It is widely recognized that institutions and governance are crucial for economic performance and welfare in general. This understanding has resulted in a veritable explosion over the last 20 years or so of both theoretical analysis and empirical research into the role of institutions and governance in various areas of the economy and the determinants of the quality of institutions. This vast literature cannot be adequately surveyed in a one-semester course. Instead of a broad survey, this course concentrates on a few areas that are covered by a set of governance indicators developed within the World Bank’s Governance and Anti-Corruption program. These indicators that have been widely used in the empirical literature measure the following six dimensions of institutional quality and governance:

(i) rule of law;
(ii) government effectiveness;
(iii) regulatory quality;
(iv) control of corruption
(v) voice and accountability;
(vi) political instability and violence.

In this course, we will study the theory underlying the importance of the institutional aspects reflected in these and related indicators, look into measurement issues, and sample the empirical work based on these and other indicators of institutional quality and governance.

This course examines both micro and macro issues, although greater emphasis is placed on microeconomic aspects of institutions. The material in the course should be particularly useful for those students who are interested in development, international economics, industrial organization, and political economy.
Course outline with references to key sources

In the following outline, references are arranged in alphabetical order. An outline of the class discussion will be provided prior to each class. Additional readings will be assigned during the semester.

1. What are institutions and governance, and why they might be important?

According to Williamson (2000), institutions generally provide for the rules of the game, including inter alia a system of property rights, contract law, polity, and the role of bureaucracy while governance describes how the game is played within the existing institutional framework, including contract management and dispute settlement. In this introductory section, we will briefly address the general theoretical reasons for the importance of property rights, contract enforcement and management, political organization, and bureaucratic quality for economic performance.

Key references:


URL (NBER version): [http://ideas.repec.org/p/nbr/nberwo/9608.html](http://ideas.repec.org/p/nbr/nberwo/9608.html);


(Stable URL: [http://www.jstor.org/stable/1942984](http://www.jstor.org/stable/1942984))


URL: [http://ksghome.harvard.edu/~drodrik/institutions.PDF](http://ksghome.harvard.edu/~drodrik/institutions.PDF); shorter version: [http://www.imf.org/External/Pubs/FT/seminar/1999/reforms/rodrik.htm](http://www.imf.org/External/Pubs/FT/seminar/1999/reforms/rodrik.htm)

2. Empirical evidence of institutional importance for economic growth

In order to evaluate empirical evidence of the importance of institutions we need first to learn how they are measured. We will review survey-based measures (primarily those by the World Bank listed above) as well as some other approaches to measuring institutional quality. Then we will look at some recent empirical work on the relationship between overall institutional quality and economic growth.

Main references:


3. Incentives vs. transaction costs

The institutional quality depends not only on the incentives that the institutions engender, but also on the transaction costs they generate. While the detailed study of these issues is beyond the scope of this course, the tradeoff between incentives and transaction costs and potentially different implications of the incentive and transaction cost approaches will reappear in several other topics below. Here we will address these issues mainly in the context of such a major institution as a firm.
Main references:


Next, we begin a more detailed examination of the different aspects of institutional quality. After looking at some general concepts of the Rule of Law (section 4), we examine its main components -- property rights protection and contract enforcement -- that represent the most important determinants of institutional quality. (For this reason, *Rule of Law* is perhaps the most important and most often used indicator of the overall measure of institutional quality.) Sections 5 through 8 address topics related to other indicators of institutional quality. Most likely, there will not be time left to cover both Sections 9 and 10, in which case either one of them or both will be dropped. Alternatively, we might go over one paper from each of these topics.

**4. Rule of Law**

Main references:


Myerson, Roger B. 2004. “Justice, Institutions, And Multiple Equilibria,” *Chicago Journal of International Law* 5(Summer):91-107. (also available here:

4.1. Private vs. government ownership


4.2. Contracts and contract enforcement


4.3. Political economy of property rights protection

Stable URL: http://www.jstor.org/stable/2677786

Stable URL: http://www.jstor.org/stable/3592952


4.4. Models of law enforcement and unofficial economy


5. Quality of regulations and government effectiveness


(Stable URL: http://www.jstor.org/stable/1942984)


6. Corruption


7. Democracy, dictatorship, political stability, decentralization


9. Natural Resource Endowment and Institutions


10. International Trade and Institutions


**Course Requirements and Grading**

The students will be responsible for assigned readings and participation in the class discussion. The course requires each student to write a research paper on a topic approved by the instructor. The paper will account for 50% of the grade in the course. The students also will be required to review one of the assigned papers in class. This presentation will be judged on the understanding of the paper's substance, organization, clarity, and answering questions, and will contribute 40% to the student's grade. The remaining component of the grade will be class participation (10%).