects from which many benefit is more likely to win re-election. This begs the question of why the Kenyans been able to pull it off, a politician-friendly system that services the people. Most obvious answer is you’ve got an electoral system that serves both.

In Mexico there was a similar system under the PRI. A politician had to be a good enough patron to mobilize people. People would volunteer to build a building hoping to get a teacher.

2. It is worth thinking about the kinds of political equilibria that allow politicians to be less self-regarding. Sometimes shamans are good, sometimes they are bad. Incentive theory talks a lot about career structures, non-monetary incentives. That said, the importance of local knowledge, networks, etc., building things that mesh with these, all these things are absolutely crucial. We should be a little wary of thinking that patronage relationships are substitutes. Feudalism is a relationship of mutual obligation too. The Madisonian answer is to tie the interests of the individual to the interests of the institutions.
3. One needs to distinguish two types of things, enforcement of property rights and enforcement of contracts. What happens when there is no law? What difference does that make? Networks are a second-best solution for enforcing contracts. Enforcement property rights is much harder than enforcing contracts. Private enforcers of property rights usually end up being expropriated.
4. One might look at postal services as key indicator. They are much less politically charged than health care. In Africa the history of the postal services is also interesting. Lumumba got his start in the Post Office. In Tanzania, under structural adjustment, post offices shut down. The World Bank has a long history of restructuring post offices.
5. There may be reasons to be concerned about politician-friendly strategies of some types. There are several programs to re-introduce traditional authorities on the ground – not always a good idea.—as well as pork barrel programs and money attached to constituencies. An important question is whether these systems promote a more factionalized system of politics.
6. Pay attention to selection and screening mechanisms. Some time ago there was some really nice work on the characteristics of successful school superintendents in Wisconsin. It found that success and failure was completely random. What was important was that the system functioned in such a way that competent people were selected. Selection strategies necessarily vary depending on the kind of position one seeks to fill.
7. It may matter who keeps the balance sheets.
8. Do some systems produce leaders who are more other-regarding? How can we configure institutions to generate “good guys”?

Field experiments on accountability

Macartan Humphreys led the second session saying, “The question is what will make it more likely that politicians will use public office to achieve public benefits rather than private gains?” There are families of answers: 1) reforms to change rules of the game, 2) efforts to import institutional strength, and 3) initiatives to change the fundamental distribution of power. Consider some examples.

Oil in Sao Tome. In Sao Tome, Fradique de Menezes issued a challenge. If Chevron offers me \$1m for favors, he said, you can be sure I will take it. I want to see institutional solutions that will

prevent me from taking money like that. He wanted a good set of laws so that future politicians wouldn't steal. There are credibility issues involved as well. Politicians are concerned that when the next guy comes in he'll spend the money differently than you would have. In principle this problem could be resolved if there was a way of ensuring future government expenditures would be moderate.

The challenge for us, as researchers, was to help design institutions to make sure money was handled well. Sao Tome could do a lot of things: public information & debate; joint control & oversight, caps on expenditure, integration with budgets; prioritize sectors. But any rule can be broken. There are costs to breaking rules and changing rules. Making something a law gives it a special status, but if the rules are broken, rule of law could be undermined more generally. Could require conditions for withdrawal (timing, multiple signatures), constrain the form of transfers, and demand approval of withdrawals.

[Comment from floor: Oversight committees may be a middle class phenomenon. In South Africa, where community policing includes oversight committees, the committees work well in middle class areas but not in poor areas. Where external mechanisms work for inducing greater accountability they do so in interaction with internal mechanisms.]

The second example comes from some research in Sierra Leone, Liberia, and the Democratic Republic of the Congo. In this case, the idea was to enable communities to decide how to spend money and to provide some training as well. Sometimes these bypassed local power structures. The hope was to build collective action capacity so that communities would be better able to engage the political process. The early phase of the projects established a baseline. We said we would come back in 3 years to find out whether these programs successfully built capacity. We also created treatment and control groups. And we varied the treatment. The concern behind the project was partly the fact that despite the enthusiasm for participatory processes, very often manipulation by leaders is very high. This work is on-going.

The third experiment concerns transparency. Models of political selection suggest that high quality politicians are more likely to enter the electoral contest if people are well informed. We worked with the African Leadership Institute (David Pulkol) to develop scorecards for MPs in Uganda. The country had a real problem with absenteeism among legislators. The scorecards rated the MPs and reported absenteeism levels. We also sponsored workshops where the MPs could defend themselves. The motivation for the project was largely theoretical, but even before we began, in anticipation, absenteeism began to decline.

This kind of problem points up the need for multiple organizations to reinforce the power of the committee that is most central. The neat thing about a scorecard, like the one used in Uganda, is that it interacts with parliamentary incentives to help build capacity and strength as long as there are NGOs to publicize and comment on the results. The MPs changed their habits in anticipation of what the system would show. Shame is an important driver for some but not all. (In Bangladesh the newspaper printed

the names of all those who hadn't paid their electrical bills, but the socialites liked having their names on the list. However, a powerful incentive in Bangladesh is how to toe the line to get hired by the UN).

There are a number of worries associated with this project, including some concerning adverse selection, manipulation of influence measures, and rejection of the treatment. Transparency could foster collusion, more conformism, and grandstanding. We are also concerned about spillover effects.

Some thoughts on theory as these projects come to completion...

- 1 Sometimes theory provides contradictory predictions.
- 2 Insights from behavioral economics have not yet played a role in this research with a few exceptions.
- 3 Experiments and microdynamics might not be appropriate for macrophenomena like statebuilding, which happens at a higher level.

It is very important to pay attention to politics of implementation—to the problems sketched in *Yes, Minister*.

Meeting participants offered several observations.

1. Who pays attention to scorecards may make a difference in the effects the scorecards have. Uganda is 87% rural, scorecards being discussed amongst the chattering classes – irrelevant to Museveni's base.
2. A big challenge is to find out whether the findings are robust to changes in setting. One can imagine many variables that differ dramatically. This is a problem with all micro-experiments, not just field experiments. A number of responses are possible. We can get some handle on issues by examining within case variation. For example, does this treatment change with higher levels of wealth/higher levels of conflict? Almost certainly a contextual factor that hugely shapes outcomes is the prior level of cohesion/political system.
3. There are some publication biases in this type of work. Non-results aren't published. It is easier to stand by non-results when you've got a strong framework. There is also site bias; partners will partner with you in situations where they know what the outcome will be.
4. The organizational context shapes the effects of things like the report card system. The neat thing about scorecards is that they represent an attempt to systematically measure capacity in parliament. They are going to point in the right direction. The big question is what difference does it make? Civil society, which hasn't been mentioned much, press and civil society come into the mix here in terms of interaction with parliament. There may be some positive externalities in this case, as in the postal system example earlier.

5. Shame is such an important driver in this instance. Does that port well to other settings? FYI, it turns out that people secrete hormones in their saliva when they feel ashamed. Maybe the feeling is universal, but perhaps not in response to the same stimuli? [Another meeting participant observed that In Bangladesh, newspapers posted delinquents on electricity bills, and on cocktail circuit it was a mark of pride to appear on the list. A third participant remarked that the Stockholm School of Economics coffee lounge had a wall where faculty were invited to post articles they had published in the past five years, as an incentive to research productivity.
6. The external validity issue could lead to some creative thinking about whether a given intervention will work or not given institutional context—something along the lines of the varieties of capitalism literature. Begin by thinking about which kinds of field interventions would work where. Any strengthening of an institution might be a result of strengthening a number of institutions.

General observations drawn from discussion of particular cases

[Please see the memoranda for short presentations of the cases under discussion. These notes do not reproduce the talks.]

In the 2004 World Development Report, principal-agent problems were central. The hardest problems arise when a function is very transaction intensive, hard to monitor, and we can't specify exactly what the person should be doing. We wanted to address this issue in policing, which is where the hardest problems arise, but the legal department would have none of it. In the context of weak states, I would go so far as to say that if policing works, other things will. See Voices of the Poor study. Some observations:

- 1) Information to the public would be important, though it is not an unambiguous part of the solution. In Calcutta's brothel district, the sex workers had complaints about the police. An NGO came in and the workers were organized. They staged demonstrations. Abuse diminished.
- 2) In Bangalore, public rating systems (surveys) of agencies did seem to yield improvement for all services except police.
- 3) It is important to have a place to complain to. The appropriate vehicle may be very context specific. In India, for example, it is complicated by caste distinctions.

It is also important to pay attention to what is monitored and who does the monitoring. In Los Angeles, the public said it wanted more arrests but it was important also to lower the number of complaints against the police. The complaints dropped but crime rates went up.

1. Police are usually relatively more immune to the embarrassment factor. In the US, much seems to depend on what gets monitored, how easy it is to monitor, and how much trouble the policeman gets into if he violates the rules. Designing a good contract for police is no picnic.
2. The other side of designing a contract is selection and recruitment, what are the kinds of contracts offered so as to attract the kind of people you would want to be on police forces. You want somebody who's kind of tough, but not too brutal. [From another participant: When Liberia went to recruit a new army the only requirement was no prior military experience.]
3. South Africa experimented with community police forums. The experience has varied. They have vague mandates and problems maintaining community interest. CPF's played a productive role in middle-class areas, where members of community forums were better able to play the role of monitors. However, simply creating these CPF's was of enormous benefit to overcoming communication problems. One concluding point, existence of these external mechanism should not be read as reducing the importance of internal management. Saying that CPF's have not been productive at directing police, is not the same as saying that it's not worthwhile to having police interacting with community. For external mechanisms to be effective, there must be internal mechanisms to respond.
4. The institutional side seems to preoccupy police reformers. All western countries rely on people going to police stations to say they are victims of crime. But if people are afraid of the police, they won't do that. Mexico also tried to engage people in police reform. They asked people for information about police behavior and performance. Crime victimization surveys are a poor second best and are not useful for monitoring performance unless highly disaggregated.
5. There is emerging evidence of terrible performance by private police in Afghanistan. Public-private provision is very central in fragile states. Vigilante groups deal out rather rough justice. But the way the Tanzanian state engaged with them is to parent them, give them quasi-legal status. One is talking about the reality of policing. That phenomenon becomes important. The problems posed in the South African case are quite different
6. We have focused a lot on selection mechanisms, but there is strong evidence that whoever goes into an organization will be transformed into what was there before. These organization cultures prove to be difficult to reform. Roosevelt got his start in politics by attacking New York police corruption. Police forces founded in the Progressive Era on the west coast still look quite good. The question is what do we do with this observation? Talking about information strategies does not get to the core of the problem.
7. You have increasing crime rates in all transitional countries. You have huge increase in crime rates during this transition period. Why? The party was engaged in policing earlier. In the transition, it is possible that political factors push the crime rate up either because the

institutions that really controlled crime have weakened or disbanded or because police are taking sides or for some other reason. There is some relationship between political institutions and policing that would be interesting to investigate.

8. In a transitional context, the transition offers the opportunity to reconfigure the military, but not the police. Invariably one has to create one's police force from scratch. The South Africa model is that of the western professional public police – maybe not so relevant to every African context. Integrating community based systems into a police system, would seem that that would necessarily be part of what you wanted to do. At the end of the day you would need to constitute some kind of public core type of agency, partly to police these other kinds of structures. I think it was partly also in some ways the culture of these agencies.
9. Perhaps it is useful to turn to recruitment in rebel organizations. Depending on package they provide to agents, may be able to figure out which agent is good and bad. If you offer material award, attract opportunists. Apply logic to police recruitment. Relates recruitment pool to organizational culture. Have a particular kind of organizational culture. Different ways of thinking about selection and recruitment strategies.

The focus shifted to other kinds of settings, outside police services, a conversation led by David Leonard. In Kenya, there was an effort to address problems in veterinary services using tools of the new institutional economics. It was found that the poor received more if they had to pay because if they aren't paying, they usually have to use social connections to get benefits, and they have even less in the way of social connections than income. Contracting out proved very difficult, though. It was essential to have an institution that could assure quality. In Africa, overwhelmingly, church-delivered care is better because the church provides oversight. Value driven non-profits can be helpful in this regard. They have a stake in quality. They don't win converts if they don't deliver. Without these groups you just get a race to the bottom. Observations made during the discussion included the following:

1. In Somalia, NGOs have taken over vet services. This is privatization in the extreme. Farmers want to export livestock but now they confront international health standards so they need someone to sign off. This kind of institution is fundamental to the economy.
2. Professionalization shouldn't be under-estimated either. It is useful where immediate face-to-face contacts are uncommon. In vet services there is a big incentive to pay a bribe to get a vet to back off. Why doesn't the vet succumb? Professional ties.
3. The institutional structure within which markets exist matters. Do we know how behavior will change as context changes?
4. It is important to have responsiveness but also operational autonomy. A quack is responsive. Accountability means insulation of practitioners from direct demands of the client.

5. Contract is important to Somalis—perhaps more fundamentally important than to the citizen of a western society. Everything is bound up around contracts. However, contracts are not rooted in the individual, but in the family. In Somalia you have to belong to a diya paying group – like an insurance policies. It would be crazy to try to survive without belonging to a diya paying group. Obligations are group-based, and contracts are enforced because groups enforce contracts. The other vehicle for part of contract enforcement is reliance on Islamic courts, where one can resolve personal and business disputes. Parties have to swear on the Koran. It is important that people believe they are going to hell. This doesn't really work in the US. It is extremely important that partners are active practitioners of the faith. If they aren't, they can't know that a party won't renege on the deal.

6. The US is the exception, not the Somalis. Avner Greif's community responsiveness system (analysis of the merchant influence in city states) is a bridge between relation-based contracting and larger systems. Hong Kong in the 1960s and 1970s was arbitrating between rule-based systems in the West and relations-based systems in the East.

7. We should be thinking about what kind of system is better for what type of contract enforcement. If contract enforcement is perfect, then markets are great. Beyond a certain level of difficulty in contract enforcement, firm structures might alter (Coase) and at some point, the public sector becomes the best provider but the performance of the public sector will never look so good because the context is rough.

8. Dinissa Duvanova offered observations on civil service reform, based on her work in Eastern Europe. Many of the countries of Eastern Europe now seek to create bureaucracies on a Weberian model. Paradoxically, they long managed weapons and put satellites into orbit but now find themselves incapable of overseeing rule enforcement in a capitalist economy. A number of state services have survived. Law enforcement, customs, and education have grown corrupt. They enforce the rules against some but they collude with criminals on a selective basis. In the 1990s, in Eastern Europe there was a changing perspective on what the state was supposed to do. The proposed reforms in the civil service were all designed to build meritocratic, professional systems. In places like Kazakhstan, civil service reform was introduced, but during the reform the quality and capacity of the civil service decreased and corruption rose. What was happening? Politicians did not want the programs to succeed. As a result of their intervention, political authorities now have more control.

Tim Frye introduced the third case under discussion. Private protection organizations produce, promote and sell protection (Gambetta, 1993). States and private protection compete. We know about protection rackets in Russia, but what's interesting is that these rackets also exist in Poland.

Are rackets preferred when states are weak? Protection economies are low information economies. They are places where reputational information does not circulate. Tax and regulatory

policies shape incentives for sharing information. Rackets tend to lose power over time (we see changes in reliance on rackets in Russia). How do we account for variation in where private protection is strong and where it is weak? We expect to see rackets where the state is too weak to meet the demand for protection and private supply is available. When there is a move to economic liberalization plus cuts in government funding this situation can arise. But this story is also possibly wrong. One might anticipate that where there is a lot of regulation we get informal economies and rackets while where there is less regulation, we see formal economies and heavier reliance on courts. These hypotheses don't hold up, however. Maybe where we have low polarization and competitive politics the result is less predatory regulation and better public goods provision while highly polarized places and competitive politics lead to predatory regulation and worse public goods provision.

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ⁱ James A. Robinson. "Politician-Proof Policy?" Paper prepared as a background document to the World Bank's 2004 World Development report. February 27, 2003.