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GOVERNMENT FAILURES IN DEVELOPMENT

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ABSTRACT

This paper takes as a given the proposition that, in many developing countries, governmental policies have been highly distortive and harmful to economic growth. These policies have included omissions, such as neglect of infrastructure, and commission such as highly restrictive trade regimes and credit rationing. The issues arising from recognition that governments, like markets, are imperfect are discussed.

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Early development economists recognized the role of government in providing "social overhead capital", or "infrastructure" to facilitate economic development. However, most analysis focussed on a second role: government should, they believed, undertake activities that would compensate for "market failures". These were regarded as being so much more extreme in developing countries as to make their economies different not only in degree but in kind from industrial countries. Market failures were thought to result from "structural rigidities", which were defined as a lack of responsiveness to price signals.[1] It was therefore concluded that governments should take a leading role in the allocation of investment, control the "commanding heights" of the economy, and otherwise intervene to compensate for market failures. Indeed, some asociated "development economics" with structuralist views and who believed that development economics was different because markets did not function. For retrospective assessments, see Hirschman (1981) and Rosenstein-Rodan (1984).

Whether this emphasis on market failures and the role of government only provided an ideological justification for what would have happened anyway, or whether governments assumed a central role in the economy because of these beliefs is not particularly relevant. The fact is that, by the 1970s and early

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1. The term "structuralism" was used to describe analyses of economists who believed that various institutional features of developing countries' economies resulted in very low, if not zero, price elasticities and responsiveness to incentives. For a description, see Streeten.

1980s, governments in most developing countries were mired down in economic policies that were manifestly unworkable. Whether market failures had been present or not, most knowledgeable observers concluded that there had been colossal government failures. In many countries, there could be little question but that government failure significantly outweighed market failure (for example, see World Bank (1983a) and Srinivasan (1985)).

There were many failures, both of omission and commission. Failures of comission included exceptionally high-cost public sector enterprises, engaged in a variety of manufacturing and other economic activities not traditionally associated with the public sector. Notable among these were: state marketing boards, which often served as a monopoly distribution distribution network and frequently also provided inputs (erratically, and often heavily subsidized if not free) to farmers[2]; state ownership of retail shops for the distribution of foods and other items deemed essential; state operation of mines and manufacturing activities;[3] state enterprises accorded monopoly rights for importing a variety of commodities; nationalized banking and even insurance operations; even luxury hotels are often found in the public sector. In

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2. Marketing Boards experienced sharp increases in costs, and hence generally lowered real returns to agricultural producers. In Tanzania, for example, it is estimated that the farmers' share of final sales value of export crops fell from 70 percent to 41 percent in the 1970-80 decade. The average real price to producers was half its 1970 level in 1980 although the world price had increased by 17 percent. See World Bank (1986), Pp. 74-5. The Ghanaian Cocoa Marketing Board began with a government share of sales revenue of 3 percent in 1947-48; that share rose to 30 percent in the mid 1950s and to 60 percent in 1978-79. The CMB's expense share was about 20 percent, and farmers received the residual. By 1979 Ghanaian producers received half the real return for cocoa that they had received ten years earlier, and production had fallen by more than half. World Bank (1983b), p. 77.

3. In many countries, state-owned enterprises account for more than 50 percent of manufacturing output and value added. For Tunisia, Egypt, Ethiopia, and Burna, the percentage is in excess of 60 percent of manufacturing value added. See Short for additional data.

addition, government investment programs were highly inefficient and wasteful; government controls over private sector activity were pervasive and costly; and government public sector deficits, fuelled by public sector enterprise deficits, excessive investment programs, and other government expenditures, led to high rates of inflation, with their attendant consequences for resource allocation, savings behavior, and the allocation of private investment.

Complementary to these phenomena were failures of omission: deterioration of transport and communications facilities, which raised costs for many private (and public) sector activities; maintenance of fixed nominal exchange rates in the face of rapid domestic inflation, buttressed by exchange controls and import licensing; insistence upon nominal rates of interest well below the rate of inflation with credit rationing so that governments could supervise credit allocation among competing claimants; and failure to maintain existing infrastructure facilities.

As by-products of these failures, large-scale and visible corruption often emerged. Further, evidence mounted that many of the programs and policies that had been adopted with the stated objective of helping the poor had in fact disproportionately benefitted the more affluent members of society.[4] All of these phenomena took place in the context of pervasive government involvement in, and control over, economic activity.[5]

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4. In most developing countries, the large-scale farmers benefit both absolutely and proportionately more than small-scale farmers, for whom inputs may be physically unavoidable, from input subsidies. See Johnson. There are many instances of subsidies to consumers where more than half the benefits go to the top half of the income distribution. See, for example, Siamwalla and Suthad on Thailand, and World Bank (1986), Pp. 74-75, and Bhalla and Glewwe on Sri Lanka.

5. It is arguable whether controls over economic activity in developing countries were greater or less than those in centrally planned economies. Certainly, they were usually less pervasive for agricultural output although Tanzania may provide a counterexample. For industry, when private activity did obtain, import licensing effectively determined the share of individual firms

"Market failure" has always been defined as being present when conditions for Pareto-optimality are not satisfied in ways in which an omniscient, selfless, social guardian government could costlessly correct. One of the lessons of experience with development is that governments are not omniscient, selfless, social guardians[6] and corrections are not costless. Two questions arise, however: what is the counterfactual to "government failure" which in principle defines it in a way parallel to market failure?;and is government failure worse than market failure?

A natural definition, parallel with that for market failure, would be to use as an ideal the achievement of a Pareto-optimal situation at a point in time and over time through interventions offsetting any deviations from the conditions under which a market solution will be Pareto-optimal. Government failure would then be the sum of actions and failures to act which resulted in a less-than-optimal situation. The difficulties with such a definition are obvious: all uncorrected market failures would be government failures and, in addition, government interventions leading to greater deviations from efficient use of resources than a market outcome would also be so regarded. However, if, instead, one uses the narrower definition of government failures - those actions of government that lead to an outcome inferior to that which would be observed under laissez-faire - there are two major difficulties: 1) there is no distinction made in this definition between government failures to provide essential public goods, such as maintenance of law and order, and

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in inputs of raw materials and intermediate goods; investment licensing and capacity licensing were frequently prerequisites for operation; there were price controls on outputs; regulations decreed the nature and extent of worker training, housing, medical care, and so on. See, for example, Krueger (1975).

6. James Buchanan has been in the forefront of those seeking a more realistic theory of government. See Buchanan.

government actions leading to greater private departures from first-best than would otherwise occur; and 2) the counterfactual is empirically unobservable. A short essay such as this cannot hope to grapple successfully with the problem, but it should be borne in mind as the argument proceeds.

Turning to the second question, whether market or government failure is worse is inherently unanswerable, especially in light of the absence of a satisfactory definition of government failure. If one takes as a rough-and-ready standard that a successful government will undertake policies that result in a satisfactory rate of growth of living standards relative to the available resources, there is some suggestive empirical evidence. First, there is no evidence that living standards fell in the now-developing countries prior to 1950, a time when many observers associate with a period of laissez-faire. In many African countries, however, living standards have been been falling - in some cases precipitously - since.[7] The latter period has been one of active government intervention, and there is no other obvious reason for the difference in performance in the two periods.

It is also suggestive, but not conclusive, that savings rates in many developing countries rose sharply from the 1950s to the 1970s, while growth rates showed little change, or even fell. India's savings rate, for example, rose from 14 percent in 1960 to 22 percent of GNP in 1987, although the growth

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7. It is estimated that Ghanaian per capita income in constant prices fell at an average annual rate of 1.3 percent between 1960 and 1982 - an implied drop in real living standards of about 25 percent before the recession of the 1980s had its impact. For the period from 1965 to 1987, the estimated rate of decline in per capita income is 1.6 percent per annum. Of the thirty-six low-income countries for which the World Bank had data in its 1989 World Development Report, there were 12 whose per capita incomes were lower in 1987 than they were in 1965. Some countries, such as Sudan, had earlier been classified as "middle income", and are now "lower-income" by virtue of their fall in income. Indeed, for SubSaharan Africa as a whole, per capita income in 1980 is estimated to have been below the 1970 level. See World Bank (1983b), P.27.

rate remained constant. Despite the increased price of oil and an increase in the savings rate from 12 to 20 percent, Nigeria experienced only a 1.1 percent annual rate of increase in per capita income over the same period (numbers are from World Bank (1983b) and World Bank (1989)). It is certainly plausible that higher rates of savings and investment should result in more rapid rates of growth: to the extent they did not do so, there is presumptive evidence that government policies were not growth-promoting.

This experience has naturally raised a large number of interrelated questions. They may broadly be grouped in four categories: 1). what is "the" government"?; 2) what is the comparative advantage of government?; 3) what are the dynamics of government intervention?; and 4) can a positive theory of political behavior be formulated that will help understand when and how alternative policies will evolve in the political arena?

This essay briefly examines each of these questions. It focuses on the insights relating directly to government behavior affecting economic activity and economic growth in developing countries. Of course, disillusionment with government has not been limited to developing countries, and there have been a variety of lines of intellectual inquiry running parallel to that focussing on the role of government in the development process. To date, these insights have been incorporated into the development literature only to a limited degree, although it is reasonable to expect that there will be increasing cross-fertilization. These fields of inquiry include, but are by no means limited to: public choice, organization theory, analysis of behavior with asymmetric or imperfect information, the theory of bureaucracy, the theory of regulation, and a growing field of political economy of international trade.[8]

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8. An exhaustive bibliography would go well beyond the scope of this paper. For the public choice perspective, the reader might refer to the recent collection of essays edited by Cowen. For a good survey of organization theory

What is "The" Government?

In the 1940s and 1950s, most development economists believed that markets in developing countries functioned highly imperfectly, and concluded that there was therefore a strong case for government intervention. See,for example, Rosenstein-Rodan (1984), P. 215. Implicitly, it was assumed that the government would behave as a benevolent social guardian, in the Fabian Socialist tradition. Economists would serve in government, calculating shadow prices and formulating planning models. Selfless bureaucrats would then carry out the plans. Coordination and administration of public sector activity was implicitly assumed to be costless. Moreover, as long as technocrats were in any event going to decide upon an investment and production plan, it was a logical next step to believe that the activities so determined should also be carried out in the public sector. Tinbergen (1984) provided a typical example of this viewpint in his "Pioneer" lecture when he concluded (p. 326): "The type of ownership of the means of production is much less important for an enterprise's efficiency than the quality of its management. So efficiency considerations need not be a stumbling block if public enterprise is chosen as a means for furthering a country's development. Rather, the nonavailability of sufficiently large private capital is the decisive point."

Experience with development over the past forty years has led to considerable skepticism about this view. One must ask why economists were ever comfortable with the simultaneous beliefs that individuals in the private sector act in their self-interest and that individuals in the public sector

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in relation to informational asymmetries, see Stiglitz (1988) and Radner (1987). For the theory of regulation, see the survey by Baron(1989). For the political economy of international trade, see Baldwin (1986). 1985

are motivated by a Benthamite vision of social justice. In addition, one must ask why collective decisions are likely to be the result of the same utility calculus as individual decisions.[9]

At a more practical level, however, other questions arose. Decisions regarding economic policy were not made by economists/technocrats, except in rare instances. Political pressures often shaped economic programs in ways that were not consistent with the ideal resource allocation goals initially envisaged. Pressure groups often exerted strong disproportionate influence over policy formulation, and policy execution was far from what had been intended. Corruption and favoritism surrounded bureaucratic allocations of investment licenses, import licenses, and the awarding of government contracts.

Although the infant industry argument was invoked as a basis for protecting domestic industry from foreign competition, for example, the scope and height of protection was usually far greater than could be defended on infant industry grounds. In Turkey, effective protection rates (ERPs) of well over 200 percent were frequent twenty years after the start-up of infant industries (Krueger and Tuncer, 1982), and Turkish protection was not regarded as unusually high. In India, Bhagwati and Srinivasan found 39 industries (of a 76-industry classification) with ERPs in excess of 100 percent in 1968-69. One industry was estimated to have an ERP equal to 3,354 percent!

Not only was protection high, but it was conferred in ways which gave virtual monopoly power to domestic enterpreneurs. Efforts to remove this "temporary" protection were infrequent and, when they did occur, met with great resistance.[10] In effect, the decision to grant some infant industry

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9. These are the same questions that are being raised by Buchanan and others about the role of government in advanced economies.

protection had several results: it resulted in pressure groups lobbying for continuation of the protection; it reduced the future power of the technocrats to formulate economic policy; and it created incentives which did not induce maximal effiency of the enterprises.

The litany could go on and on. The question here, however, is what lessons may be learned from these experiences for economists concerned with analysis of economic policy alternatives. A starting point is to recognize that "government" consists of a multitude of actors - politicians who must seek political support from various groups, bureaucrats, technocrats, and so on. There are often divisions within each of these groups, and it is rare that any individual or any group is unconstrained in its decision-making or implementation functions.

Although there are no doubt selfless civil servants and politicians concerned with the public good, not all individuals are selflesss, and it may be more realistic to assume that individual actors within the public sector are as concerned with their self interest as those in the private sector. Self-interest may be focussed on survival, on promotion, on re-election, or on other rewards.[11] On occasion, these achievements are consistent with good technocratic analysis like carrying out an appropriate cost-benefit analysis and correctly sizing and placing a dam. But on other occasions, the

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10. See, for example, the discussion of the Philippine case by Haggard and of Argentina by Kaufman. See also Nelson's generalizations, P. 352 ff.

11. Although corruption inevitably accompanies a set of controls which create large divergences between private and social profitability, self-interest may lead to undesired behavior in its absence. For example, Papanek in commenting on the tendency to neglect agriculture in Pakistan, noted that "Farming is a rather morbidly dirty business that has little appeal to the...poet-civil servant whose interests tend more toward an ever whiter shirt and a higher capacity air conditioner..."

decision-maker may well attempt to minimize social cost of a given activity subject to winning reelection, or possibly to maintaining or at least avoiding diminution of chances for promotion.

Moreover, even when there are no conflicts of interest, administrative difficulties can be overwhelming, either because of a shortage of trained personnel or because of the enormous administrative difficulties of establishing and maintaining complex operations within the public sector. On occasion, as for example when a marketing board is supposed to purchase the harvest, lack of facilities can frustrate bureaucrats. On other occasions, however, poor administration - such as siting collection points far away from farmgate and inability to pay farmers for months after harvest - of economic functions which require timely action is a major impediment. In still other instances, the political imperatives arising from the need to treat remote uneconomic areas equally with other regions, from the mandate to hire politically connected, rather than qualified, personnel, or from political pressures to underprice output can result in major problems.

From this it follows that an important question is that of institutional design: what sets of institutions and incentives are likely to be most conducive to achieving a least-cost outcome?[12] Understanding of this question is at best very partial, but two examples may illustrate. First, in many developing countries, parastatal enterprises were established which legally

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12. I omit here the difficult questions arising from a judgment as to Pareto-optimality of decisions in circumstances where there is a clear consensus of voters for an obviously inefficient outcome. There are enough glaring instances in which only a few relatively affluent individuals will benefit from a particular path, and in which there is a manifestly lower-cost solution, to permit discussion of these issues in circumstances where it is reasonably clear that _if_ the public were informed as to costs, benefits, and alternatives, an alternate decision would be made. For a discussion of some of these issues in a different context, see Krueger (1989).

were entitled to borrow from the Central Bank in the event of losses. Changing this procedure so that some form of action, embarrassing or worse for enterprise managers, reduced losses. One such procedure is to require approval of a high official such as a member of the Cabinet or the Prime Minister before borrowing is permitted. Another is to make those losses a line item in the government budget.[13] A second example is the state marketing boards that were established and given monopoly power over distribution of inputs to farmers and marketing of specified farm products. Removal of monopoly power by itself has spurred increasing efficiency of the state enterprise.[14]

What is the Comparative Advantage of Government?

Most observers believe government should undertake a list of items -- usually referred to as "infrastructure" -- that has some aspects of a public good. In addition, most infrastructure has many consumers, most of whom have little opportunity in their capacity as consumers to reward good providers or penalize poor ones; similarly, mopst infrastructure is fairly large scale. The two characteristics combined provide some basis for believing that the market may not function terribly well, and suggest that the disadvantages of large-scale organization and bureaucracy will be least in these instances.

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13. To be sure, enterprise managers often face a number of constrants, including politically mandated hiring, locating in areas which are not necessarily economic, and so on. Hence it is not always clear that even a good manager could make a profit. But the point here is that losses tend to diminish when the manager is confronted with greater disapproval, and that this disapproval is more likely when the size of the losses must be publicly reviewed. See World Bank (1983a) for an enumeration of concrete examples of these, and other institutional, changes that have altered performance.

14. For a discussion of measures for improvement of public enterprise efficiency, see Jones and Papanek, 1983.

Users of a road, for example, may not individually have sufficient incentive to monitor and hold accountable those providing road construction and maintenance services. This might imply that market provision of roads may not have an advantage over a political process that is somewhat responsive to citizens.[15] This may be especially true at early stages of development, when the presence of indivisibilities may imply that provision of infrastructure might not be privately profitable in the short run.

Infrastructure activities are often large-scale, where administration and organization are important. Moreover, the nature of government is that services provided to some probably must be provided to most, if not all. Political pressures to provide rural postal service, agricultural extension services to all farmers, and similar examples come to mind. Under these circumstances, most governmental activities require a considerable amount of organization and administration - both activities utilizing individuals of significant educational attainments. Since the available supply of skilled manpower is limited in developing countries, and resources for education are scarce, employing highly educated persons in the public sector or educating more persons in order to increase the supply available to the public sector is far from costless.

It is difficult to realize how limited administrative capacity in some developing countries is. Examples of these abound: the delivery of fertilizer too late in the season to be effective (see for example Fernando and Jensen), of an inability to collect crops for which the government had made the marketing board the monopsonistic buyer (see Krueger, Ch. 4 for a partial

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15. Toll roads, of course, may be a viable alternative, but collection costs might outweigh their benefits for smaller roads.

survey pertaining to agriculture); an average delay of 18 months in approving investment licenses (see Krueger 1975), and so on.[16]

Based on those propositions, two conclusions can be drawn. One is that undertaking any activity in the government sector is costly because it places an even greater drain on scarce administrative and organizational resources; not only will scarce talent be drained from the private sector, but administration of other governmental activities is likely to be weakened. The second is that an economically efficient division of economic activity between the public and the private sector will be based in part on the administrative and organizational requirements of the two alternatives.

Government is a non-market organization, and that it generally must do things on a large scale. It should follow that activities such as maintenance of law and order (including especially enforcement of contract), provision of information (such as agricultural research and extension) and provision of basic public services which are inherently large-scale in scope (such as roads and communications) are those in which the government is at no disadvantage in providing services on a large scale and where private agents may face a disadvantage in attempting to do so.

Although the theory seems clear, little work has been done on the comparative advantage of the public sector in these activities. What seems clear from experience is that focus on other activities (manufacturing, regulating credit and foreign exchange markets, investment licensing, etc.) has diverted governmental resources and efforts away from those areas of

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16. Even efforts to privatize can be crippled by administrative delay. Early in 1990 it was reported that Nigerian citizens, after enthusiastically subscribing to the first offering of shares in a previously publicly-owned enterprise, were failing to subscribe to later offers: officials had taken more than six months to allocate shares, holding the deposits without interest in the interim, and allocating far smaller shares than had been bid for.

activity in which the government may have a comparative advantage. Government failure may have consisted as much in failing to provide the infrastructure in which government has a large comparative advantage as it has in providing poorly things in which it does not have a comparative advantage.

Those who are critical of actual patterns of government intervention are often accused of wanting a smaller role for government. If, as seems to be the case at least in the least developed countries, there is a severe limitation on the number of persons with even minimal administrative and organizational skills available, using those persons for e.g.,allocating investment licenses or establishing an organization to distribute free fertilizer, reduces the government's capability to organize construction and maintenance of roads, communications, schools, and to develop other institutions where government's comparative advantage is far stronger. In many developing countries, the poor quality and limited supply of infrastructure constitutes a major source of high costs for all producers and consumers within the economy.

Are Some Types of Government Less Costly Than Others?

Disillusionment about the selflessness, benevolence, and costlessness of governments has led to a number of insights. Among them, three are important and worth mention here. First, when economic policies create something that is to be allocated at less than its value by any sort of government process, resources will be used in an effort to capture the rights to the items of value. Second, whenever a government policy has clearly identifiable beneficiaries and/or victims, those groups will tend to organize in support or opposition to the policies and then lobby for increasing the value of the gains or reducing the value of the losses from those policies. This is so

regardless of whether the policy instruments themselves were adopted at the instigation of the beneficiaries or were initially the result of public interest decisions.[17] Third, one may differentiate the interests of different groups and institutions within the government. "Spending ministries" will tend to become advocates of programs and policies falling within their domain. By contrast, finance ministries tend to be public interest agencies to a greater degree.

The first proposition, that people will spend resources to capture property rights from the government, is the proposition that rent-seeking behavior will occur. Whether rent-seeking takes the form of illegal activity or of legal activity is not usually relevant for economic analysis of its costs, although corruption and other forms of illegal activity do undermine the legitimacy of government, and hence reduce its capacity for maintaining law and contracts, and providing other services that are essential for the smooth functioning of economic activity. What is relevant is the economic costs of many policies - minimum wage legislation, import licensing under quantitative restrictions, credit rationing, and so on - are far greater when rent-seeking takes place than traditional welfare cost analysis would suggest. suggest. Grais, de Melo and Urata (1986) provide one estimate of the cost differentials. In some instances, policies that might otherwise appear desirable to meet noneconomic objectives, or even to correct "market failures", may result in a situation even less satisfactory than that prevailing before the policy was put in place.

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17. It has often been assumed that intervention originates from the lobbying of special interest groups. This is the perspective of Olson (1965). While that is certainly often the case, it also happens frequently that, once an intervention starts - regardless of motive - those benefitting from it organize to exert political pressure to maintain and increase their benefits. See Krueger (forthcoming) for one example.

The second proposition, that groups will spring up to defend their positions, has several implications.[18] An initial political "equilibrium" may not be a long-term equilibrium, as newly formed pressure or interest groups lobby for increasingly favorable, or less unfavorable, treatment. For example, once a system of protection against imports is in place, protected producers will generally lobby for higher tariffs and/or lower quotas, using contrasts with other levels of protection and other arguments. Likewise, initially unprotected groups will begin lobbying for protection, on the grounds that their case is at least as strong as that of already-protected interests. More generally, there will be a tendency for increasing proliferation of categories and of policy instruments, as various groups assert conflicting and competing claims,[19] and this proliferation should also be counted as a cost of the original policy.

One of the groups that normally springs up is the group administering the policies. Once a particular policy is regulated, either a group is

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18. For a model of political competition built on this insight more generally, see Becker(1983).19. For example, by the mid-1970s, the Mexican government administered a complex set of investment incentives. The country was divided into three zones, I, II, and III. Mexican investment incentives were based on eight eligibility criteria. These were whether the activity was: new within the area; processing of agricultural or other raw materials of the area; new in the country; covering deficits of at least 20 percent of the region's consumption of the commodity in the preceding year; increasing productivity sufficiently to lower prices by at least 5 percent; expanding productive capacity advantageously; reinvesting in zones II or II of the proceeds of sales of land and buildings from zones I and II. Thee were 9 different incentives: reduction of 50 percent or full remission of duties on imports of capital goods; reductions of a similar magnitude of duties on imported intermediate goods and raw materials; reductions of 50 to 100 percent in stamp taxes; reductions of the same magnitude in taxes on sale of land and buildings; accelerated depreciation rates; reductions in federal sales taxes; reduction of 20 to 40 percent in income taxes; improved credit access and terms through the Banco de Mexico; and technical assistance for small companies. See Business Mexico, 1973, P. 172. I am indebted to Derek Hardesty for this example.

established, or an existing unit of government is expanded, to fill the function. Either way, a part of the government will usually become an advocate for maintaining the functions involved and, in many cases, extending them. Those administering the policies necessarily believe that they are doing something important, and also know that discontinuance of the function would result in a loss of jobs for some and of bureaucratic power for others.[20]

To make this tendency to bureaucratic advocacy even more costly, bureaucrats tend to interpret their own ineffectiveness as a consequence of insufficient resources and policy instruments at their command. When price controls are imposed on food crops, for example, farmers tend to shift to the production of other commodities. Frustrated bureaucrats are likely to advocate controlling prices of other commodities, and possibly nationalization of wholesaling. When these controls are less effective than anticipated because of smuggling or other reasons, still other policy instruments are sought.

The political logic of economic policy evolution is little understood. Yet, in most developing countries, it would be more accurate to state that policies are in a continuous state of change than to assert that a policy, once laid down, is consistently adhered to. Certainly, the advocate of a particular policy intervention in a developing countries should at least ask what forces leading to further interventions will be created by the inauguration of the policy under consideration.

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20. Political scientists refer to the "iron triangle", in which bureaucrats have an interest in extending the scope of their activities, which are done in ways which are visible to the voters. Politicians seek reelection, and thus support - or at least dare not oppose - bureaucratic activities that provide services to constituents. Voters are made cognizant of the services provided by bureaucrats and therefore support the politicians. While the "iron triangle" was first analyzed in the context of the American congressional system, there are numerous instances where it would appear to apply in developing countries. See Fiorina (1978) for an analysis.

The third proposition, that there are different interests within the government, is a direct corollary of the view that many of those within government are self-interested. Typically, each spending ministry will want to increase spending, believing it in the social interest that those activiites within its particular domain are the most important. The finance ministry, by contrast, will be more concerned about raising revenues, and is therefore less likely to represent special interests.

In this regard, ideology becomes an important determinant of what is, and is not, generally acceptable. Clearly, in democratic societies, policy makers within governments have autonomy only insofar as the voters acquiesce in their activities, whether that permission is out of ignorance or out of sanction for their activity. At least to a degree, acquiescence is a result of the general "ethos" surrounding economic policy.

What Guidance for Policy Makers?

These considerations lead directly to the final question: based on what we know or suspect about government behavior, can any guidance be given to the policy maker? The answer is yes, although a great deal more needs to be learned.

First, and most obvious, is that action by government is not costless. Any policy affecting the allocation of resources, any economic activity undertaken in the public sector, and any regulation of private economic activity, can be undertaken only when there is a specified set of procedures or criteria for deciding what fits within the scope of the enunciated policy and also an administrative apparatus for implementing the policy. It is grossly insufficient for economists to assert that the existence of market failure

implies that there is a case for government intervention. What is needed is the specification of a set of criteria, or rules, by which interventions will be administered, and an indication as to the process by which this will occur. Then, judgments may be made as to the administrative cost and feasibility of the activity, as well as the likelihood that political pressures will quickly alter the initially-chosen process.[21]

Even when it appears that government action would actually be effective, there is something of a presumption in favor of policies and prgrams requiring a minimum of administrative and bureaucratic input. This is both because policies, once in place, appear to have a life of their own and because they divert scarce administrative resources from those in which governmental comparative advantage is stronger.

Third, if alternative mechanisms and policies might be able to achieve a given social or political objective, a presumption exists in favor of choosing a mechanism which provides least scope for rent-seeking. For example, even though tariffs invite what Bhagwati (1982) called DUP (for directly unproductive activities) like smuggling, underinvoicing, and lobbying to increase protection, they are probably less open to rent-seeking behavior than are quantitative restrictions on import licenses. Since at least some tariff revenue is likely to be turned in to the government, there are fewer rents to be sought than under equivalent quantitative restrictions. Likewise, despite the long-standing theorem that, capital flows aside, a tariff on imports and subsidy on exports is equivalent to devaluation, there is certainly nonequivalence when considering the political economy of the two alternatives:

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21. These considerations are additional to those pertaining to the choice of a least-cost policy for obtaining a given (economic or non-economic objective). There is a well-developed literature identifying first, second, and third best policy measures for the attainment of given objectives. See Bhagwati (1971).

under the tariff-subsidy alternative, there remain incentives for smuggling imports, overinvoicing exports, and so on, which do not arise in the presence of a uniform exchange rate. These examples, in turn, suggest that policies directly controlling private economic activity are likely to be less efficacious in terms of achieving their objectives than policies that provide incentives for individuals to undertake the activities which are deemed desirable. This can often be achieved by finding ways which strengthen the functioning of markets.

Yet another implication is that it is preferable to choose policies and institutional arrangements that will force tradeoffs to be faced in the administration and execution of policy. On this reasoning, a tariff commission would tend to be more protectionist than would a ministry of trade; the latter would have a constituency of exporters as well as of protected industries. Similarly, requiring that government programs be funded out of government revenue, rather than financed off-budget, should result in more satisfactory outcomes.[22]

Finally, there is a question of transparency. When the costs of a policy are obscure, special interests in the private sector and government have a greater opportunity to use those policies for their own advantage without incurring the disopprobrium of voters and other politicians. Thus, choosing the policy with lower information costs is usually preferable.

Questions

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22. The fact that tariffs generate revenue, while export incentives cost revenue, is probably an important reason for the prevalence of tariffs relative to export subsidies.

This essay has suggested some of the emerging lessons from the development literature.These answers are preliminary, and indeed rest on a less sound base than one could wish. The defense for putting them forth at all is merely that economists have demonstrated an incredible naivete with regard to government behavior.

What has been learned is that political actors have objective functions and constraints that need not mirror the common good, or even the preferences of the large majority of the public. As aptly expressed by Bates (1981, P. 6): The collective optimism of the nationalist era has given way to a sullen and embittered recognition that the sacrifices of the many have created disproportionate opportunities for the few. How do policy choices, ostensibly made for the public good, become the basis for private aggrandizement? By what process does a vision of public order erode?".

The agenda for research on these questions is huge. At a general level, there are innumerable questions as to how political and economic markets interact. At more mundane levels, there are endless opportunities for empirical research, analyzing the functioning of alternative policies and institutions, documenting and hopefully quantifying policy interventions, the responses to them, and their evolution over time.

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