

**Institutions as Economic Growth Determinants:
A Comparative Study of New Zealand and Argentina**

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Table of Abbreviations

A	Argentina
g	Growth Rate
GDP	Gross Domestic Product
GST	Goods and Services Tax
HO	Heckscher-Ohlin
I	Inflation Rate
IBRD	International Bank for Reconstruction and Development
IMF	International Monetary Fund
IRIS	Institutional Reform and the Informal Sector
Kiwibank	Kiwibank limited
MP	Member of Parliament
n. a.	Not available
n. d.	Not dated
NIE	New Institutional Economics
NGO	Non-Governmental Organisation
NZ	New Zealand
NZD	New Zealand Dollar
OECD	Organisation for Economic Co-Operation and Development
OIE	Old Institutional Economics
TFP	Total Factor Productivity
TVNZ	Television New Zealand Limited
UN	United Nations
US	United States of America, or United States
USD	United States Dollar
WWII	World War II

Attestation of Authorship

I hereby declare that this submission is my own work and that, to the best of my knowledge and belief, it contains no material previously published or written by another person (except where explicitly defined in the acknowledgements), nor material which to a substantial extent has been submitted for the award of any other degree or diploma of a university or other institution of higher learning.

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Abstract

Through the last two and a half decades academia has realised that viable explanations of the rise and decline of nations in a world in dramatic economic and political change requires more than a static neoclassical model. Among the flourishing research on institutions as economic growth determinants are the two distinct theories of Douglass North, the co-recipient of Nobel Prize in 1993, and Mancur Olson. Both scholars claim the universality of their approaches in explaining real world economic history. However, research on the differences in their theories and their applicability to small and remote countries, like New Zealand and Argentina, remains in its early stages. A more detailed investigation of conceptual differences may clarify particular economic growth parameters, and may provide more empirical support for each theory. Thus, the research question is:

Can the economic growth patterns of New Zealand and Argentina of the last quarter century be explained either by Douglass North's 'cultural heritage' hypothesis or by Mancur Olson's 'country-specific economic policy' hypothesis?

Firstly, an in-depth literature review of Douglass North's and Mancur Olson's latest academic work is conducted. Based on the examination of commonalities and differences in their terminologies and concepts, a conceptual framework for further empirical tests is derived. The framework is used to evaluate New Zealand's and Argentina's economic growth patterns in order to address the abovementioned research question.

The assessment of the literature reveals that both scholars share the notion of the role of the state in providing well-defined individual property rights, low transaction cost levels, and well-developed national capital markets to achieve economic growth potential. They ascribe growth-fostering characteristics to institutions of Britain and other relating democracies, while they see obstacles for economic success for Latin American countries. On the other hand, their propositions differ substantially in the foundation of economic policy and its ability to adjust over time.

The findings of the empirical research show that institutions play a major role. However, the proposed differences in the aforementioned indicators exist only to a limited extent. An enhanced understanding is obtained that New Zealand's and Argentina's economic growth patterns cannot be solely explained neither by North's nor Olson's theory. A combination of both theories and further amendments might account more accurately for the actual economic histories of the two countries.

1. Introduction

1.1 Focus of the Dissertation

At the centre of the research for this dissertation are Douglass Cecil North and Mancur Olson, as well as their latest theoretical propositions. North is seen as one of the leading representatives of New Institutional Economics (NIE). His theory proposes differences in cultures as reason for regional economic growth differences over the last centuries. On the other hand, Olson is described as one of the best political economists. He focussed on country specific political institutions as the main source of economic growth differentials. What both scholars have in common is that they want to provide theoretical models to explain actual economic history.

Therefore, New Zealand (NZ) and Argentina are chosen for this dissertation as real-world examples. They serve as proxies for orthogonal cultures in North's sense and for the differences between long-lasting and newly established democracies in the sense of Olson. Both peripheral countries share the fact that they started comprehensive economic reforms towards becoming open market economies at the beginning of the 1980s. The dissertation examines the capability of both models to explain their actual post-reform economic growth patterns over the last quarter century.

1.2 Douglass C. North

1.2.1 Biography of Douglass C. North

Douglass Cecil North, born in Cambridge, Massachusetts, in 1920, graduated with a triple BA degree in political science, philosophy, and economics from the University of California at Berkeley in 1942 (North, 2005a, p. 81). He started his impressive academic career at the University of Washington in Seattle in 1950, followed by various senior positions in later years. In 1983, he moved to Washington University in St Louis to become the Henry R. Luce Professor of Law and Liberty in the Department of Economics, and later served as director of the Centre in Political Economy. He was the first economic historian ever honoured with the John R. Commons Award in 1992; which is regarded as one of the economics profession's most prestigious prizes. Moreover, in 1993 Douglass North was the co-recipient, with Robert Fogel, of the Nobel Prize in Economics "for having renewed research in economic history by applying economic theory and quantitative methods in order to explain economic and institutional change" (Nobel Foundation, 1993). Three years later he was elected a

Fellow of the British Academy (North, 2005a, p. 81). Furthermore, North provides his expertise to the World Bank and to several countries, for example Argentina, with regards to economic growth issues (ibid; Encyclopædia Britannica Online, 2007). Throughout his career he published numerous articles and ten books. North's 1990 book, *Institutions, Institutional Change and Economic Performance*, a major work of his later academic career, has over 5,000 citations on Google scholar alone.

1.2.2 Douglass C. North's Academic Contributions

Douglass C. North is cited frequently as one of the groundbreaking and most influential scholars within the NIE, a growing field of research which emerged during the 1970s (Rutherford, 2001, p.173; Vandenberg, 2002, p. 218). His attempt to combine the two orthogonal stands of economic theory and economic history is seen as his major contribution to the academic world (McCloskey, 1994, p. 164). On one hand, his work has shown the need to consider institutions and actual history to neoclassical economists. On the other hand, he equipped scholars of the NIE with a theoretical tool for their analyses.

Thus, as Myhrman and Weingast (1994, p. 186) argue, his central concept of the rise of the western world is a new holistic approach to (informal) institutions and their influence on economic growth in a dynamic setting. They consider the global applicability of his approach as a key difference in comparison with other scholars. It provides a general theory to understand the economic success and failure of countries (ibid, p. 193).

Moreover, his research on single components within his central concept, like multidimensional property rights, the role of transaction costs and ideology, earned him further respect from the academic world (Fiani, 2004).

His academic honours and contributions notwithstanding, North has had to face criticism because of his inconsistent application of economic theory over time (Rutherford, 1995; Vandenberg, 2002, p. 218). Although his central concept of regional economic growth differences prevails within his work since the early stage of his career, his underlying reasoning has changed dramatically (Myhrman & Weingast, 1994)¹. For instance, North's co-authored 1973 book, *The Rise of the Western World: A New Economic History*, consisted of an almost pure neoclassical analysis. However, at the

¹ In general, Myhrman & Weingast (1994) are positive towards North's development over time and present it as a seamless process. However, if read in more detail and accompanied by other literature, a good illustration of North's structural breaks in his theory is provided.

beginning of the 1980s his work was based on features of Institutional Economics, like transaction costs, property rights, a theory of the state, and (to a certain extent) mental models, to explain the same phenomena and to extend its scope (Myhrman & Weingast, 1994, p. 190). However, in *Institutions, Institutional Change and Economic Performance*, North (1990) abandoned former key assumptions and put emphasis on elements characteristic of Old Institutional Economics (OIE) like persistent inefficiency, uncertainty, bounded rationality, social norms, and institutional change (ibid, p.192). His critics argue that at the beginning of the 1990s his model had become a “noisy rabble of all the pet concepts and theories of a variety of disciplines and sub-disciplines” (Clark, 1993, as cited in Vandenberg, 2002, p. 232). In other words, his later work of what will be called his ‘mature phase’ contains a colourful mix of orthogonal theories like neoclassical economics and OIE as well as NIE; which, in the opinion of scholars like Vandenberg, makes it nearly impossible to propose a consistent model. Inspired by his critics, the process of transformation in North’s reasoning continues with his latest focus on differences in learning (Voigt, 2006, p. 311).

1.3 Mancur Olson

1.3.1 Biography of Mancur Olson

Mancur Olson, born in 1932, gained his formal education at North Dakota State University, followed by Oxford on a Rhodes scholarship, and then by a PhD from Harvard (McLean, 2000, p. 652). Until his sudden death in 1998 he was working at Maryland University, College Park, where he founded the Centre of Institutional Reform and the Informal Sector (IRIS) in 1990 (Dixit, 1999, F445). In addition, he was Vice President of the American Economic Association, as well as one of the founding members of the Public Choice Society, and served as section president for the American Association for the Advancement of Sciences in 1989 (Oppenheimer, 2000, p. 797). Mancur Olson published three books and several journal articles which were translated into more than ten languages (McLean, 2000, p. 653).

His capabilities were valued throughout academia. Olson won several prizes from the American Political Science Association for the outstanding quality of his second book² and for *Pluralism and National Decline* as the best paper presented at the previous year’s annual meeting (Oppenheimer, 2000, p. 797). Finally, his theory of *Collective Action*, as developed in his first book,³ could have won him the Nobel Prize in

² Olson, *The Rise and Decline of Nations*. New Haven and London: Yale University Press, 1982

³ Olson, *The Logic of Collective Action*. Cambridge, MA: Harvard University Press, 1965

Economics (McLean, 2000, p. 651). As Oppenheimer (2000, p. 797) cites the Nobel laureate Herbert Simon, Olson was able “to look at things in a creative and original way”; and Robert M. Solow, another Nobel laureate, said, upon his hearing of Olson’s death, “Most of us are pretty much alike; seen one, you’ve seen them all. Mancur was different, one of a kind. All the more reason that we will miss him (ibid, p. 798).”

1.3.2 Mancur Olson’s Academic Contributions

Olson was a pioneer in combining key issues of political science and economics (Cadwell in Olson, 2000, p. xvi). Therefore, he is seen as the major founder of the interdisciplinary Public Choice Theory (Oppenheimer, 2000, p. 797). Within this framework his lifelong concerns were economic justice and fairness in the outcomes of social and governmental process (ibid).

Olson’s 1965 book, *The Theory of the Logic of Collective Action*, is regarded as his outstanding contribution to social sciences (ibid, p. 795). This more non-market related concept about social behaviour of dispersed or concentrated lobbies revolutionised many aspects of social sciences like the n-person prisoner’s dilemma of Game Theory (ibid). Even more than thirty years after the publication of his first book, it still provides grounds for lively academic debate (Cadwell in Olson, 2000, p. xvi). Another important contribution is his unique recognition of market failures in the realm of public goods and externalities, which produce the problem of *free-riders* (Schelling, 2000, p. 799). In his 1982 book, *Rise and Decline of Nations*, Olson provides invaluable insights on the rent-seeking behaviour of minor groups and its negative impact on economic growth (ibid).

In addition, his insights on free trade, on the so called ‘Coase Theorem’, and on private property rights are well regarded by other scholars (McLean, 2000, p. 662-664). Moreover, in his last phase he contributed to economic science by discussing the role of institutions, the development of under-developed countries and economies in transition (Schelling, 2000, p. 799).

However, his standing within economics was a controversial one. For instance, his work as an economic theorist was “known, honoured, and studied more outside his own discipline than within it (ibid, p. 798).” Therefore, he was more regarded as a political theorist than an economist because he studied interest groups instead of prices of goods or incomes of certain groups (ibid; McLean, 2000, p. 651). Moreover, some of his critics regarded him as a one-idea thinker in regards to his theory of collective action (ibid).

1.4 Purpose of the Dissertation

The theories of Douglass North and Mancur Olson share a lot of commonalities with each other although there are crucial differences in their approaches to explaining economic growth. Firstly, the dissertation will evaluate these characteristics on a theoretical basis. Secondly, the dissertation will examine the validity of the propositions of North and Olson in explaining actual economic history by applying them to two real world examples.

The first country is New Zealand, a former British colony. It is considered as a viable proxy for North's 'British' model, because it is often referred to as "miniature England" (Sutch, 1966, p. 29) or as "Britain of the South" (Belich, 2001, p. 16). Furthermore, NZ is one of the oldest democracies in the world and, hence, might be a suitable example for well-established democracies, maybe with a tendency towards institutional sclerosis, in the sense of Olson (Jackson, 1998, p. 491). The second country is Argentina, a former colony of Spain, and an example of the inherited 'Spanish' model, as well as being one country that was actively advised by Douglass C. North (Encyclopædia Britannica Online, 2007). Additionally, through its recent military regimes and its economic downturn during the twentieth century, it can be considered as an example of an economy in transition as in Olson's terminology (Sanz-Villarroya, 2005). Both countries have quite similar climate and initial factor endowments, and have peripheral locations on the world map, as well as a long history of similar events and developments in economic policy.⁴

Thus, the central research question of the dissertation is:

Can the economic growth patterns of New Zealand and Argentina of the last quarter century be explained either by Douglass North's 'cultural heritage' hypothesis or by Mancur Olson's 'country-specific economic policy' hypothesis?

The research will mainly utilise North's terminology, unless otherwise stated. This approach shall allow for establishing a consistent testing framework and for improving the understanding of the dissertation.

1.5 Importance of the Dissertation

The dissertation shall contribute to the relevant academic debate through the development or the improvement of economic theory. The purpose is to investigate the general applicability of North's and Olson's theories respectively as sole or dominant

⁴ New Zealand's and Argentina's suitability as real world measures for both economic theories will be examined more deeply in section 1.6 of the dissertation.

sources of economic outcomes of two former colonies of Western Europe. If necessary, ideas for extensions to the theories, or for a combination of both, shall be presented to account more comprehensively for the actual economic history of NZ and Argentina.

Furthermore, the outcome of the research might provide advice for the current strategic national economic policy discussions within both countries. That a revision of policy could be beneficial in the case of NZ has been shown by Dalziel (2002, p. 38), who calculated NZ's aggregate underperformance between 1987 and 1998 as being as high as 114 billion NZD when compared with Australia.

1.6 Context of the Dissertation

Despite being two suitable orthogonal proxies of inherited informal and formal institutions in the sense of North,⁵ New Zealand and Argentina also share a lot of historical and further commonalities. Firstly, they are located on peripheral positions on the world map. Secondly, they were land-abundant, but capital and labour scarce young settler nations with temperate climates at the end of the 19th century (De Long, 1988, p. 1144). Thirdly, both countries were among the richest nations in the world before the First World War by efficiently exploiting their natural factor endowments (Greasley & Oxley, 2000, p. 174, Sanz-Villarroya, 2005, p. 440).⁶ They experienced a spectacular period of export-led growth between 1870 and 1913 by shipping large quantities of frozen meat, wool and dairy products mainly to their main common trading partner, the United Kingdom (Greasley & Oxley, 2000, p. 175, Thompson, 1992, p. 426).⁷ Fourthly, they were among the top recipients of large-scale British investments until 1913 (ibid). These funds were mainly spent on building some of the best and most widespread railway systems in the world, and on new technologies like refrigeration and steam boats (ibid). It can be concluded, that Argentina was almost a virtual economic colony of Great Britain between 1870 and 1914, when even English customs were transferred (Bulmer-Thomas et al., 2006, p. 494). However, this could easily lead to the assumption that Argentina's success was simply based on the adoption of the British model. On the other hand, it has to be considered that the most immigrants arrived on ships from

⁵ NZ, founded in 1840 by the Treaty of Waitangi as a British colony, became a democracy and adopted UK-based institutions (Evans et. al., 1996, p. 1857). On the other hand, Argentina of the 19th and 20th centuries might have possessed North's stylised 'Spanish' incentive structure due to its large overhead costs, 'rent-seeking', and 'corruption'; and the large role of the military in a 'Balkanised' Latin America (Bulmer-Thomas et. al., 2006, p. 30).

⁶ Argentina's income level per capita of USD 3,797 exceeded that of Western Europe in 1913 (Maddison, 2001).

⁷ Both countries shared free trade with the UK. This is not surprising in the case of New Zealand as colony of Britain. However, Argentina signed the Anglo-Argentine Treaty of Friendship, Commerce and Navigation in 1825 (Thompson, 1992, p. 422)

continental Europe with their culture-coined belief systems stowed in their luggage (Thompson, 1992, p. 436). Moreover, in Argentina Spanish is official language and, hence, the main medium for communication and learning.

Furthermore, the inherited British belief system of NZ and Argentina's former strong relationship with the UK in trade did not prevent the failure of both economies to adapt successfully to structural changes of world trade over the time. According to Feinstein (1999), after 1950 developed countries moved from agricultural to industrial, and later to service-oriented economies. Furthermore, rising real incomes in the OECD group, and resulting shifts in lifestyle led to a significant decline in the share of food in overall consumption in favour of manufactured goods and financial or business services over time. In other words, the prices of NZ's and Argentina's main exports declined while imports of manufactured goods rose with higher living standards.

The policy makers of both countries decided to implement import substitution policies, which was a popular theory at the time. They both relied on import-controls to fight the involuntary balance of trade deficits; on agricultural exports; and on forced industrialisation under public control (Greasley & Oxley, 2000; Lewis, 2003). This resulted in increasing bureaucracy and transaction cost levels in both economies. The protectionism in times of globalisation led to a massive misallocation of labour, and to rising prices of scarce capital. In the case of New Zealand, its erroneous inward-looking policy of publicly controlled "manufacturing in depth" in the 1960s was worse than if it had specialised in small-scale industries. Apparently, the policy makers did not account properly for New Zealand's limited access to capital, including human capital (Sutch, 1966).

The collapse of the Bretton Woods system in 1971 and the first oil crisis in 1973 led to a rapid end of the world-wide "Golden Age" (Crafts, 1999, p. 20; Feinstein, 1999, p. 46).⁸ NZ's and Argentina's foreign spending increased because of higher world interest rates and higher prices for capital goods (Sanz-Villarroya, 2005, p. 445; Easton, 1997, p. 234). Their income deteriorated after the economic policies of the OECD members shifted towards managed trade and increasing government spending (Crafts, 1999, p. 20). As a result, New Zealand had to suffer dramatically from the loss of its trade privileges to the UK, when its main trading partner joined the European Union in 1973. Furthermore, both countries suffered from a further decline in primary product prices (Greasley & Oxley, 2000, p. 187).

⁸ Annual growth rates of real GDP per capita of the leading OECD nations fell from 1950-1973 to 1973-1996 by a level of 0.8% to 5.5% (Crafts, 1999, p. 20)

Table 1: Effects on New Zealand

Year	Current Account m NZD	Annual Inflation Rate	Budget Deficit/ GDP	Govm. Exp./GDP	Net External Government Borrowing m NZD
1973	+1,956	7.9%	-2.7%	27.1%	-998.7
1975	-8,198	14.6%	-4.0%	30.1%	1,611.4
1977	-1,816	14.1%	-3.7%	30.0%	635.4
1979	+442,8	13.6%	-8.5%	38.4%	1,694.0
1981	-815.0	15.7%	-6.6%	39.1%	2,140.6
1983	-2,389	7.4%	-6.9%	41.4%	1,462.9

Source: Statistics New Zealand (2006) for New Zealand indexed on 2000 price level

Table 2: Effects on Argentina

Year	Current Acc. m USD	Annual Inflation Rate	Budget Deficit/ GDP	Govm. Exp./GDP	Net External Government Borrowing m USD
1973	+700	23.7%	-1.4%	9.2%	948.2
1975	-1,288	444.1%	n. a.	n. a.	1,116.6
1977	+1,127	174.6%	n. a.	n. a.	1,433.3
1979	-535	101.2%	n. a.	n. a.	3,095.6
1981	-4,712	160.9%	-2.6%	15.3%	4,717.4
1983	-2,436	619.5%	-14.1%	20.3%	3,089.7

Source: UCLA (1997) for Budget deficit and Government exp.; Worldbank, (1995) for current account, inflation and government borrowing

NZ and Argentina experienced an increase in foreign debt, inflation, current account and fiscal budget deficits, as well as unemployment rates within a decade after the oil crisis (Evans et al., 1996, p. 1860; Sanz-Villarroya, 2005, p. 445).

Both countries opted for comprehensive policy reforms after 1983 to counter the crises. Therefore, the economic paths that New Zealand and Argentina took since the reforms will be in the focus of the dissertation. It will be examined whether Douglass North's or Mancur Olson's theory provides a coherent explanation for the development of both countries within the most recent two and a half decades.

1.7 Structure of the Dissertation

The following chapters of this dissertation examine the academic propositions of Douglass North and Mancur Olson on a theoretical basis, and as applied to the real world examples New Zealand and Argentina. *Chapter 2* reviews the academic work of Douglass North's mature phase, with particular emphasis on his cultural heritage hypothesis. Mancur Olson's theory, with his focus on differences in economic policies, will be examined in *Chapter 3* using North's terminology, unless otherwise stated. The key terms and the main propositions of both theories are critically evaluated and compared with each other in *Chapter 4*. In *Chapter 5* the conceptual framework of how both theories and their main hypotheses might be tested empirically on the basis of their own suggestions will be built. *Chapter 6* outlines the research methodology of this dissertation, which is applied to examining the proposed framework in the context of

New Zealand and Argentina. General economic growth patterns are evaluated in *Chapter 7*. *Chapter 8* provides further insights into the political markets of both countries. The national economic markets and, in particular, the national capital markets are examined in *Chapter 9*. *Chapter 10* summarises the key findings, the research implications, the limits of the study, and the areas for further research.

2. The Theory of Douglass C. North

2.1 Professional Field of Literature

The rationale of the dissertation will be mainly based on North's Nobel lecture (1994), which provides a good synthesis of his mature phase. It includes the relevant propositions of North's (1990) preceding book, *Institutions, Institutional Change and Economic Performance*. Additionally, further conclusions will be drawn from North's and Arthur D. Denzau's (1994) article, *Shared Mental Models: Ideologies and Institutions*. Finally, North's (2005b) latest book, *Understanding the Process of Economic Change*, which can be viewed as the culmination of his mature phase, will be utilised in the dissertation for more detailed examination of certain critical issues of his theory.

His later academic work is seen as a combination of traditional economic theory and quantitative methods with actual economic history (Rutherford, 2001, p. 189). It is also centrally placed in NIE since it stresses the importance of the institutional structure of a country in fostering economic growth by economising transaction costs (ibid, p. 173).

2.2 North's Framework and Main Elements

North's later work, as represented by his Nobel lecture, is about understanding *economic change* (North, 1994, p. 359).⁹ Instead of the static analysis of the general equilibrium model, he wants to provide a dynamic tool, which is capable to analyse the determinants of the process of economic growth over the last 200 years (ibid).

For this purpose, he builds an analytical framework, an *initial scaffolding* (ibid). This is based on neoclassical theory in regards to scarcity and competition assumptions. However, to make it workable in a dynamic setting, elements of NIE and OIE are employed. In contrast to standard neoclassical theory, his model incorporates Herbert Simon's *bounded rationality* assumption with prevailing *uncertainty* and *imperfect markets* (ibid, p. 361).¹⁰ Moreover, his latest focal point, *the intergenerational learning process*, combines *learning*, and the additional dimension of *time* (ibid, p. 360); which refers to the concept of *path-dependency*. *Formal*, and especially *informal* political *institutions*, as well as their *enforcement characteristics* are the main columns of his

⁹ Important terms of the theories of both scholars will be presented in italics at their first occurrence.

¹⁰ North (1994, p. 361) identifies 'novel' choices of individuals, which are based on new, but incomplete information, as the reasons for economic change. Moreover, he attributes changes in the price or quality of competitive products as well as in demography or stock of knowledge through technology to the sources for new information (ibid).

scaffolding, and his ‘best-fit’ samples of his research focus on cultural differences in the learning process over time (ibid, p. 359). He insists institutions are central in creating multidimensional *property rights*, the *rule of law*, as well as *competition*. Moreover, institutions are not necessarily designed to be efficient (ibid, p. 364). However, ideally they have to provide *order* over time, which is a prerequisite for ensuring economic growth (ibid, p. 366). In his Nobel lecture, North presents the vaguely defined terms of *autocratic regimes* and rule of law as two antithetic sets of formal institutions to establish order (ibid, p. 367). More recently, they are more explicitly labelled as *authoritarian political order* and *consensual political order* (North, 2005b, p. 104).

North (2005b, p. 105) attributes the following commonalities to both systems:

1. The prevailing organisations, as well as the set of rights and privileges, are shaped by the underlying formal and informal institutions;
2. Political and economic markets are in a stable structure of exchange relationships;
3. The state is committed to political rules and enforcement that protect foregoing points 1 and 2.
4. Norm internalisation and coercive enforcement ensure conformity of the citizens.

On the other hand, North (2005b, p. 104) attributes differentiating characteristics to the two ends of his dichotomy, as shown in Table 3.

Table 3: North's Model of Order-Maintaining Systems

	Authoritarian Political Order	Consensual Political Order
Order Is Established	Without the consent of the governed	With the consent of the governed
Formal Rules Are Specified by	The ruler	Common ideals calling for respect for another
Conformity Achieved by	Mixture of coercive force and social norms, where its extension depends on consistency of social norms with the rules	Internalisation of social norms in regards of obeying and enforcing the rules by a credible stake of the society (“legitimate”)
Individual Property and Civil Rights	Not ensured	Ensured
Distribution of Chances	Rent-seeking	Same people play the same game with the same pay-offs and risks

Likewise, he assigns the major role for the foundation of *disorder* to wrong perceptions of belief systems. In other words, wrongly set-up informal institutions limit economic growth (North, 1994, p. 363). In fact, disorder can affect both sets of political

order. In both cases it results either from a reduction of coercive enforcement of rules or from the weakening of norms of cooperation (North, 2005b, p. 106).¹¹

Transaction costs-minimising competition and the existence of *impersonal exchange* are further central elements of his scaffolding (North, 1994, p. 360-363). They are the keys for *economic success* in the modern world, a term he uses interchangeably with economic growth (ibid, p.365). In North's (1994, p. 361) opinion, transaction costs occur through the following:

- 1st Measuring the multiple valuable dimensions of a good or service
- 2nd The protection of individual property rights
- 3rd The enforcement of agreements.

Later, North (2005b, p. 158) adds a 4th dimension: "The integration of the dispersed knowledge of a society, or learning."

Impersonal exchange is necessary for North (1994, p. 364) to capture productivity gains from the rise in specialised knowledge as seen in the last centuries. Therefore, successful economies had to develop a comprehensive, well-defined contracting system to manage the increasing division of labour and interdependence in trade within growing markets.

2.3 North's Hypothesis of Cultural-Dependent Learning and Economic Growth

North's (1994, p. 363) main hypothesis, based on this aforementioned framework, is the existence of a seemingly seamless path-dependent link between a nation's belief system and its economic growth. In other words, his scaffolding stresses the importance of informal institutions like norms and traditions of a society in shaping its economic outcomes (ibid, p. 364). In his later work North (2005b, p. 155) depicts this coherence even easier to follow: "beliefs -> institutions -> organisations -> politics -> outcomes."

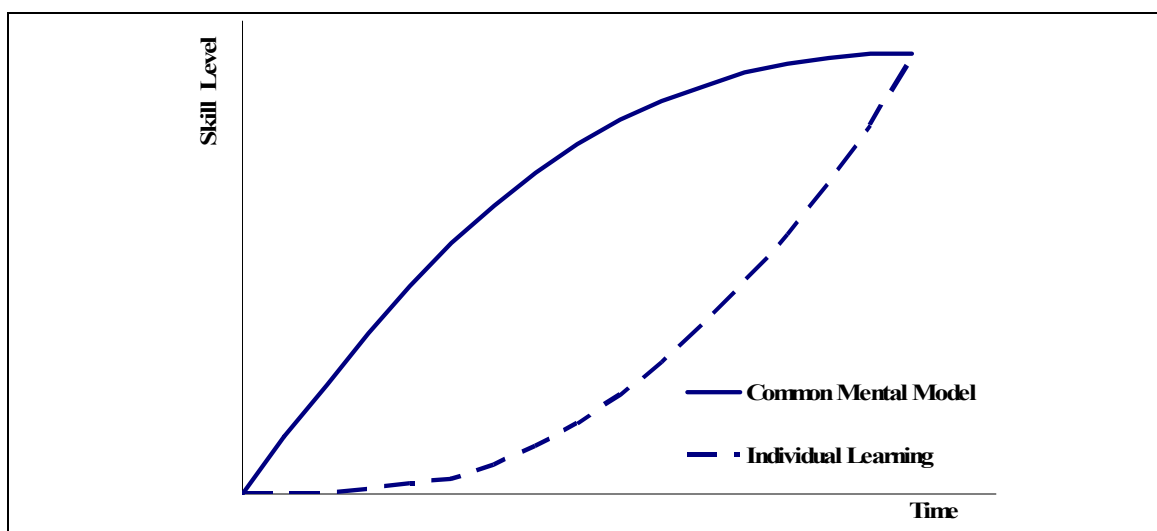
The foundations of this process are provided in Denzau and North (1994), where different ways of learning are stressed as source of differences in belief systems. They argue that the substantive rationality assumption of the economic actor does not hold in many real-world situations (ibid, p. 10).¹² Therefore, individuals have to develop rules to ease decision making, and they base them on the induction of their prior experiences

¹¹ On one hand, disorder can occur through radical changes in the rules of the game, the demise of an (autocratic) ruler or an (economic) crisis, which destroy the underlying consensus overnight. On the other hand, a gradual process of losing credibility can also affect a system over a longer period of time (North, 2005b, p. 106).

¹² The individual's ability to make decisions might be hindered by a lack of motivation, through a missing direct feedback loop, by the enormous complexity of a situation, through a high number and an unknown probability distribution of choices or by the low quality and frequency of information obtained (Denzau & North, 1994, p. 9).

(ibid, p. 11). North presents this as a process of two distinguished levels. The first stage is a period of rapid and undirected shaping of mental models, where individuals develop a structure to interpret external signals and categorise them in a meaningful way (ibid, p. 13). Once this structure is preserved and after a phase of refinement it is used to interpret a novel situation by induction (ibid). This second stage is characterised by a slow down of the development of the mental models, and by an intergenerational convergence of the individuals' perceptions through communication by a common language (ibid, p. 15). At this stage, considerable individual efficiency gains in learning are achieved within the existing framework (ibid, p. 23). On the other hand, opportunities for rapid changes in mental models occur only rarely and, therefore, shape path-dependent outcomes (ibid, p. 25). Therefore, the learning curve of mental models is seen as concave, while the one of the individuals is convex (Figure 1).

Figure 1: Pace of Learning over Time



Consequently, a nation's belief system, here an interchangeable term for culture, develops gradually over time to reduce uncertainty (North, 1994, p. 363). This shapes the informal and formal institutions, the *rules of the game*, of a nation. In turn, these *humanly devised constraints* limit the possible organisations, *the players of the game*, as well as their policies, and, hence, the economic outcomes (ibid, p. 361). In other words, North's selling point is that a nation's economic success over time depends on the incentive structure provided by its culturally-dependent institutions (ibid, p. 364).

This is the point where North's propositions about two different economic pathways, which are the focus of the research of this dissertation, come into play. North (2005b, p. 103) argues that some societies are able to re-establish order faster than others

because of their distinctive inherited belief system.¹³ Hence, solely *adaptive efficient* countries have flexible institutional matrices to adjust quickly to fundamental changes (North, 1994, p. 367; North, 2005b, p. 107). North insists that certain countries perceive external changes more correctly due to their embedded culture, incorporate them faster in their belief systems and change their institutions more accordingly (ibid).

Therefore, North (2005b, p. 107) provides four key characteristics of such countries:

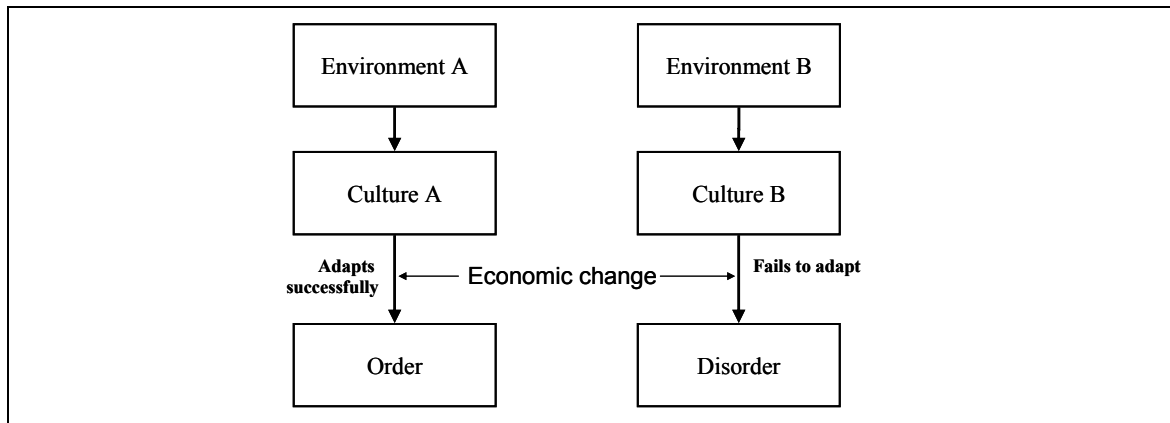
1. Established citizen rights must set up self-enforcing limits for politicians by sharing social norms (for instance by a common belief system),
2. A successful constitution limits stakes in politics by assigning citizen rights and placing limits on governmental decision-making,
3. Property rights and personal rights must be well-defined; and
4. The state and its officials must adhere to the commitments and rights.

In other words, only adaptive-efficient countries have established these ideal-type institutions of impersonal exchange that constrain the players and limit political rule-making (North, 1994, p. 164). Hence, only these societies will experience persistent economic growth.

This means that for the opposite end of the institutional spectrum, that while their formal institutions may be changed over night, their strongly-held, deeply-rooted informal institutions cannot (ibid, p. 366). Therefore, North (1994, p. 367) stresses the difficulty in establishing adaptive efficiency in societies that have experienced persistent disorder. In his latest book, North (2005b) offers two possibilities for their institutional upgrade. First, he suggests the long time taking advice of non-governmental and other external organisations to develop and implement long-lasting consensual political order (ibid, p. 164). Secondly and not very convincingly, North also offers the empowerment of an authoritarian ruler as another option to shorten the timeframe in establishing consensual policy (ibid).

¹³ Surprisingly, on one side, North (2005b, p. 107) attributes the existence of order generally to “adaptive efficiency”, a term he uses interchangeably with consensual political order. On the other side, he associates the occurrence of disorder generally with authoritarian political order (ibid).

Figure 2: Cultural Differences in Responding to Economic Changes



2.4 North's Differentiation Between the British and Spanish Models

In his Nobel lecture, North (1994, p. 365) clearly attributes economic success over the last 200 years to the *British model*, to the culture of Britain and of its colonial outposts. This leads to the following implications: First of all, because of their common cultural background these countries share almost identical informal and formal institutions. Secondly, their institutional settings are an almost ideal-type of incentive structure. They provide a market-oriented competitive environment that permit low-cost transacting in impersonal markets in the long-run (ibid, p. 362). They are flexible and adaptable to changes over time (ibid, p. 364), and their institutions have promoted consent-oriented democracy, which assures the rule of law and efficient property rights in the long-run (ibid, p. 366).

In contrast, he attributes the term *failure* to the prevailing economic institutions and political structure of the *Spanish model* (ibid, p. 365).¹⁴ This leads to the following conclusions: Spanish countries, which include former Spanish colonies due to North's common cultural heritage hypothesis, share adverse informal and formal institutions, and, hence, fail to establish essential elements for modern economic growth (ibid, p. 363). Their common incentive system can be summarised as fostering rent-seeking behaviour, as well as being autocratic, centralised and inflexible to changes. Additionally, ill-defined belief systems have been the roots of their comparatively sluggish economic development (ibid, p. 366).

In his subsequent book, North (2005b) demonstrates his ideas even more explicitly by using the United States of America and Latin America as proxies for his general culture-heritage model.

¹⁴ In North (1994, p. 365), Portugal is part of the faulty 'Iberian' institutional framework. For the purpose of this dissertation, only Spain, as former colonial power over Argentina, is considered.

North (2005b, p. 140) bases his reasoning in the medieval age. He argues that because of its isolated geographical location, Britain did not have to employ a standing army and, therefore, avoided large overhead costs. Furthermore, the crown started to provide property and civil rights in return for more revenue in a labour-scarce environment (ibid, p. 141). Hence, democracy was created by establishing a parliament serving the whole country. The evolving common law became the supreme law of the nation (ibid, p. 143).

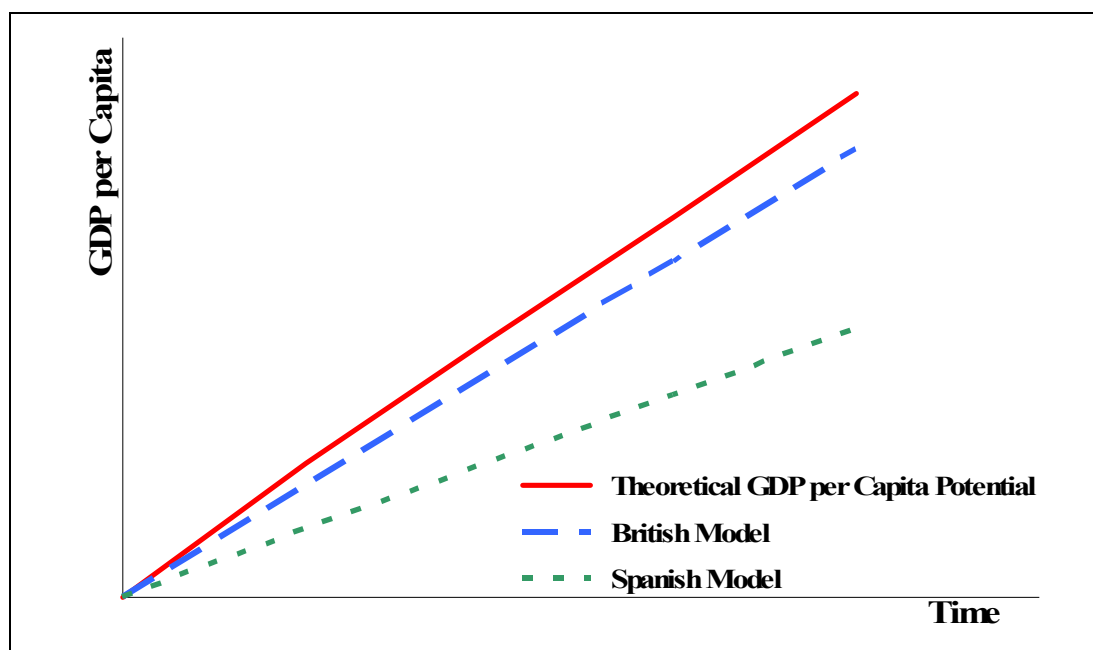
North (2005, p. 107) transfers these characteristics unmodified to the United States of America (US) as an ideological foundation of 350 years of their history. Basically, the path the US took was based on the British colonisation and the heritage of their informal and formal institutions. Therefore, they became an adaptive-efficient country with a long list of favourable characteristics: impersonal exchange; democratic self government; well-specified property rights; federalism; a complex system of specific, separated and limited powers; the rule of law; and cooperative behaviour. Furthermore, competition was achieved by increasing common market and budget constraints. In general, freedom was preferred over government. Additionally, immigration of capital and labour, and endless favourable events reinforced this belief system to support political and economic institutions (ibid, p. 111). Thus, this institutional setting encouraged exploring the particular factor endowments of the country.

North (2005b, p. 138) ascribes Spain to the other end of the political order spectrum. Its authoritarian system was reinforced after its colonies stopped delivering sufficient contribution for financing its overhead in the 16th century (ibid, p. 134). In contrast to the British model, its preference of centralised monarchy undermined competition and the rule of law by granting monopoly rights for additional revenue, by property confiscations as a mean of domestic taxation (ibid. 144).

Latin America inherited all of these features of disorder from Spain (ibid, p. 112-118): an authoritarian, centralised system; personal exchange; a lack of self-government, competition and well-specified property rights; as well as the granting of monopoly rights geared towards the extraction of precious metals. Therefore, any attempts to adapt constitutions similar to the US failed after independence from Spain. The ill-defined belief system led to a *stop and go policy* with rent-seeking, insufficient public goods, few citizen rights, and adverse income distribution (ibid, p. 119). In other words, Latin America could not experience economic growth during the last five centuries because of the inheritance of the wrong institutions.

North suggests that a country's economy works closer to its economic potential over time if based on inherited British institutions than on Spanish institutions, *ceteris paribus*. Here, North uses the two real world cultures as abstract, ideal-type samples for success and failure in economic growth over time.¹⁵ A simplified interpretation is depicted in Figure 3.

Figure 3: North's Differentiation between the British and Spanish Models



¹⁵ See Chapter 4.3.3.

3. The Theory of Mancur Olson

3.1 Professional Field of Literature

For further development of the dissertation Olson's theory will be briefly outlined as presented in his 1996 article, *Big Bills Left on the Sidewalk: Why Some Nations are Rich, and Others Poor*, and his last book, *Power and Prosperity: Outgrowing communist and capitalist dictatorships*, which was posthumously published in 2000.

3.2 Olson's Framework and Main Elements

Mancur Olson (1996) challenges the traditional assumption that economies are always working on the frontiers of their aggregate neoclassical production function. In this article, he rules out differences in natural factor endowments, in technological knowledge, and in culture as the primary sources of economic growth differentials. In his subsequent book, Olson (2000) elaborates on the foundation and the outcomes of his theory in more detail.

Olson (2000, p. 1) emphasises proper *incentives* as the main sources for modern economic growth. They enable production and cooperation by *specialisation* and *trade*. More specifically, he maintains that *formal institutions* and the *economic policies* of the resulting political organisations determine economic success (ibid, p. 194). For instance, the right formal institutions secure *individual property rights* by *enforcing contracts*, limit rent-seeking behaviour, and provide a *stable currency* (ibid, p. 26). Together, they reduce *transaction costs* significantly (ibid, p. 56), which he defines as "the costs to use a market" (ibid, p. 49).

Olson (2000, p. 61) distinguishes between *voluntary* and *enforced transactions* since transactions are not always mutually advantageous. In addition, he introduces the dimension of *time* by further differentiating between *on the spot transactions* and *long-term contracting* in *self-enforcing* or *socially contrived markets* (ibid, p. 174-176). Furthermore, Olson (2000, p. 93) differentiates between *private* and *public goods* in economic and political markets. *Collective actions*, which are the bargaining processes of rational, opportunistic individuals in small and large groups, lead to the problem of *free-riding* (ibid, p. 71). Thus, *negative* or *positive* selective incentives are needed to provide public goods (ibid, p. 85 f). Consequentially, *coercion* is a crucial element within Olson's apparatus (ibid, p. 62).

Based on these elements, Olson (2000) builds up a three-level hierarchy framework in economic growth fostering political systems. *Roving Bandits*, *Stationary Bandits* and *Democracies* share the common characteristics that their main tools are legal or illegal taxation. They all provide the country-specific base for the behaviour of profit-maximising individuals. On the other hand, Olson attributes differentiating characteristics to his model of political systems, as shown in Table 4.

Table 4: Olson's Model of Order Maintaining Systems

	Roving Bandits ("Anarchies")	Stationary Bandits ("Autocracies")	Majorities ("Democracies")
Order Is Established	No order prevails	Without the consent of the governed	With the consent of the governed
Distribution of Power	Random	Monopoly of the autocratic regime	Monopoly of a majority
Formal Rules Are Specified by	Not existent	The ruler	The majority
Rule of Law	Absent	Prevailing, but only enforced in the interest of the ruler	Prevailing and enforced
Interest of the Ruler in the Society	Minor	Encompassing	(Super) Encompassing
Conformity Achieved by	No conformity achieved	Coercive force of the ruler	Checks and balances and coercive force
Individual Property and Civil Rights	Not secured	Not secured	Ensured
Distribution of Chances	Rent-seeking	Rent-seeking	Rent-seeking

In the following section Olson's evolutionary model will be explored in a more detailed way.

3.3 Olson's Hypothesis of Individual Behaviour and Economic Growth

Olson's (2000, p. 70) theories are built on rational individuals and their bargaining behaviour over private and public goods in small and large groups, which Olson calls "collective actions." As he argues, private goods are only obtained through direct participation of the bargaining individual (ibid, p. 81). On the other hand, because of differences in collective actions, it is uncertain whether the public goods are provided

even in the absence of transaction costs (ibid). Moreover, rational, opportunistic individuals have the built-in incentive to defect in sharing the costs of public goods and to become free-riders. As shown by Olson (2000, p. 72), close ties in small groups, created through communication, punish free-riders, which in turn leads to more efficient group outcomes. On the other hand, this self-enforcement diminishes with rising population size because individuals stop voluntary bargaining because of their minuscule individual benefits from public goods (ibid, p. 77). Therefore, negative or positive selective incentives are needed to provide public goods (ibid, p. 88).

Consequently, coercion is a crucial element within Olson's apparatus (ibid, p. 62). He argues that only governmental actions can produce Pareto-efficient outcomes in the case of prevailing market failures in larger groups (ibid, p. 51). They regulate the important benefits to society, like national defence; which occur by the provision of non-excludable public goods or externalities to the society (ibid). Hence, compulsory third-party enforcement ensures that non-self-enforcing, not-on-the-spot transactions have to be fulfilled by the contracting parties. Furthermore, property rights and low inflation can only be maintained by coercion, which allow the exploitation of a country's growth potential through high investment rates in long-term investment projects (ibid, p.24).

That is where Olson's (2000, p. 7) three-level hierarchy framework of economic growth-fostering political systems comes into play. It starts with the roving bandits at the bottom, who act in a prevailing anarchy. The lack of a centrally-enforced rule of law results in substantial implicit tax rates and generates high levels of uncertainty, which marginalise long-term investment rates and paralyse productive forces (ibid, p. 64). Trades are limited to on-the-spot transactions in self-enforcing markets with high transaction cost levels (ibid, p.180). There are no public goods provided. Therefore, Olson (2000, p. 64) considers a society's move away from anarchy to any form of appropriate peaceful order as the greatest leap forward in production.

Stationary bandits, also called autocracies, are at the first level, where power is monopolised and where their leaders have an *encompassing* interest in the society. Profit-maximising autocracies avoid the distortion of incentives like over-taxation or *predation* to not harm the future exploitation potential of their sources of income. Hence, random crime, prevalent with anarchy and, therefore, uncertainty are substantially reduced by coercive force (ibid, p. 10). Moreover, within an autocracy public goods are provided to foster economic growth (ibid). Although preferred over anarchy, the governed have not voluntarily adopted autocracies (ibid, p. 11). As Olson

(2000) states, this is due to the opportunity of autocrats to override all other sources of power. Therefore, contract and property rights are not fully secured and inflation prevails (ibid, p. 28). Furthermore, autocrats can fall back to becoming roving bandits because they have a built-in bias towards shorter time-horizons through succession crisis. Hence, long-term investment rates are below their possible maximum; which limits the productivity potential of a society (ibid, p. 29).

Olson (2000, p. 15) puts democracies or majorities at the top of his model; however, he assumes that their leaders are as self-interested as autocrats. Moreover, he states that the ruling power of a democracy does not have to serve all by income redistribution, but needs majority approval to be re-elected (ibid). Olson (2000, p. 17) considers democratic systems as superior since they have implicitly lower tax rates to allow higher after-tax income for the majority. On the other hand, the more encompassing the stake of the majority is, the less are the social losses from redistribution higher taxes to itself, and, hence, the more are spent on public goods (ibid, p. 18). Furthermore, a system of checks and balances ensure the formal power is shared in democracies (ibid, p. 23). However, Olson (2000, p. 41) insists that the mere establishment of democracy does not automatically ensure the security of individual property and contract rights. On the other hand, he considers these elements as elementary to shaping a lasting democracy. Lastly, short-term time horizons in political markets can also distort economic growth in democracies (ibid, p. 42).

Summarised, the interest of the ruling elite in the society increases with the move upwards in the hierarchy. Hence, the level of uncertainty falls and economic activity rises by on-going specialisation and impersonal exchange. However, economies of the two last categories tend to *institutional sclerosis* over time because of the rent-seeking behaviour of self interest groups (ibid, p. 98). Hence, this leads to a slow down of economic growth.

Table 5: Economic Outcomes from Olson's Model of Order Maintaining Systems

	Roving Bandits ("Anarchies")	Stationary Bandits ("Autocracies")	Majorities ("Democracies")
Level of Taxation	Highest	Medium	Lowest
Availability of Public Goods	None	Provided until marginal profit of the ruler is zero	Provided
Level of Investment	Lowest	Medium	Highest
Exploitation of Productive Potential	Lowest	Medium	Highest

3.4 Olson's Differentiation Between the British and Spanish Models

Olson (1996,, 2000) does not distinguish between particular British and Spanish models as Douglass North does. However, for the sake of clarity, similar terms are used, as explained in the following paragraphs.

Olson (2000, p. 31) clearly rules out a path-dependent link between underlying cultures, existing democracies, or selfless leaders, and economic outcome. In his view, democracy can be easily accepted if mental models of the ruled were shaped by prior periods of negative feedback loops, like war. Additionally, Olson (2000, p. 31-33) bases the spontaneous and autonomous emergence of a democracy, an *accident of history*, on fulfilling the following three conditions:

- 1st No special interest group must have the bargaining strengths to become an autocratic leader.
- 2nd The roughly balanced powers should not be separated to create miniautocracies.
- 3rd Democracy could flourish in a setting where it is geographically protected from aggressive neighbouring regimes.

In other words, the enlightened self-interest of the governed leads to democracy, no matter which culture prevails.

Olson (2000, p. 38) favours certain characteristics of the British model. For him, industrialisation in the UK, and the US's economic miracle, came about because of an independent judiciary, further checks and balances, a secure common law, and the bill of rights, which made contracts enforceable and secured individual property rights. Because of the common occurrence of the aforementioned three conditions, and not on a common mental model, the governed of these nations started to cooperate in their own self interest (ibid, p. 32). Hence, Olson (2000) concludes that democracy in Britain and the US emerged coincidentally as an accident of history. In addition, autonomous external governments can establish economically successful democracies, as long as

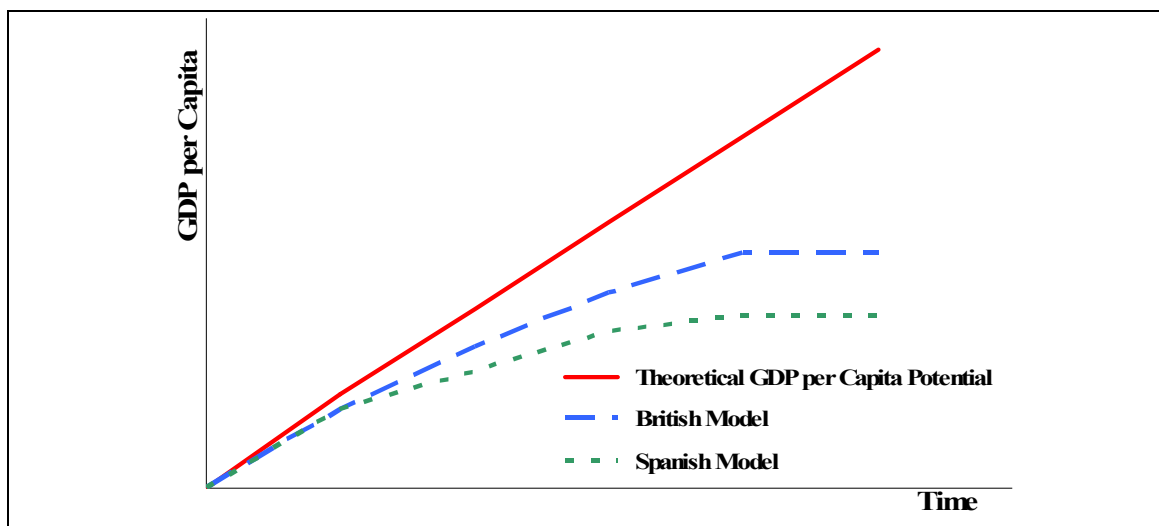
they install appropriate formal institutions, like power-sharing arrangements, to secure property and contract rights (ibid, p. 37). Hence, Olson's (2000, p. 37) model presents the 'democratic culture link' between Britain and the US and other former dominions as based on the transfer of formal institutions. Moreover, social peace is achieved by a feedback loop starting from the formal institutions (ibid, p. 103). The more property rights are established and enforced, the less crime prevails as it is in the pure self-interest of the people. Olson argues that the provided incentive of guarding one's own property leads to lower order-maintaining costs of the government as well.

Additionally, Olson (2000, p. 98) discusses rising transaction cost levels in long-established democracies, institutional sclerosis, as the loss of competition through lobbying. In his opinion, there is a built-in bias towards the emergence of special interest groups, like industry groups who employ themselves into rent-seeking by persuading the rational, 'ignorant' electorate to support their very narrow aims. Using North's terms, each democracy has the built in bias towards becoming less adaptive-efficient over time. Olson argues that Britain's long history of stability led to its *British Disease* in the second half of the 20th century (ibid).

Similar to North's Spanish model, Olson (2000, p. 27) acknowledges the occurrence of autocracies and poor economic development in Latin America. Furthermore, he also uses the empire of the Hapsburgs in Spain as an example for economic failure just as North does (ibid, p. 14). Olson (2000, p. 108) argues that solely market contrary economic policy created the incentive to circumvent the existing law and to engage in corruption and informal economic markets. Therefore, his reason for the failure is rather based on the wrongly set fiscal incentives of a country and the lack of well-defined property rights (ibid). For Olson other than North wrong incentive structures are not founded on a particular cultural heritage.¹⁶ Moreover, he sees more commonalities between Latin America and other third world countries than with Spain (ibid, p. 179).

¹⁶ See Chapter 4.3.2.

Figure 4: Olson's Differentiation between the British and Spanish Models



4. Critical Evaluation of the Two Institutional Theories

North began his career as a neoclassical theorist (Vandenberg, 2002, p. 218). However, through the years he noticed gaps within *The Wealth of Nations*. While standing at the ‘blackboard’, he recognised the ‘archives’ of OIE by turning his head around (ibid, p. 230). What appeared on North’s ‘blackboard’ changed after 1980, especially in regards to the underlying assumptions of efficiency and rationality (ibid). However, his feet remained firmly planted within NIE; which would rather extend neoclassical theory by institutional factors than replace it completely (Rutherford, 2001, p. 187). His work in the classroom became a combination of economic theory and economic history, and transformed him into a well-respected historical economist (McCloskey, 1994, p. 161). Conversely, Olson is sometimes described as “one-idea” thinker (McLean, 2000, p. 651). Beginning with his PhD thesis he intended to provide reasons for different outcomes in the behaviour of individuals and groups. Then, throughout his career, he extended these same ideas. Finally, his propositions allowed him to account for economic growth patterns of differing political systems in the real world.

4.1 Derivation of Theoretical References

Douglass North borrows heavily from the academic contributions of other important scholars like Ronald Coase, Thorstein Veblen, John R. Commons, Herbert Simon, and Friedrich A. Hayek (North, 1994). North also refers to Olson repeatedly in his work (North, 1990, , 2005b). In North’s (1990) book, *Institutions, institutional change and economic performances*, Olson’s Free-Rider Theorem is equated to the so-called one-stage, static prisoner’s dilemma of game theory; which is another theoretical rung of North’s (1994, p. 365; 2005b, p. 69) scaffolding. North (2005b, p. 114) mentions Mancur Olson’s Stationary Bandit Model as possible academic explanation for the prevailing selective property rights system in Latin America. North (2005b, p. 124) refers to Olson’s (1982) book, *The Rise and Decline of Nations*, to argue that markets tend to become inertial over time in the absence of “revolutionary institutional change.” Moreover, critical productivity improvement that lies beyond growth would be hampered by this inertia (ibid, p. 169). However, by this selective reference, North fails to conduct a more in-depth analysis of Olson’s propositions. On the other hand, Mancur Olson does not cite other scholars’ work as extensively as North. Furthermore, he does not explore his links with NIE, especially with the work of Douglass North (McLean,

2000, p. 667). Although both academics share many commonalities in their theoretical tools and propositions, they also differ very substantially in other areas. These will be exploited in the following sections.

4.2 Critical Evaluation of the Main Elements

North and Olson employ similar elements throughout their work. Among them are institutions, transaction costs, individuals, property rights, and rationality.

4.2.1 Institutions

North (1994, p. 360) defines informal and formal institutions as humanly-devised constraints that govern the opportunities for economic growth. Although North uses the among NIE widely-cited phrase of “rules of the game”, this does not mirror a generally accepted definition (Chang, 2005, p. 3). On the other hand, Mancur Olson, a political economist, does not define the term institutions as explicitly as North does, but he uses the term more in the sense of formal institutions (Olson, 2000, p. 1). However, for him, they are not mere constraints of market activities, as for North, but also incentives to enable trade by reducing transaction costs significantly (ibid, p. 56).

Major stakes in the origins of the concept of institutions stem from the work of Thorstein Veblen and John R. Commons (Groenewegen et. al, 1995, p. 468). North is close to the work of Commons with the transaction as his basic unit of analysis (ibid, p. 473). For Commons institutions are either based on a legitimate consensus or on coercion (Ramstad, 1996). This is lost in North, but close to Olson's approach. North's emphasis on path-dependent informal institutions, like customs and traditions, also follows Veblen's approach (Hodgson, 2001a, p. 66). However, Veblen and other scholars of OIE see institutions not as mere constraints, but also as liberation, and as instruments in the way of thinking and behaving (ibid). These discrepancies continue when further academic disciplines are considered. Oliver Williamson (2000), an important scholar of NIE, defines institutions quite narrowly as hierarchical “governance structure” focussing mainly on property-rights. Here, his definition is closer to Olson's than to North's. In contrast, the philosopher John R. Searl (2005, p. 3) describes institutions as “observer relative phenomena” that enable new sorts of power- or status-laden relationships than constrain them (ibid, p. 10). As there is such difficulty

defining institutions accurately, it can therefore be concluded that there will be difficulties in clearly attributing economic growth to particular institutions.¹⁷

4.2.2 Transaction Costs

Another one of the main rungs in North's and Olson's models is the reduction of transaction costs in the real world. This is a core element of NIE (Rutherford, 2001, p. 187). Although the term has a broad understanding, varying characteristics are ascribed to it. North bases his propositions on the work of Ronald Coase (North, 1994, p. 360).¹⁸ However, North mainly uses Coase's later concept of the importance of formal institutions, like legal systems, in transaction cost economising of market transactions (Coase, 1992, p. 717). However, North leaves out Coase's theories about 'make or buy' decisions of firms. Additionally, North's four-level analysis of transaction costs is more differentiated and less geared towards the firm than the approach of Oliver Williamson (2000, p. 599).¹⁹ In contrast, Olson (2000, p.49) defines transaction costs rather vaguely as "the costs to use a market". His differentiation between voluntary and enforced transactions is another considerable deviation from North's propositions. In addition, Olson's references to the ideas of Ronald Coase are broader, as he also considers 'make or buy' decisions of firms. For North, the existing transaction cost levels are based on cultural path dependency. Olson's propositions are similar to Williamson's view that transaction cost levels are a result of coincidence, and depend on the established formal governance structure.

Furthermore, North (1994, p. 364) excludes the so-called Coase Theorem of economising transaction costs by efficient self-regulating private markets. He considers them as inferior in a modern world of impersonal exchange in a specialised world (*ibid*). This is in line with Olson (2000, p. 58), who also rejects the Coase Theorem. He argues that this concept is based on the logic of voluntary transactions and implies that a country is always already at its Pareto-efficient transaction cost level (*ibid*). As well as transaction costs, North's more recent analysis also considers transaction benefits through bargaining, although he does not explicitly address this term (Kesting, forthcoming, p. 9). For instance, North's interactive learning process allows the easing of human interaction and a lowering of transaction costs through communication and

¹⁷ For the sake of clarity, I will use North's definition and differentiation of informal and formal institutions throughout the dissertation if not otherwise stated.

¹⁸ In 1991 Coase was awarded the Nobel Prize in Economics "for his discovery and clarification of the significance of transaction costs and property rights for the institutional structure and functioning of the economy" (Nobel Foundation, 1991).

¹⁹ see Chapter 2.2 of this dissertation

sharing a common belief-system. This is in contrast to Oliver Williamson, who regards bargaining only as a transaction cost (ibid). Therefore, in this instance North's point of view is similar to Olson's (2000, p. 55), who attacks the traditional view that markets are automatically in their most efficient of all possible worlds. Moreover, Olson (2000, p. 76) also considers communication as a crucial component in achieving transaction benefits, which he calls *collective goods*.

Similar to Steven Cheung (1998, p. 516), North compares transaction costs more on a relative basis to avoid potential measurement problems. Mancur Olson (2000) has a contrary view, and claims that his findings in his book are heavily supported by measurable empirical evidence.²⁰ Hence, Olson's standpoint is similar to Oliver Williamson's (2000, p. 605), who measures transaction costs in absolute terms and calls research on transaction costs an "empirical success story." However, other research has shown that Olson's suggested differences in selective incentives do not explain success differentials (David & Han, 2004, p. 52; McLean, 2000, p. 656). For instance, Olson's 'sclerotic' Britain and US have grown faster in recent times than the 'less lobbying daunted' Japan (McLean, 2000, p. 659). Furthermore, the empirical evidence of economic growth is inconclusive about autocracies and democracies, and sequence of democracy and growth (ibid, p. 660). Therefore, it might be difficult to find reliable measures, either on an absolute or on a relative basis, for attributing economic growth to particular transaction costs levels.

4.2.3 Property Rights

The establishment of efficient individual property rights systems is a central cornerstone within the theories of both scholars (North, 1994, p. 361; Olson, 1996, p. 22). This element is also a key characteristic of the NIE (Rutherford, 2001, p. 187). North follows the "internalising of externalities approach" of Harold Demsetz (1967, p. 348). Olson (2000, p. 42) defines them as "... individual rights that involve things that may be bought and sold." Olson has a broader definition of the term than North, as he also includes contract rights in his cornerstone (ibid). In accordance with Ha-Joon Chang's (2005) propositions, North's and Olson's central property rights would consist of a complex, almost non-transparent set of different institutions. Additionally, they would contain more than just the private property sphere as explained by North and Olson; and

²⁰ For instance: Olson, 2000, p. 80 for his theory of collective action; p. 43 for the relationship between length of democracy and security of property rights; p. 23 for the advantage of super encompassing majorities; and p. 99 for impressive economic growth under autocratic regimes

violating them could result in economic growth (ibid). However, neither scholar includes a more detailed discussion about corporatist private property rights, or communal and state ownership in their work. This may be because the latter two forms of property rights may be seen as inferior by them. Hence, Olson's theory of the provision of public goods should demand a more thorough analysis of other forms of property rights. Moreover, although North and Olson see property rights as complex multi-layered schemes, neither academic addresses the different layers directly. This leads to the question: how would efficient property rights be created in the sense of North and Olson? Since their definitions are vague, it is difficult to examine the differences in different property rights systems.

4.2.4 Rationality

North (1994, p. 362) has incorporated the work of Herbert Simon about individuals with bounded rationalities.²¹ This concept is now widely used by scholars of NIE (Rutherford, 2001, p 187). However, North does not provide a detailed and systematic empirical study in his literature, as demanded by Simon, to distinguish himself from 'ad-hoc' deviations from neoclassical theory (Simon, 1998, p. 267). On the other hand, Olson (2000, p. 70) does not refer to Herbert Simon's work at all, but rather describes human beings as "rational individuals." Therefore, his idea about opportunistic individuals is close to standard economics. It can be concluded that both scholars diverge substantially in their rationality assumptions, and, hence, it makes it more complex to evaluate the reasoning for policy decisions made by New Zealand and Argentina.

4.2.5 Individuals and Groups

Both North and Olson focus on group interactions and their underlying foundations. Olson's (2000, p. 70) theory of collective actions may be comparable, to a certain extent, to North's idea of personal or impersonal markets with communication as the main tool for exchanging ideas. Olson's collective actions are concerned with the differences of an individual's opportunistic behaviour in small and large groups (ibid, p. 87). The outcome of the collective actions, depending on the group size, differs substantially from the neoclassical school (ibid, p. 70). However, Olson's propositions

²¹ In 1978 Herbert Simon received the Nobel Prize in Economics "... for his pioneering research into the decision-making process within economic organizations" (Nobel Foundation, 1974).

require leaving out long-term repeated bargaining, and other motives of individuals; for example trust.

On the other hand, North (1994,, 2005b) frequently refers to Friedrich A. Hayek,²² who provides *collective learning* as a further piece in North's scaffolding. However, Hayek and the so-called Austrian School consider further sources of learning, like entrepreneurs; which are clearly suppressed by North in favour of his culture heritage hypothesis (Nooteboom, 1999, p. 128). For instance, North assumes that the national level of entrepreneurial spirit depends on the prevailing culture, is set constant, or is not a major economic growth determinant. Additionally, as an economist, North lacks the understanding of cognitive science, and, hence, his analyses for the collective learning hypothesis remain rather shallow about brain models (Voigt, 2006, p. 312). Furthermore, North uses the concept of path dependency to allow collective learning to develop incrementally over time. This concept finds its origins in OIE, and Thorstein Veblen's theory of "cumulative causation" with its notion of possible multiple futures (Hodgson, 2001a, p. 69). This again represents a substantial deviation of North from neoclassical theory; which, in contrast, remains the basis of his scaffolding.

Therefore, it can be concluded that North's and Olson's propositions about the foundations of group behaviour vary considerably. North's theory deals with changing interaction among groups over time, while Olson puts his emphasis on the opportunistic individuals without any changes through time.

4.2.6 Summary

The analysis of the key terms of both scholars reveals that North's approach is generally wider-spread, and less well-specified than that of other renowned scholars from a variety of academic disciplines. This might allow North to account for actual economic history more comprehensively. On the other hand, Olson's definitions appear more simplistic and less dependent on other academics' work. Hence, this could provide a denser basis for describing economic history. However, the absence of clear definitions makes it more difficult to address particular economic growth determinants.

²² In 1974 Friedrich A. Hayek shared the Nobel Prize in Economics with Gunnar Myrdal "for their pioneering work in the theory of money and economic fluctuations and for their penetrating analysis of the interdependence of economic, social and institutional phenomena" (Nobel Foundation, 1978).

Table 6: Summary of Differences in Key Terms

	North's Theory	Olson's Theory
Institutions	Rules of the game	Incentives
Transaction Costs	4 level transaction cost model	Costs of using the markets
Property Rights	Individual property rights	Individual property and contract rights
Rationality	Bounded rationality of Herbert Simon	Rational individuals in the neoclassical sense
Individuals and Groups	Collective learning	Collective action

4.3 Critical Evaluation of the Main Hypotheses

In his Nobel lecture, North (1994, p. 365) states that his scaffolding is suitable to explain world economic growth patterns for at least the last 200 years. Olson (2000, p. xxv) argues that he provides the answers to the puzzle of "... why there are innumerable markets in almost every society, yet riches in only a few". These are ambitious claims. Therefore, their main hypotheses will be examined to clarify the underlying reasoning and possible limitations.

4.3.1 Role of the State

Both scholars put the state at the centre of their institutional analyses. Geoffrey Hodgson (2001a, p. 77) agrees also on the continuing relevance of the state, despite the process of globalisation. However, North (1994, p. 366) regards the state as the sole source for defining and enforcing property rights. Similar to North's framework, Olson (2000, p. 1) emphasises proper formal incentives as the main sources for modern economic growth. They provide the basis for specialisation and trade, and, therefore, for rising production and cooperation. Thus, Olson also overstates and over-romanticises the role of government as the sole and outstanding source of power, and the main determinant of economic growth (McLean, 2000, p. 667). Additionally, he does not explain how to fulfil the requirements for a successful economic policy (Higges, 2001, p. 357). In contrast, Ronaldo Fiani (2004) insists, that the state is not the only single national power, and that it is integrated in the world by economic and political means. Furthermore, North's and Olson's models do not address multinational corporations, supranational organisations or non-governmental organisations (NGO's), and their influence in shaping economic outcomes (McLean, 2000, p. 667). In the case of Olson, large organisations and (international) collective actions still come into existence even without selective incentives (Higges, 2001, p. 361). Moreover, Olson's rosy picture of

the role of state does not account for the potential for governmentally initiated crime, and for the fact that crime-preventing social norms can exist even in anarchy (ibid). In addition, Olson does not explain why are there millions of people employed in the private sector to secure property rights in the US (ibid, p. 362).

By assigning the central role to the state, North and Olson mute differences in religions, either on a formal or informal basis, in their analyses. For instance, North (2005b, p. 135) addresses the work of Max Weber, who coined the idea of economic incentive differentials through religions. According to Weber, the economic development of countries based on the British model may have benefited from Protestantism. On the other side, countries based on the Spanish model may have suffered from Catholicism. Surprisingly, North (2005b, p. 137) does not clearly examine possible key differences between these two religions and their influences on his cultural heritage hypothesis. Rather he argues that the learning processes of both Christian belief systems share many more commonalities than differences in filtering information (ibid). Olson's (2000, p. 37) discussion on the influence of religion is also very limited. He only mentions British Protestantism during the 17th century briefly to show that the equal distribution of power among competing groups paralysed all economic forces until they were united again. In contrast to both scholars, propositions regarding the power of religion are still controversially discussed in academic science (Greasley & Oxley, 2000, p. 175).

North's and Olson's emphases on the role of the state also put national factor endowments as major sources for economic growth on hold (North, 1994, p. 364; Olson, 1996, p. 19). Therefore, they present antithetic theories to the Heckscher-Ohlin (HO) Theorem that considers country-specific relative factor endowments as key determinants for the national economic development (Jones, 1998). The key assumptions of the HO Theorem are free commodity trade; pure competition; constant returns to scale; and internationally immobile, perfectly inelastic productive factors. Relative factor abundance is measured by the ratio of labour to land, including all natural resources, of one country, to the corresponding ratio abroad, *ceteris paribus*. Hence, a country will export products which they can make relative intensive use of their relative abundant factors for (ibid). Furthermore, Feinstein (1999) has shown that the main receipts of the leading economies of the world have changed dramatically from agricultural products, to industrial products, to service-oriented products accompanied by rising capital intensity over the last century. Hence, national natural factor

endowments and their employment may be more important to their economic success than suggested by the two scholars.

4.3.2 Cultural Heritage

Another major point of critique is North's path-dependent cultural heritage hypothesis. By holding traditional factor endowments constant, North may want to show that the culturally-inherited belief system is the key determinant of a nation's ability to exploit its own growth potential (*ceteris paribus*). However, North's framework implies the existence of exogenous, unidirectional informal institutions; which are slowly receptive to their respective environment (Engerman & Sokoloff, 2005, p. 646). With accelerating modern economic growth and growing impersonal markets, informal institutions, like traditions, might provide much less guidance for the future and, hence, lose much of their importance (Fiori, 2002, p. 1032). Consequently, the links of culture to formal institutions weaken considerably. To fill the gap, the importance of formal rules, to reduce uncertainty, increases. In other words, with the "acceleration of historical experience" traditional mental models might lose their ability to predict correct responses to economic change (Fiori, 2002, p. 1036). Consequently, North's ex-post justifications do not consider the possibilities of dramatic changes in cultures, or of bidirectional influence of cultures, and the economic outcomes (Chang, 2005; Engerman & Sokoloff, 2005, p. 662). Moreover, the cultural heritage hypothesis plays down the possibility of major changes in incentive structures through locally-induced learning (Engerman & Sokoloff, 2005, p. 650). Here, Engerman and Sokoloff (2005, p. 654) reject North's single-source hypothesis, and present climate and natural endowments as important factors on modifying pre-existing institutions in the colonial Americas. As they argue, through institutional imitation, adaptation, as well as innovation, these colonies of different super powers were more equal with each other than with their ruling interest (*ibid*).

In sharp contrast to North, Olson (1996, p. 19) denies the existence of a path dependent cultural heritage hypothesis. Olson (2000) concludes that democracy in Britain and the US emerged coincidentally as an accident of history. Hence, his model presents North's culturally path-dependent 'democratic culture' link between Britain and the US, and other former dominions, in a substantial different light (*ibid*, p. 37). Therefore, Olson's reasoning can be seen as a crucial antithesis to North's propositions. He refers to country-specific institutions and economic policy as the single main source for differences in the wealth of nations (*ibid*). Unfortunately, Olson's detailed concept

of encompassing interest groups in a democracy is not matched by an appropriate explanation why, for example, the ‘elective dictatorships’ of Argentina and NZ might have been able to destroy existing lobbying structures in the 1980s (McLean, 2000, p. 664). However, by rejecting culture as major economic determinant of the divided post-WWII Germany, Olson does not consider the fact that, over the long-run, both German countries could have been heavily influenced by the antithetic ideologies of the US and the Soviet Union (Engerman & Sokoloff, 2005, p. 646).

Other scholars discuss this topic too. Geoffrey Hodgson (2001a, p. 75) shares North’s notion of the importance of culture in shaping economic outcomes to a certain extent. Nevertheless, Hodgson (2001a, p. 71-72) maintains a more cautious view, the Impurity Principle, where an “... economic system must rely on at least one structurally dissimilar subsystem to function”. Hence, an economic system never appears in its pure form since it also needs antithetic institutions to work over time (ibid, p. 72). Therefore, the British model might share some Spanish institutions, and vice versa. As well, in Hodgson’s opinion, existing economies are also substantially influenced by local circumstances (ibid). Thus, formal institutions, instead of being fully explained by their functions alone, might be effective in one context, but harmful in another (ibid, p. 73). On the other hand, Hodgson’s Principle of Dominance, where the vast majority of production takes place within institutions of a certain-type, builds a bridge back to North’s model (ibid, p. 75). Chang’s (2005) work provides further examples, and concludes that one institution can produce more than one outcome: Indeed, different institutions can produce the same outcomes, and lastly, different institutions in different societies may achieve the same outcome (ibid).

It can be concluded that North and Olson differ substantially in their perceptions of the influence of culture on economic growth. This will be a key issue in evaluating New Zealand’s and Argentina’s recent economic history.

4.3.3 Historical Specificity

Douglass North and Mancur Olson want to provide economic theories, which are able to account for actual economic histories.

Both scholars share the commonality of using real world examples as ‘ideal-types’ for the development of their theories, and, hence, share also similar critique. Provisionally categorised, but incomplete, pure ‘ideal-types’, a widely used term since being introduced mainly by the work of Max Weber and John R. Commons, shall allow constructing prior abstract theoretical concepts to guide the understanding of complex

socio-economic realities by further empirical investigations (Hodgson, 2001b). However, ideal-types are only means, not ends, of theory developing; with a constant need of adjustment, that imposes a priority conflict of theory over data (ibid, p. 170). Furthermore, the concept misses an underlying framework to construct adequate ideal types, and their criteria of success; and is based on a vague, neoclassical definition of rationality (ibid, p. 126). These weaknesses have to be considered, when evaluating the explanatory power of North's and Olson's theories.

North's dichotomy of the British and the Spanish model is an implicit two-point 'black-or-white' model, or 'success-or-failure' ideal-type approach to institutional systems. This assumes a kind of 'check list' for institutions that will result in particular economic growth outcomes (Chang, 2005, p. 3; Engerman & Sokoloff, 2005). Furthermore, North's framework focuses almost exclusively on the description of the development of the Western World, especially of the UK and the US, and is based on too many stylised facts. Hence, North's British and Spanish Models might be storytelling on one side, but are too imprecise when it is applied to specific economic histories on the other side (McCloskey, 1994, p. 165). Olson's propositions have to face similar criticisms as well. Olson (2000, p. xxviii) mainly bases his analyses of autocracies on the rise and decline of the Soviet Union, but then transfers the outcomes one-to-one to all former communist countries, or other nations under a recent dictatorship. Furthermore, his analyses of the communist's failures are not combined with an in-depth evaluation of success stories.

In other words, North's and Olson's theories are developed ex-post in a period of time, when American capitalism appeared to be ideal (Hodgson, 2001b, p. 32). Consequently, North's and Olson's samples of ideal-types are biased, and lack an adequate theoretical grounding. Especially North leaves out the possibility that other institutional models may be capable of consistently outperform the British model in other circumstances (ibid). For instance, North does not explain the reasons for the rapid rise of a post-war success story like Japan, its consequent inability to adapt to economic changes in the 1990s, and its resurrection in recent times (Crafts, 1999, p. 28). In contrast, Olson (2000, p. 13) is more cautious about success or failure than North, and allows rapid and long-lasting economic growth, especially under the rule of well-established autocracies.

Additionally, North's and Olson's deductive reasoning shrinks history to short paragraphs to illustrate rather than further substantiate their models (Vandenberg, 2002, p. 229). For instance, North and Olson always refer to short time periods out of various

samples of different nations, for example, from the Roman Empire, to the traders in ancient Italy, to industrial Britain. Then, both scholars rearrange their puzzle pieces to fit them into their individual theories. Finally, North (1994, p. 364) states that the outcomes of his analyses hold for any definition of economic performance. However, North usually relies on GDP data series rather than using alternative measures like life expectancy, literacy rates or others (Astorga et al., 2005, p. 765). Here, Olson's approach of using almost exclusively GDP figures shares the same shortcomings.

Summarised, North, and, to a lesser extent, Olson, run the risk to expose themselves to the same characteristic weakness of neoclassical economics of lacking historical specificity, because they almost exclusively focus on the commonalities within each of their British or Spanish models, and forget the differences to other institutional models (Hodgson, 2001b, p. 29). By utilising the aforementioned 'black and white' term, it can be concluded, North's theory does not include 'greys' because of contingencies in the development of institutions, when different institutional systems interact with or influence each other. Considering the ideas other scholars like Chang, the relationship between institutions and economic performance may be more complicated than presented by North and Olson. Hence, although they want to provide generally applicable models to explain long-term real-world economic history, they remain surprisingly ahistorical (Vandenberg, 2002, p. 229).

4.3.4 Summary

A summary of the two different theories is given in Table 7:

Table 7: Summary of Differences in the Main Hypotheses

	North's Theory	Olson's Theory
Basis	National incentive structure	National incentive structure
Full Utilisation of Productive Potential	No	No
Key Determinants for Economic Growth	The state as based on common belief systems/ informal institutions	The state as based on national formal institutions and organisations
Political Spectrum and Hierarchy	Consensual Political Order Authoritarian Political Order	Democracy Autocracy Anarchy
Importance of Religion	No	No
Importance of National Factor Endowments	No	No
Cultural Heritage	Yes	No
Establishment of Democracy	Path-dependent	'Accident of history'
Ideal-Type British Model	Democracy Adaptive efficiency Impersonal markets Cooperative mental model Rule of law Well-defined property rights	Democracy (autocracy) Institutional sclerosis over time Trend to personal markets Lobbying Rule of law Well-defined property rights
Ideal-Type Spanish Model	Autocracy Adaptive inefficiency Personal markets (corruption) Ill-defined property rights	Autocracy (democracy) Market-contrary economic policy Break up of personal markets Ill-defined property rights

Olson (2000, p. 130) states that “(m)ore than one theory can, however, be consistent with the historical facts and also meaningful, so we must ask what implications of the theory offered would expose it to further testing.” This shall be the task of the following chapter. North's concepts for establishing prosperous economies are also examined in more detail. This shall be accompanied by an in-depth look at Mancur Olson's prescriptions to economies in transition. Based on these analyses suitable proxies for empirical tests shall be presented.

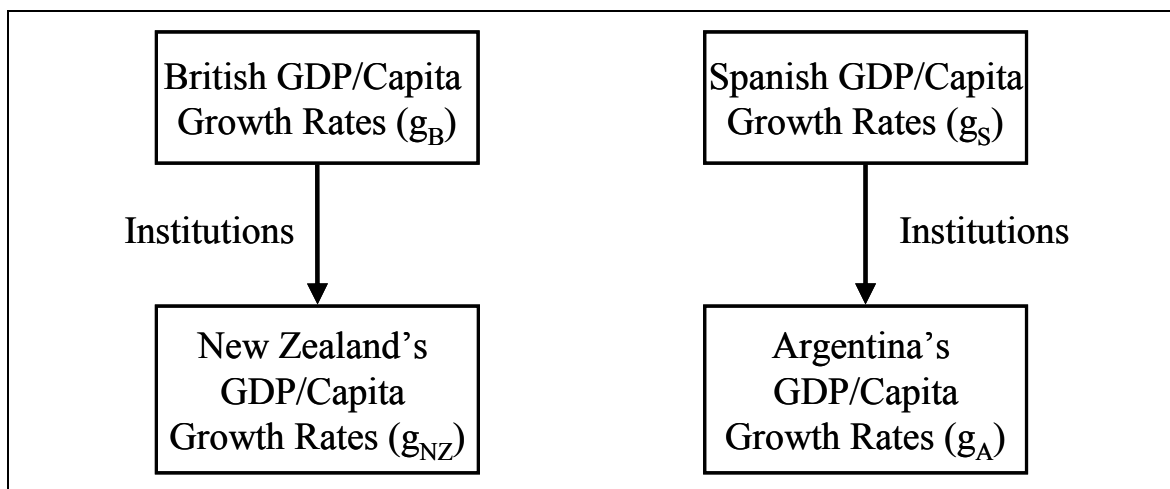
5. The Conceptual Framework

North and Olson consider country-specific political and economic institutions as the main determinants for economic growth (North, 1994, p. 359; Olson, 1996, p. 19). The validity of their propositions shall be reassessed by the evaluation of selected determinants of the political and economic markets of New Zealand and Argentina. Therefore, in this chapter a conceptual framework is developed based on the cultural framework of Douglass North as presented in Chapter 2.4 and the formal institutions framework of Mancur Olson as presented in Chapter 3.4. In contrast to just applying North's or Olson's usual top-level GDP growth comparisons, far more country-specific data shall be analysed to gain further insights of country-specific success or failure determinants. Additionally, North's (2005b) perceptions about how sustained economic growth is to be achieved will be based on Chapter 12, *Improving Economic Performance*. In addition, Chapter 10, *The Kind of Markets needed for Prosperity*, from Mancur Olson's (2000) book, *Power and Prosperity*, will be used to further refine the research agenda of the dissertation.

5.1 Overview

Due to North's (1994, p. 364) cultural heritage hypothesis, New Zealand, as a former British colony, should have experienced higher economic growth rates than Argentina, a former Spanish colony (*ceteris paribus*). A graphical representation of this relationship is given in Figure 5.

Figure 5: Common Culture and Economic Growth



The following assumptions underpin the graphic model:

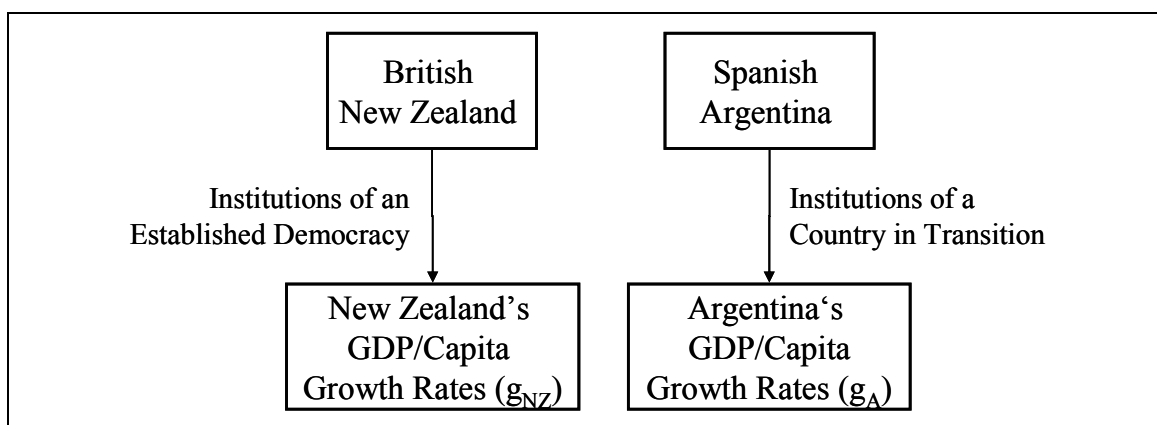
1. The British and Spanish models are ideal-types.
2. The transfer of institutions to colonies occurs on a one-to-one basis.
3. These long-lasting relationships will evolve (*ceteris paribus*):²³

$$\text{I. } g_B \approx g_{NZ}$$

$$\text{II. } g_{NZ} > g_A.$$

On the other hand, Olson's country-specific economic policy hypothesis provides a similar scenario for the economic development of New Zealand and Argentina after the economic reforms. In his opinion, New Zealand, as a long-standing democracy based on the British model, should have experienced higher economic growth rates than Spanish Argentina, because the latter had to face difficulties as an economy in transition to democracy. A graphical representation of these relationships is given in Figure 6.

Figure 6: Political System and Economic Growth



The following assumptions underpin the graphic model:

1. New Zealand's institutional structure conforms to an ideal-type established democracy; and Argentina's institutional structure conforms to ideal-type country in transition.
2. New Zealand's and Argentina's economic potentials are identical.
3. This long-lasting relationship will evolve (*ceteris paribus*):

$$\text{I. } g_{NZ} > g_A$$

New Zealand might have suffered from an institutional sclerosis, because it is one of the oldest established democracies of the world (Olson, 1996, p. 20; Jackson, 1998, p. 491). Economic growth rates would be distorted by high levels of vested interests in *political* and *economic markets*. For the sake of clarity, this special case is set aside here for a moment.

²³ Where g = average annual GDP per capita growth rates.

5.2 Political Markets

For North (2005b, p. 158) to be economically successful, an ideal-type consensual political model has to be implemented, which consists of:

1. “an institutional matrix that produces a set of organisations and establishes a set of rights and privileges;
2. a stable structure of exchange relationships in both political and economic markets;
3. an underlying structure that credibly commits the state to a set of political rules and enforcement that protects organisations and exchange relationships;
4. conformity as a result of some mixture of norm internalisation and coercive enforcement.”

Consequently, this ideal-type consensual political model shall provide the general nutritious soil for well-defined property rights as the very basis for an effective price system (ibid). Therefore, key political players have to be willing and able to implement the institutional change and to establish effective means of enforcement (ibid, p. 164). Olson (2000, p. 187) also addresses a political system ensuring individual property and contractual rights as a fundamental prerequisite. He argues that the better they are developed and enforced through impartial courts, the more sophisticated and comprehensive are the transactions in socially contrived markets, and, hence, the higher the per-capita income of a country (ibid).

In addition to ideal-type consensual political markets, North (2005b, p. 160) emphasises the importance of maintaining and enforcing political, and economic, diversity. For instance, successful economic policy has to break up personal exchange of rent seeking personal interest groups, like monopolies, corruption, or targeted spending. Hence, his emphasis on diversity provides the opportunity for ‘trial and error’ by testing alternative policies, as well as for restraining unsuccessful paths, and, thus, for developing adaptive efficiency (ibid, p. 163). Again, Olson shares similar ideas about maintaining diversity. He insists that, because of prevailing uncertainty, the best situation for an economy is when many entrepreneurs can try different paths, and experience entrepreneurial luck and failure (Olson, 2000, p. 189).

Moreover, successful economies should be characterised by their appropriate *fiscal* policy and *monetary policies*. North (1994) does not address these terms directly, but wrap them in his general expression “economic policy”. On the other hand, Olson (2000, p. 119) argues that differentiated fiscal incentives are necessary to stimulate growth. Moreover, good monetary and fiscal policy should keep price stability and

governmental spending in check, as well as avoid under-taxation of its economy (ibid, p. 158).

In addition to the aforementioned points, North (2005b, p. 163) maintains that not just the political markets and their level of diversity but also the cultural heritage has to be taken into account for a successful ‘doable’ institutional change. Hence, instead of a comprehensive, all at once going free market, a variety of governmental interventions – with all the caveats necessary for their termination over time – should have been essential in the short run to be competitive (ibid). In other words, the development of a full matrix of necessary institutions should have taken time and varying governmental interventions for New Zealand and Argentina. Otherwise, an over-night policy shift would harm less competitive countries considerably through the free access of already highly efficient competitors from more advanced countries.

Finally, the influences of external policy advices on the political and economic outcomes will be evaluated. This is based on North’s (2005b, p. 161) propositions, which see long-term investments in political skills from external sources, like non-governmental sources, as pure necessity to create a diversified, growth-fostering consensual, political system in a developing country.

5.3 Economic Markets

In addition to efficient political markets, North (2005b, p. 158) maintains the crucial necessity of specific incentives to promote low-cost transacting in particular factor and product markets. Reducing country-specific obstacles for lower transaction costs would enable the production of a variety of new goods and services (ibid, p. 163). Moreover, the incentive structures have to be realigned over time to account for changes in the environment. Thus, North (2005b, p. 159) country-specific means to lower transaction costs in specific markets are:

1. “the development of a uniform system of weights and measures, technological research for better measurement, and improved specification of property rights;
2. the creation of an effective judicial system to reduce the costs of contract enforcement;
3. the development of institutions to integrate the dispersed knowledge in a society as well as to monitor and meter agreements and adjudicate disputes.”

Olson (2000, p. 174) presents similar ideas. In general, institutions are needed; otherwise a lack of competition would inevitably lead to rising personal trade in the whole economy (ibid, p. 143). Olson regards bureaucracy as a major economic obstacle,

which fosters factor misallocation (ibid, p. 137). As before, resulting large overhead costs will distort the efficiency of investments over the long-run (ibid, p. 162). However, he argues that a comprehensive institutional framework is not as important for self-enforcing markets. On the other hand, special institutions are needed for socially-contrived markets (ibid, p. 174). In other words, Olson (2000, p. 194) is convinced that the highest economic gains can only be achieved in governmentally- or socially-contrived markets. The importance of efficient economic markets, as outlined by the both scholars, can be supported by the findings of Michael E. Porter (2002). He argues that national differences in microeconomic settings account for 81% of the variation across countries in the level of GDP per capita (ibid, p. 24).

Among the different markets, Douglass North (2005b, p. 124) regards national *capital markets* as the most sensitive economic markets with constant need for adjustment and maintenance. The importance of national capital markets is also substantiated by Mancur Olson (2000). He argues that without sophisticated capital markets a country will be restricted to trades that are self-enforcing (ibid, p. 185). Consequently, flourishing banking, insurance, and capital markets are only found in stable democracies (ibid, p. 99). However, an extensive legal system and stable political order have to be maintained to provide these markets, and to lower the cost of capital considerably (ibid, p. 185). The importance of the national capital markets is confirmed by Feinstein (1999). Successful economies experienced a rise in the employment of capital during the second half of the twentieth century when their production focus shifted away from agriculture towards industry and services (ibid, p. 48). Furthermore, financial and business services contributed largely to the economic growth of the leading OECD countries within this period (ibid, p.44). Hence, the dissertation will explicitly examine the development level of the capital markets of New Zealand and Argentina, and, their impact on economic growth.

In summary, the institutional setup of the levels of transaction costs, competition, and property rights influence the activity within the economic markets; and, hence, have to be assessed. Additionally, it has to be investigated to what extent the economic policy supported the capital markets of New Zealand and Argentina.

5.4 Summary

As the critical analysis has shown, further viable approaches to a more detailed examination of differences in the economic growth patterns of New Zealand and Argentina are imaginable.

Hence, the first focus of the conceptual testing environment will be on differences in the general economic growth patterns between New Zealand and Argentina. This shall allow for testing the aforementioned propositions from North and Olson in regards to their British and Spanish models.

This will be followed by the evaluation of the political markets of New Zealand and Argentina. On the constitutional level, differences in individual and property rights systems shall be examined. In addition, accompanied research on governmental structures and processes might provide ideas about their political diversity and the ability to keep rent-seeking of various interest groups in check. Moreover, studying the countries' particular fiscal as well as monetary policies should reveal further insights in their abilities to achieve their economic potentials. The influence of external events and organisations, like the International Monetary Fund (IMF) or the World Bank, shall also be examined.

The next step of the country analyses is the evaluation of the economic markets. At the beginning the different levels of transaction costs and competition in New Zealand and Argentina will be compared with each other. Furthermore, the literature review has revealed that the structure and development of national capital markets are central points of contention. North and Olson consider these markets as the most sensitive to the institutional environment.

Table 8: Conceptual Framework

Level	Determinant	British Model	Spanish Model
Overview			
	Economic Growth Rates	Higher	Lower
Political Markets			
	Property / Individual Rights	Encompassing	Selective
	Political Diversity	Pluralistic	Vested Interests
	Judicial Coercion	Independent	Not Independent
	Lobbying	Lower	Higher
	Fiscal Policy*	Disciplined; Foster Income Creation	Unrestrained; Foster Income Misallocation
	Monetary Policy*	High Price Stability Low Real Interest Rates	Low Price Stability High Real Interest Rates
	Change of Institutions+	Continuous, Incremental	Overnight; Stop-and-Go
	External Advice+	Lower	Higher
Economic Markets			
	Transaction Costs	Lower	Higher
	Competition	Higher	Lower
	Capital Markets	More developed	Less developed
	Capital Markets Protection*	Higher	Lower
	Cost of Capital*	Lower	Higher

+ Determinant mentioned in a detailed way by North only.

* Determinant mentioned in a detailed way by Olson only.

6. Research Methodology

6.1 Introduction

This chapter includes a discussion about the underlying methodology and design used to collect empirical data for the dissertation. The rationality for choosing a combined quantitative and qualitative methodology is given. This is followed by an overview over the research design and details of the modes of data collection. Finally, strengths and limitations of the chosen approach are addressed, and the necessity of an ethical approval is considered.

6.2 Research Methodology

As stated before, the purpose of the study is to evaluate the viability of North's and Olson's latest academic propositions in describing the impact of institutions on New Zealand's and Argentina's economic growth. At the beginning of the inquiry, the central research question of the dissertation from Chapter 1.4 is restated:

Can the economic growth patterns of New Zealand and Argentina of the last quarter century be explained either by Douglass North's 'cultural heritage' hypothesis or by Mancur Olson's 'country-specific economic policy' hypothesis?

The research question points to an amalgamation of history and analysis of a specific situation to raise the explanatory power of a study; which is typical for Institutional Economics (Atkinson & Oleson, 1996, p. 702). This is in contrast to neoclassical 'blackboard economics', where historically or culturally specific features do not matter; and severe simplifying impositions are applied (Hodgson, 2001b). When socio-economic systems are compared across space and time, then mere similarities or differences in parameters are not sufficient (ibid, p. 23). Hence, there is no single abstract deductive model that can be used for this study, where historic specificity counts (Hodgson, 1998, p. 168). Consequently, a comparative study of New Zealand's and Argentina's recent economic history requires the analysis of a comprehensive set of country and time specific phenomena of human interaction, and the development of hypotheses out of these observations (Atkinson & Oleson, 1996, p. 704). This shall allow describing and understanding causes, effects, and trends of human behaviour (ibid). A certain degree of simplification is needed to deal with the complexity of the data (ibid, p. 708). Thus, the conceptual framework from Chapter 5 guides the search for strategic similarities and differences between the two countries. This might result in the abstraction of some country-specific phenomena. In summary, this procedure should

lead to a tailored historical ‘case’ study of more operational value than an all embracing general theory (Hodgson, 1998, p. 170).

The concept of abduction shall be used as the research method for this study. This research method, as developed from Charles Peirce, achieves the creation of knowledge through a creative leap, a novel combination of different ideas, or the relation between them (Atkinson & Oleson, 1996, p. 704). In addition to quantitative data, also qualitative data have to be assessed to address merely quantifiable institutions, and allow for complementary results for the dissertation (Firestone, 1987, p. 16).

According to Hodgson (1998, p. 172), there will be examinations of stylised macroeconomic facts at the top level of the analyses. These country-specific data of New Zealand and Argentina will be supplemented by comparisons with data from OECD countries. They represent the richest countries worldwide; and include several proxies of North’s cultural heritage and Olson’s well-established democracy; for example, Australia, Canada, the US, as well as the UK. Following North’s and Olson’s propositions, these countries must have possessed the right institutional matrix to exploit their theoretical growth potential efficiently. This approach gains further support, if the fact is considered, that NZ’s reforms were undertaken, because of the dissatisfaction of its economic growth when compared with other OECD countries (Greasley & Oxley, 2000, p. 179). This quantitative part of the study will explain the findings primarily through objective measurement of a specific set of variables as conceived from the preceding conceptual framework (Firestone, 1987, p. 18).²⁴ However, the statistical analysis will be limited to a mean of research (Atkinson & Oleson, 1996, p. 708).

Based on these top-level evaluations, further underlying structural characteristics will be analysed by assessing further quantitative and qualitative data. However, the focus of this second research level will focus on institutions as the main units of analysis (Hodgson, 1998, p. 172). The task will be to explain the causal process, which leads to the macroeconomic outcomes, than just mere correlations between variables (ibid, p. 173). The analysis might also include references to other disciplines like politics and sociology (Hodgson, 1998, p. 173). This mainly qualitative part of the study enhances the understanding of further hard to quantify social phenomenon in regards to the informal and formal institutions (Firestone, 1987, p. 18).

²⁴ See chapter 5

6.3 Research Design

The dissertation will focus on institutions as the economic growth determinants for New Zealand and Argentina; and will use North's (1994, p. 361) differentiation between economic and political markets, as well as institutions and organisations. Although institutional analyses in general and of Douglass North in particular are concerned especially with informal institutions like habits and rules, this might be difficult to analyse. Hence, the research will focus on organisations, the players of the game, since they "reflect the opportunities provided by the institutional matrix (North, 1994, p. 361)." The indicators for testing the conceptual framework from Chapter 5 will be based on North's and Olson's propositions.

Firstly, the evaluation of differences in economic growth rates will be based on changes of real GDP per Capita data.

Secondly, political markets are examined since they present and provide formal institutions, the rules of the game (*ibid*). They are examined by the composition of the political institutions, and by the fiscal and monetary policy. This shall provide insights into the institutional setup to maintain political diversity, to enforce of property rights and to limit personal exchange. Among others, Olson (2000, p. 43) mentions that the age of a stable democracy, as well as the number of lawyers per 1,000 of population can be drawn as suitable predictors for vested interests in politics and, hence, slow economic growth. The research on social bodies will be included in this part and their interactions with political bodies. In Olson's (2000, p. 85) opinion, labour unions are the best-known type of organised interest group. Considering fiscal policy, the most promising candidates for tests are data about the governmental budget discipline, the tax-system, and income redistribution (*ibid*, p. 190). Furthermore, research on the new owners of privatised formerly state-run enterprises provides insights into the prevailing level of corruption in a country (*ibid*, p. 158). Moreover, Olson (2000, p. 158) pinpoints the quality of monetary policy down to price stability and low interest rates. In addition to that the pace of institutional change and the influence of external events and organisations on the political markets will be addressed.

Thirdly, the development of the economic markets of both countries is reviewed. Olson (2000, p. 162) mentions higher average firm sizes, or industry concentration ratios, as examples for prevailing high transaction costs in certain industries; which lead to 'make' instead of 'buy' decisions. Similarly, the quality of certain consumer goods is an indicator of the bargaining power of individuals or of the level of competition within a specific industry (*ibid*, p. 140). Because both countries are depending on foreign trade,

evaluating differences in exports of financial services should provide valuable insights. Additionally, he insists the size of informal sectors in economies as further predictor for the quality of the institutional framework (ibid, p. 179). Separately assessed are the capital markets as source of corporate financing. Olson (2000, p. 43) argues that capital flees from non-established democracies to countries with lower nominal yield, but higher face value protection. Hence, national capital flows, real interest rate levels, and the protection of capital will be examined.

In a nutshell, the quantitative and qualitative variables, as received from an extensive literature review and the access of different databases and other online resources, shall allow for the appropriate application of the conceptual framework on the economic histories (Table 9). By accessing these data it shall be investigated whether the country specific growth patterns match either North's or Olson's theory.

Table 9: Indicators for the Assessment

Level	Determinant	Indicators
Overview	Economic Growth Rates	Real GDP/Capita Growth Rates
Political Markets	Property/Individual Rights	Constitutional Protection of Civil Rights and Property Rights
	Political Diversity	Structure and Processes of the Parliament and the Government
	Judicial Coercion	Independence of the Constitutional Courts
	Lobbying	Structure and Processes of the Political Markets; Number of Lawyers; Unionisation Rates; Age of the Democracies
	Fiscal Policy	Balance of Fiscal Budgets; Incentives for Production and Saving; Tax System; Income (Re-) Distribution; Social Security Systems; New Owners of Privatised State-Run Enterprises; Crime Rates
	Monetary Policy	Price Stability; Exchange Rates
	Change of Institutions	Pace and Extent of the Implementation of the Reforms
	External Advice	Influence of External Events and Organisations like OECD, IMF and World Bank
Economic Markets	Transaction Costs	Bureaucracy as Measured by Time or Number of Procedures Required for Certain Business Transactions and for Legal Claims; Average Firm Size
	Competition	Number of Patent Registrations; Number of Businesses in a Sector; Exports of Financial Services
	Capital Markets	Size of the National Debt, and Equity Markets; Quality of Banking Products; Direction of Capital Flows
	Capital Markets Protection	Confiscation of Capital
	Cost of Capital	Interest Rates

6.4 Data Collection

The investigator of a study within Institutional Economics must begin by observing, recording, reading history and describing the situation (Atkinson & Oleson, 1996, p. 706). Therefore, documentary research will be the main way of data collection for this dissertation (Fisher, 2004, p. 135). The dissertation will be based on external secondary data; and, therefore, based on information gathered by someone other than the researcher conducting the current study (Sekaran, 2000, p. 255). The data for the dissertation will be obtained primarily through an extensive review of economic history books and articles from peer reviewed economic journals. Additionally, further publications of economic indicators, census data, statistical abstracts, media reports, and databases will be accessed. Because the comparability of the data is important, common data sources, like the World Development Indicators (WDI) of the World Bank, are preferred for the quantitative assessments. This data shall be accompanied by several country specific databases and further literature. The research for the quantitative assessment is largely determined by the conceptual framework, as developed in the preceding chapters. On the other hand, the qualitative part of the study will be more explorative by discovering commonalities in New Zealand's and Argentina's past economic policies.

6.5 Strengths and Weaknesses of the Approach Chosen

Abduction, a common research approach in Institutional Economics, avoids problems of “the mathematical-deductivist methodology of mainstream economics [that] constrains economics from realising its potential to be not only explanatorily powerful, but scientific in the sense of natural science (Tony Lawson as cited in Bush, 2004, p. 857).” The combination of quantitative and qualitative research for the study contributes to its robustness and the stability of the findings, and allows for the establishment of relationships of cause and effect (Firestone, 1987, p. 20; Hodgson, 2001b, p. 9). By using a quantitative assessment of certain key variables the magnitude of their relationships can be determined more precisely (ibid). On the other hand, qualitative research allows for the depiction of hardly quantifiable details and a portrait of the process that the two countries experienced. Furthermore, the advantages of using secondary data lie in savings in time and costs of acquiring information (Sekaran, 2000, p. 256). The development of the conceptual framework in Chapter 5 facilitates the

structuring of the research agenda for New Zealand's and Argentina's economic histories.

On the other hand, the chosen research methodology might also have its limitations and weaknesses. Firstly, the theories of North and Olson differ in certain aspects, and, therefore, there is no single consistent theory or model, which can be easily tested. The complexity of the topic makes it impossible to have total control over the direction of the research (Atkinson & Oleson, 1996, p. 710). Because of relying on a conceptual framework as derived from North's and Olson's propositions alone, there might be a selection bias towards the outcomes (Hodgson, 1998, p. 174). Consequently, this could lead to the exclusion of further important economic growth determinants of New Zealand and Argentina. Additionally, the causal relationships, as established by the qualitative data, might not provide the same outcomes as predicted by the findings of quantitative assessment. Moreover, the data, as assessed by basing the study only on secondary sources, might be obsolete or do not meet the specific needs of the particular setting (Sekaran, 2000, p. 256). The nature of a comparative empirical study also leads to the need of prior classifications and accessing different data sources; which might hinder direct comparability (Hodgson, 2001b, p. 9). Missing data can be another weakness of the study, especially in the case of assessing internal secondary data. Incorporating them into the study could provide more insights on the processes of economic policies and the underlying mental models of the political decision makers. Lastly, there are limits in measuring certain criteria, like property rights, on a quantitative as well as on a qualitative basis.

6.6 The Issue of Ethics

Ethics in business research refers to a code of conduct or expected societal norm of behaviour while conducting research (Sekaran, 2000, p. 17). However, the study will not be based on primary data involving human participants or internal secondary data. Consequently, this dissertation does not need ethical approval from the Auckland University of Technology Ethics Committee as it was written in the research proposal. Additionally, since only publicly accessible data are used for the study, the results of the dissertation are not confidential.

7. Assessment of the Economic Growth Rates

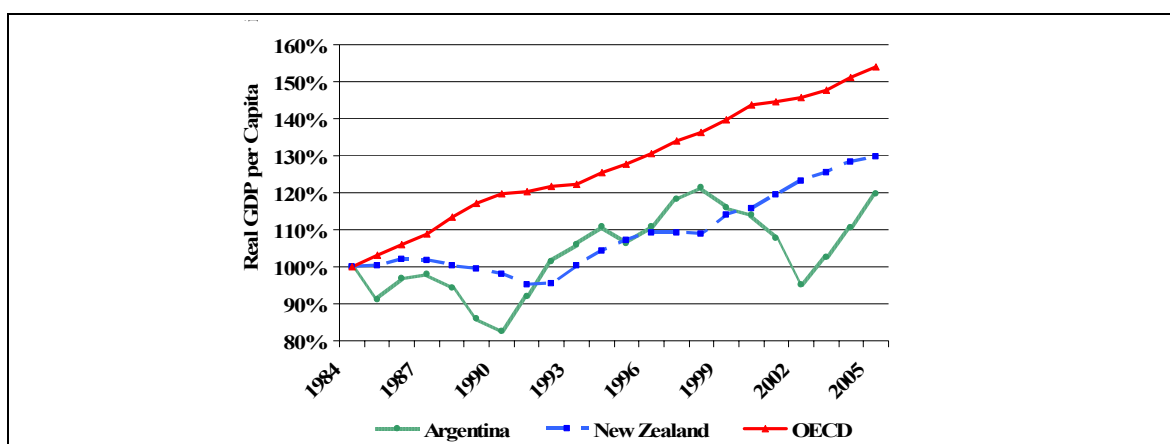
7.1 Introduction

Capital outflows caused by bad economic outlooks and subsequent exchange crises led to institutional crises in both New Zealand and Argentina at the beginning of the 1980s (Evans et al., 1996, p. 1860; Sanz-Villarroya, 2005, p. 445). In contrast to North's 'black-or-white' models, both New Zealand and Argentina showed a staggeringly rapid and comprehensive adoption of new, and quite similar, institutions. In July 1984, the Fourth Labour Government, with David Lange as the Prime Minister, came into power in NZ (Belich, 2001, p. 405). However, the government's economic policy was largely determined by the Treasury, and its head, Finance Minister Roger Douglass, until 1988 (ibid).²⁵ Although being introduced by the leftwing Labour party, his laissez-faire, often called "New Right Revolution" deregulated the economy almost overnight towards one of the most liberal free market economies within the OECD (Evans et al., 1996, p. 1856; Easton, 1997, p. 38). The response of Argentina was even more substantial by a reversal of its political system towards democracy in 1982/1983 (Lewis, 2003, p. 24). Similar to NZ, comprehensive neo-liberal economic policies were established, with the introduction of the Austral Plan in June 1985 among the most prominent policy pieces (ibid).

7.2 Economic Growth Rates

According to Douglass North and Mancur Olson, New Zealand should have shown a higher growth in real GDP per capita than Argentina from 1984 onwards. This is examined in Figure 7.

Figure 7: Economic Growth Rates



Source: The World Bank (2007), *World Development Indicators*; Based on USD at year 2000 prices; 1984 = 100

²⁵ See Chapter 8.1.1

Both New Zealand and Argentina experienced flat or negative economic growth rates until the early 1990's, when they experienced their 'lost decade' (Dalziel, 2002, p. 37; Kydland & Zarazaga, 2003, p. 3). Conversely, both economies saw staggering development during the 1990s, even with Argentina's out-performance over NZ. While NZ's path of growth continued, Argentina had to cope with a severe economic crisis at the beginning of the new millennium, but it recovered in a comparatively short time. Nevertheless, both economies could not keep pace with the economic growth of other OECD countries.

Taking these facts into account, the promises of flourishing economies based on the economic reforms in both countries have not been fulfilled as predicted (Dalziel, 2002, p. 28; Sanz-Villarroya, 2005, p. 452). Although New Zealand is still one of the OECD countries of the world, it has failed to remain in the "British Dominions Club" when based on national GDP per capita data (Greasley & Oxley, 2000, p. 185; Easton, 1997, p. 13). In 2005, New Zealand's GDP per capita rank was 27th in the world, and Argentina's was 123rd respectively (OECD, 2005). Thus, Argentina is now undoubtedly in the lower ranks of the income charts.

Based on North's and Olson's propositions the following first conclusions can be drawn after considering these key macroeconomic variables (Table 10).

Table 10: Comparison between Predicted and Actual Economic Outcomes

Theory	Theory	Reality
Douglass North	I. $g_B \approx g_{NZ}$	I. $g_B > g_{NZ}$
	II. $g_{NZ} > g_A$	II. $g_{NZ} > g_A$
Mancur Olson	I. $g_{NZ} > g_A$	I. $g_{NZ} > g_A$

Where g = average annual GDP per capita growth rates

North's predictions fail in the case of relation I. In other words, his culture heritage hypothesis may not explain why New Zealand fell well behind other success stories of the British model immediately after the start of its economic reforms. On the other hand, Douglass North's propositions seem to hold for relation II over the long-run. However, Argentina experienced higher economic growth rates for eleven out of the 22 years under consideration; despite being a volatile development process. The assessment indicates that North's theory provides some reasons for economic growth differentials between New Zealand and Argentina, but does not account for the full

story. In the case of Olson, similar conclusions can be drawn. Relation I of Mancur Olson's propositions holds. New Zealand's persistent lower economic dynamism throughout the 1980s and Argentina's better economic development through the 1990s also show the inconsistencies of Olson's British and Spanish models.

7.3 Summary

In general, North's and Olson's propositions hold to a great extent, when both countries are compared just with each other over the long run. This is not the case for sub-periods, and with comparisons to the real world example of the OECD countries. Apparently, the anomalies of New Zealand and Argentina, as discovered in the assessment of changes in GDP per capita data, point to a gap within each of the ideal-type models of North and Olson. Both economies have shared more similarities than suggested by the arguments of both scholars. New Zealand's economic development after the reforms exhibits periods of slow growth, like they are characteristic of the Spanish model. On the other hand, Argentina may award itself a 'New Zealand-ish' or 'British' touch for its periods of high economic growth rates. Using Olson's terminology, New Zealand showed characteristics of a long-established democracy tending towards sclerosis. Argentina is one of these 'in between cases' as well. The assessment provides evidence for its successful economic policy and also for its mal-adaptation to economic change. Therefore, both economies must have missed important elements to fully exploit their production potential during this period. The reasons for their underperformance might be found in their country-specific political and economic markets, which are discussed in the following chapters.

Table 11: Assessment of the Economic Growth Rates

Theory	New Zealand	Argentina
North	+ Average GDP per capita growth rates are higher. - Does not hold for extended sub-periods and in comparison to OECD.	+ Average GDP per capita growth rates are lower. - Does not hold for extended sub-periods in comparison to NZ and OECD.
Olson	+ Average GDP per capita growth rates are higher. - Does not hold for extended sub-periods in comparison to Argentina.	+ Average GDP per capita growth rates are lower. - Does not hold for extended sub-periods and in comparison to OECD.

Where: '+' = According to the scholar's theory; '-' = In contrast to the scholar's theory

8. Assessment of the Political Markets

Douglass North (1994, p. 366) and Mancur Olson (1997, p. 19) stress the role of the state as main determinant of national economic growth patterns. The individual economic policies, based either on cultural heritage, or on specific formal institutions, are held responsible for economic success or failure. In other words, the study of New Zealand's and Argentina's political markets, their structures and processes, their fiscal policies, as well as their monetary policies, should reveal further insights about their economic histories.

8.1 Political Structures and Processes

New Zealand is a parliamentary constitutional monarchy as established through the New Zealand Constitution Act of 1852 by Britain (Jackson, 1998, p. 491). Furthermore, similar to the UK, no formal constitution exists; the British Common Law, including the principles and rules of equity, the Magna Carta, the Bill of Rights, the Act of Settlement, and an independent judiciary provide the basis for NZ's government (ibid, p. 492). Finally, the Governor General represents the British monarch, who continues to be the head of the country (ibid). On the other hand, after being a Spanish colony Argentina's parliamentary democracy was established on the 1st of May, 1853, and was interrupted six times in the last century by several military regimes (Ladmann, 1998, p. 16). However, in 1983, civil and political rights, as anchored within its written constitution, were restored (Lewis, 2003, p. 34). During the economic crisis in 2001/2002, public protest led to political unrest, but did not destroy democracy itself as had happened in the past (Armony & Armony, 2005, p. 49).

At the first glance, New Zealand's informal and formal political institutions seem to prove Douglass North's cultural hypothesis. In the case of Mancur Olson, the further facts that NZ is one of the nine oldest democracies in the world, and has universal and direct suffrage, attributes itself to one of the so-defined well-established systems of ruling majorities (Jackson, 1998, p. 491). In the case of Argentina, the facts lead to the conclusion that it is a newly established democracy with a long, hard to overcome Spanish background, in the sense of North, and a country in transition from an autocratic background, in the sense of Olson. Because of the ascribed central role of the state and the inconsistencies as discovered in Chapter 7 more detailed research on the prevailing political structure and historical procedures follow.

8.1.1 New Zealand

This first affirmative assessment in regards to both theories gets leaks if considered in a more detailed way. For instance, other typical democratic elements are heavily muted in the case of New Zealand. Its supreme and sole legislature on any political matter, the House of Representatives, can control its own major constraining powers, which is unique among the British democracies (Jackson, 1998, p. 492). A Member of Parliament's (MP's) rights of individual voting is, in the most cases, constrained by the party caucus (ibid, p. 499). Although the simple plurality electoral system, which allowed an elected majority to have almost unlimited power through its triennial term, was replaced by a proportional representation system in 1996, the remaining high degree of cohesion under the system of two dominating parties has further weakened the role of the legislature (ibid, p. 496). Due to its right to reject members' bills, the government is the single main law-making agency (ibid, p. 494). The government's majority limits the independence of the committees, which should monitor its policy (ibid, p. 495). The Governor General's limited functions are "... to be consulted, to encourage, and to warn" (ibid, p. 491), and, therefore, the required affirmation of all bills, under the Constitution Act of 1986, is rather a formality. In other words, NZ' political system permits a strong prime minister to dominate the cabinet, which dominates the government caucus, which in turn dominates a small, controlled, unicameral parliament (Belich, 2001, p. 396, Evans et. al., 2002, p. 1856).

In the context of missing checks and balances, when compared to the British model, NZ's policy markets were highly personalised over a considerable period of time by a closed community with leading members from the 'inner circle' of the Treasury, Cabinet, the Reserve Bank, the Business Roundtable, and other strategically located institutions (Goldfinch, 2000, p. 12). For instance, until at least 1988, Roger Douglass and the Treasury could exclude other sources of economic advice by its sheer numbers of economists, and, therefore, dominated the orchestration of the neoclassical policies (Belich, 2001, p. 411). Only the lack of diversity maintaining political structures in the system allowed for the 'crash through' approach to economic liberalisation, and undermined the political legitimacy of the process (Goldfinch, 2000, p. 17). Moreover, semi-corruption prevailed due to a built-in 'looking for your mates' culture; which dominated the governmental process of the appointment to over 4,000 positions (Belich, 2001, p. 403). Another example for semi-corruption, the Waitangi Tribunal was set up in 1985 to hear Māori claims on land and water retrospective to 1840 (Belich, 2001, p. 410). It became an industry of income distributions for Pākehā lawyers and small

Māori elite based on an increase from 180 claims in 1989 to over 700 in 1999. The Treaty was worth something, which means that contractual rights were enforced, but it was misused (Belich, 2001, p. 480). Additionally, the labour market reforms were delayed by the Labour party and hindered economic growth during the 1980s (Evans et al., 1996, p. 1871). Only with the new National government, the Employment Contracts Act of 1991 led to individual job contracts and halving of trade union membership numbers within three years (Dalziel, 2002, p. 42; Belich, 2001, p. 411). Almost a decade after the start of the economic reforms, New Zealand's job market became one of the most flexible worldwide (McMillan, 2004, p. 13).

8.1.2 Argentina

Argentina exhibits further evidence of North's and Olson's theories about political markets of their Spanish models if examined in a more detailed way. Its legislature, the Congress, consists of two chambers, the House of Deputies and the Senate (Ladmann, 1998, p. 17). The law-making process and the performance of the government are vulnerable to intensive lobbying, because of the high fraction of representatives from the autonomous capital in the lower house, and the constitutionally specified minimum income for candidates for the Senate (ibid, p. 18-19). An indicator for this might be the fact that in 1994 nearly half of the members of the congress were lawyers (ibid). The MP's individual voting rights are also constrained due to the risk of losing her or his seat with a vote to the contrary (ibid, p.20). Moreover, the legislative power over Argentina's public foreign debt, the declaration of siege, and federal intervention in the provinces are reserved to the executive (ibid, p.17). The presidents Alfonsín and Menem used the means resorting to decrees to take away further legislative power. Although lower courts usually follow the Supreme Court's decisions, they are not formally binding (ibid). Lastly, it is even theoretically possible to abolish international human rights treaties, which were included in the constitution of 1994 (ibid).

Although after the establishment of democracy certain interest groups experienced limitations of their influence, others remained strong. The role of the military was diminished through fiscal means under the presidencies of Alfonsín and Menem (ibid, p. 10). Labour unions lost their privileges at the end of the 1980s through lower membership rates and rising informal markets (ibid, p. 14). Societal change brought about the loss of the political influence of the Catholic Church because of its anti-democratic role during the Dirty War (ibid, p. 19). On the other hand, the influence of business and political interest groups has remained a big problem (ibid, p. 29). After

1983, the various highly personalised parties could not achieve a political consensus in favour for democratic institutional renovation to underpin the macroeconomic stabilisation policies (ibid, p. 23). The faulty political system and further informal rules allowed a slow ‘deinstitutionalisation of politics’ through a corrupt, unresponsive political class since its return to democracy (Armony & Armony, 2005, p. 30). A fragmented, uncooperative political system, its longstanding perception of the citizens’ subordination under the leader’s decisions, and a corrupt autocratic style of policymaking has suppressed the economic development over the past two decades (ibid). This resulted in the social mobilisation of the citizens against the neo-liberal policies in the 1990s (ibid, p. 33). The longer the reforms continued in Argentina, the more the social bonds weakened, and led to increasing levels of crime and broader social fragmentation (ibid, p. 34). In the view of Argentina’s citizens, the bond of trust between them and ‘the ruling class’ was broken (ibid, p. 35). This finally culminated in a political crisis of the democratic regime in 2001 (ibid, p. 30; Lewis, 2003, p. 19).

8.1.3 Summary

It can be concluded that New Zealand inherited the establishment of personal rights and an independent supreme court from the British democracy, but failed quite dramatically to maintain political diversity. As a result, this may have allowed NZ to become “the fastest law makers in the West” with the ability to pass a law within 24 hours (Jackson, 1998, p. 494). However, this made the system vulnerable to ad-hoc policies and lobbying. This means that Douglass North’s cultural heritage hypothesis accounts for the roots of NZ’s political markets, but the ideal-type political structure is only partially present. Mancur Olson’s British model does not account for the source of certain institutions, such as NZ’s unwritten constitution, and New Zealand’s type of democracy misses further important characteristics of his ‘ideal type’. However, his sclerotic democracy term might be a better description of NZ’s political markets. On the other hand, Argentina’s system provides more comprehensive checks and balances, but they are employed only on a selective basis. This selectivity, extensive lobbying, limitations of individual rights, as well as the weak role of the judiciary system would substantiate North’s and Olson’s individual Spanish models. In other words, Argentina has failed to develop clear and sound rules to institutionalise the democratic political game (Armony & Armony, 2005, p. 31).

Table 12: Assessment of the Political Structures and Processes

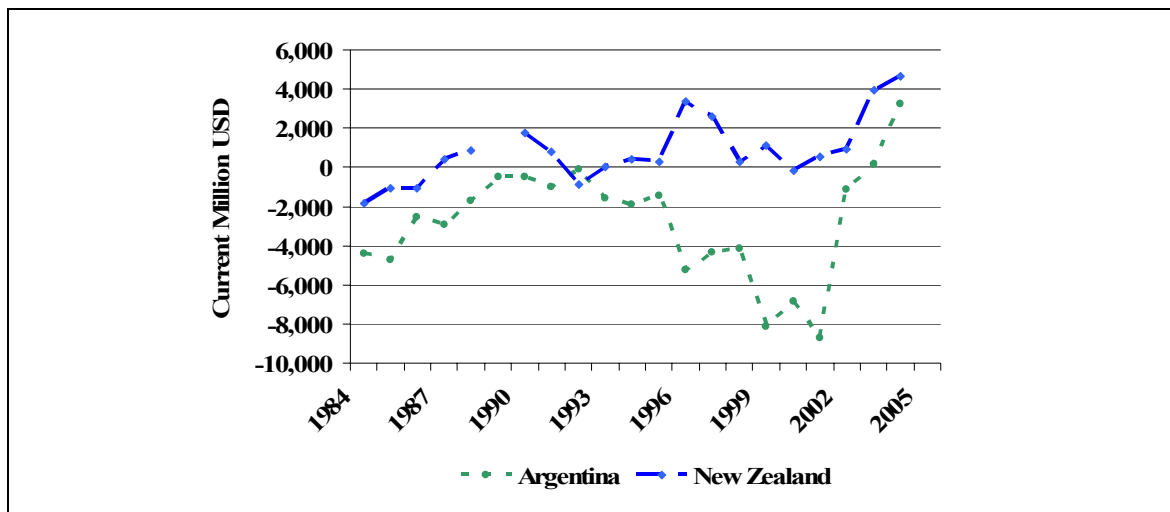
Theory	New Zealand	Argentina
North	<ul style="list-style-type: none"> + Cultural heritage of a well-working system of property rights and an independent judiciary without written constitution. - Political diversity is missing. - High degree of susceptibility to lobbying. 	<ul style="list-style-type: none"> + Individual rights are insured by a formal constitution, but can be abandoned. + Independency of the judiciary is not ensured. + Formal political diversity prevails, but is selective, and can be overridden. + High degree of susceptibility to lobbying within political markets. + Hard to overcome inertial process of ‘de-institutionalisation of politics’
Olson	<ul style="list-style-type: none"> + Formal political system set up to ensure property rights + Independent judiciary exists. - Political diversity is missed. + High degree of susceptibility to lobbying as a case of institutional sclerosis. 	<ul style="list-style-type: none"> + Ill-established formal political system, where individual rights can be abandoned. + Independency of the judiciary is not ensured. + Formal political diversity prevails, but is selective, and can be overridden. + High degree of susceptibility to lobbying within Political Markets.

Where: ‘+’ = According to the scholar’s theory; ‘-’ = In contrast to the scholar’s theory

8.2 Fiscal Policy

According to Olson (2000, p. 157-158), Argentina should provide evidence for an eroded tax-system if compared to New Zealand. Therefore, Argentina’s fiscal budgets should have been negative over the last decades, while NZ’s governmental spending should have been in balance with its revenues (ibid). Finally, New Zealand should have provided better fiscal incentives than Argentina to foster capital formation, or, in other words, savings (ibid, p. 133).

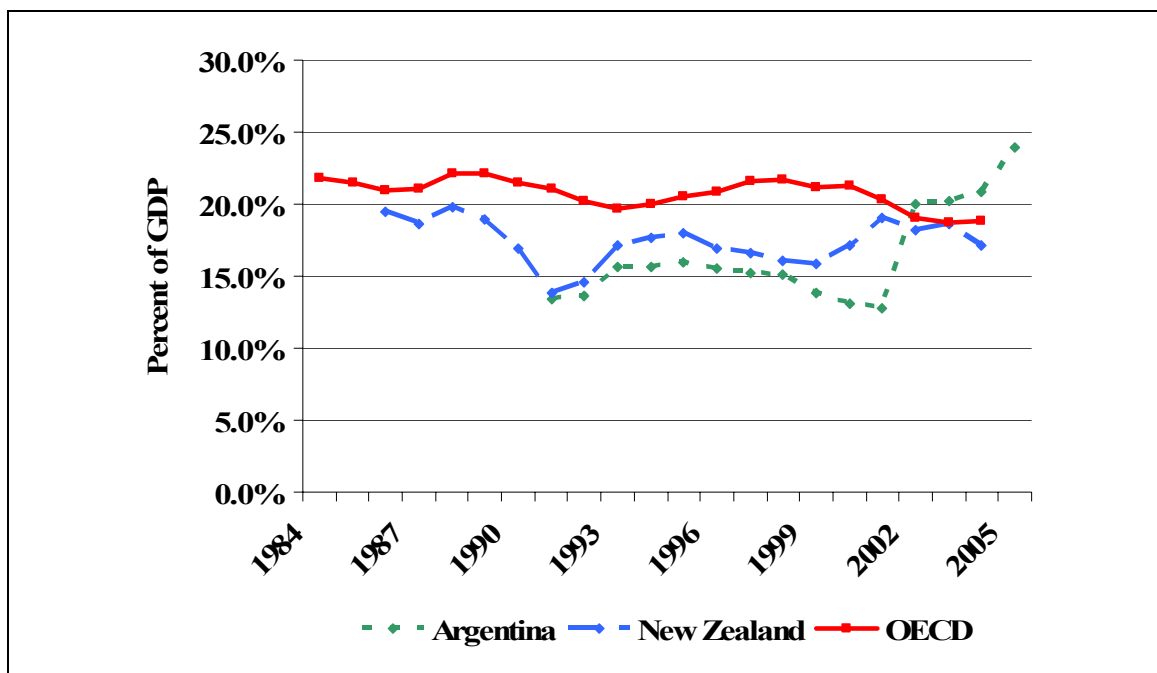
Figure 8: Fiscal Budget Balance



Source: The International Monetary Fund (2007); World Financial Statistics; Deficit or Surplus of Fiscal Budgets for NZ until 2000, and for Argentina until 2004; The Treasury (2007), Archives of the Financial Statements for NZ until 2004; in current m USD

According to Figure 8, New Zealand could manage to achieve balanced fiscal budgets after the implementation of the reforms. Moreover, Argentina's unrestrained governmental spending also provides evidence for Olson's Spanish model. Hence, at the first glance, Olson's theory can be supported by the actual economic history of both economies.

Figure 9: Gross Savings



Source: The World Bank (2007), World Development Indicators; Gross Savings; Data for New Zealand from 1986; Data for Argentina from 1991

However, as Figure 9 shows, the savings rates in New Zealand and Argentina remained considerably below those of the OECD average, at least until the beginning of the new millennium. Hence, fiscal incentives to save were missing in both economies. Especially through the 1990s, both nations showed similar patterns, and Argentina's savings rates finally rose above the OECD benchmark levels since the beginning of the recent decade. This is in contrast to Olson (2000, p. 185), who addresses the need of capital formation to foster the production of complex goods. Therefore, the fiscal policies of both countries need further evaluations.

8.2.1 New Zealand

Roger Douglass' programme, often called "Rogernomics", tried to attack the huge budget deficits of the government by focussing on three main issues: reduction and reorganisation of the state sector, international trade deregulation and the ending of the state support for industry (Belich, 2001, p. 408). Another goal was to break-up existing lobbying structures by following the principle that "individual groups lose their

privileges but simultaneously they no longer have to carry the cost of paying for the privileges of other groups” (Roger Douglass, as cited in Belich, 2001, p. 412).

In regards to cutting support to industries, the NZ government implemented a ‘hands-off’ policy in the early 1980s to not give special preference to particular trade-able products (Easton, 1997, p. 239). Roger Douglass’ policy removed most agricultural subsidies within a year (Dalziel, 2002, p. 31). Furthermore, monopoly rights in the transport sector, and international barriers, like import tariffs or export incentives, were unilateral removed (Belich, 2001, p. 410). On the state reduction side, NZ sold 13 billion NZD of state assets between 1987 and 1993 (ibid, p. 394). More than 80,000 people, around 29% of core state services, were fired (ibid, p. 409). This led to substantial productivity improvements in many sectors (Dalziel, 2002, p. 32).

Further fiscal actions involved the cutting and streamlining of the income tax system; the introduction of ‘user pays’ for the use of public services and the Goods and Services Tax (GST) from 1986 onwards; and the abandoning of assisted home ownership, free tertiary education, and other aspects of the welfare system (Belich, 2001, p. 409; Skilling & Waldegrave, 2004, p. 25). The fourth National Party government from 1990 followed ‘Rogernomics’ enthusiastically, and cut a further 1.6 billion NZD from the welfare system, semi-corporatised schools and hospitals, and reduced income taxes further (ibid, p. 408; Dalziel, 2002, p. 32).

The speed of the implementation of the politics was only possible because of the missing checks and balances, and did not consider further economic or social needs (Belich, 2001, p. 412).²⁶ Because the original problems were misdiagnosed, NZ’s fiscal reforms did not achieve the outcomes as predicted. The changes did not solve the surge in the costs of the state, lobbying, and slow economic growth (ibid, p. 423).

Regardless of other reforms, failed alignments of the superannuation and unemployment policies led to a sharp increase in social security payments to 40% of state spending in 1990 (Belich, 2001, p. 421). Nowadays, 80% of people over 65 depend on national superannuation as an almost exclusive source of retirement income (Skilling and Waldegrave, 2004, p. 11). Hence, in contrast to limiting government spending, current expenditures peaked at 39.4% of GDP in June 1991 (Evans et al., 1996, p. 1868). Long-lasting periods of fiscal surpluses were finally achieved with the introduction of the Fiscal Responsibility Act in 1994, and continued to be achieved since then (Dalziel, 2002, p. 32). However, the sole focus on fiscal deflation led to pro-cyclical cuts and to further harm of weakened export sector (Goldfinch, 2000, p. 19;

²⁶ See chapter 8.1.1

Skilling & Boven, 2005). Furthermore, the reforms led to almost constant amounts of state funding for the tertiary education system until the 1990s, despite the quadrupling of tertiary students within 20 years, and to a dramatic drop in public funding of research and development (Belich, 2001, p. 422-423).

Moreover, NZ's privatisation was badly timed and was accompanied by comprehensive lobbying. The government forwent substantially higher revenues by selling its public assets below their market value, in a buyer's market, after the stock market crash in 1987 (Belich, 2001, p. 456). Former permanent secretaries of state-owned businesses became chief executive officers of the new privatised companies with even higher salaries (ibid, p. 409). The process of privatisation also involved substantial transaction fees to financiers, accountants, lawyers, economists, public-relation specialist and others (Easton, 1997, p. 246). In the case of Telecom NZ, the government spent over 100 million NZD on private advice immediately after the stock market crash of 1987 had dried up the financial industry's income basis (ibid).

In addition, the restructuring ravaged a lot of the pre-1984 social capital, which led to a significant increase in transaction costs (Belich, 2001, p. 458). Young, singles, people of Māori or Pasifika descent, and people with many children were negatively affected by NZ's fiscal policies (Skilling and Waldegrave, 2004, p. 7). For instance, violent offences increased from 4,000 in 1960 to 40,000 in 1999 (Belich, 2001, p. 464). In 1997, 44% of the prison population was Māori, although they represented only 15% of the total population (ibid, p. 481). At the same time, the unemployment rates of Māori had risen to four times higher than of the Pākehā (ibid, p. 474). Moreover, non-Pākehā earned less money throughout the time, and suffered more during the economic stagnation until the early 1990s (Chatterjee & Podder, 2007, p. 20).²⁷ Further demographic and ethnic income differentials remained, where the recently retired benefited from previous housing schemes and from higher retirement benefits, while students were required to pay compulsory tuition fees (Belich, 2001, p. 419).

Furthermore, the rich benefited more than the poor from most of these changes (Belich, 2001, p. 409; Dalziel, 2002, p. 44).²⁸ While the rising income and wealth distribution could be seen in other nations over the last two decades, New Zealand is unique with its 16% share of its citizens with negative wealth, compared to 4% to 8% in other Anglophone countries in 2002 (Skilling & Waldegrave, 2004, p. 8). The reforms

²⁷ See Appendix C for further details

²⁸ According to Skilling and Waldegrave (2004, p. 5), 10% of New Zealand's population hold more than 50% of total household wealth of 367 billion NZD while the poorer half of the population had accumulated only 3% of total household wealth in 2001.

established a virtual ‘threshold level’ for incomes, which did not allow almost 50% of the population to save (ibid, p. 12). Moreover, the immediate deregulation of imports also fostered the decline in savings (ibid, p. 22). In other words, the abolishment of the aforementioned means of income redistribution and channelling exports receipts away from consumption of imported goods contributed considerably to New Zealand’s inability to build up sophisticated national capital markets (ibid, p. 25).

8.2.2 Argentina

At the end of 1983, the new government realised that Argentina’s newly established democracy and its weakened production sectors needed a radical programme for more economic efficiency and macroeconomic stabilisation (Lewis, 2003, p. 22). In contrast to neo-structuralist Mexico or Brasil, which put emphasis on raising their efficiencies before international reopening, Argentina decided on neo-liberal policy, where the market should do the work, as favoured by many international experts (Lewis, n. d., p. 18). Similar to New Zealand, the four aims of its neo-liberal policy were balanced budgets, deregulation, privatisation, and international economic re-insertion (ibid, p. 19).

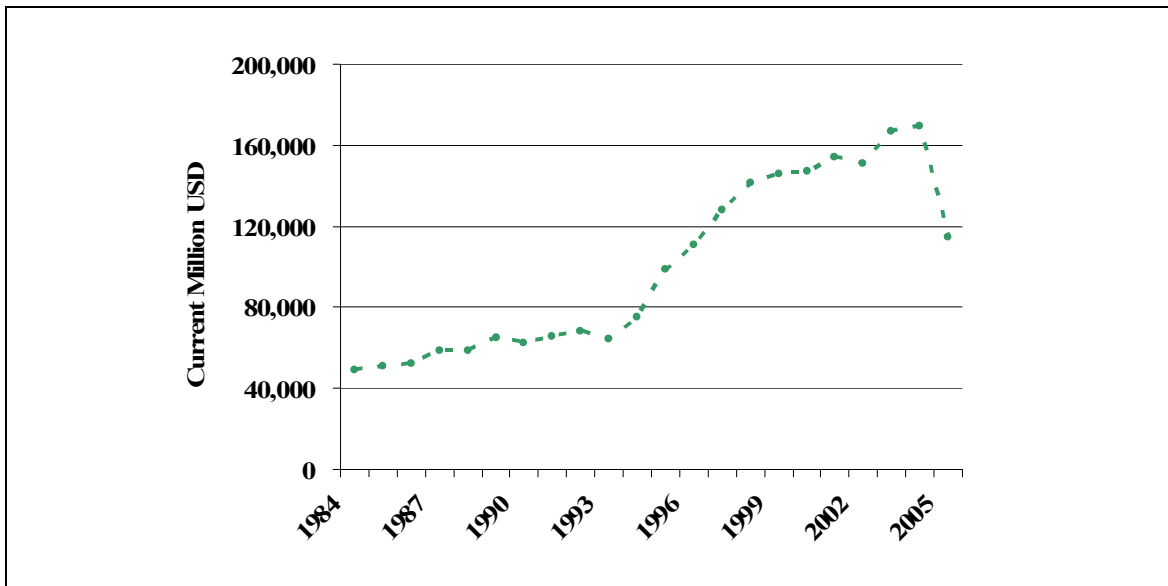
In June 1985 the Austral Plan, one of many economic policy packages aiming at immediate stabilisation through economic growth, was introduced (Lewis, 2003, p. 24). Short-term measures were implemented including the reduction in wages, which led to a fall of real-incomes (Sanz-Villarroya, 2005, p. 445). It was begun to liberalise foreign trade by cutting fiscal incentives for exports and restrictions of imports (ibid). However, fiscal policies to increase national savings rates were not implemented. Hence, the returning consumer confidence resulted, in contrast to the predicted increase in domestic savings, in a consumption boom of imported goods, and in a lowering of investment rates (Lewis, n. d., p. 18). Argentina did not downsize its governmental overhead through its ‘lost decade’ until the 1990s (Kydland & Zarazaga, 2003, p. 13). The divergences between economic and political timetables resulted in the half-hearted initiation of the process of privatisation and higher public saving (Lewis, 2003, p. 25). For instance, the mean of public work was actively used as a substitute for unemployment insurance (Kydland & Zarazaga, 2003, p. 14).²⁹ This kept real wages higher than marginal product of labour, and productivity low.

²⁹ Kydland and Zarazaga (2003, p.14) estimate that up to 25% of the total workforce was employed in the public sector during the lost decade.

The aim of implementing neo-liberal policies continued with the change of the ruling party and the inauguration of Carlos Menem as the new president in 1989 (Lewis, 2003, p. 8). His administration finalised privatisation, and undertook further fiscal reforms to liberalise the economy (Lewis, 2003). However, the processes of fiscal policy-making remained the target of diverse interest groups. For instance, in 1993, the change of the pension system from pay-as-you-go to a funded system resulted in less intra- and intergenerational income redistribution, and, hence, in less consumption by the citizens (Arza, 2006, p. 469; Bleaney, 2004, p. 711). Elaborate informal policymaking, beyond the written rules, by the national income elite set up the basement of future pension benefits almost exclusively on individual contributory capacity (Arza, 2006, p. 471). Hence, in 2000, only 52% of the working population within the formal economy was covered; and the value of the benefits fell by approximately 50% (ibid, p. 469). Moreover, the privately administered new pension-scheme led to lower social security contributions of the tax-payers to the governmental budgets; while the stake of the public in pension transfers for the old system increased from 40% in the mid 1980s to 60% in 2000 (ibid; Bleaney, 2004, p. 711). As another example, in 1996 the government introduced the “Trabajar” programme, a low wage public work on community projects in poor areas (Ravallion, 2004, p. 116). The results of the programme varied over time. After initial successes on aiming the poor, the aggregate spending on the programme tended to protect the rich (ibid, p. 119).

Based on these circumstances, the debt burden of 48 billion USD in 1984 grew unrestrained (Bruno, 2006, p. 363). Argentina’s ongoing fiscal deficits to finance the current budgets led to a dramatic rise of its public debt to 200% of its GDP in 2001 despite its debt restructuring through the Brady Plan in 1992 (ibid, p. 364). The fiscal budget became more vulnerable to revenue shocks from declining export prices (Lewis, 2003, p. 24).

Figure 10: Argentina's Total External Debt



Source: The World Bank (2007), World Development Indicators; Total External Debt from 1984 to 2005; in current m USD

On behalf of its revenue, Argentina continued its long history of a general weak tax collection, although it reformed its tax system (Bleaney, 2004, p. 706). However, the government policies penalised the accumulation of capital directly or indirectly by higher capital taxes through bank deposit confiscations and sovereign debt defaults after the 1980s (Kydland & Zarazaga, 2003, p. 15). This continued, with defaults in the public debt during the economic crisis in 2002, which led to capital taxation of nearly 100% (Bleaney, 2004, p. 700).

Nevertheless, the fiscal reforms are not just an example of the failures within Argentina's economic policy, because their implementation, for example, of the pension system, was based on the economic advice from the World Bank and Chile (Bleaney, 2004, p. 711). Moreover, instead of fostering different fiscal policies, the IBRD relaxed borrowing regulations to finance public work programs (Lewis, 2003, p. 24).

8.2.3 Summary

New Zealand's fiscal reforms and the laissez-faire policies were not unique among OECD countries, but their extent and rapidity were (Dalziel, 2002, p. 34). However, by cutting taxes, export subsidies, tariffs, and social benefits, important incentives for economic growth and income redistribution were abolished. Instead of fighting interest groups, these 'hands-off' policies resulted in a worsening of social structures and in a lowering of the incentives to engage in economic activity. North's British model does not provide the right propositions to explain NZ's fiscal policy of the last quarter century. Lobbying could not be eliminated; valuable social capital was destroyed; the

important export sector was harmed; and private savings soured. Olson's picture of a well-working democracy is also not supported by the data. Although fiscal discipline was achieved, further incentives were missing; for example to limit lobbying, and to foster competition and the accumulation of capital. Again, despite the rapidity of the reforms, elements of a sclerotic nation are seen.

Similar to New Zealand, Argentina did not consider cross influences of single policy means between each other. Argentina has seen fiscal reforms, like a social insurance reform, but it lacked a general political reform (C. M. Lewis, 2003, p. 34). Its constitution lacked a formal prohibition of the occurrence of public debt as New Zealand had (Bruno, 2006, p. 362). Hence, the ill-implemented fiscal policy provides evidence for North's hypothesis, as well as for Olson's. However, Argentina's decision-makers were not the single source of the fiscal mal-adaptation, because they were erroneously advised by external organisations, like the World Bank.

Table 13: Assessment of the Fiscal Policies

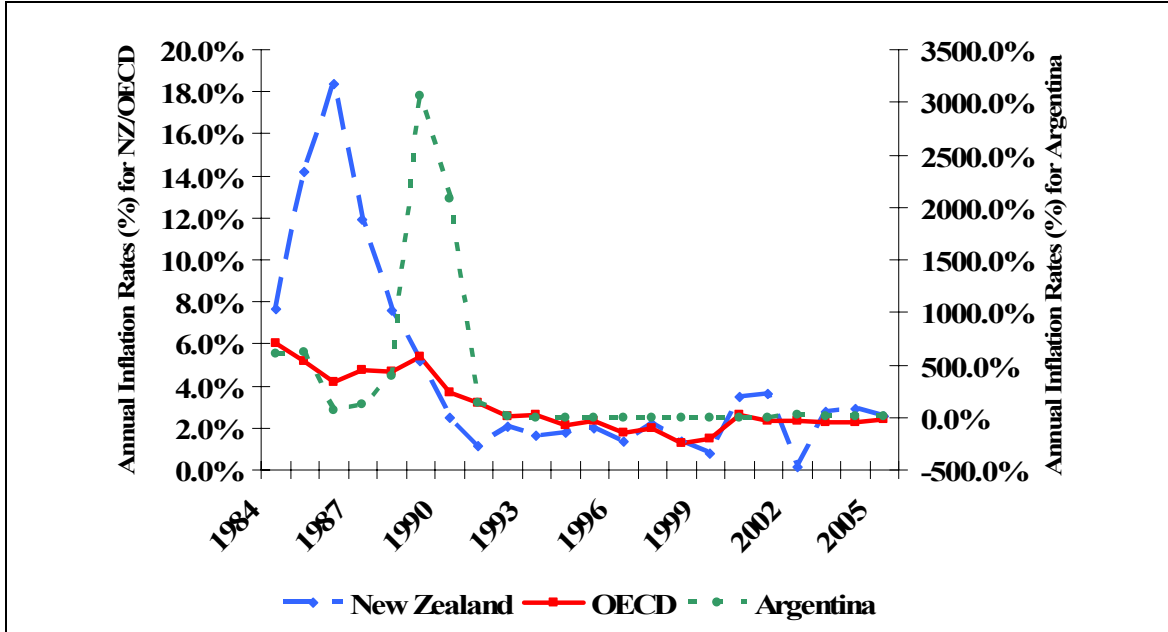
Theory	New Zealand	Argentina
North	<ul style="list-style-type: none"> - Exporting productive sector was harmed by the unilateral removal of export incentives and import restraints damaged. - Missing institutions for the accumulation of capital. - Lobbying during the process of privatisation and other reforms. - Rapidity and extent of economic reforms resulted in rising transaction costs. 	<ul style="list-style-type: none"> + Unilateral removal of export incentives and import restraints damaged the export sector. + Missing institutions for the accumulation of capital. + Slow adaptation to comprehensive fiscal reforms. + Lobbying during the process of privatisation and other reforms. - Reforms were supported by World Bank and others.
Olson	<ul style="list-style-type: none"> + Fiscal discipline achieved after 1994. - Tax reforms did not benefit the majority. - Missing fiscal incentives for the accumulation of capital. - Lobbying during the process of privatisation and other fiscal reforms. - Economic diversity only partially achieved by its 'hand-off policy'. 	<ul style="list-style-type: none"> + Unconstrained fiscal spending. + Weak tax collection and tax reforms benefited only a minority. + Large taxes on capital (confiscations). + Lobbying during reforms of the social security systems. + Missing fiscal incentives for the accumulation of capital.

Where '+' = According to the scholar's theory; '-' = In contrast to the scholar's theory

8.3 Monetary Policy

The capability to provide monetary stability, to reduce uncertainty in the economic decision-making of individuals, is seen as a key essential of a prospering economy especially by Olson. According to the theoretical models of them, New Zealand's monetary policy should have been better in addressing this (Figure 11).

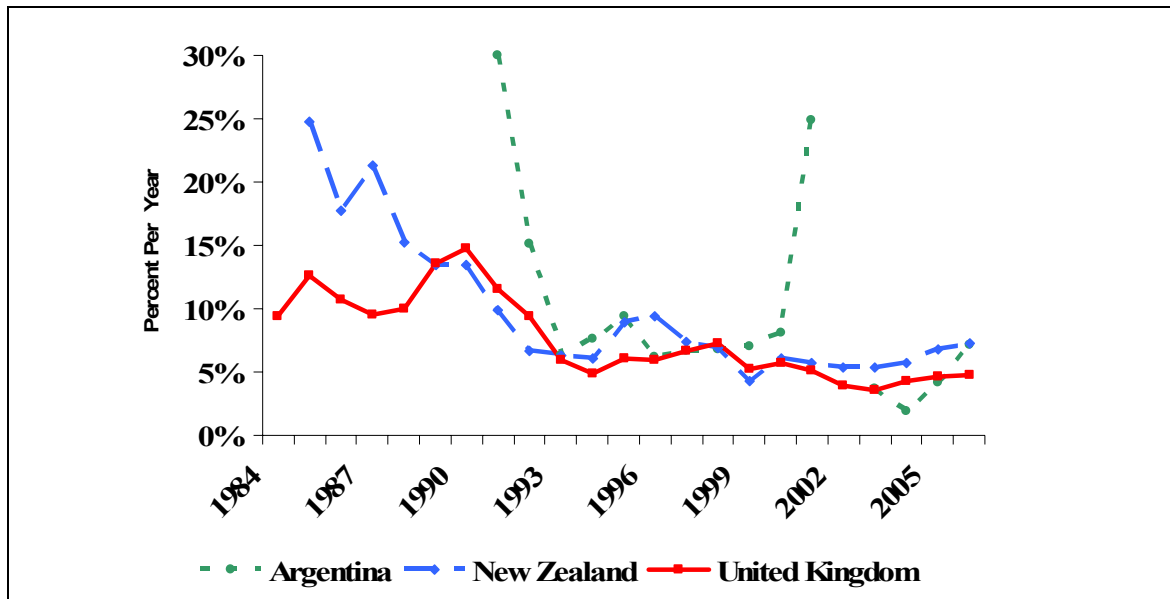
Figure 11: Annual Change in Prices



Source: The World Bank (2007), World Development Indicators, GDP Deflator between 1984 and 2005

Both New Zealand and Argentina have experienced initial periods of rapid increases in prices, with hyperinflation in the case of Argentina, until the early 1990's, when they had their 'lost decade' (Dalziel, 2002, p. 37; Kydland & Zarazaga, 2003, p. 3). Both countries were able to remedy these problems almost overnight, at approximately the same time, between 1989 and 1991. Hence, their economies saw negligible price increases during the 1990s. With the beginning of the new decade both countries experienced higher inflation rates again.

Figure 12: Money Market Interest Rates



Source: The International Monetary Fund (2007); World Financial Statistics; Money Market Rate from 1984 to 2006; Annual Interest Rates higher than 30% , as in the Case of Argentina for the Period until 1991 and again in 2002, are cut off for the Sake of better Visibility; the respective Values are: 1,182%, 1,160%, 134%, 252%, 523%,1,387,180%, 9,695,420%, 71%, and 41%

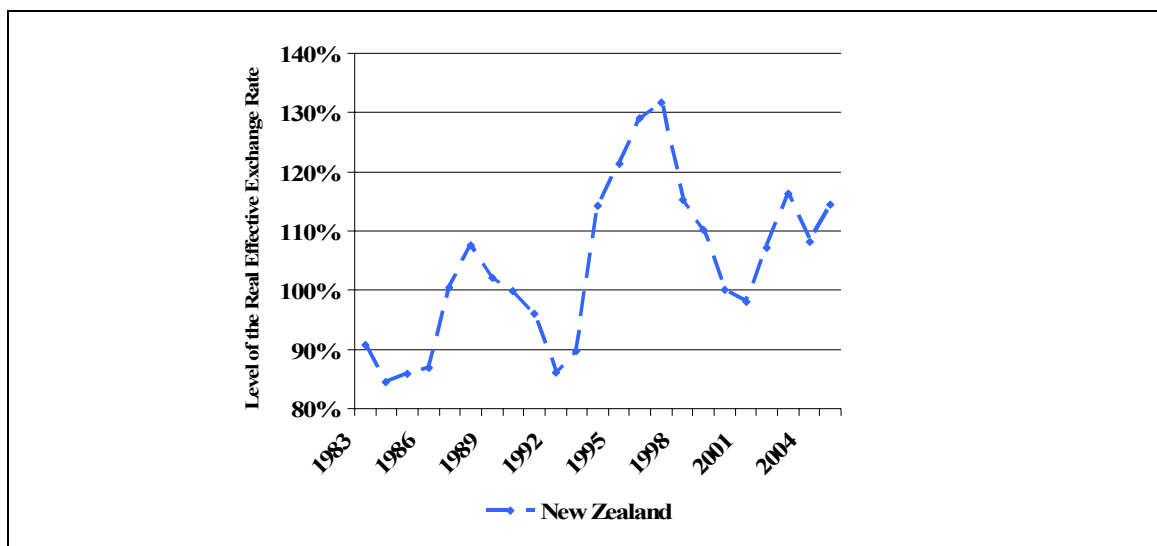
Figure 12 helps to examine differences in the national interest rates of New Zealand and Argentina. In general, NZ economic environment provided lower costs of borrowing to its businesses than Argentina, except of the deflationary period after 2002. Especially during the crisis in 2001, Argentina showed that its monetary policy lacked the means to ensure the provision of low borrowing costs. However, New Zealand did not achieve to provide low capital costs as its benchmark, the United Kingdom.

As a first conclusion, New Zealand and Argentina shared a common inflation rates' pattern, but diverged in the interest rates they could offer to their national borrowers. North's and Olson's theories do not provide a totally satisfying answer to that outcome at the first view. Hence, a more detailed evaluation will follow.

8.3.1 New Zealand

New Zealand's monetary policy went 'free market' almost overnight. In 1984 all interest rate barriers and international capital restrictions were abandoned (Easton, 1997, p. 238; Dalziel, 2002, p. 15). Due to the recognition of a substantial overvaluation of the currency in 1984, the New Zealand Dollar was set to a total free float from March 1985 onwards and fell 20% immediately (Belich, 2001, p. 408). The Treasury mistakenly believed that "with a floating exchange rate, there is less risk that poor monetary and fiscal policies will impoverish those industries exposed to world trade while generating spiralling external debt problems" (Easton, 1997, p. 237).

Figure 13: New Zealand's Real Effective Exchange Rate



Source: The World Bank (2007), World Development Indicators; Year 2000 = 100

However, the NZ Dollar became overvalued again just 1.5 years later due to a worsening of the current account balance, and periods of high inflation until the end of the 1980s (ibid, p. 232).³⁰ The Reserve Bank Act of 1989 finally led to the independence of the Reserve Bank from governmental interference, and effective inflation rate targeting was achieved (Belich, 2001, p. 409). However, because of the narrowly focussed mono-regulation and missing links to other monetary triggers no efforts were taken to mitigate the externally driven rise of real interest rates (Easton, 1997, p. 235; Dalziel, 2002, p. 15). Additionally, due to the preceding extensive financial deregulation, former policy instruments, like ratio controls and credit restrictions, were no longer available (Evans et al., 1996, p. 1866). These circumstances, in combination with a low savings ratio, underdeveloped debt markets and already outstanding high overseas debt, led to an increase in the already overvalued exchange rate (Evans et al., 1996, p. 1871; Skilling & Waldegrave, 2004, p. 21). Moreover, it resulted in the further weakening of its terms of trade, and in one of the largest stocks of external debt in the OECD, due to large capital inflows over the last decades (ibid).

8.3.2 Argentina

On the other hand, Argentina's monetary policy was equally bad and ill conceived. Firstly, substantial inflation existed throughout the 1980s with a hyperinflationary period at the end of that decade (Sanz-Villarroya, 2005, p. 445). After decades of rapidly increasing price levels, the common opinion was that this kind of inertial inflation increase and the resulting lack of credibility of its currency could not be

³⁰ See chapter 7 and 8.2

tackled by orthodox means (Lewis, n. d., p. 18). According to Shigeto Kitano (2005, p. 368), decision makers saw no other options but the establishment of a peg of the Peso to the US Dollar with the introduction of the Convertibility Plan in 1991. This should have been combined with a whole series of institutional reforms in bank regulations, extensive deregulation and privatisation (Bleaney, 2004, p. 700).

Indeed, inflation came under control after 1991, and the current account deficit was covered by massive capital inflows, but the exchange rate remained significantly overvalued (ibid). Between 1994 and 1999, Argentina successfully fought the influence of several international currency crises, like the Mexican Crisis, the Russian Crisis, the Asian Crisis and the Brazilian Crisis (Kitano, 2005, p. 368; Bleaney, 2004 p. 701). External experts, like the International Monetary Fund (IMF), and other economists congratulated Argentina on its achievements (ibid). For international investors it provided a highly welcomed mean of eliminating currency-risks (Hunter, 2006, p. 808). The psychological impact of the price stability on Argentina's citizens and their dream of glory also cannot be exaggerated (Armony & Armony, 2005, p. 42). However, Argentina's success came at the cost of giving up the chance of being the lender of last resort (Bleaney, 2004, p. 700).

On the 9th of January 2002, the currency board collapsed during a dramatic currency crisis and Argentina went into an exceptionally severe recession (Bleaney, 2004, p. 700). Since inflation was not the trigger, Argentina did not follow the familiar pattern of failed exchange rate based stabilisation (ibid, p. 702). Moreover, the currency board backed the entire monetary base with international reserves, hence, it was not the reason of the currency crisis either (Kitano, 2005, p. 369). The main reason for the crisis, similar to New Zealand, was the single focus on inflation (ibid). The monetary policy did not consider the overseas borrowing that was used to finance government deficits (ibid). Argentina's currency became even more overvalued after the Russian Crisis, and the following stoppage in capital inflows led to an increase in real interest rates, and repression of macroeconomic development (Bleaney, 2004, p. 710). All checks and balances failed. The IMF did not intervene, imports were not compressed by active fiscal policy, and currency devaluation was not possible under the currency board (Bleaney, 2004, p. 704-710; Bruno, 2006, p. 360). Although warning signs existed, the government of de la Rúa did not abandon the Convertibility Plan since the preceding stability had become the 'Holy Grail' of the electorate (Armony & Armony, 2005, p. 46).

8.3.3 Summary

Obviously, both theories cannot explain why both countries' monetary policies were solely aimed at lowering inflation while forgetting to make linkages to the exchange rate and fiscal policies.

Although, from 1989, low inflation existed in the case of New Zealand, the overvalued currency and the complete lack of the consideration for the business cycle harmed the economy and its export sector substantially (Evans et al., 1996, p. 1865; Easton, 1997, p. 247).³¹ Relying on capital inflows contributed to NZ's lack of decent domestic bond markets that were present in Australia and the US (Skilling & Waldegrave, 2004, p. 32).

In the case of Argentina, the peg of the Peso to the US Dollar was the wrong monetary policy for its geographically diversified trade (Bleaney, 2004, p. 712). It also failed in developing appropriate domestic bond markets including indexed bonds (ibid). Additionally, Argentina relied on lower yielding external funding sources. Its initial aim of raising investor confidence was not achieved, as approximately 60% of bank deposits and loans were denominated in US Dollars by the late 1990's (ibid, p. 700).

Lastly, stated as an anecdote, neither North nor Olson can explain, why New Zealand plans to establish a currency board with Australia despite negative experiences worldwide (TVNZ, 2007; Skilling & Boven, 2006, p. 25).

Table 14: Assessment of the Monetary Policies

Theory	New Zealand	Argentina
North	- Did not provide an adaptive efficient monetary environment to foster economic growth.	+ Fail to abandon the Convertibility Plan in time. - External experts, like IMF, encouraged the peg to the USD.
Olson	+ Inflation came under control. - No control of domestic real-interest rates. - No control of the exchange rate.	- Inflation came under control. + No control of the exchange rate. + No control of domestic real-interest rates.

Where '+' = According to the scholar's theory; '-' = In contrast to the scholar's theory

³¹ That New Zealand must have adopted the wrong policy shows the fact that it's economy would have been 20% larger in 1991/2 if it would have grown like the OECD economies, on average (Easton, 1997, p. 232).

9. Assessment of the Economic Markets

9.1 Transaction Costs and Competition

According to Douglass North's and Mancur Olson's theories, New Zealand should have provided a more positive incentive structure to its businesses during the period under consideration. This means, lower transaction costs through lower bureaucracy, higher competition, and more well-established property rights should have prevailed since 1984. These indicators of economic development are compared in Table 15.

Table 15: Current Levels of Transaction Costs

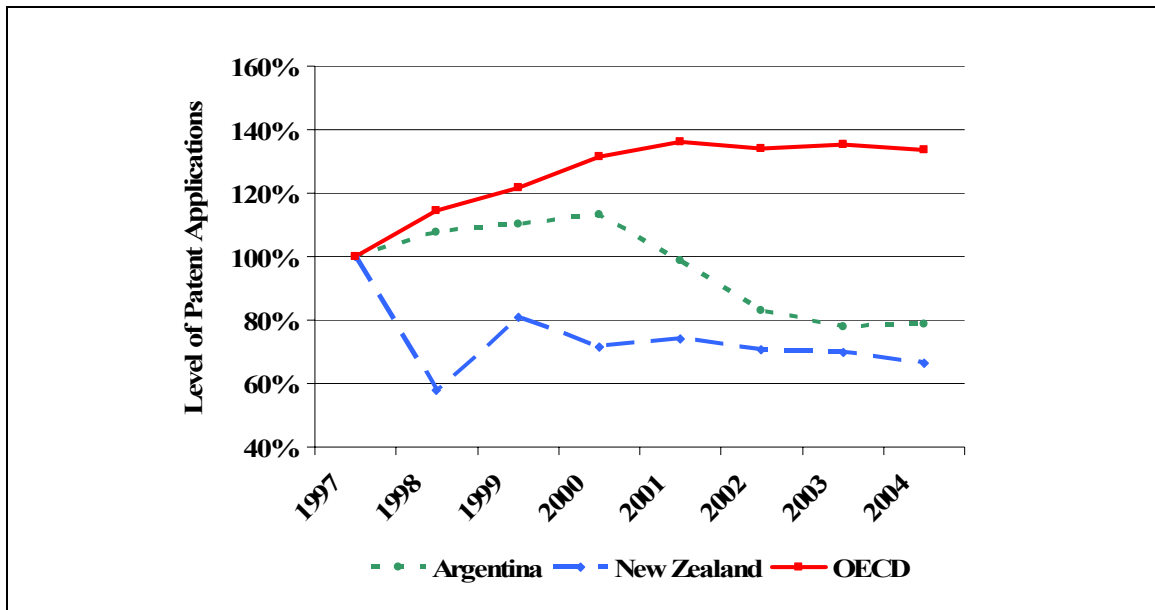
	New Zealand	Argentina	OECD
<i>Time required to build a Warehouse (Days)</i>	184	288	149
<i>Procedures to build a Warehouse (Number)</i>	7	23	14
<i>Time required to enforce a contract (days)</i>	109	520	351
<i>Procedures to enforce a contract (number)</i>	28	33	22
<i>Time required to register property (days)</i>	2	44	32
<i>Procedures to register property (number)</i>	2	5	5
<i>Time required to start a business (days)</i>	12	32	16
<i>Procedures to register a Start-up business (number)</i>	2	15	6
<i>Cost of business start-up procedures (% of GNI per capita)</i>	0.2	12.1	5.3
<i>Time to prepare and pay taxes (hours)</i>	70	615	203
<i>Time to resolve insolvency (years)</i>	2	2.8	1.4
<i>Ease of doing business index (1=most business-friendly regulations)</i>	2	101	N/A

Source: The World Bank (2007); World Development Indicators; figures for OECD rounded, data are 2006 figures

The general picture of Table 15 shows that nowadays New Zealand provides a much more deregulated environment to its businesses than Argentina. In general, procedures, times and costs needed to comply with NZ's red tape requirements are similar, or even lower, than in other OECD countries. On the other hand, Argentina's economy is still confronted with an overarching bureaucracy.

According to Feinstein (1999, p. 40), the successful economies of the OECD shifted their economic activities towards sophisticated consumer goods and services during the last decades of the preceding century. Does this mean that New Zealand was more able to adapt efficiently to the new economic environment, as suggested by Douglass North? Could New Zealand provide more sophisticated socially contrived markets, as suggested by Mancur Olson?

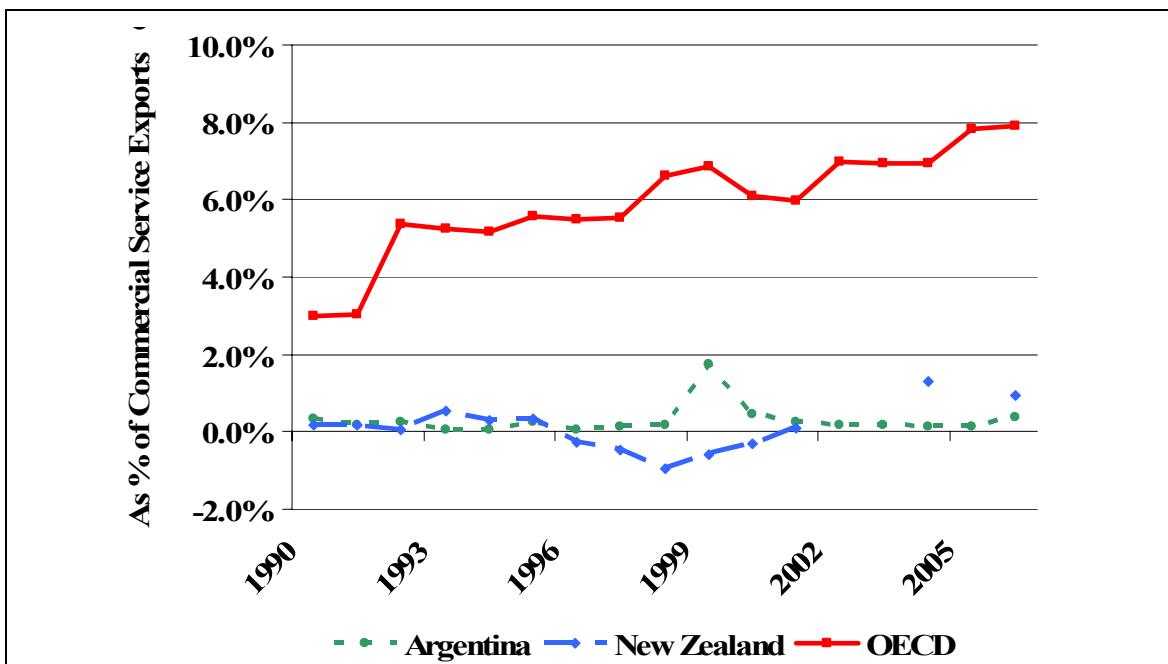
Figure 14: Patent Applications



Source: The World Bank (2007); World Development Indicators; 1997 = 100

Figure 14 shows that both countries under consideration fell behind the OECD in their rates of innovation during the last decade. In other words, certain economic markets of New Zealand and Argentina missed incentives to compete by innovation. Although equipped with antithetic transaction cost levels, as seen in Table 15, neither of the two economies provided the incentive structures for competitive industries similar to the OECD.

Figure 15: Export of Insurance and Financial Services



Source: The World Bank (2007), World Development Indicators

Furthermore, Figure 15 shows that both financial industries did not become as international competitive as the OECD countries in these socially contrived markets. New Zealand's financial industry seems to be in an even worse state than Argentina's between 1996 and 2001, when NZ's financial service sector saw net imports. Moreover, Figure 15 provides evidence for the missing national incentives to foster a change of the products and services in the export basket, which contributed to the economic strength of the OECD countries, and which may have helped to overcome their geographical disadvantages (Feinstein, 1999).

Although equipped with antithetic bureaucracy levels, both New Zealand and Argentina must have lacked particular institutions to foster the development of Olson's socially contrived markets, or to exhibit North's adaptive efficiency to economic change. Hence, a more detailed country-specific investigation should enlighten matters.

9.1.1 New Zealand

New Zealand's comprehensive deregulation through the 1980s and 1990s was aimed at fostering competition, especially from overseas, and on increasing productivity to raise microeconomic efficiency (Belich, 2001, p. 416). As a result, New Zealand currently has a dozen television channels, numerous private radio stations, innumerable licensed restaurants, extensive opening hours for supermarkets, a variety of newspapers, and one of the highest per capita car ownership levels in the world (*ibid*, p. 463). Entrepreneurship is commonplace, with more than 240,000 small firms, with under six employees each, in the country (McMillan, 2004, p. 5). Moreover, New Zealand's rich tend to be self-made, which supports the thesis of a better economic climate (*ibid*, p. 6). However, although this addresses small companies in certain low-key industries, NZ has informal barriers to economic growth in others (*ibid*, p. 17). Thus, in some industries with scale economies, public regulation went, but private regulation may have remained (Belich, 2001, p. 415; McMillan, 2004, p. 20). Deregulation ended 'systemic' cartelism, but created virtual private monopolies (Belich, 2001, p. 416). In other words, because of its small size, and remoteness, 'endemic' unofficial oligopolies remained in NZ, and newly arrived competitors from abroad preferred high profits to high sales (*ibid*, p. 416; Skilling & Boven, 2005). In short, competitive capitalism, with its merits in a large economy, did not work properly in New Zealand (Belich, 2001, p. 417). Certain New Zealand markets needed structural underpinning, some of which only government could have provided (McMillan, 2004).

9.1.2 Argentina

Argentina's microeconomic reforms were not sufficient either. On one hand, transaction costs were lowered and competition increased in certain markets through international re-insertion and privatisation. Some industries with high exposure to trade experienced high labour productivity growth between 1990 and 2001 (Sanchez & Butler, 2004, p. 254). The reasons were the transition to flexible work contracts and changes in labour taxes. Argentina's labour market became even more flexible than some of the OECD countries (Loayza et. al., 2005, p. 10). On the other hand, privatisation also led to quasi monopolies because of the favourable terms of the privatisation contracts (Lewis, 2003, p. 30). As a result, Argentina's citizen did not benefit from these productivity gains as much as the new owners of the newly privatised companies. Remaining restrictive product market regulations limited the numbers of entrants (Loayza et. al., 2005, p. 19). Hence, company turnover ratios remained comparatively low, and exits from the market resulted more often from external macroeconomic shocks than from national competition (ibid, p. 7). In other words, barriers to competition remained, and the lack of reforms of overhead regulations kept transaction cost levels up. Thus, Argentina lacked microeconomic reforms to increase employment and productivity growth; and, hence, to release some of the burden on the governmental budgets (Porter, 2002, p. 38).

9.1.3 Summary

In general, transaction cost levels, as measured by bureaucracy, were significantly lower in New Zealand than in Argentina, as predicted by North's and Olson's models. However, North's propositions do not account for remaining high transaction costs due to missing incentives in particular sectors of NZ's economy, which kept them from growing. Moreover, NZ small markets missed the institutions to foster competition as suggested by North. Olson's indicator of average firm size as predictor for prevailing transaction cost levels holds just to a limited extent. It does not include the case, when missing incentives create barriers to keep companies from growing. Additionally, North and Olson would gain from including the influence of national factor endowments into their institutional analyses; because NZ's small markets allowed 'endemic' monopolies to exist even in a highly deregulated economy. On the other hand, Argentina's high transaction cost levels and distorted incentives for competition provide affirmation for North's and Olson's Spanish models.

Table 16: Assessment of the Transaction Costs and Competition Levels

Theory	New Zealand	Argentina
North	<ul style="list-style-type: none"> + Transaction costs in certain industries were low. - The lack of regulations kept transaction costs in other sectors high. - Competition in various important sectors remained 'endemically' limited. 	<ul style="list-style-type: none"> + General transaction cost levels remained high. + Cartelism prevented the public from benefiting from productivity gains in newly privatised sectors. + Competition in some sectors was high since they did not need comprehensive regulations to prosper.
Olson	<ul style="list-style-type: none"> + Transaction costs in certain industries were low. - The lack of regulations kept transaction costs in other sectors high. - Competition in various important sectors is 'endemically' limited. 	<ul style="list-style-type: none"> + General transaction cost levels remained high. + Cartelism prevented the public from benefiting from productivity gains in newly privatised sectors. + Competition in self-enforcing markets was high since they did not need comprehensive regulations to prosper.

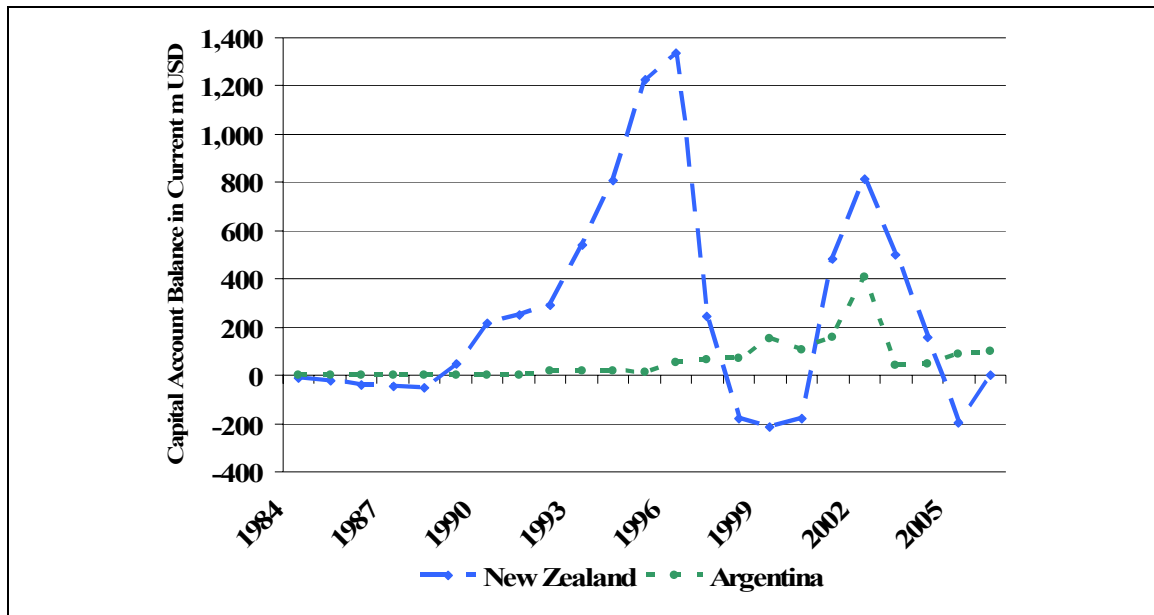
Where '+' = According to the scholar's theory; '-' = In contrast to the scholar's theory

9.2 Capital Markets

In the opinions of North and Olson, highly efficient national capital markets are necessary for flourishing economic growth, and are highly sensitive to the underlying institutional framework. In addition, capital markets represent one of Olson's socially contrived markets, which cannot exist without an institutional framework (North, 2005b, p. 124; Olson, 2000, p. 185). Therefore, the capital in- and outflows, the national debt and equity markets should be viable proxies for the quality of New Zealand's and Argentina's institutional performance. They should provide insights in the levels of property rights, competition, and fostering economic growth of both countries.

The assessment of the national capital-flows show, that New Zealand and Argentina experienced periods of massive capital-inflows (Figure 16).

Figure 16: National Capital Flows

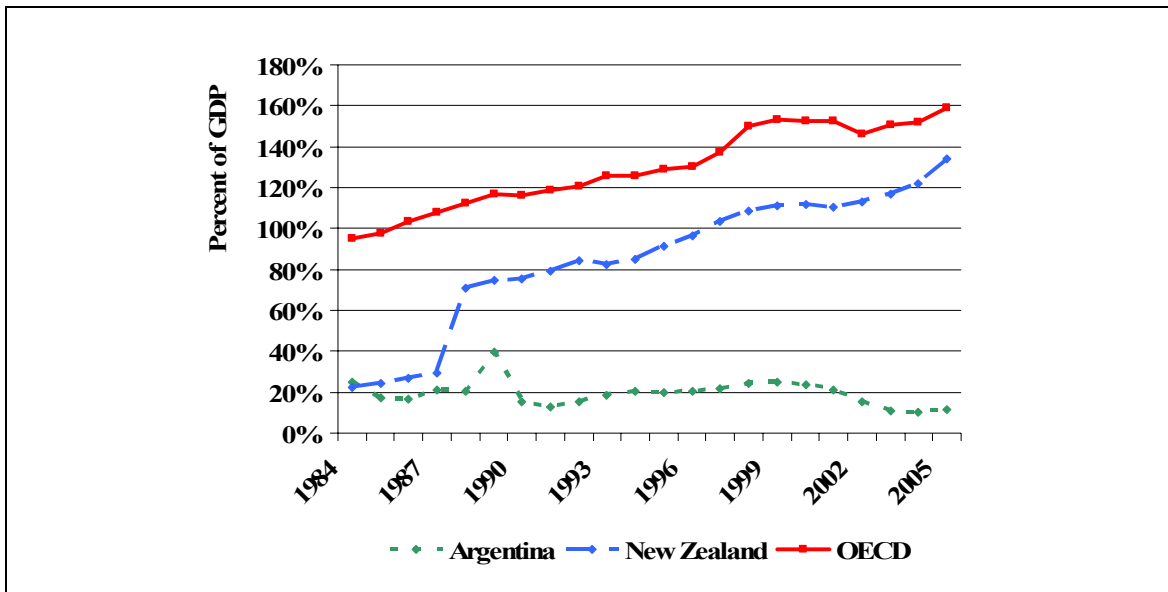


Source: The International Monetary Fund (2007); World Financial Statistics; Capital Account Data, N.I.E.; in current m USD

Generally, the amounts invested into New Zealand's economy were multiples of those invested into Argentina during the 1990s and at the start of the new millennium. Argentina's economic crisis at the end of the last century led to a sudden stop of the capital inflows. These patterns provide some evidence for the theory of Olson. On the other hand, the continuous capital inflows into New Zealand and Argentina should have been the result of established national property-rights structures in both countries, according to Olson's arguing. In addition, capital flew out of New Zealand before 1989, between 1999 and 2001, and again in 2005. Thus, the periods of capital outflows from New Zealand would account for bad economic policy, when solely based on Olson's theory. Therefore, the evaluation of mere capital-flows might not result in unambiguous results in regards to Olson's propositions.

Hence, assessing the national credit markets may allow drawing further conclusions about the level of development of the national capital markets, like the level of property-rights (Figure 17).

Figure 17: Domestic Credit to Private Sector

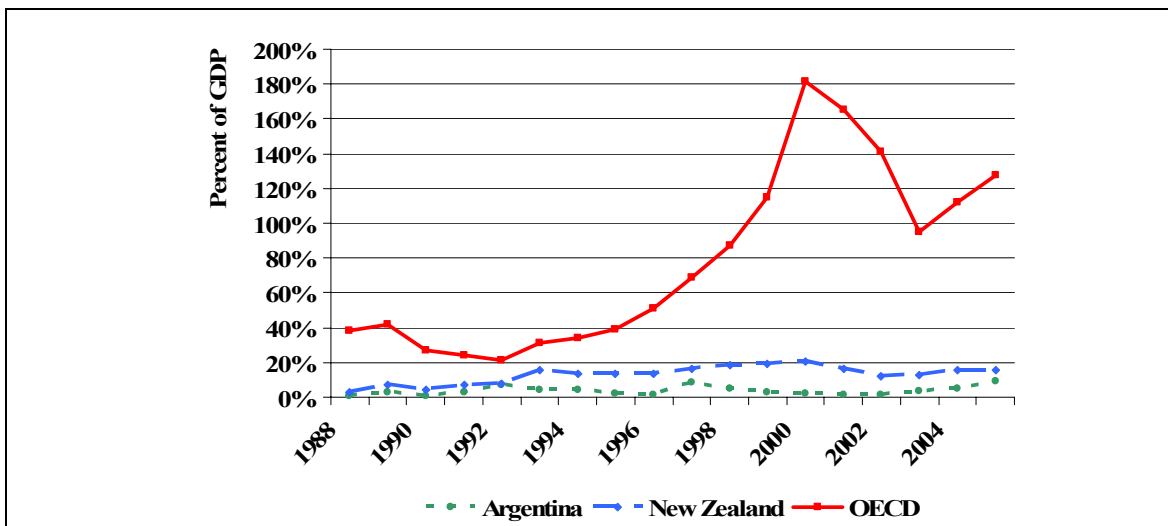


Source: The World Bank (2007), World Development Indicators ; Domestic Credit to Private Sector (% of GDP)

NZ's domestic credit sector caught up in the volume to other developed markets, especially from 1989 onwards after the establishment of the independent Reserve Bank.³² In contrast, Argentina's credit sector remained virtually flat over time. At the first glance, this shows that NZ's financial deregulation and capital market reforms have been more successful than Argentina's, when evaluated by Olson's propositions.

In contrast to this affirmation of the theory, the data of the stock markets show a different picture of the development status of the national capital markets (Figure 18).

Figure 18: Total Value of Stocks Traded



Source: The World Bank (2007), World Development Indicators; Stocks Traded, Total Value (% of GDP); Data from 1988 onwards

Although the burst of the 'bubbles' in 1987 and 2000 led to dramatic temporary falls of company values in the OECD countries, the importance of the stock markets as source for funding economic growth has risen over the decades. The underperformance

³² See Chapter 8.3.1.

of the stock markets of New Zealand and Argentina, as expressed by the low volume of stock trades, imply that both countries must have missed important institutions since the start of the reforms. This can be confirmed by the fact that the relative sizes of the stock markets in the other British democracies are about three times as NZ's (McMillan, 2004, p. 23).

So far, the study on the national capital markets has revealed that especially New Zealand does not fit neither North's nor Olson's ideal-type model. Although the data imply a higher level of property rights in New Zealand; there are not such clear differences between the two countries in regards to the national equity markets, as sources for financing business projects. Therefore, country-specific analyses might be useful to examine the capital markets in a more detailed way.

9.2.1 New Zealand

New Zealand's periods of massive capital inflows within the last quarter century are only partially a good sign for well-established institutions for capital markets. On one hand, they assert that enforceable property rights backed up international investments. On the other hand, the capital flows are also signs of a lack of adequate controlling instruments. Moreover, the ways that the capital inflows took, influenced the economic outcome of NZ differently than expected by the policy-makers. The aforementioned missing targeting of the overvalued currency through the monetary policy assured international investors that they would not suffer from currency depreciation of their investments (Easton, 1997, p. 241). Additionally, New Zealand's initial fiscal deficits resulted in high real-interest rate bonds, which were backed by NZ's taxpayers (ibid). Consequently, the export-oriented industries were strangled by an overvalued foreign exchange rate and high real interest rates. Because the export industries merely could afford the high real interest rates, the money flew into other opportunities (Easton, 1997, p. 242). Hence, the incoming capital was directed in the real estate sector (Skilling & Waldegrave, 2004, p. 16). However, the new 'wealth' of the homeowners changed their consumption patterns over time (ibid, p. 32). People stopped saving for their retirements and spent increasingly on imported goods and services after the fall of the trade barriers. Because NZ's citizens took the upward spiral of house price changes for granted, their rising willingness to greater indebtedness blew up total overseas debt from 47% of GNP in 1983 to 103% in 1999 (ibid, p. 34). As a result, the following lower credit worthiness of the country led to higher financing costs for New Zealand's businesses (ibid). In other words, although fiscal tightening occurred from the mid

1990s, which resulted in the fall of overseas public debt fell from 50% of GDP in the late 1980s to 20% in 1999, there was a reversal from public to private overseas debt (Belich, 2001, p. 421). Finally, in contrast to the government's general 'hands-off' policy, in 2001, the Kiwibank was founded (Tripe, 2005, p. 9). However, as shown above, it can be doubted that its aim of increasing competition in the national credit markets were as successful and, hence, necessary as intended.

In contrast to the capital inflows and well-established credit markets is the lack sophisticated stock markets. Although the share market tripled its value between 1984 and 1987, this was due only due to financial deregulation, capital inflows, and speculation; and not through a sustained development (Belich, 2001, p. 406). The grid of controlling incentives, either formal or informal, was not provided to absorb the negative effects on almost 900,000 New Zealander's, or approximately 40% of the adult population from the external 1987' stock market crash in the US. NZ's stock markets experienced a slump, which was not seen in any other major stock market worldwide (ibid, p. 407). Because the government followed stoically its 'hands-off' policy, the market was not fully recovered until 2000 (ibid). Additionally, lax regulations did not circumvent shoddy practice in stock-broking firms, 'insider trading' and further unprofessional or even illegal conduct in investment companies (ibid; Easton, 1997, p. 246). Hence, New Zealand experienced its 'Greedy Decade' in the 1980s as foundations of public morality shifted to "greed is acceptable" (Easton, 1997, p. 248). As a result of lacking incentives to save in financial securities, only 21% of the citizens had superannuation assets, 21% possessed shares, and 9% managed funds and 5% had bonds in 2001 (Skilling & Waldegrave, 2004, p. 14). Even the total value in cars with 16.9 billion NZD was higher than the overall share market value of 14 billion NZD (ibid, p. 15). Moreover, share holdings were highly concentrated. Just 30% of the largest listed companies are widely held; and 25% of the 20 largest listed companies are family controlled (McMillan, 2004, p. 22). The thin, inflexible capital markets hampered the growth of companies to become large (ibid, p. 17). Furthermore, it deteriorated the growth of the capital-labour ratio compared to other nations (McMillan, 2004, p. 2).

9.2.2 Argentina

Argentina also wanted to raise the efficiency of its financial markets and to lower the costs of capital, for example through radical liberalisation of their stock markets (Hunter, 2006, p. 796). However, it took until November 1989, before Argentina became one of the freest emerging markets by allowing unrestricted capital flows and by not imposing any taxes on dividends or capital gains (ibid, p. 801).

Nevertheless, Argentina's financial deregulation did not consider the necessity of additional regulations for its small open economy to overcome borrowing constraints, as seen especially during periods of expansions in the 1990s (Kydland & Zarazaga, 2003, p. 16). The currency board fostered capital inflows during the 1990s. Unfortunately, they were often misallocated to no-return projects and led to an under-performance of the investments (Lewis, 2003, p. 7). Moreover, higher possible capital inflows from international investors were hampered through the missing property rights protection. Debt defaults in mid 1980s and confiscations of deposits in 1990 resulted in rising indirect capital tax balances, up to a level of confiscation (ibid). Furthermore, in 2001, Argentina's government imposed the largest confiscations of deposits in its history and proceeded to declare a massive default on its sovereign debt obligations (ibid). Finally, in 2005, Argentina cancelled its credits with the IMF (Bruno, 2006, p. 361). However, this case shows not only a mere lack of national property rights in Argentina. In addition, international courts in the US and Europe allowed Argentina to follow its own interests against the less-organised large group of individual bondholders (ibid). This example shows that international democratic powers did not follow the route to enforce property rights either.

In other words, the financial market reforms failed, because, in contrast to the aims, the cost of capital rose dramatically (Sanchez & Butler, 2004, p. 256). Without the right incentive structure, domestic capital markets remained small and shallow (Lewis, 2003, p. 28). Institutions to facilitate higher savings rate were not enacted (ibid, p. 7). Argentina's stock markets also remained little integrated in the world because of both direct and indirect barriers (Hunter, 2006, p. 816). For instance, Argentina's currency board could not diminish negative effects of currency crises on the level of integration, and, therefore, on higher risk premiums (ibid, p. 817).

9.2.3 Summary

Both, New Zealand and Argentina, are examples of countries with underdeveloped capital markets.

In the case of New Zealand, property rights are ensured generally. Transaction costs are not a major burden either. These facts are in line with North's and Olson's propositions. However, the ideal-type British models of both scholars do not hold for further issues. New Zealand's sluggish performance of its household wealth to disposable income ratio is different to other Anglo-American countries (*ibid*, p. 20). In other words, although well-developed debt-markets existed, they were mainly financed from overseas with international risk premiums on interest rates (Skilling & Boven, 2006, p. 22). The capital markets lacked institutions to grow, and remained small and illiquid (*ibid*). Hence, New Zealander's low investments in the stock markets were a major economic constraint. New Zealand lacked incentives, like the compulsory superannuation schemes in the US that contributed to lifting the stockholders level to 52% of the population (Skilling & Waldegrave, 2004, p. 17). Hence, in contrast to North's and Olson's theories, New Zealand could not provide sophisticated capital markets to modern, capital intensive industries as they would have needed for further growth (McMillan, 2004, p. 17). Lastly, in the case of New Zealand, the experience of the 'greedy decade' provides evidence of missing checks and balances, and the possibility of corruption and fraud within the British model. Here, Olson's collective action theory becomes true, because individuals could cheat uninterrupted within a sufficient large group of individual stockholders, where sufficient means of coercion were absent (Easton, 1997, p. 249).

The capital confiscations are a clear example of the lack of encompassing property rights in Argentina. Checks and balances were missing to support the markets during crises and to prevent fraud. In addition, incentives to raise the national savings rate, as a source for financing investments, were not applied. Instead, Argentina relied mainly on 'hot money' from international sources with its destabilising effects (Hunter, 2006, p. 797). These deficiencies can be explained by North's and Olson's Spanish models. However, North's and Olson's theories need amendments to account more precisely for the showcase of Argentina. The assessment clarified that Olson's theory of capital inflows as an indicator for the strength of these markets is of limited value only. Moreover, the differences in real-interest rates to other countries were not as significant as suggested by the ideal-type models of Olson. Moreover, the property rights spheres of both scholars' theories have to be extended. The foreign investor's contractual rights

were also limited by their national courts, which show that the state is not the single source of power.

Table 17: Assessment of the National Capital Markets

Theory	New Zealand	Argentina
North	<ul style="list-style-type: none"> + Property rights were ensured. +/- Debt markets were well developed, but lacked domestic funding. - Equity markets were underdeveloped. - Personal markets in the form of greed and insider trading prevailed. - Governmental interference into well working markets while less developed markets remained unconsidered. 	<ul style="list-style-type: none"> + Property rights were missing. + Equity and debt markets were underdeveloped. + The banking sector missed checks and balances to cope with a sector crisis. + Underdeveloped incentives to save. - National courts in British countries supported Argentina's violation of property rights in the case of the capital confiscations.
Olson	<ul style="list-style-type: none"> + Property rights were ensured. +/- Debt markets were well developed, but lacked domestic funding. - Equity markets were underdeveloped. - Personal markets in the form of greed and insider trading prevailed. - Governmental interference into well working markets while less developed markets remained unconsidered. 	<ul style="list-style-type: none"> + Property rights were missing. + Equity and debt markets were underdeveloped. + The banking sector missed checks and balances to cope with a sector crisis. - National courts in British countries supported Argentina's violation of property rights in the case of the capital confiscations. - Capital flows and interest rates are only partially viable indicators of the quality of institutions.

Where: '+' = According to the scholar's theory; '-' = In contrast to the scholar's theory

10. Conclusions and Recommendations

10.1 Introduction

The analytical part of the dissertation was centred on the following research question

Can the economic growth patterns of New Zealand and Argentina of the last quarter century be explained either by Douglass North's 'cultural heritage' hypothesis or by Mancur Olson's 'country-specific economic policy' hypothesis?

Firstly, the two theories were evaluated on a theoretical basis to find differences and commonalities among them. Therefore, North's and Olson's theoretical frameworks and their main elements were presented. These were followed by the description of their distinctive main hypotheses.

Secondly, the recent economic histories of New Zealand and Argentina were compared with each other and further OECD data to examine the validity of North's and Olson's propositions. Therefore, a conceptual framework, as based on both scholars' suggestions about successful economic policy, was developed in Chapter 5, and complemented by a refined research design in Chapter 6. At the beginning of the country analyses, the economic growth patterns of both countries since 1984 were evaluated. Because of the ambiguity of the results, further research on the political and economic markets was conducted. The foci within the political markets were on the country-specific political structures and processes, and on their fiscal and monetary policies. In the next section, New Zealand's and Argentina's economic markets were assessed in their ability to provide efficient microeconomic environments. The research concluded with the examination of the national capital markets.

The assessment of North's and Olson's theories and their applicability to the recent economic histories of New Zealand and Argentina provide numerable significant findings in regards to the aforementioned research question.

10.2 Findings

10.2.1 From the Comparison of the Two Theories

The literature review of North's (1994, , 2005b) and Olson's (1996, , 2000) latest academic work discovered their key terms and main hypotheses. Among the key terms are institutions, transaction costs, individual property rights, rationality, and the interaction between individuals and groups.

Both scholars put institutions in the centre of their research. However, neither North's emphasis on the importance of informal institutions, nor Olson's focus on

formal institutions reflects a generally accepted understanding of this term. Transaction costs, their next key element, are based on the work of Ronald Coase; but North and Olson differ considerably in the depth of their analyses and their suggestions about the measurability of these costs. Moreover, both academics' examinations of individual property rights, a further central element, do not consider the different spheres of these complex multi-layered schemes. In addition, North and Olson base their propositions about the decision making of individuals on contrary academic concepts of human rationality. Furthermore, North puts notion on cultural dependent collective learning, while Olson stresses the role of collective actions as the reason of human behaviour. Finally, in general, North's less pinpointed propositions are established on the concepts of other renowned scholars. On the other hand, Olson's definitions appear more simplistic and less dependent on other academics' work. Summarised, because of some lack of clarity in the definitions of the key terms, obstacles for empirical testing of particular economic growth determinants remained.

The evaluation of their main hypotheses focussed on the role of the state, the significance of path-dependency and cultural heritage, and the accountability for economic history by using an ideal-type-real-type methodology.

By referring to the state as the single main source for modern economic growth, North and Olson downplay national factor endowments, and neglect further important national and international sources of policy power. Olson's country-specific formal economic policy hypothesis was discovered as a crucial antipode to North's path-dependent cultural heritage hypothesis. Hence, these differences provided the triggers for examining the reasons for the economic histories of New Zealand and Argentina. In addition, both scholars use real-types to build up their theories of ideal-types, which lead to a limited theoretical foundation of their work. Finally, North and Olson base their propositions on limited national data and, therefore, remain relatively ahistorical.

10.2.2 From the Comparison of the Two Countries

The study evaluated North's and Olson's propositions in their validity of explaining the post-reform economic histories of New Zealand and Argentina. Therefore, the empirical assessment considered the economic growth patterns; the political systems, the fiscal and monetary policies; the economic markets, and the national capital markets of both countries.

The assessment of the GDP per capita data shows that a gap within each of the ideal-type models of North and Olson exists, when NZ is compared to other OECD countries,

or because Argentina exhibits the highest economic growth rates for extended sub-periods. Consequently, Olson's special case of institutional sclerosis might be a better description for New Zealand than North's purified 'success story'.

The examinations of the political systems, the fiscal and monetary policies substantiated North's and Olson's common emphasis on the role of the state in influencing economic growth. Furthermore, the foundation of New Zealand's political system supports North's culture heritage hypothesis. Nevertheless, North's theory lacks the reasoning for NZ's missing checks and balances of its political system. In this case, Olson's institutional sclerosis accounts more appropriately for the research outcome. On the other hand, North's and Olson's Spanish models can explain the misalignment of Argentina's political system to a great extent.

Differences in the pace of the adaptation of radical laissez faire fiscal policies cannot be used to argue in favour of either North's cultural adaptive efficiency hypothesis or Olson's better country-specific economic policy hypothesis. Although NZ's fiscal budget surpluses in later years maybe rated as a distinctive policy advantage, NZ's 'hands-off' policies and their resulting negative outcomes do not reflect the positive characteristics of the British models. On the other hand, Argentina's ill-implemented fiscal policy provides evidence for North's and Olson's Spanish models. However, their frameworks need extensions, because Argentina's decision-makers were erroneously advised by external organisations, like the World Bank.

Furthermore, the study shows that, in contrast to North's and Olson's British models, both countries, NZ and Argentina, implemented the wrong, single aimed monetary policies with their sole focus on lowering inflation; while other elements remained unconsidered. Consequently, Olson's special case of institutional sclerosis may correspond more to the observed reality of NZ than North's propositions.

The findings in regards to the differences of the transaction cost levels and general competition within the two economic markets seem to support North's and Olson's propositions. However, NZ's low rates of innovation and inability to develop an international competitive financial industry point to a gap within each of the ideal-type models of both scholars.

The study supports the ascribed importance of the national capital markets. The country-specific economic policies and levels of property rights clearly influenced the performance of these important economic markets. However, the ideal-type British models of both scholars do not provide reasons for the underdevelopment of NZ's capital markets; especially for its rudimentary stock markets. Lastly, in contrast to the

academics' ideal-type models, both capital markets were equally receptive to corruption.

Summarised, both theories describe the failure of Argentina more accurately than the success of New Zealand. Olson's special case of institutional sclerosis might be a viable alternative in the case of New Zealand. It can be concluded in regards to the abovementioned research question, neither North's 'cultural heritage' hypothesis, nor Olson's 'country-specific economic policy' hypothesis can explain the economic growth patterns of New Zealand and Argentina of the last quarter century, if they remain unmodified.

10.3 Implications

A review of the study reveals a number of contributions to economic theory and economic policy. In the broadest sense, the dissertation contributes to the relevant academic debate by providing the results of a comparison of North's and Olson's latest academic propositions on a theoretical and an empirical basis. Furthermore, the outcomes of the research offer suggestions to decision makers about beneficial revisions of national economic policies.

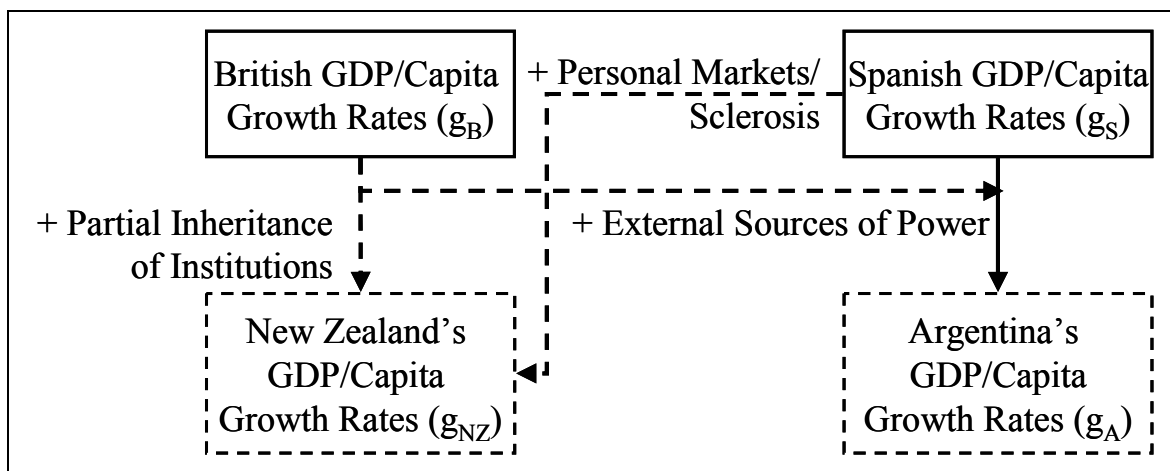
10.3.1 Implications for Economic Theory

As shown by the study, country-specific institutions, transaction costs levels and property rights are significant economic growth determinants. North and Olson correctly underline their importance. However, based on the findings, it can also be concluded that each theory describes the recent economic histories of New Zealand and Argentina only to a limited extent. In other words, North's and Olson's suggested theoretical differences in their ideal-type British and Spanish models suffer from practical inconsistencies. For the sake of simplicity, the following paragraphs will focus on the necessary amendments to both theories.

North's uncontrolled transfer of characteristics from the UK and Spain to their former colonies is only partially possible. National factor endowments, like the size of the population and the distance to other markets, play a more important role on the performance of the markets than acknowledged by North. As shown for the case of New Zealand, North's automatic inheritance of British political and economic diversity has to be replaced by a broader statement, which incorporates the conceivable occurrence of endemic monopolies and lobbying in small markets. Additional propositions should be

developed of how competition in small and distant markets can be fostered. Moreover, the rapid pace of neo-liberal economic reforms in NZ shows that North's propositions of incremental and adaptive efficient institutional change is not a matter of course of the British model. Hence, North's British mental model has to be supplemented by the fact that it can misperceive economic change and, therefore, implement the wrong economic policy. In addition, the national capital markets of North's British model might also include less efficient outcomes. In other words, the ability of capturing the theoretical national output potential can also vary considerably within the samples of the British models. Therefore, North's theory should allow for the possibility that the Spanish model can outperform the British model, depending on the period under consideration. In addition, as seen for Argentina's fiscal and monetary policies, as well as for its capital markets, North's suggestions, about the influence of external sources of power on national economic policy and individual property rights, have to be reassessed. Olson's propositions about institutional sclerosis cover some of the aforementioned shortcomings.

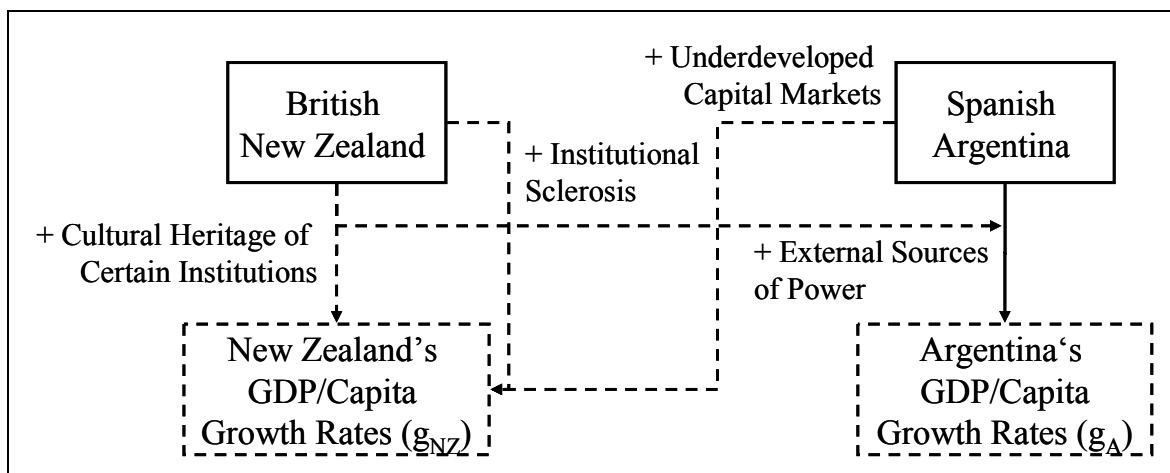
Figure 19: Amendments of North's Common Culture and Economic Growth



On the other hand, Olson's dichotomy of long established versus newly established democracies does not exist to that extent in the case of the research sample. Olson's theory of prevailing property rights and independent judicial coercion as a mere accident of history needs to be updated; for instance by North's cultural heritage hypothesis. In regards to differences in fiscal policies, Olson's institutional sclerosis hypothesis should gain more attention to explain possible extensive lobbying and growth hindering incentives in established democracies. Olson's propositions about national monetary policies proofed to be fragile. As shown by the two sample nations, their inflation rates cannot be used as sole indicators for the quality of institutions. In

contrast, the level of domestic real-interest rates and real-exchange rates showed some evidence of the quality of the incentive structure. However, only when all of these indicators are addressed simultaneously, it can be spoken of a better institutional set-up. Additionally, Olson's theory about economic markets needs to be refined to account for endemic monopolies in sophisticated and deregulated industries of well-established democracies. Further amendments to Olson's propositions in regards to capital markets have to be made. The direction of capital-flows is only partially a viable indicator for good economic policy. In contrast, it could be determined that capital inflows can also be used as a proxy for the lack of the development of sophisticated domestic capital. Finally, Olson's importance of the state will be partially mitigated by the inclusion of further international sources of power, like foreign national courts, and their influences on economic policy and domestic individual property rights.

Figure 20: Amendments of Olson's Political Systems and Economic Growth



It can be concluded that North's and Olson's methodology of using real-types for their ideal-type models neglects certain individual aspects of different economic histories. In general, both scholars can already provide a good reasoning for Argentina's development. However, throughout the study it became evident that New Zealand's economic history is a special case for both theories. Hence, both theories need amendments. Certain elements of the two theories can be exchanged with each other; and further elements have to be redeveloped by future research.

10.3.2 Implication for Economic Policy

The outcome of the research provides advice for the current strategic national economic policy discussions within New Zealand and Argentina. Based on the ideas gained through this comparative study, critical weaknesses in country-specific institutional settings could be identified. In other words, the almost unrestricted pursuit of neo-liberal policies after 1984 must be partially revised in order to enhance future economic growth prospects.

In the case of New Zealand, several tasks become evident. Among them, further checks and balances in the law making process should be established, for instance by the re-introduction of the second chamber of the parliament, or by establishing further means of plurality or supervision over the government's decision-making. However, in reality, these advices possess a more hypothetical value. On the other hand, NZ's fiscal policies provide ground for doable changes. NZ needs a more differentiated tax system. For instance, it should address the economically unjustified spiralling increases in house prices, and foster the development of internationally active, competitive innovative industries (Skilling & Boven, 2006, p. 30). Moreover, on one hand, it should lower the tax-burden, explicit or implicit, of young and low-income households, and of outward foreign direct investments (Skilling & Waldegrave, 2004; Skilling, 2005). On the other hand, simultaneously, it should increase the incentives to save (Skilling & Waldegrave, 2004). NZ's monetary policy should abandon its single aimed focus on low inflation rates and include further targets like the exchange rate and the aforementioned fiscal means (Skilling & Boven, 2006, p. 24). These have to be addressed simultaneously. Otherwise, single interventions of the Reserve Bank in the exchange markets will fail (Subhanij, 2007). Maintaining diversity in the economic markets is another central task for New Zealand's decision makers. Innovative ideas, including the state as participant in the economy, have to be found to increase quality and competition in socially contrived markets, like the banking sector, and national and international infrastructure, like the telecommunication and logistics sectors (Skilling & Boven, 2006, p. 31; Skilling & Boven, 2007). Finally, the financial markets need to be upgraded (OECD, 2007). As an example, the reform of the pension system with the introduction of the Kiwisaver programme is a first step towards higher savings rates and a higher domestic funding of business activities, although amendments are already suggested (ibid).

In the case of Argentina, the most prominent tasks for enhancing the long-run standards of living of its citizens are the comprehensive protection of property and

individual rights; the establishment of limits to lobbying; and the cutting down of transaction costs to foster competition, especially in socially contrived markets.

A more encompassing protection of property rights and less political corruption might be achieved by a reform of the political system (Lewis, 2003, p. 34). The independence of the judiciary and the indefeasibility of the individual rights have to be anchored within its written constitution. Furthermore, the legislative power of the president and the reliance of a MP's seat at the parliament to a particular party should be limited. Increased political awareness of the citizenry can also help to create a more efficient political system (Armony & Armony, 2005, p.49).

In regards to Argentina's fiscal policy, decision maker should strive for governmental budget surpluses by broadening the tax base, and for better governance to limit the influence of interest groups (The World Bank, 2003, p. 45). Furthermore, international trade should be fostered by the reduction of export taxes (ibid). Large, inefficient public work programmes, created as substitutes for social security programmes, should be abolished (ibid, p. 46). The monetary policy should follow its aim to provide a low inflation-rate environment, but should also focus on its links to fiscal policies. In regards to its economic markets, Argentina has to foster competition in the formal sector by decreasing transaction cost levels, as caused by its bureaucracy; and to nurture the strength of its banking system (ibid, p. 46). Furthermore, to foster the supply of capital for its industry, and to lower the reliance on hot money, Argentina has to develop domestic sophisticated bond and stock markets (Bleaney, 2004, p. 713; Hunter, 2006, p. 820).

10.4 Limitations of the Study

Reflections on the study undertaken reveal a number of limitations. Especially, they become evident with respect to the scope of the study, the research approach, and the findings.

Firstly, the scope of the conceptual framework was almost exclusively derived from the propositions of North and Olson. Moreover, the empirical assessment was limited on two deliberately selected countries, New Zealand and Argentina. This leads, by definition, to a biased selection of country-specific data in accordance to North's and Olson's theories (Hodgson, 1998, p. 174). Therefore, other important economic growth determinants, different industries, further indicators, or different countries were left out from the research agenda. In other words, a broader range of samples of important industries, like the foreign trade sectors of the two countries; alternative economic

growth measures; and further countries, might provide a different view on the validity of North's and Olson's theories. An extension of the conceptual framework to incorporate further theories, like Hodgson's (2001a) impurity principle, can be beneficial for the research outcomes. In addition, the evaluation of the impact of the reforms after a short period, a quarter century, can be misleading.

In respect to the research methodology, an abductive approach was chosen as the most appropriate mean to investigate the validity of North's and Olson's theories. However, the terminology and propositions of North and Olson differ in certain aspects,³³ and, therefore, there is no single consistent theory or model, which could be easily tested. Hence, the outcomes of the study depend heavily on the correct interpretation of the key terms and main hypotheses. Especially the development of the individual British and Spanish models, and Olson's diverging propositions about economic growth advantages of democracies and institutional sclerosis are very sensitive to interpretations of the scholars' work. Furthermore, although the conceptual framework provided a guideline through the study, the complexity of the topic made it impossible to have total coverage of the research, as acknowledged by Atkinson and Oleson (1996, p. 710).

Although the approach taken continues to be viewed as appropriate, the findings cannot be easily generalised. Moreover, the nature of a comparative empirical study led to the necessity of accessing different data sources, which hindered the direct comparability, especially in the case of qualitative data (Hodgson, 2001b, p. 9). To overcome these challenges, mutual databases, like the World Development Indicators of the World Bank, were accessed. However, this led to further limitations. These databases missed certain indicators, like real interest rates, or certain time-periods for other data. The lack of access to more specific, non-public or proprietary data, like the comprehensive data sets of the OECD or Statistics New Zealand, led to restraints in the data available for the specific needs of the particular research setting (Sekaran, 2000, p. 256). In addition, improved statistical methods could have provided more insights over correlations between different economic growth determinants. Lastly, there were limits in measuring certain criteria, like property rights, on a quantitative as well as on a qualitative basis.

However, these limitations can be overcome largely by further research and provide further valuable extensions to academic theory as well as economic policymaking.

³³ See Chapter 4 for a more detailed discussion.

10.5 Areas for Further Research

As noted previously, research on the differences in the theories of Douglass North and Mancur Olson, especially on an empirical basis, remains in the early stages. Although this study has contributed to the refinement of academic theory and actual economic policy, a range of issues are still not addressed or explored. Such issues reflect both the scope of this study, as well as the resulting findings.

Due to the novelty of the comparison of North's and Olson's institutional theories, a detailed analysis of their main elements and hypotheses was considered as necessary for this study. It has been shown that theoretical and practical gaps among the key terms institutions, property rights, transaction costs, and competition still remain. In the case of institutions, longer time periods under consideration might reveal more insights about the mutual influence of informal and formal institutions over time, and how 'bad' institutional set-ups can be overcome. Although North's and Olson's emphasis on the importance of property rights could be confirmed, further research is necessary to find out, which are the different layers of these multiple-layered schemes, and how they are established within particular national environments. For example, property rights seem to be protected even without an unwritten constitution in certain countries, for instance in New Zealand, while they are not protected in certain democracies with a written constitution, as in the case of Argentina. Another open point on the research agenda are the particular institutions necessary for specific political and economic markets, like national capital markets, to lower the prevailing transaction cost levels, but to foster diversity, competition, and impersonal markets, especially in small and remote economies. Although these issues have not been uncovered completely by this study, a more refined understanding of both institutional theories could be established. Therefore, the findings of the dissertation may be used subsequently as a basis for investigations of this topic from a broader perspective. Accordingly, the examination of other institutional theories might reveal either further evidence or rejection of North's and Olson's propositions. For instance, Hodgson's (2001a) impurity principle is a viable candidate to enrich the academic discussion.

Moreover, empirical research could encompass further indicators, as well as national key industries and the national infrastructure. Pablo Astorga et. al. (2005) have shown for the case of Argentina that the sole reliance on GDP data does not capture the quality of the living standards in Latin America. Although the development of per capita income was unsatisfactory, the progresses in the literacy and life expectancy rates were comparable to first world economies (ibid, p. 766). Hence, future research should

consider alternative measures of human well-being. Furthermore, different sectors of the economy could be on the research agenda. For instance, Skilling and Boven (2005, , 2007) consider the high level of primary products exports and the accompanying underdeveloped infrastructure, like international internet connection and sea and air ports, as main obstacles for the economic development of New Zealand. In addition, the influence of non-governmental organisations or other sources of political and economic power, both from within the country or abroad, on the national economic policy could also be examined in a more detailed way.

Similarly, the extension of the research on this topic on a larger sample size of different countries will also provide the opportunity to compare and further verify such findings. In particular, subsequent evaluations of North's and Olson's theories may encompass a broader or more diverse sample with respect to the period under consideration or the number of countries with different cultural background. Such research will add a greater level of empirical justification, and, hence, will clarify the extent to which the existing findings can be generalised and associated with a particular theoretical model.

Summarised, the gaps in both theories, as discovered through the dissertation, provide ground for further studies and the development of some refined synthesis or theory. Consequently, future research, as part of a PhD programme, might address some of the open points of the research agenda.

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Appendix A: Major Economic Policy Dates for New Zealand

Date	Incident	Description
14/07/1984	Election Victory of the Labour Party	David Lange becomes the new prime minister ending nine years of National Party rule. Sir Roger Douglas becomes new minister of finance.
18/07/1984-21/12/1984	Abolishment of All Interest Rate and Foreign Exchange Controls	The New Zealand Dollar devalues 20%, and floats free from 1985.
1985	International Re-opening	Limits on foreign ownership were lifted. The speeding up of the phasing out of import licensing was announced.
1986	Constitution Act, Commerce Act	They were passed as means to foster competition in New Zealand.
1986	Goods and Services Tax Introduced; Income Tax Reduced and Simplified	A shift from taxes on income to taxes on spending is implemented. The rich benefited more than the poor from this change.
1987	Restructuring of the State-Owned Enterprises	The Bank of New Zealand is partially privatised. Further nine state-owned enterprises are formed.
15/12/1989	Reserve Bank Act	The Reserve Bank achieves greater independence of with price stability as its main target.
1990	Election Victory of the National Party	Jim Bolger, Prime Minister, and Ruth Richardson, Finance Minister, continue the politics of the Labour Government.
15/05/1991	Employment Contract Act	Compulsory unionism is abolished and replaced by individual employer-employee contracts. Flexibility in the labour market shall lead to rising labour productivity.
01/07/1992	End of Import Licensing	

Date	Incident	Description
06/11/1993	Electoral Referendum	The distribution of the seats in the next parliament, which is elected in 1996, is based on proportional representation. It marks the beginning of rising party plurality in the NZ parliament.
27/06/1994	Fiscal Responsibility Act	The annual setting fiscal goals for a 10-years horizon are required to maintain balanced budgets, prudent levels of debt, and Crown net worth.
2000	Employment Relations Act	The Employment Contract Act from 1991 is replaced.

Source: Belich (2001); Chatterjee & Podder (2007); Dalziel (2002); Easton (1997); Evans et. al. (1996); Jackson (1998); McMillan (2004); Skilling & Waldegrave (2004)

Appendix B: Major Economic Policy Dates for Argentina

Date	Incident	Description
10/12/1983	Establishment of Democracy	The democratic order with universal suffrage and civil rights is re-stored by holding free elections. Raul Alfonsin becomes the President of the state.
June 1985	Austral Plan	During Alfonsin's presidency an independent team headed by Sourrouille develops the first of several economic policy packages to revive Argentina's economy.
1989	Election of President Menem	Because of the on-going lack of economic success, a change in the governing party occurs. It marks the beginning of the establishment of drastic economic policy means.
1990-1991	Convertibility Plan with the Establishment of the Currency Board	Argentina's Peso becomes fixed to the US Dollar to enhance the currency's credibility and to fight high inflation rates. The US Dollar becomes a legal tender in Argentina.
1992	Brady Plan	Its debt burden, as collected over the preceding decades, leaves Argentina with an unpayable account. The restructuring negotiations, which allow Argentina to write-off a credible amount of its foreign debt, are concluded with the Brady Plan in 1992.
1993	Reform of the Pension System	Changes from a pay-as-you-go system to a funded system are implemented in 1994. It leaves the state with even higher social security payments.
Until 1994	Implementation of Further Neo-Liberal Economic Policy Means	President Menem and Minister of Economy Cavallo wanted to connect Argentina's economy to its successful history from the beginning of the preceding century by comprehensive privatisations; capital and current account liberalisation; and labour market reforms.

Date	Incident	Description
1994	Change of the Constitution	The shift to the direct election of the members of the Congress represents the latest amendment of the formal constitution.
1995	Further Reforms	Foreign trade is further liberalised by the establishment of the South-American free-trade zone, Mercosur. Labour taxes are lowered. The banking system is restructured after the Mexican crisis in 1994. President Carlos Saul Menem is re- elected.
1996	Trabajar Programme	Start of a huge public work programme, with a low wage rate for community projects in poor areas, as substitute for unemployment systems.
1999	General Elections	Alliance of UCR and Frepaso comes into governmental power again.
09/01/2002	End of the Currency Board	Due to the economic crisis and the collapse of the currency board, the Argentine Peso starts free-floating. The exchange rate falls to one-third of its pre-crisis levels.

Source: Armony & Armony (2005); Arza (2006); Astorga et. al. (2005); Bleaney (2004); Bruno (2006); Kitano (2005); Kydland & Zarazaga (2003); Ladmann (1998); Lewis (2003, , n. d.); Loayza et. al. (2005); Sanchez & Butler (2004); Sanz-Villarroya (2005)

Appendix C: Ethnic Income Distribution for New Zealand

	1983/84	1991/92	1995/96	1997/98
	Income Share / Population Share	Income Share / Population Share	Income Share / Population Share	Income Share / Population Share
Pākehā	1.05	1.09	1.07	1.08
Māori and Pacific Islanders	0.65	0.61	0.65	0.66
Others	0.85	0.96	0.79	0.67

Source: Chatterjee and Podder (2007, p. 20), Table 1; own calculations; a value of “1” means income share equals population share