THE IMPERATIVE OF STATE-BUILDING

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Excerpted from the book, State-Building: A New Agenda, *by Francis Fukuyama, published May 2004 by Cornell University Press.*

State-building—the creation of new governmental institutions and the strengthening of existing ones—is a crucial issue for the world community today. Weak or failed states are close to the root of many of the world's most serious problems, from poverty and AIDS to drug trafficking and terrorism. While we know a lot about state-building, there is a great deal that we do not know, particularly about how to transfer strong institutions to developing countries. We know how to transfer resources, people, and technology across cultural borders. But well-functioning public institutions require certain habits of mind, and operate in complex ways that resist being moved. We need to focus a great deal more thought, attention, and research on this area.

The idea that building up, rather than limiting or cutting back the state, should be at the top of our agenda may strike some as odd or even perverse. After all, the dominant trend in world politics for the past generation has been the critique of "big government" and the attempt to move activities from the state sector to private markets or to civil society. Yet particularly in the developing world, weak, incompetent, or nonexistent government has been and continues to be a source of severe difficulties.

For example, the AIDS epidemic in Africa has infected more than 25 million people and will take a staggering toll of lives. AIDS can be treated, as it has been in the developed world, with anti-retroviral drugs. There has been a strong push to provide foreign assistance for AIDS medicines or else to force pharmaceutical companies to permit the marketing of cheaper forms of their products in Africa and other parts of the Third World.

While part of the AIDS problem is a matter of resources, another important aspect is the government capacity to manage health programs. Anti-retroviral drugs are not only costly, but complicated to administer. Unlike one-shot vaccines, they must be taken in complex doses over long periods of time; failure to follow the proper regimen may actually make the epidemic worse by allowing the HIV virus to mutate and develop drug resistance. Effective treatment requires a strong public-health infrastructure, public education, and knowledge about the epidemiology of the disease in specific regions. Even if the resources were there, the institutional capacity to treat the disease is lacking in most countries in sub-Saharan Africa (though some, like Uganda, have done a much better job than others). Dealing with this epidemic thus requires helping afflicted countries develop the institutional capacity to use what resources they may acquire.

Lack of state capacity in poor countries has come to haunt the developed world much more directly. The end of the Cold War left a band of failed or weak states stretching from the Balkans through the Caucasus, the Middle East, Central Asia, and South Asia. State collapse or weakness had already created major humanitarian and human rights disasters with hundreds of thousands of victims during the 1990s in Somalia, Haiti, Cambodia, Bosnia, Kosovo, and East Timor. For a while, the United States and other countries could pretend that these problems were just local, but the terrorist attacks of September 11 proved that state weakness constituted a huge strategic challenge as well. Radical Islamist terrorism combined with the availability of weapons of mass destruction added a major security dimension to the burden of problems created by weak governance. In the wake of military actions taken since 9/11, the United States has taken on major new responsibilities for nation-building and state-building in Afghanistan and Iraq. Suddenly the ability to shore up or create from whole cloth missing state capabilities and institutions has risen to the top of the global agenda and seems likely to be a major condition for the possibility of security in important parts of the world. Thus state weakness is both a national and an international issue today of the first order.

Governance and Modernity

The problem of weak states and the need for state-building have existed for many years; the September 11 attacks have made them more obvious. Poverty is not the proximate cause of terrorism: The organizers of the 9/11 terror plot came from relatively well-off backgrounds and became recruits of violent Islamism not in their native countries, but while pursuing higher studies in Western Europe. The attack, however, brought attention to a central problem for the West: The modern world offers an attractive package, combining the market economy's material prosperity with liberal democracy's heritage of political and cultural freedom. It is a package that many people in the world want, as evidenced by the largely one-way flows of immigrants and refugees from less-developed to more-developed countries.

The modernity of the liberal West is difficult to achieve for many societies around the world. While some countries in East Asia have made this transition successfully over the past two generations, others in the developing world have either been stuck or have actually regressed over the same period. At issue is the question of whether the institutions and values of the liberal West are indeed universal, or whether they represent, as Samuel P. Huntington argued in *The Clash of Civilizations,* merely the outgrowth of cultural habits of a certain part of the northern European world.[1] The fact that Western governments and multilateral development agencies have not been able to provide much useful advice or help to developing countries undercuts the higher ends that they seek to foster.

Controversies over the size and strength of the state heavily shaped the politics of the twentieth century. It began with a liberal international order presided over by the world's leading liberal state, Great Britain. The scope of nonmilitary state activity was relatively narrow in Britain and all the other leading European powers, and in the United States it was even more restricted. As the century proceeded through war, revolution, depression, and war again, that liberal world order crumbled. Across much of the world, the minimalist liberal state gave way to a much more centralized and active one.

One stream of development led by way of two branches toward the "totalitarian" state, which focused on wholly abolishing civil society as an independent sphere and subordinating it to state purposes instead. In a sense, both branches came to a stop in Berlin: the right-wing branch when Hitler's bunker there was overrun and the Nazi Third Reich crushed in 1945, and the left-wing branch when the Berlin Wall was torn down in 1989 and the communist experiment crumbled under the weight of its own contradictions across Eastern Europe and the former Soviet Union.

Yet the first three-quarters of the century saw the size, functions, and scope of the state increase in nontotalitarian countries as well, including virtually all the democracies. In 1900, state sectors in Western Europe and the United States generally consumed no more than 10 percent of annual Gross Domestic Product (GDP); by the 1980s that figure approached 50 percent, and in the case of social-democratic Sweden, 70 percent.

This growth, and the inefficiencies and unanticipated consequences that it brought, led to a vigorous countertrend in the form of Thatcherism and Reaganism. The politics of the last two decades of the century were characterized by the reascendancy of liberal ideas throughout much of the developed world, and attempts to control if not reverse state-sector growth. The collapse of the most extreme form of statism—communism—gave extra impetus to the movement to reduce the size of the state in noncommunist countries. At midcentury, the Austrian-American economist and classical-liberal thinker Friedrich A. Hayek was pilloried for suggesting that there was a connection between totalitarianism and the modern welfare state. By the time of Hayek's death in 1992, his ideas were being taken much more seriously.[2] This was true not just in the political world, where conservative and center-right parties came to power, but in academia as well, where neoclassical economics gained enormously in prestige as the leading social science.

Reducing the size of the state sector was the dominant theme of policy during the critical years of the 1980s and early 1990s when a wide variety of countries in the former communist world, Latin America, Asia, and Africa were emerging from authoritarian rule. There was no question that the all-encompassing state sectors of the former communist world needed to be dramatically scaled back. But state bloat had affected many noncommunist developing countries as well.

In response to these trends, the advice offered by the U.S. government and by international financial institutions such as the International Monetary Fund (IMF) and the World Bank stressed measures meant to reduce the degree of state intervention in economic affairs. One of the formulators of these measures would dub them the "Washington Consensus."[3] Detractors, particularly in Latin America, referred to them as "neoliberalism." In recent years, the Washington Consensus has come under relentless attack not only from antiglobalization protesters but also from academic critics with serious credentials in economics.[4]

In retrospect, there was nothing wrong with the Washington Consensus per se: Many developing-country state sectors were in fact obstacles to growth, and in the long run only economic liberalization could fix them. The problem was rather that while states needed to be cut back in certain areas, they needed to be simultaneously strengthened in others. The economists who promoted liberalizing economic reform understood this perfectly well in theory. But the relative emphasis in this period lay heavily on the reduction of state activity, which could often be honestly confused with or deliberately misconstrued as an effort to cut back state capacity across the board. The state-building agenda, which was at least as important as the state-reducing one, received no particular thought or emphasis. The result was that liberalizing economic reform failed to deliver on its promise in many countries. Some particularly ill-equipped countries even found that the lack of a proper institutional framework left them worse off after liberalization than they would have been had it never occurred. The problem lay in basic conceptual failures to unpack the different dimensions of "stateness," and to understand how they relate to economic development.

Measuring the State: Scope versus Strength

A good way to begin analyzing the role of the state in development is to ask whether the United States has a strong or a weak state. One clear-cut answer comes from scholars such as Seymour Martin Lipset, who argue that U.S. political institutions are deliberately designed to weaken or limit the exercise of state power. The United States was born in a revolution against state authority, and the resulting antistatist political culture asserted itself through such constraints on state power as constitutional government with clear protections for individual rights, the separation of powers, federalism, and the like. Lipset points out that the American welfare state was established later and remains much more limited (for example, no comprehensive national health-care system) than those of other developed democracies, that U.S. markets are much less regulated, and that the United States was in the forefront of the movement to contain or roll back the welfare state in the 1980s and 1990s.[5]

On the other hand, there is another sense in which the United States lives under a very strong state. The eminent German sociologist Max Weber famously defined the state as "a human community that (successfully) claims the *monopoly of the legitimate use of physical force* within a given territory."[6] In other words, the essence of stateness is *enforcement:* the ability, ultimately, to send someone with a uniform and a gun to force people to comply with the state's laws. In this respect, the United States as a state is extraordinarily strong: Across its territory there exists a plethora of police and other agencies—local, state, and federal—to enforce everything from traffic rules and commercial-law regulations to criminal statutes and the Bill of Rights.

The United States, in other words, has a system of limited government that carefully restricts the *scope* of state activity. But within that scope, the state has ample power—and not just on paper—to frame and carry out laws and policies. Of course U.S. citizens often give voice to a certain justified cynicism regarding the efficiency and good sense of their own public authorities. In colloquial American English, saying that a job has been done to standards that are "close enough for government work" is not a term of praise. Yet there is no mistaking that the U.S. rule of law is and ought to be the envy of much of the rest of the world: Americans who complain about how their local motor-vehicles bureau treats them should try getting a driver's license or dealing with a traffic ticket in Mexico City or Jakarta.

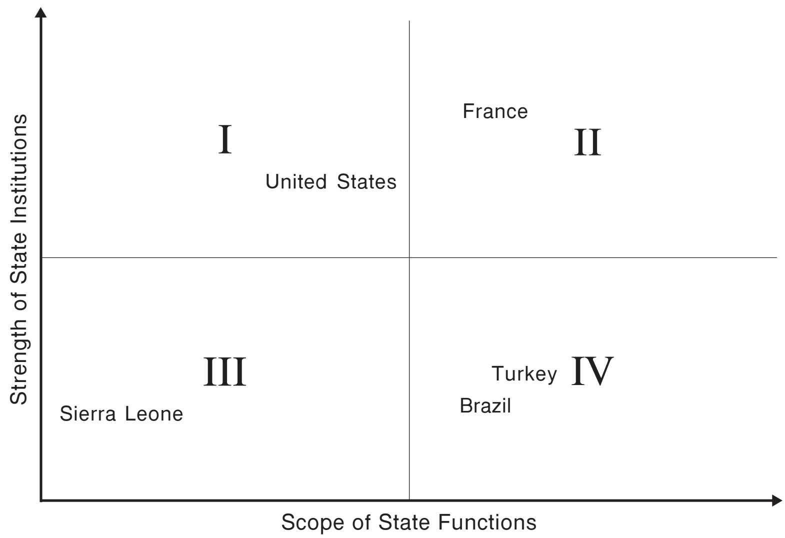
It therefore makes sense to distinguish between the *scope* of state activities, which refers to the different functions and goals taken on by governments, and the *strength* of state power, which has to do with the ability of states to plan and execute policies, and to enforce laws cleanly and transparently—what is now commonly referred to as state or institutional capacity. One of the confusions in our understanding of stateness is the fact that the word "strength" is often used indifferently to refer both to what is here labeled "scope," and to "strength" or capacity.

Distinguishing between these two dimensions of stateness allows us to create a matrix that will help us to differentiate the degrees of stateness in a variety of countries around the world. We can array the scope of state activities along a continuum that stretches from necessary and important to merely desirable to optional and in certain cases counterproductive or even destructive. There is of course no agreed hierarchy of state functions, particularly when it comes to questions of redistribution and social policy. Most people would agree that there has to be *some* degree of hierarchy: States need to provide public order and defense from external invasion before they provide universal health insurance or free higher education. The World Bank's 1997 *World Development Report* provides one plausible list of state functions, divided into three categories that range from "minimal" to "intermediate" to "activist." This list is obviously not exhaustive, but provides useful benchmarks for gauging state scope.

Different countries of course fall at different points along the minimal-to-activist continuum depending on how ambitious they are in terms of what their governments seek to accomplish. There are countries that attempt complex governance tasks like running parastatal business enterprises or allocating investment credits, while at the same time failing to provide such basic public goods as law and order or public infrastructure. It is best to array countries along the continuum according to the most ambitious functions they seek to perform, even if they fail at or do not care much about more basic ones.

Another continuum, which we may think of as running perpendicular to the first, can be used to rate the comparative strength of various states' overall institutional capabilities. Strength in this sense includes, as noted above, the ability to enact statutes and to frame and execute policies; to administer the public business with relative efficiency; to control graft, corruption, and bribery; to maintain high levels of transparency and accountability in governmental institutions; and most importantly, to *enforce* laws. There is obviously no commonly accepted standard of measurement by which to assess the precise strength of state institutions. Moreover, different state agencies may perform at varying levels. In Egypt, for instance, the state-security apparat is brutally effective while other government agencies routinely mishandle simple tasks like processing visa applications or licensing small businesses.[7] The governments of Mexico and Argentina have shown themselves fairly skillful at reforming state institutions such as central banks, but not so adept at controlling fiscal policy or providing high-quality public

Figure 1—State Scope and Strength



schooling or health care. Thus we should think of state capacity as a mostly uneven rather than a smooth phenomenon, since it can vary so strongly from one type of state function to another within the same country.

With the renewed emphasis on institutional quality in the 1990s, a number of relevant indices now exist that can help place countries on the effectiveness scale. One of these is Transparency International's Corruption Perception Index, which draws primarily upon surveys answered by businesspeople who operate in different countries. Another is the privately produced International Country Risk Guide, which breaks the numbers down into categories measuring corruption, law and order, and bureaucratic quality. In addition, the World Bank has recently developed a composite indicator of governance covering 199 countries.[8] Finally, there are broader, politically oriented measures such as Freedom House's annual global survey of political rights and civil liberties, as well as the Polity IV dataset.[9]

Figure 1 above combines these two dimensions into a single graph that arrays scope against strength. The matrix divides neatly into quadrants. From the economists' standpoint, the optimal place to be is in quadrant I, which combines a limited scope for state functions with strong institutional effectiveness. Economic growth will cease, of course, if a state moves too far to the left and fails to perform minimal functions such as protecting property rights, but the presumption is that growth will fall as states become more interventionist and move further right on the horizontal axis.

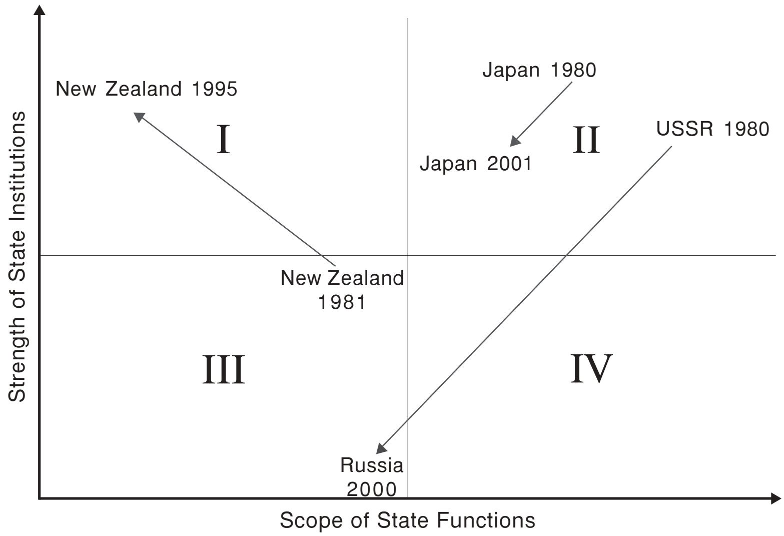
Economic efficiency is not, of course, the only reason for preferring a given scope of state functions. Many Europeans would argue that U.S.-style efficiency comes at the price of social justice and that they are happy to be in quadrant II rather than quadrant I. On the other hand, the worst place to be in efficiency terms is in quadrant IV, where an ineffective state takes on an ambitious range of activities that it cannot perform well. Unfortunately, this is exactly where a large number of developing countries are to be found.

The United States belongs in quadrant I rather than quadrant II because it has a less extensive state than either France or Japan; the United States has not attempted to manage broad sectoral transitions through credit allocation, as Japan did with its industrial policy during the 1960s and 1970s. Nor does the United States boast the same kind of high-quality top-level bureaucracy as France with its *grandes écoles*. In this sense at least, the French state has a higher capacity. On the other hand, the quality of public bureaucracies in the United States is considerably higher than in most developing countries. Turkey and Brazil, by contrast, have funneled large proportions of GDP through their state sectors, run nationalized industries, and regulated and protected a wide range of economic activities.

It is not possible to be highly precise about where to locate countries along either axis, if only because state capacity almost always varies from agency to agency within the same country, and measures applied across several countries at once may not adequately capture all the phenomena. If one goes by outright transfers of income or social-program budgets, for instance, Japan has a smaller welfare state relative to the size of its economy than either France or Germany. Yet Japan provides an equivalent social safety net through the use of regulations (such as rules protecting small family-owned retail businesses), as well as through its use of private-sector microeconomic institutions like lifetime employment and the seniority wage system. On the other hand, Japan's industrial policies historically have been more interventionist than those of most West European states, and its level of domestic regulation is very high. So is the Japanese state more active and administratively ambitious than a typical European welfare state? It is difficult to say.

It should also be clear that over time countries can change their location within the matrix, which also is useful in helping us to understand the dynamic nature of changes in stateness (see Figure 2). Thus the former USSR went from being a state of extensive scope (private property did not exist) with a moderate degree of administrative strength to being a state of narrower scope with an equally diminished degree of state capacity. The same can be said of Japan over the past two decades. It has made hesitant efforts at market liberalization, privatizing some state-owned companies and deregulating some domestic industries (largely under international pressure). At the same time, Japan's vaunted

Figure 2—Changes in State Scope and Strength



bureaucracies (particularly the finance ministry) have deteriorated in quality or have been captured by interest groups within society. Hence both Japan and Russia saw their state sectors move in the same direction—decreasing in both scope and strength—between about 1980 and 2000, though obviously starting from different places and moving at different speeds.

These cases stand in sharp contrast to that of New Zealand, which began a series of liberalizing reforms in the mid-1980s under the guidance of the Labour Party and its finance minister, Roger Douglas. By the start of that decade, New Zealand had developed one of the world's most extensive welfare states, but one that was clearly heading for crisis with the ballooning of national debt and a steady decline in the current account. The initial set of reforms begun in 1984 floated the New Zealand dollar; abolished currency controls; did away with agricultural and consumer subsidies, import licenses and export incentives; changed the tax structure from income and sales taxes to a broad-based consumption tax; and privatized state industries.[10] All of these were classic measures to reduce the scope of the state in New Zealand. But with passage of the State Sector Act in 1988, a second phase of reform began that sought to strengthen the administrative capacity of those core state agencies that remained. These reforms required departments to file monthly financial reports using commercial accounting standards; put the departments under the direction of chief executives who were hired under term contracts that set out conditions for employment; increased managerial discretion to permit shifting of the mix of inputs to be used to produce agreed outputs; and established a system of accountability using contract-like arrangements within the government. By the mid-1990s, therefore, New Zealand had gone some way along the optimal vector described by a state that has managed both to moderate its scope and raise its level of effectiveness.

Scope, Strength, and Economic Development

The development agenda for many international financial institutions shifted dramatically during the 1990s in a way that can be illustrated as follows. Look again at the Figure 1. There is no question that it is better to be in quadrant I than in quadrant IV, but is it better to be in quadrant II, with strong institutions and an extensive state, or quadrant III, with weak institutions and a limited state? A decade ago, many economists would have preferred quadrant III, on the grounds that markets would be self-organizing or that institutions and residual state capabilities would somehow take care of themselves. The Washington Consensus was a perfectly sensible list of economic-policy measures designed to reduce state scope through lower tariffs, privatization, subsidy cuts, deregulation, and the like. There is no reason, after all, for the Brazilian government to operate steel mills, or for Argentina to have a domestic automobile industry. In many cases, transitional and emerging-market countries were advised to move as rapidly as possible toward smaller state scope, on the grounds that the political window for engaging in this kind of reform would close quickly, and that it was better to get the pain of adjustment over with all at once.

The problem for many countries was that in the process of reducing state scope they either decreased state strength, or else generated demands for new types of state capabilities that were either weak or nonexistent. The austerity required by stabilization and structural adjustment policies became an excuse for cutting state capacity across the board, and not just in more-ambitious activities. In other words, while the optimal reform path would have been to decrease scope while increasing strength, many countries actually decreased both scope and strength. Instead of ending up in quadrant I, they ended up in quadrant III.

Something like this occurred in sub-Saharan Africa in the last quarter of the twentieth century. It is common to characterize regimes in this region as "neopatrimonial"—that is, with political power used to service a clientalist network of supporters. In some cases, like Mobutu's Zaire, the neopatrimonial state could only be described as predatory. In other cases, it led to simple rent-seeking by families, tribes, regions, or ethnic groups. As Nicolas van de Walle points out, the neopatrimonial regime, usually embodied in the office of the president, exists side-by-side with a Weberian rational bureaucracy, often created in colonial times, that exists to perform the routine tasks of public administration.[11] The neopatrimonial regime is often threatened by the existence of the "modern" state sector and is a competitor with it for resources.

The dual nature of the African state meant that donor-imposed stabilization and structural-adjustment programs during the 1980s and 1990s had an unintended and counterproductive effect. The international lending community called for cutbacks in state scope through implementation of orthodox adjustment and liberalization programs. But neopatrimonial regimes, given their ultimate political dominance, used external conditionality as an excuse for cutting back on the modern state sectors while protecting and often expanding the scope of the neopatrimonial state. Thus basic investments in roads, primary schooling, agriculture, and public health plummeted during the last decades of the century, while "sovereignty expenditures" on armed forces, diplomatic posts, and jobs connected to African presidential offices increased dramatically. In Kenya, for example, the size of the president's office more than doubled, growing from about 18,000 employees in 1971 to more than 43,000 in 1990. No international lender or bilateral donor wanted to see this happen, yet no lender or donor could devise a form of conditionality to keep this from happening.

Many proponents of the Washington Consensus now say that they *of course* understood the importance of institutions, rule of law, and the proper sequencing of reforms. But questions of state capacity and state-building were largely absent from policy discussion in the late 1980s and early 1990s, and few policy makers in Washington warned of how liberalization might fail or be turned to perverse ends without proper political, legal, and administrative institutions to provide a context within which the reforms could work. Indeed, the general inclination among policy makers at the time was that any liberalization was likely to be better than no liberalization at all.[12]

Shaking Up the Washington Consensus

Thinking on these issues began to shift only after the East Asian economic crisis of 1997–98 and the problems experienced by Russia and other postcommunist countries. The financial crises in Thailand and South Korea were directly related to premature capital-account liberalization. In both countries, foreign short-term capital suddenly flooded into domestic banks while regulatory institutions lagged in effectiveness.[13] It is clear in retrospect that, under such circumstances, a little liberalization can be more dangerous than no liberalization at all. South Korea, for example, liberalized its capital account as a condition for OECD entry but without a corresponding opening of its equity markets or greater foreign direct investment. As a result, foreign investors who wanted a piece of the Korean economic miracle had their money in short-term accounts that could be withdrawn at the first sign of trouble. When Korea's current account began to deteriorate in 1996–97, the national currency came under irresistible pressure as short-term capital was withdrawn. This then set the stage for the economic crisis of late 1997.

Russia and other postcommunist countries faced a different problem. The privatization of state-owned enterprises is of course an appropriate goal of economic reform, but it takes institutional capacity to do this properly. Privatization inevitably creates huge information asymmetries that governments have the duty to correct. Assets and ownership rights have to be properly identified, valued, and transferred transparently; the rights of new minority shareholders have to be protected to prevent asset-stripping, tunneling, and other abuses. Thus while privatization involves a reduction in the scope of state functions, it requires a high degree of state capacity to implement. This capacity did not exist in Russia, and the stealing of public resources by the so-called oligarchs did much to delegitimize the postcommunist Russian state.

This new recognition of the priority of strength over scope is reflected in a comment made by Milton Friedman, the dean of orthodox free-market economists, in 2001. He noted that a decade earlier he would have had just three words of advice for countries making the transition from socialism: "privatize, privatize, privatize." To this he added: "But I was wrong. It turns out that the rule of law is probably more basic than privatization."[14]

From the standpoint of economic efficiency, is it more important to reduce state scope or increase state strength? Which will lead to greater growth? It is of course impossible to generalize, since economic performance will depend on the specific institutional capacities and state functions in question. There is evidence, however, that the strength of state institutions is more important, broadly speaking, than the scope of state functions. We have, after all, the growth record of Western Europe, whose scope of state functions is far larger than that of the United States, but whose institutions are strong as well. And why have East Asia's economies grown more robustly than their Latin American counterparts over the last 40 years? The likely answer has more to do with the former region's higher-quality state institutions than with any differences in state scope.[15] East Asian states have scopes that range from minimal (Hong Kong) to highly interventionist (South Korea), yet all achieved extraordinarily high rates of per capita GDP growth. By contrast, Latin America as a region scores worse than Asia on virtually every dimension of governance.

A further reason for thinking that strength is more important than scope in determining long-term economic-growth rates is the fact that there is a fairly strong positive correlation across a wide variety of countries between per capita GDP and percentage of GDP extracted by governments in taxes. That is, richer countries tend to funnel higher proportions of national wealth through their state sectors.[16] The rate of tax extraction is, of course, a measure of state scope, particularly for countries with higher levels of per capita GDP, but it is also a measure of administrative capacity (and is increasingly used as a metric by international financial institutions). That is, there are any number of countries that would like to be able to take in a larger share of GDP in taxes, but which cannot do so because their capacities for collecting taxes and enforcing tax laws are too weak. The fact that a strong positive correlation exists between tax extraction and level of development suggests that, generally and over time, the positive effects of greater administrative capacity counterbalance the negative effects of excessive state scope.[17]

The New Conventional Wisdom

Those who make and study development policy now take for granted much that has been said so far about the importance of state strength. "Institutions matter" has been a watchword since at least 1997. The concern over state strength, which goes under a variety of headings including governance, state capacity, or institutional quality, has in some sense always been around in development economics. In 1989, Hernando de Soto's *The Other Path: The Invisible Revolution in the Third World* reminded the development community that formal property rights made a difference, and more broadly, that smoothly functioning legal institutions promoted economic efficiency. De Soto sent researchers to find out what it would take to get a small business licensed in Lima, Peru. Ten months, 11 offices, and US$1,231 later, they came back with the papers.[18] In the United States or Canada, the same process would take less than two days. Noting the inefficiencies and barriers to new business startups caused by such a slow, tortuous, and expensive process, de Soto observed that it was no wonder poor entrepreneurs were electing to stay in the "informal" sector of licit yet unlicensed businesses. That sector was dynamic and often served as the only source for certain goods and services in poor neighborhoods. Yet the insecurity and unpredictability that go with the lack of formal, enforceable property rights narrowed investment horizons and prevented small businesses from becoming big ones with more jobs to fill and the like.

The development-policy community thus finds itself in an ironic position. The post–Cold War era began under the intellectual dominance of economists, who pushed strongly for liberalization and a minimal state. Ten years later, many economists have concluded that some of the most important variables affecting development are not economic but institutional and political in nature. There was an entire missing dimension of stateness—that of state-building—and hence of development studies that had been ignored amid all the talk about state scope. Many economists found themselves blowing the dust off half-century-old books on public administration, or else reinventing the wheel with regard to anticorruption strategies.

The new conventional wisdom that institutions are the critical variable in development now stands backed by a host of studies providing empirical documentation that this is so. There has, in addition, been a large and evolving literature on institutions and institutional development.[19] As in the case of all forms of conventional wisdom, the very fact that this view has become received wisdom should make us cautious. Michael Woolcock and Lant Pritchett talk about the problem of "getting to Denmark," where "Denmark" stands generically for a developed country with well-functioning state institutions.[20] We know what "Denmark" looks like, and something about how the actual Denmark came to be historically. But to what extent is that knowledge transferable to countries as far away historically and culturally from Denmark as Somalia or Moldova?

Unfortunately, the problem of how to get to Denmark is one that probably cannot be solved for quite a few countries. The obstacle is not a cognitive one: We know by and large how they differ from Denmark, and what a Denmark-like solution would be; the problem is that we do not have the political means of arriving there because there is insufficient local demand for reform. Well-meaning developed countries have tried a variety of strategies for stimulating such local demand, from loan conditionality to outright military occupation. The record, however, if we look at it honestly, is not an impressive one, and in many cases our interventions have actually made things worse.

NOTES

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3. John Williamson, *The Political Economy of Policy Reform* (Washington, D.C.: Institute for International Economics, 1994), 26–27.

4. Dani Rodrik, *Has Globalization Gone Too Far?* (Washington, D.C.: Institute for International Economics, 1997); Joseph E. Stiglitz, *Globalization and Its Discontents* (New York: W.W. Norton, 2002).

5. Seymour Martin Lipset, *American Exceptionalism: A Double-Edged Sword* (New York: W.W. Norton, 1995).

6. Max Weber, *From Max Weber: Essays in Sociology* (New York: Oxford University Press, 1946), 78.

7. Diane Singerman, *Avenues of Participation: Family, Politics, and Networks in Urban Quarters of Cairo* (Princeton: Princeton University Press, 1995).

8. Indicators for six aspects of governance are available at *www.worldbank.org/wbi/governance/govdata2002*.

9. Adrian Karatnycky, "The 2003 Freedom House Annual Survey: National Income and Liberty," *Journal of Democracy* 15 (January 2004): 82–93. The Polity IV data are available at *www.cidcm.umd.edu/inscr/polity.*

10. New Zealand State Services Commission (1998), "New Zealand's State Sector Reform: A Decade of Change," at *www.ssc.govt.nz/display/document.asp?docid=2384.*

11. Nicolas van de Walle, *African Economies and the Politics of Permanent Crisis, 1979–1999* (Cambridge: Cambridge University Press, 2001).

12. This characterized the thinking of Clinton administration officials at the time of the South Korean entry into the OECD and in policy toward Thailand in the early 1990s, for example, when there was little evidence of warnings concerning premature capital-account liberalization. See David Sanger and Nicholas Kristof, "How U.S. Wooed Asia To Let Cash Flow In," *New York Times,* 16 February 1999, A1.

13. Anthony Lanyi and Young Lee, *Governance Aspects of the East Asian Financial Crisis* (College Park, Md.: IRIS Working Paper 226, 1999); Stephan Haggard, *The Political Economy of the Asian Financial Crisis* (Washington: Institute for International Economics, 2000).

14. Interview with Milton Friedman in the Preface to *Economic Freedom of the World Annual Report* (Vancouver, B.C.: Fraser Institute, 2002), xvii.

15. Francis Fukuyama and Sanjay Marwah, "Comparing East Asia and Latin America: Dimensions of Development," *Journal of Democracy* 11 (October 2000): 80–99.

16. World Bank, *Building Institutions for Markets: World Development Report 2002* (Washington, D.C.: Oxford University Press, 2002).

17. Some forms of taxation are unambiguously bad for growth, like tariffs and other taxes on international trade. World Bank, *Building Institutions for Markets.*

18. Hernando de Soto, *The Other Path: The Invisible Revolution in the Third World* (New York: Harper & Row, 1989), 134.

19. For empirical reinforcement of the new conventional wisdom, see, among others, James A. Robinson and Daron Acemoglu, et al., "The Colonial Origins of Comparative Development: An Empirical Investigation" (Washington, D.C., NBER Working Paper 7771, 2000; William R. Easterly, *The Elusive Quest for Growth: Economists' Adventures and Misadventures in the Tropics* (Cambridge: MIT Press, 2001); Nicolas van de Walle, *African Economies and the Politics of Permanent Crisis, 1979–1999.* On institutions and how they develop, see Robert E. Klitgaard, *Controlling Corruption* (Berkeley, Calif.: University of California Press, 1988); Merilee S. Grindle, *Getting Good Government: Capacity Building in the Public Sector of Developing Countries* (Cambridge: Harvard Institute For International Development, 1997); Merilee S. Grindle, *Audacious Reforms: Institutional Invention and Democracy in Latin America* (Baltimore: Johns Hopkins University Press, 2000); Judith Tendler, *Good Government in the Tropics* (Baltimore: Johns Hopkins University Press, 1997); World Bank, et al., *The State in a Changing World* (Oxford: Oxford University Press, 1997); World Bank, *Reforming Public Institutions and Strengthening Governance* (Washington, D.C.: World Bank, 2000); World Bank, *Building Institutions for Markets.*

20. Michael Woolmark and Lant Pritchett, "Solutions When the Solution Is the Problem: Arraying the Disarray in Development, Center for Global Development," Washington, D.C., September 2002.