
NEW INSTITUTIONAL ECONOMICS: A CONCEPT PAPER

Draft
For Discussion Purposes Only

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TABLE OF CONTENTS

	PAGE
EXECUTIVE SUMMARY	i
I. INTRODUCTION	1
II. PROJECT DESCRIPTION	2
A. Perceived Problem	2
B. Project Goal	4
C. Project Purposes	4
D. Project Activities and Expected Achievements	6
E. Project Implementation	7
III. CONCLUSION	9
APPENDIX A: ELEMENTS OF A NEW INSTITUTIONALIST STRATEGY	i

**NEW INSTITUTIONAL ECONOMICS:
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EXECUTIVE SUMMARY

A. Introduction

The Bureau for Private Enterprise has proposed a \$5 million Research Project on New Institutional Economics (NIE) to begin in FY 1990. (The term "new institutional economics" is used as a "shorthand" for describing a new way of looking at economic growth in developing countries that goes beyond the realm of traditional macroeconomics to include public choice, political economy, industrial organization, and law, among other fields.) The research project will be devoted to the development of an intellectual framework that will challenge traditional approaches to economic development and promote the emergence of new ideas on the institutional and policy requirements for attaining sustainable, private sector-led economic growth. This framework will be used to support the policy dialogue agenda of A.I.D. with LDC policy makers, a key objective of which is promoting pro-growth policy reforms aimed at improving the efficiency of markets. In addition, the project will build intellectual human capital in the United States and in developing countries to support the activities of A.I.D., other international development agencies, and policy makers in the United States and in developing countries.

B. Project Goal

The major objective of the Research Project on NIE is to assist U.S. and LDC policy makers in identifying the appropriate legal, administrative, and political institutions which would promote effective functioning of markets and broad-based private enterprise, and support the policy reform process.

C. Project Purposes

The principal purposes of the project are the following:

1. Develop an Intellectual Framework

The research project aims at creating the intellectual foundations of a new development approach and building a systematic knowledge base in the United States that will be accessible to LDC officials and research organizations.

2. Mobilize Additional U.S. Academic and Technical Talent

A second purpose of the Research Project on NIE is to mobilize additional U.S. academic and technical talent in economic

development in order to build a cadre of academic "stars" and junior associates whom A.I.D. and other international development agencies can "tap" in the future in developing and implementing their policies and programs.

3. Build Network with LDC Research/Academic Organizations

A key purpose of the project is to promote development of informal networks between U.S. and LDC scholars and academics. In that sense, the project will function as a brokerage firm dealing in the development of linkages between U.S. and Third World universities and research centers, and in the promotion of collaborative research efforts.

4. Examine Transaction Costs in Comparative Perspective and Approaches for Reducing Costs

An important purpose of the project is to examine transaction costs in comparative, historical perspective and to explore approaches for reducing these costs.

D. Project Components

The principal activities or components of the Research Project on NIE include the following:

1. Research and Development

This component aims at promoting and supporting research by scholars and academics in the United States on the constraints to economic growth in developing countries. Given the broad focus of NIE and the long-list of possible research topics, the project will build on the existing body of knowledge on NIE and set a list of priority research areas in order to maximize the impact of the limited A.I.D. resources available. This research component will also include the development of new operations (pilot projects) in the field and the promotion of empirical research to validate key premises/theories of NIE.

2. Dissemination of Information

The project will encourage dissemination of information on NIE by supporting the following:

- o **Publications:** The project will support the development of a series on the state of the art of NIE and the publication of papers and articles produced under the project.
- o **Conferences (LDC-U.S. Collaboration):** The project will promote conferences with participants from the

United States and LDCs to explore research gaps and discuss the findings and propositions of research papers developed under the project.

- o Training: The project will also encourage and support education/training of LDC students in the United States.

3. Synthesis of Information/Research

To ensure that research supported by the project is policy-relevant, a key activity will be to distill the policy implications of the research for use by A.I.D., other international donor agencies, and LDC policy makers.

4. Enhance Individual Capabilities

The project will build an expanded cadre of neoinstitutionalist researchers and practitioners in the United States and in developing countries, and encourage development of Third World institutions like the Institute of Liberty and Democracy (ILD) in Peru.

5. Networking

A key component of the project will be to promote development of linkages between theoreticians and practitioners and between U.S. and Third World scholars and institutions.

6. Direct Operational Support

The project will provide technical assistance in the design and implementation of policy reform programs.

**NEW INSTITUTIONAL ECONOMICS:
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I. INTRODUCTION

The Agency for International Development's Bureau for Private Enterprise (PRE) has proposed a \$5 million Research Project on New Institutional Economics (NIE) to begin in FY 1990. The major objective is to assist U.S. and LDC policy makers in correcting the legal, political, and institutional constraints to sustained economic growth. The project is aimed at mobilizing additional U.S. academic and technical talent, and at promoting the development of linkages between U.S. and LDC institutions, scholars and practitioners. In future years, PRE is considering support for additional activities which would complement the research and networking begun under the FY 1990 project.

A.I.D.'s interest in supporting a Research Project on NIE stems from recognition that the Agency must play a role in the development of new research and ideas that can influence and lead to the development of new and more effective interdisciplinary approaches for promoting economic growth and equity in developing countries. In reviewing the effectiveness of its programs in promoting economic development, A.I.D. has tentatively concluded that:

- o Policies that encourage competitive market forces are key to attaining sustainable economic growth in LDCs.
- o Politics and institutions play a crucial role in sustaining growth-oriented policies.
- o Policies and programs of international development agencies like A.I.D., the World Bank, and the International Monetary Fund place too much emphasis on macroeconomic paradigms and fail to pay sufficient attention to institutional bottlenecks and political constraints.

As Ronald Coase has pointed out,

Until comparatively recently economists tended to devise their proposals for economic reform by comparing what is actually done with what would happen in an ideal state. Such a procedure is pointless. We can carry out the operations required to bring about the ideal state on a blackboard but they have no counterpart in real life. In the real world, to influence economic policy, we set up or abolish an agency, amend the law, change the personnel and so on: we work through institutions. The choice in economic policy is a choice of institutions. And what matters is the effects that a

modification of these institutions will actually make in the real world.

The term "New Institutional Economics" is used as a "shorthand" for describing a new way of looking at economic growth in developing countries that goes beyond the realm of traditional macroeconomics to include public choice, political economy, law, industrial organization, and other fields. The principal elements of this new institutionalist strategy and its relevance to development policy are described in Appendix A.

II. PROJECT DESCRIPTION

A. Perceived Problem

In implementing its development assistance projects, A.I.D. has confronted a series of interrelated issues that affect the potential for realizing the global aspirations for economic growth and equity through greater private sector participation in Third World economies. These include the following:

1. Importance of Growth-Oriented Policies

Failed attempts at economic development guided primarily by government planning have re-focused attention on the need to improve the efficiency and equity of markets to reverse negative trends in economic growth and to broaden participation in the economy. As the Administrator of A.I.D. has noted in his recent report, Development and the National Interest: U.S. Economic Assistance into the 21st Century, the impact of development assistance is relatively small, and economic development can really only take place if an LDC commits itself to "growth and opportunity-oriented domestic policies." Thus, even though it is necessary to shape development assistance programs in order to encourage such policies, "each sovereign state must ultimately chart its own developmental course."

2. Political and Institutional Impediments to Growth

A.I.D.'s efforts to promote private enterprise development and implement pro-growth policy reforms have been hindered by institutional barriers, including lack of protection and enforcement of property rights; high costs for establishing or expanding a business; and a gamut of other legal, regulatory, and political obstacles.

Politics and institutions play a key role in economic development through their effects on the costs of transactions which, in turn, influence the behavior of economic agents with

respect to the allocation and utilization of economic resources. When laws and institutions provide for the effective protection and enforcement of property rights and other contractual arrangements, transaction costs are low, and markets are efficient. If, on the other hand, the legal framework is inadequate, transaction costs are high and block the efficient development and operation of the market.

3. Growth of Informality/Limits to Formality

Growth of informal economies in the Third World is linked to the institutional impediments mentioned above and described so well by Hernando de Soto in his book, The Other Path: The Invisible Revolution in the Third World. The growth of informality points to the limits of economic growth arising from the high costs associated with participation in the formal economy, and from the consequent inefficiencies in scale and production techniques. The informal sector, however, insofar as it embodies the entrepreneurial energies of the poor, also points to the latent growth opportunities that might be realized if key policies and institutions are reformed.

Evidence on the magnitude of informal sector activities and their contribution to economic growth in many developing countries is still scanty at best, and no definitive methodology for measuring these activities is currently available. Yet, studies of the informal sector, like that of Hernando de Soto and his associates in Peru, reveal that some 40-50 percent of the GDP of developing countries comes from contributions made by the informal economy. The contributions of the informal sector, however, are not included in traditional measures of national income and growth, on which development projects and programs are generally based.

4. Limits of Traditional Approaches

Traditional approaches to economic development have been criticized for being too abstract and failing to deal with the "real world" problems that challenge policy makers in their attempts to promote sustainable growth policies.

This "abstractness" has often been reflected in the policies and programs of international development agencies. Critics of these programs argue that they are sometimes too theoretical, and that they ignore crucial political and institutional aspects of implementing and sustaining policy reforms. The structural adjustment programs of the International Monetary Fund and the World Bank, for example, often focus on "getting the prices right" in the short-term by adjusting exchange rates and eliminating price controls,

while paying little attention to institutional bottlenecks like ineffective legal systems or political coalition-building.

B. Project Goal

The major objective of the Research Project on NIE is to assist U.S. and LDC policy makers in identifying the appropriate legal, administrative, and political institutions which would promote effective functioning of markets and broad-based private enterprise, and support the policy reform process.

C. Project Purposes

The principal purposes of the project are described below.

1. Develop an Intellectual Framework

The Research Project on NIE is devoted to the development of an intellectual framework that will challenge traditional approaches to economic development and promote the emergence of new ideas on the institutional and policy requirements for attaining sustainable rates of economic growth. More specifically, the research project aims at creating the intellectual foundations of a new development approach and building a systematic knowledge base in the United States that will be accessible to LDC officials and research organizations. Accomplishing this mission will require:

- o Examining the need for revision of current approaches to economic development;
- o Moving development economics into the realm of political economy; and
- o Increasing the contribution of other disciplines (besides economics) such as law, history, and political science to the development field.

2. Mobilize Additional U.S. Academic and Technical Talent

A second purpose of the Research Project on NIE is to mobilize additional U.S. academic and technical talent in economic development in order to build a cadre of academic "stars" and junior associates whom A.I.D. and other international development agencies can "tap" in the future in developing their policies/programs and in implementing these policies/programs. A.I.D. believes it has a responsibility to support research by U.S. academics as well as the development of the specialized skills that are required for

development agencies to carry out their programs effectively and successfully.

3. Build Network with LDC Research/Academic Organizations

A key purpose of the project is to promote development of informal networks between U.S. and LDC scholars and academics. In this regard, the experience of the Institute of Liberty and Democracy in Peru is very valuable. Hernando de Soto and his associates at the ILD have been influenced by (and have influenced) U.S. academics and development specialists, and have established networks with U.S. universities like Washington University in St. Louis. This has contributed to the development of a program in political economy at Washington University that focuses on Third World problems, and to the development of a research program at the ILD that applies some of the concepts of NIE.

The institution selected to run this Research Project on NIE will serve as a point of contact between U.S. and Third World researchers and academics. In that sense, the project will function as a brokerage firm dealing in the development of linkages between U.S. and Third World universities and research centers, and in the promotion of collaborative research efforts.

Another important objective of the project is to build on, and profit from, the informal network that currently exists between U.S. academics and their former or current graduate students from LDCs. The purpose of establishing this U.S. - LDC network is both to guarantee Third World access to U.S. knowledge, and to develop Third World expertise. It is hoped that the local ownership of ideas that the project would facilitate will increase domestic pressures for reform and, thereby, influence the course of development policies and programs in a particular country.

4. Examine Transaction Costs in Comparative Perspective and Approaches for Reducing Costs

An important purpose of the project is to examine transaction costs in comparative, historical perspective and to explore approaches for reducing these costs. This will require development and application of a methodology for measuring transaction costs in different countries. This should lead to the development of a policy/institutional reform matrix that would "map" out the issues that need to be considered in developing a policy reform agenda.

D. Project Activities and Expected Achievements

The principal activities or components of the Research Project on NIE, and the major expected achievements of the project, include the following:

1. Research and Development

This component aims at promoting and supporting research by scholars and academics in the United States on the constraints to economic growth in developing countries. Given the broad focus of NIE and the long-list of possible research topics, the project will have to set a list of priority research areas in order to maximize the impact of the limited A.I.D. resources available.

The project will build on the existing body of knowledge on NIE. This will require an initial assessment of the state of the art in NIE and identification of key research gaps. Based on these gaps and apparent Third World needs, the project would then develop a list of priority research topics such as: the role of government in the promotion of effective development policies; the political economy of reform, and; lessons learned from economic successes/failures in particular countries.

This research component will also include the development of new operations (pilot projects) in the field and the promotion of empirical research to validate key premises/theories of NIE.

2. Dissemination of Information

The project will encourage dissemination of information on NIE by supporting the following:

- o **Publications:** The project will support the development of a series on the state of the art of NIE and the publication of papers and articles produced under the project.
- o **Conferences (LDC-U.S. Collaboration):** The project will promote conferences with participants from the United States and LDCs to explore research gaps and discuss the findings and propositions of research papers developed under the project.
- o **Training:** The project will also encourage and support short-term education/training of LDC students in the United States.

3. Synthesis of Information/Research

To ensure that research supported by the project is policy-relevant, a key activity will be to distill the policy implications of the research for use by A.I.D., other international donor agencies, and LDC policy makers.

4. Enhance Individual Capabilities

The project will enhance individual capabilities in both the United States and overseas. Two expected achievements are:

- o Building an expanded cadre of neoinstitutionalist researchers and practitioners in the United States and in developing countries, and
- o Encouraging development of Third World institutions like the Institute of Liberty and Democracy (ILD) in Peru.

5. Networking

Networking will be an essential component of the Research Project on NIE. The institution or vehicle set up to manage the project will, in collaboration with A.I.D. officials, serve as a brokerage firm linking U.S. and Third World scholars and practitioners. A key objective and expected achievement of this networking activity will be to promote development of a) linkages between theoreticians and practitioners as well as b) linkages between U.S. and Third World scholars and institutions.

6. Direct Operational Support

The project will provide technical assistance in the design and implementation of policy reform programs.

E. Project Implementation

The vehicle or institutional mechanism for implementing the Research Project on NIE has not yet been selected. A number of institutional "models" or mechanisms are being considered, including the following:

- o Washington-based "think tank": One option is to allocate A.I.D. funds through a think tank that would set up a program in NIE and attract resident and visiting fellows to the program. All of the major activities of the project, including research, dissemination of information, and networking would be administered by the think tank.

- o Establishing an A.I.D. Center for Privatization-type institution. A.I.D.'s Center for Privatization was set up by the Bureau for Private Enterprise as a "center for excellence" to provide technical assistance in privatization to AID missions worldwide. Long-term advisors are brought in to provide R&D capacity, while short-term advisors provide specific advice to USAID missions and LDCs.
- o Contracting with a consulting firm. The Private Enterprise Development Support Project (PEDS) is administered by Arthur Young, under contract with the Bureau for Private Enterprise. Under this type of arrangement, the consulting firm manages the contract for A.I.D., maintains a high level of communication with the Agency, and responds quickly and efficiently to the needs or requirements of A.I.D. and the individual academics and academic institutions involved.
- o Supporting a University Center following the "Ohio State Model". AID's Bureau for Science and Technology has supported a research program on rural financial markets and agricultural economics at Ohio State University for 15 years. A similar arrangement with this or another university might be an option.
- o Supporting a DARPA-like arrangement. DARPA is the Defense Advanced Research Projects Agency located in Rosslyn, Virginia. Its impact on the U.S. economy reportedly has been so profound that some call it "America's MITI," after the Ministry of International Trade and Industry in Japan. Officially, DARPA is charged with fostering the type of basic research that has a potentially high payoff for military applications in the future but is too far removed from the immediate agendas of the Army, Navy and Air Force to command their attention. Stealth, Star Wars and smart weapons began as DARPA research initiatives, as did advanced integrated circuits, computer graphics, computer networks and even the civilian space program. DARPA, which employs about 160 people, has been described as having "an austere management style virtually unique in the federal bureaucracy".
- o Supporting a National Bureau for Economic Research (NBER)-type model. NBER is a private, non-profit organization that supports research in five key areas: economic fluctuations, financial markets, international studies, labor studies, and taxation. Unlike the typical think tank model, NBER has no resident academics. The majority of grants are provided to individual academics

through the particular university or research institute at which he/she works. Selection of grantees is generally based on "networking," although once a year NBER holds a university research conference as an open call for papers and as a means of attracting new contributors.

- o Promoting the "Chile Model". A.I.D. provided support to the University of Chicago to promote research on market-based economic policies and models. In the 1960s, the University's Center for Latin American Economic Studies (CLAES) developed close links with the Catholic University of Chile and has had a tremendous impact on the course of economic policy in Chile. An important feature of this "model" was sponsoring graduate training of Chilean students at the University of Chicago. These Chileans were instrumental in implementing the liberalization program in Chile.
- o Building an "In-House" Capability. Another option is to mobilize the requisite human resources to institutionalize the research project within A.I.D.

Regardless of the vehicle selected for implementation of the project, a key objective of A.I.D. is to expand the sources of funding for the project by attracting foundations and other private contributors.

III. CONCLUSION

In the decades since World War II, A.I.D. has put forward many policies and programs in an attempt to promote economic growth in LDCs. Economic growth has been and continues to be the central strategy of U.S. development assistance. In the words of the Administrator, "We believed then, and we believe now, that the economic development of other nations is in our national interest. However, we also recognize that much of what has haphazardly evolved as development assistance over the past four decades has not worked, has sometimes not even been aimed at the correct objectives, and, above all, has been overtaken by events."

Policy reform and equity has been a central theme of A.I.D.'s private sector initiative. In promoting freer markets and a more active role by the private sector in the economies of Third World countries, A.I.D. has sought to expand the income-earning opportunities for the poor and to increase self-reliance. Yet, as the work of Hernando de Soto has illustrated, the institutional infrastructure in LDCs can hinder the entrepreneurial energies of the poor and curb the growth and expansion of private sector firms in the formal sector.

Development policy and assistance programs must be devised based on proposals for economic reform that recognize both the limits imposed by institutions and the realistic opportunities that a modification of these institutions will offer policy makers striving to change the course of economic development in a particular country.

The realities the Agency and other government agencies will face in the 1990s and in the 21st century demand that future U.S. government assistance programs be "radically" reshaped. As the Administrator pointed out in his report, however, "America's intellectual leadership role can be even more important than its dollar contribution to development." A key aspiration of this Research Project on NIE is to ensure that once again the United States provides the intellectual leadership required in charting new and more effective paths for promoting economic growth and equity in developing countries.

APPENDIX A

I. ELEMENTS OF A NEW INSTITUTIONALIST STRATEGY

The term "New Institutional Economics" is used to describe an interdisciplinary undertaking which examines the role of politics and institutions in economic development, and their impact on the efficiency and equity of markets. NIE goes beyond the traditional realm of macroeconomics to focus on a variety of problems and fields, including growth of the informal economy, property rights, public choice, rent-seeking, transaction costs, comparative economic history, and the political economy of reform, among others.

The principal elements of a new institutionalist strategy are the following:

1. The Informal Sector

Growth of the informal sector in LDCs is not a new phenomenon, and international donor agencies and development professionals have for many decades looked upon the informal sector as a potential source of employment and income for the poor, and have developed projects to assist the informal sector in getting access to capital, training, and technical assistance.

More recently, however, attention has shifted to focus on the causes and characteristics of informality in the context of developing economies. This shift has come about largely as a result of the work of Hernando de Soto and the Institute of Liberty and Democracy in Peru. De Soto has challenged traditional views of the informal sector as employer of last resort for the poor, and has focused instead on the entrepreneurial qualities of informality and on the impediments to participation in the formal economy.

De Soto views the choice between working formally or informally as a rational process ensuing from analysis of the relative costs and benefits of formal sector participation in the context of a highly complex and inadequate legal and regulatory environment. It follows then that the low levels of growth of the economy arise from the "high costs of formality", which result in: low productivity due to inefficient specialization; low levels of productive investment; high taxes which discourage creation and expansion of business; and disincentives to technological progress and innovation. In short, the roots of underdevelopment can be traced in large measure to government policies and institutions which raise the costs of transactions required for participation in the formal economy, and encourage exit into the informal sector.

Research on NIE can play an important role in promoting analysis of the role laws and institutions play in encouraging/discouraging

participation in the formal economy, and in discouraging/encouraging entrance into the informal economy. For A.I.D. and other international development agencies, study of the institutional framework in individual countries is fundamental to understanding the causes of informality and hence underdevelopment in A.I.D. assisted countries.

2. The Politics of Sustaining Pro-Growth Policies

In recent years, a growing number of developing countries have expressed their commitment to private sector initiatives and have recognized the importance of increasing the role of the private sector in the economy in an effort to reverse negative trends in economic growth. Yet, it is unrealistic to expect that it is only necessary to point out the impediments to growth created by these policies to bring about the necessary policy and institutional reforms. In most instances, these policies were established with very specific objectives in mind, and to address conditions that at the time the policies were crafted were seen as obstructing growth. Moreover, economic policies, laws and regulations are often designed in response to pressures from powerful interest groups ("mercantilists" as de Soto calls them), or as a result of ethnic or strategic considerations. Consequently, many LDC governments are limited by political and other considerations in what they can change and in how rapidly they can institute the reforms required for promoting and sustaining pro-growth policies.

By focusing attention on the institutional constraints to economic growth, and by supporting comparative analyses of the reform and growth strategies in different Asian, African, and Latin American countries, the Research Project on NIE can shed light on the political economy of reform, and assist A.I.D. in developing programmatic interventions in support of policy and institutional reform. As Douglass North has pointed out, because ultimately a third party must monitor the enforcement of property rights, "a theory of institutions also inevitably involves an analysis of the political structure of a society and the degree to which that political structure provides a framework of effective enforcement." Research under the project might explore such questions as how best to institute liberalization programs and how to mobilize constituencies in favor of market-driven policies.

3. Transaction Costs

Transaction cost economics is a central pillar of the New Institutional Economics. Indeed, as Oliver Williamson has pointed out, "if transaction costs are negligible, the organization of economic activity is irrelevant, since any advantages one mode of organization appears to hold over another will simply be eliminated by costless contracting." Transaction costs thus give rise to what Williamson has called the "governance structure," or firm, which enables individuals to economize on the costs of transacting.

For purposes of this research project, transaction costs may be defined as the costs of doing business in the formal sector of the economy. Because these costs are heavily influenced by the legal and institutional infrastructure that governs property rights and the exchange of these rights, transaction costs can be used as proxies to measure the costs of complying with regulations, and as a means to explore the relationship between these costs of doing business and the level of income or rate of economic growth.

Thus, in the context of international development, research on transaction costs may serve to identify differences in levels of economic growth and development among countries arising from institutional deficiencies and barriers.

4. Property Rights

Research on property rights generally has been concerned primarily with the use and function of legal property rights in economic systems. An assumption has been that these rights are protected and enforced by the prevailing body of law. In many developing countries, however, laws may be incoherent, inefficient, and may or may not be enforced. In some countries, the proliferation of often contradictory laws is also a problem arising because laws may be "purchased" by special interest groups. In this context, property owners may be forced to resort to informal contractual arrangements to protect their property rights, and entrepreneurs may be reluctant to make investments or engage in many types of "formal" market exchange.

Neoinstitutionalists have drawn attention to the importance of the institutional framework which governs the establishment and enforcement of property rights and determines the costs of transacting in the economy. Lack of protection and enforcement of property rights raises the costs of transactions and these costs, in turn, affect the allocation of resources and the efficient functioning of markets.

The implications for international economic development of this relationship between politics, property rights and transaction costs is significant. Indeed, it implies that countries which lack an adequate political and institutional infrastructure for the protection and enforcement of property rights experience high transaction costs and, therefore, poor economic performance. Conversely, countries with efficient, well-developed political and institutional frameworks have low transaction costs, and consequently higher rates of economic growth over extended periods of time.

5. Comparative Economic History

The impact of political systems and institutions on transaction

costs, property rights, and economic growth needs to be explored in a comparative historical context, and a neoinstitutionalist strategy should place considerable emphasis on the importance of promoting this type of research to validate the theoretical foundations of this new approach.

Thus far, the evidence from neoinstitutionalist economic historians like Douglass North indicates that transaction costs are central to the performance of economies, and that politics and institutions play a key role in the ability of countries to sustain adequate rates of economic growth. Indeed, the enormous discrepancies in income between the developed countries of the West and the developing countries of the Third World may be explained, to a significant extent, by the differential costs of transacting arising from differences in the political and institutional framework or "rules of the game" that govern the establishment and enforcement of property rights.

II. RELEVANCE TO DEVELOPMENT POLICY

The theoretical underpinnings of a neoinstitutionalist approach have important implications for A.I.D. and for A.I.D.'s private enterprise initiative. Increasing support of private initiative involves removing existing constraints to private sector developments such as: interest rate controls which inhibit the mobilization of savings and limit the availability of resources for productive investment; foreign exchange and price controls; and a gamut of legal and regulatory impediments to the formation, operation, and expansion of business. As a result, promotion of private initiatives requires that the Agency assess the key policy and institutional constraints to private sector investment and growth, and engage in policy dialogue with LDC governments in favor of market liberalizing reforms that will enhance the ability of private enterprises to respond to the opportunities of the open market.

A.I.D. support of research on NIE represents an important step towards the development of a better and more comprehensive understanding of the constraints to private sector-led, sustainable economic growth. Thus, this research project is potentially extremely relevant to the formulation of A.I.D. development policies and programs.