



Role Of Institutions In Socio-Economic Development: An Evaluation Of The 2024 Nobel Prize In Economics

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Abstract

Institutions, whether rules or organizations, play a key role in the socio-economic development of any region. They act as catalysts for enhancing efficiency and reducing uncertainty in organizational functioning. The 2024 Nobel Prize in Economics evolves around the nexus between these two terms: institutional quality and socio-economic progress. What the Nobel laureates brought to the attention of the global community is the key role played by 'institutions' in transforming the regions of the world

Key Words: Institutional Quality, Socio-economic Development, Colonialism, Democracy

1. Introduction

The 2024 Nobel Prize in Economics is significant as it highlights the factors that ultimately determine a country's long-term economic success. U.S. economists Daron Acemoglu, Simon Johnson, and James A. Robinson were awarded for their research on 'how the quality of a nation's institutions can determine its economic destiny'. The tale of two cities, Arizona and Sonora, has paved the groundwork for their study. They observed the historical background of both cities and their key focus was on the nexus between colonialism and institutional quality. The Swedish Academy put the 2024 Nobel Prize for Economics towards the study of 'how institutions are formed and whether they affect prosperity?'

Daron Acemoglu, was born in 1967 in Istanbul, Turkey, and Simon Johnson, was born in 1963 in Sheffield, United Kingdom. Both are professors at the Massachusetts Institute of Technology, USA. James Robinson (born 1960) is a British economist and political scientist, currently a professor at the University of Chicago's Harris School of Public Policy. Acemoglu is also the author of the 2012 bestseller 'Why Nations Fail: The Origins of Power, Prosperity, and Poverty'. The Nobel Prize Committee assessed that the laureates explained the relationship between institutions and prosperity by analyzing the political and economic systems and institutions established during European colonial rule. The Swedish Academy goes without saying that the award underscores the importance of democratic institutions.

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2. Role of Institutions in Economic Development

Economists interpret institutions mainly in two directions. The first is as 'rules of the game' and the second is organizations. Institutions are the formal and informal constraints on political, economic, and social interactions (North, 1990). As per this definition, good institutions mean those structures that put in place an "incentive structure" that reduces uncertainty and promotes efficiency. Institutions make up some of the most important determinants of any economic outcome. Protection of property rights, effective law enforcement, and efficient bureaucracies, together with a broad range of norms and civic mores, are found to be strongly correlated to better economic performance over time (Ferrini, 2012)

A huge amount of literature links economic development and institutional dynamics. Institutional quality is the widely acknowledged precondition of economic development. Easterly (2008) argues that institutions are endogenous to economic development and that economic growth may be driven by other factors such as geography or culture. Using data from 25 developing nations, Rodrik (2008) exposed a positive association between institutional quality and economic development. Kaufmann et al. (2010), for illustration, admit the limits of the Worldwide Governance Indicators (WGI) and the problems in gauging institutional quality, indicating that linking institutions and economic development is complex and challenging to capture in a single indicator. Overall, the examination of the studies specifies a complicated and nuanced link between institutions and economic development and that the factors that impact economic growth can change depending on the situation and the period.

3. Looking into the 2024 Nobel Prize

If we look at the Nations of the World, the economic disparity between countries is evident. To say it honestly, the world's richest 20% are 30 times richer than the world's poorest 20%. Moreover, the existing income gap is widening. Therefore, reducing the income gap between countries also poses a challenge. The role of social institutions in achieving the goal of economic growth is also not small. The 2024 Economics Nobel laureates should also be evaluated as relevant to raise awareness about the role played by social institutions in reducing economic disparity and achieving economic growth.

3.1 The Tale of the Two Cities

The Nobel laureates studied mainly the city of Nogales on the US-Mexican border. Nogales - Arizona is a city in the US, and Nogales - Sonora is a city in Mexico. Although there are no fundamental differences in topography, climate, culture, and lifestyle, the economic conditions of both cities are very different. The people of Arizona are blessed with a high standard of living, economic stability, high life expectancy, and excellent education. But Sonora has a completely different social atmosphere. Sonora is impoverished by poverty, organized crime, and corruption. History has shown that many firms are reluctant to start new ventures, which makes the city of Sonora, Mexico, even more economically backward.

Here, it is understood that the crucial factors behind the transformation of regions with the same culture, climate, and way of life into different economic conditions are not their geography or culture, but their '*Institutions*'. Those who live north of the border live within the economic system of the USA. For them, more opportunities, educational facilities and employment opportunities are available. Moreover, people who are part of the existing political system in the US also enjoy a wide range of political rights. Meanwhile those in the South of the border are going through a completely different life situation. Mexico's social systems, institutions and political system, set limits to people's ability to influence law-making and in their democratic rights.

A similar pattern of economic development and prosperity is generally evident in American-Mexican regions that could also claim socio-cultural similarities. However, opposite economic and social conditions can be observed in both regions. This regional disparity was the main concern of the Nobel laureates. According to them, exposing the divided city of Nogales was not just an isolated historical event, rather, it is a clear pattern with roots stretching back to the colonial period.

3.2 Colonial Institutions

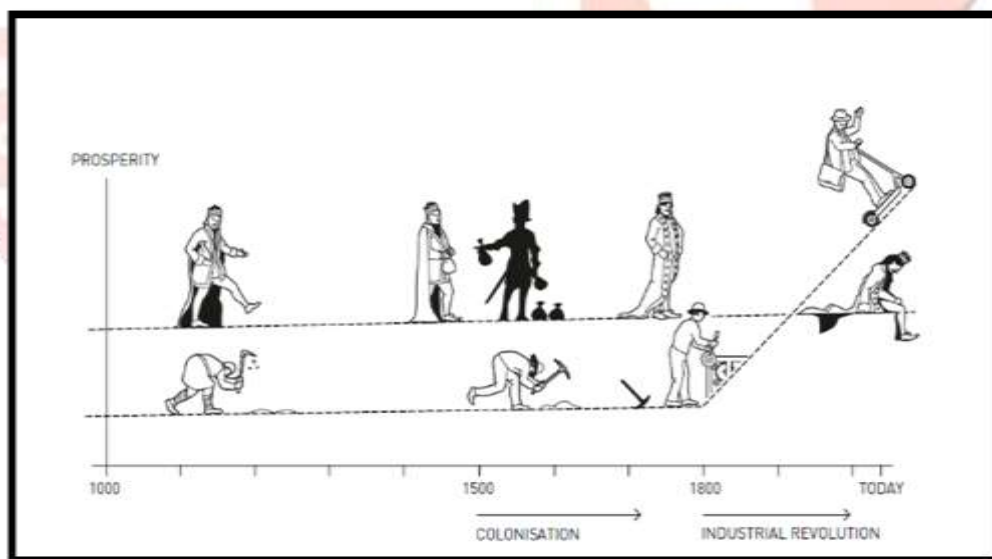
As Europeans established colonies around the world, they dramatically changed the systems and institutions that existed there. Moreover, European strategies were not uniform everywhere. In some colonies, the European's aim was simply to exploit the indigenous peoples and their natural resources for their own benefit. But elsewhere, they were also concerned with establishing 'inclusive' political and social systems aimed at the long-term benefits of European immigrants.

A crucial factor influencing colonization was the population density of such areas. In densely populated colonies, Europeans naturally expected collective resistance from the population. Therefore, very few Europeans were interested in colonizing densely populated areas. On the contrary, they naturally expected relatively less resistance from less densely populated areas. Hence Europeans mostly focused on such areas.

Europeans were interested in establishing extractive institutions (where power and resources were concentrated in the hands of a small elite or ruling class) in areas with few colonists. It set a limit to the political and social rights of the natives. On the contrary, they also consciously took care to build inclusive socio-economic institutions in areas where there were more colonists. Such social institutions encouraged them to work hard and invest in their homelands to ensure growth. Here the colonies also had access to more political and social powers.

3.3 The Fall and the Pointer to Change

Coming to the two cities, paradoxically, it seems that the currently poorer regions were relatively richer about 500 years ago. Urbanization, if taken as a measure of prosperity, is better in Mexico under the Aztecs than in North America. In the relatively poor, sparsely populated Northern Region, European colonists created social institutions aimed at their long-term prosperity. Meanwhile, extractive institutions were established in the rich, densely populated Mexican side. It was naturally growth-limiting. Social institutions established in such impoverished areas paved the way for massive economic progress following the Industrial Revolution in the mid-nineteenth century.



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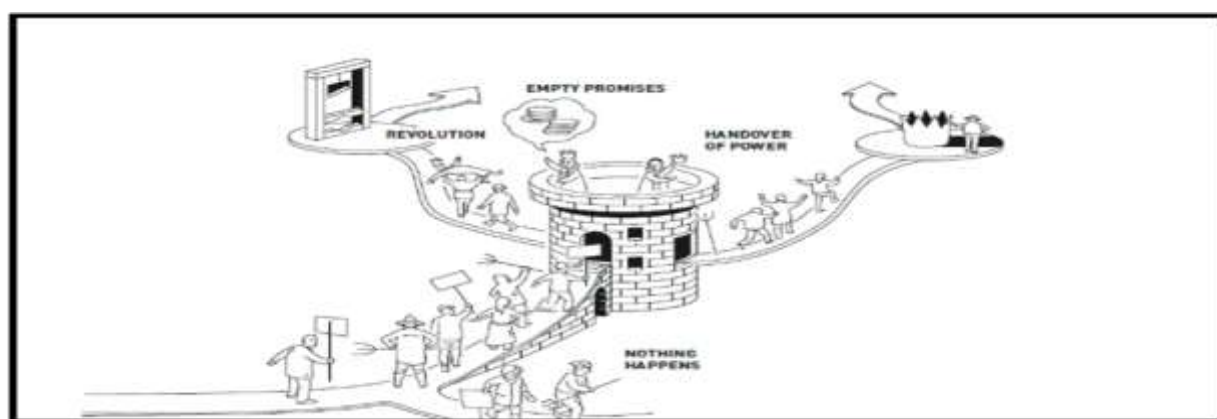
Acemoglu, Johnson, and Robinson found a clear chain of relationships as described above. Institutions established to exploit Indigenous populations were found detrimental to long-term economic growth. Conversely, institutions that emphasize economic independence and the rule of law in colonies fostered long-term development. Although an extractive system only serves the short-term financial gain of the elite, the establishment of inclusive institutions and the restoration of the rule of law helped to achieve long-term benefits for all.

There is something else that Laureate's observations and studies point towards. There exist constant conflicts over power and also an issue of trust between the ruling class and the people. People don't trust their promises of economic reform as long as the political system is designed to benefit only the elite. At the same time, even if a new system is introduced, the elites have a credence that the people will not throw

them out for their loss of economic benefits in the past. Such a commitment traps the common people in continuing the domination of extractive institutions and elite classes.

Even if, the situations are like this, the Nobel laureates found that there are some ways of restoring democracy in the respective regions. Even though the people of non-democratic countries lack formal political power, they have a weapon that the ruling elites fear. The public at large acts as a huge force. Often such people can mobilize the masses and become a great revolutionary force. The more peaceful their threat of revolution, the more successful it will be. Through the peaceful revolutionary movement, people can mobilize more people in protest. As mass unrest intensifies, the elite will face an unprecedented dilemma. It goes into their new tricks of promising economic reforms, but people are unlikely to believe in such promises. Then only one option is left before the elite state - transfer of power and restoration of democracy.

Laureates' model of how political institutions are formed has three components such as (i) the conflict over how resources are allocated and who has the power to do so in society (ii) the possibility of mobilizing the masses and seizing power through revolutionary action and intimidation and (iii) the problem of commitment to transfer power to the people as the only possible alternative. This model of the Nobel laureates can be seen as useful in explaining the process of democratic restoration that took place in Western Europe in the late nineteenth and early twentieth centuries.



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4. Conclusion

In summary, Acemoglu, Johnson, and Robinson's constructive research helped to explain what factors determine the economic prosperity of countries on a long-term basis. Their research highlights the vital importance of political and economic institutions established during colonial rule. The theoretical expositions of the trio depict how difficult it is to reform extractive institutions, even though it can happen under certain necessary conditions. The research experiments and findings of the Nobel laureates are not limited to the field of Economics. They open up new dimensions in the changing political and social dimensions. Emphasizing economic progress and growth has a historical place. That is what the Swedish Academy calls upon the Nations of the World through the message of the Nobel Prize.

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