

# The Political Economy of Economic Policy Advice

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## Abstract

This article examines the political economy of economic policy advice. It offers a framework for assessing how to maximise the economic development impact of advice, allowing for the political incentives of those in power. It argues for a ‘second best’ analysis that looks to maximise development impact given political incentives and shows how standard advice often given by researchers, government advisors or international organisations such as the World Bank and the IMF may not be this second best option. Furthermore, it looks at the implications of treating political constraints as endogenous. Some examples illustrate how research and advice can be more impactful by considering local political economy conditions.

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## 1. Introduction

Much economic policy advice may seem reasonable to the advisor giving it, but it does not mean that it will be followed. Instead, policies that most economists think are unreasonable are often pursued. I have encountered some blatant examples (see [Dercon, 2022](#)). In one case, the governor of a central bank of a hugely import-dependent African country, facing severe forex scarcity and a large premium in the black market exchange rate, dismissed any need to address the highly overvalued official exchange rate as part of improving the trade balance, stating ‘I would prefer if we simply closed our borders to all trade’. In another case, the most senior and powerful advisor to a president stated that there was no risk to taking loans from China, as ‘trust me, we will never have to pay [the loans] back’. All this is more closely linked to politics than economics, so spare a thought for those within such decision-making systems who try to provide sensible advice on economic matters of national importance.

In this article, I will discuss how to think about giving economic advice to policy makers—and how we can improve the impact of such advice in practice. Despite a perpetual push by funders of research that research must be policy relevant, there is surprisingly little written on how to offer economic advice to policy makers. What has been written tends to largely focus on the supply side: what is the evidence and how should it be supplied? For example, [Lucas \(1980\)](#) sums up the advisor’s role as ‘to make clear... the

questions that currently available expertise can hope to answer successfully [and] to base policy recommendations on the well-understood and empirically substantiated propositions of... economics, discouragingly modest as these may be...' This is echoed in more recent micro-development economics as well as in [Chupein and Glennerster \(2018\)](#) on how the supply of evidence when offered may inform policy making. Experimental evidence has suggested, as least for taxation in Brazil, that supplying such evidence may improve policy making ([Hjort \*et al.\*, 2021](#)).

Here, I pay more attention to the demand side, and note that it cannot be taken for granted that policy makers welcome economic advice from researchers, or at least not always or on all issues. The key is that policy makers may not necessarily be interested in economic growth or poverty reduction, but have other objectives. It means that to understand how to give economic advice for better economic or development outcomes, economists better understand the economy's politics and the economic decisions that serve the political outcomes. Some have written about this before, in other ways. Best known is [Acemoglu and Robinson \(2013\)](#) who offer a framework for how economic policy making needs to endogenously consider the political equilibrium it may produce. In this article, I more concretely focus on the implications of accounting for the politics of decision making and the political economy of implementation in the advice we give.

First, in the next section, I will sketch—including using a simple model—how standard economic advice tends to be given: one assumes governments want to maximise economic or development outcomes, and 'first best' advice is given on how to maximise these outcomes. However, governments rarely 'just' want to focus on economic or development outcomes—they have other objectives such as staying in power, at times at any cost, and reward those who help them to do so, and restrict the activities of those who may oppose them. Examples could be excessively focusing on the military, on friendly economic actors, on specific regions or ethnic or religious groups or particular target voters, even when it may be economically inefficient to do so. The simple answer to why this may take place is 'politics' but I will argue there is more behind it, and I will give a framework to think more systematically about this.

Next, in section 3, I will sketch what this means for economic advice. If the objective is not maximising economic or development outcomes, then it is not self-evident that the 'best' possible advice will be to argue for the 'first best' as earlier suggested: advice may only be partially implemented or just ignored given the government's objectives. If actual impact and implementation of the advice is valued by the advisor, the 'optimal' advice will then be different. I will describe three cases. First, the 'best' advice that maximises the objectives of the government, including their non-developmental aims—an alternative way of thinking about the 'first best'. For example, proposing policies that help business groups that are crucial to keep in power those currently in power, even if not the best for the economy. Second, 'second best' advice: provide advice to promote economic and development objectives, but take the non-development objectives of those in power as a constraint. For example, a tax policy that maximises revenue but with least possible burden on business groups closely connected to those in power, and a high burden on opposing business groups. Third, policy advice that does not take the objectives as given, but treats the government's current objectives as endogenous to the advice. For example, a tax policy that still takes the objectives of those in power into account but in a way that weakens their dependence on powerful business groups over time. In the latter case, the advice is used to encourage economic policies that may steer it away from these non-developmental objectives. In this paper I refer to these three types of economic advisors, somewhat tongue-in-cheek, as mercenaries, as politically-informed economic advisors and as politically-subversive economic advisors. This is in contrast to politically-uninformed advisors, who may give 'first-best' advice, but whose advice, at best partly implemented given the political economy constraints, may not improve economic or development outcomes, but even make them worse.

This paper is not offering a complete treatment of these issues, but just offers a framework to show that offering advice that ignores politics and the objectives of those in power is not just naive but could be sub-optimal and even may entrench bad outcomes. In the final section, I will then present, both conceptually and with some examples, how economic research and the advice we derive from it can be tailored far more effectively. I will use examples from fossil fuel subsidies and education policy to illustrate these. The implications for research conclude this paper.

## 2. First best policy advice

In economic models, the standard approach to analysing policy issues is to assume the government will maximise an objective function that suggests an interest in maximising some measure of overall welfare in a country. Often this will be overall income in society or that of some representative household. This may be just in a one period model, or, for dynamic issues, such as when considering growth, include some intertemporal version of this objective. When distributional issues are being considered, a social welfare function that attributes some value to poverty or inequality may augment this. The key point here is that economic and development outcome variables, both in aggregate and across the distribution, dominate here, even though there can be plenty of disagreement on what to include and what weight to give to constituent factors, such as poverty, inequality, health or education.

It leads to the kind of policy advice that is familiar to the economist. For example, let us assume that the objective function for a country is to maximise the welfare  $V$  of some representative household, defined in terms of income  $Y$  (with  $V_Y > 0$ ,  $V_{YY} < 0$ ) and  $Y$  is produced via some production function  $f(X)$  (with  $f_X > 0$ ,  $f_{XX} < 0$ ), where  $X$  is a vector of all kinds of inputs in terms of human, physical, institutional or other capital. The best possible policy advice bundle  $A^*$  that may shift elements of  $X$  is then chosen using:

$$\begin{aligned} \max_A V(Y) \\ \text{s.t. } Y = F(X) \end{aligned} \quad (1)$$

Let's now consider a set of possible policy measures  $A = \{a_1, a_2, \dots, a_n\}$  and one element of this set  $a_i \in A$  on which the advisor may advice, and that may impact on  $X$ , and in this way on  $Y$ . The impact of policy advice to implement  $a_i$ , if adopted, is then written as:

$$\frac{dV}{da_i} = \frac{dV}{dY} \frac{dY}{dX} \frac{dX}{da_i} \quad (2)$$

Equation (2) implies that the way society's outcomes are affected through some technical economic process only: a policy changes  $X$ , impacting  $Y$  and through it society's outcome  $V$ . The advisor would recommend the state to implement this advice until, jointly, the best possible impact of a set of actual implemented policy measures  $A^* \subseteq A$ , is found so that the impact of any additional  $a_i$  would be equal to (or smaller than) zero in equation (2).

This is the standard way of giving advice, based on assessing the implications of proposing various policy measures for specific economic and development outcomes. It is the way much discussion of 'policy implications' takes place in research, answering the question what 'should' be done to promote such outcomes. It is also usually how advice from international organisations, such as the World Bank or the IMF, is given.

This may seem reasonable, but political economics research tends to question this way of thinking about the government's objectives: economic actions impact on politics, but politics will also affect economic actions and outcomes. Political economy models in economics, in

particular, would allow for these interactions. And it will have something to say whether those in charge will take the advice derived in this way.

Drawing inspiration from seminal work such as North *et al.* (2013), plenty of recent applied political economy analysis has highlighted that those who decide the direction of the economy of a country are often not quite inspired by growth or inclusion in many developing countries (Acemoglu and Robinson, 2012; Pritchett *et al.*, 2017; Dercon, 2022). Whether this is largely linked to historical institutional factors or more time-specific political bargains is part of a thriving literature in economics and political science (North *et al.* 2013; World Bank, 2017; Khan, 2018; Kelsall *et al.*, 2022).

Building on a series of case-studies, Dercon (2022) uses this literature to suggest that to understand economic and development policy making in any country, it is important to understand the underlying ‘elite bargain’ that is dominant. The elite here is not simply any ‘traditional elites’ such as aristocrats or historically landed classes. It is not simply those who form the government, the president or the minister of finance, but those with power and influence—whether in politics, among business leaders, those in the top levels of the public administration, civil society leaders, senior journalists and even some in think tanks and universities. North *et al.* (2013) view the historical origin of the state as the emergence of a coalition, a deal, a bargain, between elite groups to control the rents from economic resources and activities to overcome violent ways of capturing these rents. States today, and at any moment in time, could still be viewed as reflecting such an ever evolving elite bargain, a political deal with an embedded economic deal on how resources are generated, accessed and distributed.<sup>1</sup>

These elite bargains no doubt have historical roots, given the persistence of institutions, but they also involve agency: the actions and behaviours of those who have power or who can influence those in power will matter. In its rawest form, those with power in some locality may evolve from what Olsen (2000) called ‘roving bandits’ to be ‘stationary bandits’, whereby a state may emerge but also is captured in order to control and distribute rents to a small cabal of people, maybe not unlike Mobutu’s Zaire in the 1980s, often referred to as a kleptocracy. This may be an extreme example. More commonly, states are instruments for patronage—whereby those in power provide rents and rewards to particular groups, often with ‘clientelist’ objectives, i.e., to reward those who have shown loyalty with jobs, contracts or other forms of support. Such behaviours are common in Africa but also widespread elsewhere, in rich and less rich countries alike.

While other conceptualisations could be made, it suggests that simply assuming that states and those who have power and influence over economic policies are not necessarily going to be taking actions that simply support economic growth or inclusion, but are driven by various objectives, including maintaining power, offering patronage to gain support and using clientelism to reward loyalty to those in power. In short, the objective function of those who control economic decision making or influence its direction is not simply to maximise representative households’ incomes or growth or to ensure inclusion of the poor. The development objective may be one of many competing objectives, but others may dominate.

Dercon (2022) argues that differences in the underlying objective function (consistent with the prevailing elite bargain) go some way to explain the differences between countries’ apparent relative success or failure in growth and development. In recent decades countries like Nigeria and the Democratic Republic of Congo appear to be characterised by elite bargains that, in their most simplified way, mostly focused on capturing and selectively redistributing the rents from them, at least until quite recently. In contrast, countries such as Bangladesh, Ghana, Ethiopia, Indonesia or China—while far from perfect in economic governance—have achieved economic growth rates well above the median for low and

<sup>1</sup> The idea of a ‘political settlement’ as in Kahn (2018) or Kelsall *et al.* (2022) has many similar features.

middle income countries during the three decades up to 2020, and managed to half the number of people living in extreme poverty in the same period.<sup>2</sup> Despite their differences in histories, political systems, and economic policies, these countries seem to have shared a serious and consistent commitment to growth and development from 1990 to 2020, with reasonable success. Dercon (2022) argues that a crucial common factor was the commitment of powerful and influential elites to broad-based growth and development; although this commitment often coexisted with clientelism or corruption, it largely outweighed other narrower objectives.<sup>3</sup>

### 3. Advice when economic policy is politics

Such analysis has important consequences for providing economic advice and its impact. It helps to explain why some advice will be ignored while other advice is quickly taken up: those in power will be most interested in or only take up advice that helps to improve their objectives. For example, if their power depends on providing sufficient rents to one particular region or ethnic group, or support from a particular set of business leaders, advice that removes distortions in markets that were favouring them will not be followed, but new regulations that hit other groups will be eagerly accepted. In fact, those keen to have uptake from their research may have to resign themselves that some policy advice from sound analysis will hardly have any impact despite being likely to be beneficial for growth and poverty reduction.

Formally, if the state's objective function is not simply  $V(Y)$  but is  $W(Y, \theta)$ , i.e., the state has additional objectives  $\theta$ , reflecting the interests of groups with power and influence in the state (with as before  $W_Y > 0$ ,  $W_{YY} < 0$ , but also  $W_\theta > 0$ ) then the bundle giving best advice  $A^{**}$  for a government is found using (3):

$$\begin{aligned} \max_A W(Y, \theta) \\ \text{s.t. } Y = F(X) \\ \theta = g(Z, Y) \end{aligned} \quad (3)$$

As written here, the government objective will be directly and indirectly (via  $\theta$ ) influenced by boosting national income  $Y$ , but how exactly will be through some process  $g(\cdot)$  in which  $Z$  interacts with economic outcomes through  $Y$ , and how  $\theta$  and  $Y$  are valued in the objective function. For example, let  $\theta$  be the probability that those in power in politics will stay there, whether through legitimate or illegitimate means. Measures to boost  $Y$  may either positively or negatively affect  $\theta$ —for example, broadening the tax base, liberalising imports for certain products or improving procurement transparency for government contracts may boost GDP but may undermine  $\theta$  if those businesses that are connected to government, for example through political financing, are currently benefiting from tax breaks, protectionism and shady access to government contracts.

Formally, we allow the effect of policy measures to work through the economy via  $Y$  but also directly through  $Z$ . For example, the announcement of a new tax regime cutting benefits for powerful industrial groups may immediately lead to their withdrawal of support, irrespective of how it works through the economy.

<sup>2</sup> Based on World Bank World Development Indicators (<https://databank.worldbank.org/source/world-development-indicators>) and data from Our World in Data (<https://ourworldindata.org/>), and with extreme poverty using the international poverty line of 1.90 US dollars per day per person in purchasing power parity prices of 2011.

<sup>3</sup> Kaffenberger (2022) makes a similar point specifically for successful educational policies to promote learning in developing countries: a serious commitment to make progress in educational outcomes is a key explanation for success.

So the impact of a particular policy measure  $a_i$  as seen by those in power is no longer determined by (2) but by:

$$\frac{dW}{da_i} = \frac{dW}{dY} \frac{dY}{dX} \frac{dX}{da_i} + \frac{dW}{d\theta} \left( \frac{d\theta}{dY} \frac{dY}{dX} \frac{dX}{da_i} + \frac{d\theta}{dZ} \frac{dZ}{da_i} \right) \quad (4)$$

When written as (4), the overall impact of policy advice, if adopted on the government's objectives, is not only via  $Y$  directly but also how it is mediated through the impact of economic and political variables on  $\theta$ . Consider then policies that increased  $Y$  so the first term of this equation, which is similar to (2), is positive. If, however, the policy measure reduced  $\theta$ , and if this effect outweighs the direct impact on  $Y$  (the first term), then surely the government will not adopt this measure, even though it boosted  $Y$ . Any policy that may boost national income but reduces the overall outcome for those in power surely will not be adopted.

It raises an important but troublesome implication about economic advice. Suppose one wants to or is expected to serve the government in power with economic advice to maximise *their* objectives. Then the best advice for the government (and the set of policies most likely to be adopted) will be finding  $A^{**}$  that solve this maximisation problem, which will be the best package that boosts  $W$ , and that package will be different from  $A^*$ , the package that boosted  $V$ , i.e., an objective function not defined in  $\theta$ . It offers a serious dilemma for the economic advisor: Will I advise on the best possible way to maximise  $W$ , even if it includes elements  $\theta$  that are questionable, such as linked to clientelism, discrimination of certain groups or allowing non-competitive behaviour by favoured firms?

The extent to which the optimal advice based on  $W(Y, \theta)$  in (3) is different from the advice given based on  $V(Y)$  will depend on how important these political objectives  $\theta$  are in this country. This issue of questionable objectives particularly becomes a problem in countries where the underlying elite bargain does not attach much weight to growth or broad-based development in its objective. Some examples include exchange rate policies or financial regulations that encourage corruption or illicit flows, procurement rules that give undue power to politicians and their cronies, or tax regimes that exclude the rich and powerful. It makes giving advice and seeking impact morally challenging, akin to being a *mercenary* for a potentially destructive cause. For some, this may be a choice, and one way to have 'impact' as a researcher or an advisor. For those working as public servants, there may be less choice and more seen as an obligation: provide the 'first best' defined by the objective function of those in power and not the 'first best' defined by an objective function with growth and development as arguments.

Fortunately, it is possible that the moral choice is not so hard. A striking feature of recent decades is that more and more countries appear to have economic policies that are broadly consistent with pursuing growth and development, even if, at times, highly imperfectly. This is consistent with objective functions in which  $W$  gives a high weight to boosting  $Y$  and/or  $\theta$  tends to respond positively to increases in  $Y$ . For example, in [Dercon \(2022\)](#), it is suggested that politicians may seek legitimacy from progress in development, even if their regimes are undemocratic in the ways usually understood (as in China after 1979 under Deng Xiaoping, Rwanda under Paul Kagame or Ethiopia under Meles Zenawi), or politicians and elite players may implicitly work together across business and civil society to support development (as in Bangladesh from the mid-1980s or thereabouts), or with political processes moving more towards seeking legitimacy from development even in elections (as in Ghana from the mid-1990s or in Indonesia since the late 1990s).<sup>4</sup> Nevertheless, it is hard to disagree that such weight on broad-based growth and development in the state's

<sup>4</sup> Even in rich Western countries this focus on political legitimacy from progress in growth and development is still a relatively recent phenomenon, possibly only clearly from the time of the New Deal in the United States in the 1930s and after the various world wars of the 20th century across Western Europe.

objective function (and the underlying elite bargain) is still absent in many African and other countries, making the plight of the economic advisor difficult.

Nevertheless, in general, it is clear that  $A^*$  (the best advice if  $V(Y)$  is the objective, i.e., promoting growth and development) will be different from  $A^{**}$ . The latter is the best advice if  $W(Y, \theta)$  is the objective function of the government, obtained by finding the set of actual implemented policy measures  $A^{**} \subseteq A$  whose impact of any additional  $a_i$  would be equal to (or smaller than) zero in equation (4).

There may nevertheless be some overlap, and it would be tempting to propose  $A^*$  in the hope that some elements will be implemented. This is a common approach: for example, the International Monetary Fund or the World Bank may use this 'first best' list of  $A^*$  as pre-conditions, conditionality or milestones for payouts. They are likely to be aware that some policies will not be implemented by the authorities as they would reduce rather than enhance  $W(Y, \theta)$ , through the effect on  $\theta$  through  $Z$  as in (4). They would still propose  $A^*$  in the hope that at least some 'reforms' would take place, as some may overlap with  $A^{**}$ . It may be tempting to suggest this is realpolitik on behalf of these institutions, even if they recognise that not all will be implemented. Researchers similarly may be tempted to offer 'policy implications' from their research to governments or whoever may want to hear it, describing a set of actions that together offer best possible response to improve economic or development outcomes, knowing full well that some may simply not be politically feasible. Examples would be a comprehensive tax policy or a public procurement reform to root out corruption.

However, an important implication for economic policy making is generally less well appreciated: promoting  $A^*$  may not be a good or harmless idea, if the objective function that drives implementation is  $W(Y, \theta)$  and not  $V(Y)$ . Implementing some but not all 'first best' reforms or policy measures is not necessarily leading to the best possible outcome for  $Y$  or  $V(Y)$ , given these political economy constraints in which the government is maximising the objective function  $W(Y, \theta)$ . For example, while a comprehensive tax reform is proposed, including indirect and direct taxation focusing on all firms and households, it may only be selectively implemented to exclude a small set of powerful and connected firms or a procurement reform that leaves out military contracts, linked to specific powerful firms. The 'capture' involved, in which policies are selectively implemented to serve those in power, may then increase  $W(Y, \theta)$  but not necessarily  $V(Y)$ . In short, advice uninformed by an understanding of the political economy given by politically-uninformed advisors may sometimes make matters worse.

This is a direct application of the theory of the second best: if there are multiple distortions, lifting some but not all distortions is not necessarily Pareto improving (Lipsey and Lancaster, 1956). For example, suppose cargo is moved either by trucks or by trains. Let the (private) trucking companies benefit from diesel subsidies, while the train cargo network is state owned, directly subsidised and run on electricity from hydro-power. In that case, privatising the train cargo company and forcing them to charge market rates without any subsidies, while trucking companies continue to benefit from fuel subsidies, is not necessarily Pareto-improving, even though one distortion has been removed. If diesel fuel subsidies are not removed, keeping some subsidies is likely to be better for creating a competitive market for moving goods: the second best when diesel subsidies cannot be removed may involve subsidies for the train network. Advising the first best  $A^*$ , knowing full well that not all measures of this set can politically be implemented is therefore not smart: it is not the second best. Another example would be taxation: suppose profit taxes are increased or their enforcement is strengthened to fight tax avoidance, but certain firms, linked to senior political or military figures, are no-go areas for the tax audit authorities, then the main result would be a serious competitive advantage for these connected firms, who then may manage to push others out of the market and get monopoly powers, reducing overall production and therefore the opposite of a Pareto-improvement. The second-best

may have been not to tax at all in certain markets, or maybe, if enforceable, use some commodity taxation (such as sales taxes) to keep a level playing field.

More generally, suppose the advisor wants to promote economic development, but knows there are political constraints to implementing certain policies. If there are political objectives that go against promoting growth and development, and these cannot quite be lifted, what would be the best possible advice such a politically-informed advisor keen on growth and development, could give? In other words, what is the second best, given that the advisor's objective function is  $V(Y)$ , but the government will only implement based on what is improving  $W(Y, \theta)$  taking into account politics and their quest to remain in power? This now becomes a Principal Agent problem: the Principal, the advisor, can choose what to advise, but the Agent, the implementing government, will only accept what improves its outcome  $W(Y, \theta)$ . As usual, to solve a principal agent problem, one ought to take the agent's problem as the constraint, and then optimise.

The government will only implement a bundle of measures that increases its objective function, and that now becomes the constraint. This constraint for the government can be written as:

$$\sum_i \frac{dW}{da_i} \cdot da_i \geq 0 \tag{5}$$

This equation (5) states that only bundles of advice (a set of  $a_i$ ) that jointly improve  $W$  will be accepted—and that involves working through the political effects on  $\theta$ . Note that the Agent's constraint, using (4), could also be written as:

$$\sum_i \frac{dW}{da_i} \cdot da_i = \sum_i \left( \frac{dW}{dY} \frac{dY}{dX} \frac{dX}{da_i} + \frac{dW}{d\theta} \left( \frac{d\theta}{dY} \frac{dY}{dX} \frac{dX}{da_i} + \frac{d\theta}{dZ} \frac{dZ}{da_i} \right) \right) \cdot da_i \geq 0 \tag{6}$$

In other words, the impact of the set of measures works not just through  $Y$  directly but also how it affects  $\theta$  directly or via  $Y$  would need to be considered. This becomes the participation, or more aptly called here, the implementation constraint.

To get to the 'second best' advice, the problem for the Principal can then be written as:

$$\begin{aligned} & \max_A V(Y) \\ & \text{s.t. } Y = F(X) \\ & \sum_i \frac{dW(Y, \theta)}{da_i} \cdot da_i \geq 0 \end{aligned} \tag{7}$$

In short, an advisor keen to provide the best possible outcomes in terms of growth and development better understands how policy measures work through policy, or the advice is not the second best. Just giving first best advice is not the best that can in practice be achieved in the country. A politically-informed advisor will provide better advice to improve economic and development outcomes than a politically-uninformed advisor.

Surely this is uncomfortable for the technocratic advisor keen to keep politics out of economic advice. The comfort of only having to look at the economic impacts through a narrow technical lens disappears, and it appears one needs to step into a world of politics and normative value judgements. However, even if the advisors gave the 'first best' advice, only focusing on maximising  $V(Y)$ , they already made a 'normative choice': they made the choice that governments ought to maximise a particular objective function, and possibly not the one they are in practice keen to maximise, risking worse outcomes for the economic development. Another way of saying this is that our advice is, in fact, political even when we hide behind a pure technical piece of advice.

By suggesting governments ought to take these actions and possibly even advocate for it, we are then well beyond simple ‘analysis’. This is different from the challenge the researcher faces in the first instance: it is perfectly reasonable to do an analysis of what the impact is of  $a_i$  on  $Y$  ignoring politics. The problem arises if this researcher wants to have impact on outcomes such as  $Y$  in practice. If improving  $Y$  (or its transformation  $V(Y)$ ) is not quite the ‘objective function’ of those in charge, then if the researcher does advocacy or writes policy briefs to argue for particular policies to boost  $Y$  using (1), we are both implicitly questioning the objective function of those with power, but also not necessarily offering the advice that can have the best achievable impact on those matters this researcher values.

The steps into the logic of the theory of the second best and the Principal-Agent problem as described above are then simply steps to make sure the advice we give is the best possible for growth and development, as the first best will not be implemented given the objectives of those in power. The normative choice to focus on income or other indicators of development to judge impact remains, but the advisors using (7) boost these as much as possible, given the political constraints.

Such an advisor is not quite a mercenary anymore—just trying to maximise  $W(Y, \theta)$ —but politically-informed: finding ways around those in power pursuing  $W(Y, \theta)$  but doing as well as possible for  $V(Y)$ . They take into account how policy measures not just impact on  $Y$  through standard economic processes (via  $X$ ), but also impact on  $\theta$  both through  $Y$  but also through  $Z$  (see (6)). The optimal set of policy advice  $A^{**}$  that solves (7) may or may not overlap with  $A^*$ , the first best from optimising (1) in the previous section.

There is something ‘subversive’ about this optimal set: one takes into account the existing elite bargain, the existing ‘political equilibrium’, but tries to work around it, including through affecting  $Z$  and thereby  $\theta$  (see (6)): power is essentially endogenous to the problem. Here, the problem was described as a static one-period model, and there would be little room to change much about existing power structures in such a time frame. However, in a dynamic model, with  $\theta$  and other factors affecting  $Z$  endogenous, one can imagine that policy actions, such as growth and development, may change the political dependence on certain connected people and firms, allowing more focus on growth and development.

The subversive adviser, keen on promoting growth and development, can then plot a sequence of actions, satisfying the implementation constraints, but in due course changing power structures. Acemoglu and Robinson (2013) develop something of this nature. In their paper, a framework is presented that, just like here, makes factors similar to  $\theta$  endogenous via the impact of economic policy measures, but also allows these factors to be intertemporally shifted towards new political equilibria, i.e., new elite bargains. In other words, economic advice could, through the economic policy measures it results in, shift political equilibria in the future, for better or for worse.<sup>5</sup> Advisors, and the researchers building the evidence base to support them, become genuinely subversive in their pursuit of growth and development.

#### 4. Discussion, implications and examples

These are more than abstract arguments. Researchers are encouraged by their funders to do quality technical analysis and derive their advice from this analysis, and not from in-depth considerations of political constraints. Often expectations on ‘impact’ are stated, but the analysis illustrated that there are good reasons why policy makers will not follow certain

<sup>5</sup> Whether those driving power today would allow this advice to be implemented is another matter, as they are unlikely to be myopic, and they may change behaviour as well. This would imply that the implementation constraints change in response. A complete strategic game-theoretic treatment is obviously well beyond our discussion here.

advice. Economists in government bodies or in international organisations are similarly encouraged to perform analysis away from political issues.

Most formal economic advice given by international agencies such as the International Monetary Fund (IMF) tends to be their understanding of the ‘first best’. The IMF Articles of Agreement for example state that ‘[t]hese principles shall respect the domestic social and political policies of members...’ (IMF, 2020, p.7), but in practice, partly due to the involvement of their Strategy, Policy and Review (SPR) department and the G7-controlled Board of the IMF, the expectations as part of their support programmes tend to be informed by their view of what is best for economy, narrowly considered, without much in-depth consideration of the local political economy.<sup>6</sup>

The World Bank is even more explicitly wary of being seen to take into account local politics in their advice. For example, Article 10 of the Articles of Agreement state that: ‘The Bank and its officers shall not interfere in the political affairs of any member; nor shall they be influenced in their decisions by the political character of the member or members concerned. Only economic considerations shall be relevant to their decisions, and these considerations shall be weighed impartially in order to achieve [economic development objectives].’ (World Bank, 2012, p.)

If one is really concerned with growth and development objectives, then the practice that follows from it is surely not constrained pareto-optimal: given political constraints, other advice than the ‘first best’ would be pareto-improving. Given the centrality of their economic development objectives, these statements surely leave some room for optimising their advice in view of the political circumstances, as in the ‘second best’ case in the previous section, and not simply give the ‘first best’. However, in view of these articles, they typically are afraid of being seen to take the politics into account.<sup>7</sup> Nevertheless, in practice, anyone involved in trying to get sensible advice and policy implemented, including in any government, the IMF or the World Bank, tends to look for ways of ‘getting things done’. The approach in the previous section suggests that to get improvements, it makes sense to build in a proper understanding of the politics of the economy and development already at the time of the analysis and the advice derived from it.

There are areas in public policy where economists and others, including from these international organisations, seem to have little objection to this form of reasoning. Vast amounts of research is commissioned and published on the position of women including by international organisations such as the World Bank, and based on this research, policy changes are being proposed to improve women’s positions in countries where those in power clearly are consciously restricting women in public life and the economy, and therefore questioning the underlying ‘objective function’ of the state. At the same time, few will question that to have impact from such research in terms of improving the position of women in countries like Qatar or Saudi Arabia, it is wise to give policy recommendations tailored to their context, as policy advice blind to this context is unlikely to be implemented or only very selectively, creating risks to embed these inequalities in opportunities even further.

When it comes to the political economy of economic challenges, there appears to be more caution. Further examples would help illustrate the challenge but also how one may go about giving second best advice that is politically-informed. Let us consider two: first, the case of fossil fuel subsidies and then, education interventions in support of learning.

Fossil fuel subsidies are not just a problem in developing countries. They definitely are distortionary, and not just affecting the fuel market, but also are going against the need to price in the externalities to the economy and society, and affecting the development of clean

<sup>6</sup> For a lament on the role of SPR, see Syed (2023).

<sup>7</sup> In my experience, when discussing ideas like this with World Bank audiences, including on the back of presentations of the main ideas in Dercon (2022), there always is someone senior in the room quickly stating that legally they cannot take politics into account.

alternatives. Given their cost and the external costs to the environment implied, standard first best policy advice tends to be to abolish fossil fuel subsidies, and try to tax them instead, to deal with the externalities. However, this is not easily implemented in any political setting: opponents can quite easily mobilise those benefiting from subsidies. Even if these subsidies are regressive, anyone, including the poor would still have benefited, and mobilisation of protest against those in power is not difficult.

It means that fuel subsidy reversals are really hard to implement and come at considerable political risk. Governments trying to do this often promise that the poorest will be compensated—in line with first best advice, through cash transfers to the poorest. Credibly implementing this policy is not easy, not least in a political environment with a state that is captured or finds it difficult to implement due to political risks. The results are vast untargeted fuel price subsidies across the world, at huge fiscal cost: fuel subsidies hit 7.1 percent of global GDP in 2022, according to IMF data (Black *et al.*, 2023).

There are ways around this. The case of fuel subsidy reform in Iran in 2010, where fuel subsidies were removed despite strong political opposition, is illuminating (see Guillaume *et al.*, 2011). Working with the Central Bank, the government put compensating cash transfers into 80 percent of the population's bank accounts, but in a way that they were locked and could not yet be used. It was then announced that these would be unlocked only when parliament agreed to the fuel subsidy reform, creating credibility that support would come in other (and economically less distortionary) ways. It undermined those opposing it: support in parliament was now overwhelming, protests on the street were minimal and the reform was successful. This was definitely not a first best policy: the fiscal cost of these compensatory payments to households and similar payments made to firms was equivalent of about 75 percent of the first year's fiscal savings from the abolition, and the scale of compensation to 80 percent of the population was definitely not to the poorest only. However, it allowed the transition to go relatively smoothly.

This example shows the importance of a good understanding of how politics works in a country. However, good economic advice in support of growth and development is not just politics—it also must involve thinking carefully about the economics involved, and about how to find the least distortionary ways to protect living standards if that is required to achieve the reform in political terms.

Other areas of development, such as service delivery in health and education, could also benefit from this type of reasoning. Let us consider the example of trying to boost learning outcomes for children. There is now plenty of research on what type of interventions, if they can be applied in educational systems, could improve learning most efficiently—for a review see Angrist *et al.* (2020). Suppose one now wants to advice on how to implement these.

Kaffenberger *et al.* (2022) argued that political commitment is required to make serious progress work. First best advice may be possible in some countries: there is good evidence from countries like Vietnam that rapid progress is possible. If it exists, then advising as in Angrist *et al.* (2020) could be done. They found that motivating parents about the benefits of education for their children, ensuring teaching occurred at the right level of attainment for each child and adapt the pedagogy to work for children and teachers offered some of the highest returns in terms of learning (first best).

Matters become more difficult if the political commitment to implement actions to boost learning is simply not there, or that for political reasons policy makers are attracted to more eye-catching educational programmes, even if they are less effective. One example is the experience with Tusome in Kenya, one of the high return programmes documented in Angrist *et al.* (2020). This was a largely donor-funded innovative programme to improve learning operating in part of the country, and evidence was emerging that it was successful in boosting learning (Piper *et al.*, 2018). However, the successful presidential candidate Uhuru Kenyatta, ignored this evidence: he had made an election pledge in 2013 to deliver a version of the 'one laptop per child' in Kenya. It meant that the latter became the political priority,

even though it was becoming well-known that in other countries ‘one laptop per child’ typically failed to deliver improvements in educational outcomes (see e.g., *Cristia et al., 2017*). Billions of Kenyan Shillings were subsequently spent (if not wasted) on this ‘one laptop per child’ scheme until it was prematurely stopped in 2019, having underdelivered. Meanwhile, government engagement with Tusome, despite its proven educational benefits, remained limited.

One way of looking at this, however, is that one could have been more successful in scaling a programme such as Tusome in Kenya, working with the government and beyond the original programme areas, if one had more carefully considered the President’s ill-fated election commitment, and looked for (second-best) ways to allow him to deliver on his promise but make sure that some of the lessons from Tusome had been captured as well. Indeed, in a way, it is not clear that without the kind of ‘easy’ political gain that ‘one laptop per child’ can offer, other learning interventions can be easily pulled off in this relatively poorly functioning education system with considerable leakage, low teacher motivation and general underachievement. Without finding ways of keeping politicians interested in education, learning interventions may be a hard sell, even given reasonably capable ministries such as in Kenya.

## 5. What does this mean for the researcher?

This discussion on education brings home a further implication: how to do research for impact. It is still a worthwhile pursuit to uncover whether and how particular interventions or policy measures may impact outcomes, as in the ‘first best’, in idealised contexts of implementation with high commitment to try to make it work. There are also plenty of organisations and parts of government that would be committed to such development success and with enough capability to get it done. There are, however, many instances where these conditions are not satisfied. Pleading with them to take research results seriously is honourable, but the political and bureaucratic reality cannot be ignored if one really wants to have an impact in the more difficult places where needs are highest and outcomes worst. In short, this article offers a glimpse on how to do research for impact, when the demand-side is deeply flawed.

This is then a plea for investment and effort in research that tries to uncover the solution to the Principal-Agent problem in the previous section: to find the best development or economic measures that recognise the objectives and therefore incentives of those with political and bureaucratic power in countries simply not committed to maximising growth, bringing down poverty and spreading development. Those designing programmes, in government ministries, donor agencies or international organisations would do well to take these problems seriously. I find it surprising that this is rarely done, not least by economists. The earlier examples give a flavour of how to begin to think about it and make it a more direct part of the research and impact agenda.

It makes advisors more than distant technocrats and forces them to recognise and understand politics, operate within it as politically-informed advisors, and possibly to be subversive by promoting those measures that shift the economic and development outcomes. It also suggests that it is wise to stay away from the mercenary actions that embed those in power further or from hiding behind politically-uninformed technocracy.

## Data availability

No new data were used in this article; anything cited is publicly available and appropriately referenced.

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