

## Leszek Balcerowicz

### Title

Institutional Economics

### Outline

Definition and the main types of institutions and their systems. Role of institutions versus psychological and social factors in economic performance. Importance of political and economic institutions for economic growth. Types of property rights systems. Monetary regimes. Financial system. Public finances, taxes. Institutions of labor market. Institutions and economic growth. Institutional change.

### Purpose

To present how institutions affect economic performance, and what drives their changes.

### General required reading

- A. Balcerowicz L., *Socialism, Capitalism, Transformation*, Central European University Press, Budapest 1995;
- B. Balcerowicz L., *Toward a Limited State*, "Cato Journal", Vol. 24, No. 3, Fall 2004;
- C. Balcerowicz L., Institutional System and the Quality of Life (powerpoint presentation)
- D. Baumol W., *Good Capitalism, Bad Capitalism, and the Economics of Growth and Prosperity*, Yale University Press
- E. Hazlitt H., *Economics in One Lesson*, Three Rivers Press, 1988.
- F. Oleh Havrylyshyn, Xiaofan Meng, and Marian L. Tupy, *25 Years of Reforms in Ex-Communist Countries: Fast and Extensive Reforms Led to Higher Growth and More Political Freedom*, Cato Institute, POLICY ANALYSIS NO. 795

### Schedule

#### I. The Scope of Institutional Economics – Introduction.

1. Institutional factors in mainstream economics.
2. Research areas of economics which focus on institutions.
3. Main goals of institutional economics:
  - basic concepts, measurement of institutional variables;
  - dimensions and types of institutional systems;
  - relations between institutional factors in various areas;
  - institutional systems and outcomes;
  - dynamics of institutions (institutional change).

## Literature:

- Coase R., *The New Institutional Economics*, "American Economic Review", Vol. 88, No. 2, May 1998, 72-72;
- Cooper R. and T. Ulen, "Law and Economics", Pearson Education, Inc., Chapt. 1, 2008;
- North D.C., *Institutions*, "Journal of Economic Perspectives", Nr 1, 1991;
- Lemieux P., *The Public Choice Revolution*, "Regulation", Fall 2004;
- Tullock G., *People Are People. The Elements of Public Choice* [in:] G. Tullock et al, CATO Institute, 2002;

## II. The Institutional System.

1. Formal and informal institutions. Institutional Systems.
2. Three interrelated components of the institutional systems.
  - The legal framework;
  - The set of organizations;
  - The mechanisms of interactions.
3. Main dimensions of institutional systems:
  - the extent of political controls over individuals;
  - the mechanisms of turnover on the positions of power;
  - the level of the rule of law;
  - the level of the law enforcement.
4. Main types of Contemporary Institutional Systems

## Literature:

- Balcerowicz L., Institutional System and the Quality of Life (powerpoint presentation)
- V. K. Blorooah and S. Iyer, "Vidya, veda and varna ..." The Journal of Development Studies, Nov., 2005, p. 369 – 1404;
- Nozick, "Anarchy, State, and Utopia", Basic Books, 1974, p. 3-138
- Balcerowicz L., Toward a Limited State, "Cato Journal", Vol. 24, No. 3, Fall 2004;
- Holmes S., *Lineages of the Rule of Law*, [in:] *Democracy and the Rule of Law*, ed. By J. M. Maravell and A. Przeworski, Cambridge 2001, chapt 1.
- Elster J., "Social Norms and Economic Theory", Journal of Economic Perspectives, Nov., 1989, p. 99-117.

## III. Political systems. Economic Systems

1. How to delineate them?

2. Socialism, capitalism, democracy: the relationships.
3. Political systems and the functioning and growth of the economy.

#### Literature

- Balcerowicz L., Institutional System and the Quality of Life (powerpoint presentation);
- Balcerowicz L., Socialism, Capitalism, Transformation, Central European University Press, Budapest 1995, chapter 7;
- Persson T. and G. Tebellini, *Constitutions and Economic Policy*, "Journal of Economic Perspectives", No. 7, 2004.

#### IV. The economic systems: the main dimensions and types

1. Conventional tools in the analysis of the state in the economy: public – private goods, externalities, market failures.
2. Forms of the State's presence in the economy:
  - ownership;
  - regulation;
  - fiscal, welfare state
  - money and monetary policy
3. Main dimensions of the economic system
  - type of property rights and structures of ownership;
  - the justice system;
  - type of coordination mechanism and the scope of market;
  - monetary system;
  - type of financial system;
  - public finance, social policy, taxes;
  - the territorial structure (fiscal federalism).
4. Capitalism and its variants.
5. Command economy.

#### Literature:

- Buchanan, J.M., *The Politization of Market Failure*, [w:] *The Economics and the Ethics of Constitutional Order*, Ann Arbor, The University of Michigan Press, 1991, s. 67-79;
- Bergh A. and M. Henrekson, *Lessons From the Swedish Welfare State*, „Wall Street Journal”, 11.07.2010;

#### V. Outcomes (performance)

1. A general concept
2. Main types of outcomes
3. Different concepts of efficiency

4. Inequality: of situation and of opportunity
5. Relationships between various kind of outcomes.

Literature:

- Balcerowicz L., *Institutional Systems, Policies, Inequalities*, The keynote speech at the 24th IPSA World Congress of Political Science in Poznań, July 2016  
[http://www.balcerowicz.pl/pliki/artykuly/48\\_Institutional-Systems-Policies-Inequalities.pdf](http://www.balcerowicz.pl/pliki/artykuly/48_Institutional-Systems-Policies-Inequalities.pdf)
- Balcerowicz L., *Socialism, Capitalism, Transformation*, Central European University Press, Budapest 1995;, Roz. 2;
- Balcerowicz L., *Toward a Limited State*, "Cato Journal", Vol. 24, No. 3, Fall 2004;
- Ferreira, H.G., M. Walton, *Inequality of Opportunity and Economic Development*, „World Bank Policy Working Paper”, 3816, January 2006;
- Becker, G.S. et al., *The Quantity and Quality of Life and the Evolution of World Inequality*, „AER”, March 2005, No. 1, s. 277-291;

VI. Institutional systems and outcomes.

1. Three types of impact

- situational
- selective
- formative

2. The relative role of institutional and non-institutional factors in determining outcomes. Institutional systems versus public policy.

Literature:

- Balcerowicz L., *Socialism, Capitalism, Transformation*, Central European University Press, Budapest 1995, p. 1-19;

VII. The psycho-social factors in the analysis of institutional systems

1. Various dimensions of a society: socio-economic, demographic, psycho-social.
2. Psycho- social invariants (the universals): a general concept.
3. The cognitive (informational) invariants and their consequences: imperfect information, information asymmetry, etc.
4. The motivational invariants motivators.
5. The psycho-social variables and the economic outcomes:
  - the relative importance of psycho-social and institutional factors (formal institutions)

- the main types of psycho-social variables (religion, social capital, trust, cultural and ethnic differentiation) and their impact on economic outcomes.

6. Institutional systems and psycho-social variables:

- the structure of human capital
- other legacies?

Literature:

- Alesina A., et al, Ethnic Diversity and Economic Performance, "Journal of Economic Literature", Sept. 2005;
- Berggren N., H. Jordahl, *Free to Trust? Economic Freedom and Social Capital*, „Kyklos”, No. 2, 2006 ;
- Glaeser E.L., *Psychology and the Market*, NBER Working Paper No. 10203, December 2003;
- Kanneman D., *A Psychological Perspective on Economics*, American Economic Review, May 2003;
- Pinker S., *The Blank Slate*, Penguin Books Ltd. 2002, p. 1-136.

VIII. Property Rights as a Basic Institutional Variable.

1. Scarce good and rights to them.
2. Property rights regimes.
3. Ownership structure.
4. Types of enterprises according to ownership.
5. Property rights and economic efficiency.

Literature:

- Balcerowicz L., *Socialism, Capitalism, Transformation*, Central European University Press, Budapest 1995; chapt. 7;
- Gonzáles-Paramo, P. H. de Cos, *The Impact of Public Ownership and Competition on Productivity*, „Kyklos”, No. 4, 2005.
- Pipes, R., *Property and Freedom*, 1999, chapt. 1 and 2;
- Schleifer, A. *State versus Private Ownership*, Journal of Economic Perspective, Fall 1998, p. 133-150.

IX. Monetary Systems, Financial Systems

1. Basic concepts, money, credit, financial intermediaries, financial markets.
2. Types of monetary systems.
3. Diversity of financial systems.
4. Financial system, financial crisis, growth.

Literature:

- World Bank, *Finance for Growth*, World Bank, Washington, 2001; p. 1-28.

- Friedman M., *Money Mischief: Episodes in Monetary History*, A Harvest Book 1994, chapt. 1, 2, 8, 10;
- Bordo M., H. James., *One World Money, then and now*, “NBER Working Paper” 12189, April 2006;
- Bordo M., A.J. Schwartz, *Monetary Policy Regimes and Economic Performance: the Historical Record*, “NBER Working Paper” 6201, 1997;

#### X. Public Finance and Taxes, the Fiscal Position of a State, the Welfare State.

1. Main dimensions of public finance.
2. Government expenditure, the welfare state, individual’s behaviors
3. Taxes, individual’s behavior, economic performance.
4. Deficit, public debt, economic growth.

##### Literature:

- Balcerowicz L., Radzikowski M., *The Case for a Targeted Criticism of the Welfare State*, *Cato Journal*, Vol. 38, No. 1 (Winter 2018), <https://object.cato.org/sites/cato.org/files/serials/files/cato-journal/2018/2/cato-journal-v38n1-chapter-1.pdf>;
- Tanzi V., *A Lower Tax Future. The Economic Role of the State in the 12th Century*, “CATO Journal”, No. 3, 2005;
- Feldstein M., *Rethinking Social Insurance*, “AER”, No. 1, March 2005;
- Bergh A., M. Henrekson, *Government Size and Implications for Economic Growth*, 2010, the AEI Press.

#### XI. Labor Market from Institutional Perspective.

1. Employment, non-employment, unemployment.
2. Differences in these variables across time and across countries.
3. Explaining these differences: the role of and the interactions between the institutional and non-institutional factors.
4. Interactions between different labor market institutions.
5. Review of international experience on labor market reforms.

##### Literature:

- Blanchard O., *European unemployment. Evolution of facts and ideas*, “Economic Policy”, Vol. 21, 2006;
- Howitt P., *Looking Inside the Labour Market: a Review Article*, “Journal of Economic Literature”, March 2002, p. 125-138;
- Nickel S., *Unemployment and Labour Market Rigidities: Europe versus North America*, “Journal of Economic Perspective”, Summer 1997 Vol. 18, No. 4, Fall 2004.

## XII. Institutional System and Long-term Growth (Successes and Failures in Real Convergence)

1. Failures and causes of failures
2. Successes and causes of successes.
3. The relative role of institutional and non-institutional factors.

### Literature:

- Balcerowicz, L., *Institutional Systems and Economic Growth*, in: A. Åslund, M. Dąbrowski, *Challenges of Globalization. Imbalances and Growth*, Peterson Institute for International Economics, Washington, DC, 2008.
- Weede E., *Human Rights, Limited Government and Capitalism*, "CATO Journal", No. 1, 2008;
- Baumol W., *Good Capitalism, Bad Capitalism, and the Economics of Growth and Prosperity*, Yale University Press.

## XIII. Transition in Europe in a Comparative Perspective.

1. Types of Institutional Dynamics
2. How to analyze economic reforms?
3. Significance of initial conditions.
4. Economic policy in transition: main areas.
5. Initial conditions, economic policy, economic performance.
6. Other transitions as a point of reference.
7. Special features of the transition in Central-Eastern Europe.
8. Special features of the political transition in the region.

### Literature:

- Balcerowicz L., *Institutional Systems and Their Dynamics, Including Good and Bad Transitions*, "The Populist Threats to the Free Society and the Reconstruction of the Liberal Project" in Stockholm, Sweden, November 2 – 5, 2017;
- Balcerowicz L., *Institutional Change After Socialism and the Rule of Law*, The "Hague Journal of the Rule of Law", No. 7, 2009;
- Balcerowicz L., *Socialism, Capitalism, Transformation*, Central European University Press, Budapest 1995;
- Åslund A. *The Great Rebirth: Lessons from the Victory of Capitalism over Communism*, Washington DC, 2014;
- Havrylyshyn O., Meng X., and Tupy M., *25 Years of Reforms in Ex-Communist Countries: Fast and Extensive Reforms Led to Higher Growth and More Political Freedom*, Cato Institute, POLICY ANALYSIS NO. 795;

## XIV. The Ways to Private Market Economy.

1. Privatization of economy

2. Initial conditions and privatization process.
3. main empirical cases of privatization.
4. The problem of optimal pace and optimal method of privatization in European post-socialist economies
5. Empirical findings.

Literature:

- Balcerowicz L., *Socialism, Capitalism, Transformation*, Central European University Press, Budapest 1995, chapter 7;
- Djankov S., Murrell P., *Enterprise Restructuring in Transition: A Quantitative Survey*, "Journal of Economic Literature", Vo. XL, September 2002, 739-792;
- Guriev S., W. Magginson, *Privatization: Lessons from a Quarter of Century*, "Beyond Transition", Oct.-Dec. 2005, p. 16-17;
- Bonin, J. P., et al, *Privatization Matters: Bank Efficiency in Transition Countries*, „Journal of Banking and Finance”, 29, 2005, p. 2155-2178.

XV. Common Fallacies in Discussions on Economy and Economic Reforms.

1. General logical mistakes.
2. Misunderstandings related to economic transition.
3. Erroneous use of empirical examples in general discussions on reforms.
  
4. Mistakes in discussions on inflation and stabilization.
5. Mistakes in discussions on social and political results of economic reforms.

Literature:

- Balcerowicz L., *Socialism, Capitalism, Transformation*, Central European University Press, Budapest 1995,, chapter 12;
- Hazlitt H., *Economics in One Lesson*, Three Rivers Press, 1988.
- Palmer T., "Twenty Myths About Market, in: "Realizing Freedom", CATO Institute, Washington DC, 2009, p. 155-181.

**Final exam:**

Written exam, students have to answer to two out of three questions. Duration of the exam is 90 minutes.