

## Foreword

I am delighted to write a foreword to this splendid collection of articles on a very important subject, the role of entrepreneurship in the process of economic development. One of the important conclusions of *The Political Economy of Poverty, Equity and Growth—A Comparative Study*, in which Hal Myint and I directed the study of the economic history of twenty-one developing countries until the late 1980s, was the importance of entrepreneurship and what may be called a classical liberal policy framework in explaining the differing economic performances of developing countries in the post-World War II period. The case studies in this volume, particularly of developed countries not included in the Lal-Myint (1996) study—namely, Romania, Sweden, China, India, Ireland, New Zealand, and Botswana—add strength to its conclusions besides providing incisive accounts of the processes of economic repression and reform (however limited) in these countries.

Particularly noteworthy are the case studies of Sweden and New Zealand. The former, which has become the poster boy of the New Dirigiste backlash against the classical liberal policy package embodied in the so-called Washington consensus (see Lal 2006), represents a country that has succeeded in creating a “capitalism with a human face.” The latter is an example of a country that has supposedly adopted the classical liberal package without any marked effect on its growth rate. The authors of the careful case studies of these two countries show that Sweden’s

overexpansion of its welfare state has led to a sclerotic economic performance compared with its earlier performance. On the other hand, it is the failure of New Zealand to fully implement the classical liberal package that has led to its relatively poor economic turnaround. The same can be seen to be true of Latin America in the excellent Chapter 7 surveying its economic performance.

It might, however, be useful to put these essays into a broader theoretical and historical perspective in this foreword, even if that means rather vaingloriously blowing my own trumpet! Over the last decade, I have been trying to put some content into the black box of “institutions” that, it is increasingly agreed, provides the basic reasons for the differing wealths of nations. Particularly in my Ohlin lectures (Lal 1998, 2006), I have argued that institutions are the means to constrain the self-seeking instincts that we are endowed with as part of our basic human nature. They reduce the transactions costs involved in the efficiency of exchange and those associated with policing opportunistic behavior by economic agents. These two types of transactions costs are in turn related to a distinction I make between the “material” and the “cosmological” beliefs of a culture—which is the informal aspect of institutions that constrains human behavior. “Material” beliefs relate to ways of making a living and can change quite quickly as the material environment changes—see Chapters 10 and 11 on China and India, respectively, in this volume. “Cosmological” beliefs concern, in Plato’s words, “how one should live.” They provide the moral anchor of different civilizations and are slow to change. They are determined by the ecological conditions in which different civilizations arose as well as the language group to which the cultures belong. They are transmitted through child-rearing practices using the moral emotions of shame and guilt to perpetuate them through the generations. I also argued that it is the material beliefs that are relevant for economic performance.

The material beliefs of all the agrarian Eurasian civilizations were inimical to the risk-taking and novelty-seeking merchants and entrepreneurs who, with their capitalist institutions such as markets, banking, bills of exchange, and business firms, go back to ancient Mesopotamia (see Baechler 1975). Tolerated as a necessary evil to extract and transfer the food needed by the men of the sword and the book in the towns, they were subject to constant predation by the state. It was due to the eleventh-century papal legal and administrative revolution of Pope Greg-

ory VII that western Europe alone of all the agrarian Eurasian civilizations broke from these dysfunctional material beliefs. The legal papal revolution created a church-state that protected property rights across western Christendom (see Berman 1984). This led to the Great Divergence, with the slow rise of the West from the twelfth century onward until it overtook the other hitherto richer Eurasian civilizations by the eighteenth century (Maddison 2001). This legal and administrative infrastructure for a market economy, which makes the risk-taking and novelty-seeking activities of entrepreneurs secure, can and has been transferred (however imperfectly) to many non-Western countries, first as part of globalization in the nineteenth century under the aegis of the British empire and today, after the interwar breakdown of this liberal international economic order, under U.S. hegemony (Lal 2004, 2006).

This globalization of capitalism has, however, been resisted by two groups—the cultural nationalists of the Third World and various dirigistes in all three worlds. The origins of this hatred of capitalism and its main agents—entrepreneurs—arise because the change in material beliefs associated with the eleventh-century legal papal revolution was preceded and precipitated by an earlier papal family revolution in the sixth century by Pope Gregory the Great. This changed the West's cosmological beliefs by promoting individualism, the independence of the young, and love marriages (see Goody 1983), as contrasted to the communalist values and arranged marriages that remain common to this day in the rest of Eurasia. This change in the West's cosmological beliefs can be characterized as Westernization, whereas the later change in its material beliefs associated with the eleventh-century legal papal revolution can be characterized as modernization. Although temporally conjoined in the trajectory of the West for economic prosperity and the promotion and protection of the entrepreneur on which it is based, it is only the material beliefs associated with modernization that the rest need to adopt. They can modernize without Westernizing (i.e., accepting the cosmological beliefs of the West), as shown by Japan in its Meiji revolution and more recently by the increasing (although still incomplete) acceptance of the market by the two ancient Eurasian civilizations of China and India (see Lal 1998, 2000a).

The dirigisme that began in the late nineteenth century in Europe with the creation of welfare states and became rampant in the post-World

War II Third World was based on the attractions of various varieties of socialism as a route that offered modernity without sacrificing traditional communalist cosmological beliefs. The socialist panaceas combined the rationalism of the Enlightenment with the critique of the Romantic revolt as represented in the writings of the young Marx and the Fabian socialism of the Webbs and William Morris in the United Kingdom. They offered a route whereby countries could modernize without losing their souls. With the death of the countries of “really existing socialism,” the harder socialist panaceas based on the plan were seen to be dead ends, but a softer version based on the desire to have “capitalism with a human face” still survives (see Lal 2006). Chapter 9 on Sweden in this volume is thus salutary in showing that this, too, is a dead end for sustaining long-term economic growth.

The cycles of repression and reform representing changes in material beliefs documented in the case studies in this volume also underline two other major themes of the earlier Lal–Myint (1996) comparative study. The first is the role of crises arising from past dirigisme in initiating reform (see Lal 1987). The chapters on China and India exemplify the process, whilst the excellent survey in Chapter 6 on sub-Saharan Africa’s decades-long crisis of growth shows why even an enduring long-term crisis might not lead to reform in natural resource-rich economies. Here my model of the predatory state (first outlined in Lal 1984 and incorporated in Lal 1988–2005), combined with the different paths to development in a model incorporating land along with the traditional factors of production—labor and capital—charted by Krueger (1977) and Leamer (1987), provides a theoretical framework for explaining the political economy of countries for whom natural resources become a “precious bane.” It was used by Lal–Myint (1996) to provide an explanatory framework for the changing economic policies adopted by twenty-five developing countries until the late 1980s. The Chapter 6 survey on Africa and the rather sad Chapter 14 on the deteriorating performance of the hitherto star African performer Botswana in this volume show how the continent’s natural resource abundance is still proving a precious bane, not least because of the predatory behavior of its postindependence nationalist elites (also see Lal 2004 on these problems of creating and maintaining the minimal “order” required for economic prosperity).

Finally, although not explicitly dealt with in this volume, there is

the question of whether a particular type of polity is conducive for economic development. The current political panacea is the promotion of democracy in the Third World. However, the Lal–Myint volume found no relationship between the type of polity and economic performance. In contradistinction to the technocratic economic explanation for dictatorship and democracy recently provided by Acemoglou and Robinson (2005), which I find unpersuasive, I have argued (Lal 1998, 2000b) that political habits are part of a civilization’s cosmological beliefs, determined in large part by the exigencies of the geography in the region where the civilization is born. Thus I do not see China giving up its ancient bureaucratic authoritarian political habits nor India eschewing its democratic ones.

The tragedy of Africa is that its traditional polities, based on the legitimacy of tribal chiefs, were destroyed by the colonial impact. The artificial states bequeathed to nationalist successors cut through ancient configurations and amalgamated historically opposing tribes within their borders. So, apart from intertribal conflict within their borders to garner the rents from their natural resources, they have also been threatened by claimants from “across the border.” The shining exception (as documented in Chapter 14 in this volume) is Botswana. It was fortunate that, largely because of its backwardness and seeming lack of natural resources, the British allowed it to preserve its precolonial internal autonomy and tribal chiefs. They delivered unparalleled economic growth after independence. But, as the chapter shows, the rent seeking associated with natural resources, after diamonds were discovered in the country, seems to be emerging in even this African success story.

Latin America is also a region plagued by the curse of natural resources. Given its Christian heritage, its egalitarian cosmological beliefs are in dissonance with its ecology, which generates large inequalities of income and wealth. The neo-Thomist beliefs it inherited from Spain and Portugal involve a form of fundamentalist universalism not found in its Protestant neighbor to the north. It also accounts, in my view, for the continent-wide shifts and fashions in economic policy over the last two hundred years. These swings in fashion are rather like religious conversions, while the dissonance between an unequal social reality and egalitarian cosmological beliefs has led to cycles of democratic populism followed by authoritarian repression as the distributional consequences of the populist phase are found unacceptable by the upper classes. Chile seems the

only one to have broken the cycle, while in the others—particularly in the Andean countries and Venezuela—we seem to have swung back to democratic populism, however unjustly its proponents criticize the previous decade of half-hearted liberal reforms, as Chapter 7 on Latin America in the volume ably demonstrates.

I hope this puts the essays in this book into a broader perspective. These excellent essays demonstrate how departures from classical liberalism and the ensuing atavistic suppression of the entrepreneurial instinct continue to hamper continuing economic progress in the world.

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