6. Conclusion: connection between the general institutional analysis and the case study on the MENA region

This study has examined whether formal and informal institutions separately influence economic growth and whether the economic performance of the MENA region can be traced back to its institutions. It further questioned why Arab institutions developed in this special way and not as, for example, Western European institutions. Since the illustration of the whole institutional development path went beyond the scope of the study, emphasis has been placed on how early institutional development was responsible for varying development paths as well as formal and informal institutions. Not only political, legal, and economic systems have been considered, but also cultural components such as value systems, worldviews, and the resulting morals and norms. These informal institutions determine the form of societal organization, which has a direct impact on economic development.

During the analysis it was demonstrated that institutions significantly impact on economic development. If institutions differ between regions the economic performances must also differ. However, the analysis partly supports a kind of cultural determinism. This would indicate that Arab countries are in a hopeless state or an institutional trap. The hypothesis of cultural determinism was partly affirmed through the equilibrium view of institutions. This view leaves no space for institutional change and adaption besides an exogenous shock.

However, the current study does not only depict the equilibrium view. Theories of institutional change, incorporating institutional transplantation, are also discussed. Since the equilibrium view depicts a model or a theory, it might not reflect the real world. It can be used to theoretically demonstrate and explain the persistence of institutions resulting from equilibrium strategies. Since institutional persistence inter alia depends on deadlocked behavioral rules, the application of the theory is justified. Traditional value systems, which determine the behaviors of societies, cannot be easily changed because informal institutions are mental constructs that provide individuals with mental stability and self-identification. To understand the rigid character of value systems, these can be described as institutions resulting in equilibrium strategies that cannot be changed.

However, the equilibrium view has its drawbacks. It omits further possibilities of endogenous institutional change, even though Aoki’s (2001) model includes the possibility of action profiles influencing the institutional environment. Accordingly, institutions are exogenous to a single agent, but are endogenous regarding the set of technologically possible action profiles or rather society per
Hence, institutions are shaped by society, often unconsciously, but are exogenous constraints to the single individual.

Even the equilibrium view, and classical game theory in general, must be described as an inadequate instrument to examine institutions in their entirety. Institutional dynamics cannot be examined using these tools. In any case, institutional dynamics are not the main issue in institutional analysis, since institutional persistence is the bigger problem to first understand before considering solutions for institutional change. Game theory and the equilibrium view emanate from rational agents and predetermined strategies. History plays no role and behavior is future-oriented. Furthermore, the equilibrium view contradicts some of the statements made in the first part of this study. It was emphasized that institutions are influenced by innumerable factors with a society’s history playing a decisive role. In addition, several drawback mechanisms between institutions and the level of economic development must be considered. However, it was also stated that the application of every theory can be justifiable; the user, however, must clearly describe his intentions and must be aware of the fact that the theory does not depict a world formula, but solely describes one channel that could be useful for understanding the bigger picture.

To use Greif’s (2006) words, who also uses game-theoretic tools to analyze institutions, “Institutions are not game-theoretic equilibria, games are not the basic unit of institutional analysis and game theory does not provide us with a theory of institutions. Indeed, the key to advancing institutional analysis by using game theory is precisely to recognize the difference between game-theoretic equilibrium analysis and institutional analysis” (p. 19).

Using the equilibrium view, the issue of institutional persistence and thereby unchanging value systems and codes of conduct is depicted. Using Greif’s (1994) model, it is further demonstrated that different belief systems result in different forms of societal organization. Since belief systems and the consequent behavior depict optimal strategies for society, its history, and further prerequisites, these systems are rigid and can be compared with institutional equilibria to demonstrate the influence rigid value systems have on societal organization and economic development. It does not intend to define every society as an equilibrium state and every individual as a rational, purely future-oriented agent.

According to the analysis, different value systems result in different forms of societal organization and, therefore, varying economic outcomes. It has been demonstrated that equilibrium wages vary between societies and that levels of social mobility and specialization depend on the form of societal organization. Accordingly, limited morality, which describes a collectivist, traditionalist society, leads to lower wages and a horizontal social structure, whereas generalized morality, which is defined an individualistic, modern society, results in higher wages and a vertical social structure. Both outcomes are optimal for the present conditions. Hence, a society with relatively lower living standards and growth
rates cannot be described as inefficient per se. Every societal and economic outcome is a result of the society’s history and its institutional environment (of course, geography plays a role but this factor is not included in this study).

If history and institutions determine everything and cannot be changed, then nothing can be done regarding the low living standards of less developed societies. According to the preceding analysis of this study, this is partly true. But institutional change is still possible and the feedback mechanism running from economic development to institutions should not be underestimated. Exogenous institutional change in the form of institutional transplantation can work. However, there can be no general solution or set of institutions that lead to economic growth in every society. Instead, every case must be individually considered. The transplanted institutions must fit the – often informal – institutional basis. However, this implies that the institutions of property rights, the rule of law, political participation, and market liberalization cannot be implemented immediately because they do not match the prevalent institutional environment. Even if it sounds strange to Western economists, free markets and the corresponding political, civil, and legal rights might not lead to immediate growth in every society.

Increasing living standards influence peoples’ preferences. Material security alters utility functions and shifts the purpose of life from survival to self-realization. Hence, economic development induces institutional change. Values and attitudes change with higher incomes, although the basic identifying informal institutions might persist. But this does not imply that as time goes by every population will develop into a Western-style, individualistic society. Instead, differing institutional environments and forms of societal organization will prevail, implying varying economic performances. Underdevelopment should, therefore, not be accepted as an unchangeable matter of fact. Of course, living standards in poor economies must be increased. But how this can be achieved must be considered in every case anew, and it should be understood that societies do differ and do realize different outcomes, whether economically, politically, legally, or morally, and that some of these differences will always persist.

The enduring character of cultural differences was shown by regression analysis, which indicated that religious affiliation still influences the nature of institutions even though the currently affected parts of the population might not be practicing believers. Religious affiliation measured via the percentage of a population belonging to a certain religion indicates the underlying religious influence that is not consciously felt and implemented by the individual. That is to say, a certain religious moral prevalent in a particular region might no longer be consciously implemented by the population. But the values and morals resulting from the religion have become a part of the culture and of the general value system. Hence, people are still influenced by early religious values and morals,
even if they describe themselves as non-religious since the prevalent culture and society was shaped by a certain belief.

This is demonstrated by the fact that countries with majority Muslim populations have significantly different formal and informal institutions compared with countries with majority Protestant populations. Because of data availability and the necessity to match several data sets, only two religious directions could be incorporated. However, since the present work emphasizes institutions in the Arab region the approach is adequate.

Accordingly, countries with mainly Muslim populations realize informal institutions that intend a form of generalized morality, and formal institutions that do not assure secure property rights, a constrained executive, and an independent judiciary. Countries with a majority of Protestant citizens implement informal institutions that can be equated with generalized morality. In addition, the formal institutional index indicates secure property rights, a constrained executive, and the implementation of an independent judiciary. Hence, Islam and Protestantism seem to result in partly different institutions. Furthermore, it was demonstrated via the regression analysis that informal and formal institutions have a significant impact on the level of per capita income.

The theoretical and empirical findings permit several conclusions regarding the MENA region. Institutions in Muslim countries differ to institutions in Protestant countries. Furthermore, institutions influence per capita income. Hence, the varying institutions of mainly Muslim and mainly Protestant countries result in different economic outcomes. This is further exemplified by the descriptive empirical analysis of the MENA region. Nearly all indicators show significant differences between institutions in the MENA region and the Western advanced economies (as a matter of interest, Japan is included as an advanced economy although it neither belongs to MENA nor to the Western hemisphere). According to the first part of the study, the institutions implemented in the MENA countries do not correspond to the institutions that were described as being neoclassically growth supportive. For example, insecure property rights do not allow optimal individual utility maximization. The same holds for a missing independent judiciary. Furthermore, autocratic governments are predominant in MENA and civil liberties and political rights are not ensured. These institutions inhibit individual utility maximization and restrain incentives to invest.

Regarding informal institutions, the evaluation of WVS data indicated a societal structure of limited morality in the MENA region. The results regarding trust and control are not that obvious; however, respect and obedience indicate a hierarchical society with an emphasis on collective and hierarchic structures. In addition, the analysis of further survey questions showed a traditional attitude regarding the roles of women, education, work, and family in general.

According to institutional theory, these patterns – whether informal or formal – are difficult to change. Consulting the equilibrium view of institutions to
understand the issue of institutional persistence in the Arab region, only an exogenous shock could alter the equilibrium strategies determined by institutions. That is to say, the prevalent traditional and conservative value system that emphasizes the collective, attributes major importance to religion, disadvantages women regarding education and work, and supports hierarchic structures is persistent. The same holds for historically and culturally rooted formal institutions. The model indicated that change is not possible regarding the observed institution. However, apart from the equilibrium view model it was stated that in fact most institutions are dynamic entities. But marginal change can take hundreds of years to become obvious. This means that the institutional environment in the MENA region can and does change. However, a complete reversal is unlikely since the historical development path has pushed the region in a certain direction. Moderate modernization might take place but it will take time.

Regarding formal institutions, exogenous change is only partly promising. The successful implementation of exogenous institutions into MENA countries – for example, the rule of law, civil liberties, democracy, and market liberalization – depends on the distance to the prevalent institutional structure. Hence, the institutions might be abolished, they might be disregarded, or they might disturb the prevalent institutional structure and lead to destabilization; but they might also fit the prevalent institutions and lead to a general adjustment and thereby modernization, at least in the long run.

In most countries of the MENA region, the prevalent institutions lead to considerably lower per capita incomes and, therefore, living standards compared with highly developed Western states. The historical analysis demonstrated why this is the case and showed that MENA institutions could only develop this way. Historical accidents and institutional and societal developments made other alternatives impossible. That is to say, the current institutional and economic situation of the MENA region is a logical consequence of its development path.

In particular, the historical analysis showed the importance of worldview and a certain belief system for societal and economic development, factors currently omitted from mainstream economic analysis. However, as stated in the

---

72 However, some MENA countries realize high per capita incomes and growth rates, for example the UAE. At any rate, these are the RRLI countries and their richness can be traced back to special characteristics. All of the rich Arab countries are oil exporting countries, and thereby they owe their economic successes to resource richness and low indigenous populations. These countries are able to afford growth-inhibiting institutions since oil incomes compensate for the institutional environment. However, the descriptive statistical analysis of the MENA region shows that the oil states do not possess significantly different institutions to the non-oil countries of the MENA region. Still, the current work does not go into detail regarding the Arab countries with high per capita incomes. The objective of the study is not to examine how far the current structures of the MENA countries differ, but to demonstrate the unique institutional development and its implication on economic growth; omitting specialities resulting from resource endowment.
case study, Western European development depended on the acquisition and society-wide implementation of the naturalistic worldview. This was not an easy process and the Christian church battled naturalism and sciences. But, as shown, things were different to in the MENA region. The prevalent institutions and accidental events led to the Industrial Revolution, sustainable growth, and the development of a free civic society. The rejection of naturalism and the acceptance of Islamic occasionalism made a similar development in the MENA region impossible. Without being persuaded by cause and reason and thereby without natural laws, modern sciences and a physical worldview could not emerge. From an Islamic point of view, what happened was a logical conclusion. Assuming the Quran to be unchangeable and non-interpretable, and assuming God to be the only creator, natural laws indeed make no sense. However, for the same reason none of the two development paths, neither the Arab nor the Western European, can be described as better or worse.

Regarding the high population growth rates and low living standards, the MENA region will face even more economic problems in the future. Increasing economic growth rates in the past few years cannot hide this fact. However, studying institutions and institutional development in the MENA region helps explain why Arabic institutions developed by this means. Hence, we now know why the Arab region took this particular development path and we know why the economic performance is worse than other regions. However, what we cannot say is how the MENA countries should solve their problems. This is not possible since the analysis demonstrated that institutions, even if they are economically inefficient, can depict a kind of optimal state regarding the particular society and that exogenous institutional change is hardly possible. This is a depressing result for the MENA region and also for other less developed countries.

However, it was shown that institutions are dynamic and even the institutions of the MENA region can change over time. Furthermore, exogenous institutional change is possible. Hence, there is a chance for development economics and in- and outsiders that are interested in institutional change in the MENA countries. But the realization per se will be difficult. The transplanted institutions must fit the prevalent institutional environment. That is to say, they do not necessarily belong to Western-style political, legal, and economic institutions. However, Western organizations of any form will find it morally debatable and also theoretically senseless to exogenously install non-Western institutions in a foreign country. Indigenous forces might find it easier to induce change. They will also know better which institutions fit the cultural basis. However, IEX and IEN institutional change might still result in region-specific outcomes. Hence, the institutional environment and the corresponding economic performance might still not match Western and mainstream economic claims. Furthermore, indigenously introduced change, whether endogenous or exogenous, is not predictable. Actions fostering economic productivity and growth are desirable,
since increasing living standards change preferences and thereby institutions. However, of all things the prevalent institutions in the MENA region hinder an increase in productivity and growth.