13.

WHY NATIONS FAIL TODAY

HOW TO WIN THE LOTTERY IN ZIMBABWE

IT WAS JANUARY 2000 in Harare, Zimbabwe. Master of Ceremonies Fallot Chawawa was in charge of drawing the winning ticket for the national lottery organized by a partly state-owned bank, the Zimbabwe Banking Corporation (Zimbank). The lottery was open to all clients who had kept five thousand or more Zimbabwe dollars in their accounts during December 1999. When Chawawa drew the ticket, he was dumfounded. As the public statement of Zimbank put it, "Master of Ceremonies Fallot Chawawa could hardly believe his eyes when the ticket drawn for the Z$100,000 prize was handed to him and he saw His Excellency RG Mugabe written on it."

President Robert Mugabe, who had ruled Zimbabwe by hook or by crook, and usually with an iron fist, since 1980, had won the lottery, which was worth a hundred thousand Zimbabwe dollars, about five times the annual per capita income of the country. Zimbank claimed that Mr. Mugabe's name had been drawn from among thousands of eligible customers. What a lucky man! Needless to say he didn't really need the money. Mugabe had in fact only recently awarded himself and his cabinet salary hikes of up to 200 percent.

The lottery ticket was just one more indication of Zimbabwe's extractive institutions. One could call this corruption, but it is just a symptom of the institutional malaise in Zimbabwe. The fact that Mugabe could even win the lottery if he wanted showed how much control he had over matters in Zimbabwe, and gave the world a glimpse of the extent of the country's extractive institutions.

The most common reason why nations fail today is because they

have extractive institutions. Zimbabwe under Mugabe's regime vividly illustrates the economic and social consequences. Though the national statistics in Zimbabwe are very unreliable, the best estimate is that by 2008, Zimbabwe's per capita income was about half of what it was when the country gained its independence in 1980. Dramatic as this sounds, it does not in fact begin to capture the deterioration in living standards in Zimbabwe. The state has collapsed and more or less stopped providing any basic public services. In 2008–2009 the deterioration in the health systems led to an outbreak of cholera across the country. As of January 10, 2010, there have been 98,741 reported cases and 4,293 deaths, making it the deadliest cholera outbreak in Africa over the previous fifteen years. In the meantime, mass unemployment has also reached unprecedented levels. In early 2009, the UN Office for the Coordination of Humanitarian Affairs claimed that the unemployment rate had hit an incredible 94 percent.

The roots of many economic and political institutions in Zimbabwe, as is the case for much of sub-Saharan Africa, can be traced back to the colonial period. In 1890 Cecil Rhodes's British South Africa Company sent a military expedition into the then-kingdom of the Ndebele, based in Matabeleland, and also into the neighboring Mashonaland. Their superior weaponry quickly suppressed African resistance, and by 1901 the colony of Southern Rhodesia, named after Rhodes, had been formed in the area that is currently Zimbabwe. Now that the area was a privately owned concession of the British South Africa Company, Rhodes anticipated making money there through prospecting and mining for precious minerals. The ventures never got off the ground, but the very rich farmlands began attracting white migration. These settlers soon annexed much of the land. By 1923 they had freed themselves from the rule of the British South Africa Company and persuaded the British government to grant them self-government. What then occurred is very similar to what had happened in South Africa a decade or so previously. The 1913 Natives Land Act (pages 265–266) created a dual economy in South Africa. Rhodesia passed very similar laws, and inspired by the South African model, a white-only apartheid state was constructed soon after 1923.

As the European colonial empires collapsed in the late 1950s and

early 1960s, the white elite in Rhodesia, led by Ian Smith, comprising possibly 5 percent of the population, declared independence from Britain in 1965. Few international governments recognized Rhodesia's independence, and the United Nations levied economic and political sanctions against it. The black citizens organized a guerrilla war from bases in the neighboring countries of Mozambique and Zambia. International pressure and the rebellion waged by the two main groups, Mugabe's ZANU (the Zimbabwe African National Union) and ZAPU (the Zimbabwe African People's Union), led by Joshua Nkomo, resulted in a negotiated end to white rule. The state of Zimbabwe was created in 1980.

After independence, Mugabe quickly established his personal control. He either violently eliminated his opponents or co-opted them. The most egregious acts of violence happened in Matabeleland, the heartland of support for ZAPU, where as many as twenty thousand people were killed in the early 1980s. By 1987 ZAPU had merged with ZANU to create ZANU-PF, and Joshua Nkomo was sidelined politically. Mugabe was able to rewrite the constitution he had inherited as a part of the independence negotiation, making himself president (he had started as prime minister), abolishing white voter rolls that were part of the independence agreement, and eventually, in 1990, getting rid of the Senate altogether and introducing positions in the legislature that he could nominate. A de facto one-party state headed by Mugabe was the result.

Upon independence, Mugabe took over a set of extractive economic institutions created by the white regime. These included a host of regulations on prices and international trade, state-run industries, and the obligatory agricultural marketing boards. State employment expanded rapidly, with jobs given to supporters of ZANU-PF. The tight government regulation of the economy suited the ZANU-PF elites because it made it difficult for an independent class of African businessmen, who might then have challenged the former's political monopoly, to emerge. This was very similar to the situation we saw in Ghana in the 1960s in chapter 2 (pages 64–68). Ironically, of course, this left whites as the main business class. During this period the main strengths of the white economy, particularly the highly productive

agricultural export sector, was left untouched. But this would last only until Mugabe became unpopular.

The model of regulation and market intervention gradually became unsustainable, and a process of institutional change, with the support of the World Bank and the International Monetary Fund, began in 1991 after a severe fiscal crisis. The deteriorating economic performance finally led to the emergence of a serious political opposition to ZANU-PF's one-party rule: the Movement for Democratic Change (MDC). The 1995 parliamentary elections were far from competitive. ZANU-PF won 81 percent of the vote and 118 out of the 120 seats. Fifty-five of these members of Parliament were elected unopposed. The presidential election the following year showed even more signs of irregularities and fraud. Mugabe won 93 percent of the vote, but his two opponents, Abel Muzorewa and Ndabaningi Sithole, had already withdrawn their candidacy prior to the election, accusing the government of coercion and fraud.

After 2000, despite all the corruption, ZANU-PF's grip was weakening. It took only 49 percent of the popular vote, and only 63 seats. All were contested by the MDC, who took every seat in the capital, Harare. In the presidential election of 2002, Mugabe scraped home with only 56 percent of the vote. Both sets of elections went ZANU-PF's way only because of violence and intimidation, coupled with electoral fraud.

The response of Mugabe to the breakdown of his political control was to intensify both the repression and the use of government policies to buy support. He unleashed a full-scale assault on white landowners. Starting in 2000, he encouraged and supported an extensive series of land occupations and expropriations. They were often led by war veterans' associations, groups supposedly comprised of former combatants in the war of independence. Some of the expropriated land was given to these groups, but much of it also went to the ZANU-PF elites. The insecurity of property rights wrought by Mugabe and ZANU-PF led to a collapse of agricultural output and productivity. As the economy crumbled, the only thing left was to print money to buy support, which led to enormous hyperinflation. In January 2009, it became legal to use other currencies, such as the South African

rand, and the Zimbabwean dollar vanished from circulation, a worthless piece of paper.

What happened in Zimbabwe after 1980 was commonplace in sub-Saharan Africa since independence. Zimbabwe inherited a set of highly extractive political and economic institutions in 1980. For the first decade and a half, these were maintained relatively untouched. While elections took place, political institutions were anything but inclusive. Economic institutions changed somewhat; for example, there was no longer explicit discrimination against blacks. But on the whole the institutions remained extractive, with the only difference being that instead of Ian Smith and the whites doing the extracting, it was Robert Mugabe and the ZANU-PF elites filling their pockets. Over time the institutions became even more extractive, and incomes in Zimbabwe collapsed. The economic and political failure in Zimbabwe is yet another manifestation of the iron law of oligarchy—in this instance, with the extractive and repressive regime of Ian Smith being replaced by the extractive, corrupt, and repressive regime of Robert Mugabe. Mugabe's fake lottery win in 2000 was then simply the tip of a very corrupt and historically shaped iceberg.

NATIONS FAIL TODAY because their extractive economic institutions do not create the incentives needed for people to save, invest, and innovate. Extractive political institutions support these economic institutions by cementing the power of those who benefit from the extraction. Extractive economic and political institutions, though their details vary under different circumstances, are always at the root of this failure. In many cases, for example, as we will see in Argentina, Colombia, and Egypt, this failure takes the form of lack of sufficient economic activity, because the politicians are just too happy to extract resources or quash any type of independent economic activity that threatens themselves and the economic elites. In some extreme cases, as in Zimbabwe and Sierra Leone, which we discuss next, extractive institutions pave the way for complete state failure, destroying not only law and order but also even the most basic economic incentives. The result is economic stagnation and—as the recent history of

Angola, Cameroon, Chad, the Democratic Republic of Congo, Haiti, Liberia, Nepal, Sierra Leone, Sudan, and Zimbabwe illustrates—civil wars, mass displacements, famines, and epidemics, making many of these countries poorer today than they were in the 1960s.

A CHILDREN'S CRUSADE?

On March 23, 1991, a group of armed men under the leadership of Foday Sankoh crossed the border from Liberia into Sierra Leone and attacked the southern frontier town of Kailahun. Sankoh, formerly a corporal in the Sierra Leonean army, had been imprisoned after taking part in an abortive coup against Siaka Stevens's government in 1971. After being released, he eventually ended up in Libya, where he entered a training camp that the Libyan dictator Colonel Qaddafi ran for African revolutionaries. There he met Charles Taylor, who was plotting to overthrow the government in Liberia. When Taylor invaded Liberia on Christmas Eve 1989, Sankoh was with him, and it was with a group of Taylor's men, mostly Liberians and Burkinabes (citizens of Burkina Faso), that Sankoh invaded Sierra Leone. They called themselves the RUF, the Revolutionary United Front, and they announced that they were there to overthrow the corrupt and tyrannical government of the APC.

As we saw in the previous chapter, Siaka Stevens and his All People's Congress, the APC, took over and intensified the extractive institutions of colonial rule in Sierra Leone, just as Mugabe and ZANU-PF did in Zimbabwe. By 1985, when Stevens, ill with cancer, brought in Joseph Momoh to replace him, the economy was collapsing. Stevens, apparently without irony, used to enjoy quoting the aphorism "The cow eats where it is tethered." And where Stevens had once eaten, Momoh now gorged. The roads fell to pieces, and schools disintegrated. National television broadcasts stopped in 1987, when the transmitter was sold by the minister of information, and in 1989 a radio tower that relayed radio signals outside Freetown fell down, ending transmissions outside the capital. An analysis published in a newspaper in the capital city of Freetown in 1995 rings very true:

> by the end of Momoh's rule he had stopped paying civil servants, teachers and even Paramount Chiefs. Central government had collapsed, and then of course we had border incursions, "rebels" and all the automatic weapons pouring over the border from Liberia. The NPRC, the "rebels" and the "sobels" [soldiers turned rebels] all amount to the chaos one expects when government disappears. None of them are the causes of our problems, but they are symptoms.

The collapse of the state under Momoh, once again a consequence of the vicious circle unleashed by the extreme extractive institutions under Stevens, meant that there was nothing to stop the RUF from coming across the border in 1991. The state had no capacity to oppose it. Stevens had already emasculated the military, because he worried they might overthrow him. It was then easy for a relatively small number of armed men to create chaos in most of the country. They even had a manifesto called "Footpaths to Democracy," which started with a quote from the black intellectual Frantz Fanon: "Each generation must, out of relative obscurity, discover its mission, fulfill it or betray it." The section "What Are We Fighting For?" begins:

> We continue to fight because we are tired of being perpetual victims of state sponsored poverty and human degradation visited on us by years of autocratic rule and militarism. But, we shall exercise restraint and continue to wait patiently at the rendezvous of peace—where we shall all be winners. We are committed to peace, by any means necessary, but what we are not committed to is becoming victims of peace. We know our cause to be just and God/Allah will never abandon us in our struggle to reconstruct a new Sierra Leone.

Though Sankoh and other RUF leaders may have started with political grievances, and the grievances of the people suffering under

the APC's extractive institutions may have encouraged them to join the movement early on, the situation quickly changed and spun out of control. The "mission" of the RUF plunged the country into agony, as in the testimony of a teenager from Geoma, in the south of Sierra Leone:

> They gathered some of us . . . They chose some of our friends and killed them, two of them. These were people whose fathers were the chiefs, and they had soldiers' boots and property in their houses. They were shot, for no other reason than that they were accused of harbouring soldiers. The chiefs were also killed—as part of the government. They chose someone to be the new chief. They were still saying they had come to free us from the APC. After a point, they were not choosing people to kill, just shooting people.

In the first year of the invasion, any intellectual roots that the RUF may have had were completely extinguished. Sankoh executed those who criticized the mounting stream of atrocities. Soon, few voluntarily joined the RUF. Instead they turned to forcible recruitment, particularly of children. Indeed, all sides did this, including the army. If the Sierra Leonean civil war was a crusade to build a better society, in the end it was a children's crusade. The conflict intensified with massacres and massive human rights abuses, including mass rapes and the amputation of hands and ears. When the RUF took over areas, they also engaged in economic exploitation. It was most obvious in the diamond mining areas, where they press-ganged people into diamond mining, but was widespread elsewhere as well.

The RUF wasn't alone in committing atrocities, massacres, and organized forced labor. The government did so as well. Such was the collapse of law and order that it became difficult for people to tell who was a soldier and who was a rebel. Military discipline completely vanished. By the time the war ended in 2001, probably eighty thousand people had died and the whole country had been devastated. Roads, houses, and buildings were entirely destroyed. Today, if you

go to Koidu, a major diamond-producing area in the east, you'll still see rows of burned-out houses scarred with bullet holes.

By 1991 the state in Sierra Leone had totally failed. Think of what King Shyaam started with the Bushong (pages 133–136): he set up extractive institutions to cement his power and extract the output the rest of society would produce. But even extractive institutions with central authority concentrated in his hands were an improvement over the situation without any law and order, central authority, or property rights that characterized the Lele society on the other side of the river Kasai. Such lack of order and central authority has been the fate of many African nations in recent decades, partly because the process of political centralization was historically delayed in much of sub-Saharan Africa, but also because the vicious circle of extractive institutions reversed any state centralization that existed, paving the way for state failure.

Sierra Leone during her bloody civil war of ten years, from 1991 to 2001, was a typical case of a failed state. It started out as just another country marred by extractive institutions, albeit of a particularly vicious and inefficient type. Countries become failed states not because of their geography or their culture, but because of the legacy of extractive institutions, which concentrate power and wealth in the hands of those controlling the state, opening the way for unrest, strife, and civil war. Extractive institutions also directly contribute to the gradual failing of the state by neglecting investment in the most basic public services, exactly what happened in Sierra Leone.

Extractive institutions that expropriate and impoverish the people and block economic development are quite common in Africa, Asia, and South America. Charles Taylor helped to start the civil war in Sierra Leone while at the same time initiating a savage conflict in Liberia, which led to state failure there, too. The pattern of extractive institutions collapsing into civil war and state failure has happened elsewhere in Africa; for example, in Angola, Côte d'Ivoire, the Democratic Republic of Congo, Mozambique, Republic of Congo, Somalia, Sudan, and Uganda. Extraction paves the way for conflict, not unlike the conflict that the highly extractive institutions of the Maya city-states generated almost a thousand years ago. Conflict precipitates

state failure. So another reason why nations fail today is that their states fail. This, in turn, is a consequence of decades of rule under extractive economic and political institutions.

WHO IS THE STATE?

The cases of Zimbabwe, Somalia, and Sierra Leone, even if typical of poor countries in Africa, and perhaps even some in Asia, seem rather extreme. Surely Latin American countries do not have failed states? Surely their presidents are not brazen enough to win the lottery?

In Colombia, the Andean Mountains gradually merge to the north with a large coastal plain that borders the Caribbean Ocean. Colombians call this the *tierra caliente,* the "hot country," as distinct from the Andean world of the *tierra fria,* the "cold country." For the last fifty years, Colombia has been regarded by most political scientists and governments as a democracy. The United States feels happy to negotiate a potential free trade agreement with the country and pours all kinds of aid into it, particularly military aid. After a short-lived military government, which ended in 1958, elections have been regularly held, even though until 1974 a pact rotated political power and the presidency between the two traditional political parties, the Conservatives and the Liberals. Still, this pact, the National Front, was itself ratified by the Colombian people via a plebiscite, and this all seems democratic enough.

Yet while Colombia has a long history of democratic elections, it does not have inclusive institutions. Instead, its history has been marred by violations of civil liberties, extrajudicial executions, violence against civilians, and civil war. Not the sort of outcomes we expect from a democracy. The civil war in Colombia is different from that in Sierra Leone, where the state and society collapsed and chaos reigned. But it is a civil war nonetheless and one that has caused far more casualties. The military rule of the 1950s was itself partially in response to a civil war known in Spanish simply as La Violencia, or "The Violence." Since that time quite a range of insurgent groups, mostly communist revolutionaries, have plagued the countryside, kidnapping and murdering. To avoid either of these unpleasant options

in rural Colombia, you have to pay the *vacuna,* literally "the vaccination," meaning that you have to vaccinate yourself against being murdered or kidnapped by paying off some group of armed thugs each month.

Not all armed groups in Colombia are communists. In 1981 members of the main communist guerrilla group in Colombia, the Fuerzas Armadas Revolucionarias de Colombia (the FARC—the Revolutionary Armed Forces of Colombia) kidnapped a dairy farmer, Jesus Castaño, who lived in a small town called Amalfi in the hot country in the northeastern part of the department of Antioquia. The FARC demanded a ransom amounting to $7,500, a small fortune in rural Colombia. The family raised it by mortgaging the farm, but their father's corpse was found anyway, chained to a tree. Enough was enough for three of Castaño's sons, Carlos, Fidel, and Vicente. They founded a paramilitary group, Los Tangueros, to hunt down members of the FARC and avenge this act. The brothers were good at organizing, and soon their group grew and began to find a common interest with other similar paramilitary groups that had developed from similar causes. Colombians in many areas were suffering at the hands of left-wing guerrillas, and right-wing paramilitaries formed in opposition. Paramilitaries were being used by landowners to defend themselves against the guerrillas, but they were also involved in drug trafficking, extortion, and the kidnapping and murder of citizens.

By 1997 the paramilitaries, under the leadership of the Castaño brothers, had managed to form a national organization for paramilitaries called the Autodefensas Unidas de Colombia (the AUC—United Self-Defense Forces of Colombia). The AUC expanded into large parts of the country, particularly into the hot country, in the departments of Córdoba, Sucre, Magdalena, and César. By 2001 the AUC may have had as many as thirty thousand armed men at its disposal and was organized into different blocks. In Córdoba, the paramilitary Bloque Catatumbo was led by Salvatore Mancuso. As its power continued to grow, the AUC made a strategic decision to get involved in politics. Paramilitaries and politicians courted each other. Several of the leaders of the AUC organized a meeting with prominent politicians in the town of Santa Fé de Ralito in Córdoba. A joint document, a pact, calling for the "refounding of the country" was issued and signed by leading members of the AUC, such as "Jorge 40" (the nickname for Rodrigo Tovar Pupo), Adolfo Paz (a nom de guerre for Diego Fernando "Don Berna" Murillo), and Diego Vecino (real name: Edwar Cobo Téllez), along with politicians, including national senators William Montes and Miguel de la Espriella. By this point the AUC was running large tracts of Colombia, and it was easy for them to fix who got elected in the 2002 elections for the Congress and Senate. For example, in the municipality of San Onofre, in Sucre, the election was arranged by the paramilitary leader Cadena ("chain"). One eyewitness described what happened as follows:

> The trucks sent by Cadena went around the neighborhoods, corregimientos and rural areas of San Onofre picking people up. According to some inhabitants . . . for the 2002 elections hundreds of peasants were taken to the corregimiento Plan Parejo so they could see the faces of the candidates they had to vote for in the parliamentarian elections: Jairo Merlano for Senate and Muriel Benito Rebollo for Congress.
>
> Cadena put in a bag the names of the members of the municipal council, took out two and said that he would kill them and other people chosen randomly if Muriel did not win.

The threat seems to have worked: each candidate obtained forty thousand votes in the whole of Sucre. It is no surprise that the mayor of San Onofre signed the pact of Santa Fé de Ralito. Probably one-third of the congressmen and senators owed their election in 2002 to paramilitary support, and Map 20 (page 380), which depicts the areas of Colombia under paramilitary control, shows how widespread their hold was. Salvatore Mancuso himself put it in an interview in the following way:

> 35 percent of the Congress was elected in areas where there were states of the Self-Defense groups, in those

> states we were the ones collecting taxes, we delivered justice, and we had the military and territorial control of the region and all the people who wanted to go into politics had to come and deal with the political representatives we had there.

It is not difficult to imagine the effect of this extent of paramilitary control of politics and society on economic institutions and public policy. The expansion of the AUC was not a peaceful affair. The

Map 20: Paramilitary presence across Colombia, 1997–2005

group not only fought against the FARC, but also murdered innocent civilians and terrorized and displaced hundreds of thousands of people from their homes. According to the Internal Displacement Monitoring Centre (IDMC) of the Norwegian Refugee Council, in early 2010 around 10 percent of Colombia's population, nearly 4.5 million people, was internally displaced. The paramilitaries also, as Mancuso suggested, took over the government and all its functions, except that the taxes they collected were just expropriation for their own pockets. An extraordinary pact between the paramilitary leader Martín Llanos (real name: Héctor Germán Buitrago) and the mayors of the municipalities of Tauramena, Aguazul, Maní, Villanueva, Monterrey, and Sabanalarga, in the department of Casanare in eastern Colombia, lists the following rules to which the mayors had to adhere by order of the "Paramilitary Peasants of Casanare":

9) Give 50 percent of the municipality budget to be managed by the Paramilitary Peasants of Casanare.
10) 10 percent of each and every contract of the municipality [to be given to the Paramilitary Peasants of Casanare].
11) Mandatory assistance to all the meetings called by the Paramilitary Peasants of Casanare.
12) Inclusion of the Paramilitary Peasants of Casanare in every infrastructure project.
13) Affiliation to the new political party formed by the Paramilitary Peasants of Casanare.
14) Accomplishment of his/hers governance program.

Casanare is not a poor department. On the contrary, it has the highest level of per capita income of any Colombian department, because it has significant oil deposits, just the kind of resources that attract paramilitaries. In fact, once they gained power, the paramilitaries intensified their systematic expropriation of property. Mancuso himself reputedly accumulated $25 million worth of urban and rural property. Estimates of land expropriated in Colombia by paramilitaries are as high as 10 percent of all rural land.

Colombia is not a case of a failed state about to collapse. But it is

a state without sufficient centralization and with far-from-complete authority over all its territory. Though the state is able to provide security and public services in large urban areas such as Bogotá and Barranquilla, there are significant parts of the country where it provides few public services and almost no law and order. Instead, alternative groups and people, such as Mancuso, control politics and resources. In parts of the country, economic institutions function quite well, and there are high levels of human capital and entrepreneurial skill; in other parts the institutions are highly extractive, even failing to provide a minimal degree of state authority.

It might be hard to understand how a situation like this can sustain itself for decades, even centuries. But in fact, the situation has a logic of its own, as a type of vicious circle. Violence and the absence of centralized state institutions of this type enter into a symbiotic relationship with politicians running the functional parts of the society. The symbiotic relationship arises because national politicians exploit the lawlessness in peripheral parts of the country, while paramilitary groups are left to their own devices by the national government.

This pattern became particularly apparent in the 2000s. In 2002 the presidential election was won by Álvaro Uribe. Uribe had something in common with the Castaño brothers: his father had been killed by the FARC. Uribe ran a campaign repudiating the attempts of the previous administration to try to make peace with the FARC. In 2002 his vote share was 3 percentage points higher in areas with paramilitaries than without them. In 2006, when he was reelected, his vote share was 11 percentage points higher in such areas. If Mancuso and his partners could deliver the vote for Congress and the Senate, they could do so in presidential elections as well, particularly for a president strongly aligned with their worldview and likely to be lenient on them. As Jairo Angarita, Salvatore Mancuso's deputy and the former leader of the AUC's Sinú and San Jorge blocs, declared in September 2005, he was proud to work for the "reelection of the best president we have ever had."

Once elected, the paramilitary senators and congressmen voted for what Uribe wanted, in particular changing the constitution so that he

could be reelected in 2006, which had not been allowed at the time of his first election, in 2002. In exchange, President Uribe delivered a highly lenient law that allowed the paramilitaries to demobilize. Demobilization did not mean the end of paramilitarism, simply its institutionalization in large parts of Colombia and the Colombian state, which the paramilitaries had taken over and were allowed to keep.

In Colombia many aspects of economic and political institutions have become more inclusive over time. But certain major extractive elements remain. Lawlessness and insecure property rights are endemic in large swaths of the country, and this is a consequence of the lack of control by the national state in many parts of the country, and the particular form of lack of state centralization in Colombia. But this state of affairs is not an inevitable outcome. It is itself a consequence of dynamics mirroring the vicious circle: political institutions in Colombia do not generate incentives for politicians to provide public services and law and order in much of the country and do not put enough constraints on them to prevent them from entering into implicit or explicit deals with paramilitaries and thugs.

EL CORRALITO

Argentina was in the grip of an economic crisis in late 2001. For three years, income had been falling, unemployment had been rising, and the country had accumulated a massive international debt. The policies leading to this situation were adopted after 1989 by the government of Carlos Menem, to stop hyperinflation and stabilize the economy. For a time they were successful.

In 1991 Menem tied the Argentine peso to the U.S. dollar. One peso was equal to one dollar by law. There was to be no change in the exchange rate. End of story. Well, almost. To convince people that the government really meant to stick to the law, it persuaded people to open bank accounts in U.S. dollars. Dollars could be used in the shops of the capital city of Buenos Aires and withdrawn from cash machines all over the city. This policy may have helped stabilize the economy, but it had one big drawback. It made Argentine exports

very expensive and foreign imports very cheap. Exports dribbled to a halt; imports gushed in. The only way to pay for them was to borrow. It was an unsustainable situation. As more people began worrying about the sustainability of the peso, they put more of their wealth into dollar accounts at banks. After all, if the government ripped up the law and devalued the peso, they would be safe with dollar accounts, right? They were right to be worried about the peso. But they were too optimistic about their dollars.

On December 1, 2001, the government froze all bank accounts, initially for ninety days. Only a small amount of cash was allowed for withdrawal on a weekly basis. First it was 250 pesos, still worth $250; then 300 pesos. But this was allowed to be withdrawn only from peso accounts. Nobody was allowed to withdraw money from their dollar accounts, unless they agreed to convert the dollars into pesos. Nobody wanted to do so. Argentines dubbed this situation El Corralito, "the Little Corral": depositors were hemmed into a corral like cows, with nowhere to go. In January the devaluation was finally enacted, and instead of there being one peso for one dollar, there were soon four pesos for one dollar. This should have been a vindication of those who thought that they should put their savings in dollars. But it wasn't, because the government then forcibly converted all the dollar bank accounts into pesos, but at the old one-for-one exchange rate. Someone who had had $1,000 saved suddenly found himself with only $250. The government had expropriated three-quarters of people's savings.

For economists, Argentina is a perplexing country. To illustrate how difficult it was to understand Argentina, the Nobel Prize–winning economist Simon Kuznets once famously remarked that there were four sorts of countries: developed, underdeveloped, Japan, and Argentina. Kuznets thought so because, around the time of the First World War, Argentina was one of the richest countries in the world. It then began a steady decline relative to the other rich countries in Western Europe and North America, which turned, in the 1970s and '80s, into an absolute decline. On the surface of it, Argentina's economic performance is puzzling, but the reasons for its decline be-

come clearer when looked at through the lens of inclusive and extractive institutions.

It is true that before 1914, Argentina experienced around fifty years of economic growth, but this was a classic case of growth under extractive institutions. Argentina was then ruled by a narrow elite heavily invested in the agricultural export economy. The economy grew by exporting beef, hides, and grain in the middle of a boom in the world prices of these commodities. Like all such experiences of growth under extractive institutions, it involved no creative destruction and no innovation. And it was not sustainable. Around the time of the First World War, mounting political instability and armed revolts induced the Argentine elites to try to broaden the political system, but this led to the mobilization of forces they could not control, and in 1930 came the first military coup. Between then and 1983, Argentina oscillated backward and forward between dictatorship and democracy and between various extractive institutions. There was mass repression under military rule, which peaked in the 1970s with at least nine thousand people and probably far more being illegally executed. Hundreds of thousands were imprisoned and tortured.

During the periods of civilian rule there were elections—a democracy of sorts. But the political system was far from inclusive. Since the rise of Perón in the 1940s, democratic Argentina has been dominated by the political party he created, the Partido Justicialista, usually just called the Perónist Party. The Perónists won elections thanks to a huge political machine, which succeeded by buying votes, dispensing patronage, and engaging in corruption, including government contracts and jobs in exchange for political support. In a sense this was a democracy, but it was not pluralistic. Power was highly concentrated in the Perónist Party, which faced few constraints on what it could do, at least in the period when the military restrained from throwing it from power. As we saw earlier (pages 329–332), if the Supreme Court challenged a policy, so much the worse for the Supreme Court.

In the 1940s, Perón had cultivated the labor movement as a political base. When it was weakened by military repression in the 1970s and '80s, his party simply switched to buying votes from others

instead. Economic policies and institutions were designed to deliver income to their supporters, not to create a level playing field. When President Menem faced a term limit that kept him from being re-elected in the 1990s, it was just more of the same; he could simply rewrite the constitution and get rid of the term limit. As El Corralito shows, even if Argentina has elections and popularly elected governments, the government is quite able to override property rights and expropriate its own citizens with impunity. There is little check on Argentine presidents and political elites, and certainly no pluralism.

What puzzled Kuznets, and no doubt many others who visit Buenos Aires, is that the city seems so different from Lima, Guatemala City, or even Mexico City. You do not see indigenous people, and you do not see the descendants of former slaves. Mostly you see the glorious architecture and buildings put up during the Belle Epoch, the years of growth under extractive institutions. But in Buenos Aires you see only part of Argentina. Menem, for example, was not from Buenos Aires. He was born in Anillaco, in the province of La Rioja, in the mountains far to the northwest of Buenos Aires, and he served three terms as governor of the province. At the time of the conquest of the Americas by the Spanish, this area of Argentina was an outlying part of the Inca Empire and had a dense population of indigenous people (see Map 1 on page 17). The Spanish created *encomiendas* here, and a highly extractive economy developed growing food and breeding mules for the miners in Potosí to the north. In fact, La Rioja was much more like the area of Potosí in Peru and Bolivia than it was like Buenos Aires. In the nineteenth century, La Rioja produced the famous warlord Facundo Quiroga, who ruled the area lawlessly and marched his army on Buenos Aires. The story about the development of Argentine political institutions is a story about how the interior provinces, such as La Rioja, reached agreements with Buenos Aires. These agreements were a truce: the warlords of La Rioja agreed to leave Buenos Aires alone so that it could make money. In return, the Buenos Aires elites gave up on reforming the institutions of "the interior." So Argentina at first appears a world apart from Peru or Bolivia, but it is really not so different once you leave the elegant boulevards of Buenos Aires. That the preferences and the politics of the interior got embedded into Argentine institutions is the reason why the country has experienced a very similar institutional path to those of other extractive Latin American countries.

That elections have not brought either inclusive political or economic institutions is the typical case in Latin America. In Colombia, paramilitaries can fix one-third of national elections. In Venezuela today, as in Argentina, the democratically elected government of Hugo Chávez attacks its opponents, fires them from public-sector jobs, closes down newspapers whose editorials it doesn't like, and expropriates property. In whatever he does, Chávez is much more powerful and less constrained than Sir Robert Walpole was in Britain in the 1720s, when he was unable to condemn John Huntridge under the Black Act (pages 302–308). Huntridge would have fared much less well in present-day Venezuela or Argentina.

While the democracy emerging in Latin America is in principle diametrically opposed to elite rule, and in rhetoric and action it tries to redistribute rights and opportunities away from at least a segment of the elite, its roots are firmly based in extractive regimes in two senses. First, inequities persisting for centuries under extractive regimes make voters in newly emerging democracies vote in favor of politicians with extreme policies. It is not that Argentinians are just naïve and think that Juan Perón or the more recent Perónist politicians such as Menem or the Kirchners are selfless and looking out for their interests, or that Venezuelans see their salvation in Chávez. Instead, many Argentinians and Venezuelans recognize that all other politicians and parties have for so long failed to give them voice, to provide them with the most basic public services, such as roads and education, and to protect them from exploitation by local elites. So many Venezuelans today support the policies that Chávez is adopting even if these come with corruption and waste in the same way that many Argentinians supported Perón's policies in the 1940s and 1970s. Second, it is again the underlying extractive institutions that make politics so attractive to, and so biased in favor of, strongmen such as Perón and Chávez, rather than an effective party system producing socially desirable alternatives. Perón, Chávez, and dozens of other strongmen in Latin America are just another facet of the iron law of

oligarchy, and as the name suggests, the roots of this iron law lies in the underlying elite-controlled regimes.

THE NEW ABSOLUTISM

In November 2009, the government of North Korea implemented what economists call a currency reform. Severe bouts of inflation are often the reasons for such reforms. In France in January 1960, a currency reform introduced a new franc that was equal to 100 of the existing francs. Old francs continued in circulation and people even quoted prices in them as the change to the new francs was gradually made. Finally, old francs ceased to be legal tender in January 2002, when France introduced the euro. The North Korean reform looked similar on the face of it. Like the French in 1960, the North Korean government decided to take two zeros off the currency. One hundred old wons, the currency of North Korea, were to be worth one new won. Individuals were allowed to come forward to exchange their old currency for the newly printed currency, though this had to be done in one week, rather than forty-two years, as in the French case. Then came the catch: the government announced that no one could convert more than 100,000 won, though it later relaxed this to 500,000. One hundred thousand won was about $40 at the black market exchange rate. In one stroke, the government had wiped out a huge fraction of North Korean citizens' private wealth; we do not know exactly how much, but it is probably greater than that expropriated by the Argentine government in 2002.

The government in North Korea is a communist dictatorship opposed to private property and markets. But it is difficult to control black markets, and black markets make transactions in cash. Of course quite a bit of foreign exchange is involved, particularly Chinese currency, but many transactions use won. The currency reform was designed to punish people who used these markets and, more specifically, to make sure that they did not become too wealthy or powerful enough to threaten the regime. Keeping them poor was safer. Black markets are not the whole story. People in North Korea

also keep their savings in wons because there are few banks in Korea, and they are all owned by the government. In effect, the government used the currency reform to expropriate much of people's savings.

Though the government says it regards markets as bad, the North Korean elite rather like what markets can produce for them. The leader, Kim Jong-Il, had a seven-story pleasure palace equipped with a bar, a karaoke machine, and a mini movie theater. The ground floor had an enormous swimming pool with a wave machine, where Kim liked to use a body board fitted with a small motor. When in 2006 the United States placed sanctions on North Korea, it knew how to really hit the regime where it hurt. It made it illegal to export more than sixty luxury items to North Korea, including yachts, water scooters, racing cars, motorcycles, DVD players, and televisions larger than twenty-nine inches. There would be no more silk scarves, designer fountain pens, furs, or leather luggage. These were exactly the items collected by Kim and his Communist Party elites. One scholar used sales figures from the French company Hennessy to estimate that Kim's annual cognac budget before the sanctions could have been as high as $800,000 a year.

It is impossible to understand many of the poorest regions of the world at the end of the twentieth century without understanding the new absolutism of the twentieth century: communism. Marx's vision was a system that would generate prosperity under more humane conditions and without inequality. Lenin and his Communist Party were inspired by Marx, but the practice could not have been more different from the theory. The Bolshevik Revolution of 1917 was a bloody affair, and there was no humane aspect to it. Equality was not part of the equation, either, since the first thing Lenin and his entourage did was to create a new elite, themselves, at the head of the Bolshevik Party. In doing so, they purged and murdered not only non-communist elements, but also other communists who could have threatened their power. But the real tragedies were yet to come: first with the Civil War, and then under Stalin's collectivization and his all-too-frequent purges, which may have killed as many as forty million people. Russian communism was brutal, repressive, and bloody, but

not unique. The economic consequences and the human suffering were quite typical of what happened elsewhere—for example, in Cambodia in the 1970s under the Khmer Rouge, in China, and in North Korea. In all cases communism brought vicious dictatorships and widespread human rights abuses. Beyond the human suffering and carnage, the communist regimes all set up various types of extractive institutions. The economic institutions, with or without markets, were designed to extract resources from the people, and by entirely abhorring property rights, they often created poverty instead of prosperity. In the Soviet case, as we saw in chapter 5, the Communist system at first generated rapid growth, but then faltered and led to stagnation. The consequences were much more devastating in China under Mao, in Cambodia under the Khmer Rouge, and in North Korea, where the Communist economic institutions led to economic collapse and famine.

The Communist economic institutions were in turn supported by extractive political institutions, concentrating all power in the hands of Communist parties and introducing no constraints on the exercise of this power. Though these were different extractive institutions in form, they had similar effects on the livelihoods of the people as the extractive institutions in Zimbabwe and Sierra Leone.

KING COTTON

Cotton accounts for about 45 percent of the exports of Uzbekistan, making it the most important crop since the country established independence at the breakup of the Soviet Union in 1991. Under Soviet communism all farmland in Uzbekistan was under the control of 2,048 state-owned farms. These were broken up and the land distributed after 1991. But that didn't mean farmers could act independently. Cotton was too valuable to the new government of Uzbekistan's first, and so far only, president, Islam Karimov. Instead, regulations were introduced that determined what farmers could plant and exactly how much they could sell it for. Cotton was a valuable export, and farmers were paid a small fraction of world market prices for their crop, with

the government taking the rest. Nobody would have grown cotton at the prices paid, so the government forced them. Every farmer now has to allocate 35 percent of his land to cotton. This caused many problems, difficulties with machinery being one. At the time of independence, about 40 percent of the harvest was picked by combine harvesters. After 1991, not surprisingly, given the incentives that President Karimov's regime created for farmers, they were not willing to buy these or maintain them. Recognizing the problem, Karimov came up with a solution, in fact, a cheaper option than combine harvesters: schoolchildren.

The cotton bolls start to ripen and are ready to be picked in early September, at about the same time that children return to school. Karimov issued orders to local governors to send cotton delivery quotas to schools. In early September the schools are emptied of 2.7 million children (2006 figures). Teachers, instead of being instructors, became labor recruiters. Gulnaz, a mother of two of these children, explained what happens:

> At the beginning of each school year, approximately at the beginning of September, the classes in school are suspended, and instead of classes children are sent to the cotton harvest. Nobody asks for the consent of parents. They don't have weekend holidays [during the harvesting season]. If a child is for any reason left at home, his teacher or class curator comes over and denounces the parents. They assign a plan to each child, from 20 to 60 kg per day depending on the child's age. If a child fails to fulfil this plan then next morning he is lambasted in front of the whole class.

The harvest lasts for two months. Rural children lucky enough to be assigned to farms close to home can walk or are bused to work. Children farther away or from urban areas have to sleep in the sheds or storehouses with the machinery and animals. There are no toilets or kitchens. Children have to bring their own food for lunch.

The main beneficiaries from all this forced labor are the political elites, led by President Karimov, the de facto king of all Uzbeki cotton. The schoolchildren are supposedly paid for their labor, but only supposedly. In 2006, when the world price of cotton was around $1.40 (U.S.) per kilo, the children were paid about $0.03 for their daily quota of twenty to sixty kilos. Probably 75 percent of the cotton harvest is now picked by children. In the spring, school is closed for compulsory hoeing, weeding, and transplanting.

How did it all come to this? Uzbekistan, like the other Soviet Socialist Republics, was supposed to gain its independence after the collapse of the Soviet Union and develop a market economy and democracy. As in many other Soviet Republics, this is not what happened, however. President Karimov, who began his political career in the Communist Party of the old Soviet Union, rising to the post of first secretary for Uzbekistan at the opportune moment of 1989, just as the Berlin Wall was collapsing, managed to reinvent himself as a nationalist. With the crucial support of the security forces, in December 1991 he won Uzbekistan's first-ever presidential election. After taking power, he cracked down on the independent political opposition. Opponents are now in prison or exile. There is no free media in Uzbekistan, and no nongovernmental organizations are allowed. The apogee of the intensifying repression came in 2005, when possibly 750, maybe more, demonstrators were murdered by the police and army in Andijon.

Using this command of the security forces and total control of the media, Karimov first extended his presidential term for five years, through a referendum, and then won reelection for a new seven-year term in 2000, with 91.2 percent of the vote. His only opponent declared that he had voted for Karimov! In his 2007 reelection, widely regarded as fraudulent, he won 88 percent of the vote. Elections in Uzbekistan are similar to those that Joseph Stalin used to organize in the heyday of the Soviet Union. One in 1937 was famously covered by *New York Times* correspondent Harold Denny, who reproduced a translation from *Pravda,* the newspaper of the Communist Party, which was meant to convey the tension and excitement of Soviet elections:

> Midnight has struck. The twelfth of December, the day of the first general, equal and direct elections to the Supreme Soviet, has ended. The result of the voting is about to be announced.
>
> The commission remains alone in its room. It is quiet, and the lamps are shining solemnly. Amid the general attentive and intense expectation the chairman performs all the necessary formalities before counting of the ballots—checking up by list how many voters there were and how many have voted—and the result is 100 per cent. 100 per cent! What election in what country for what candidate has given a 100 per cent response?
>
> The main business starts now. Excitedly the chairman inspects the seals on the boxes. Then the members of the commission inspect them. The seals are intact and are cut off. The boxes are opened.
>
> It is quiet. They sit attentively and seriously, these election inspectors and executives.
>
> Now it is time to open the envelopes. Three members of the commission take scissors. The chairman rises. The tellers have their copybooks ready. The first envelope is slit. All eyes are directed to it. The chairman takes out two slips—white [for a candidate for the Soviet of the Union] and blue [for a candidate for the Soviet of Nationalities]—and reads loudly and distinctly, "Comrade Stalin."
>
> Instantly the solemnity is broken. Everybody in the room jumps up and applauds joyously and stormily for the first ballot of the first general secret election under the Stalinist Constitution—a ballot with the name of the Constitution's creator.

This mood would have captured the suspense surrounding the reelections of Karimov, who appears an apt pupil of Stalin when it

comes to repression and political control and seems to organize elections that compete with those of Stalin in their surrealism.

Under Karimov, Uzbekistan is a country with very extractive political and economic institutions. And it is poor. Probably one-third of the people live in poverty, and the average annual income is around $1,000. Not all the development indicators are bad. According to World Bank data, school enrollment is 100 percent . . . well, except possibly during the cotton picking season. Literacy is also very high, though apart from controlling all the media, the regime also bans books and censors the Internet. While most people are paid only a few cents a day to pick cotton, the Karimov family and former communist cadres who reinvented themselves after 1989 as the new economic and political elites of Uzbekistan have become fabulously wealthy.

The family economic interests are run by Karimov's daughter Gulnora, who is expected to succeed her father as president. In a country so untransparent and secretive, nobody knows exactly what the Karimov family controls or how much money they earn, but the experience of the U.S. company Interspan is indicative of what has happened in the Uzbek economy in the last two decades. Cotton is not the only agricultural crop; parts of the country are ideal for growing tea, and Interspan decided to invest. By 2005 it had taken over 30 percent of the local market, but then it ran into trouble. Gulnora decided that the tea industry looked economically promising. Soon Interspan's local personnel started to be arrested, beaten up, and tortured. It became impossible to operate, and by August 2006 the company had pulled out. Its assets were taken over by the Karimov families' rapidly expanding tea interests, at the time representing 67 percent of the market, up from 2 percent a couple of years earlier.

Uzbekistan in many ways looks like a relic from the past, a forgotten age. It is a country languishing under the absolutism of a single family and the cronies surrounding them, with an economy based on forced labor—in fact, the forced labor of children. Except that it isn't. It's part of the current mosaic of societies failing under extractive institutions, and unfortunately it has many commonalities with other former Soviet Socialist Republics, ranging from Armenia and Azerbaijan to Kyrgyzstan, Tajikistan, and Turkmenistan, and reminds us that even in the twenty-first century, extractive economic and political institutions can take an unashamed atrociously extractive form.

KEEPING THE PLAYING FIELD AT AN ANGLE

The 1990s were a period of reform in Egypt. Since the military coup that removed the monarchy in 1954, Egypt had been run as a quasi-socialist society in which the government played a central role in the economy. Many sectors of the economy were dominated by state-owned enterprises. Over the years, the rhetoric of socialism lapsed, markets opened, and the private sector developed. Yet these were not inclusive markets, but markets controlled by the state and by a handful of businessmen allied with the National Democratic Party (NDP), the political party founded by President Anwar Sadat in 1978. Businessmen became more and more involved with the party, and the party became more and more involved with them under the government of Hosni Mubarak. Mubarak, who became president in 1981 following Anwar Sadat's assassination, ruled with the NDP until being forced from power by popular protests and the military in February 2011, as we discussed in the Preface (page 1).

Major businesspeople were appointed to key government posts in areas closely related to their economic interests. Rasheed Mohamed Rasheed, former president of Unilever AMET (Africa, Middle East, and Turkey), became minister of foreign trade and industry; Mohamed Zoheir Wahid Garana, the owner and managing director of Garana Travel Company, one of the largest in Egypt, became minister of tourism; Amin Ahmed Mohamed Osman Abaza, founder of the Nile Cotton Trade Company, the largest cotton-exporting company in Egypt, became minister of agriculture.

In many sectors of the economy, businessmen persuaded the government to restrict entry through state regulation. These sectors included the media, iron and steel, the automotive industry, alcoholic beverages, and cement. Each sector was very concentrated with high entry barriers protecting the politically connected businessmen and

firms. Big businessmen close to the regime, such as Ahmed Ezz (iron and steel), the Sawiris family (multimedia, beverages, and telecommunications), and Mohamed Nosseir (beverages and telecommunications) received not only protection from the state but also government contracts and large bank loans without needing to put up collateral. Ahmed Ezz was both the chairman of Ezz Steel, the largest company in the country's steel industry, producing 70 percent of Egypt's steel, and also a high-ranking member of the NDP, the chairman of the People's Assembly Budget and Planning Committee, and a close associate of Gamal Mubarak, one of President Mubarak's sons.

The economic reforms of the 1990s promoted by international financial institutions and economists were aimed at freeing up markets and reducing the role of the state in the economy. A key pillar of such reforms everywhere was the privatization of state-owned assets. Mexican privatization (pages 38–40), instead of increasing competition, simply turned state-owned monopolies into privately owned monopolies, in the process enriching politically connected businessmen such as Carlos Slim. Exactly the same thing took place in Egypt. The businesspeople connected to the regime were able to heavily influence implementation of Egypt's privatization program so that it favored the wealthy business elite—or the "whales," as they are known locally. At the time that privatization began, the economy was dominated by thirty-two of these whales.

One was Ahmed Zayat, at the helm of the Luxor Group. In 1996 the government decided to privatize Al Ahram beverages (ABC), which was the monopoly maker of beer in Egypt. A bid came in from a consortium of the Egyptian Finance Company, led by real estate developer Farid Saad, along with the first venture capital company formed in Egypt in 1995. The consortium included Fouad Sultan, former minister of tourism, Mohamed Nosseir, and Mohamed Ragab, another elite businessman. The group was well connected, but not well connected enough. Its bid of 400 million Egyptian pounds was turned down as too low. Zayat was better connected. He didn't have the money to purchase ABC, so he came up with a scheme of Carlos Slim–type ingenuity. ABC shares were floated for the first time on the

London Stock Exchange, and the Luxor Group acquired 74.9 percent of those shares at 68.5 Egyptian pounds per share. Three months later the shares were then split in two, and the Luxor Group was able to sell all of them at 52.5 pounds each, netting a 36 percent profit, with which Zayat was able to fund the purchase of ABC for 231 million pounds the next month. At the time, ABC was making an annual profit of around 41.3 million Egyptian pounds and had cash reserves of 93 million Egyptian pounds. It was quite a bargain. In 1999 the newly privatized ABC extended its monopoly from beer into wine by buying the privatized national wine monopoly Gianaclis. Gianaclis was a very profitable company, nestling behind a 3,000 percent tariff imposed on imported wines, and it had a 70 percent profit margin on what it sold. In 2002 the monopoly changed hands again when Zayat sold ABC to Heineken for 1.3 billion Egyptian pounds. A 563 percent profit in five years.

Mohamed Nosseir hadn't always been on the losing side. In 1993 he purchased the privatized El Nasr Bottling Company, which had the monopoly rights to bottle and sell Coca-Cola in Egypt. Nosseir's relations with the then-minister of the public business sector, Atef Ebeid, allowed him to make the purchase with little competition. Nosseir then sold the company after two years for more than three times the acquisition price. Another example was the move in the late 1990s to involve the private sector in the state cinema industry. Again political connections implied that only two families were allowed to bid for and operate the cinemas—one of whom was the Sawiris family.

Egypt today is a poor nation—not as poor as most countries to the south, in sub-Saharan Africa, but still one where around 40 percent of the population is very poor and lives on less than two dollars a day. Ironically, as we saw earlier (pages 61–62), in the nineteenth century Egypt was the site of an initially successful attempt at institutional change and economic modernization under Muhammad Ali, who did generate a period of extractive economic growth before it was effectively annexed to the British Empire. From the British colonial period a set of extractive institutions emerged, and were continued by the

military after 1954. There was some economic growth and investment in education, but the majority of the population had few economic opportunities, while the new elite could benefit from their connections to the government.

These extractive economic institutions were again supported by extractive political institutions. President Mubarak planned to begin a political dynasty, grooming his son Gamal to replace him. His plan was cut short only by the collapse of his extractive regime in early 2011 in the face of widespread unrest and demonstrations during the so-called Arab Spring. During the period when Nasser was president, there were some inclusive aspects of economic institutions, and the state did open up the education system and provide some opportunities that the previous regime of King Farouk had not. But this was an example of an unstable combination of extractive political institutions with some inclusivity of economic institutions.

The inevitable outcome, which came during Mubarak's reign, was that economic institutions became more extractive, reflecting the distribution of political power in society. In some sense the Arab Spring was a reaction to this. This was true not just in Egypt but also in Tunisia. Three decades of Tunisian growth under extractive political institutions started to go into reverse as President Ben Ali and his family began to prey more and more on the economy.

WHY NATIONS FAIL

Nations fail economically because of extractive institutions. These institutions keep poor countries poor and prevent them from embarking on a path to economic growth. This is true today in Africa, in places such as Zimbabwe and Sierra Leone; in South America, in countries such as Colombia and Argentina; in Asia, in countries such as North Korea and Uzbekistan; and in the Middle East, in nations such as Egypt. There are notable differences among these countries. Some are tropical, some are in temperate latitudes. Some were colonies of Britain; others, of Japan, Spain, and Russia. They have very

different histories, languages, and cultures. What they all share is extractive institutions. In all these cases the basis of these institutions is an elite who design economic institutions in order to enrich themselves and perpetuate their power at the expense of the vast majority of people in society. The different histories and social structures of the countries lead to the differences in the nature of the elites and in the details of the extractive institutions. But the reason why these extractive institutions persist is always related to the vicious circle, and the implications of these institutions in terms of impoverishing their citizens are similar—even if their intensity differs.

In Zimbabwe, for example, the elite comprise Robert Mugabe and the core of ZANU-PF, who spearheaded the anticolonial fight in the 1970s. In North Korea, they are the clique around Kim Jong-Il and the Communist Party. In Uzbekistan it is President Islam Karimov, his family, and his reinvented Soviet Union–era cronies. These groups are obviously very different, and these differences, along with the variegated polities and economies they govern, mean that the specific form the extractive institutions take differs. For instance, because North Korea was created by a communist revolution, it takes as its political model the one-party rule of the Communist Party. Though Mugabe did invite the North Korean military into Zimbabwe in the 1980s to massacre his opponents in Matabeleland, such a model for extractive political institutions is not applicable in Zimbabwe. Instead, because of the way he came to power in the anticolonial struggle, Mugabe had to cloak his rule with elections, even if for a while he managed actually to engineer a constitutionally sanctified one-party state.

In contrast, Colombia has had a long history of elections, which emerged historically as a method for sharing power between the Liberal and Conservative parties in the wake of independence from Spain. Not only is the nature of elites different, but their numbers are. In Uzbekistan, Karimov could hijack the remnants of the Soviet state, which gave him a strong apparatus to suppress and murder alternative elites. In Colombia, the lack of authority of the central state in parts of the country has naturally led to much more fragmented

elites—in fact, so much so that they sometimes murder one another. Nevertheless, despite these variegated elites and political institutions, these institutions often manage to cement and reproduce the power of the elite that created them. But sometimes the infighting they induce leads to the collapse of the state, as in Sierra Leone.

Just as different histories and structures mean that the identity of elites and the details of extractive political institutions differ, so do the details of the extractive economic institutions that the elites set up. In North Korea, the tools of extraction were again inherited from the communist toolkit: the abolition of private property, state-run farms, and industry.

In Egypt, the situation was quite similar under the avowedly socialist military regime created by Colonel Nasser after 1952. Nasser sided with the Soviet Union in the cold war, expropriating foreign investments, such as the British-owned Suez Canal, and took into public ownership much of the economy. However, the situation in Egypt in the 1950s and '60s was very different from that in North Korea in the 1940s. It was much easier for the North Koreans to create a more radically communist-style economy, since they could expropriate former Japanese assets and build on the economic model of the Chinese Revolution.

In contrast, the Egyptian Revolution was more a coup by a group of military officers. When Egypt changed sides in the cold war and became pro-Western, it was therefore relatively easy, as well as expedient, for the Egyptian military to change from central command to crony capitalism as a method of extraction. Even so, the better economic performance of Egypt compared with North Korea was a consequence of the more limited extractive nature of Egyptian institutions. For one thing, lacking the stifling control of the North Korean Communist Party, the Egyptian regime had to placate its population in a way that the North Korean regime does not. For another, even crony capitalism generates some incentives for investment, at least among those favored by the regime, that are totally absent in North Korea.

Though these details are all important and interesting, the more

critical lessons are in the big picture, which reveals that in each of these cases, extractive political institutions have created extractive economic institutions, transferring wealth and power toward the elite.

The intensity of extraction in these different countries obviously varies and has important consequences for prosperity. In Argentina, for example, the constitution and democratic elections do not work well to promote pluralism, but they do function much better than in Colombia. At least the state can claim the monopoly of violence in Argentina. Partly as a consequence, income per capita in Argentina is double that of Colombia. The political institutions of both countries do a much better job of restraining elites than those in Zimbabwe and Sierra Leone, and as a result, Zimbabwe and Sierra Leone are much poorer than Argentina and Colombia.

The vicious circle also implies that even when extractive institutions lead to the collapse of the state, as in Sierra Leone and Zimbabwe, this doesn't put a conclusive end to the rule of these institutions. We have already seen that civil wars and revolutions, while they may occur during critical junctures, do not necessarily lead to institutional change. The events in Sierra Leone since the civil war ended in 2002 vividly illustrate this possibility.

In 2007 in a democratic election, the old party of Siaka Stevens, the APC, returned to power. Though the man who won the presidential election, Ernest Bai Koroma, had no association with the old APC governments, many of his cabinet did. Two of Stevens's sons, Bockarie and Jengo, were even made ambassadors to the United States and Germany. In a sense this is a more volatile version of what we saw happen in Colombia. There the lack of state authority in many parts of the country persists over time because it is in the interests of part of the national political elite to allow it to do so, but the core state institutions are also strong enough to prevent this disorder from turning into complete chaos. In Sierra Leone, partly because of the more extractive nature of economic institutions and partly because of the country's history of highly extractive political institutions, the society has not only suffered economically but has also tipped between com-

plete disorder and some sort of order. Still, the long-run effect is the same: the state all but remains absent, and institutions are extractive.

In all these cases there has been a long history of extractive institutions since at least the nineteenth century. Each country is trapped in a vicious circle. In Colombia and Argentina, they are rooted in the institutions of Spanish colonial rule (pages 9–19). Zimbabwe and Sierra Leone originated in British colonial regimes set up in the late nineteenth century. In Sierra Leone, in the absence of white settlers, these regimes built extensively on precolonial extractive structures of political power and intensified them. These structures themselves were the outcome of a long vicious circle that featured lack of political centralization and the disastrous effects of the slave trade. In Zimbabwe, there was much more of a construction of a new form of extractive institutions, because the British South Africa Company created a dual economy. Uzbekistan could take over the extractive institutions of the Soviet Union and, like Egypt, modify them into crony capitalism. The Soviet Union's extractive institutions themselves were in many ways a continuation of those of the tsarist regime, again in a pattern predicated on the iron law of oligarchy. As these various vicious circles played out in different parts of the world over the past 250 years, world inequality emerged, and persists.

The solution to the economic and political failure of nations today is to transform their extractive institutions toward inclusive ones. The vicious circle means that this is not easy. But it is not impossible, and the iron law of oligarchy is not inevitable. Either some preexisting inclusive elements in institutions, or the presence of broad coalitions leading the fight against the existing regime, or just the contingent nature of history, can break vicious circles. Just like the civil war in Sierra Leone, the Glorious Revolution in 1688 was a struggle for power. But it was a struggle of a very different nature than the civil war in Sierra Leone. Conceivably some in Parliament fighting to remove James II in the wake of the Glorious Revolution imagined themselves playing the role of the new absolutist, as Oliver Cromwell did after the English Civil War. But the fact that Parliament was already powerful and made up of a broad coalition consisting of different economic interests and different points of view made the iron law of

oligarchy less likely to apply in 1688. And it was helped by the fact that luck was on the side of Parliament against James II. In the next chapter, we will see other examples of countries that have managed to break the mold and transform their institutions for the better, even after a long history of extractive institutions.