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## **Leaders & institutions key to growth**

***Sustained progress is a continuous endeavour to ensure the successful design and implementation of good policies***

**By EDWARD ROBINSON AND TAN YIN YING**

AS Singapore commemorates her 42nd year of independence, her citizens can take pride in the remarkable economic transformation of the country 'from third world to first world'. After adjusting for purchasing power, Singapore's gross domestic product (GDP) per head of population in 2003 was nearly five times higher than in 1965.(1.)

Singapore's high growth rates were neither assured nor expected, and, given her endowments, there was little reason to expect newly independent Singapore to count among the growth outperformers. Indeed, the pace of economic development over the past four decades has varied widely across countries.

At the global level, average GDP per head was US\$10,000 in 2003, just over two and a half times the level in 1960. This rising average belies the very disparate experiences: a person in high-income Luxembourg was, on average, better off than a citizen of the Democratic Republic of Congo - one of the world's poorest countries - by some US\$48,800 in 2003. In comparison, the gap between the world's richest and poorest economies was only US\$14,900 in 1960.

Clearly, some economies have consistently grown faster and become richer than others. Traditional economic models are however not very good at explaining this disparity in growth rates. According to these models, economic growth is primarily a function of factor accumulation and the improvement in the quality of these factors.

The more labour, capital, or technology an economy can harness in the production of goods and services, the higher the rate at which output, and thus income, can grow. Such models also predict that growth disparities between rich and poor countries, or even differences in income levels, will narrow over time.

This happens as poorer economies grow faster and 'catch-up' with richer ones because of the former's relatively abundant resources and low level of technology. Eventually, economic growth in the poorer countries slows and income levels should converge with those in the more advanced economies.

But we know that the reality is quite different - many economies have continued to lag behind. Alternative models have been developed, which take into account a richer set of underlying factors that might impact long-term growth and development. By adopting a more empirical strain, these models seek to understand, for example, whether low growth rates are endemic because of unsuitable geography that facilitates the transmission of diseases (the tropics) or hinders trade (land-locked countries); or if they are influenced by the quality of institutions established from historical legacy.

History has shown us that popular growth paradigms are not always relevant to all countries at all times, nor have 'recipes for growth' been particularly successful.

Formulating the right set of pro-growth policies is difficult, and implementing these policies in a local context is no easier.

Consistent with the empirical research on the causes of growth, and drawing on Singapore's own development experience, we have been working on a political-economy framework that attempts to account for growth disparities amongst developing economies.(2.)

This framework incorporates elements of geography, institutions, leadership and society, and seeks to explore, more specifically, the elusive quality of 'reform implementation' as a key determinant of growth differentials.

We have attempted to quantify each of the above four factors in a manner that is comparable across our sample of developing countries.

### **Extremes**

Looking at the period from 1960 to 2003, we first narrow our focus by setting aside the extremes of countries whose incomes per head have generally been either above the global 50th percentile (the 'developed economies') or consistently remained at the bottom 25th percentile (the 'underdeveloped economies').

Our focus is on the remaining second quartile of 'developing economies' which can be further divided into three broad categories. These are the growth underperformers, whose incomes have broadly moved down the global income distribution ladder over the intervening 40 years; the average growth economies, whose incomes have remained within the second quartile, and the growth advancers, whose incomes have risen in the global rankings.

We find, perhaps unsurprisingly, that geography does matter, but fails to tell the whole story. In general, growth advancers enjoyed better access to the sea (and hence trade routes), while a larger proportion of the economies in the other two categories were land-locked. However, some land-locked economies, such as Botswana, have grown strongly.

Moreover, while the average growth and underperforming economies tend to have greater natural resource wealth than growth advancers, these resource endowments have not guaranteed strong economic performance.

Other researchers have also drawn the link between natural resources and institutional quality. Countries with strong institutions tend to implement policies that channel natural resources into the generation of sustained growth and the accumulation of national wealth. Those with weaker institutions tend to do the opposite and implement exploitative policies that benefit select groups in the short term, but which are detrimental to the economy and the broader populace over the longer term. This is important, as these institutions are passed down over time, and shape the quality of policy implementation for subsequent generations.

Institutions are defined by their functional capabilities and, importantly, by the people who lead and staff them. We find that the quality of key institutions, such as legislative and regulatory bodies, is unequivocally higher by a large margin in the growth advancers. These economies also outscore average and underperforming economies in indicators measuring leadership quality: for example, leaders in these countries are, on average, perceived to be less corrupt, more effective, and able to create a more stable political environment, and more accountable to their electorates. Leaders are the public face of policies and help build social consensus for pro-growth reforms. Reforms typically involve many different groups, not all of whom will share 'weal and woe' in proportion, and growth advancers appear better able to garner social consensus than growth underperformers. Without competent leadership, effective institutions and genuine social consensus, good policies could easily be undermined at the implementation stage.

As the developing world looks admiringly at the growth rates of China and India, we ought to remember that there is no standard recipe for growth, no 'one-size-fits-all' yellow brick road to prosperity. Economics principles, such as those espoused by the Washington Consensus, do not translate easily onto a neat set of policy prescriptions for long-term sustainable growth; after all, a market mechanism can develop via rapid Latin American-type liberalisation, or through the gradualism of Deng Xiaoping's China. Instead, we suggest that governments should put in place the people and institutional supports that will allow them to implement pragmatic and relevant policies, and to chart an enlightened course in executing necessary and sustainable reforms.

Our findings ultimately return to the critical role played by the three elements of robust institutions, good leaders and people consensus. Generating sustained progress is a continuous endeavour, with each of these elements interacting with the others in a self-reinforcing fashion to ensure the successful design, refinement, and implementation of good growth policies.

*Mr Robinson is the Executive Director of the Economic Policy & Macroeconomic Surveillance Departments (MSD) and Ms Tan is Senior Economist in the MSD at the Monetary Authority of Singapore (MAS). The views expressed here should not be attributed to the MAS*

*(1.) Figures are denoted in purchasing power adjusted international dollars. In a given year, one international dollar has the same value as one US dollar.*

*Source: Heston, A, Summers, R and Bettina, A, (September 2006), Penn World Table Version 6.2, Center for International Comparisons of Production, Income and Prices at the University of Pennsylvania*

*(2.) Tan, Y Y, Eng, A, Robinson, E (August 2007) 'Perspectives on Growth: A Political-Economy Framework', MAS Staff Paper No 47, available at <http://www.mas.gov.sg>*

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