# The Economic Reach of the State: African Development Reconsidered[1]

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> *Divergence in relative productivity levels and living standards is the dominant feature of modern economic history. In the last century, incomes in the "less developed" (or euphemistically, the "developing") countries have fallen far behind those in the "developed" countries, both proportionately and absolutely. I estimate that from 1870 to 1990 the ratio of per capita incomes between the richest and the poorest countries increased by roughly a factor of five and that the difference in income between the richest country and all others has increased by an order of magnitude. This divergence is the result of the very different patterns in the long-run economic performance of two sets of countries* [Pritchett, 1997, p. 3].

## I. The Problem

It is an article of faith among the development community that convergence is the natural state of affairs—that is, historical disparities in per capita incomes and living standards across the globe will disappear as the technology, the institutions, and the economic insights from the developed world make their way to the poorer countries. This conjecture underpins the commitment, following World War II, to establish the Bretton Woods organizations—the International Monetary Fund and the International Bank for Reconstruction and Development (the World Bank). Despite this general confidence, there is mounting evidence that the standard approaches to economic development in Africa have brought disappointing results [Bigsten, 2002; Easterly, 2001, 2006; Easterly and Levine, 1997; Herbst, 2000; Leonard and Straus, 2003; Ndulu and O'Connell, 1999; Pritchett, 1997; Rodrik, 2003; Sender, 1999; Tiffen, 2003; van de

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Walle, 2001]. The Washington Consensus now seems discredited [Rodrik, 2006; World Bank, 2005], and it appears that many countries in Africa will fail to meet the Millennium Development Goals by the year 2015. Several reasons are advanced for these discouraging circumstances: (1) lack of commitment by governments to implement and to persist in the development policies formulated for them; (2) unwillingness on the part of donors to advance a consistent development scenario in the face of shifting government priorities; (3) insufficient funding by donors to accomplish the desired development agenda; and (4) chronic corruption that undermines the effectiveness of even the most coherent development prescriptions.

Left unnoticed in the many reasons why development assistance has not produced better results is the possibility that development advice—the specific policy prescriptions—directed to particular nations on the African continent is predicated on an inappropriate conceptual model of the actual <u>process</u> of economic development. In other words, if past and current development activities are predicated on a flawed understanding of the reasons why many African nations seem resistant to the standard development catechism then the blame for failed development performance lies not with desultory African governments, nor with endemic corruption, nor with inappropriate institutions, nor is it the fault of inadequate funding. Rather, the fault lies with an inappropriate conceptual model that informs development policies on the continent.

With this dubious development model intact, and with little good to show for decades of development assistance, the conversation now seems to have coalesced around two new strategies: (1) the great leap forward; and (2) smart searching. The first view is associated with Jeffrey Sachs [2005, 2008], while the second is associated with William Easterly [2006]. Following Sachs requires that we are not in doubt about what is necessary and sufficient to induce self-sustaining growth and development—we must simply do more of it, and with a greater intensity of funds and technical assistance. Following Easterly also requires that we are not in doubt about the essential causal structure and implies that we need only to be more circumspect in our programmatic focus and emphasis. Easterly invokes the metaphor of the <u>searcher</u> as opposed to the <u>planner</u>.

My purpose here is to suggest that development progress in Africa is elusive not because of failed states or failed leadership. Rather, development has been elusive because of an inappropriate conceptual basis for the programs, projects, and policy prescriptions offered up as a guide to development assistance for the African continent. To anticipate my argument:

1. African development has suffered because much of the continent is characterized by what I call the <u>notional state</u>.

2. The concept of notional states must not be confused with familiar rhetoric of corruption and failed states. Rather, the <u>effective reach</u> of the African state is rationally attenuated by both historic and contemporary considerations of the benefits and costs of extending coherent governance across vast landscapes of dubious economic value;

3. The concept of the notional state is not well understood in the development community because it differs from the common conception of the state as it is known among those who offer advice to African governments. That shared <u>idea</u> of the state implicit in standard models of development is informed by familiarity with the process of nation building and the emergence of the state in Western Europe. That history entails the emergence of strong states motivated to protect valuable agricultural assets that eventually underwrote the transition—epitomized by the Industrial Revolution—to contemporary developed economies. By the $18^{th}$ century several of these strong states were in a military and financial position to colonize Africa and impose this European idea—but not the empirical reality—of the state on a very different agro-ecological asset base;

4. The imposition of this idea of the state failed to take hold in Africa because the inherent quality of the agricultural asset base could not support expansive governance across space and the gradual establishment of the <u>empirical</u> state as it has emerged in more favorable ecological and economic settings. As a result, colonialism left Africa with juridical states—boundaries on a map—with little empirical content beyond the capital city. Following independence, post-colonial governments have likewise found no <u>economic basis</u> to transform these juridical (notional) states into empirical states. The contemporary African state is optimally attenuated.

5. For development to get underway in Africa, the notional state must first be transformed into a functional empirical reality whose writ and obligations encompass the entire spatial extent of existing juridical domains.

6. The <u>tax bargain</u> is the necessary institutional innovation by which the notional state can be transformed into the empirical state. The tax bargain will cause capital city-focused governments to pay attention to the needs of the non-urban citizenry, and it will induce these disenfranchised citizens to identify with the governance structures and processes that can bring improvements in their economic and social circumstances.

## II. The Economic Rationale of the Notional State

> *…ecological conditions throughout most of the [African] continent do not allow high densities of people to be easily supported. More than 50 percent of Africa has inadequate rainfall; indeed, contrary to the popular imagination, only 8 percent of the continent has a tropical climate. Approximately one third of the world's arid land is in Africa* [Herbst, 2000, pp. 11-12].

It requires little imagination to acknowledge that the development and evolution of systems of material provisioning—both local economies and national economies—are largely pre-ordained by the agro-ecological settings and circumstances in which a people are situated. We may think of these settings and circumstances as the resource set, or the asset base, that underwrites future material progress. Central aspects of this resource set include climate, weather, soils, rainfall, solar energy, and wind. It is from within this complex of circumstances that people set about to feed and clothe themselves. And it is from this physical endowment that future technical and institutional change enables the gradual augmentation of provisioning. These ecological conditions do <u>not</u> pre-ordain any particular future material provisioning—the conditions merely make possible certain materialist strategies, while precluding others. Equally important, political structures and the governance arrangements co-evolve with the livelihood strategies in particular agro-ecological circumstances. These processes can be understood in the context of an economic model that provides an explanation of two kinds of states—the operational (empirical) state and the notional (juridical) state.

Consider a stylized von Thünen featureless plane. This plane is situated in a rich and bounteous agro-ecological setting typical of Western Europe. On this promising plane there are two central places—call them "seats of government." These two capital cities are separated by a large distance, yet the demarcation of the exact national boundary between the two is of little moment to the residents of the expansive territory between the two capitals. The ability of the government of each capital city to exercise dominion over this intervening terrain depends on the costs of doing so. The willingness of the government in this regard entails the weighing of the benefits and costs of extending governance across space. Dominion entails the provision of certain goods and services—construction and maintenance of communication infrastructure, provision of certain public services (schools, utilities, defense against outsiders), and a legal structure that acknowledges and enforces various property regimes, contracts, and judicial protections.

Now imagine a second featureless plane situated in an extremely arid and meager setting. Unlike the above agro-ecological circumstances, here soils are shallow, acidic, and of poor structure. Rainfall is minimal, and a decent living is quite difficult to achieve. As above, consider two different capital cities situated at some distance from each other in this relatively unfavorable environment. Assume von Thünen rent gradients emanating out from these two capital cities in the quite unfavorable setting. If these rent gradients are plotted on the same axes as above, and if the two capital cities are again placed at opposite ends of a horizontal axis, we could create Figure 1.

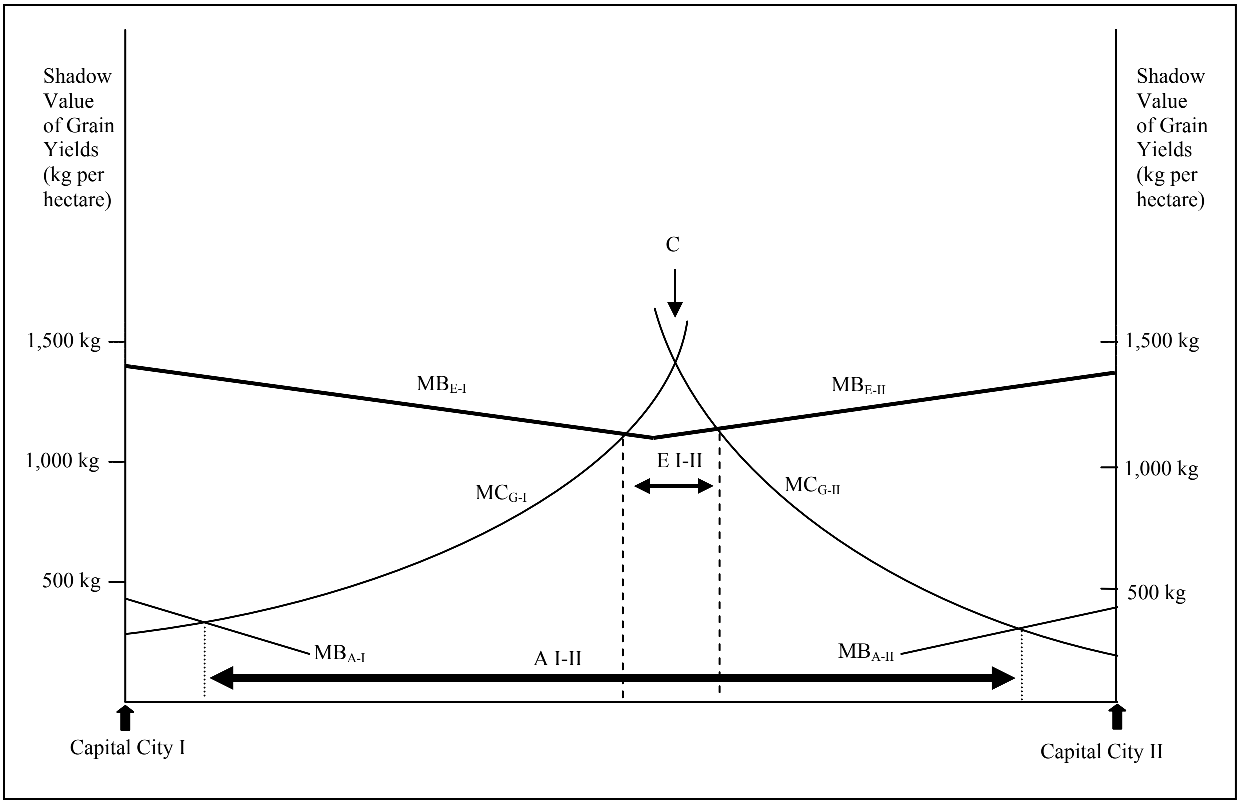


Figure 1. The Economic Limits of the State

Assume that the per-unit costs of delivering a bundle of goods and services to individuals across this rather inhospitable space do not differ materially from the per-unit costs of the same bundle in the more favorable environment. This allows us to consider a common set of marginal cost curves for the provision of governance in both ecological circumstances. The pertinent difference between the two featureless planes resides in the natural fertility and bounty of the first plane, and the stark impecunious prospects offered by the second. In Figure 1 we see that the first-approximation of the boundary between the two governance regimes is where the marginal costs to each regime are brought into equality (point C).

However, as suggested above, the interest of each capital in providing governance across this space must also be understood to depend upon the perceived benefits of doing so. Reference to both the benefits and costs of governance across space reminds us that at some distance from the capital city the extension of dominion across space becomes economically infeasible. Consider the point at which the <u>marginal benefits</u> of dominion for each capital city equal the <u>marginal costs</u> of delivering the goods and services that must accompany that dominion. It is here that the rent gradient emanating out from each capital city intersects the two marginal cost curves ($MC_{G\text{-}I}$ and $MC_{G\text{-}II}$). Notice that the two rent gradients for region A (Africa) lie considerably below those for region E (Europe), and that they decline more quickly as one moves away from one capital city and out into the hinterland.

For the more favored natural environment the distance *E I-II* is a region between the two regimes where it is uneconomic for either capital city to consider the extension of dominion a compelling proposition. While a boundary will indeed be arrived at, this area is unlikely to be seriously courted—except as a buffer. In European history these regions were known as the "marches" and were watched with considerable interest by those on both sides of the boundary. The "Marcher Lords" (Earls or Counts) were often the most trusted agents of the King's realm. However, in the less-favored environment, this region of little appeal to a central government is much greater in extent. In Figure 1 the region denoted as *A I-II* encompasses a much great proportion of the territory between capital cities in the less favorable environment. The minimal wealth of the countryside holds little interest for either government.

Figure 1 reveals the economic limits of the state in two different agro-ecological settings. Where natural assets are economically promising there is obvious advantage in controlling those valuable spaces and extending governance over them. On the contrary, where natural assets are relatively worthless there is little interest in those spaces. The implications to be drawn from this model of the economic reach of the state are especially pertinent to the discussion of the contemporary state in Africa. In the 18th and 19th centuries, while most European nations were engaged in diplomacy and armed warfare over the geographic extent of their city-states—Rome, Paris, Berlin, London, Moscow, Vienna—some of them were also projecting political and military rule over Africa. For the most part, this interest in Africa was driven by a desire for the natural resources that could be extracted and sold on world markets, or shipped to Europe for domestic use. Copper, gold, diamonds, timber, and a few crops (cotton, tea, coffee, tobacco) were the objects of greatest interest. However, throughout much of this time slaves were the dominant export [Maddison, 2007].

After World War II, when European nations lost interest in Africa, the new African governments inherited a tradition of governance that reflected the attenuated spatial reach of the state—and its governance—as depicted in Figure 1. The stark differences between Europe and Africa in the inherent quality of the natural landscape explain these different governance strategies. Europe had a bounteous asset base worth fighting over and controlling, while the material circumstances in Africa represented vast domains largely devoid of compelling economic potential. European states grew strong in the 18th and 19th centuries because they had to be. African states in these years were weak because they had no reason to be strong. And so, at independence, African political structures and processes were centered on the capital cities and, nearly five decades later, remain that way. African states were (and are) weak because, unlike those in Europe, they have never had compelling reasons to be strong. The state in Africa is a notional state. Individuals scattered across the meager landscapes of Africa are not the subjects of the governments in charge of the notional state. They are merely there—behind the mask of citizenship. Leonard and Straus [2003] argue that Africa's political problems are the result of "personal rule." I suggest that the "mask of citizenship" is a more fitting descriptor.

## III. The Development Challenge in a Notional State

The challenge to received development theory and practice is seen in comparing the asset-centric logic of the empirical state in Western Europe with the city-centric logic of the notional state in Africa [Jackson and Rosberg, 1982]. These two distinct logics—and histories—are central to how economic development has played out in the two places. The first task here is to understand how a "theory" of economic development derived from one of these logics (and historic processes) has then been deployed over the past six decades to justify specific development programs and projects in circumstances that differ so profoundly from those that provided the particularistic empirical basis for that received theory. The agro-ecological settings and circumstances from Western Europe have given rise to particularistic political and economic arrangements that reinforced the extraordinary importance of investing in and controlling land, both in specific locations as well as across relatively favorable locations. This location-specific capital deepening then provided the economic foundation of the modern European nation-state. And the institutional arrangements associated with that gradually enhanced asset, including the fiscal bargain between owners and the state, provided a governance structure that bound scattered populations to their government. The result is what we call the empirical state.

That is, these favorable agro-ecological settings gradually gave rise to an economy based on sedentary agriculture predicated on familiar Ricardian quality differentials. Coincident with this emergence of a particular agricultural economy there evolved the need for correlated political arrangements dedicated to the protection of that augmented asset base with its embodied (sunk) capital, and its politically "attached"—through elaborate land-centered property rights arrangements—labor and management of the "owner." We call the end product of this evolutionary process <u>capitalist agriculture</u>. It is capitalist agriculture because one person (or one family) was granted ownership over a specific parcel of this increasingly valuable asset base, and that owner was then free to contract with the large number of those who did <u>not</u> own land in order to bring their labor power to bear on the landed estate of the capitalist. The asset base explains the evolution of a particular ownership structure, and that ownership structure explains the evolution of the associated political and economic structures.

Notice that from this quite specific constellation of ecological, economic, and political circumstances, gradually forming the conditions upon which powerful nation-states might arise, economists have gradually built up a theory of the idea of economic development. If a country wishes for development it must replicate the process as we have interpreted it from Western Europe—a process then replicated in other places (Southeast Asia comes to mind) that also possess, thanks to abundant water, favorable agro-ecological circumstances. This shared understanding of the processes by which the various nations of Western Europe evolved into modern industrial powers has underwritten the crafting of a theory of what others must do if they wish for a prosperous future. Such is the theory of economic development.

Peter Timmer [1990] has summarized the received theory of development, which—if not explicit in every Poverty Reduction Strategy Paper—is implicit therein. In the first stage emphasis must be placed on ridding the economy of distortions, on encouraging technical change, on the nurturing of markets for the movement of factors of production and the resulting outputs, and a major commitment must be made to improvements in rural infrastructure. A second stage sees the agricultural sector becoming more closely linked with the urban (industrial and service) economy, there is continuing pressure to improve technology in agriculture, and emphasis must be put on improving factor markets to mobilize rural resources. The third stage finds agriculture rather completely integrated with the emerging industrial sector. Urban consumers find that the share of their income devoted to food starts to fall—thereby freeing up disposable incomes for other urban investments. The pressure on agriculture to become even more efficient induces further replacement of labor with machinery, thus freeing rural labor to migrate to urban centers—providing a willing army of workers prepared to work at low wages. If rural incomes start to lag then some political remediation may be necessary. The journey is complete when agriculture eventually becomes a minor source of labor income. While agriculture may come to be a dominant engine of foreign exchange, it soon comprises a small part of total GNP. Notice that there is no timeline associated with this process. In some countries it has taken centuries. In Japan and Korea, where the U.S. was forcing the process in the wake of war, it seems to have been accomplished in a generation or two. John Mellor summarized this process by saying that:

> Economic development is a process by which an economy is transformed from one that is dominantly rural and agricultural to one that is dominantly urban, industrial, and service-oriented in composition. The objectives of the process can be usefully categorized as increased social wealth, equity, and stability. But because these objectives require a diversification of the economy away from agriculture (no high-income, equitable, stable nations have agriculture as their dominant activity), the process is one of major structural transformation [Mellor, 1990, p. 70].

The question worth asking, especially with reference to Africa, is whether or not this development model is a universal prescriptive law. If it is indeed a universal law of what development entails, and of how to bring it about, then the <u>great leap forward</u> of Jeff Sachs or the <u>careful searching</u> of Bill Easterly may yet turn out to be the correct recipe for Africa. On the other hand, if the historic settings and circumstances of Western Europe are the empirical basis for a highly particularistic understanding of economic development (and how to induce it), and if the settings and circumstances into which that derived theory is now deployed in the service of replicating that quite specific empirical account differ substantially from the circumstances that underwrite that theory, a development strategy entailing "more of the same"—even if accompanied by more money, or even if applied more cleverly—is doomed to failure. To make the point in a different way, if the logic and processes spelled out by Timmer and Mellor are nothing but a recapitulation of the historic pattern followed in Western Europe and a few other places sharing favorable agro-ecological circumstances then the applicability of that process for Africa—with a vastly different asset base and associated governance logic—is problematic.

Indeed, the model showing the implications of vastly different agro-ecological circumstances in Africa from those in Western Europe during the emergence of strong states offers an opening to challenge the idea that there is but one universally applicable theory of development. Specifically, differences in the inherent quality of the asset base as between Western Europe and Africa offer a plausible explanation of the quite different structure of land ownership in the two settings. With this model in hand we can begin to see the flaw in many policy recommendations concerning property regimes. Indeed, most alleged "explanations" of these different institutional arrangements appeal to nothing more substantive than claimed "primitive" property rights that are both the result of, and the cause of, poverty. From there it is a specious leap to suggest that the property institutions must be altered in order to solve poverty.

The model offered here situates the emergence and evolution of property regimes, economic strategies, and governance in an agro-ecological context that invites reflection on economic reasons for what we observe out on the ground. To the extent that observed governance structures and institutional arrangements are the evolutionary entailment of these quite particular agro-ecological circumstances, development prescriptions urging the "modernization" of those particular institutional arrangements are logically flawed [Bromley, 1991, 2008a, 2008b; Larson and Bromley, 1990; Lund, 2000; Migot-Adholla, et al. 1991; Ouedraogo, et al., 1996; Place and Hazell, 1993; Platteau, 1996; Sjaastad and Bromley, 1997, 2000]. Notice that if particular economic and social circumstances are not plausibly responsible for certain unwanted outcomes then policies that alter those circumstances are perverse in the extreme.

Moving to the political realm, the nature and quality of the agricultural assets in Africa suggest profound differences in the logic and spatial extent of governance. Moreover, when the asset base to which capital and labor is to be applied is of a kind that little lasting good can be realized from that investment, even the most committed improving landlord will adopt a different provisioning strategy. It will soon become evident that investing additional capital and labor in a specific parcel of land is not a feasible economic undertaking. Other things become evident as well. Extensive military efforts to prevent others colonizing a decidedly indifferent natural asset base seem not worth the cost. And so, with the recent exception of a few border struggles in the Horn of Africa, the continent throughout its history has been free of military campaigns by one country to expropriate the territory of another. The contrast with Western Europe is striking.

This also means that efforts by governments to extract taxes from individuals scattered across the meager landscape are generally not worth the trouble. In the absence of a serious commitment to particular parcels of land, and given the inability to raise much public revenue from those in control of these indifferent parcels, those who rule over these great spaces at the extensive margin find that they are unable to mobilize the means to defend such assets against others. Luckily, the indifferent quality—and minimal economic value—of the landed estate renders those assets unattractive to others, and therefore expensive operations to acquire them are largely fruitless. Why fight over asset that have so little economic value? Land in much of Africa is not worth the trouble to acquire, nor is it worth the trouble to defend should others—for non-economic reasons—decide to expropriate it from those now in possession. Much land in Africa is an asset of dubious distinction.

Note that these circumstances have given rise to economic strategies that place great value in mobility across space. We see a mixed agricultural economy—small-scale crop production, some livestock rearing, and a correlated commitment to the cultivation of social networks near and far. Second, this extensification strategy leads to the evolution of political arrangements and governance structures that are supportive of a broad-spectrum survival program. For example, property regimes differ profoundly from those that evolved in Western Europe [Baland and Platteau, 1996; Bromley, 1991; Sjaastad and Bromley, 1997, 2000]. Third, as above, seeing no need to be regional military powers many African states are weak in comparison to states elsewhere in the world. African states are relatively weak because they have not had to be strong.

Consider the contrast with what we know of Western Europe.

> …starting in the fifteenth century in Italy and later elsewhere, population densities increased…[and] European nations began to compete for territory, a tendency that only makes sense if population densities are relatively high and vacant land is limited or nonexistent… In turn, there was significant pressure to strengthen states in order to fight wars….Because European states were forged with iron and blood, it was critical for the capital to physically control its hinterland….Successful European state development was therefore characterized by profound links between the cities—the core political areas—and the surrounding territories. Indeed, the growth of states was closely correlated with the development of significant urban areas [Herbst, 2000, pp. 13-14].

Herbst goes on to point out that it was not until 1975 that Africa recorded the sort of population densities common in Europe in 1500. In Africa the current states were created long before many of the capital cities had developed beyond large towns. The Europeans, in their African colonizing, relied on urban areas but the majority of these were on the coasts where they served the interests of the colonial power rather than those in the rural interior. Herbst continues:

> Due to low population densities and the large amount of open land in Africa, wars of territorial conquest…have seldom been a significant aspect of the continent's history. In precolonial Africa, the primary object of warfare…was to capture people and treasure, not land which was available to all….African leaders mainly exploited people outside their own polity because the point of war was to take women, cattle, and slaves. Thus the slave trade, especially in the eighteenth century, should be seen as part of the process by which African states grew: by capturing people rather than by gaining control over territory [Herbst, 2000, pp. 20-21].

With political and economic relations plausibly derivative of the underlying economic assets, it seems reasonable that a land-centric survival program would give rise to an emphasis on continual investments for the purpose of increasing the quantity and quality of labor and capital applied to particular parcels of Ricardian space in order to enhance the economic surplus. However, if the inherent asset base is poor, and only grudgingly yields payoff from investments in technology and agricultural know-how then other economic strategies will recommend themselves. It soon becomes evident that investing in specific parcels of land is a less rational economic strategy than investing in those activities that enhance economic prospects when it is necessary to move about.

The paradox is complete. Desultory agro-ecological settings and circumstances in Africa have given rise to a household economic program that rewards extensification (mobility) over intensification (stationarity). The minimal economic value attributable to land offers a reason why African governments have had little reason to show much interest in the hinterland. And by showing little interest in the impecunious hinterland there is no reason for African governments to expect those individuals scattered across such vast spaces to hold the national government in much esteem. The economic estrangement is reciprocal. Those far from the center get nothing from the central government, and they give little to it. And the center, getting little in the way of tangible benefit from occupants of the hinterland find few good reasons to pay them any attention. It is here that the mask of citizenship offers a clearer idea of the problem than the appeal to "personal rule." If we anchor Africa's development problems on the predominance of personal rule it conjures up the traditional images of tribalism, payoffs, and corruption. This avenue suggests that African culture must be destroyed or reformed before development can get underway.

On the other hand, if we understand the economic origins of the mask of citizenship it shifts the reasons for observed governance arrangements away from some allegedly-defective African cultural trait and situates those reasons in the realm of economics and the "rationally attenuated" (notional) state. This is a much more promising basis for the necessary political reforms that can begin to underpin much-needed economic reforms. The pertinent question then becomes: What can be done in such circumstances to create the conditions in which economic progress is possible? A necessary condition for economic advancement in Africa therefore is to create the foundations of what I shall call the <u>tax bargain</u>. Until the widely scattered peoples of Africa are "stitched" together in an effective <u>relational contract</u> with their government, all of the standard development prescriptions, projects, and programs will not—and cannot—succeed. The tax bargain is not sufficient to induce development in Africa. I do however, suggest that it is necessary.

## V. The Tax Bargain

> *There is a long history of the idea that there is some strong, consistent connection between the ways in which governments are financed and the ways in which they govern….There is also a more theoretical tradition of academic work that links long-term changes in society and governance to changes in the ways in which states obtain the*

> *resources they need to govern. Its leading exponents also see close affinities between the dependence of governments on general taxation, modern capitalism, and liberal democracy* [Moore, 2007, p. 80].

Moore elaborates the above idea by suggesting that "Dependence on general taxation provides incentives for state elites and taxpayers to resolve their differences through bargaining [Moore, 2007, p. 84]." On the contrary, when governments in developing countries do not rely on <u>general</u> taxation, but instead derive their necessary revenues from: (1) export or import taxes; (2) surpluses arising from monopoly (state) control of agricultural surpluses; (3) surpluses arising from trade in consumer goods; (4) surpluses from state property; or (5) from the export of natural resources such as oil, timber, fish, or minerals, those governments have little need to engage the larger citizenry in the business of governance. The tax bargain must be understood as an essential aspect of governance and hence of development.

The core idea behind the tax bargain is that all governments and their citizens necessarily engage in continual "bargaining" over the control of financial resources. Individuals earn incomes from those economic activities that are sanctioned by the state. The state, in its commitments to such collective consumption goods as roads, rail lines, general communications networks, the judicial system, police, and what is now called "the rule of law" requires financial resources to deliver those goods and services. Citizens need the services of government and the government needs to make sure that citizens are satisfied with the delivery of goods and services so that the required resources continue to be forthcoming. Parliaments are the locus of this bargaining. Some interests wish for less government and lower taxes while others see a more expansive role for government which implies higher taxes. The nation-state is a domain of redistribution and much of that redistributive debate centers on this issue.

In most states, with taxation falling on individuals in the form of annual assessments against income and/or wealth, there is a mutuality of interests. Improving economic conditions across the political landscape bring benefits to individuals and households, and those improving conditions then yield greater revenue to the government. The underlying incentives, therefore, induce both parties to the tax bargain—politicians and citizens—to support policies that will encourage growth. Of course their common interests diverge over the taxes that will be levied against the individual (household) gains from that growth. However, the dominant incentive lies in the direction of increasing the private income position of the individual or household and then arguing about what share of that new increment will be taxed away. Notice that when taxes are <u>not</u> levied as a share of personal income and wealth the mutuality of interests is sundered. In the absence of this key nexus, political elites lack a commitment to economic prosperity among the general population and will focus their attention instead on other means by which they might benefit financially—even though the nation as a whole is not doing well. It is here that the concern for corruption emerges.

A second incentive property of the tax bargain is that when the provision of goods and services is supported from general tax revenues—as opposed to import or export taxes—there is constant pressure on the government to improve the efficacy with which it delivers those goods and services. If the citizens are paying taxes directly tied to the expected delivery of a bundle of goods and services they are likely to be more demanding of government to make sure that it is acting in accord with those expectations.

Third, this aspect also serves to draw citizens more directly into the broader political arena to make them more involved across a wide range of issues. We see that the tax bargain is really part of the broader <u>citizenship bargain</u>. In other words, making citizens "pay" brings them more directly into the broader arena of governance and political attentiveness. It is to be expected that the degree of government accountability will increase. Of course, in much of Africa the political elite are often quite satisfied to be insulated from the demands of the citizenry. If their economic interests can be met by import and export taxes they do not need to devote much attention to the concerns of those thinly scattered across the rural hinterland. The tax bargain works to render political and economic estrangement less acceptable.

The idea that to get development launched in Africa requires the imposition of a general tax on those living at the extensive margin, and exceedingly poor, seems counter-intuitive. But consider Figure 2. Here we see the classic von Thünen model with three regions: (1) urban; (2) peri-urban, and (2) rural.

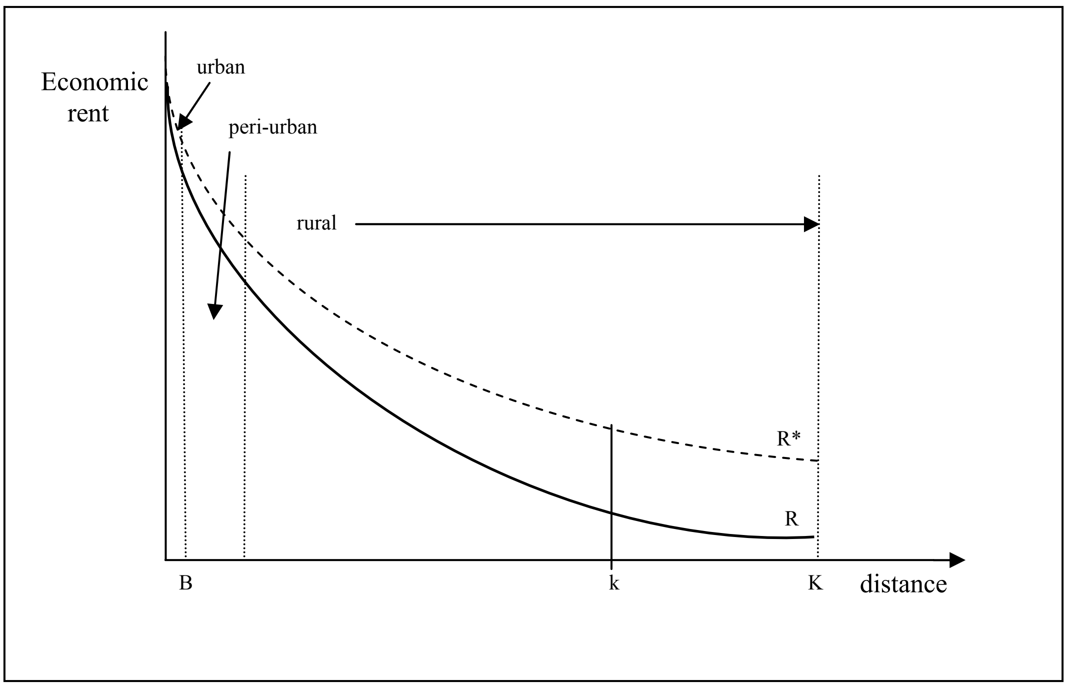


Figure 2. Actual and the Counterfactual Rent Gradients

Consider the rent gradient *R*. We may think of this as the rent gradient under the present situation in much of Africa where the central government is largely absent out in the hinterland.

Under these conditions there are few government services, there is little legal presence, transport is poor and insecure, and communication is difficult. The central government is largely missing. In such circumstances the economy operates in a "state of nature" where transaction costs—the costs of gaining information about market opportunities, the costs of contracting, and the costs of enforcing bargains and contracts—are high enough to stifle most all entrepreneurial activity [Kronman, 1985; Bromley and Chavas, 1989].

Consider, however, a counter-factual rent gradient $R^*$. This shadow gradient reflects an institutional situation in which transportation systems are safe and reliable, communication systems are ubiquitous and affordable, legal services are present and trustworthy, and credit and product markets are ubiquitous and work with considerable efficiency. In other words, there is a general presence of what we might consider to be good governance out on the ground. The point of considering this counter-factual gradient is to permit a discussion of what it might be worth for those in rural Africa to enjoy much the same level of government services, indeed governance, as that enjoyed in many other rural areas throughout the developing world. This consideration will be necessary because it will help to leverage a serious discussion about a gradual introduction of the tax bargain into a domain where it now does not exist.

The rent gradient $R^*$ in Figure 2 depicts the <u>rent possibilities frontier</u> under a governance counterfactual. While $R^*$ is simply one of a family of possible gradients, we may consider it an idealized gradient depicting the net income possibilities of rural producers under the assumption of complete and well-specified institutional arrangements concerning the movement, contracting over, and disposition of traded goods from the rural economy. It also captures the idea of "good governance" out on the ground. As above, economic development in the hinterland is stifled because high transactions costs dissipate the possible gains from efforts to improve agricultural productivity [Bromley, 2008a; Bromley and Chavas, 1989]. This rent possibilities frontier shows the plausible gains from coherent governance.

Let $\varphi_k$ depict the extent to which the current <u>net</u> income potential of a unit of land is reduced by the absence of coherent governance at distance *k* from the capital city, where:

$$0 \leq \varphi_k < 1 \tag{1}$$

When $\varphi_k \approx 0$ the income potential of a unit of land approaches that possible under an idealized governance regime offering a bundle of goods and services designed to encourage and support investment and entrepreneurial activity, not defeat such activity. On the other hand, if the current governance situation in the hinterland is deleterious then $\varphi_k \approx 1$ and the current rent gradient *R* is pertinent. Write the net rent available from a hectare of land at point *k* as:

$$R = Q[(p_t - \varphi_k) - TC] - Qck \tag{2}$$

where *Q* is the average yield of a hectare of land at *k*, $p_t$ is the sale price of that unit of produce in the urban center, $\varphi_k$ is an index of the depreciation caused by the absence of good governance at point *k*, *TC* is the average total and variable cost of producing a unit of *Q* at point *k*, *c* is the transport costs per unit of *Q* per unit of distance from the urban center, and *k* is distance from the urban center. Notice that when $\varphi_k = 0$ equation (2) reduces to the counterfactual <u>rent possibilities gradient</u> (*R** in Figure 2), but that when $\varphi_k$ takes on values greater than zero then the inferior gradient *R* becomes a plausible depiction of the situation on the ground in much of Africa.

We see that $\varphi_k$ can be thought of as a measure of the private opportunity cost to the individual at point *k* made necessary by operating under a governance regime that approaches a state of nature. Indeed, we may think of $\varphi_k$ as an index of the private willingness to pay of an individual at $k$ to be able to undertake economic activity in a regime of coherent governance. If we imagine a large number of individuals ($N$) seeking to make a living situated $k$ units from the capital city, then equation (3)

$$\sum_{i=1}^{N} \varphi_{i,k} \tag{3}$$

is an indexed transformation of the aggregate willingness to pay on the part of all individuals located at distance $k$ from the central city to engage in economic activity parameterized by a regime of good governance. If we want to think of this willingness to pay encompassing all individuals beyond the boundary ($B$) of the urban center, and extending to the national frontier ($K$) then equation (4) is of interest.

$$\sum_{i=1}^{N} \sum_{k=B}^{K} \varphi_{i,k} \tag{4}$$

We see that the tax bargain must not be allowed to suggest that individuals out in the hinterlands are being asked to pay for something that will not benefit them. Indeed, the key here is that rural residents can realize important net income gains by a well-instituted general tax regime in which small increments of taxes on income and wealth are rewarded by gradually increasing increments of a collective consumption good I call <u>coherent governance</u>. The obvious question is how to induce individuals to submit to taxation in exchange for an expectation that it would be possible to realize the rent possibilities frontier. This exchange can be leveraged by considering a voting model in which the central government is forced to compete for votes from residents of the three jurisdictions in Figure 2—urban, peri-urban, and rural. With the government seeking votes and promising a package of <u>governance services</u>, rural residents would be able to reward and punish the central government. A multi-jurisdiction voting model offers insights into this process [Gupta, 2001].

Consider Figure 2 with its three political and fiscal jurisdictions—*u*, *p*, and *r*. Assume there is but a single individual in each jurisdiction. These individuals are assumed to be identical and they cannot move to either of the other jurisdictions in search of a better bundle of public goods. The urban jurisdiction (*u*) contains the central government, financial and commercial services, but no agriculture. The peri-urban jurisdiction (*p*) contains only food production destined for the urban market, while the rural jurisdiction (*r*) contains only livestock production destined for the peri-urban and urban jurisdictions. That is, goods produced in *p* and *r* are consumed locally or transported into the urban jurisdiction. No goods from *u* flow to *p* or *r*, and no goods from *p* flow to *r*.

If the central government is to levy taxes it must also deliver a certain bundle of goods and services to citizens in the three jurisdictions. That is, the central government must compete for support against a contender, and the winner will be the party that can gain the support of two of the three jurisdictions. Assume that each of the three jurisdictions has a local government which seeks to maximize the welfare of its single resident. We can write the utility of a representative individual in jurisdiction $i$ ($i = u, p, r$) as:

$$U(x,l) + b(g_i) + B(G) \tag{5}$$

where $x$ is the private good (a numeraire) that is consumed, $l$ is the amount of leisure enjoyed by an individual, $g_i$ is the local public good provided in jurisdiction $i$, and $G$ is the central government's public good. All three functions are increasing and concave throughout. The budget constraint facing an individual is

$$x = (\omega - \tau)(1 - l) \tag{6}$$

where $\omega$ is the wage rate, and $\tau$ the tax on labor. This tax on labor is given by $\tau = t + T$, where $t$ is the local jurisdiction's tax, and $T$ is the tax levied by the central government. This central tax rate is equal across all three jurisdictions. Time available to the individual is normalized at 1 giving the utility maximizing level of leisure available to individuals as a function of the net wage rate $l = l(\omega - \tau)$ and the indirect utility function

$$V(\omega - \tau) + b(g_i) + B(G) \tag{7}$$

The production of goods follows $Y = c_3[(1-l)]^{\delta}$ where $c_3$ and δ are parameters, with 0 < δ <1 assuring diminishing returns. This output can be used interchangeably to produce the centrally provided public good, the locally provided public good, or the private good. The marginal rates of substitution across all possibilities are normalized at unity. Competition in the economy assures that the wage rate ($\omega$) is given by the marginal productivity condition

$$\omega = c_3\delta[1 - l(\omega - \tau)]^{\delta - 1} \tag{8}$$

Assume that the government is able to levy a tax on all economic rents—in this case it would be the surplus over and above the wage bill. This revenue is used by the central government to provide G, or it is distributed to local governments to provide $g_i$, or it is returned to individuals as a private good in the form of a wage subsidy. The profit in a typical jurisdiction that is taxed away is given by

$$\pi(\tau) = Y(l(\omega(\tau) - \tau)) - \omega(\tau)[1 - l(\omega(\tau) - \tau)] \tag{9}$$

The central government obtains tax proceeds from individuals in each jurisdiction and the government provides public or private goods to individuals in those jurisdictions. Notice that the mask of citizenship can be lifted only if individuals in each jurisdiction have the ability to express satisfaction—or to withhold that expression—with respect to the performance of the central government in providing the local public goods. We see that the introduction of a tax on income introduces new incentives on the part of citizens to reward or punish the central government. Consider the central government's re-election prospects to depend on a typical individual's level of satisfaction ($V(\cdot)$) compared to that individual's expected satisfaction under an alternative government ($\underline{V}$). Think of this as the individual's reservation utility under a rival political leader. The individual in jurisdiction *i* is satisfied with the central government and votes for it to remain in office if and only if

$$V(\cdot) > \underline{V} \tag{10}$$

The central government must win two of the three jurisdictions in order to remain in office. This requirement induces the central government to concentrate on those issues regarded as important by citizens in the three jurisdictions. Unlike the arrangement in many African countries in which the central government is focused on its urban-based governing allies and ignores the remainder of the citizenry, the tax bargain brings with it a strong incentive to pay attention to citizens out in the hinterland. In the absence of the tax bargain, the notional state remains exclusively focused on the urban political elite—and on revenue sources consisting largely of primary commodity exports.

Despite the unitary structure suggested in this tax/voting model, all nations have other units of government. However, often these entities are mere regional extensions of the central government. Such local governments rarely have taxing authority, with perhaps the exception of fees or royalties on certain commodities that might originate in the region. Indeed this fiscal arrangement often works as an inducement for local governments to promote the extraction of natural resources—it is their sole source of revenue apart from grants from the central government.

In the unitary structure modeled here, the central government must decide on the optimal tax rate $\tau_U$ and on the amount of local public good to be awarded to a favored jurisdiction $g_{Uf}$. The local public good to a particular jurisdiction is confined to that jurisdiction, thus ruling out spillovers and spill-ins. Once the center decides on $\tau_U$ and $g_{Uf}$, it is able to determine the level of the nationwide public good $G_U$ on the basis of the budget constraint. We see that the political problem for the central government is to allocate a limited budget for the local public good across the three jurisdictions (*u*, *p*, *r*) in order to enhance the odds of remaining in office. The optimal strategy for an opposition party seeking election is to offer to split the resources available for the jurisdiction-specific public goods equally between any two of the three jurisdictions. In Gupta's model individuals consider this split to be their reservation level of utility. The maximum welfare that can be realized in any two of the three jurisdictions is therefore given by

$$\max_{\tau, g_{Uf}} V(\omega(\tau_U) - \tau_U) + b(g_{Uf}) + B(G_U)] \tag{11}$$

subject to the budget constraint

$$G_U + 2g_{uf} = 3[\tau_U\{1 - l(\omega(\tau_U) - \tau_U)\} + \pi(\tau_U)] \tag{12}$$

With $\tau_U^*, g_{Uf}^*, G_U^*$ as the solutions to equation (12), individuals will set their reservation utility to be

$$V^{Uf} = V(\omega(\tau_U^*) - \tau_U^*) + b(g_{Uf}^*) + B(G_U^*)] \tag{13}$$

The central government can win the next election if and only if it allocates the public good as specified by equation (11). The optimality conditions are

$$\frac{3B'(G_U)}{U_x} = \frac{1.5b'(g_{Uf})}{U_x} = \frac{1}{1 + \frac{\tau_U l'}{1 - l}} \tag{14}$$

The provision of both central and local public goods to the favored jurisdiction is optimal where the marginal benefits of those two provisioning strategies are brought into equality with the marginal cost of the public funds required by that provisioning program. The requirement of equal taxation across jurisdictions constrains the government in its ability to favor certain jurisdictions through lower tax rates. The only instrument available to the center is to alter the supply of public good allocated to each jurisdiction.

An extension of the above model would allow us to explore the welfare and taxing implications of a federal system in which each of the three jurisdictions *u*, *p*, and *r* is represented by a local government that levies its own taxes, and delivers its own jurisdiction-specific bundle of a public good. For now it seems most pertinent to consider how the international development community can play a constructive role in the implementation of a credible regime of taxes and provision of public goods across all three jurisdictions in a unitary structure of governance depicted in the above model. The critical issue here is credibility. That is, how can the disenfranchised citizens of a notional state be persuaded to accept the implementation of a tax in exchange for the gradual delivery of much-valued public goods in those jurisdictions? This is the essence of the tax bargain—the essential *quid pro quo* by which the notional state begins the evolution to an empirical state.

## VI. Getting Started

The above model of the tax bargain requires that the political process be reformed in order that the central government would be forced to compete for political support across jurisdictions. In this way the tax bargain becomes the means by which the mask of citizenship might be lifted. But of course, reforming the political system is unlikely to seem compelling to international donors who are correctly averse to meddling in political matters. Is there a way to launch a program of reform without explicitly confronting the political structure of a country? I will demonstrate the approach by drawing on my work in Sudan.[1]

It is well understood that Sudan has been in perpetual conflict since the mid-1950s when British colonial rule came to an end. Indeed Sudan is a singular exemplar of the optimally attenuated state. While Sudan is the largest country in Africa, until recently there were no more than 20 miles of paved road in the South—heavy trucks often require 15 days to travel 400 km. between regional towns. The long-running civil war that was halted by the Comprehensive Peace Agreement of early 2005 has many "causes", but paramount among them would be that the South was long ignored by the North, but then was "noticed" in 1983 by an effort to impose various forms of Muslim law over Christian and animist peoples. Discovery of oil in 1978—mostly in what had been the South—added to the tension. And then after many years, the peace accord between North and South reminded the stateless warlords of Darfur that indeed there might be good reasons to wage guerrilla warfare against the North. Darfur, approximately the size of France, has never in recorded history had a governance regime that resembles in any way what we think of as a "state." With the prospects of a share of new oil revenues, with equally notional states to the Northwest (Libya), to the West (Chad), to the Southwest (Central African Republic and the Democratic Republic of Congo), to the South (Uganda), and with the government in Khartoum missing in action, the mystery is why the situation in Darfur is not worse than it is.

When peace between the North and South finally seemed promising in the summer of 2004, the first official "development" activity was the preparation of a Joint Assessment Mission (JAM) driven by the World Bank. The JAM was a joint activity because there was participation by the Government of Sudan (the "North"), the Sudan People's Liberation Movement (soon to become the Government of the South), 17 UN agencies, 10 bilateral donors, 7 multilateral organizations, and numerous other interested parties. A year later, when the Government of Sudan signed a peace accord with the main rebel group on Darfur (May, 2006) yet another JAM was created—again led by the World Bank. This latter effort was suspended soon after getting started because of renewed conflict in Darfur.

The main (North-South) JAM is over 450 single-spaced pages, and it was prepared in less than 9 months. Given the impossibility of travel in Southern Sudan during the rainy season, and following so soon after the war, it would be a mistake to assume that this report contains much in the way of first-hand knowledge of the situation on the ground. And precisely for that reason it has not proven to be a very useful document from the point of view of Ministers in the new Government of National Unity. As might be predicted from the manner of its creation, we see the rather standard boilerplate nostrums about how to get development moving. Despite this, and to its great credit, we also see some encouraging language about governance:

> 3. Underlying the CPA {Comprehensive Peace Agreement} and the proposed Framework is the recognition that large parts of Sudan are isolated and underdeveloped, with very minimal access to basic services and infrastructure; this is particularly the case in the South, war-affected areas of the North, West and East, and the Three Areas of Blue Nile, Southern Kordofan, and Abyei. Indeed, wide disparities have characterized the country historically, including along regional lines, between urban and rural areas, and by gender. These disparities suggest the need for targeted efforts, though the basic needs for peace and development are clearly applicable nationwide, as outlined in a joint concept note for a Poverty Eradication Strategy (PES).
>
> 4. The National Government (NG) faces several major challenges. Chief among these is improving governance and creating the decentralized governmental system envisioned in the CPA that allows for community-driven recovery and an important role for a vibrant civil society and independent media. In turn, more equitable distribution of the national wealth and public resources will enable state and local governments to fulfill their service delivery responsibilities, and lead to better education, healthcare, and water and sanitation access in underdeveloped regions. This requires an ongoing shift in prioritization of public spending toward programmes and investments that facilitate broad-based

> economic growth, including via increased traditional agricultural and livestock productivity along with support for private sector development. The NG has additional responsibilities related to guaranteeing the special status of, and enabling development in, the Three Areas. These goals will be pursued while maintaining macro-economic stability.
>
> 5. The Government of Southern Sudan (GOSS) has adopted a vision for equitable development and poverty eradication, but will start from a much lower level in terms of institutional capacity and socio-economic development. Key education and health indicators, such as child and maternal mortality and primary enrolment, are among the worst in the world. Infrastructure is virtually non-existent, with no paved roads outside the main urban centres, and a civil service and service delivery structures for service delivery must be created essentially from scratch. Millions of IDPs {Internally Displaced Persons} are expected to return to the South, compounding the challenges. The strategy is to promote rural development through a big push on basic infrastructure to support intraregional, North-South, and international trade linkages, and based around market towns, services to promote the productivity of agriculture, and expanded access to basic social services, especially education. Through the CPA the GOSS will have access to substantial domestically-generated revenue, but additional resources will be needed to enable the realization of development objectives [JAM, Sudan, 2005].

The interesting thing about this language, stripped of the allusions to civil war, is that the conditions being discussed can be found in the vast majority of countries in Africa—isolated towns and regions, poor transport, bad communications, mal-distribution of assets, backward regions, the complete absence of governance, etc. Why are these conditions noticed only after a civil war? What policy initiatives might introduce aspects of the tax bargain without existing fragile political processes? These and other issues warrant much more attention than they normally receive.

## VII. Implications

The development challenge in Africa remains problematic because of a flawed conceptual model of the reasons for Africa's current immiserization. The reigning mental model of development is a particularistic structure dependent for its theoretical and empirical content on agro-ecological conditions in Western Europe over the previous three centuries. Progress in

Africa awaits the introduction of the tax bargain alone by which the mask of citizenship can be lifted, and the notional state thereby transformed into the empirical state.

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# Endnotes

[1] I served as an advisor to the SPLM/SPLA starting in early 2004 while work was underway to prepare the SPLM to join the Government of Sudan in a government of national unity (GNU). More recently I advised the GNU on the preparation of the Darfur JAM, and assisted in scoping out a program of work to strengthen governance in the South, and in Darfur.