

Why ‘good governance’ fails – lessons from regional economic development in Colombia

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Abstract: By critically reviewing different strands of literature on institutional change and development this paper argues that in order to fully understand sub-national economic development we need to move away from 'good governance' explanations in which geography-specific analyses of power structures and elite interests are largely absent. Using findings for Colombia and insights from economic geography and heterodox political economy theories, this paper gives theoretical and conceptual guidelines and approximations for future studies on regional economic development. The contribution provides a place-based discussion of how the historically evolved distribution of power balances, context-specific elite interests, and the interaction between place-bound actors and place-less dynamics affect sub-national institutional arrangements shaping policies and development outcomes. The conclusions drawn from this discussion are not limited to Colombia, but also help researchers for future studies on regional economic development in sub-national contexts in other parts of the world.

Arguably one of the most influential propositions in social science research and policy circles on development is that the failure to achieve economic development is rooted in the institutional incapacity to achieve ‘good governance’ (see Acemoglu and Robinson, 2012; World Bank, 2017). Emerging from a paradigm shift in international development and economic scholarship during the 1990s ‘good governance’ is understood as a standard set of governance reforms focussing on the reduction of market distortion caused by political rent seeking (Krueger, 1974; Acemoglu *et al.*, 2004; Rodrik, 2004; Acemoglu and Robinson, 2013). The literature proposing such ‘one-size-fits-all’ reforms see the establishment of rules and regulations to achieve transparency, to guarantee stable private property rights, to decrease corruption, and to establish a rule of law as necessary and sufficient conditions for achieving growth and development (World Bank, 1992, 2000; North, 1995; Kauffman *et al.*, 1999).

By contrast, this paper argues that such dominant ‘good governance’ approaches fail in providing context- and geography-specific explanations of uneven development at the sub-national level. This spatial blindness to context- and place-specific institutional arrangements reinforces problems related to linear understandings of the relationship between institutional change and regional economic development. The main contribution of

this paper is not to propose yet another standard theoretical approach. Instead, and by critically reflecting on the mainstream theories on institutions and economic development, this paper shows how the analysis of the interdependent relationship between context-specific power balances and institutional arrangements can help future research in the study of regional economic development in countries of the Global South.

During the past two decades, most Latin American countries closely followed ‘good governance’ policy prescriptions. However, evidence suggests that despite implementing the standard consensus policy reforms, most Latin American countries have experienced disappointing changes to per capita incomes and an increasing divergence in regional development indicators (Davis, 2005; Roberts, 2005; Sklair, 2005; McMillan and Rodrik, 2011; Palma, 2011). This is also true for Colombia where divergence between the economic and productivity performances of the different regions has *increased* following the implementation of political and economic governance reforms (see Barón, 2003; Barón and Meisel, 2003; Clavijo *et al.*, 2012). The experience of Colombia illustrates the shortcomings of the ‘good governance’ approach to institutions and regional economic development fairly well. However, most countries of the Global South continue following such static policy prescriptions, including Colombia where recent policy proposals for a post-conflict society still focus on regional development strategies that ‘transform territories through efforts to improve governance and Good Governance’ (DNP, 2014, p. 604). As such, studying the relationship between institutions and regional economic development through the lens of Colombia’s experience not only helps in the understanding of Colombia. The conclusions drawn from the analysis is also helpful in the theoretical approximation of regional economic development in other parts of the world.

Divergent regional economic development in Colombia

In response to the end of the developmental model of import substitution industrialization (ISI) in the late-twentieth century, elites in Colombia started to reorganize the basic institutional setup of the country’s political economy. Besides economic liberalization and the selective transfer of state capabilities and power to ‘place-less’ actors (i.e. supranational organizations) (see Hambleton, 2015), this restructuring included a wide range of decentralization reforms (Montero, A. P. and Samuels, 2004; Falleti, 2010).

Many of the existing empirical evaluations of regional development trajectories in Colombia emphasize that after the implementation of structural reforms in the 1980s and 1990s, inter-departmental economic disparities have increased rather than diminished (see Cuervo, 2003). In a quantitative analysis, Barón (2003) looks at regional development trajectories since Colombia introduced first liberalization reforms in the late-1980s. He finds that reforms of economic openness (*apertura*) did not help in achieving inter-regional convergence. Rather, the overall share of the gross domestic product (GDP) per capita in the poorest regions remained very low and economic disparities increased in the 1990s. Barón and Meisel (2003) present evidence that in the first ten years after the introduction of decentralization reforms, economic disparities between different regional territories in Colombia increased. Barón and Meisel (2003) furthermore show that fiscal transfers from the national government have not contributed to diminishing this gap.

There are numerous studies on regional productivity growth in Colombia. Calculating Total Factor Productivity (TFP) from an aggregate production function there is a great heterogeneity in findings on regional development. While some authors find

regional economic convergence (Cárdenas *et al.*, 1993) others find evidence for an increasing economic divergence between the different regions (see Clavijo, 1990, 1994). Using panel data regressions, Iregui *et al.* (2001) find that due to the large differences in sectoral and territorial development in terms of productivity performances and employment and capital elasticities, economic divergence increased in the period 1975-2000.

Recognizing the weaknesses and shortcomings of TFP studies, Ramírez *et al.* (2014) engage in a very detailed disaggregated analysis of sectoral and regional productivity indices in different Colombian regions. Their analysis shows that in terms of GDP per capita only four regions are above the Colombian average, namely the Bogotá region, Bolívar (Cartagena), Antioquia (Medellín), and Santander (Bucaramanga). Ramírez *et al.* (2014) find similar trends for labour productivity, where Bolívar (Cartagena), leads over the Bogotá region and Antioquia (Medellín).

Apart from standard neoclassical analyses of growth and development in Colombia (Easterly *et al.*, 1997; i.e. Clavijo *et al.*, 2012) and purely quantitative studies (i.e. Barón, 2003; Ramírez *et al.*, 2014), González and Ocampo (2006) take a multidisciplinary look at the impacts of globalization on sub-national development in the country. They argue that the implications on institutional functioning, power balances, and economic development of Colombia's global economic integration led to very different economic results in the country's regions. Their book finds that globalization as an ideological phenomenon has led to an inter-regional economic divergence. Betancur *et al.* (2001), Franco Restrepo (2005), and Franz (2017, 2018) also find that the implementation of structural reforms has resulted in rather disappointing development outcomes in different Colombian regions and cities.

Gutiérrez *et al.* (2012) make a comparison between different regions. The authors claim that in the successful local development experiences, 'interest-based bargaining was shunned, and specific social and economic sectors were not privileged' (Gutiérrez *et al.*, 2012, p. 190). Gutiérrez *et al.* (2012, pp. 194–95) stress that the successful cases implemented governance models 'based on guaranteed stability of property rights and reduced corruption'. This resonates with Gilbert's (2006) findings of Bogotá as a 'model city' where 'good urban governance' was responsible for a positive economic and social transformation.

The great heterogeneity of empirical findings on and explanations of regional development is also evident in the literature on regional economic development in other parts of the world (see Amin, 2002; Cashin and Sahay, 1996; Démurger, 2001; Sachs *et al.*, 2002). This heterogeneity of findings on regional economic divergence or convergence suggests the need to discuss theoretical and analytical arguments of the literature on institutions, economic geography and political economy of development.

Institutions, growth and regional economic development: challenging 'Good Governance' explanations

In the past three decades, most countries of the Global South have implemented economic reforms very much in line with general structural reform agendas (Williamson, 1990) basing policy recommendations on theoretical considerations of neoclassical economic growth models (see Abramovitz, 1986; Romer, 1986; Lucas, 1988; Barro and Sala-i-Martin, 1995). These models follow the logic that countries can achieve convergence through liberalizing their capital and current accounts to benefit from transfers of foreign technologies. Following rather disappointing results (including an increase in divergence of

regional development indicators), the effectiveness of the market-led reforms have been called into question (see World Bank, 2005; Williamson, 2008; Ostry *et al.*, 2016).

From one side, economic scholars such as Krugman (1991) argued that mainstream theories ignored the geographical aspects of production. The models proposed by New Economic Geography (NEG) theories, in other words, stress the importance of analysing locational aspects of production within a country (see Krugman and Venables, 1995; Fujita *et al.*, 1999). The NGE models argue that clustering of firms and the spatial composition of an economy depend on ‘the interplay between costs of transactions across space and various types of increasing returns to scale’ (Venables, 2008, p. 207). However, and acknowledged by Krugman (2011, p. 6) himself, the core-periphery model of the NGE ‘has a kind of steampunk feel, so that the stories it tells seem more suited to the U.S. economy of 1900 than that of 2010.’ Furthermore, the NGE has been criticized for ignoring the role of historico-institutional factors in the development of the different analysed localities (Martin, 1999, p. 80).

The theoretical transformation in the mainstream debate on (regional) economic development that followed was the institutional turn in economics. In principle, the focus went from neoclassical and endogenous growth theories arguing the key to economic development is ‘getting the prices right’ to the need of a ‘right institutional infrastructure...for markets to function’ (Stiglitz, 1998, pp. 10–11). This new agenda bases much of its theoretical guidelines on New Institutional Economics (NIE).

The large bulk of the NIE literature finds that less developed countries fail to develop because of institutional constraints, namely ill-defined property rights and misguided regulation (Acemoglu and Robinson, 2012). For the NIE the failure of less developed countries to achieve sustainable development is rooted in the reoccurrence of market failures that arise because of the persistence of wrong intuitions. Consequently, competitive market equilibria and development can be achieved through establishing ‘good governance’ institutions, which are understood as a standard set of governance reforms to achieve transparency, guarantee stable private property rights, decrease corruption, and establish a rule of law (Kauffman *et al.*, 1999; Acemoglu *et al.*, 2004).

Critics of the dominant institutionalist agenda claim that similar to neoclassical and endogenous growth theories, the NIE is largely oblivious to spatial dimensions of economic, political and social development (see Barca *et al.*, 2012). It furthermore remains a vague and generalized pro-market agenda promoting neoliberal ideas and ideals. Rodrik (2006, pp. 979–80) argues ‘getting the institutions right’ and ‘good governance’ became a generalized mantra that are of little help for less developed countries in terms of actual policy advice. ‘Good governance’ or improving governance can become intangible development end goals in and of themselves, discarding the achievement of increased economic and social indicators. Önis and Senses (2005, p. 286), furthermore point out that the focus of the consensus agenda ‘fails to address the fundamental power relations and asymmetries of power that exist between classes at the level of the nation state’.

This criticism also resonates in political economy approaches to uneven development emphasizing that national and sub-national differences in economic development is a direct and inherent result of capitalism’s search for additional accumulation and greater value extraction from new spaces (Harvey, 1982; Massey, 1985; Brenner and Theodore, 2002). In an attempt to bridge the gaps in the orthodox geography literature and heterodox political economy debates, Smith (2008, p. 4) sees uneven development a structural and ‘systematic geographical expression of the contradictions

inherent to the very constitution and structure of capital'. Drawing on Hudson (2005), MacKinnon et al. (2009, p. 137), also emphasize that 'spatial evolution must be explicitly related to the dynamics of capital accumulation, underpinned by the creation and realization of value through spatial circuits of production, circulation, consumption, and regulation'. Territorial divisions of labour and a historical evolution of class structures therefore determine the position of different places within broader capitalist structures (see Massey, 1985; Hudson, 2005).

From this theoretical point of view the productive agglomeration of firms in a specific region is not the result of transaction costs-reducing institutions as seen by the NIE (see Hodgson, 2002). Rather, large multinational corporations invest in a territory due to their interests in extracting profits from (cheap) labour. These 'place-less' organizations are supported by place-based regional actors who formulate their policy strategies in ways that attract such investments by enhancing broader territorial division of labour (see Hambleton, 2015).

Questions of uneven development of capitalism and the recognition that power structures shape different institutional environments in which economic policies are adapted are also at the core of the so-called political settlements framework. The political settlements literature, pioneered by Khan (1995), stresses that there are no 'good' or 'bad' institutions (Khan, 2010; Hickey, 2013; Laws and Leftwich, 2014; Pospisil and Rocha Menocal, 2017). Rather, developmental outcomes are a result of the configuration of the context-specific political settlement, which describes 'a combination of power and institutions that is mutually compatible and also sustainable in terms of economic and political viability' (Khan, 2010, p. 4).

This dynamic analysis includes the study of how horizontal (between groups) as well as vertical (within groups) bargaining games shape power balances and influence institutional efficiency functions (to reduce transaction costs) and distributive functions (to maintain political stability by transferring benefits according to predominant power balances) (Di John and Putzel, 2009). The analysis of power and institutional functions helps in differentiating wasteful benefits (i.e. political rents) from growth-enhancing ones that incentivize strategic, medium and high productivity investments. Taken these considerations to the policy arena lets us identify constraints and possibilities for governance agencies to create growth-enhancing mechanisms as well as institutions that enforce and monitor the conditions on recipient firms (Khan, 2010, p. 4).

Similar to Martin (2000), the political settlements framework distinguishes between 'institutional environments' shaping a policy and development outcomes (i.e. developmental effects of formal rule or regulation) and 'institutional arrangements', which are other factors that enhance or slow down the efficacy of institutions (i.e. power balances affecting institutional implementation and enforcement) (see Rodríguez-Pose, 2013). However, much like other approaches in institutional economics, the political settlements literature largely misses to explicitly conceptualize or theorize the links between national institutional arrangements with subnational ones. The focus on methodological nationalism on which much of the political settlements analyses are based makes the framework spatially blind with regard to the importance of geography and context specificity in local and regional institutional environments and institutional arrangements.

Taking theoretical considerations of geography-inflicted literature into account might help in overcoming the gap in the heterodox political economy analysis of institutional change and development. Rodríguez-Pose (2013, p. 1042) for example argues

that strategies for regional development need to be ‘tailored to the potential of place-bounded institutions in order to make the most of intervention’. Such a place-based analysis would overcome problems related to ‘one-size-fits-all’ approaches, including the conflation between institutional environment and arrangements, the neglect of analysing ‘soft’ or informal institutions, and the difficulties of measuring institutional impact on economic development at the local or regional scale (see Rodríguez-Pose, 2013; Pike *et al.*, 2017, Montero and Chapple, 2018). Such an approach would not only focus on institutions that build on particular local capabilities and provide the basis for interaction between place-based and place-less actors for policy design and implementation (see Barca *et al.*, 2012), but would also emphasize institutional diversity and socially constructed institutional arrangements at the sub-national level.

As such, this paper argues that a detailed understanding of local and regional policies and their indeterminate developmental outcomes requires the analysis of the way in which the interaction between powerful local elites and external, place-less dynamics shape the context in which local institutions are implemented and enforced. Taking these theoretical reflections and the empirical findings on regional economic development in Colombia into account, the next section will point towards some important factors for the study and understanding of the relationship between institutional capacity and regional economic development.

Power structures, institutions and elite interests: towards a place-based political economy approach for regional development

Three main implications emerge from this that can be of help for future theoretical and empirical research of regional development in Colombia and beyond.

Firstly, the analysis of regional developmental outcomes need to go beyond the static and linear understanding of the relationship between institutions and regional economic development. Besides the more direct institutional influences on the reduction of transaction costs, the study of regional economic development should also consider the way in which context-specific power balances affect local and regional institutions in their distributive function. This includes the distribution of wasteful political rents as well as the distribution of benefits to economic agents in order to create incentives and compulsions for productive investments.

This can also help in the proposition of regional economic policies. Researchers can learn from contexts where local institutional mechanisms successfully diminished transaction costs and distributed growth-enhancing rents to achieve sustainable levels of regional economic development. For example, the way in which local and regional institutions in East Asian ‘local developmental states’ supported and incentivized economic agents in strategic sectors in the acquisition of entrepreneurial and productive capabilities and technologies (see Jessop and Sum, 2000; Zhu, 2004; Lan, 2009) can provide helpful insights. Institutional tools for achieving productivity growth of local firms in these settings included subsidies, protection for infant industries (tariff and non-tariff), tax breaks, and other forms of direct support. While this learning from successful financing instruments that prevailed elsewhere can be an important source of institutional innovation (Rodrik, 2014, p. 26), a simple emulation of such growth-enhancing institutions can very well result in disappointing outcomes, as effective policy design, implementation and enforcement are interdependently connected to the wider politico-economic and geographic specificities.

This brings me to the second implication. In order to overcome the problems related to 'one-size-fits-all' approaches, the analysis needs to go beyond the study of the institutional environment that shapes economic, political and social development trajectories. A place-based analysis of the historical evolution of the distribution of power at the local or regional level can help in identifying institutional barriers to policy implementation and enforcement. This needs to include the analysis of tensions among local and regional elites, inter-regional disputes between elite factions, as well as tensions between regional and national elites. The way in which these different powerful groups formally as well as informally engage in influencing institutional environments can give important insights into the efficiency and distributive functioning of local, regional and national institutions, which helps in understanding policies and development outcomes at the analysed sub-national level. The socially and historically evolved interests and capabilities of powerful economic groups further indicate the kind of bargaining game elites might employ to access institutional benefits or influence policy design and implementation.

Elite structures in Colombia, for example, have historically been characterized by the existence of some very powerful regional elite factions with large organizational influence and weaker regional elites that have little influence in shaping policy strategies (Palacios, 2006; Restrepo Santamaría, 2011). This is likely to have led to a perpetuation of uneven economic, political and organizational powers of the different elite factions. Such compositions of elite structures are also dominant in other countries of the Global South. Thus, the understanding regional economic development in these settings requires a historical analysis of the way in which the powerful position of a particular elite faction has hindered the emergence of institutional arrangements that can challenge prevailing uneven regional economic development.

The third implication is concerning several external factors that need to be included in the analysis of institutional efficacy and development at the sub-national level. National policies, for example, continue to have important implications for local and regional institutional functioning and development. Globalized dynamics also influence sub-national institutional arrangements, interests of regional elite factions, and bargaining games between different powerful actors.

Similar to Colombia where structural reforms lead to 'the emergence of radically different rules of the game' (Cuervo, 2001), national and global forces influence sub-national institutional and economic dynamics in other countries of the Global South affecting the constellation of power balances, elite interests and institutional arrangements. While in most countries this resulted in a decrease in industrial incomes, traditionally powerful regional elite factions have still been able to influence new institutional mechanisms for regional and decentralized accumulation strategies (i.e. through privatization or deregulation).

In many cases, this has increased locational pressures and territorial competitiveness of sub-national economies (see Scott and Storper, 2003; Silva, 2005), reinforcing tendencies of low productivity growth. The resulting increase in activities that depend on unskilled and cheap labour and the attraction of Foreign Direct Investments (FDI) into sectors at the low productivity end of the global value chain can have detrimental developmental outcomes for national and sub-national economies (see Sassen, 1991; Brenner and Theodore, 2002; Reyes, 2003; Rettberg, 2005; Robinson, 2014), which can result in an increased economic divergence between different regions.

In a sub-national context where cheap labour supply is abundant (reinforced by policies of suppressing real wages), investments and efforts in learning and acquisition of technology to discover higher-value comparative advantages are likely to be marginal, as profits are generated through labour-intensive activities at the lower end of the value ladder. External pressures on local and regional elites to insert their economies into the global chain of production and value creation while accepting the static and low-productive nature of the comparative advantages of their economies need to be considered in future research on sub-national policies and development outcomes.

Conclusion

This paper provided critical reflections of theoretical approaches to the study of regional economic development, arguing that the static and linear understanding of institutional change and its influence on regional economic development fail in providing analytical toolsets for the study of regional economic development. In particular, the paper argued that in order to understand economic development at the sub-national level we need to go beyond the 'one-size-fits-all' explanations of the 'good governance' approach.

Like most institutional theories on economic development, the 'good governance' paradigm largely ignores spatial and geographical differences in institutional environments and institutional arrangements. This obfuscates understandings of the way in which power relations, spatial asymmetries, and geography-specific social structures shape the relationship between institutions and regional economic development. Empirical findings of regional economic development in Colombia demonstrate that a focus on improving governance does not linearly transfer into regional development or economic convergence. Given that the policy priority of most less developed countries continues to be the improvement of governance indicators, the failure of such a policy focus in Colombia helps to draw important lessons for future research of regional economic development in other countries.

The starting point to a place-based study of local and regional institutional change and development is the analysis of factors that shape the relationship between institutional change and regional economic development. This includes the historical and social evolution of context-specific power balances, the interests, capabilities and position of elites and firms within this balance, and the interaction between place-based actors and place-less globalized dynamics. A comprehensive analysis of such context- and geography-specific factors not only contributes to the understanding of institutional implementation and enforcement capacities of regional governance agencies. It also helps to differentiate between efficiency functions of institutions reducing transaction costs and distributive functions of institutions creating productive or unproductive benefits for powerful actors, regional capitalist firms and multinational companies. Such an approach can help future research in the study of the way in which the context- and geography-specific interdependent relationship between power balances and institutions affect economic development in a regional setting not just in Colombia but also in other parts of the world.

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