PART THREE

REINVigorating INSTITUTIONAL CAPABILITY

Parts One and Two have underscored that the state makes a vital contribution to economic development when its role matches its institutional capability. But capability is not destiny. It can and must be improved if governments are to promote further improvements in economic and social welfare. This part of the Report discusses how this can be achieved.

State capability refers to the ability of the state to undertake collective actions at least cost to society. This notion of capability encompasses the administrative or technical capacity of state officials, but it is much broader than that. It also includes the deeper, institutional mechanisms that give politicians and civil servants the flexibility, rules, and restraints to enable them to act in the collective interest.

Three interrelated sets of institutional mechanisms can help create incentives that will strengthen the state's capability. These mechanisms aim to:

- Enforce rules and restraints in society as well as within the state
- Promote competitive pressures from outside and from within the state; and
- Facilitate voice and partnerships both outside and within the state.

Over the long term, sustainable institutions have been built on formal checks and balances, anchored around core state institutions such as an independent
judiciary and the separation of powers. These are essential for ensuring that neither state officials nor anyone else in society is above the law.

But rule-based government is not enough. State capability will also be improved by institutional arrangements that foster partnerships with, and provide competitive pressures from, actors both outside and within the state. Partnerships with and participation in state activities by external stakeholders—businesses and civil society—can build credibility and consensus and supplement low state capability. Partnerships within the state can build commitment and loyalty on the part of government workers and reduce the costs of achieving shared goals.

The flip side of partnership is competitive pressure—from markets and civil society and within the state itself. Such pressure can improve incentives for performance and check the abuse of the state’s monopoly in policymaking and service delivery. Similarly, competitive or merit-based recruitment and promotion are crucial for building a capable bureaucracy.

This part of the Report starts with a look at ways to reinvigorate state institutions, by building the foundations of an effective public sector (Chapter 5) and, more broadly, by instituting formal checks and balances and controlling corruption (Chapter 6). Chapter 7 then examines how to sharpen competitive pressure, strengthen voice, and promote partnership by bringing the state closer to the people—an important means of which is decentralization, or the shifting of power and resources to lower levels of government. Finally, Chapter 8 discusses partnerships and competitive pressures that cross the boundaries of nation-states, and how countries can cooperate in providing collective goods.