

Institutional Problem-Solving versus Good Governance As Neoteric Paradigms for Development*

by

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Abstract

Rapid political developments and technological change have, over the course of the past decade, changed the problem environment that large multilateral development agencies face in terms of serving the needs of the agents of their donor and recipient countries. These events have led to the recognition of the importance of the role of the State in a globally integrating economy. However, this new concern with 'Good Governance'— which seeks to enhance the capacity of the State to act in a more enlightened manner— continues to address itself in terms of the orthodox development paradigm. This paradigm, which emphasizes capital accumulation to reproduce in poor countries the features associated with the success of the rich ones, has been acknowledged as having not produced the theoretical results forecasted. The paper argues that successful adaptation to the new regime requires a new representation of the problem environment based on the paradigm of 'institutional problem-solving.' This alternative breaks open the dichotomy between 'the State' and 'the People'³ central to the orthodox model and instead looks at how structuring institutions to deal with collective action problems in their relevant contexts will lead to the endogenous generation of those characteristics that the Good Governance approach superficially and in piecemeal fashion essays to recreate.

I. The State as Problem-Solver

Problem-solving is the core and constant activity of individuals. We each confront a complex environment and seek to adapt to it through both our individual efforts and through collective action. The degree to which we are able individually and/or collectively to problem-solve reflects then on our individual well-being or adaptive success. Problem-solving through collective action can be directed or coordinated through a range of facilities, from ad hoc side agreements among a few individuals to the complex of rules that characterize formal governance structures. Given a problem environment, the diverse ways in which these governance structures are designed in turn variably affect our ability to problem-solve. Variation in these arrangements range from those of the State as a fully centralized command and control apparatus to those systems of order that stress local autonomy in problem-solving.

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The State is commonly conceived in the social sciences literature as an entity possessing a monopoly prerogatives over collective problem-solving and conflict resolution; the rulership is considered vested with the authority to resolve conflicts and other predicaments of coordination or cooperation and to impose a solution, if necessary through coercive means. In this interpretation, the rulership claims a specialization in problem-solving the enhanced competence of those who devote themselves solely to the exercise of governance prerogatives, based on their superior knowledge, experience and access to statistical information, then serves as a basis for the centralization of problem-solving. Accordingly, a centralized, omnipotent and omniscient government is to set out the rules of interaction and exchange, adjudicate conflicts, diagnose problems, resolve them, and finally execute its response. Improving the problem-solving capacity of society within this paradigm then rests in enhancing the governance capability of the State. Improved discipline over the administrative functions, more information to be alerted to problems, and better training in solving them are seen as bettering the problem-solving capacity of the State.

Neoclassical economics is informed by this view of the State as a problem-solving black box. More, the field of Development economics, which views underdevelopment as a social and economic problem, relies on the State as the principal instrument of alleviating poverty, encouraging equity, and directing economic growth and human development as gauged through statistical data. Development economics has long been devoted to providing the policy expertise and to introducing from abroad the capital and investment seen as needed to provide the State with the added means to solve the problem of underdevelopment. The model of the State as a central problem-solving agent, which underlies the development economics paradigm, is however subject to question when we pry open this theoretical black box.

Three principal considerations call into doubt the usefulness of considering the State as a black box of problem-solving competence. The first ground for reevaluation rests upon the issue of the self-interest of the agents of the State. A founding assumption of the Public Choice tradition in economics holds that agents of government act in a no less self-interested manner than the rest of us (Buchanan and Tullock 1962). This brings to question how the way in which the governance apparatus of the State is structured so as to bring the *self-interest* of the agents of the State into compliance with the interests of its citizens; are

the interests of the agents of the State conditioned in such a manner as to be responsive to the problems faced by the citizens of the State.

The second ground for pause remains even if we assume that agents of government are concerned, public minded, and responsive. As arguments well developed within the Austrian School point out, no agent of the State, no matter how enlightened or well informed, can gather and use the full knowledge of time and space contingencies contained in society.¹ Practical knowledge requires attention to local conditions; and if such knowledge is to be invoked, the search for solutions to the problems individuals face must thus involve participation among those who are on the spot.

The final ground for hesitancy about the State as black box relates to its ignorance of institutions and processes. Orthodox development economics does not take into account the structure of governance, preferring to view the State as a conveyance for invoking and implementing policy. As such, it views the State as a means for putting into place characteristics associated with development as these are found to be lacking as measured by aggregate statistics. In this, it fails to appreciate that the features that we associate with advanced societies, and found wanting in less developed ones, are the results and manifestations of processes of interaction and that only changes in these patterns of interactions can produce outcomes alternative to those now experienced²; replicating these outward characteristics without appreciating what brings them about will not yield sustainable results.

Given these weaknesses of orthodox development theory, it is perhaps not surprising that it has not been in general successful in addressing the problems of the citizens of underdeveloped countries. Indeed, the failure of traditional approaches to

¹ "The peculiar character of the problem of a rational economic order is determined precisely by the fact that the knowledge of the circumstances of which we must make use never exists in concentrated or integrated form but solely as the dispersed bits of incomplete and frequently contradictory knowledge which all the separate individuals possess. The economic problem of society is thus not merely a problem of how to allocate "given" resources— if "given" is taken to mean given to a single mind which deliberately solves the problem set by these "data." It is rather a problem of how to secure the best use of resources known to any of the members of society, for ends whose relative importance only these individuals know: (Hayek 1948, 78).

² Hayek (1973, Ch. 2) distinguishes between *taxis*, deliberate institutional arrangements, and *cosmos*, which is the spontaneous result of individuals interacting within the structure of such arrangements. The literature in Constitutional Political Economy has pointed out that attempts to change the character of such spontaneous orders is best affected through considered changes in the frameworks through which individuals interact. Vanberg (1986) points out that one has to ask why and under what conditions individual problem solving activities can be expected to generate a pattern of social outcomes considered desirable.

development has been recently acknowledged by the World Bank, a significant consumer of development theory. However, the diagnosis for this failure has been traced to a lack of institutional capacity in the State to carry out the advice formulated within the framework of orthodox development theory. Accordingly, the catch phrase "Good Governance" has been invoked to refer to the theme behind making the State a more effective institution at directing development. Improving institutional capacity is interpreted here as measures to enhance the omnipotence and omniscience of the State as a centralized problem-solver. It does not reflect an appreciation that the capacity of systems of governance to serve as means to conflict resolution and problem-solving rests on more a fundamental design of its organization to incorporate local knowledge and to adopt constraints against the abuse of power in the problem-solving process.

This paper contrasts Good Governance with Institutional Problem-Solving as a theoretical alternative that is both process-based and design-sensitive. It first looks at events that have prompted a reappraisal by multilateral aid agencies of the effectiveness of development strategies to date and the emergence of Good Governance as a response. Next, the paper sets out the basis for Institutional Problem-Solving as a theoretical alternative to Good Governance. Finally, the article points out that although Good Governance is an attempt to respond to the problem environment faced by development agencies, this response is being addressed within the framework of a particular theory of the State as problem-solver. If multinational development agencies are to successfully survive by adapting to a new world regime, the alternative strategy for development is required—one that incorporates a more careful appreciation of the structure of the State in gauging its problem-solving potential.

II. Good Governance as an Issue in Development

The issue of governance, and particularly "Good Governance," has of late become fashionable in development circles. The 1997 *World Development Report*, put out by the World Bank, is devoted to the role of the State in development. The United Nations Development Programme (UNDP 1998) has recently revamped its policy document on the subject reflecting the fact that more than a third of its programming budget is now earmarked for activities in governance. Finally, a review of listings on the *Econlit* database reveals that a slew of articles have emerged in professional journals on the topic over the past ten years.

The relevance of governance to success in developmental endeavor was itself first noted in a 1989 World Bank report on Africa³. This awakening to the institutional aspects of development is traditionally interpreted as arising from a realization that carefully considered economic policies have not had the expected impact on development due in part to a lack of institutional capacity. As interpreted by these aid agencies, governance programming thus focuses on enhancing the capacity of the State by providing training and resources to agents of government and by restructuring rules and procedures to reduce bureaucratic hurdles to policy implementation. In turn, this added capacity in building a more efficient State apparatus is expected to support the execution and sustainability of well-constructed policies that are designed to enhance human development and spur economic growth.

All this recent attention on Good Governance however prompts a critical look at this concept as interpreted by the World Bank and the UNDP: how has the issue of governance in development been treated; how is it conceived of now; and in what way is this conception limited and flawed?

a. Origins of the shift in the development paradigm

Orthodox development economics, as developed in the mid twentieth century, relied upon an earlier philosophic tradition associated with thinkers as varied as Hume, Rousseau, Bentham, Ricardo, and Mill, who regarded the poverty of the working classes as a natural result of the competitive processes in market capitalism and who considered how this freedom of contract could be constrained by the government in the public or general interest. Friedrich List in 1885 argued that "artificial means" were required for "less advanced nations" to catch up with those more advanced and that it was the role of the State to "accomplish the economic development of the nation and to prepare it for admission into the universal society of the future" (175). Although poised against this background, modern development economics itself came up in the context of the aftermath of the Second World War. Its founders were strongly influenced by democratic socialism, Keynesian economics, and a romantic illusion of the possibility of rapid economic transformation through authoritarian planning. The works of such writers as Rosenstein-Rodan, Nurske, Scitovsky, and Hirschman emphasized the intervention of governments, in the face of market-failure, to intervene in the control of resources and to guide investment.

³ World Bank (1989) *Sub-Saharan Africa: From Crisis to Sustainable Growth*. Washington DC: The World Bank

The Keynesian paradigm has, in particular profoundly affected the course of development economics in two ways: First, Keynes, as did many of his contemporaries, assumed that policies would be developed by a priesthood of enlightened 'Harvey Road' economists and that these policies would be carried out by a ruling elite who were selflessly dedicated to improving the public welfare. Accordingly, the role of governance, associated with the faithful execution of considered policy, was taken for granted and emphasis was placed in developing the 'right' policies. Second, as a leading architect of the Bretton Woods system, Keynes effectively ensured the institutionalization and preservation of this world-view. Indeed, the World Bank and the International Monetary Fund (IMF)—Bretton Woods institutions— as leading consumers of development economics, continue to influence the course of development theory in this regard. Given that these institutions are set up to operate by way of the agents of governments in the course of their development activities, they seek theoretical guidance that fits within this operational framework. The dichotomy between the development of theory by experts and its application by agents of government is thus a distinguishing feature of the philosophy and conduct of the current orthodoxy in development economics.

For development studies side of this dichotomy, a particular theory of growth where capital is central to reconstruction and progress took root. Growth here was considered in terms of a mechanical process, wholly determined by the growth of certain factors of production and the laws of production. Kuznets (1965) considered that the capital oriented development experience of the industrialized countries could be directly transplanted to the developing world. In the influential Solow (1956) model of growth, national output in a closed economy was taken as a function of homogenous labor and homogenous capital; per capita national output is then determined by the capital-labor ratio. Among neoclassical economists, the argument ran that the returns on capital would be higher in the developing world where capital was scarcer in relation to other factors of production. The constraint facing the developing world, it was held however, was that it did not possess the resources to acquire the capital to stimulate this growth. The role of aid then was to cover this domestic resource gap through an injection of external capital so as to release domestic economic growth—what Rostow (1960) referred to as "take-off". Chenery and Strout (1966) noted that during the initial stages of development, aid was required to bridge the difference between capital investment and domestic savings—the internal gap—and the shortfall

needed to finance the necessary increase in imports—the external gap. An adjunct distinguishing feature of orthodox development economics is thus an emphasis on the role that capital injections play in development.

Through the period from the 1940's to the 1980's, the other side of the policy formulation - implementation dichotomy was not given full attention. Although Rostow had noted the need for an institutional framework to facilitate the ongoing expansion, this aspect of the policy program was ignored. Why have institutions been so disregarded? To answer this, we have to consider the features that mediate the relationship between the supply and demand for economic theory and policy advice. Although policy recommendations are treated as being scientifically derived and impartially tendered, the selection of theory is influenced by the usefulness of the arguments, it provides and the policy conclusions it supports to the self-interests of its direct consumers, as constrained. Successful policy analysts, as entrepreneurs in the market for policy, are those who are attentive to the needs of their customers in this regard (Shivakumar, 1998). Accordingly, if we are to consider why attention has shifted over the course of development economics from issues of capital accumulation to institutional development, we have to examine the factors motivating and constraining its most significant immediate consumers—i.e., large bilateral and multilateral development agencies and the donor governments that fund them.

Thus, in contrast to the assumptions of the development paradigm where an intellectual vanguard produces policy that is carried out by benign policy makers, the present analysis considers the possibility of self-interested policy makers who select from among policy alternative that option which, within the constraints under which they function, best serves their own well-being. The overall characteristics of programs of study thus reflect not only the innovative potential but also the effects of selection and of retention and replication of successful features. Here success can be thought of in terms of theoretical characteristics selected for. The growth and change of economic theory can thus be understood fruitfully in terms of the population thinking⁴ interpretation of Darwinian evolution.

⁴ Population Thinking, as introduced by Ernst Mayr (1982), stresses the uniqueness of the individual over its type. What we take to be a 'type' consists of a recognition of a distribution of particular characteristics within a population of distinct units. Such individuals, in dealing with their problem environment, may generate novelties in their form or behavior that may prove to provide a better adaptive fit. As such alterations are imitated or otherwise propagated within the population, the distribution will change, reflecting the increased prevalence of the new features and capacities that deal more successfully with the problem environment. In time, such changes may come to become recognized or categorized as distinct from the original array of

(i) Factors influencing the growth of Orthodox development theory

What factors influenced selection from among policy innovations in development studies? Aside from the humanitarian concern to uplift conditions in the poorer parts of the world, development aid has and has always had other requisite motivations. We highlight three in particular: First, the Cold War rivalry between the United States and the Soviet Union cast the provision of development aid within the dynamics of that strategic environment. Development aid was seen as one way of securing geopolitical alliances—and as such, the institutional aspects of third world development were not significant. An egregious example of such aid-provision was that offered to the Said Barre regime in Somalia. The subsequent collapse of that state and the resulting civil strife and famine has been related to the effects such Cold War politics⁵.

A second reason that can be offered for the lack of interest in matters of institutions and governance can be traced to the commercial motivations for development aid⁶. Agents of donor countries use funds derived from broad based taxation to support particular domestic industrial and service lobbies by enabling poor countries to purchase or finance the purchase of heavy machinery and other capital goods that they produce. While the advancing theory in development economics, with its emphasis on capital accumulation, provided the cover for rent-seeking activities in donor countries, there was little interest or demand for any corresponding theory on the sustainability of such capital acquisitions on the part of aid recipients. There was also little demand for theoretical development on institutional or governance issues on the part of the agents of the recipient countries as there was more political capital (or bribes) to be gained in procuring and inaugurating shiny new projects than in maintaining them.

Finally, the growth of the development industrial complex was concurrent with the process of decolonization and this also played a role in the progress (or lack thereof) of institutional issues in the development literature. When their colonial possessions were still

characteristics as taken at an earlier point in time. In this way, given that the problem environment itself does not change, the system can be said to 'shift' to form an adaptive fit.

⁵ "Said Barre played off the Cold War superpowers against each other. His external support, first from the Soviet Union and then from the United States, unbalanced the fragile social ecology of Somalia's clan politics and introduced high levels of lethal weaponry" (World Bank 1997,159).

⁶ See: GAO/NSIAD-95-37 Foreign assistance - Selected Donors' approaches for managing aid programs.

under their control, countries such as Britain and France invested significantly in their administration and infrastructure. Indeed, it is often noted that Britain's principal legacies to India have been its military and civil service traditions as well as the railways⁷. These investments in governance and infrastructure benefited and subsidized those domestic companies that had invested in producing in the colonies, what was in the main, raw commodities for export to the mother country for further processing. With independence, most new polities adopted the constitutional forms of the erstwhile imperial power and inherited administrative norms that were exercised previously by the officers of the colonial civil service. Most newly independent countries from the 1940s through the 1960s themselves were occupied, as a first order of business in nation-building, with setting up institutes or schools of public administration to replace the posts vacated by colonial officers. Thus, there was little demand for investment in governance and institution building activity on the part of donors. What however concerned the former colonists were the capital investments they left behind. Browne (1997, 4) notes that "independence encouraged new bilateral donors to build aid programmes as a continuation of their colonial obligations." Indeed, this was the rationale behind the establishment of the British Overseas Development Agency.

(ii) Factors influencing a reassessment of orthodox development economics

Events over the past decade and more have however motivated a reassessment of the need for an institutional component to development theory. This new interest can be traced to three factors:

First, with the demise of the Soviet Union, the motivation to use development aid as a strategic tool in geopolitics waned in significance. Indeed, western donors could now attach explicit political and institutional conditions to their aid directed at 'third-world' recipients without fear of losing their clients to the Soviet camp. More, the volatility of newly independent former Soviet Republics that were facing transitions to statehood, democracy and market economies⁸, and other similar transition economies of the former

⁷ It should be noted that when the British left India, they took with them all the blueprints for engines and other rolling stock so that any repair or capital addition to the railways had to be purchased from British firms.

⁸ Browne and Pflaumer (1996) refer to this as the "triple transition."

'second-world,' heightened interest among western donors in their political and economic stabilization

Second, the commercial interests of many donor country firms in recipient countries evolved, particularly in wake of advances in production management and technology. Globalization of production processes— where parts are produced at various locations for cost reasons and assembled using "just in time" techniques— have created a new need for reliable physical and governance infrastructure at those remote sites to facilitate to coordination required, A stable framework of local laws and labor practices are needed, as well as the necessary physical infrastructure to convey reliably these products to the next stage of global assembly or distribution for sale. A prominent symptom of this change in production has been the rise in Foreign Direct Investment (FDI). Indeed, FDI has eclipsed traditional aid as a tool of economic development in East Asia and elsewhere⁹. Multinational firms set up in developing countries see it in their common interest to lobby their domestic politicians for support in areas of governance and infrastructure. The shift to globalized production and rise of FDI has thus in turn created more demand for an institutional component to development theory.

Finally, the institutional infrastructure of governance that many developing countries had inherited at independence has eroded over time and this has created a greater awareness for the institutional components of development. Political destabilization through such things as military coups and excessive bureaucratization and top-heavy administrative practices have marked the post-colonial experience in many developing countries; the patterns of public sector vendibility, lack of accountability, and lackluster improvements in well-being that have resulted have made their populations restive. More, even as the decline of traditional forms of aid has led to fewer opportunities to harvest rents, agents of recipient countries increasingly find themselves at a competitive disadvantage with those of others in attracting foreign investment. Consequently, these same agents have become more open to reform in spheres that might have otherwise been delimited based on arguments of sovereignty.

⁹ Between 1990 and 1995, Official development assistance to developing countries remained between US\$55 to 60 billion whereas private investment flows increased from US\$44 to 170 billion. (Source: OECD DAC Reports)

These events have led to reorientation of the interests of western donors who dominate the policy making boards of major development institutions, as well as those of the representatives of recipient countries, and hence to the policy predisposition of these development institutions themselves¹⁰. In turn, this has drawn increased attention to ongoing efforts at scholarship in such areas as New Institutional Economics which emphasizes the importance of stable institutions for the development of a market economy, neo-liberal arguments concerning the virtues of a slim and efficient bureaucracy, as well as explanations for the failures of fifty years of organized development effort¹¹. The World Bank in 1997 admitted that "foreign aid to developing countries has had no impact on either the recipients' growth rate or the quality of their economic policies" except in cases where the appropriate institutional framework was in place.

b. Putting 'Good Governance' into practice

If the importance of Good Governance has been seized upon of late, how is this being translated into theory and practice? The approach taken by the World Bank and the UNDP has been to identify elements associated with effective government in western polities and to strengthen the capacity of the governments of developing nations in each of these respects. The role of the State in correcting perceived market failures and in directing human and economic development is left unchallenged. According to the World Bank's *World Development Report*, (1997, 30-38) it is the appropriate role of the State to develop good policies and the institutional environment where they can be implemented. The State is seen to be that entity which establishes and adjudicates the economic, social, and political rules and regulations. It is also a major player in all these spheres. Its function is to furnish active macroeconomic management, to provide or ensure the provision of basic education, health, and environmental protection, and to render a fertile institutional soil within which markets can grow. The UNDP similarly views the State as on one hand establishing and maintaining a stable and effective legal and regulatory framework while at the same time actively engaged

¹⁰ Professor Vincent Ostrom points out that this donor orientation to development can be alternatively viewed as enlightened self-interest or as a part of a system of *cryptoimpenalism*. This notion, set out in Miles Copland's *The Game of Nations*, is discussed in V. Ostrom(1988).

¹¹ The change in outlook of the Bank and IMF however tends to be portrayed more as an intellectual realization of the merits of the emerging "neo-liberal ascendancy" and as a result of the lessons learned from

in such things as managing the macroeconomic variables, providing public services, and protecting the rights of the vulnerable. The purpose of aid is thus to strengthen the capacity of governments in each of these respects.

Such strengthening is interpreted here as increasing the potential of the State to carry out its roles more efficiently. Development is seen to flow from enhancing the quality of central policy-making and coordination, and in upgrading "delivery systems." In this regard, there is viewed a need to discipline policy-makers to adopt expert advice and to increase the motivation and capability of civil servants to comply and carry out policies so established. The role of governance programming is thus to reinvigorate the State's capability by setting up procedures and incentives for State officials to act in the collective or general interest and to restrain arbitrary action. To this end projects relating to governance typically provide for:

- Training economists and other policy innovators, leading to an improvement in the quality of advice offered to policy makers.
- Training parliamentarians on legislative procedure and sensitizing them to social and economic issues and corresponding policy options.
- Supporting statistical agencies to provide better inputs to the policy making process and to develop more accountability. By disseminating information on economic variables, society's ability to judge the performance of public officials is seen to be enhanced.
- Training civil servants in administration. Greater adherence to procedure in bureaucratic management is seen to create an enabling environment for the private sector. Training civil servants also is seen to enhance "delivery systems" or mechanisms by which policy adopted by more benign policy makers from the suggestions of better trained economists is more faithfully executed and administered.
- Training judges and other legal professionals. Adherence to due process is also linked to the creation of an enabling environment for the private sector.
- Purchases of office automation equipment to increase efficiency and to provide access to modern electronic information systems.
- Funding for voter registration and elections.

the structural adjustment policies carried out in the 1980s. This observation is based on conversations with current and former Bank officials. Also see Leftwich (1994, 368) for example.

- Support for "civil society" organizations such as non-governmental organizations so that they may serve as intermediaries between the people and the State.

c. Is Good Governance sustainable?

The immediate appeal of putting to practice projects and programs that enhance each of the features associated with Good Governance is that by making government work better, it promises to enhance the sustainability of other developmental initiatives. If such things as poor implementation, a lack of interest in maintenance, corruption and political venality underlie the reasons why rational and sound policy has not yet yielded the developmental results predicted by theory, then recognizing and improving the institutional setting within which such policies are carried out would seem to improve the prospects for policy and hence developmental success. For the effects of policy initiatives to be sustained, good governance is required. What, however ensures the viability of good governance? The Bank and the UNDP rely on particular interpretations of greater transparency and accountability, and to a lesser extent decentralization, to address this. However, an examination of these conceptions reveals them as somewhat fragile.

In the view of the two multilateral development agencies considered, Good Governance is maintained through the proper conduct and interaction of each of its four components: the policy making and administrative organs, the statistical and auditing services, the judiciary, and finally, "civil society organizations." Good Governance, first, is self-maintained through the professionalization of the public sector. The Bank advocates smaller and smarter states where hiring *is* based on established procedure and training is provided in policy analysis and economic management. (World Bank, 1989a, 60; 1989b). Second, auditing, accounting and information dissemination procedures are to be developed in order that citizens can better judge the performance of government (World Bank, 1992). Statistical services are also to be upgraded since otherwise, it is argued, society will not have enough information about the activities and accomplishments of the State to hold it accountable for its actions. Third, a legal system, by channeling procedures of conduct and making it open to view, is to facilitate greater transparency in government. This entails redrawing laws on property rights, bankruptcy, trade, etc., as well as training and support for judges, lawyers and other court officials. Finally, encouragement for civil society organizations is endorsed since they are seen to act as intermediaries between the

government and the people¹² (UNDP 1998). These groups are to provide a countervailing force to the power of the State and hold it accountable, though within certain if unspecified regularized procedural constraints. As Williams (1996, 159) concludes, the practice of the Bank in its attempts to improve the governance of its borrowers relies on "an attempt to transplant many of the disciplinary characteristics of the developed world, and in particular the disciplinary techniques of 'the survey,' 'the audit,' and 'the procedures.'"

Reference is made by the Bank and the UNDP to decentralization as a means of increasing the accountability of the State though enthusiasm in this is somewhat diluted by the consideration that this implies loss of control over policy management. A review of the 1997 *World Development Report* reveals less resistance to administrative decentralization which involves the transfer of such state functions from higher to lower levels of government while retaining control of budgets and policy making. However, fiscal decentralization is seen to conflict with the core State responsibility of managing macroeconomic variables while the devolution of political authority to lower levels of government will lead, it is feared, to regional disparities in service provisions, misallocation of resources and inadequate policy guidance¹³ (World Bank 1997). Both the World Bank and UNDP vision of reform in governance therefore rely heavily on the professionalization of public servants; although a perusal of the 1997 *World Development Report* leaves the reader impressed with the breadth of topics considered, the prototype for action left standing at the end of the day *is* one where efficient delivery of public goods takes place in correspondence with the latest advances in technical know-how and policy advice through a centrally consolidated provision of the services by the State. If the public good in question is good governance, then it is again the responsibility of the State to put into place the necessary conditions to upgrade its own credibility, consistency and predictability.

In essence therefore, the proposed approach towards securing Good Governance does not differ from the general character of development practices associated with the earlier mixed attempts to spur development by bridging the capital gap. Given that it is not secured on an institutional footing either, attempts to operationalize Good Governance

¹² The UNDP policy document introduces Civil Society Organizations as an intermediary to represent the interests of citizens to policy makers so that they will in turn be more responsive to the public. Left unclear, however is how civil society organizations would operate so as to represent fairly the public's interest in pending policy decisions.

¹³ Bardhan (1996) expresses similar reservations.

would fall prey to the same problems of sustainability. Good Governance attempts to address, what we may coin, the institutional gap by replicating on a piecemeal basis characteristics associated with good governance in the politics of the developed world in the developing world without understanding that these characteristics are themselves a part of the complex order that is generated through the conditioned interactions of individuals acting purposefully within the bounds of certain fundamental levels of social and political rules and institutions. Good Governance—in the sense of an operational strategy—does not diagnose what institutional factor gives rise to the observed characteristics of good governance—in the sense of a desirable state of affairs.

As has been interpreted therefore, Good Governance is not institutionally robust. It continues to be rooted in certain essentialist views of 'the State' and 'the People,' where the former entity gathers data, diagnoses problems, develops solutions and implements them upon a passive populace. Left unexplained consequently is how the conflicts inherent in the State acting as rule-maker, referee, and player may be resolved. Good Governance as proposed continues to rely on the mid-century development paradigm in considering the dichotomy between the remote development of policy by enlightened social scientists and implementation by benign agents of the State, as well as a naive confidence that development will occur when the each of the many characteristics associated with it are more faithfully individually replicated and assembled.

It is difficult to disagree with the need for good governance; the question though is how we may better achieve it. The following section introduces problem-solving as an institutionally robust paradigmatic alternate for realizing the characteristics and benefits of good governance.

III. Institutional Problem-Solving

In contrast to the Good Governance approach where the State is taken up as an idealized entity that serves the public and whose performance can be improved by better statistics, policy, and professionalism, the proposed alternative—Institutional Problem-Solving—breaks open the conceptual black box of the State to reveal how the way it is structured can facilitate or hinder the ability of citizens to solve their collective problems. The nature of these structures is then reflected in the orders they generate through the

conduct of individuals acting, adapting, and problem-solving within these constraints. Appropriately structured, these institutions can foster the display characteristics we associate with that of good governance and advanced development.

The exposition of this alternative requires a shift in narrative gears to introduce the basics of the new concepts involved. After reviewing what is meant by the terms 'problem-solving' and 'institution,' we return to address how enhancing the problem-solving capabilities of public institutions can lead to the desired characteristics of governance and development.

a. Problem-Solving

Problem-solving relates to a process by which an organism seeks, through the generation of innovation through standards of selection, to increase its adaptive fit with respect to the predicaments posed by its environment. In the context of evolutionary biology, such innovations are introduced through genetic mutations and the species may be said to 'solve' the problems posed by its environment through the enhanced mating ability, fertility, fecundity and survivorship of those who possess or are passed on the helpful trait. Given the usefulness of the given innovation in adaptation to those who possess it, the array of characteristics that we associate with the species change over succeeding generations and, given that the problem environment does itself not change, the system can be said to have shifted to form an adaptive fit. The Darwinian system thus deals with a process by which novelty or variation is generated, a process by which innovation is selected based on some standard, and a process by which such changes are preserved, reproduced or propagated. In this way, the alterations produced in the features and capacities developed within the system enable an increase in the adaptive fit with respect to solving the problems posed by the environment.

The evolutionary processes by which an organism solves the problems posed by its environment can be considered to operate in the same manner at all levels of learning and among all organisms. As Popper has noted, learning takes place "by the method of trial and error: new relations, new forms, new organs, new modes of behavior, new hypotheses, are tentatively put forward and controlled by error elimination (1972, 242). Such trial and error processes also characterize the "correction and modification of previous knowledge"(ibid. 259). This mode of evolutionary problem-solving at the level of species can be extended to

processes of learning; the same scheme then applies equally to the development of new forms among living organisms as to the emergence of new scientific theories. As in Popper's phrase, the growth of knowledge through the proposition and elimination of tentative solutions is the same from "ameba to Einstein" (ibid. 261).

The concept of Human Problem-solving, as crystallized by Newell and Simon (1972), addresses the issue as it applies to cognitive psychology. They note that when an individual is faced with a problem—that is, when the individual wants something but does not know immediately what series of steps of actions can be performed to obtain that goal—his first task is to represent that external situation within an internal mental framework. Once thus represented, particular methods to solve the problem can be serially tested. Thus, within a conjectured representation of the problem environment, conjectured solutions to the problem as represented are carried out.

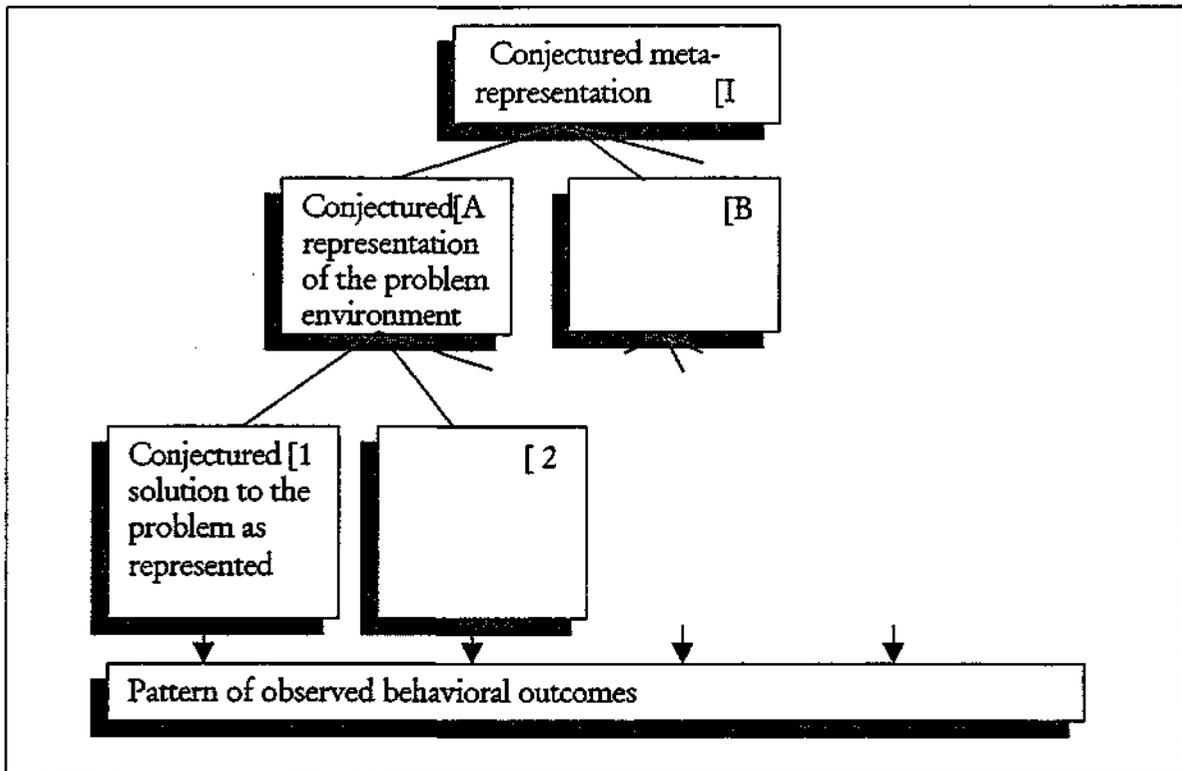


Figure 1: The Architecture of Cognitive Problem Solving

Hayek's (1952) formulation in *Sensory Order* can be seen as a further generalization of this explanation (Shivakumar 1997). In terms of Figure 1, this extension would consider that a failure to produce a satisfactory solution [1, 2, ...] to the particular problem within a given internal mental framework [A] may trigger the invocation of alternative mental frameworks [B,C,...]—alternative internal representations of the problem environment—

within which problem-solving activities may proceed. In contrast to biological problem-solving where innovation *is* blind with respect to its adaptive use in addressing the problem environment, cognitive problem-solving involves the introduction of competing innovations as possible responses to the problem as internally represented, with that internal representation itself one among other competing present or potential depictions of the problem environment. The overall observed behavior of the individual is then the outcome of the problem-solving process working through these routines.

b. The role of institutions in problem-solving

We have so far considered problem-solving, whether in the context of biological, epistemological or cognitive evolution, in terms of an individual adapting to a given external environment or problem space. Social rules and institutions gain relevance when individuals face other individuals as a part of their problem environment or through efforts at joint problem-solving.

Social institutions facilitate the problem-solving activities of its members by reducing uncertainty. When individuals in a group agree to be governed by a common set of rules, they mutually exchange limits on their own freedom of action in order to be able to anticipate better the actions of the other. As Brennan and Buchanan (1985) note, by setting out informational boundaries for the actions of others, rules and institutions provide predictability about the behavior of others. This in turn restricts the problem space and thus simplifies problem-solving. The extent to which this problem space can be limited thus depends on how well-recognized and well-observed the rules are. Institutions, as complexes of rules socially considered, thus play a role in promoting the predictability of our environment and conversely, reducing uncertainty by confining the scope of activity.

While we each might simplify the other's problem environment by behaving predictably and staying out of the way, the resolution of certain problems may require us to interact with other—to solve problems collectively. Institutions can serve to enhance our ability to problem-solve in this context by acting as sources of coordination. Lachmann (1971) refers to institutions in this regard as nodal points of society. Such coordination solutions tend to be self-policing and self-enforcing. Institutional constraints can also promote cooperative modes of problem-solving by setting up the deliberate and organized enforcement that is

needed to curb strategic or opportunistic behavior, such as described in the Prisoner's Dilemma story.

c. The structure of social institutions in problem-solving

Adaptive competence in humans is associated with the ability of an individual's cognitive faculties to recognize and solve problems posed by the environment. In this respect, current thought in cognitive psychology alludes to the formation and internal representation of the problem environment as mental models, and the triggering of evaluative processes within this provisionally accepted though tentative framework¹⁴. Such mental models, by organizing information about our environment as knowledge, enhance our ability to assimilate pertinent information from the environment and to react rationally and adaptively within the context of that framework. Such organization, made necessary by the limitations of memory, affects our ability to problem-solve and this is reflected in our overall behavioral characteristics.

Following this scheme, we can understand social institutions also as problem-solving apparatuses whose overall characteristic and capability derives from the organization of its structure. Even as institutions enhance the problem-solving abilities of individuals, the structure of such institutions affects the extent of such adaptive potential. Institutions, we have seen, by limiting what is taken for consideration and how it is appraised, enables the individual participant to recognize patterns considered relevant in his or her environment and to predict and thus exploit the movement of these variables to advantage. Sharing a particular conjectured mental representation of the problem environment could lead to a community of understanding, which can serve as a basis for addressing common problems in a coordinated manner. More, by variously altering different aspects of our physical and social environment, institutions can be designed to facilitate cooperative solutions to particular types of collective action problems¹⁵. In turn, this raises the issue of modifying or

¹⁴ See: Holland et al. (1986) for instance.

¹⁵ "How individual interests relate to common interests needs to be clarified through processes of conflict and conflict resolution that serve the correlative purposes of generating common knowledge and shared communities of understanding that create a consciousness of complementary social identities. The structure of incentives needs to be such that the quest for cooperative endeavors is reinforced in ways that are compatible with fundamental values, such as peace, enlightenment, liberty, justice, or well-being; such values should have the potential for becoming universal public goods" (V. Ostrom 1997, 113).

replacing features of extant institutional arrangements in an effort to find an improved solution to problems collectively addressed.

Solutions to collective action problems can be thought of as proceeding within the framework of certain institutional arrangements [A, B, ...] that serve to coordinate and foster cooperation among the group. Such institutional arrangements themselves represent conjectures (whether deliberately set or not) as to the structure of the order that facilitates joint dealings with the problem forecast or at hand. As such, the scope of such conjectures are themselves circumscribed by relatively more absolute frameworks [I] although, these constitutional level constraints are themselves not immune from reappraisal. The posing of day to day solutions to problems of collective action [1, 2, ...] are however ordinarily considered within the bounds of the provisionally adopted institutional arrangement. If alternate conjectured approaches [1, 2, ...] to solving collective action problems within the framework of the institutional arrangements conjectured to deal with them [A] are unsatisfactory, an alternative [B] may be employed, and so forth.

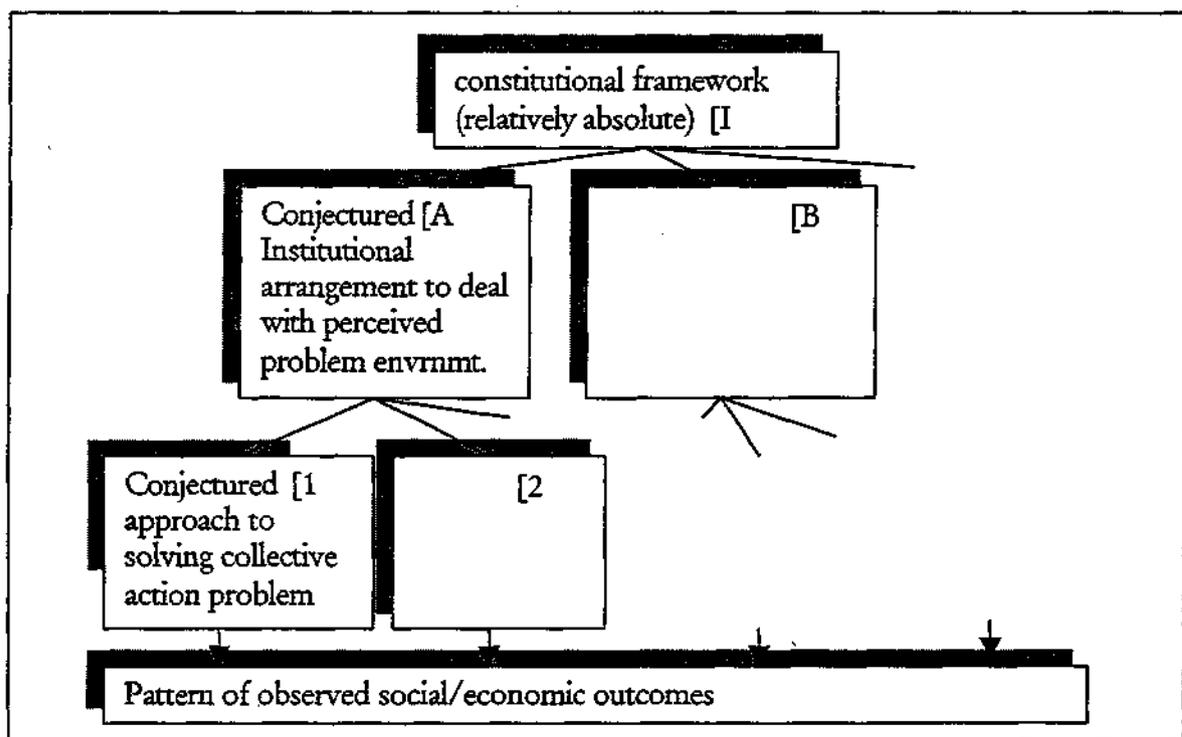


Figure 2: The Architecture of Social Problem-Solving

In this respect therefore, institutions serve in the same capacity and in the same way as mental models in serving as a problem-solving tool¹⁶. The overall characteristic of the social order is then the outcome of individuals working within the channels of such problem-solving processes. Social outcomes are the product of the problem solving efforts of numerous individuals through varied institutions, each with multiple layers of institutional arrangements and operating under myriad competitive constraints. As such these set out who is placed to judge the fitness of conjectured solutions to given problems and under what applicable dynamic standards .

d. Governance as a capacity to problem-solve collective action problems

Having examined what is meant by institutional problem-solving in the abstract, we can return to the central theme of the paper—that getting to the characteristics associated with good governance and advanced development rests fundamentally on enhancing the institutional problem-solving capacity of the social institutions, including the State.

The State is an institutional mechanism that can be sought to solve a variety of collective action problems. Buchanan (1975) distinguishes between the *protective* and the *productive* roles of the State. The former role views the State emerging as "the enforcing agency or institution, conceptually external to the contracting parties and charged with the single responsibility of enforcing agreed-on rights and claims along with contracts which involve voluntarily negotiated exchanges of such claims" (68). In the latter role, the State is conceived as "that agency through which individuals provide themselves with "public goods" in postconstitutional contract"(68). The State is thus an instrument for enforcing private solutions to collective action problems as well as forum for public deliberation, choice, and implementation of putative solutions to problems faced by the collectivity.

The competence of the State as a problem-solving mechanism, whether in its protective or productive roles depends on how it is structured. In the first instance, the coercive power entrusted in the State in its aspect as an enforcer raises questions as to how its own behavior may be constrained while in the second, the issue of how the organization of the State impinges on its capacity as a collective action problem-solver in and of itself,

¹⁶ In describing rules as social tools, Hayek points out that rules are like pre-formed implements that have been refined through use to become well-adapted in dealing with recurrent problems. Accordingly, he notes, "like most tools, rules are not a part of a plan of action but rather equipment for certain unknown contingencies" (1976, 23).

gains prominence. If conflicts among individual agents stand in the way of resolving collective action problems, the necessity of an external enforcing agent arises. The capacity of the State to facilitate problem solving in its protective role is however to be set against the potential for those who are empowered to enforce these standards from going beyond their limits. *Quis custodiet ipsos custodes?* The problem-solving capacity of the State is thus in part dependent on various institutional devices designed to restrict the abusive use of coercive power. These vary from Plato's recommendations in *The Republic* on the instructional regimen of the student prince to the medieval opposition between a decentralized nobility and a centralized church in Western Europe (Berman 1989), to the concept of checks and balances as clarified by Madison (Federalist 51).

The capacity of the State in its productive role to resolve collective action problems depends on its problem-solving architecture for governance. Within an overall constitutional framework, the immediate problem-solving ability depends on the success of particular conjectured approaches given under a particular institutional arrangement. Within the scope of a particular institutional framework, the capacity to problem-solve depends on the extent to which alternative or innovated solutions can be tried out—whether in serial or parallel experimentation—and the standards by which competing alternatives are judged. It also depends on the extent to which options to the present institutional arrangement can be experimented with if dissatisfaction arises with the operational alternatives made possible within that present set-up. Again, this requires the consideration of options, whether existing or innovated, against certain evaluative standards.

The capacity for structures of governance to problem-solve results from the choice of standards for selection among institutional or operational alternatives. If, for example, the experimentation among institutional alternatives were so structured as to create a rapid turnover, then such expectations would deter attempts to resolve problems within any particular institutional arrangement. Typically, therefore, successful governance structures are designed so that successively more fundamental levels of rules are experimented with higher thresholds for deliberation, consultation, and rule adoption. Governance structures that are more successful at problem-solving are also those where experimentation from the local to the constitutional level takes place simultaneously, though at different rates and where each level of government sets out the constraints within which experimentation at the next level can take place.

In the political science literature, these notions are affiliated with the term polycentricity which is invoked to describe a system of governance for metropolitan areas based on many competing, sometimes overlapping centers of decision-making, each reflecting the locally relevant scale and scope, and emphasizing local participation in the resolving collective action problems (V. Ostrom, Tiebout and Warren 1961; V. Ostrom and E. Ostrom 1977). The problem-solving superiority of such systems as opposed to a monocentric order has been the subject of considerable empirical scrutiny—in particular with regard to the provision of police services (E. Ostrom and Whitaker 1973; E. Ostrom 1997)

IV. The Problem-Solving Potential of Good Governance

In recognizing the importance of institutions to the development process, Good Governance recommends improvement in the State's capacity to develop and implement aggressively policies to address directly perceived shortcomings in patterns of development while also seeking to maintain a stable regulatory environment conducive to private sector growth. As conceived, Good Governance is a variation on orthodox development economics and as such retains that framework's distinction between 'the State' and 'the People.' As such, it still has little room for the participation of ordinary individuals in the development of their public problem-solving institutions. Rather it relies developing a perfected delivery system for allocative solutions developed by an elite cadre based on more comprehensive statistical information on the patterns of social outcomes.

The notion of Good Governance is paradoxical in that it although it seeks to complement traditional development theory with an institutional overlay, it is in itself not institutionally robust. Good Governance does not address the problem of how self-interest is to be reined, it does not appreciate that effective collective problem-solving involves the use of local and idiosyncratic knowledge, and it does not appreciate the role institutions play in conditioning the growth of spontaneous orders. Rather, it attempts to overcome issues of self-interest through training and professionalization, address collective action problems through policy improved through better statistics, and patches perceived market failures rooted in poor institutional design through particular targeted aid programs. Good Governance is, in short, an intensified approach to setting in place features of the pattern of outcomes associated with the political conditions seen in the 'developed' world rather than a process conditioning the behavior of individuals through a particular architecture of

institutional arrangements to solve local problems and promote interaction in ways which would endogenously produce a state of affairs judged superior by the local public.

Good Governance itself may be an earnest attempt to respond to the need for a more institutionally robust approach to development. The response offered to this challenge however, has been conceived within the framework of the neoclassical orthodoxy. In terms of figures 1 or 2, we have moved from the theoretical approach of orthodox development economics[1] to an institutionally enhanced variation[2]. However given that this new version, identified as Good Governance, is itself rests on weak institutional foundations, its model extensions are likely to not be sustainable as well. Analytically, the problem rests in [A]—the neoclassical theoretical framework. Suggested therefore is a shift to a robust institutional alternative [B]—from which a theory of Institutional Problem-Solving can be consistently be derived and hence serve as a guide in subsequent model building.

This paper has considered the issue of problem-solving as it relates to adaptation and survival in a changing world. Individuals struggle to adapt by innovating within the constraints and facilities provided by existing rules and institutions. Yet, they also have to capacity to imagine alternatives—artifactual creations within which they may be more successful in their endeavors. The ability of individuals to solve their problems and resolve conflicts vary with the tools they possess or are able to acquire or innovate in this regard. Such an ability to solve problems is manifested in visual and statistical images we associate with development. Sustainable development thus involves applying innovated problem-solving routines conjectured to produce patterns of outcomes that are considered desirable rather an attempt to replicate such features on a program by program basis; it is necessarily a process of growth from within.

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