ELSEVIER
www.elsevier.com/locate/worlddev

*World Development* Vol. xx, pp. xxx–xxx, 2013

0305-750X/$ - see front matter

http://dx.doi.org/10.1016/j.worlddev.2013.01.002

# Decentralization and Governance

JEAN-PAUL FAGUET *
*London School of Economics and Political Science, UK*

**Summary.** — The most important theoretical argument concerning decentralization is that it can make government more accountable and responsive to the governed. Improving governance is also a central justification of real-world reformers. But the literature has mostly focused on policy-relevant outcomes, such as education and health services, public investment, and fiscal deficits. This paper examines how decentralization affects governance, in particular how it might increase political competition, improve public accountability, reduce political instability, and impose incentive-compatible limits on government power, but also threaten fiscal sustainability. Such improvements in governance can help spur the broad historical transitions that define development.


*Key words* — local government, accountability, political competition, instability, limits on power, health

## 1. INTRODUCTION

Decentralization is one of the most important reforms of the past generation, both in terms of the number of countries affected and the potentially deep implications for the nature and quality of governance. A decade ago, estimates of the number of decentralization experiments ranged from 80% of the world's countries to effectively all of them (Manor, 1999). Since then, further reforms have been announced in several dozen countries as diverse as Bolivia, Cambodia, Ethiopia, France, Indonesia, Japan, Peru, South Africa, South Korea, Uganda, the UK, and many others. The trend encompasses all of the world's regions, and includes nations rich and poor, large and small, and with very different colonial histories. In short, decentralization is being implemented essentially everywhere.

The importance of reform goes well beyond the sheer number of experiments under way. At least in their intention, many decentralizations aim to reconstitute government—from a hierarchical, bureaucratic mechanism of top-down management to a system of nested self-governments characterized by participation and cooperation, where transparency is high and accountability to the governed acts as a binding constraint on public servants' behavior. In pursuit of this, the scope of authority and resources that many countries have devolved to their sub-national governments is impressive. According to Campbell (2001, p. 2), in Latin America "local governments began spending 10–50% of central government revenues." Campbell calls this "the quiet revolution," and argues that it has generated a new model of governance based on innovative, capable leadership, high popular participation, and a new implicit contract governing local taxation. Rodden (2006, pp. 1–2) makes a similar point: "[o]ther than transitions to democracy, decentralization and the spread of federalism are perhaps the most important trends in governance around the world over the last 50 years."

This policy enthusiasm has inspired a huge wave of research seeking to identify the effects of decentralization on a range of policy-relevant outcomes, as well as attempts to understand why countries undertake reform, and the timing of such decisions. These empirical studies of decentralization number in the hundreds of published academic works over the past 40 years; add in policy reports from international and development organizations (such as the World Bank and UNDP) and the number rises into the thousands. Most of these studies focus on decentralization's effects on public sector outputs, such as investment levels, public service provision, education and health indicators, and macroeconomic stability, to name a few of the larger threads. Good summaries of this research can be found in Rondinelli, Cheema, and Nellis (1983), Manor (1999), Treisman (2007), and Faguet (2012).

Comparatively few studies investigate decentralization's effects on the quality of governance; some exceptions include Bardhan (2002), de Mello and Barenstein (2001), and Oxhorn, Tulchin, and Selee (2004). The reasons for this are not hard to fathom: (i) the data required to empirically examine decentralization's effects on things like health investment or school enrollment are more commonly available than for governance-type issues like accountability, political competition, and participation in public decision-making; and (ii) the multilateral organizations that sponsor much decentralization research are more interested in service outputs than governance outcomes.

Nonetheless the divergence between the concerns that are most researched and the principal issues that motivate decentralization—both as a theoretical proposition and in real-world reforms—is striking. The strongest theoretical argument in favor of decentralization is that (a) it will improve the accountability and responsiveness of government by altering its structure so as to increase citizen voice and change the deep incentives that public officials face (Faguet, 2012). Other arguments in favor are that it can: (b) reduce abuses of power by transferring certain central government functions and resources to lower levels, (c) improve political stability by giving aggrieved minorities control over subnational governments with limited power over issues that affect them directly, and (d) increase political competition by creating many smaller arenas that politicians vie to control. Decentralization's effects on budgets and service provision are certainly important questions, but are not the most important, a point stressed also by Eaton, Kaiser, and Smoke (2011).

* I gratefully acknowledge financial support from the Hewlett Foundation for IPD's Decentralization Task Force. I am grateful to Elliott Green, Sarah Green, Kai Kaiser, Akbar Noman, José Antonio Ocampo, Lawrence Saez, Farah Siddique, Joseph Stiglitz, workshop participants at the Initiative for Policy Dialogue, and my LSE DV406 and DV431 students for their thoughtful suggestions. All remaining errors are my own..

Reformers around the world agree. Decentralization programs across rich and poor countries are centrally motivated by a quest to improve governance. The preamble of the Bolivian Law of Popular Participation states that its main goal is to improve citizens' quality of life by perfecting representative democracy and facilitating participation (Government of Bolivia, 1994). Sixteen years later, the Framework Law of Autonomies and Decentralization expands on these ideas by declaring as its goal "the effective participation of citizens in decision-making, the deepening of democracy, the satisfaction of collective necessities, and the integral socioeconomic development of the country" (Government of Bolivia, 2010). Likewise, devolution in Britain was aimed at "re-balancing power between citizen and government" in order to "move us away from a centralised Britain to a more democratic, decentralised, plural state" (Blair, 2001). Levels of investment and service provision are a part of this, but the ambitions of these reforms go much further. In Egypt, the Mubarak regime turned to decentralization in 2004 as a way of deepening democracy "and enhancing community partnerships." [1] Far from becoming derailed by the recent upheavals, enthusiasm for reform has increased, with influential voices calling on the transitional administration to decentralize more vigorously lest the grassroots rise up a second time and do it for them (Ben-Meir, 2011).

The Peruvian government views its decentralization as a means to improve citizen participation in government, and "a singular opportunity to confront the inequalities that have historically characterized our country, and promote equal access to opportunities . . . for all" (Government of Peru, 2011). According to the Cambodian government, decentralization is being pursued there above all to strengthen and expand democracy by driving it down to the local level. Reform, it is hoped, will strengthen democratic representation, increase popular participation, strengthen public accountability, and improve government effectiveness (Government of Cambodia, 2005; Romeo & Spyckerelle, 2003). These sentiments are closely shared by the Ugandan government (Mulumba, 2004). Likewise Mexico, which undertook decentralization in order to "improve the political involvement of the people in public decision-making," and so "strengthen democracy and spur the country's development efforts" (Muñoz, Acosta, & Moreno, 2006).

Other countries are motivated by more specific governance challenges. Colombia's decentralization was designed as an explicit response to violence. Elected local governments, it was hoped, would give citizens more voice in public affairs, and so drain the reservoir of discontent that fed its left- and right-wing insurgencies (USAID, 2009). South Africa's decentralization was an essential component of its transition from apartheid to democracy, demanded by a white National Party that could hope to hold on to power in certain jurisdictions as it lost power nationally to the African National Congress. Federalism was also demanded nationally by the majority-Zulu Inkatha Freedom Party (USAID, 2009). In Ethiopia, where social diversity is striking, decentralization was aimed at giving political representation to different ethnic groups in order to help the state meet the needs and aspirations of a heterogeneous population (IFAD, 2004). Lastly, and echoing—finally—the great mass of the empirical literature, both India and Tanzania chose decentralization primarily as a means to improve the low level and quality of their public goods (IFAD, 2004; USAID, 2009).

This collection of papers is aimed at the large gap between real reformers' motivations and what we consider to be the most powerful arguments in favor of decentralization, on the one hand, and the bulk of the empirical literature on the other. It does so by focusing squarely on the role that decentralization can play in deepening democracy and improving governance at the national and local levels. Most of our contributions are empirical, based on both qualitative and quantitative methods. Our two theoretical contributions (Weingast, Myerson) take their analyses of the role of decentralization in constructing democratic governance deeper than the literature previously has done, examining the powerful interactions between decentralization and political competition, the vexed problem of over-mighty government, and alternative vectors of political instability.

The papers in this collection come out of an unusual workshop held at Columbia University in June, 2009, sponsored by the Initiative for Policy Dialogue's Decentralization Task Force. Seeking to re-unite academics studying decentralization with the policymakers who implement it, the 2-day event brought together researchers working at the empirical and theoretical frontiers of decentralization and local government with policy practitioners who have implemented or supported reform at the highest levels of government and international organizations. The purpose of the workshop was not only to exchange ideas, but to marry policymakers' detailed knowledge and insights about real reform processes with academics' conceptual clarity and analytical rigor. The workshop was explicitly structured to facilitate this integration; this collection is the result.

The papers that follow are based on academic research presented at the workshop, revised in light of the detailed discussions they received, complemented by additional papers commissioned specifically for this issue. At its core this research is interdisciplinary political economy, with most authors trained mainly as political scientists or economists, but working in a way that reaches across that divide. The methods employed are both qualitative and quantitative, with several papers blending the two. This collection shows the analytical power of what might be called a one-country, large-N approach. This is an approach fast gaining adherents among social scientists (see e.g., Diaz-Cayeros, 2006; Faguet, 2012; Magaloni, 2006; Rao & Woolcock, 2003, chap. 8; Remmer & Wibbels, 2000; Rodden, 2006; Shami, 2010; Wietzke, 2012) in which a detailed knowledge of the institutional, historical, and economic characteristics of a country (or state or region) is combined with quantitative research on subnational units of analysis, such as municipalities or provinces. By blending deep qualitative knowledge with rigorous quantitative research methods, researchers can approach the elusive goal of explanations that have both generality and a fine-grained, nuanced understanding. They can avoid problems of cross-country comparison—variations in external shocks, political regimes, institutions, colonial legacies, cultural features, and other exogenous factors that are not well accounted for in the data—while still benefiting from the formal rigor that large-N studies provide. And they can stratify their analysis at the national, regional, and local levels, as different questions demand, and yet retain a central focus on complex explanatory factors, such as accountability, trust, and political entrepreneurialism, that are hard to treat quantitatively.

Before proceeding, it is useful to define the two terms in this paper's title. We follow Faguet and Sánchez (2008) and Manor (1999) in defining *decentralization* as the devolution by central (i.e., national) government of specific functions, with all of the administrative, political, and economic attributes that these entail, to regional and local (i.e., state/provincial and municipal) governments that are independent of the center within given geographic and functional domains. And we follow

Fukuyama (2012) in defining *governance* as "a government's ability to make and enforce rules, and to deliver services, regardless of whether that government is democratic or subject to the rule of law." [2] Notice that neither definition is specific to democracies. This is because nondemocracies also decentralize, and also experience (a different kind of) governance, and theoretically robust definitions should not exclude them.

The rest of this paper examines the overarching themes explored in the collection. Section 2 analyzes the nature of political competition in a decentralized system, how it is affected by the form of the party system, and how it affects, in turn, accountability and the quality of policy. Section 3 examines different forms of accountability in federal or decentralized systems, and their effects on corruption. Section 4 turns to how decentralized incentives can dampen or heighten political instability. Section 5 investigates how weak institutions in many developing countries impose insufficient limits on government power, with adverse implications for political accountability, fiscal sustainability, civil conflict, and the level of innovation and growth in the economy. Decentralization provides an incentive-compatible means for limiting overmighty government. Section 6 analyzes the connection between multilevel fiscal governance and macroeconomic instability. Section 7 contributes to the large literature on decentralization's effects on public sector outputs. Section 8 concludes, synthesizing our range of theoretical and empirical insights into a broad argument about decentralization's potential to contribute to the broad transformations in political, economic, and social relations that define development.

## 2. THE NATURE OF POLITICAL COMPETITION

If decentralization is to improve governance in a democracy as its proponents claim, then at least part of the chain of causality must involve political competition. Decentralization might re-center (some) competitive political discourse on local—as opposed to national—concerns, or increase levels of political entrepreneurship or heterogeneity by lowering the costs of entry, or provoke changes in the internal characteristics of political parties. Any one of these could lead to improvement or degradation in governance outcomes. And yet curiously, how decentralization affects the nature of political competition has not been at the forefront of the literature in recent decades. It is telling, for example, that neither of the two most recent reviews of the broad decentralization literature (Faguet, 2012; Treisman, 2007) treats the issue directly. [3]

This collection does. Myerson notes that one of the deep justifications for democracy is that competition should motivate politicians to offer better public services at a lower corruption-price. A well-ordered federal system can significantly increase political competition in a number of ways, providing strong incentives for higher-quality policy making and tighter reins of accountability to the governed. Myerson's underlying logic draws lessons and analogies from the economic analysis of oligopolies for political competition and democratic design. The first of these concerns alternative routes for candidates entering national politics. If there is only one route—for example, through national parties—then parliamentary leaders can collude to keep out challengers, with potentially dire effects for efficiency and accountability. Federalism can provide alternative routes into national politics though provincial and local governments, thus increasing total competition and so the quality and probity of a nation's policymaking.

Decentralization further increases competition through several distinct but related mechanisms. First, it creates new opportunities for independently elected politicians to demonstrate their abilities to govern. The possibility that successful local officials will advance to higher levels of power in a federal system increases the elasticity of political demand for politicians at each level below the top, and thus increases their competitive incentives to offer better public services. The principle of democratic advancement also increases subnational politicians' efforts to win popular support, which strengthens their party competitively in national elections. But this transmission path works in both directions. Thus national party sponsorship of local challengers can raise competition in local elections, and so improve the quality of local policy-making. Hence, Myerson argues, national parties should not be restricted from participating in local elections as they are, for example, through formal means in Pakistan and informal means in Uganda.

Likewise, the enhancement of competition implies that obstacles to new party formation be removed. In any country, the goal is to make sure there are at least two strong national parties, each of which includes many politicians with good reputations for public service, and that new parties can develop when old parties do not meet voters' expectations. Erecting barriers to new party formation can help entrenched parties to survive longer than they would in a political "free market," which is why entrenched party leaders often push for barriers. Ridding politics of such barriers, and by extension ridding the legislature of impediments to new coalition or bloc formation, can increase competition and so improve the quality of governance.

The costs of ignoring Myerson's advice are on rich display in Argentina, a country that—Ardanaz, Leiras, and Tommasi point out—suffers a far lower quality of public policy than its level of human development would predict. Why? The authors find an answer in the politics of Argentina's particular federal system. This system is characterized by strong political "baronies," some of them actually inherited, in some of Argentina's poorer, less developed provinces. The structure of legislative accountability in Argentina (discussed below) allows such provincial barons to extract fiscal rents from the federal government and in effect run "rentier subnational states" (Gervasoni, 2010, p. 303). In a neatly vicious circle, incumbents then use these rents to restrict political competition at home, weaken institutional and legal limits on their power at the national level, and ultimately undermine competitive democracy throughout Argentina.

One of the lessons of Argentina is that subnational actors have large incentives to distort a federal system to their own ends. How can decentralizing countries avoid this? In Weingast's formulation, "what are the institutions and forces that provide incentives for political officials to honor the rules of federalism? As Riker (1964) observed, federal stability is challenged by two problems: *centripetal forces* whereby the center captures the powers of the lower jurisdictions; and *fissiparous forces* whereby free-riding and common pool problems facing lower jurisdictions cause the federal system to fail." [4] To be stable, a federal system must chart a path between these opposing dangers. How does it do so?

The form of the party system, Weingast argues, is the key. Some countries have party systems that give national elites dominance, while others give priority to local elites, and still others balance the powers of the two. Where national elites dominate parties, local leaders can be forced to acquiesce to institutional changes that compromise their powers. Examples include Mexico under the Institutional Revolutionary Party (*Partido Revolucionario Institucional*, PRI) during 1929–2000, and India under the Congress Party during 1947–96. By

Please cite this article in press as: Faguet, J. -P. Decentralization and Governance, *World Development* (2013), http://dx.doi.org/10.1016/j.worlddev.2013.01.002

contrast where local elites have dominance, the party system can be used to force national elites to accept subnational abuse of common pool resources. Argentina's problem of recurrent provincial bailouts is a good example. But where a party system is balanced between national and local elites, each side will defend its prerogative, creating a healthy tension in which federalism can flourish. [5]

Two conditions are required for such a balanced, integrated party system to emerge,

Weingast argues.

> "First, politicians must have incentives to cooperate across political levels and jurisdictions in order to win elections; and second, once in office, political officials must have incentives to abide by restrictions. Such a system, for example, may have local politicians who rely on the national brand name or reputation of their party; and national politicians, unable to create their own independent national organization, who must cooperate and mobilize local political organizations in order to win national elections. Politicians across levels must therefore cooperate with one another rather than attempt to take advantage of one another. This creates a vertically integrated political system." [6]

that sustains federalism.

All of these arguments rely on competition that is mediated through political parties, by far the most studied form. But what about nonparty political competition, a persistent, low-level phenomenon that occurs mostly in developing countries? Despite being much less studied than party-political competition, strong claims are often made about its beneficial effects on participation, accountability, and stability (Carbone, 2003). Diaz-Cayeros, Magaloni, and Ruiz examine one variant of nonparty competition, the traditional collective decision-making processes known as *usos y costumbres* [7] in Oaxaca, Mexico. These represent one variant of the many traditional forms of local self-government practiced throughout Latin America, the roots of which go back to pre-Columbian times. The authors find that poor indigenous communities governed by *usos y costumbres* enjoy higher levels of civic engagement and better governance than similarly poor communities where parties compete for power. These advantages are qualitatively observable and statistically significant in 640 municipalities. Their findings throw into sharp relief the underlying questions of what "political competition" means, how contests should be bounded, and what sorts of organizations should be involved for the many theorized benefits of competition to materialize.

## 3. PUBLIC ACCOUNTABILITY AND CORRUPTION

The question of public accountability has been treated far more extensively than that of political competition in the decentralization literature. The theory of decentralization and public accountability go back to Mill (1993 [1895–61]), Montesquieu (1989 [1748]), Rousseau (1978 [1762]), and de Tocqueville (1994 [1835–40]), who debated the optimal size and conformation of political units that served the interests of their citizens. The modern treatment of this question is perhaps best represented by the widely cited Wallis and Oates (1988), who argue that decentralization can make government more responsive to local needs by "tailoring levels of consumption to the preferences of smaller, more homogeneous groups" (p. 5).

The logic behind this argument relies on a powerful comparative static that goes as follows. By devolving power and authority from higher to lower levels of government elected by local constituencies, decentralization fundamentally changes the incentives that local authorities face, and thus their behavior. Under centralization, "local" authorities are not elected by local citizens but rather *selected* by higher-level authorities. Immediate accountability for their performance is thus upward to the center, which has power over their careers, salaries, and broader professional prospects (Riker, 1964). Accountability does not run downward to the citizens who consume local public goods and services except at one or more removes, in the sense that central officials are ultimately beholden to national, and not local, electorates. "Local" officials thus face clear, strong incentives to respond to central government priorities and concerns, and weak, muffled incentives to respond to local citizens' needs. Decentralization re-orients these incentives; this is its most important effect. "Local" officials become local officials, whose tenure and career prospects are in the hands of the citizens they serve, who elect them. The effect of decentralization is to dramatically tighten the loop of accountability between those who produce public goods and services and those who consume them.

The potential for decentralization to increase accountability can be undermined if the relatively smaller scale of local government makes it more susceptible to capture by elites, such as landowners or employers. In this case, locally "big" interest groups can deploy their wealth and social influence, for example by financing a local campaign or pressing employees to vote in a particular way, to distort policy-making in their own favor. Such behavior can rapidly undermine local government's accountability to voters, as Bardhan and Mookherjee (1999, 2006), Blair (2000), Dreze and Sen (1996), and Prud'homme (1995) have argued.

The testing of such claims was among the principal concerns of empiricists a generation ago, of which Rondinelli *et al.* (1983) is one classic and much cited example of many. This generation of studies produced results that were at best mixed, with positive and ambiguous country experiences more than counterbalanced by studies finding that, for example, decentralization has been largely neutralized across most countries by elaborate mechanisms of central supervision and control (Samoff, 1990; Slater, 1989); where neutralization failed, the small electoral environments that reform created were typically distorted by powerful interests, and accountability to the majority undermined (Smith, 1985). In more recent years the theme has largely fallen from favor, a casualty perhaps of increasing quantification in the field. But it is interesting to note that the smaller number of newer, typically quantitative studies that do examine the issue have found far more positive results. Hence decentralization makes government more responsive to local needs (Alderman, 2002; Faguet & Sánchez, 2008; Manor, 1999), increases citizen satisfaction with local services (World Bank., 1995), and helps government target poverty programs better (Galasso & Ravallion, 2005).

The papers in this special issue use rich, multilayered evidence from Argentina, China, and Mexico to push the theory of accountability and corruption away from these static intuitions, toward a deeper understanding of the dynamic incentives that operate across fiscal and political relations in a federal system. By moving to a higher level of complexity, these papers are able to embed the linear "bureaucratic-vs.-electoral" incentives described above in a broader model that interacts fiscal with political imperatives, and embraces public officials at the local, regional, and central levels.

Ardanaz *et al.* analyze Argentine federalism through the lens of its particular policy-making process, in which policy is often the product of exchanges between the president and provincial governors. In these exchanges, presidents trade fiscal transfers for support from provincial actors for national policies. But such transactions seldom take place in Congress, which operates more often as a rubber-stamping body, formalizing deals that the President, provincial governors and interest groups

Please cite this article in press as: Faguet, J. -P. Decentralization and Governance, *World Development* (2013), http://dx.doi.org/10.1016/j.worlddev.2013.01.002

have already struck in informal arenas. Congressmen tend to see their provincial party leaders as their principals, especially when the leader is the governor. "In sum," the authors say, "provincial party leaders decide whether to 'send' someone to the National Congress and, controlling re-nominations, for how long (Jones, Saiegh, Spiller, & Tommasi, 2002). Therefore, political careers are structured at the provincial level and political fates decided in provincial jousts."[8]

The deeper effect of this federal dynamic is to short-circuit legislative accountability by making congressmen accountable to provincial party leaders, and not voters. This in turn allows provincial leaders to gain control over aspects of national policy (e.g., electoral law, fiscal resources) in such a way as to perpetuate themselves and extend their influence. The governors most effective at this game are those from the least developed provinces with the most distorted politics. The ultimate result is impaired public accountability—not just for certain provinces but for the whole country. This, in the authors' view, is the root of Argentina's infamous policy volatility, resulting in a lack of credibility and a failure to achieve desirable economic and social outcomes.

Contrast this with the federal system that Birney analyzes in China. In contrast to Western federations like Brazil, Canada, Germany, or the United States, whose political and party-political characteristics are central, China's is fundamentally an administrative and fiscal federalism predicated on single-party rule.[9] Here, poor public accountability is due not to the legislative balance of power, but rather to severe informational problems intimately tied up with the form and direction of accountability. This is the product of what she christens the *rule of mandates*, a system for maintaining political control of lower level officials through well-defined incentives, such as contracts that list targets distinguished by level of importance, and associated bonuses, promotions, fines, and other penalties. Mandates exist alongside the regime's own laws, but—unlike laws—are not public, cover only a limited set of issues, and call for the production of particular outcomes instead of adherence to particular processes. In terms of career incentives for local officials, mandates trump laws.

In the context of Chinese federalism, the rule of mandates makes it particularly difficult for the regime to identify and punish corrupt officials. First, collective responsibility implies that officials face institutionalized incentives to aid their colleagues by overlooking or assisting in false reporting. Second, higher officials have little access to the information that villagers have on the local implementation of laws, which would be too costly to collect systematically. Democratic decentralization solves this problem through local elections, lobbying, campaigning, a free press, and all of the associated apparatus of democracy which elicits and aggregates individuals' information on local performance at relatively low cost. Communist Party rule in China rules out a number of these mechanisms, and the rule of mandates imposes additional constraints. The public is seldom aware of the mandates local officials are given, and so has no way to evaluate their performance. And were the public to be informed, many might well object to the priorities implicit in these mandates, provoking not accountability but political instability. Birney's evidence suggests that local officials do indeed hide behind mandates to shelter their corruption.

Hence, the form that accountability takes in China strongly affects its ability to achieve one of its principal goals—limiting corruption. Diaz-Cayeros *et al.* underline this broader point. Local government by nonparty *usos y costumbres* achieves a more responsive, accountable government because of the processes that characterize *usos* itself: ongoing consultation with the citizenry, continuous monitoring, and sanctioning when citizens gather in public assemblies. The absence of these processes in partisan democracies leads to agency loss by citizens, when compared to more participatory democracies.

## 4. REDUCING POLITICAL INSTABILITY

A much smaller thread in the decentralization literature, but one that is germane to some of the world's most difficult policy problems, examines ethnic conflict and political instability. By devolving power and resources to lower levels of government, could decentralization relieve political tensions and reduce the risk of violence or secession? These sorts of questions are most relevant for heterogeneous countries with strong subnational (typically ethnic, regional, or religious) identities. When such groups form a minority of the national population but a majority in some areas, a highly centralized government can exacerbate grievances and lead to demands for violence or secession by coherent groups who feel themselves excluded from power. Decentralization, it is argued, can relieve these tensions by handing control over subnational governments and resources to local leaders throughout the country, who in some regions will be leaders of the aggrieved group(s).

Proponents (e.g., Diamond, Linz, & Lipset, 1995; Hechter, 2000; Horowitz, 1991) argue for a twofold beneficial effect. First, decentralized governments can implement policies better suited to the local needs and preferences of a heterogeneous population (e.g., education, broadcasting, *etc.* in minority languages), thus addressing the substance of minority groups' grievances. And second, by meeting the demands of those willing to settle for limited autonomy, the national government can peel away layers of political support from leaders who promote violence or secession. Where a complex set of complaints and demands meets a wall of centralization, calls for radical action are much more likely to prosper than where such demands meet a flexible, accommodative state. Put another way, monolithic central government is more likely to promote—even if inadvertently—the rise of firebrand leaders within minority groups who promote rebellion against the state. A multi-tiered decentralized system will promote the rise of a different, managerial kind of leader—one who seeks to work within the state to their, and their constituents', advantage.

Although arguments about decentralization and political instability are often treated as a separate theoretical class, they are at their core a particular application of the accountability argument developed above. In the particular context of a heterogeneous country with spatial concentrations of identity groups, decentralization can drain political tensions if it creates governments more responsive to the demands and interests of these groups. Doing so has the further, knock-on effect of changing the internal dynamics of organization and leadership within minority groups, replacing systemic preferences for charisma and mobilization around grievance with preferences for administration, organization, and delivery. This further reduces political instability and lessens the risk of conflict.

This collection builds on such ideas by first applying them to an especially unstable and dangerous country, Pakistan, and then driving the analysis further, beyond heterogeneous countries, to the more nuanced and more general problem of privilege, incentives and stability in all countries. Myerson notes cross-country empirical evidence that presidential systems are significantly more likely to suffer democratic breakdown than parliamentary systems (Boix, 2003; Przeworski, Alvarez, Cheibub, & Limongi, 2000). This is at least in part, in his view, because in order to actually govern, both systems rely on the cooperation of many political agents, who must have confidence in the leader. Parliamentary democracy aligns the incentives of these agents more closely with those of the executive. A president, by contrast, can rely on his personal mandate from the voters to try to circumvent other agents, thus weakening party discipline or converting it into personal loyalty, either of which weakens democracy. Another advantage of parliamentary systems is that they provide a way out of political crises when the leader suffers a scandal or loss of credibility. Presidential systems find it difficult to change a leader with a popular mandate before her term has finished. In a parliamentary system, the coalition can continue to exercise authority without the affected leader, or a new coalition can form far more fluidly. Thus Myerson recommends parliamentary over presidential democracy for diverse developing countries like Pakistan, at both national and subnational levels.

The need to cooperate features centrally in Weingast's treatment of political decentralization and instability too. In a democracy, elections allocate power to political teams, who can use this power to tax, regulate, and jail people, (re)define their property rights, and otherwise threaten them. Many developing countries lack the institutional features that limit government discretion and protect citizens from abuses of power. Hence when an election brings an unfriendly team into power in a developing country, influential people may resort to extra-constitutional means to defend themselves, their property and interests from real or imagined encroachments. This is one of the main vectors of political instability in immature democracies, and a key explanation of why most new democracies fail (Elkins, Ginsburg, & Melton, 2009, quoted in Weingast).

The incentive to encroach on others' rights or resources affects intergovernmental relations as well. Political officials across different levels of a federation will be tempted to encroach upon the authority and resources of others below and above them. Ardanaz *et al.* illustrate this point, and its many dire consequences, richly with the case of Argentina. What holds a healthy federal system together? Incentives says Weingast. In a stable democracy (i.e., a stable institutional equilibrium), elections provide countervailing incentives. Political officials from all levels of a federation need one another to win national, regional, and local offices. Encroachments sow discord within a party or coalition, opening political opportunities for the opposition. Thus the need to win elections imposes discipline upon parties and politicians, leading them to work together more than they might do otherwise.

Less mature democracies deal with a lack of institutions limiting state power by granting special privileges to groups sufficiently powerful to threaten stability, to keep them in the game. But doing so is inherently undemocratic in the sense that it conflicts with the substance of democracy—the participative self-government of equals, and letting citizens decide their own fate. Granting special privileges may achieve stability, but at the cost of conferring greater voice in public decisions to a favored group. It pushes democracy toward aristocracy.

Herein lies an oddity: The promotion of democracy around the world almost always focuses on national government, especially free and fair elections. But young democracies mostly lack the complementary, power-limiting institutions that protect citizens' rights, and so make transfers of power amenable to those with the most to lose. In such a context, to promote democracy is nontrivially to promote democratic fragility and instability. But how do we construct democracy-enhancing institutions in countries where democracy is fragile or missing? Decentralization, Weingast suggests, is a crucial part of the answer. By decentralizing government, reformers can square this circle by simultaneously building a culture and experience of democratic practice while limiting the power of central authorities, and hence the threat—real and perceived—to powerful elites. It also lowers the cost to entrenched elites of losing power, as parties losing national power can still hope to retain control of subnational levels, so deterring them from undermining the system. For the case of authoritarian transition, Weingast proposes beginning with democracy at the local level, and then opening up politics to the national level only gradually. Taiwan—one of the most stable new democracies—took just this path.

But is not decentralization inherently destabilizing? Myerson considers the possibility that federalism can exacerbate the risk of regional secession—a turning on its head of the argument presented above. The older literature on federalism (Maddox, 1941; Tocqueville, 1994 [1835–40]; Watts, 1966 quoted in Treisman, 2007) often claimed that decentralization in a diverse country would institutionalize social or ethnic cleavages, preventing them from fading over time, and would also provide a power and resource base for separatist leaders. Such a risk will be greater for larger, wealthier provinces that are more likely to be viable as independent countries. A straightforward remedy, Myerson suggests, is to have smaller provinces. He suggests a rule of thumb that no province should comprise more than 20% of the national population. In Pakistan, this would imply the breakup of Punjab into two or more provinces. Doing so should provide the additional benefit of increasing democratic competitiveness along the lines discussed above.

## 5. LIMITS ON POWER

The problem of limiting government power is intimately tied up with the problem of political instability, as we saw above. But Weingast takes the issue much further. All successful democracies satisfy the *limit condition*, which limits the stakes of power by restricting the scope of political authority against the interests of citizens and groups. As we saw above, this can be achieved via institutional rules with general effect (as in mature democracies), or the granting of special privileges to the powerful (common in immature democracies). One of the key ways in which these strategies are implemented is through open vs. limited access orders. *Limited access* is when society allows only certain groups or individuals to form organizations that receive specific privileges defined by law (i.e., limited liability). *Open access* is when any individual or group may form such an organization. Most developing countries are limited access societies, whereas most developed countries have open access.

Unfortunately for developing countries, the question of open vs. limited access goes far beyond descriptive attribution, affecting the rate of economic growth, the size of the informal sector, and the level of innovation and efficiency of an economy. Open, competitive markets, Weingast points out, require open access organizations, such as that provided by general incorporation regimes. By contrast closed access, such as provided by special incorporation (which requires a legislative act), is more closely associated with the use of political discretion to create and distribute rents to favored groups. Economies characterized by closed access typically suffer high rates of informality (around 50% in Latin America and 75% in

Africa), low rates of investment and innovation, and artificially low rates of productivity and growth given their wage rates and resource endowments. In this way the nature of the political system directly affects the structure and productive potential of the economy.

But the importance of open access is not limited to the economy. Because it allows opponents of the regime to organize and compete for power, open access to political organizations is a critical component of political competition. And much research has shown that responsive, accountable government relies on a society densely populated by independent civic organizations (Faguet, 2009, 2012; Putnam, 1993; Widner, 2001). Hence open access to civic organizations is also important to a healthy democracy. Indeed, most weak democracies and authoritarian regimes restrict access to both political and economic organization, and many of the latter to civic organization as well, because such organizations can weaken their hold on power by disrupting the clientelistic relationships on which they are based.

By providing incentive-compatible limits on the powers of different levels of government, decentralization can support democratic stability. But to thrive—and especially to produce accountable local governments—decentralization requires open access political, economic, and civic organizations that support open, competitive politics, and give officials strong incentives to respond to local citizens' needs. To ensure their independence and so allow the benefits of federalism that theory predicts to flow through, Myerson adds, subnational governments' budgets and authority should be defined and protected in the constitution.

## 6. MULTILEVEL FISCAL GOVERNANCE

The connection between decentralization and fiscal sustainability is well researched in the literature. Theoretical findings are mostly pessimistic, and centrally concerned with the problem of fiscal incentives and behaviors—that is, governance—in a multi-level federal environment (Rodden, 2006; Rodden, Eskeland, & Litvack, 2003). Decentralized countries face the intrinsic problem of soft budget constraints because local politicians have strong incentives to overspend and reap the benefits themselves, while nationalizing the cost of their behavior through central bailouts. Such behavior is underpinned by the knowledge that at least some of the blame for a local government default, with attendant reductions in public services, investment, and employment, would attach to central government politicians for two reasons: (a) many such services are jointly financed and voters may not clearly distinguish among responsible parties, and (b) the center could have averted default by bailing out the insolvent municipality. Meanwhile, central government faces a commitment problem: any promise not to bail out in future is not credible precisely because voters will punish it. All local governments know this, and hence all have incentives to overspend today in the hope of being bailed out (Prud'homme, 1995; Rodden, 2006; Rodden *et al.*, 2003; Tanzi, 1995). In the aggregate, such behavior can lead to large national deficits, and hence macroeconomic instability.

This collection analyzes the political economy dynamic in a federal system that drives macroeconomic instability. Ardanaz *et al.* analyze how the Argentine policy-making process described above, which makes legislators accountable not to voters but to their provincial governors, plays out in the fiscal realm. Provincial governments undertake a large share of total spending in Argentina, yet they collect on average only one-third of this amount themselves. In a large number of less populous provinces, the transfers received from the federal government constitute over 80% of provincial revenue. "In this logic," the authors explain, "most provincial governments are resource hungry political units eager to extract fiscal favors from the national government. In turn, the federal government needs votes in Congress to implement nationwide economic policies. This situation creates potential gains from trade between presidents and governors, while Congress merely serves as the 'ratifier' of agreements that are struck in other more informal arenas (Saiegh, 2004)."

Argentina thus presents an extreme fiscal example of the broader common-pool problem that has been analyzed extensively in the institutional literature (e.g., Ostrom, 1990). Argentine governors exploit influence in the national arena both fiscally and politically. National governments, effectively dependent on their cooperation to achieve the congressional majorities required to govern, are held to ransom. Provincial leaders extract resources with which they further develop their local dominance, and also construct national-level political careers. It is not accidental that some of the most successful national politicians of the last 20 years, including presidents Menem, Rodriguez Saa, and Nestor Kirchner, hail from the three lowest-ranking provinces (La Rioja, San Luis, and Santa Cruz) in the index of subnational democracy compiled by Gervasoni (2010).

The culture of fiscal ransoms has costs both political and economic. On the political side, it weakens one of the most important institutional mechanisms of democratic accountability—horizontal accountability (O'Donnell, 1998). And on the economic side, repeated provincial bailouts lead to chronic and increasing central deficits that cannot be sustained indefinitely, as modern Argentine economic history richly illustrates. Although popular attention at the time focused more on the currency peg, the Argentine economic disaster of 2001 was very largely a fiscal disaster rooted in uncontrolled profligacy in the provinces. It was profoundly destabilizing to politics as well, destroying the de la Rua government and altering the competitive balance among parties in ways that persist to this day. This is not in itself surprising, as macroeconomic crises have been observed to bring down governments and threatened democratic stability across dozens of countries in the past. Dillinger and Webb (1999), Wildasin (1998), de Mello (2000), and Montero and Samuels (2004) confirm an empirical link between decentralization and macroeconomic instability for different samples of developing and developed countries.

## 7. PUBLIC SECTOR OUTPUTS AND OUTCOMES

The theoretical literature argues that decentralization should improve public sector outputs by improving the accountability and responsiveness of government (Wallis & Oates, 1988). Greater local participation and transparency in the production of public services should result in services that are better suited to the real needs of local people, and also of higher quality or lower cost. Against this, others (Prud'homme, 1995; Treisman, 2007) argue that decentralization will worsen public service provision by decreasing productive efficiency and decreasing the quality of policy-making. They argue that central government benefits from greater economies of scale in public goods production and a higher quality of human capital. Decentralization entails a loss in both respects, leading to more expensive and/or lower quality public goods.

The existence of plausible, contradictory arguments implies that theory is ambiguous, opening the door for empirical work to resolve the matter. And empiricists have indeed taken up questions of public service provision (e.g., education, health) and sectoral outcomes (e.g., literacy and disease rates) with relish. Whereas the studies of three and four decades ago typically relied on qualitative evidence and country-level case study, a more recent literature has emerged in which the unit of analysis is the municipality or province, and a deep knowledge of the institutions, history, and culture of a country are combined with large-N econometric methods. This collection adds to the latter with deep studies of decentralization in Brazil, Colombia, and Oaxaca, Mexico.

Gonçalvez addresses the question of accountability and service provision directly in her study of Participatory Budgeting (PB) in Brazil. PB is an alternative budgeting process that solicits citizen inputs on municipal budgets and investment priorities. Pioneered in Porto Alegre, it has been implemented broadly in Brazil; about 30% of the country's 200 million people live in municipalities that use PB. It operates via two distinct channels: (i) it improves information flows between citizens and policy makers, raising the chances that goods and services more closely match public needs; and (ii) it stimulated more frequent and informed oversight of politicians' (very public) promises by citizens, the press, and watchdog groups, so strengthening politicians' accountability to voters.

Gonçalvez exploits an original panel dataset covering all Brazilian municipalities during 1990–2004, with rich variation in the time and duration of adoption, both within and across municipalities across time (i.e., some municipalities adopted PB early, others late, some later dropped out, and many never adopted). She finds that municipalities adopting PB increased spending on health and sanitation significantly more than those that did not—by between 20% and 30% of the sample mean. This is in line with preferences consistently expressed in PB meetings. Interestingly, these preference-driven increases took place in budget-neutral environments, and are not the result of larger overall budgets or greater per capita municipal expenditures.

More impressive still is PB's effect on real outcomes. Gonçalvez finds that municipalities adopting PB registered a significant drop in infant mortality of one and two infants per 100,000, between 5% and 10% of the total infant mortality rate at the beginning of the period. This is particularly striking given that changes in indicators like infant mortality are driven by economic, demographic, and scientific factors well beyond budget allocations, and hence we would not necessarily expect to find any detectable effect of PB. The evidence implies that PB reduces the informational asymmetries between policy makers and citizens, and encourages more intensive oversight of the formers' activities by the latter. This serves to improve government accountability and responsiveness along some of the very channels that the theory of decentralization predicts.

Granados and Sánchez report on an interesting natural experiment in Colombia in which some municipalities spun off water and sewerage services to private sector firms and others retained them in the hands of local government. With a large database including over 95% of the 1200 Colombian municipalities, they estimate a difference-in-differences model that allows them to control for municipal characteristics in order to estimate the effects of reform in water and sewerage services on child mortality. Their results show that municipalities that privatized service provision suffered a significant rise in child mortality compared to municipalities that maintained services in the hands of local government.

These findings are interesting not only because of the evidence they provide regarding decentralization per se, but because they provide strong evidence about the relative efficacy of different forms of decentralization. The standard view is that the market represents a decentralized form of provision. This view goes back to Adam Smith's (1991 [1776]) *Wealth of Nations* and 18th century debates about the appropriate role of the state in a market economy. It also became a central theme in the important 1930s debate concerning efficiency in the allocation of resources in socialist vs. market economies. In this debate, Hayek (1958 [1948]) and others pointed out that the information required for resources to be efficiently allocated is dispersed among agents throughout the economy. A market economy solves the information problem by decentralizing decision making authority to individual agents, who act in accordance with their self-interest and are coordinated by market prices. Socialist economies, by contrast, invest decision-making authority in a central planner, who acts on the basis of information communicated by individual agents.

Centralized socialist and decentralized market resource allocation systems were compared on the basis of the communication and information processing demands each entailed, and the individual incentives and behaviors that each gave rise to. Proponents of the market claimed superior efficiency on the basis of a much lower requirement for active, accurate communication in a context suffused with market signals, and the fact that information processing is distributed across agents throughout the economy, whose selfish incentives guide them toward accurate calculation. Proponents of the socialist economy countered that central planning was a natural way to avoid deep problems of distributional equity, externalities, increasing returns, and public goods that naturally bedevil decentralized systems. Hurwicz (1972, 1973, 1977) provides an excellent overview of this earlier literature and its subsequent development. Mookherjee (2006) reviews more recent theoretical contributions, focusing on mechanism design theory.

But on the empirical side, no study to our knowledge has compared decentralized market provision of public services to decentralized public provision. Empirical studies of state vs. market are often motivated by privatization reforms, and thus collapse by default into many vs. mono comparisons in which the market equilibria of competitive firms are shown to be more efficient or innovative than a public monopoly. This may reflect the real experience of many countries, and thus response to specific policy debates there. But it does not compare like with like, and at a theoretical level might reasonably be viewed as stacking the deck.

Our Colombia paper breaks with that pattern in an unusual way: it compares decentralized market provision *with decentralized public provision*. Granados and Sánchez' results contradict the view that private sector incentives naturally lead to better-quality public service provision. In municipalities of similar size, within a common legal and institutional context, decentralized public water and sewerage provision performed better than decentralized private provision. Much more research is needed to uncover why this may have been the case (Poor local regulation? Less experienced private providers? There are many more possibilities). But for now the evidence implies that local public officials proved more accountable than private businessmen to water and sanitation users.

Diaz-Cayeros, Magaloni, and Ruiz continue in this vein, examining the effects of a particular kind of decentralization—via traditional *usos y costumbres* self-government described above—on public goods provision in Oaxaca, Mexico. In order to solve the problem of selection bias in a nonexperimental setting, they calculate average treatment effects on the treated via a multi-method approach that, first, estimates the effects of indigenous autonomy through propensity score matching, and, second, uses difference-in-differences to control for fixed unobservables. They find that municipalities governed by traditional collective choice methods enjoyed improvements in electricity provision, larger reductions in extreme poverty, and no differences in political entrenchment by local political bosses compared to similar municipalities in the control group.

These results contradict claims that indigenous autonomy disguises authoritarian enclaves and entrenches local *caciques*. To the contrary, communities governed by *usos* registered higher civic engagement, better governance indicators, and better access to local public goods than similarly poor communities run by political parties. In this context *usos* in Mexico is similar to PB in Brazil, the one based on traditional and the other on modern social forms. Both can interact positively with decentralization, by increasing informational and participative intensity, to improve first accountability and responsiveness, then public service outputs, and finally real outcomes of interest like poverty and infant mortality. This last step is exceedingly rare in the decentralization literature.

## 8. CONCLUSION: DECENTRALIZATION, AND DEVELOPMENT TRANSITIONS

Much of the decentralization literature examines what could be characterized as fairly simple linear relationships between decentralization and policy-relevant outcomes such as education and health services, public investments, the level of corruption, and national and subnational fiscal deficits. Decades of research has shown that decentralization both improves and worsens all of these outcomes, in different countries at different times, leaving us unable to draw broader conclusions. Most theoretical and empirical analyses are exercises in comparative statics: pre- and post-reform equilibria are compared to see whether the policy-relevant variable of interest X (e.g., school enrollments, medical interventions, investment in water and sanitation) rises or falls. Relatively few studies attempt to tease out the underlying dynamic relationships that must be at work for any comparative static to hold.

This is especially ironic because the "underlying relationships" in question comprise governance, better governance is the single biggest theoretical justification for decentralization, and in practice it is the major political justification driving real reforms around the world. And yet the effects of decentralization on governance have been largely ignored in favor of other, more concrete outcomes that are more easily measured. Although such issues are also important, and many of these individual studies are excellent, in the aggregate they have left important gaps in our knowledge that this collection begins to fill.

The first two gaps concern decentralization's effects on accountability and the nature of political competition in a democracy. Theory argues that decentralization can re-orient politicians' incentives downward toward local voters, and increase the level of political competition in a country, resulting in higher-quality policy and tighter reins of accountability on government officials. Decentralization increases competition by providing alternative routes of entry for new politicians, and by providing local officials with incentives to compete harder in elections on their own and their party's behalf, and then perform better once in government, in the hope of ascending to higher levels of government.

But the form of federalism matters. In a democracy, the incentives described can be perverted to very different ends. The experience of Argentina shows that subnational actors have large incentives to distort a federal system in order to extract resources and reduce political competition at the local and national levels. This subverts the accountability of both subnational and national politicians, contributing to policy volatility, a lack of credibility, and the kinds of poor economic and social outcomes that Argentina has suffered in recent decades. The form of federalism matters for nondemocracies as well. In China, central-local relations are largely defined by the rule of mandates, which severely limits central authorities' information, and hence accountability, allowing corruption to flourish. The opposite is the case in certain parts of Oaxaca, where traditional community self-government achieves a more responsive, accountable government than party-political rule. Where democracies are concerned, a political party system that balances the power of local and national elites, forcing them to cooperate in order to win elections at both levels, can help avoid these risks.

Decentralization can also reduce political instability. In institutionally underdeveloped democracies, elites who fear the unchecked power of unfriendly governments may resort to violence to protect themselves and their interests. Many such countries protect against this risk by granting special privileges to elites in order to keep them in the democratic game. But this undermines the substance of democracy. Decentralization can help by providing an incentive-compatible way to limit government powers by dividing them up among different hierarchical levels, each with a democratic mandate, that must cooperate in positive-sum games to maximize their outputs.

Such considerations underscore a deeper point about decentralization reform: it is not exogenous to the issue of who has power and what they want. Indeed, the question of multilevel governance—the form of federalism—is itself an endogenous outcome of struggles among the powerful for advantage. This explains a great deal of the variation we observe across countries in the scale of "local" vs. "regional" government, the authority and discretion devolved to them, and the resources they control. [10] That in turn has important impacts on the governance and service outcomes we observe.

This collection adds to the literature on public sector outputs and outcomes as well. In Brazil, participative local budgeting not only improved the matching between public investment and citizens' wishes, but also decreased infant mortality rates in those municipalities that adopted it. Results from Colombia imply that it is not just the fact of decentralization, but how decentralization is carried out that matters. Municipalities that privatized water and sewerage services saw increases in child mortality compared to those that maintained these services in municipal hands. And in Mexico, the traditional community institutions of *usos y costumbres* improved electricity provision and reduced extreme poverty compared to neighboring municipalities run by conventional partisan administrations. It is notable that these results flow through the mechanism of higher civic engagement and better governance.

Lastly, let us place the insights of this collection in a broader context. Not only can reform spur improvements in public services such as health and electricity, and real outcomes such as infant mortality and poverty—impressive and important as such findings are. They can also contribute to the institutional changes that accompany broad historical transitions to increasing wealth and freedom. The study of such transitions has seen a remarkable resurgence in recent years. Regardless of whether development transitions are conceived of as leading to open-access societies and economies (North, Wallis, &

Please cite this article in press as: Faguet, J. -P. Decentralization and Governance, *World Development* (2013), http://dx.doi.org/10.1016/j.worlddev.2013.01.002

Weingast, 2009), or inclusive institutions (Acemoglu & Robinson, 2012), theorists agree that they consist of a complex of interdependent changes across government, the economy, and social relations (Brett, 2009; Boone & Faguet, 1998).

Many of these changes, such as technical upgrading in the productive sector, are not susceptible to decentralization. For others, such as infrastructure expansion and human capital formation, decentralization can be a useful contributory measure. But for some of the most important transformations involving governance and the exercise of power, such as increasing political competition, improving public accountability, decreasing corruption, enhancing political stability, limiting government power, and promoting economic stability, decentralization is centrally implicated. As we have seen, it can be a key factor driving improvements in all of these areas, or a key element fomenting instability, opacity, capture, and decline.

Recognizing this forces us to shift our attention away from the "decentralization success factors" stressed by so many studies, a focus that typically blames failure on absent factors such as a lack of political will, low bureaucratic capacity, and insufficient resources. We are led instead to focus on the hierarchical institutions and the structure of incentives in which decentralization operates. In this context, the first-order answer to the question "Is decentralization good for development?" is not that it will improve children's health, which in the long term will boost a country's prospects, although such a connection is certainly valid and important.

Rather our first answer will take the form: If reform divides public resources and authority among many independent units in a transparent way, decentralization will provide an incentive-compatible means of limiting the power of government to threaten powerful elites. If these independent units must cooperate to achieve positive-sum outcomes, and this structure of incentives is replicated within political parties and the public administration, then decentralization will generate competitive incentives compatible with deepening democracy and strengthening the rule of law. Subnational officials will tend to compete within the rules of the game to further their careers by improving local services. And the currency of such competition will often be cooperation with other independent government units—either central or peripheral—as a means to capture more resources, and as an independent form of validation.

Such a system not only increases political stability, but also promotes open access economic, political, and social organizations. Open-access organizations in turn support competitive political systems and a vibrant civil society, both important to accountable government, as well as promoting innovation and growth in the economy. But if transparency is absent and some units can blackmail others, decentralization can instead undermine both political accountability and economic stability.

What is the difference between decentralizations that promote development transitions and those that undermine them? We can only speculate for now—much more empirical research is needed on decentralization and governance before general conclusions can be ventured with any confidence. But the research in this special issue suggests that the electoral incentives embedded in a competitive democracy are responsible. In authoritarian regimes, for example, decentralization may decrease the chances of closed-to-open-access transitions by providing the center with incentives to undermine transparency and local accountability, as occurs in China. In uncompetitive or distorted democracies, such as Argentina, a broadly similar result may obtain through an upward, instead of downward, channel, as political "barons" reach up from the regions they have captured to twist national politics away from the national interest.

In a competitive democracy, by contrast, we can understand the argument that decentralization re-orients accountability incentives downward to voters as an *opening-access* argument—because more public officials become beholden to more citizens, effectively incorporating more people and more information into a society's governance. Thus the key element that allows decentralization to spur closed-to-open-access transitions is open, competitive democracy. Subjecting public office to elections is what changes the incentives politicians throughout a system face when that system is decentralized. Electionless decentralization does not have the same effect.

So decentralization requires democracy in order to achieve its potential. But paradoxically, democracy may require a measure of decentralization—which divides power and lessens the ability of the state to threaten elites—in order to emerge out of autocracy. Which should come first? Where should reformers focus their efforts? We are left with a classic chicken-and-egg conundrum from which theory provides no escape, and hence an area ripe for further empirical research. In this context, the concrete results of reform that our colleagues identify in Brazil, Mexico, and Colombia provide the beginnings of an answer. The gains documented in each are not the technocratic products of bureaucratic adjustments, but rather leading indicators of deepening democracy, improving governance, and expanding freedom.

## NOTES

1. Prime Minister Ahmad Nazeef, Statement of the Cabinet to the People's Assembly, 19 December 2004.

2. P.1. The 2012 online Oxford English Dictionary defines governance as "The action or manner of governing," and "The manner in which something is governed or regulated."

3. Although related issues, such as accountability, are treated in detail.

4. P.2, my emphasis.

5. This is a rich, well-developed field. To explore further, Sartori (1976) is the classic treatise on parties and party systems. Lijphart (1999) connects party systems to electoral rules, parliamentary regimes, and broader government performance.

6. P.6.

7. According to the authors, *usos y costumbres* "entails electing individuals to leadership positions through customary law in non-partisan elections, making decisions through participatory democracy, and monitoring compliance through a parallel (and often informal) system of law enforcement and community justice" (p. 10).

8. P.9.

9. Gupta, Stern, and Hussain (1995) and Montinola, Qian, and Weingast (1996) discuss China's federal characteristics and their various effects.

10. Eaton *et al.* (2011) make a similar point.

Please cite this article in press as: Faguet, J. -P. Decentralization and Governance, *World Development* (2013), http://dx.doi.org/10.1016/j.worlddev.2013.01.002

## REFERENCES


Acemoglu, D., & Robinson, J. (2012). *Why nations fail: The origins of power, prosperity and poverty*. New York: Crown.

Alderman, H. (2002). Do local officials know something we don't? Decentralization of targeted transfers in Albania. *Journal of Public Economics, 83*, 375–404.

Bardhan, P. (2002). Decentralization of governance and development. *Journal of Economic Perspectives, 16*, 185–205.

Bardhan, P., & Mookherjee, D. (1999). Relative capture of local and central governments: An essay in the political economy of decentralization. Unpublished paper, University of California, Berkeley.

Bardhan, P., & Mookherjee, D. (Eds.) (2006). *Decentralization and local governance in developing countries: A comparative perspective*. Cambridge, MA: MIT Press.

Ben-Meir, Y. (2011). *Egypt's second grassroots resurgence*. TheDailyNewsEgypt.com. http://www.thedailynewsegypt.com/egypts-second-grassroots-resurgence.html Accessed 22.06.11.

Blair, A. (2001). Speech to the Welsh assembly. http://www.totalpolitics.com/speeches/devolved-politics/devolution/33433/tony-blairs-speech-to-the-welsh-assembly.thtml Accessed 22.06.11.

Blair, H. (2000). Participation and accountability at the periphery: Democratic local governance in six countries. *World Development, 28*(1), 21–39.

Boix, C. (2003). *Democracy and redistribution*. New York: Cambridge University Press.

Boone, P., & Faguet, J. P. (1998). Multilateral aid, politics and poverty: Past failures and future challenges. In R. Grant, & J. Nijman (Eds.), *The global crisis in foreign aid*. Syracuse: Syracuse University Press.

Brett, E. A. (2009). *Reconstructing development theory*. Basingstoke: Palgrave Macmillan.

Campbell, T. (2001). *The quiet revolution: The rise of political participation and leading cities with decentralization in Latin America and the Caribbean*. Pittsburgh: University of Pittsburgh Press.

Carbone, G. M. (2003). Political parties in a 'no-party democracy': Hegemony and opposition under 'movement democracy' in Uganda. *Party Politics, 9*(4), 485–501.

de Mello, L. (2000). Can fiscal decentralization strengthen social capital? International Monetary Fund Working Paper WP/00/129, Washington, DC.

de Mello, L., & Barenstein, M. (2001). Fiscal decentralization and governance: A cross-country analysis. International Monetary Fund Working Paper 01/71, Washington, DC.

de Tocqueville, A. (1994 [1835–40]) *Democracy in America*. London: Everyman's Library, trans. H. Reeve.

Diamond, L., Linz, J. J., & Lipset, S. M. (1995). *Politics in developing countries: Comparing experiences with democracy*. Boulder, CO: Lynne Reinner.

Diaz-Cayeros, A. (2006). *Federalism, fiscal authority and centralization in Latin America*. Cambridge: Cambridge University Press.

Dillinger, W., & Webb, S. B. (1999). Decentralization and fiscal management in Colombia. World Bank Policy Research Working Paper 2122, Washington, DC.

Dreze, J., & Sen, A. (1996). *India: Economic development and social opportunity*. Delhi: Oxford University Press.

Eaton, K., Kaiser, K., & Smoke, P. J. (2011). *The political economy of decentralization reforms: Implications for aid effectiveness*. Washington, DC: The World Bank.

Elkins, Z., Ginsburg, T., & Melton, J. (2009). *The endurance of national constitutions*. Cambridge: Cambridge University Press.

Faguet, J. P. (2012). *Decentralization and popular democracy: Governance from below in Bolivia*. Ann Arbor: University of Michigan Press.

Faguet, J. P. (2009). Governance from below in Bolivia: A theory of local government with two empirical tests. *Latin American Politics & Society, 29*(4), 29–68.

Faguet, J. P., & Sánchez, F. (2008). Decentralization's effects on educational outcomes in Bolivia and Colombia. *World Development, 36*, 1294–1316.

Fukuyama, F. (2012). What is governance? Unpublished Discussion Paper, Stanford University.

Galasso, E., & Ravallion, M. (2005). Decentralized targeting of an antipoverty program. *Journal of Public Economics, 89*, 705–727.

Gervasoni, C. (2010). A rentier theory of subnational regimes: Fiscal federalism, democracy, and authoritarianism in the Argentine Provinces. *World Politics, 62*(2), 302–340.

Government of Bolivia (2010). *Framework law of autonomies and decentralization*. La Paz: Government of Bolivia.

Government of Bolivia (1994). *Law of popular participation*. La Paz: Government of Bolivia.

Government of Cambodia (2005). *Strategic framework for decentralization and de-concentration reforms*. Phnom Penh: Government of Cambodia.

Government of Peru. (2011). Programa de Descentralización y Buen Gobierno. Defensoría del Pueblo del Perú. http://www.defensoria.gob.pe/programa-gob.php Accessed 23.05.11.

Gupta, S. P., Stern, N. H., & Hussain, A. (1995). *Development patterns and institutional structures: China and India*. New Delhi: Allied Publishers.

Hayek, F. A. (1958). *Individualism and economic order* . Chicago: University of Chicago Press.

Hechter, M. (2000). *Containing nationalism*. New York: Oxford University Press.

Horowitz, D. L. (1991). *A democratic South Africa? Constitutional engineering in a divided society*. Berkeley: University of California Press.

Hurwicz, L. (1972). On informationally decentralized systems. In R. Radner, & C. McGuire (Eds.), *Decision and organization* (pp. 297–336). Amsterdam: North Holland.

Hurwicz, L. (1973). The design of mechanisms for resource allocation. *American Economic Review, 63*, 1–30.

Hurwicz, L. (1977). On the dimensional requirements of informationally decentralized pareto-satisfactory processes. In K. Arrow, & L. Hurwicz (Eds.), *Studies in resource allocation processes*. Cambridge: Cambridge University Press.

IFAD (International Fund for Agricultural Development) (2004). *IFAD's performance and impact in decentralizing environments: Experiences from Ethiopia, Tanzania and Uganda*. Rome: IFAD.

Jones, M., Saiegh, S., Spiller, P., & Tommasi, M. (2002). Amateur legislators—professional politicians: The consequences of party-centered electoral rules in a federal system. *American Journal of Political Science, 46*(3), 656–669.

Lijphart, A. (1999). *Patterns of democracy: Government forms and performance in thirty-six countries*. New Haven: Yale University Press.

Maddox, W. P. (1941). The political basis of federation. *American Political Science Review, 35*(6), 1120–1127.

Magaloni, B. (2006). *Voting for autocracy: Hegemonic party survival and its demise in Mexico*. New York: Cambridge University Press.

Manor, J. (1999). *The political economy of democratic decentralization*. Washington, DC: The World Bank.

Mill, J. S. (1993 [1895-61]). Utilitarianism; on liberty; considerations on representative government; remarks on Bentham's Philosophy. In G. Williams (Ed.). London: Everyman.

Montero, A. P., & Samuels, D. J. (Eds.) (2004). *Decentralization and democracy in Latin America*. Notre Dame, IN: University of Notre Dame Press.

Montesquieu, Baron de (C de Secondat). (1989). The spirit of the laws. Cambridge: Cambridge University Press, trans. A. M. Cohler, B. C. Miller and H. Stone.

Montinola, G., Qian, Y., & Weingast, B. R. (1996). Federalism, Chinese style: The political basis for economic success. *World Politics, 48*(1), 50–81.

Mookherjee, D. (2006). Decentralization, hierarchies, and incentives: A mechanism design perspective. *Journal of Economic Literature, 44*(2), 367–390.

Mulumba, D. (2004). *Uganda: Country review of the framework of decentralization*. IFAD, Office of Evaluation.

Muñoz, L. G. C., Acosta, A. J. O., & Moreno, L. D. (2006). *Aspectos básicos de la descentralización en México*. Mexico City: Instituto Nacional para el Federalismo y el Desarrollo Municipal.

North, D. C., Wallis, J. J., & Weingast, B. R. (2009). *Violence and social orders: A conceptual framework for interpreting recorded human history*. Cambridge: Cambridge University Press.

O'Donnell, G. (1998). Horizontal accountability in new democracies. *Journal of Democracy, 9*(3), 112–126.


Please cite this article in press as: Faguet, J. -P. Decentralization and Governance, *World Development* (2013), http://dx.doi.org/10.1016/j.worlddev.2013.01.002

Ostrom, E. (1990). *Governing the commons*. Cambridge: Cambridge University Press.

Oxhorn, P., Tulchin, J. S., & Selee, A. D. (2004). *Decentralization, democratic governance, and civil society in comparative perspective: Africa, Asia and Latin America*. Washington, DC: Woodrow Wilson Center Press.

Oxford English Dictionary, online version. (2012). Oxford: Oxford University Press. Available from http://www.oed.com/.

Prud'homme, R. (1995). On the dangers of decentralization. *World Bank Research Observer, 10*, 210–226.

Przeworski, A., Alvarez, M. E., Cheibub, J. A., & Limongi, F. (2000). *Democracy and development*. New York: Cambridge University Press.

Putnam, R. D. (1993). *Making democracy work: Civic traditions in Modern Italy*. Princeton: Princeton University Press.

Rao, V., & Woolcock, M. (2003). Integrating qualitative and quantitative approaches in program evaluation. In F. Bourguignon, & L. A. Pereira da Silva (Eds.), *The impact of economic policies on poverty and income distribution: Evaluation techniques and tools*. New York: Oxford University Press and The World Bank, Chapter 8.

Remmer, K. L., & Wibbels, E. (2000). The subnational politics of economic adjustment: Provincial politics and fiscal performance in Argentina. *Comparative Political Studies, 33*, 419–451.

Riker, W. H. (1964). *Federalism: Origin, operation, significance*. Boston: Little Brown.

Rodden, J. A. (2006). *Hamilton's paradox: The promise and peril of fiscal federalism*. Cambridge: Cambridge University Press.

Rodden, J. A., Eskeland, G. S., & Litvack, J. (2003). *Fiscal decentralization and the challenge of hard budget constraints*. Cambridge, MA: MIT Press.

Romeo, L. G., & Spyckerelle, L. (2003). Decentralization reforms and commune-level services delivery in Cambodia. Unpublished case study submitted at the Workshop on "Local Government Pro-Poor Service Delivery", Manila, February 9–13, 2004.

Rondinelli, D. A., Cheema, G. S., & Nellis, J. (1983). Decentralization in developing countries: A review of recent experience. World Bank Staff Working Paper No. 581, Washington, DC.

Rousseau, J. J. (1978 [1762]). On the social contract. In R. D. Masters (Ed.). New York: St. Martin's Press, trans. J. R. Masters.

Saiegh, S. (2004). The 'sub-national' connection: Legislative coalitions, cross-voting, and policymaking in Argentina. In F. Fiorucci, & M. Klein (Eds.), *The argentine crisis at the turn of the millennium: Causes, consequences, and explanations* (pp. 107–126). Amsterdam: Aksant Academic Publishers.

Samoff, J. (1990). Decentralization: The politics of interventionism. *Development and Change, 21*, 513–530.

Sartori, G. (1976). *Parties and party systems: A framework for analysis*. Cambridge: Cambridge University Press.

Shami, M. (2010). The impact of market exposure on public goods provision. Institute of Food and Resource Economics Working Paper 2010/13, University of Copenhagen.

Slater, D. (1989). Territorial power and the peripheral state: The issue of decentralization. *Development and Change, 20*, 501–531.

Smith, A. (1991 [1776]). *An inquiry in the nature and causes of the wealth of nations*. London: Everyman.

Smith, B. C. (1985). *Decentralization: The territorial dimension of the state*. London: George Allen & Unwin.

Tanzi, V. (1995). Fiscal federalism and decentralization: A review of some efficiency and macroeconomic aspects. In *Annual World Bank conference on development economics*. Washington, DC: World Bank.

Treisman, D. (2007). *The architecture of government: Rethinking political decentralization*. New York: Cambridge University Press.

USAID (2009). *Democratic decentralization programming handbook*. Washington, DC: USAID.

Wallis, J. J., & Oates, W. E. (1988). Decentralization in the public sector: An empirical study of state and local government. In H. Rosen (Ed.), *Fiscal federalism quantitative studies* (pp. 5–32). Chicago: University of Chicago Press.

Watts, R. L. (1966). *New federations: Experiments in the commonwealth*. Oxford: Oxford University Press.

Widner, J. A. (2001). *Building the rule of law*. New York: W.W. Norton.

Wietzke, F. B. (2012). Universal primary education, private schooling, and interreligious inequality: Evidence from Madagascar. Manuscript, London School of Economics.

Wildasin, D. E. (1998). Fiscal aspects of evolving federations: Issues for policy and research. World Bank Policy Research Working Paper 1884, Washington, DC.

World Bank. (1995). Colombia local government capacity: Beyond technical assistance. World Bank Report 14085-C. Washington, DC: World Bank.



Please cite this article in press as: Faguet, J. -P. Decentralization and Governance, *World Development* (2013), http://dx.doi.org/10.1016/j.worlddev.2013.01.002