
NONMARKET INSTITUTIONS

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The last 10 years of formal economics research have yielded significant lessons on poverty. This presentation transmits the broad thrust of the literature over this period—what has been learned on topics now recognized as objects of study, but which economists still do not appear to understand. Every example given here probably has a counter example, but it is important to disregard these for the moment and move ahead with the debate.

What We Know

State and market institutions. Institutions merit priority consideration. That is where the greatest development in economic theory and applied economics has occurred in the attempt to understand the nature of poverty in poorer countries. Until the end of the 1980s, the two institutions discussed extensively by economists were the state and markets. Economists, although they borrowed ideas on the state from political scientists, did not pretend to understand the state.

In fact, an interesting dualism developed in the ways economists or development economists wrote about the state, as an agency doing almost anything it wanted, while the market, whether doing well or badly, demanded considerable scrutiny to identify the ways in which it was failing as an institution. When the state came under criticism, the comments emanated from political science, not economics, literature. Economists lacked a model of the state.

Nonmarket institutions. The big change over the last 10 years came in a growing understanding of nonmarket institutions. Economists owe this conceptual shift very much to the extensive work of anthropologists. From it came the tight modeling that buttresses our understanding of markets and increasingly, nonmarket institutions. The latter include not only the state as an agency of the populace but those institutions that lie between the individual and the state, such as household- and village-level organizations.

The hallmark of nonmarket institutions is an agreement mechanism based on self-enforcement among individuals or groups, or on the power of emotional bonds among the participants themselves. Smaller, more permanent membership institutions are often held together in this way.

A good deal of the work on nonmarket local institutions has been done in the context of local common property resource management. The development economics literature over the last 10 years reveals a far greater sensitivity than in the past to the way rural people rely on their local environmental resource base. The aspects of environmental economics that can be married to development economics reflect the growing interest in nonmarket institutions.

Malfunctioning institutions. Economists recognize that although certain nonmarket institutions may have been justified in the past because they served their purpose extremely well, these institutions may not be able cope with modernization, causing certain groups of people to fall out or become disenfranchised. Several models have been constructed to show how this process generates poverty traps. Positive feedback loops operate in such a way that even if an economy as a whole grows not only in terms of income but also in the sense of the HDI, it can happen that certain groups lose out. The merit of working with these models is that they enable us to identify such groups. The empirical literature by anthropologists and NGOs on the experience of

acute rural poverty during a period of economic growth has been captured quite well by the models.

Another kind of malfunctioning is the situation where progressive institutions are blocked by entrenched nonmarket institutions that may have had a rationale in the past but are now dysfunctional precisely because they are preventing the growth of such progressive institutions.

What We Do Not Know

Although certain societies work and others do not, the literature presumes well-ordered societies without serious civic disturbances. Observers cannot predict upheavals involving large numbers of people, but they can describe them and might even smell them coming! We do not yet know the kinds of policies or even how to think about policies that need to be formulated in a world in which people are killing one another. Economists, and probably most other people, have absolutely no understanding of this kind of total disruption. Nor does well-ordered imply a “good” society, but only a society in which policies can be predicted to work one way or the other, a society where one can have a reasoned expectation of what lies ahead.

When a society collapses, whether from groups unable to live together or from an overly oppressive state, we do not understand the processes that have brought about that calamity. This is where informal, nonmarket institutions, which pre-date market ones and their third-party approaches, can be reexamined for their capacity to forge and sustain implicit agreements. If people get together and create something communally or collectively, even just by striking a bargain, what kinds of guarantees do they have that the agreement will be carried out?

That, in my judgment, is probably the most fundamental question in the social sciences today. Nonmarket institutions represent a particular route to solving that problem. Up to now, much of the work in development economics has emphasized that a faulty third party—the state—is malfunctioning. There are already indications that even nonmarket institutions are faltering because society is falling apart. We really do not understand how to think about that.