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Institutional change and economic development: a conceptual analysis of the African case

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Abstract

Purpose

The purpose of this paper is to explain the African socio-economic development and policy design problems using the new institutional economics methodology. The paper emphasizes the importance of carefully considering the policy environment setting before changing the rules of the society (institutional change) and making policy choices.

Design/methodology/approach

A conceptual approach is used to explain why major economic development policies fail in Africa and the developing world as a whole. To illustrate policy-environment-dependent institutional and policy change decision making, examples of potential institutional and policy changes are examined for Ghana's financial, retail, and land resource sectors.

Findings

It is argued that the concept of institutional efficiency must be looked at quite differently from the Pareto-optimal concept in the neoclassical economic theory. This is because institutional analysis leans more toward normative rather than positive economics. The paper explains the counterintuitive findings that although the African business environment is low on trust due to high ethnic diversity, African business depends more on trust than contracts – weak enforcement of institutions accounts for such twists. Potential institutional changes that can help address specific

The paper lays bare several research hypotheses that can now be tested using the available data. These include hypotheses that strong economic growth precedes growth in the stock market activity (not the other way round); an asymmetric Tobin tax that taxes conversion into foreign currencies more than conversion into local currency reverses local currency depreciation; and for import-dependent countries, strengthening the local currency provides a positive shock to local production and budget balance.

Originality/value

The paper illustrates the pitfalls associated with blanket application of theoretical frameworks without proper contextualization. A promising way out for weak African economies is to adapt the theoretical economic predictions to local environments and help refine general economic theory through their experiences.

Keywords

- Uncertainty
- Development
- Efficiency
- Enforcement
- Institutions and institutional analysis

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