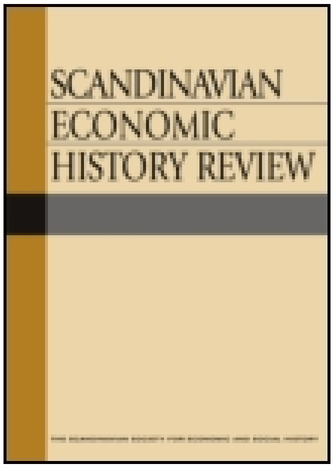

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Ultimate and proximate growth causality: A critique of Mancur Olson on the rise and decline of nations[1]

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A Critique of Mancur Olson on the Rise and Decline of Nations[1]

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In the past three decades analysis of the "proximate" causes of economic growth has been greatly enriched by both theoretical developments and quantitative studies. Technocratic supply-side growth accounts are available in considerable sophistication and detail,[2] but analysis of deeper causality is still rare.

One must therefore welcome a major study which turns back to more "ultimate causes" of growth acceleration and deceleration somewhat in the spirit of Max Weber and which shows some of the links between ultimate and proximate causality. Of course, Olson's evidence is often flimsy but this is, to some extent inevitable, and is not a disadvantage in ventilating a new idea as Weber himself demonstrated.[3]

The hard core of the argument is that various interest groups develop modes of collective action to further their particular interests, and increasingly over time their activities distort the efficiency of resource allocation to a very important degree. The theory derives directly from his earlier book[4], but the new elements are the assertions that these processes cumulate as a very significant growth constraint in countries where the social order has not been interrupted by war or revolution, and that they are always a very powerful, if not the most powerful influence on growth.

As in the earlier book, he argues that it is easier to form small groups than big ones, that the conflict between group and general interest is always larger with small groups, and that some latent groups, e.g. of consumers are not constructable. Some countries are lucky because they tend to develop larger, "encompassing", groups which are less harmful to the general interest, but he rejects the argument of John R.

1 Olson, M., *The Rise and Decline of Nations*, Yale, 1982.

2 See Maddison, A., "Growth and Slowdown in Advanced Capitalist Economies: Techniques of Quantitative Assessment", *Journal of Economic Literature*, June 1987, for a survey of "proximate" growth accounts.

3 See the sweeping assertiveness of Weber, M., *The Protestant Ethic and The Spirit of Capitalism*, Unwin, 1971 (first published 1904-5) p.35 where he states (on the basis of some figures "one of my pupils" dug out) "business leaders and owners of capital, as well as the higher grades of skilled labour, and even more the higher technically and commercially trained personnel of modern enterprises, are overwhelmingly Protestant".

4 Olson, M., *The Logic of Collective Action*, Harvard, 1965.

Commons[5] and J.K. Galbraith[6] that reasonably satisfactory outcomes can be attained by each group exercising countervailing power. He asserts that no country can attain "symmetrical organisation" where interest groups and latent groups can engage in comprehensive bargaining to achieve optimal outcomes.

His strongest evidence concerns the postwar perfomance of advanced capitalist countries, for which he advances a number of quite plausible propositions. Thus the U.K. has had slow growth and relative decline because its ancient social order has not been seriously interrupted by revolution or war. The social order itself and some of the coalitions which it fosters have been of major significance in retarding growth. Sweden, whose traditional order was similarly uninterrupted has done better because its pressure groups are more encompassing. United States postwar growth has been slower than that of the U.K. but it has retained its position as the leader in real income levels, because the country has benefitted from the absence of a medieval past, and from its size. Australia and New Zealand have done badly because pressure group influence has distorted resource allocation through protection. Germany and Japan did very well because defeat in war shattered the old growth impeding coalitions.

As Olson is neither a revolutionary or a warmonger he does not actually recommend periodic destruction of the social order. He would weaken the power of distributional coalitions by free trade, free entry for foreign and multinational investors, and free migration (pp. 141-2). He would dismantle regulation, reduce subsidies and welfare payments (p. 172-5), abandon activist macropolicy aspirations (p. 230) and promote price flexibility (p. 224). He assumes that (a) unconstrained competition is "staggeringly powerful" (p. 59) in producing beneficial outcomes; (b) there are no macroeconomic problems if you get your microeconomics right; and (c) in most cases government intervention to mitigate inequality will make inequality worse.

Olson's basic schema is quite simple. He accepts that GDP (Y) per head of population (D) is a reasonable measure of economic performance. The ultimate influcences on its growth are the institutions (I) that constitute the social order, and the degree of sociopolitical conflict (S) engendered by interest groups within a given order. I and S exert their influence mainly on the efficiency of resource allocation (E). Otherwise the supply potential is more or less given by the available production factors augmented by available technology (F). Olson does not disaggregate the production factors and practically ignores the influcence of I and S on F . Historical events (H) enter into his schema because they (i.e. war and revolution) shake up I and break the constraining power of S. Policy hovers off-stage as an unwelcome phantom. He considers macropolicy to be generally malign in its impact and he wants an economy where discretionary government action virtually disappears.

5 Commons, J.R., *The Economics of Collective Action*, Macmillan, New York, 1950.

6 Galbraith, J.K., *American Capitalism*, New York, 1952.

One may represent Olson's explanatory schema as follows:

$$H \rightarrow \boxed{IS} \qquad \text{Ultimate Causality}$$

$$\frac{Y}{D} = f\left(\frac{F'}{D}\right)E \qquad \text{Proximate Causality}$$

I have the following comments on Olson's schema:

(a) I would stress the importance and legitimacy of articulate and discretionary macroeconomic policy implemented by governments who exist because they were elected within a framework of universal suffrage. Variations in macropolicy between countries, and changes in policy mix in different phases of capitalist development have had a significant impact on growth. Thus I would add a firm and powerful (P) for policy in the line describing ultimate causality.

(b) I think Olson is right to stress the role of social conflict, but the origins of such conflict go deeper than he suggests. Inequalities which arise from social institutions and market forces are important additional causes. Nevertheless my judgement is that Olson probably exaggerates the causal influence of group conflict as distinct from institutions and policy. This is of course only a hunch, because, like Olson, I do not know how to measure their importance.

(c) Olson's stress on the role of specific historical events is very useful. However, it should be noted that some of these, e.g. the OPEC price rises and the collapse of the Bretton Woods monetary system were oecumenic "system shocks" which have had a simultaneous and similar rather than a differentiating impact on growth performance of different countries.

(d) Olson refers occasionally to the leader-follower dichotomy and the distance from the technical frontier in his treatment of particular countries. In fact, this phenomenon explains a good deal of the postwar differences in growth performance between countries, and should figure explicitly in the growth schema.

(e) The way in which ultimate causality has its impact on growth performance is more complex than Olson suggests. He puts all the weight on efficiency but I, S and P can affect the rate of growth of the physical capital stock, the quality of the labour force, the level and stability of demand, the rate of structural change etc. The growth schema should therefore spell out these proximate influences on growth more fully than Olson does.

(f) Olson more or less rejects the possibility that output may be below potential because of lack of demand. To my mind any schema which deals with comparative growth performance must include at least a crude notion of capacity use.

(g) When dealing with comparative growth performance on a world wide scale, one must allow something for colonial exploitation or conversely for foreign aid. Olson's discussion of pre and postwar Asain development excludes consideration of the malign effect of colonialism or the favourable impact of aid, even though (to quote somewhat extreme cases) the prewar drain from Indonesia took 8 per cent from its GDP[7] and postwar aid to Korea added 8 per cent to its GDP[8] in the 1950s and 1960s.

Olson's view of the interaction of ultimate and proximate causality is too simple. I would suggest a more complex explanatory schema, as follows:

An Alternative View of Growth Causality

$$H \rightarrow \boxed{I\ S\ P} \rightarrow \boxed{T} \qquad \text{Ultimate Causality}$$

$$\frac{Y}{D} = f\,\boxed{\left(\frac{N'\ L'\ K'}{D}\right) EC \pm A} \qquad \text{Proximate Causality}$$

Y = GDP; D = Population
H = Significant historical events
I = Basic Social order as characterised by Institutions, Beliefs and Ideology
S = Degree of Sociopolitical Conflict within a given social order
P = Macroeconomic Policies for Growth and Stability
T = Distance from Technical Frontier
N' = Natural resources developed and augmented
L' = Human capital, i.e. labour force augmented by investment in health, education and training
K' = Stock of all kinds of physical capital augmented by technical progress
E = Efficiency of resource allocation
C = Degree of Capacity Use
A = Foreign Aid (-) or Plunder (+)

Olson is concerned almost entirely with the relative performance of nations. He says virtually nothing on the reasons why the tempo of growth has varied in different phases of capitalist development. In a way he gives some sort of explanation of why there was a golden age between the end of the war and 1973, though his explanation could have been richer if his model had been more articulate about the general significance of the catch-up phenomenon which separated the USA from the rest. However he does not make any serious attempt to explain or measure the general slowdown since 1973 apart from suggesting that apparently all countries suffer from an increasing price stickiness.

It is useful for economists to specify their theory of the state, and it seems to me that four are available. One is the Marxist view that the state is an organ which the ruling class uses as an instrument of exploitation. This rules out the Olson thesis and he naturally rejects Marxism hook line and sinker. The second view is the social engineering one which assumes that rational state action can achieve optimal out-

7 See Maddison, A., Dutch Income in and from Indonesia, 1700-1938, in Maddison, A. and Prince, G., eds., *Economic Growth in Indonesia 1820-1940*, KITLV, Leiden, 1988.

8 Maddison, A., *Economic Progress and Policy in Developing Countries*, Allen and Unwin, London, 1970, pp. 310-11.

comes. This Olson would reject as naive. Olson's own theory is an ethereal version of the liberal one. His objectives are similar to Hayek's, but for Olson the state is a piece of scenery - all real action is concentrated on his distributional coalitions. He does not mention bureaucratic power and threats to freedom, which are central to Hayek.

My own theory of society and the state is more eclectic than Olson's. I share the liberal concern with the dangers and distortions of bureaucracy, and am all in favour of a hands-off policy in most microeconomic matters. In macroeconomic matters I think there is a strong case for articulate and activist policy. On distributive issues, some degree of conflict is always present in the socioeconomic process, but the nature and locus of conflict varies over time, and is not necessarily cumulative. I also believe that state redistributive action has played an important and useful role in mitigating social conflict over the past century.

The original context of Olson's theory of collective action was the United States economy. It seems legitimate to extend it to the advanced capitalist countries as a group, even though there are differences in constitutions, party systems, proportional representation etc., which affect the way in which distributive coalitions operate. However, he is on thin ground when claiming that his theory can be readily applied to third world countries which are not pluralist democracies, or when he tells the citizens of the biggest third world democracy that they would have been better off to remain a colony of the slowest growing capitalist country (p.179).

My final problem with Olson's approach is that he is vague about measurement. He does not tell us how to measure the strength of distributive coalitions, how to measure the degree to which they are encompassing, or how to measure allocative efficiency. He does not tell us how to rebut alternative explanations of the growth phenomena he discusses. He is obviously aware of the need for some quantitative evidence because he includes 20 pages of Kwang Choi's analysis of growth experience within the USA. Unfortunately this regional evidence is irrelevant in a study of the rise and decline of nations.