

GERALD W. SCULLY (1992) *Constitutional Environments and Economic Growth*. Princeton: Princeton University Press.

Gerald W. Scully's book addresses how government affects economic growth and income distribution and, within ten chapters, provides a detailed, scholarly and original treatment of this most important issue. Rather than taking the traditional focus of examining the relationship between public spending and economic performance, Scully extends the analysis of the role of the public sector by examining how the legal, political and economic framework of society influences economic growth and income distribution. The central theme is that the constitutional setting of an economy is an extremely important determinant of the ability of individuals to transform economic resources into output. The research question that Scully examines is whether or not there is a link between individual liberty and national economic progress.

Chapter 1 concludes with the hypothesis that economic growth is as affected by choice of the economic, legal, and political institutions as it is by resource endowment and technological progress. Economic, legal and political systems embody visions of human progress and, from alternative visions, come arguments in support or against such issues as collective ownership of resources and public sector allocation of resources. In other words, alternative visions lead to alternative "rules of the games" for the rights and responsibilities of the individual versus government and the rules and order of a society. In Chapter 2, Scully suggests that the traditional focus of economists considers growth to be a mechanical process, a sort of alchemy, which is wholly determined by growth of inputs and the laws of production. Neoclassical growth models simply hypothesize a relationship between national income and capital-labor ratios, with technology fixed and the resulting "black box" theory is argued to contribute nothing to the debate of individual versus government control of resources.

Building on the research program initiated by Buchanan and Tullock, Chapter 3 derives a theory of how the range of the constitutional setting determines the possible gains from exchange. Topics include how the scope and inclusiveness of individual rights affect efficiency and income distribution, the importance of policies regarding dispute resolution and enforcement of agreements, how rational individuals contract for income re-distribution policies during the pre-constitutional stage, whether rules of order emerge spontaneously or through fiat and the role played by legal systems. The theory of the evolution of the constitutional setting is developed in Chapter 4. Through amendments

to constitutions and by laws passed by legislatures, changes may be made in the constitutional setting. By expanding the role of the monopoly agents of government to include the brokering of changes in the structure of rights, a pattern of the evolution of the constitution is shown to lead to a steady-state constitutional setting. Rent-seeking and constitutional revolution are shown to be substitutes for growth-enhancing activities.

Measures of economic liberty for a wide range of countries are constructed in Chapter 5. Fifteen attributes of economic liberty are argued to meet the criteria of being credible and include: freedom of property, movement, information, civil rights, type of economic system and freedom of print and broadcast media. In order to weigh the attributes of liberty in constructing an overall index of liberty, Scully uses an instrumental variable or hedonic approach and weights by regression coefficients. In Chapter 6, various hypotheses regarding effects of legal systems on freedom are developed and tested on a sample of 167 countries. Fifty-four countries have common (or judge-made) law where legal rules emerge from the judicial resolution of disputes between parties of equal standing. Ninety-four of the countries operate under civil law which basically means that law is what those who govern say it is. Also discussed are Muslim law (41 countries in the sample) and Marxist-Leninist law (19 countries). The general hypothesis is that liberty is greatest under common law and empirical evidence confirms that freedom has prospered under common law and liberty suffers under other traditions. In Chapter 7, economic growth and efficiency measures for 115 economies over the period 1960–1980 are compared to measures of freedom. Regression analysis shows that the rights structure has significant and large effects on efficiency and the growth rate of economies. Relatively free countries are found to grow at three times the rate and are two and one-half times as efficient economically in transforming inputs into national output as countries in which freedom is relatively absent.

Empirical evidence in Chapter 8 demonstrates that a large fraction of the observed inequality of income across countries is due to inequality in individual rights. Societies are shown to have much larger shares of income going to the middle 60 percent of the distribution when they are politically open, have private property and market allocation of resources. Conventional wisdom of a negative trade-off between efficiency and equity is not observed and therefore suggests that an increase in freedom yields an improvement both in efficiency and in equity. Changes which raise freedom are therefore argued to be Pareto-efficient.

In Chapter 9, the effects of government expenditures on economic growth and efficiency are measured. Consistent with previous studies, empirical evidence shows that nations with large public sectors grow more slowly than those with small public sectors. The evidence on economic efficiency, however, has not been previously examined and shows that smaller public sectors tend to have more efficient economies. The final chapter sums up the evidence in the following way: “Private property, freedom of contract, and free market exchange free the Scotsman in everyone. Collective ownership and the political allocation of resources waste a nation’s natural endowment” (213).

I will only focus on two of Scully's contributions here. One contribution is his logical integration of the theory of constitutional political economy into the theory of economic growth. One need only browse through recent articles and books on economic development to witness first hand the extent to which academicians have ignored the role of the constitutional setting in influencing economic performance. With the seminal work of Buchanan and Tullock as the cornerstone of his theory, Scully logically leads the reader into understanding the role of the constitutional framework in determining the possibilities of gains from exchange which ultimately play a crucial role in determining how economic resources are transferred into national income. While the tradition of public finance has examined the costs and benefits of having the public sector direct resource allocations, constitutional political economy demonstrates that the design of institutions is also an important choice that economists may examine. Scully's book provides evidence on the influence of institutions, or rules, upon economic performance. Another contribution is the wealth of empirical evidence provided on a large variety of hypotheses. This is clearly a case where theory and empirical work blend together to produce a convincing argument. By going beyond the traditional focus on public spending, examination of liberty and legal variables is clearly in the best tradition of what constitutional political economy adds to the study of the public sector.

One indication of the usefulness of a book is whether or not it leaves the reader with applications in other areas. Two applications come easily to my mind. One area is how the issue of federalism affects the constitutional environment. While Scully briefly argues that countries in which central governments are awarded relatively large roles are also countries with relatively large public sectors, I am left wondering how, within the constitutional political economy framework, federalism affects economic growth and income distribution.

Another application is in the area of restrictions on the influence of the public sector in our lives. Scully briefly discusses three methods of constraining the public sector: (1) constitutional restrictions on taxes and expenditures; (2) a Wicksellian voting rule of unanimity; and (3) a principle of taxation equal to benefits as in user fees. I believe that it would also be useful to consider the implications of his work regarding the importance of legal, political and economic institutions for the growing literature which studies how to design constraints on the role of the public sector in our lives. For example, how would a constitutional political economist re-design international political agencies, such as the World Bank, so that they take advantage of the advice offered in this book? Is it possible for these agencies to re-direct their policies in such a way that they promote efficient re-design of the constitutional environments of less-developed countries?

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