

What is the fundamental difference between Rich and Poor Nations

Why Nations Fail – The Origins of Power, Prosperity and Poverty
By Daren Acemoglu and James A. Robinson

I am talking to James Robinson in the newly opened Bulgari hotel in upmarket London after listening to him deliver a talk about the book that he has co-authored. I am wondering whether the voice of the middle class - despairing, disenfranchised, disillusioned - turn the tide for India. James says that it is a strong possibility. They have at last found their voice in a sympathetic media and a class agnostic Internet has empowered them – first with Anna Hazaare and then the Delhi rape case among others. Sceptics are wishing it away but I am listening to James very carefully.

In their book Why Nations Fail, Acemoglu and Robinson, one an economist from MIT and the other a Professor of Government at Harvard come together and through the unusual combined lens of history, economics and politics, offer answers to questions that we are and have been struggling with.

Why is it that seemingly great civilisations came to ruination and others that seemed primitive and poor rose to such prominence and success and have held sway over the world for centuries? Think of the ancient civilisations of Greece, China, India and Egypt followed by Mayan, Incas and Aztecs – why did they not last the course and instead the US of A which is barely 300 years old, Western Europe and Japan take their place. History suggests that some of them regained their lost glory only to lose it again; India and China once more come to mind. There are others such as sub Saharan Africa and some of the Latin American countries that have not been able to rise out of poverty. We know that the industrial revolution first came to Britain – but what forces made that happen? What are the odds that China can really sustain the rate of growth in the future and what are the possible road blocks?

Does the book throw any light on India and suggest any prescriptions for the malaise that has seemingly dimmed the lights for us? While the authors offer specific views about China, India is hardly mentioned, if at all.

Is it geography, history, culture or race that decides prosperity of nations?

Over time, various economists and social scientists including Amartya Sen, Olson and Jeffrey Sachs have offered explanations for the rise and decline of nations. These range from history, geographical location, culture to race and genes. Robinson and Acemoglu illustrate with examples spanning the globe and going back several centuries BC that it is none of these.

While the difference between successful nations and others can be traced back to history, authors show through multiple examples that history is not destiny. Latin America was the

house of the Mayan, Inca and Aztec civilizations but the Spanish conquistadores exploited both the rich natural resources and the indigenous population thus marking the end of those great civilisations. Unfortunately, subsequent rulers continued to rely on the exploitative model with power concentrated in the oligarchy. In contrast, North America colonised by the British escaped the same fate due to a set of circumstances that forced the colonisers to i) give incentives to indigenous population and British settlers to work, ii) award them property rights, and, iii) involve them in the political process. The rest is history – these initiatives laid the foundation of a society with democratic principles. Today we see the difference between the USA and Latin American countries.

The authors demolish the other arguments with examples from across the world. One such is the city of Nogales that was split into half with one part in Mexico and the other in Arizona, USA. Today, there is a significant difference in their income levels, civil rights, infrastructure, education and health. Residents of the city in Mexico live with corruption and an ineffective State while democracy and its fruits are second nature to the half living on the American side. There is no difference in geography, climate, backgrounds of people, ancestors, food, and ‘culture’. East and West Germany, North and South Korea are other obvious examples. These countries shared a common history, geography and ‘culture’.

So what does?

Robinson and Acemoglu argue that it is the political and economic institutions that decide the fate of a nation and society. If power is held among a few people, they will invariably exploit people and resources for their own good. It is, therefore, important to have power distributed for better checks and balances and this is what they call inclusive political institutions as opposed to extractive ones with power concentrated among a few. However, some centralised power is important for the governing body to take effective decisions and provide public services. Often when dictators or oligarchs are overthrown, the very revolutionaries turn into autocrats failing to share power and the vicious circle starts all over again. As a result, these societies fail to enjoy sustainable growth. This is the ironclad law of oligarchy. Africa is one such continent with a long history of such usurpers of power. Unless this pattern is broken Africa is likely to continue to lag behind the world.

In contrast, inclusive political institutions provide rule of law, protection of private property and democratic rights to citizens. They shape inclusive economic institutions that promise free markets and equal opportunities for growth to each and every individual. Edison was the son of working class parents and so was James Watt, the inventor of the steam engine. The industrial revolution came to England first because it had democratic institutions in place where inventors and entrepreneurs were assured that their ideas and hard work would be rewarded and protected and that banks would lend them money to transform ideas into reality. For those with ideas and no means of financing them have the banking

and financial networks to transform those ideas into businesses. Extractive economic institutions, on the other hand, favour only the elite excluding the majority of the society from opportunities to grow thus encouraging inequality and social tensions. Growth benefits only the powerful.

World's richest countries have inclusive political and economic institutions. However, some countries that have joined the club – Singapore, South Korea have extractive political institutions. But it is the inclusive economic institutions that have made them so successful. Free enterprise, incentives, easy finance, creates the right infrastructure for business to flourish. China is another such nation.

For growth, societies need **creative destruction** where new innovations will change old paradigms. It is about destroying the existing and the old to create a new, better model and method. The handlooms gave way to textile machinery, horse carriages to the motor car and factory workers to automation and now white collared jobs are being replaced by software algorithms, smart computers and artificial intelligence. But in societies with power limited to a few, creative destruction is feared and unwelcome because it threatens the old structure and the power base of the incumbents. This encourages status quo, no growth and ultimately stagnation. This is one of reasons why so many societies went into a downward spiral of economic decline from the pinnacle of prosperity. Unless China makes a significant shift to an inclusive political state, the authors question the future of China as the largest economy of the world. The book argues that once the large untapped productive assets have been used up in China, growth will stop.

Talking to James A Robinson

I asked James the reason why India is still so poor despite its supposed democratic institutions. At the outset he claims he does not know enough about India.

James traces the roots of India's poverty to its age old rigid caste system - which has denied social mobility and equal opportunity to all, and, to the extractive Mughal rule followed by the colonial period. He does not doubt Nehru's good intentions but believes that the economic model he adopted slowed India's growth. Today, India has a mix of extractive and inclusive political and economic institutions that, he believes, continue to hold India back. However, James is bullish on India as he believes that having democratic institutions in place gives it a huge advantage over China.

He relates the intra state disparity in growth rate to colonial history; Bihar and Orissa were among the richest states with natural resources till the British colonial forces stripped them

of their riches. Subsequently, repeated oligarchic political institutions failed to provide the services due to its citizens.

What is the future of India?

I remind James that India is growing even though GDP may have hit some road bumps. There is a growing middle class which has benefited from the inclusive economic institutions supporting entrepreneurial activity. There is greater devolution of power as the regional political parties are becoming stronger forcing coalition politics at the Centre. Does he see that as a weakening at the Centre and not enough authority and power to deliver public services? He does not feel that is the case. He is clear though that the middle class will be the harbingers of change calling for more inclusion in political and economic process and demanding basic rights due a citizen in a democracy.

On China there are views contrary to his; Chinese government is bolstering innovation for growth and encouraging creative destruction. There is a famous story told to me by a Chinese Professor in Shanghai about how he watched the pounding of an electric loom by a crane in the public square marking the end of the manufacturing age and ushering in the knowledge era. He watched the workers who all welcomed this as the next step up for the nation. China has among the highest number of patents. From James own examples in the book about North America and Britain, it is not easy to withdraw inclusion because that too can threaten the basis of power. As the middle class gets empowered in China it will press for political participation and it will be difficult to deny the people. How China handles the transition is, perhaps, the key to China's future.