Economy and institutions II

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- Check the message **Welcome greeting** published in the News Bulletin Board.
- Dear student please edit your profile uploading a photo where your face is clearly visible.
- The purpose of the virtual meetings is to answer questions and not to make a summary of the study material.
- If you want to participate, please fill out the following survey: Primer corte 30% > Learning Activities > Tu opinión sobre la economía colombiana
- This presentation is based on (Cardenas 2020, chap. 4)

Analyze the role of institutions in the economy

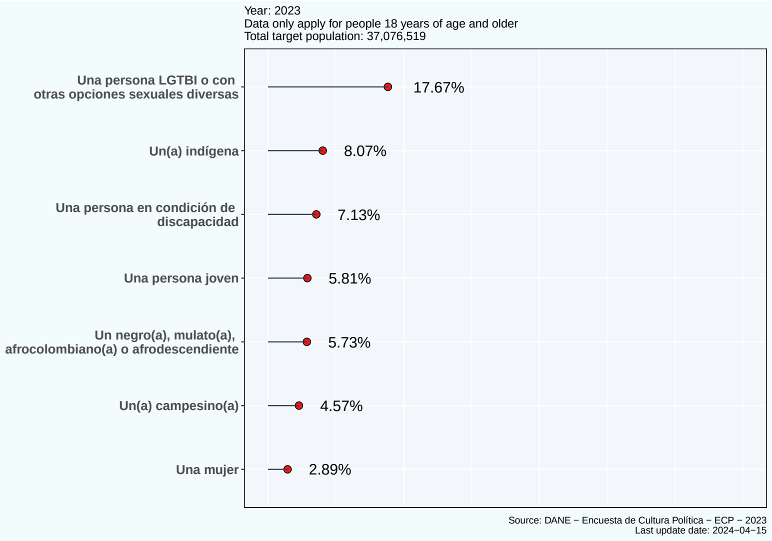

Figure 1: Percentage of people who would never vote for

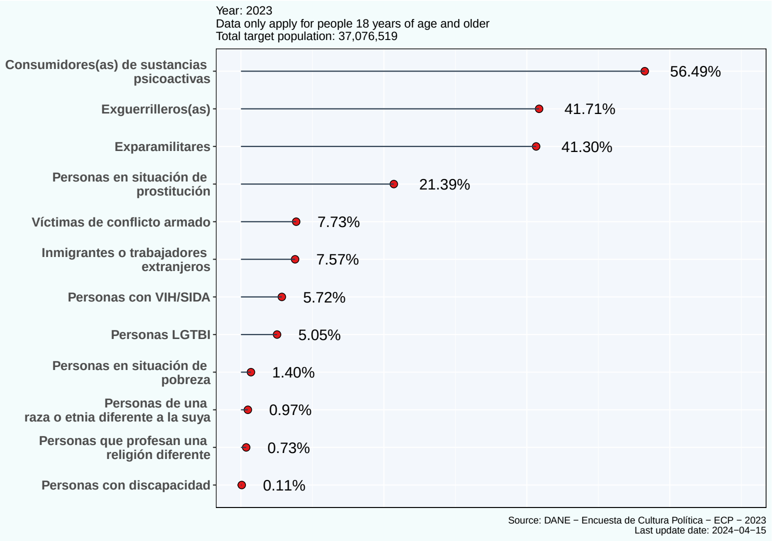

Figure 2: Percentage of people who would never like to have a certain neighbor

- The big question: **Why are some countries much poorer than others?**
  - According to (Acemoglu, Johnson, and Robinson 2005, 389–93) the key variables are the **political institutions** and the **distribution of resources**
- The **political institutions** are the rules that govern incentives in politics. They determine (Acemoglu and Robinson 2013, 79–80):
  - How the government is chosen
  - Which part of the government has the right to do what
  - Who has power in society
  - To what ends that power can be used

- The **political institutions** determine the **economic institutions**
  - The **economic institutions** are (Acemoglu and Robinson 2013, 73–74):
    - The rules influencing how the economy works
    - The incentives that motivate people

- The argument by (Acemoglu, Johnson, and Robinson 2005, 389–93) in relation to how **political institutions** and the **distribution of resources** determine economic performance is as follows:
  - Economic institutions shape the incentives of key economic actors in society where they influence investments in physical and human capital and technology, and the organization of production (Acemoglu, Johnson, and Robinson 2005, 389–90).

$$\text{economic institutions}_t \Longrightarrow \begin{cases} \text{economic performance}_t \\ \text{distribution of resources}_{t+1} \end{cases}$$

- The argument by (Acemoglu, Johnson, and Robinson 2005, 389–93) in relation to how **political institutions** and the **distribution of resources** determine economic performance is as follows:
  - Economic institutions are determined as collective choices of the society. However, there is no guarantee that all individuals will prefer the same set of economic institutions because they lead to different distributions of resources. So, there will typically be a conflict of interest among various individuals over the choice of economic institutions (Acemoglu, Johnson, and Robinson 2005, 390).
  - So how are economic institutions determined? Whichever individuals have more political power are likely to secure the set of economic institutions that they prefer.

$$\text{political power}_t \Longrightarrow \text{economic institutions}_t$$

- There are 2 components of political power (Acemoglu, Johnson, and Robinson 2005, 390–91):
  - **De jure (institutional)**: refers to power that originates from the political institutions in society
  - **De facto**: the power that derives from actual influence, irrespective of the formal institutional framework. It can be based on factors such as wealth, control of resources, or the ability to mobilize people, among others.

- In the case of the **de jure (institutional)** power according to (Acemoglu, Johnson, and Robinson 2005, 391) this aspect implies that:

$$\text{political institutions}_t \Longrightarrow \text{de jure political power}_t$$

- In the case of the **de facto** power according to (Acemoglu, Johnson, and Robinson 2005, 391) this aspect depends on 2 sources:
  - The ability of the group of individuals to act together and avoid the incentives of some individuals to benefit without contributing.
    - In the economic literature this is known as **solving the collective action problem** and the **free-rider problem**
  - The economic resources of the group which determine the ability to use existing political institutions and force against other individuals
- Because (Acemoglu, Johnson, and Robinson 2005, 391) don't have a satisfactory theory about how individuals solve the **collective action problem** they focus on:

$$\text{distributions of resources}_t \Longrightarrow \text{de facto political power}_t$$

- Also (Acemoglu, Johnson, and Robinson 2005, 391–92) point out that political institutions and the distribution of resources tend to change relatively slowly but determine economic institutions and economic performance both directly and indirectly.

$$\text{political power}_t \Longrightarrow \text{political institutions}_{t+1}$$

- Putting all these pieces together (Acemoglu, Johnson, and Robinson 2005, 392) describe in a simplistic schematic representation this framework in the following way:

$$\left.\begin{array}{lcl} \text{political institutions}_t & \Rightarrow & \text{de jure political power}_t \\ & & \\ \text{distribution of resources}_t & \Rightarrow & \text{de facto political power}_t \end{array}\right\} \Rightarrow \begin{array}{l} \text{economic institutions}_t \Rightarrow \left\{\begin{array}{l}\text{economic performance}_t \\ \text{distribution of resources}_{t+1}\end{array}\right. \\ \\ \text{political institutions}_t \end{array}$$

- To my family that supports me
- To the taxpayers of Colombia and the **UMNG students** who pay my salary
- To the **Business Science** and **R4DS Online Learning** communities where I learn **R** and π-**thon**
- To the **R Core Team**, the creators of **RStudio IDE**, **Quarto** and the authors and maintainers of the packages and **tinytex** for allowing me to access these tools without paying for a license
- To the **Linux kernel community** for allowing me the possibility to use some **Linux distributions** as my main **OS** without paying for a license

References I

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