

Institutional Constraints on Modern Economic Growth

How to import modern Western Institutions to suppress economic growth in underdeveloped countries? Russian experience and some warnings for newcomers reformers

Introduction

The monograph *Institutional Constraints on Modern Economic Growth* deals with the most dangerous obstacles standing in the way of long term economic growth. Some of these obstacles have been studied extensively, while others are well known but have been largely forgotten over time; finally, there are some that for various reasons are normally ignored.

The economic discipline considers human behavior through the prism of people's interests and attempts to maximize a certain good under conditions of limited resources. People's interests to a large extent depend on "the rules of the game" in effect in a given country and society, and on the organizations and social structures ranging from family to government, which ensure that these rules are observed. Most countries and peoples live in poverty, remaining for centuries unable to "catch up" with the leaders. In such countries, the true law is not a written text, but the arbitrary will of the ruler or the leader of some armed group. The value of human life for the state and society in such countries is negligible, while losses and victims can be counted by the thousand, or even by the million.

Economists are all in agreement that securely guaranteed rights of private property are a *sine qua non* for long term economic growth. In countries where human life does not constitute a value for the state, the right to private property cannot be guaranteed. That is, in such countries there is no way to ensure the availability of the minimal conditions for economic growth.

The majority of stimuli which contribute to economic growth constitute a system of logically interconnected elements. In the same way, the majority of obstacles standing in the way of long term economic growth have common roots.

The book which we want to introduce to the reader at present is first of all devoted to the problems which arise in any country making attempts to rise up and maintain itself on the way to stable (*sustainable*) long term economic growth.

There are two leading approaches to solving the problems which arise in connection with the relations between society and the individual.

The first approach is based on the assumption of the citizens' limited capacity for concerted action, and the state's having access to the total (or significant) quantity of information. In this case, the citizens are in need of protection from the market and from free

competition. In the modern world, this approach finds its expression in the state's seeking to extend its sphere of responsibility and authority in such a way as to make it encompass not only the "pure public goods," but also the "mixed public goods," and at times even the private goods. At the same time, the state's responsibility to the citizen incapable of concerted action is minimal, while its control of citizens' behavior and the behavior of private organizations reaches maximum possible levels.

By contrast with the first approach, the second presupposes that nobody can solve the individual's problems better than the individual him or herself. Despite the individual's limited access to information, he or she can resolve problems independently, without interference by the state. The individual can also correct his or her own mistakes, provided nothing threatens the individual's life and liberty. The second approach considers the individual to be perfectly capable of concerted rational action, such that nobody can dispose of the individual's property better than the individual himself. Given such an approach, the state's only function is to provide the "pure public goods" (that is, defense, security, and justice).

At the end of the 18th century, V. F. Humboldt formulated the objectives of the state, which correspond to these two approaches: "A State, then, has one of two ends in view; it designs either to promote happiness, or simply to prevent evil"¹

Ever since Adam Smith, economists have been comparing the leading and the backward countries with each other, in an attempt to explain the successes and the fiascoes in their economic development.

For the greater part of humanity and in most countries today, the problem of retarded development is still a real concern. This is why it is crucial to come up with a detailed description of reasonably reliable development venues. Such a description requires a thorough understanding of what must be adopted from other sources and what must be initially available (capital, knowledge, reasonable laws, and so on) in order for the economy to embark on a road of stable growth, and to do so at a rate higher than that in the developed countries.

After two centuries of modern economic growth,² a phenomenon now widespread among a considerable, even though still a minority part of the human race, is the widening of the gap between the rich and the poor countries. This gap today exceeds any bounds it had ever known

¹ Humboldt W. von, *The Sphere and Duties of Government (The Limits of State Action)* http://oll.libertyfund.org/index.php?option=com_staticxt&staticfile=show.php%3Ftitle=589&Itemid=28 Chapter III (1854 ed.) [1792]. In what follows, as we analyze the import of religion and ideology in economic terms, we will specify the religious-ethical roots of these two approaches.

² The notion of "modern economic growth" involves economic growth rates which stably exceed the rate of population growth over time. See Kuznets 1966.

before. At the same time, a large part, even if not the majority, of humanity today continues to enjoy the same standard of living³ it had a thousand years ago: that is, it continues to balance on the edge of survival.

Countries which have reached a medium level of development have problems of their own, as well. Among such countries are Russia and Argentina, two states which, a series of jerks and tugs notwithstanding, are not managing to augment the list of developed countries with their own names or even to continue significantly and at a regular rate to decrease their lagging behind.

Economists today have a unique opportunity to observe and compare former socialist states which, having gotten off to a more or less simultaneous start, have introduced new institutions at home in the hope of ensuring the conditions necessary for embarking on a path of long term economic growth. Such a comparison is interesting because of the variety of the institutions being introduced (from highly competitive democracy in Lithuania to the grandiose regime in Turkmenia; from the “old fashioned” and nearly free market in Estonia to the interference by functionaries and officials in the management of individual ventures or businesses in many countries of the CIS).

A study of the most recent developments in the post-Soviet states, along with a comparative institutional analysis of the economic history of the 19th and 20th centuries, can help single out the key factors in economic growth. An influx of capital does not on its own guarantee successful “catching up” in development; nor can such catching up be guaranteed by the import of knowledge and technologies. Capital influx and imported knowledge and technologies may turn out to be of little use if there is no borrowing and entrenching of effectively functioning institutions at home.

Are there institutions which make it possible to turn a backward economy into a quickly growing one which can later become a highly developed economy, as well⁴? If there are, then what are these institutions, and what are the conditions necessary for their effective functioning? The answers to the questions posed make it clear that *the most significant institutions are the protection of private property and the inviolability of the individual person (protection from arbitrary arrest and detention)*. This last presumes the availability of a package of the principal “political” rights, such as freedom of speech, freedom of thought and

³ \$400-600 in 1990. See Maddison 2001, 2003.

⁴ We are here concerned only with those institutions which have long since established a solid reputation for themselves in other countries, not with locally invented constructs.

conscience, and so on. At the same time, the impact of such institutions as legislation concerning entrepreneurship (registration, licensing, bankruptcy), taxes, funds market regulations, and the like, is in fact limited (see Appendix 1).

These conclusions are arrived at on the basis of a comparative and statistical analysis of institutions in various countries of the world over the last 180-200 years,⁵ as well as institutions in the post-communist states in the nineties of the 20th century.⁶

Key Definitions

The present work relies on a series of concepts which require precise defining. These are first of all the notions of institution, constitution, society of the “Rule of Law,” society of the “Rule of Force,” and modern or contemporary economic growth.

Douglas North defines the notion of “institution” in the following way:

“Institutions are the rules of the game in a society or, more formally, are the humanly devised constraints that shape human interaction.”⁷

Without going into any ideological or philosophical-theological debates about the origin of laws and legislation, let us note a number of circumstances:

- Institutions founded upon principles of natural law have proven to be more effective than those institutions, which were constructed upon positivistic principles⁸;
- Some rational subjects are of the opinion that certain constraints are given not by humanity, but by a higher Being. This conviction impacts considerably on laws and legislative practices.

Hayek’s notion of the natural selection of institutions also presupposes that human beings are incapable of rationally constructing an economically effective ethical and legal system based exclusively on individual persons’ own and the historical general experience.⁹ That is, at least, the entire system of norms cannot be rationally and consciously constructed by the individual or even a group of individuals consciously coordinating their efforts. So as not to go into a

⁵ K. E. Yanovskiy and S. G. Shulgin, “*Instituty, demokratiya i ekonomicheskiy rost: test 180-letnego razvitiya*” (“Institutions, Democracy, and Economic Growth: Testing 180 Years of Development,” Rus.), 2008, as well as see Appendix 1.

⁶ Mau, Yanovskiy, Zhavoronkov, et al. 2003.

⁷ D.C. North 1990 (“Institutions, Institutional Change and Economic Performance”), p. 3.

⁸ “Positivistic” principles, based on an understanding of law as a function of power, could not provide for the stability and guarantees of the rights of market subjects. Both the Anglo-American and the French system of new (that is, beginning with the 17-19th centuries) institutions are based on allowing for a super-state, super-authority origin of the basic laws and rights, and on the absence of the right of the state to alter these basic laws or delimit these basic rights.

⁹ “*Pagubnaya samonadeyannost*” (“Fatal Self-Assuredness,” Rus.), Moscow, *Novosti*, 1992. See pp. 61-63 for key institutions, and pp. 47-48 for the evolutionary selection of institutions.

discussion of the problem of the primacy of matter or consciousness in the present work, let us introduce a somewhat more general definition of the notion of “institutions”:

Institutions are humanly acknowledged constraints which shape human interaction.

Elaborating upon the definition given by D. North, we also take into consideration those institutions which are based on Biblical moral norms. These institutions are the object of general acceptance and acknowledgement, independently of the will of the authorities.

By the “import of institutions” we will mean the conscious copying (even if not necessarily exact copying) of a well known norm, as well as the instruments for its implementation. **Norms** are any dictates or prohibitions against the performance of some action.

Society of the “Rule of Law” is a society governed in accord with generally known judicial norms.¹⁰ These norms are based on prioritizing basic individual rights and freedoms over group and state interests. In such a society, requisite safeguards for individual rights and freedoms are securely provided, including the use of force to ensure these rights and freedoms. Such safeguards include the independence of the courts, which is provided for by law and tradition. The courts’ independence finds its expression in that the state, as represented by the highest ranking officials and agencies of the authorities, may in the course of litigation in court lose¹¹ a suit of some considerable social import against a private individual.¹²

An institutions package is the sum total of the norms and offices historically integrated as complex unities and possessing a common ideological grounding. The component elements of an institutions package may be some set of traditions, religion, church organizations, morals, types of family relations, or various legislative constructs. However, there is no way to indicate with any degree of precision which of these elements play a decisive role in determining the eventual successes and failures in the course of the economic development of a society that makes use of a particular package of institutional instruments. But we can analyze the practice of implementing particular institutions packages. Some of them yield positive results and provide a way to embark on a path of long term economic growth, while others do not.

¹⁰ At the same time, norms may be an unwritten but generally accepted tradition; they may be founded on a precedent court decision; or they may exist as a formally ratified law.

¹¹ As an example, we may cite the US Supreme Court decision concerning the illegality of the procedure used to reach decisions about arresting terrorists at the Guantanamo military base. The decision caused serious problems for the US administration. See the decision in the case of *Hamden vs. Rumsfeld*, 04-70, decision of June 29, 2006.

¹² Mention of such a process can easily be come by in the archives of the press. Losing in court in case of a labor dispute or dispute concerning property (that is, a dispute concerning small claims) was a real possibility for a government or state office or enterprise even in a totalitarian state, including the USSR. For instance, cases of rehabilitation at work as based on a court decision were even then not outstanding exceptions, even though in situations of this kind the suing party would normally be an individual person, and the defense a state or government agency.

Occasionally, the real integration of institutions packages takes place during elections when a party makes an offer and the voters choose not some one particular institution, but rather an entire package. In developed countries a consensus with regard to basal values prevails. Accordingly, parties discuss the relationship between taxes and social programs (taxes a bit higher and more social programs, or taxes a bit lower and fewer social programs) and the accent marks in the structure of the public goods provided (more defense and security or more state spending on health services and education). Basal institutions, by contrast, do not come within the purview of the discussion. For example, in modern informational society there is no problem of proportional coordinating along the lines of: “the right to life (security) or freedom of speech.” In transit countries no consensus concerning basal norms has as yet been arrived at, so that the institutions packages under discussion may differ from each other in fundamental respects. Some packages may contain a set of institutions typical of a totalitarian state, while others may feature sets of institutions associated with “Rule of Law” societies.

Free elections are elections to government office, conducted in the presence of the press from the opposition, and freedom of union. Government agencies are authorized to act in ways which are limited only by the rights of citizens and other private persons, a fact which is, as a rule, established clearly by the constitution. Elections of the sort specified are elections conducted on the basis of a declarative order of the registration of parties, blocks, and candidates; on the basis of the physical security of their campaigning; and on the basis of a transparent totaling of votes, as well as of the absence of any opportunity or precedent of arbitrary denial of right of access to the elections for a party represented in parliament or having a rating which is a priori sufficient for participation in the elections.¹³ Freedom of choice necessarily presupposes guarantees of the physical security of the voters, both during the elections and following the announcement of the election results.¹⁴

Opposition press is the press which accuses the head of the executive branch of the government of illegal or immoral action, or else of ineffectiveness which endangers the country or society and of discharging his or her obligations in improper ways. In such a case, the head of the executive branch of the government required to be (should be) replaced on the basis of new elections (recalled from his or her position).

¹³ At the same time, the elections mechanism is of no crucial significance (we presume that, if genuine political competition is assured, all the players in the game will adapt to any legislation concerning elections). We are concerned only with an actually operative mechanism for reaching decisions collectively or for altering the type of regime in power.

¹⁴ For the consequences of the absence of such guarantees, see Yanovskiy, Zhavoronkov, and Zatkovetsky 2007.

In view of the widespread use of terms such as “**transit economy**” and “**country with a transit economy**” in the present work, we want to focus on the issue of what constitutes such a condition of being in “transit.” Per capita GNP is inappropriate as a choice of the main criterion for assessing the condition of the economy in this case. For example, high petroleum prices could make Saudi Arabia a rich country, but clearly not a “developed” one in any complete sense of the word, just as earlier a favorable combination of factors had made Argentina rich, even though this nation was unable to retain its place among the wealthiest countries of the 20th century. This is why a country with a transit economy is, first of all, one whose institutions do not provide for an effective functioning of the market economy.

By **contemporary** or **modern growth** we mean economic growth rates stably exceeding the rates of population growth. In earlier times, periods of economic growth led primarily to rapid population increase. In more recent centuries, a typical feature of economic growth has been an inverse proportional relation between population growth rates and the GNP. Such a relation between these indicators is in fact what placed countries and their institutions in the center of researchers’ attention.

A *constitution* is the set of values and norms which have become deeply entrenched and accepted among the overwhelming majority of agents. These norms are implemented or put to use with minimal (close to zero) costs, because they are accepted by the overwhelming majority of agents. An “entrenched set” means that changes in these norms are realized at maximum cost.¹⁵

Society of the “Rule of Force” is one in which authority legitimates itself exclusively by force and readiness to resort to coercion in critical situations. In countries run by order of this sort, laws are displaced by the right of the authorities to use force. Force is, then, the main law in a society of the “Rule of Force” type.

By **basic individual rights and freedoms** we mean: the inviolability of the individual person (the individual’s protection from arbitrary arrest and detention), taken in the most general sense of the term, including not only the right to life, but also the inviolability of the individual person who publicly criticizes the authorities or adheres to a creed of which the authorities do not approve. The term also includes private property, including freedom to determine prices and values and freedom of trade. This set of rights and freedoms coincides perfectly with the set of

¹⁵ Changes may take decades. Thus Biblical values, which form the basis for the institutions of the US, cannot be subject to change. Changes in the US Constitution, not as a formal legal act, but as a totality of norms, cannot be realized within a time span of average duration, insofar as they call for changes in the “soft infrastructure” (for details, see W. Niskanen, “The Soft Infrastructure of a Market Economy,” *CATO Journal*, Fall 1991, vol. 11, issue 2, p. 233).

“natural rights” as described by John Locke.¹⁶ Society may limit these rights only with the aim of preventing the infliction of damage by some private persons upon others, and only on the basis of extant laws.

Basal institutions are the totality of basic individual rights and freedoms, and the norms and law enforcing structures which guarantee their being adhered to.¹⁷ Basal institutions have priority from the point of view of borrowing, construction, entrenching, and protection.

In order to begin to consider the costs of such borrowing, construction, entrenching, and protection, it is imperative to assess the way in which the majority of agents relate to them, as well as this majority’s readiness to follow or to resist new rules. In this connection it is essential for us to consider the following definition.

Demand for institutions (patent, or revealed demand for institutions) consists of those steps taken by the population, which promote the creation and establishment of certain sets of institutions (voting for parties which support some certain set of institutions, joining in the activities of these parties, taking part in events which include demanding that certain norms be introduced or abolished, and so on). The value of the demand for institutions may be both positive or negative.

The following two definitions will be necessary for a more complete understanding of the demand for institutions (as expressed in voter behavior). These definitions describe two principal “ideal types” of politicians.

A “*leftist politician*” in the present work is a certain “ideal type” of politician in a Rule of Law democratic state. Such a politician argues for expanding the functions of the state *beyond supplying the pure public goods*. A “leftist politician” considers these new functions (supplying mixed public goods, controlling the behavior of citizens and markets) as the main ones for a modern state. He or she believes that there must be higher taxes for the “rich” than for the “poor,” and that taxation must be progressive. A “leftist politician” also speaks out against lump sum taxes (when the same tax amount is levied from every taxpayer). Working on the assumption of citizens’ limited capacity for concerted action and the assumption of the total awareness of all events by the state, a “leftist politician” believes that citizens are in need of

¹⁶ See John Locke, “Concerning Civil Government, Second Essay,” [http://www.swan.ac.uk/poli/texts/locke/Article 87](http://www.swan.ac.uk/poli/texts/locke/Article87), in Chapter 7, “Of Political or Civil Society”: “87. **Man being born, as has been proved, with a title to perfect freedom and an uncontrolled enjoyment of all the rights and privileges of the law of Nature**, equally with any other man, or number of men in the world, hath by nature a power not only to preserve his property- **that is, his life, liberty, and estate...**”

¹⁷ Independent courts (independence of judges, their irremovability, the high costs of their dismissal); the transparency of the activity of the law enforcing agencies of the government.

protection from the market and from free competition. Such a politician is, accordingly, convinced of the utility of state controls, explaining all and any failures encountered by such controls by their incompleteness and failure to be all-encompassing.

In other words, a “leftist politician” treats private property and freedom of contract with suspicion, preferring equality of results to equal opportunities. Such a politician is sure of the state’s ability to perform the task of supplying mixed public goods better than the market and private non-state organizations can.

A “leftist politician” defends imposing limits on:

- freedom of consumer choice (in the guise of “protection for the consumer”);
- freedom of speech, by supporting “public” television and radio broadcasts, as well as by imposing limitations on freedom of statements made to the mass media (introducing such constraints under the rubric of “political correctness”), and so on;
- freedom of conscience (i.e., the state imposes some particular attitude toward any one given faith);
- freedom to bear arms and the right of any human being to self-defense and to the defense of his or her dignity and property.¹⁸

A “*rightist (conservative) politician*” is the proponent of views and preferences that are the mirror opposite of those of the “leftist politician.” He or she assumes that the only function of the state is to supply pure public goods (that is, the state only performs the function of the “night watchman”). A “rightist politician” speaks up for minimal taxation based on a flat rate, and supports indiscriminating lump sum taxation. He or she supposes that only a free media market provides for freedom of speech, and, accordingly, speaks out against the state’s involvement in any activities in this area.¹⁹ From the point of view of the “rightist politician,” an “exemplary” state does not interfere in private affairs, whether business, community, or family. A “rightist politician” is a supporter of the freedom to bear arms.

¹⁸ In view of the sum total of these indicators, the conservative press occasionally refers to such a politician as a communist. We should make an explanatory note, however, to point out that a considerable number of such politicians have surfaced since the end of the 1960s. Leftist politicians in democratic countries of the early to the mid-1900s often spoke out against private property and the freedom of enterprise, but rarely rejected all basal institutions wholesale. Such rejection, even if in a mild form, has been typical of leftist politicians of the last four decades.

¹⁹ The rightist politician is against setting up administrative barriers in connection with entry into the market, and against state spending used to support any particular mass media.

That is, a rightist politician does not accept Weber's definition of the state as a subject successfully claiming a "monopoly on legitimate physical force."²⁰ The principal player in this sense does not amount to being the only one.

Based on the outcomes of his research, Vernon Smith draws the conclusion that the tendency to shift one's burden onto others is not all that widespread, and that the free-rider minority is quite comparable with a different minority, namely, the one which, for a variety of reasons, tends to assume a disproportionately high share of the public expenses. Clearly enough, this outcome can be obtained only based on a sample which does not include such agents as those who are confident of their right to enjoy free public goods. Agents not seeing themselves as payers, less for financial reasons than on "ideological" grounds ("ideological" free riders, pretenders for a free ticket) destroy the picture. Their significant minority (if it has not yet in some countries become the majority) can no longer be balanced out by a small group of wealthy philanthropists.

We devote particular attention to the institutions grounded in the moral norms of **monotheism**. This last presumes the teaching based on what has come to be known as "Sinaitic Revelation." The teaching's sacred texts include a set of much reiterated requirements toward the individual and the state to impose restraints on one's own behavior and wishes in accord with laws given from on High. The teaching also encourages its followers to study its texts, including doing so even by means of independent effort. At the same time, monotheism does not cover those versions of the teaching, which are founded upon a notion of successful violence as ethical or that represent their patron as a Higher Being whose chief expression of favor to his believers is granting them success in violence²¹ ("Divine judgment" in the Middle Ages in Europe, cult of the Shahids, and the like).

Generalizing, we can say that a "rightist politician" is a classic liberal of the 17th to the late 18th centuries, characterized by a neutral or positive attitude toward religion.

By a "closed **democracy**" in this book we mean a political regime which conducts formally competitive elections. At the same time, the majority of the electorate has no chance of changing the authorities' policies by means of voting and while remaining within the framework of the Constitution, because of the constraints imposed on them by the non-elected institutions. Among such non-elected institutions are: the legal system of courts, the law enforcing agencies of the government, the mass media, and the army.

²⁰ Weber 1990, p. 645.

²¹ The distinctive feature of paganism consists less in the multiplicity of deities than in anthropomorphic notions of the Divine. In the thinking of a pagan, a divine being is subject to the same passions as humans, but experiences them remarkably strongly. The god Odin, who welcomes the mighty and valorous slain fighters to Valhalla in Old Norse mythology, appears more ethically demanding and less "humanlike" in this respect than a formally unique "God" who ushers the murderers of women and children into heaven.

On Reasons for the Wealth of Nations

A fundamental condition for the inviolability of private property involves guarantees of the inviolability of the individual person (protection from arbitrary arrest and detention). This conclusion is confirmed by the results of a comparative inter-country analysis of institutions over the course of the last two centuries and an analysis of the institutions in countries having a transit economy.²² Only when not fearing for their lives and unafraid of arbitrary arrest, are economic agents likely to concentrate their efforts on activities of production, to defend their property in times of need, or to insist on their rights and legal interests in different spheres of endeavor, rather than seek opportunities of business emigration.

A sine qua non for the development of private initiative is the condition of the individual citizens' resting assured that their success or prosperity, as manifested by their having houses better than the police officer's, or having cars more expensive than the town mayor's, or having spouses more beautiful than the governor's, will not lead to castigating measures taken against them by any one of these functionaries. If this condition is not fulfilled, any formal guarantees of freedom of private enterprise and protection of private property are not worth the cost of the paper they are printed on.

Accelerated development in countries ruled by authoritarian regimes often turns out to be unstable.²³ By contrast, countries which guarantee authentic inviolability of the individual person not only successfully develop in their own right, but also contribute to the acceleration of economic growth rates in the entire world (by means of information and knowledge, capital, and institutions).

Why Stable Systems Turn Out to Be Unstable

One of the principal questions addressed in the present work is the issue of why the classically liberal system of a compact state, the "night watchman" of the 19th century, turned out to be unstable. At the same time, we have no intention of competing with Ludwig von Mises, Friedrich Hayek, Adam Smith, Charles-Louis Montesquieu, Frederic Bastiat, or Richard Cobden in explaining the reasons for the unraveling of socialist and statist systems.

²² K. E. Yanovskiy and S. G. Shulgin, "*Instituty, demokratiya i ekonomicheskiy rost: Test 180-letnego razvitiya*" ("Institutions, Democracy, and Economic Growth: Testing 180-year-long Development," Rus.), 2008; see also Appendix 1.

²³ Przeworski et al., 2000; see also Appendix 3 to Chapter 5.

On the Reasons for the Poverty of Nations

In analyzing particular instances, we will resort to the method of proof by contradiction, or *reductio ad absurdum*. We will consider the outcomes to which the absence of guarantees for the security of the individual person and property leads.

Richard Pipes notes²⁴ that any despot considers any property and all life to be found on the territory under his control as part of his own property. Institutions functioning on such territory completely preclude safeguards for the security of the individual person or property, thus effectively “preventing” long term economic growth. Such an attitude toward people and property was typical, inter alia, of Hitler: to the question of why he does not socialize property in Germany, he is reputed to have answered that he has already socialized people.

The Robbers of Today: Special Interests Groups

In the Rule of Law democracies, there is never a dearth of people who evince a clear tendency to social parasitism. That is, people who consider independent work and wages to be something insufficiently prestigious. Operating within the parameters determined by law, such people attempt to achieve a partial “takeover” of the state so as to derive some benefit of their own from it.

In what follows we will begin to consider the behavior of groups of people who specialize and do their training in forced redistribution “within the framework of the law.” This discussion opens with the survey of works by Mancur Olson, who first introduced and provided a detailed description of the notion of “special interests groups.”

Groups of this sort seek opportunities, including resorting to force, to limit and regulate the market by means of taking over the state; that is, by infiltrating state institutions. The force to which they resort is supposedly rendered legal by elections and modern court procedure. It is important to note that this force is much more considerable than what is available to any team of gangsters or any “roving bandit.”

Special interests groups (the “modern gangs”) have no long term interests. This is precisely what makes them capable rather quickly of bringing entire sectors of the economy into a condition of decline, and of endangering the likelihood of continued economic growth in large developed countries.²⁵

²⁴ Pipes 2000, based primarily on the example of Russia.

²⁵ For instance, the coalition of small transport operators, who lobbied – and achieved – regulation controls of the railroads in the 1930-’70s in the US; or car manufacturing trade unions of the 20th to the early 21st centuries, also in the US. For further detail, see the Chapter on interests groups.

Regrettably, Russia has managed to accouter herself with a considerable number of influential special interests groups, even though she has not yet constructed that many Rule of Law Democracy institutions.

A special interests group stands behind almost every case of extraneous regulating and control or any other form of interference by the state in the life of private citizens (or market agents). The wellbeing of such groups increases at the expense of society as a whole. The greatest of the losses to society consists in the delimitation of opportunities for economic growth.

A challenge along these lines, with the interests of special groups pitted against opportunities for economic growth, is typical not only of societies of the Rule of Law type, but also of the type of the Rule of Force. The difference consists in that in societies of the Rule of Force type, the spectrum of possible ways of influencing the behavior of private persons is significantly wider, including the most diverse forms of coercion. The opportunities of eliminating resources are also correspondingly greater. However, the resources themselves are as a rule fewer in number, since societies of the Rule of Force type are not rich.

Institutions in the Rule of Law type of society put constraints on the activities of politicians and special interests groups which are aimed at channeling administrative revenues their own way. By contrast, societies of the Rule of Force type, where power derives from coercion, there is nothing to limit the activities of the groups of people listed, whose actions are aimed at benefitting themselves to the detriment of economic growth.

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