Book Review

WHY NATIONS FAIL: THE ORIGINS OF POWER, PROSPERITY, AND POVERTY

Acemoglu, D., & Robinson, J. A. (2012)
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The prosperity of a nation is often associated with the happiness of her people, while poverty is associated with discontent. Consequently, factors that foster the economic prosperity of a country are of great interest to economists, policymakers, and the public. Identifying these factors is equivalent to investigating why some nations are rich (and why some are poor). Such a question has been one of the central questions for economists and social scientists to tackle in their research over the past twenty years.

There is a vast body of prior work on this issue. It has been found that there are reasons for some nations to be rich while others are poor; it is not accidental. There is a systematic explanation for the patterns of economic growth. Investment in education and technology and providing incentives through property rights have been identified as key factors driving economic prosperity and growth. However, knowing so does not mean that all the nations will be successful at carrying out such investments, offering incentives and thereby enjoying prosperity. The reason for the success or failure lies in each nation's economic institutions, those that facilitate economic transactions and handle market failure.

Nonetheless, there is no consensus on the desirable characteristics of an economic institution, how they come about, and why they persist over time. These classic but crucial questions are tackled in this critically acclaimed book, "Why Nations Fail." The authors use compelling examples: Nogales, Arizona vs. Nogales, Sonora, and South vs. North Korea to debunk popular theories such as geography and culture as the determinants of economic performance. These locations share the same geography and culture as their counterparts. Yet they experienced different patterns of economic growth.

The authors argue that it is the inclusive economic institutions – offering broad access to economic opportunities (e.g., public education, banking that serves the public, and patent rights available to anyone, including people of modest means) or allowing for competition amongst the population – that result in economic prosperity. On the other hand, the extractive institutions – offering access to economic opportunities only to a small population or having virtually no competition (e.g., private education, banking that serves only the privileged, and patent rights only for the rich) – eventually bring poverty.

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The extractive economic institutions normally perpetuate over time through extractive political institutions that keep decision-making power amongst a small group of individuals. These individuals can safeguard their personal gains by running the political and economic institutions that best serve their interests but not necessarily the public's interest. In contrast, inclusive economic institutions are likely remain over time through inclusive political institutions, where a broad population has centralized decision-making power. Such inclusive institutions are more likely to serve the public's best interests and economic growth (There were also rare cases in which inclusive economic institutions are governed by extractive political institutions, but they are not likely to be sustainable in the long run.)

The extractive economic and political institutions tend to persist over time unless there is a catastrophic event that transforms the institutions into more inclusive ones. For example, the Black Death in Europe (which resulted in about 50 percent loss of population) made it eventually impossible to tie scarce labor to the land under the system of serfdom that was designed for tying abundant labor to land.

This book's contribution is not about better understanding why a particular institution arises. Instead, the authors imply that this could be accidental. But, it sheds light on the type of institutions that will stand the test of time in generating economic prosperity. These would be the inclusive ones, allowing the broad population to have access to economic and political opportunities, as opposed to the extractive ones that only give the power of decision-making to a handful of people. The reason behind this is that inclusive institutions are flexible and can better withstand the dynamic changes in the economic environment. There are no long-term designated individuals or families with economic and political power. They can be replaced by individuals best suited to the current situation (for example, Facebook cannot prevent TikTok from entering the domain of social media service providers, and Google was able to rise as a popular Internet search engine despite yahoo's dominance in the early days). Such flexibility to adapt to changes is absent in extractive institutions. These institutions are normally controlled by a small group of individuals, while adapting to changes may dilute the controlling party's power (cotton plantation owners did not invest in infrastructure for manufacturing factories in the South after the Civil War.)

This book is one of the pioneers in exploring the impact of political institutions on the economic development of nations. It is the result of a research collaboration between Daron Acemoglu, an economist who is widely recognized for his work on political economy, and James A. Robinson, a political scientist specializing in Africa and Latin America. Acemoglu, who is currently an Institute professor at MIT, earned the John Bate Clark Medal from the American Economic Association in 2005 for being the best American economist under 40. Roughly one-third of the medalists were eventually awarded a Nobel Prize in Economics. Robinson is currently a David Florence Professor of Government at Harvard University.

The book is a product of a methodical scholarly work. It uses extensive historical evidence from various cultures and nations across the globe to support its arguments. It is not surprising that the book was selected for the 2012 best books of the year by the Washington Post, the Economist, the Financial Times, Business Week, and the Council of Foreign Relations. This book is a companion to the authors' earlier major works on political economy and institutional economics, including their 2001 American Economic Review article entitled Colonial Origins of Comparative Development: An Empirical Investigation (with Simon Johnson), and their 2006 book entitled Economic Origins of Dictatorship and Democracy.

The book will appeal to the reader who is interested in understanding how politics affects a nation's economic progress and the standard of living of her people, how a different form of government will lead to a different development path, or how a nation can overcome an undesirable institutional legacy to establish an infrastructure for long term prosperity. This book's findings are still relevant a decade after it was first published. They are applicable to understanding the impact of the recent global changes (e.g., the political landscape of the U.S. and the rise of Xi Jinping's supremacy in China).