

LOCAL FOUNDATIONS FOR BETTER GOVERNANCE

A Review of Ghazala Mansuri and Vijayendra Rao's *Localizing Development*

by Roger B. Myerson, November 2014

<http://home.uchicago.edu/~rmyerson/research/locgov.pdf>

Abstract: In *Localizing Development*, Mansuri and Rao survey theory and evidence for development strategies based on local community empowerment. This note extends their theoretical argument by focusing on local government as a vital source of new leadership. Local leaders who provide better public service can prove their qualifications for higher office, but new competition from popular local leaders may be against the interests of incumbent national leaders. Thus, decentralization reforms that could benefit economic development may face powerful resistance. International assistance should promote a balanced development of local and national governments, along with a free press to monitor government at all levels. To better inform public discussions of decentralization reforms, the World Bank should actively support research on comparative subnational politics.

1. Local participatory development and political change

There are fundamental reasons to see the World Bank's report *Localizing Development*, by Ghazala Mansuri and Vijayendra Rao, as one of the most important books on development in recent years. Trade and investment for economic growth depend on basic public services and infrastructure which must be provided by government, and the quality of government is determined by political leaders who hold recognized authority in every community. When markets fail to provide gainful employment for people's talents and resources in a poor country, the market failure may be due to a government failure, which in turn may be due to a failure of civil society to hold political leaders properly accountable. Thus, successful economic development may require the strengthening of local political institutions that empower people to demand better services from their government.

In *Localizing Development*, Mansuri and Rao provide a comprehensive overview of the theory and evidence for development strategies that are based on local community empowerment. An important contribution of their book is its critical survey of the evidence on effectiveness of participatory development strategies (see particularly chapters 4-6 of Mansuri and Rao, 2013). When the goal of development assistance includes broad political change, the desired results are hard to summarize in a few quantitative measures, and comparisons that span different countries and different kinds of public goods inevitably involve a great deal of noise. Still, Mansuri and Rao find broad evidence that community involvement can improve the quality

and sustainability of public investments in several areas.

But they find that the political relationship between the center and localities matters greatly, as do the incentives of local politicians under democratic decentralization, and theory is essential to help us identify the potentially important institutional variables. Mansuri and Rao work to provide a broad theoretical framework for such analysis. In this note, I want to support and extend their theoretical argument by focusing on the role of local government as a vital source for new leadership.

2. Educating people or opening new paths for leadership?

Mansuri and Rao lay the theoretical groundwork for their analysis in chapters 1-3. They cite great social theorists going back to Jean-Jacques Rousseau and John Stuart Mill who have argued that participatory institutions of local government can be a training ground for citizenship, where people develop social values and learn how to engage constructively in democratic deliberations about public decisions. If such an active educated citizenry is the fundamental key to a successful society, then participatory exercises in collective decision-making may indeed be the best way to help a society to build the basis for strong economic development. On the other hand, when foreign development agencies sponsor ad-hoc community projects that are not integrated into the local political system, there is a danger of simply teaching some local agents how to influence the foreign development agencies.

Of course, educational programs to promote civic values may have benefits even without decentralization of power. Voters would be better able to hold elected officials responsible if students in public schools were taught how to read basic public budget reports. Public advertising campaigns could try to create norms against bribery and vote-buying. But here I want to begin shifting the focus away from participatory training exercises to the substance of local government itself.

There are good reasons to expect that responsible locally elected governments can help economic development by providing better mechanisms for local public investments. A poor community can mobilize its resources for public investments that are essential for its economic development only when members of the community are coordinated by local leaders whom they can trust to appropriately reward contributors and discipline free-riders. Such trust can be expected only from leaders whose authority is based in local politics. Local officials whose

positions depend on national political patronage are inevitably less concerned about developing trust among the residents of a small poor community. Thus, integrated efforts to achieve economic development throughout a nation may depend on a political system which admits autonomously elected local leaders into the national network of power. (Fortmann 1983 has argued persuasively for the importance of such local political institutions for rural development in Botswana.)

From this basic point about benefits of decentralization for local public investment, I want to argue more broadly that political decentralization can be a force for better governance at all levels of government by helping citizens to identify better candidates for leadership. That is, in understanding the benefits of decentralization, I would shift the focus from training better citizens to identifying better leaders.

A fundamental key to successful democratic development in a nation is to increase its supply of leaders with good reputations for using public resources responsibly. Without such trusted leadership, a nation must suffer from a lack of public services and infrastructure that are essential to prosperity. Even when the prospective returns to local public investments could be much greater than the cost that the community would have to pay for them, beneficial public investments will not be undertaken if people cannot identify anyone who can be trusted to manage valuable public resources without misappropriating them.

The problem of inducing an agent to manage public resources without misappropriating them for short-term private benefit is an example of what economic theorists call *moral hazard*. An agent who could derive great private benefits from abuse of power must be motivated to use power appropriately by an expectation of greater long-term rewards, called *moral-hazard rents*, that the agent might lose by short-term abuse of power. The essential key is that the agent must expect that he can maintain a privileged position only by good behavior. In successful societies, responsibility for public investments is given to trusted leaders who can expect to enjoy privileges of a high position in the society only if they maintain their reputation for managing public resources appropriately.

There is a serious problem, however, if nobody in a society has a reputation for managing public resources well, because then people would have no reason to replace a corrupt leader if they believed that the next leader would not be any better. On the other hand, if many individuals have reputations for good responsible leadership, then any one leader who is seen to

abuse his power can expect strong social pressure to replace him with someone who has a better reputation. (See Myerson 2006 for a simple game model of this argument.)

From this perspective, the problem of development is to create more opportunities for individuals to begin building good reputations for responsible governance. The number of such opportunities for new leadership can be most effectively increased by political decentralization which gives substantial autonomous resources and responsibilities to locally elected officials. When locally elected leaders have clear administrative and budgetary responsibility for the successes and failures of local government, then those who succeed will enlarge the nation's vital supply of popularly trusted leaders.

This reputational-leadership theory of decentralization has some logical connection to the education theory of participatory development through the issue of changing people's expectations of their political leaders, whose authority depends on popular recognition. In a nation where history has led people to expect that any political leader would maintain a corrupt patronage network that may violate laws with impunity, this low expectation is likely to be fulfilled. For successful democratic development, people must somehow come to expect better public service from those whom they will recognize as their leaders.

However, an incumbent national leader has no incentive to raise voters' expectations, and citizens have no reason to believe promises of better government from a candidate who has never exercised power. An incentive to raise expectations can be combined with the potential to do so only when voters allocate power at two or more levels of government, so that elected officials at lower levels can hope for election to higher office if they demonstrate an ability to serve the voters better. So there is good reason to expect better performance from democratic government when voters can elect responsible officials at two or more levels of government.

Thus, democratic local government can help to make national democracy more competitive, as a record of using public resources responsibly in local government can qualify a local leader to become a competitive candidate for power at higher levels of government. In effect, local democracy can reduce barriers against entry into national democratic competition. (Economists understand that barriers against new entrants can be important determinants of the level of profit-taking by suppliers in any imperfectly competitive market.) From this perspective, an ideal system of federal democracy should have several levels of sub-national governments, so that elected offices at different levels could form a ladder of democratic

political advancement that effective leaders can climb from local politics to provincial and national politics.

This leadership theory of decentralization does not say that local government will be less corrupt than national government. The point is that democratic local governments can help to make national democracy more competitive, by providing a supply of candidates who have proven their ability to manage public resources responsibly at the local level. If established national leaders were all perceived as corrupt, then voters could turn to a local leader who has developed a reputation for better public service.

Mansuri and Rao raise concerns about potential disadvantages of decentralization for one issue in development assistance: the problem of ensuring that anti-poverty programs are targeted to the poorest members. Where the neediest individuals are a minority of the community, their interest may not prevail in local democratic politics. Indeed, we may expect that, in many communities, the poorest individuals may be those who have the least ability to express their concerns effectively in organized society, and then participatory development exercises that involve the poorest might have some civic educational value. But the reputational-leadership theory of decentralization can also offer a useful perspective on this issue.

I have argued that the most important benefit of political decentralization may be that it increases the supply of leaders who have developed good reputations for efficient provision of public goods and services. This effect depends critically on what people consider to be public goods. Although donors of international development assistance may appropriately care about the alleviation of poverty for the poorest people as a global public good, within a poor community itself the not-quite-poorest residents might not consider targeting of benefits to their poorest neighbors to be a public good. In that case, democratically elected local leaders might actually enhance their reputations for good public service to their constituents by diverting poverty-assistance funds to benefit other parts of the community. Closer centralized supervision of such poverty-assistance programs may then be appropriate to the donors' concerns. But where the problem is general poverty of entire communities because of a failure by the government to supply essential public goods, then decentralizing some share of autonomous responsibility for local public goods may be beneficial.

3. Monitoring and evaluation of public spending

Mansuri and Rao correctly emphasize the importance of evaluating results of development assistance programs. Although open discussion of failures is an unpleasant and often thankless task, learning from experience is possible only by seeking honest feedback about failures as well as successes. Furthermore, when the central goal is to make demand for good government more effective by greater accountability, public reporting of failures as well as successes becomes absolutely essential to the mission.

In the reputational-leadership theory, decentralization is supposed to help create more opportunities for leaders to build reputations for good public service. So public reporting of failures is as important as successes for people to distinguish which of their leaders have better records of managing public resources responsibly. The effectiveness of public management by different leaders cannot be compared without also providing information about the budgetary resources that each had available. So international development-assistance providers should also insist on clear public accounting for all funds that are spent by political leaders at all levels. The essential accounting here must be to the local population, however, not just to foreigners who provided the funds (Ghani and Lockhart 2008). Local people must be able to learn what funds were spent by their leaders and must be able to monitor what public services were provided by these funds. In such matters, a free press has vital importance.

Mansuri and Rao find complementarities between systems of accountability at the local and national level, and they observe that decentralized government may be most effective when higher-level institutions of accountability have the capability to monitor local service providers. Indeed, one important advantage of federal separation of powers is that national law enforcement agencies can more objectively investigate allegations of corruption in local governments that are politically autonomous. International development assistance should encourage capacity-building in both national and local governments.

Strong complementarities can be found also between democratic competition at different levels. I have argued that local democracy strengthens national democratic competition as successful local leaders can become strong competitive candidates for higher offices. But national democracy can also strengthen local democratic competition, as national parties can support alternatives to established local bosses. The risk of local government being dominated by an unpopular local autocrat can be countered by the participation of competitive national

political parties in local elections. Local political bosses should know that, if they lose popular support, they could face serious challengers supported by a rival national party. Competitive national political parties played an important role in the successful introduction of local democracy in Bolivia as described by Faguet (2012). Crook and Manor (1998), Enikolopov and Zhuravskaya (2007), and Hankla et al. (2012) find cross-national evidence that the benefits of political decentralization can depend on strong competitive political parties at the national level.

But a development assistance strategy must consider where to start when accountability is weak at all levels. One may start with monitoring of local public projects at least by the international assistance organizations that are involved, with public reporting of all positive and negative results. Then, if the national political system allows proven successful local leaders to advance democratically into higher offices, the islands of better governance should spread.

Mansuri and Rao observe that, when our goal is not just investment in public goods but also political development, the outcomes need to be evaluated over the long term with respect to the nation's broad social and historical context. A few statistics are not enough. This is the broad view of journalism. In successful nations, the results of public spending are regularly evaluated in the broad social and historical context by investigative reporters of a free press. Thus a free press with strong traditions of investigative journalism may be essential for successful economic development.

4. High-level resistance against decentralization

In spite of the advantages of democratic decentralization that I have listed, there can be powerful forces against the introduction of democratic local government in nations where it has not previously existed. The potential of autonomous subnational governments to become sources of new competition for national power is itself a substantial reason why established national leaders might not want to share power with locally elected governors and mayors. Indeed, a national leader is likely to find particularly strong opposition to political decentralization among his most important supporters, those who may hope someday to be appointed to an office of mayor or governor as a highly valued reward for their political support. Any move to let local voters select their own mayors and governors would, from the perspective of these key supporters, be a disappointing diminution of their potential rewards. It is risky for any political leader to do anything that would so disappoint such important supporters.

Thus, we have basic reasons to expect that political decentralization may often be undersupplied, relative to what would be best for the general population, because it runs against the vested interests of those who hold power at the national level. Much evidence can be found to support this prediction. In Pakistan, elected politicians of national and provincial government have three times dissolved institutions of local democracy that had been created by military rulers. In Egypt, three constitutions in a row (those introduced under Sadat, under Morsi, and under Sisi) promised an eventual devolution of power to locally elected councils but then allowed the current national leaders to postpone such decentralization and continue the centralized appointment of local governors. (Myerson 2014 considers other historical examples.)

However, a constitutional system with democratic local government can become politically stable once it is established. When governors and mayors have been locally elected, they become local power-brokers from whom national politicians must regularly seek support in competition for national power. So it then would be very costly for any national leader to threaten the constitutional powers of these elected local officials.

Thus, a transition to a decentralized federal democratic system, once achieved, can be self-sustaining. International assistance organizations may appropriately aim to support a balanced development of accountable government across different levels, from municipal and provincial governments to national government. This balance could be upset by providing foreign support for political leaders only at the national level. International aid donors might better support balanced democratic development by insisting that some share of foreign assistance funds should be allocated directly to autonomously elected institutions of provincial and municipal governments.

One might argue that, to demonstrate an appropriate respect for national sovereignty, foreign supporters should only work with sovereign national governments. But the principle of channeling all development assistance through the national government can actually strengthen forces for the centralization of power, by giving national political leaders a source of funds that does not require support or acquiescence from anyone else in the country. Thus, a greater centralization of power may itself be a result of foreign support. In this case, the constitutional impact of foreign support could actually be reduced when foreign supporters press national leaders to accept more political decentralization, even as such decentralization could help achieve the goals of better governance and economic development.

5. Conclusions and recommendations

Following Mansuri and Rao, we have argued that better governance is essential for economic development, but competitive political incentives to improve governance may fail when citizens believe that any leader would abuse power corruptly. Democratic competition can be an effective force for better governance only when there is an ample supply of potential candidates who have good reputations for responsible public service. This essential supply of trusted democratic leadership can develop best in responsible institutions of democratic local government, where successful local leaders can prove their qualifications to compete for higher office. However, new competition from popular local leaders runs against the vested interests of established incumbent national leaders, and so there may be powerful internal resistance from the top against decentralization reforms even when they could benefit economic development.

Thus, we have fundamental reasons to believe that political decentralization may be undersupplied in many poor countries. When this is true, international organizations for development assistance should appropriately encourage a more balanced distribution of responsibilities and budgetary authority across different levels of government, from municipal and provincial governments to national government. Let me offer here three broad recommendations that follow from this general argument.

The first recommendation of this report is that the World Bank should consider ways to expand direct assistance to subnational governments. Provincial and municipal governments should have opportunities to finance public investments with international assistance even when the national leadership views provincial and municipal leaders as potential political rivals.

For assistance in the form of loans, a fundamental difficulty here is that the sovereign national government cannot be reasonably held as guarantor for loans which it has not authorized to its subnational governments. But if that implies that an international development-assistance organization may need to examine and certify the credit-worthiness of subnational governments, such fiscal certification itself may be an important service. (See Sargent 2012 for an eloquent discussion of the importance of the right to separate credit positions for subnational governments in the history of the United States.)

As we have discussed, social forces for better governance and development depend on a free press which can provide the information that people need to evaluate the performance of

their leaders. Thus, a second recommendation of this report is that the World Bank should consider creating an international program of multi-year fellowships for promising journalists. The mission of such World Bank journalism fellows would be to write investigative articles which provide information and analysis about the results of development projects, and which could be published in the local or international press. In any country that receives development assistance, such journalism fellows might work together in teams that could include both local and international journalists. The goals of this journalism fellowship program would be both to help people better evaluate the effectiveness of development efforts in their country, and to encourage the wider development of professional journalism throughout the world.

The third recommendation of this report is that the World Bank should actively promote more research about comparative subnational politics, collecting information about the different forms of subnational political institutions that exist in different countries around the world, and analyzing the comparative effects of different forms of subnational government on development outcomes. Such research could be important both to guide future policy-making by the World Bank and also to provide better information for public discussions of decentralization reforms. Broad public understanding of these issues may be essential for decentralization reforms to get appropriate consideration against the opposition of powerful national elites that have a vested interest in centralization. There has been some fundamental research on comparisons of local political institutions (see UCLG 2007, Ghosh 2012, Hankla et al 2012, Faguet 2014), but this is a vital area where the great research capabilities of the World Bank could make a particularly important contribution.

References

- Richard C. Crook and James Manor, *Democracy and Decentralization in South Asia and West Africa* (Cambridge U. Press, 1998).
- Ruben Enikolopov and Ekaterina Zhuravskaya, "Decentralization and political institutions," *Journal of Public Economics* 91:2261-2290 (2007).
- Jean-Paul Faguet, *Decentralization and Popular Democracy: Governance from below in Bolivia*, (U. Michigan Press, 2012).
- Jean-Paul Faguet, editor, special issue on "Decentralization and Governance," *World Development* 53(1):1-112 (January 2014).

- Louise Fortmann, "The Role of Local Institutions in Communal Area Development," (Gaborone, Botswana: Applied Research Unit, Ministry of Local Government and Lands, 1983), http://pdf.usaid.gov/pdf_docs/PNAAT392.pdf (accessed Feb 2013).
- Ashraf Ghani and Clare Lockhart, *Fixing Failed States* (Oxford U. Press, 2008).
- Sharmishtha Ghosh, "List of resources on local democracy in the developing world" (2012) <http://home.uchicago.edu/~rmyerson/research/locdemocinfo.pdf>
- Charles A. Hankla, Jorge Martinez-Vazquez, Raul A. Ponce-Rodriguez, and Eunice Heredia-Ortiz, "Rethinking the political economy of decentralization: how elections and parties shape the provision of local public goods," working paper 12-32, International Center for Public Policy, Andrew Young School, Georgia State University (2012). http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1903106
- Ghazala Mansuri and Vijayendra Rao, *Localizing Development: Does Participation Work?* (International Bank for Reconstruction and Development, 2013).
- Roger Myerson, "Federalism and incentives for success of democracy," *Quarterly Journal of Political Science* 1(1):3-23 (2006).
- Roger Myerson, "Toward a theory of leadership and state building," *Proceedings of the National Academy of Sciences USA* 108(supplement 4):21297-21301 (2011).
- Roger Myerson, "Democratic Decentralization and Economic Development", to appear in *Oxford Handbook of Africa and Economics: Context and Concepts*, edited by Justin Yifu Lin and Célestin Monga (2014).
- Thomas J. Sargent, "United States Then, Europe Now," *Journal of Political Economy* 120(1):1-40 (2012).
- United Cities and Local Governments, *Local Governments in the World: Basic Facts on 82 Selected Countries* (2007). http://www.cities-localgovernments.org/gold/upload/pocketbook_complete.pdf