Why Good Institutions Aren't Enough

The Missing Variable in Development Economics Is Not Institutional Quality—It's Institutional Speed

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IDEA IN BRIEF

THE PROBLEM

Development economics has spent three decades measuring institutions as static rules—property rights, legal systems, constraints on power—and scoring them on quality indices. This explains why rich countries stay rich, but it doesn't explain why some countries industrialize at extraordinary speed under the "wrong" institutions, or why others stagnate despite adopting the "right" ones.

THE ARGUMENT

Institutions aren't rules; they're coordination architectures—structured systems that align investment, standards, infrastructure, finance, and governance. What separates countries that transform from those that stagnate is not institutional form but adaptive bandwidth: how fast institutions can update when technology, markets, and governance fall out of sync.

THE IMPLICATION

"Development" is not convergence toward a fixed institutional template but an endogenous process of institutional evolution. Countries that build high-bandwidth architectures capable of coordinating change under uncertainty can compress development timelines. On the other hand, countries that import institutions designed for stability into economies that need transformation will continue to stall.

There is a question that has haunted development economics for decades: if we know what good institutions look like, why can't countries that adopt them seem to grow?

The field has a powerful answer for why rich countries stay rich. Secure property rights, predictable legal systems, constraints on political power—these features correlate strongly with long-run prosperity, and the research establishing this relationship is among the most influential in modern economics.

But that same framework struggles badly with a different set of facts. Japan, South Korea, Taiwan, Singapore, and later China industrialized at extraordinary speed under institutional configurations that looked nothing like the textbook. State-directed credit, managed competition, high bureaucratic discretion, iterative policy experimentation—these weren't deviations from the model, they *were* the model. Meanwhile, country after country that inherited Western legal and administrative frameworks—parliamentary systems, professional civil services, codified property rights—failed to industrialize at all.

The standard explanation is that the latter group had institutions that were somehow lower quality, or incomplete, or corrupted. But this doesn't necessarily hold up, because many of these countries had formal institutional architectures that scored well on governance indices. They had the rules, but what they didn't have was the capacity to coordinate.

And that's where the existing framework breaks down. It can tell you what institutions look like when they're working, yet it cannot tell you how they change, how fast they adapt, or why some institutional systems can reorganize an entire

economy under pressure while others can't reorganize a procurement process.

INSTITUTIONS AREN'T RULES, THEY'RE COORDINATION SYSTEMS.

The problem is conceptual in that economics treats institutions as *rules of the game*—static constraints that shape incentives. That's fine for explaining why things stay the same, but it's useless for explaining how things change.

Structural transformation—industrialization, technological catch-up, the creation of entirely new markets—doesn't just need stable rules, it needs active coordination across interdependent actors, sectors, and levels of government. What's needed isn't a better score on a governance index. Rather, it's a fundamentally different idea of what institutions *are*.

The reframing proposed here treats institutions as coordination architectures: structured systems that organize, align, and stabilize interactions among different actors under uncertainty. They have purpose functions, adjustable settings (discretion, enforcement, standards, procurement, risk-sharing), constraints, interfaces between different parts of the system, and feedback loops that determine whether the system learns from its mistakes or just repeats them.

Through this lens, the question of whether a country has secure property rights or independent courts becomes a lot less relevant than whether its institutional system can revise standards fast enough, redirect finance when conditions change, and coordinate complementary investments across sectors that don't yet exist.

Development economics asks whether countries have the right institutions. The better question is whether they have institutions capable of changing fast enough.

THE VARIABLE THAT'S MISSING: ADAPTIVE BANDWIDTH

If institutions are architectures, the key question becomes how fast they can update. That's what **adaptive bandwidth** measures: the rate at which an institutional system can revise its settings in response to misalignment between technology, markets, and governance.

High-bandwidth systems process feedback frequently, tolerate experimentation, and allow adjustments to propagate across the system. They can revise standards, redirect finance, reallocate authority, or reorganize coordination structures without everything grinding to a halt.

Think of South Korea in the 1970s: the government restructured entire industrial sectors in response to changing export conditions, redirected credit, revised standards, and reorganized state–business interfaces—repeatedly, iteratively, and fast.

Low-bandwidth systems are on the other end of this spectrum: they are optimized for stability. They emphasize predictability, rule enforcement, and consistency—which is exactly what you want when you're managing a complex, mature economy. But those same features become liabilities when the economy needs to change. Adjustment is slow, politically contested, and often reactive. The gap between what the technology can do and what the institutional system can support persists—or widens.

This is what existing institutional quality measures miss entirely; they may capture whether property rights are secure or courts are independent, but they don't capture whether the system can move when it needs to.

THREE DEVELOPMENT REGIMES

Variation in adaptive bandwidth produces three distinct outcomes.

In a **transformation regime**, institutions adjust fast enough to keep pace with technological change.

When a gap opens between what the economy can technically produce and what its markets and governance can support, the response is rapid: standards are revised, finance is redirected, coordination structures are reorganized. The gap closes. This is the regime that characterized the East Asian industrializers—economies where institutional architectures were built to move.

In an **optimization regime**, institutions adjust slowly but maintain a steady alignment with the existing economic structure. The system works well for what it already does, but when new technologies or coordination demands arise, the response is incremental and contested. The gap doesn't widen dramatically—but it doesn't close either. This is the condition of most advanced Western economies today.

In a **premature regime**, institutions can't keep up. Technology advances, but the markets, infrastructure, standards, and governance arrangements needed to turn that technology into economic activity lag further and further behind. Industrial projects stall, markets remain shallow, coordination failures repeat. This is the trap that holds many post-colonial economies—not because they lack institutions, but because the institutions they inherited were designed for stability, not transformation.

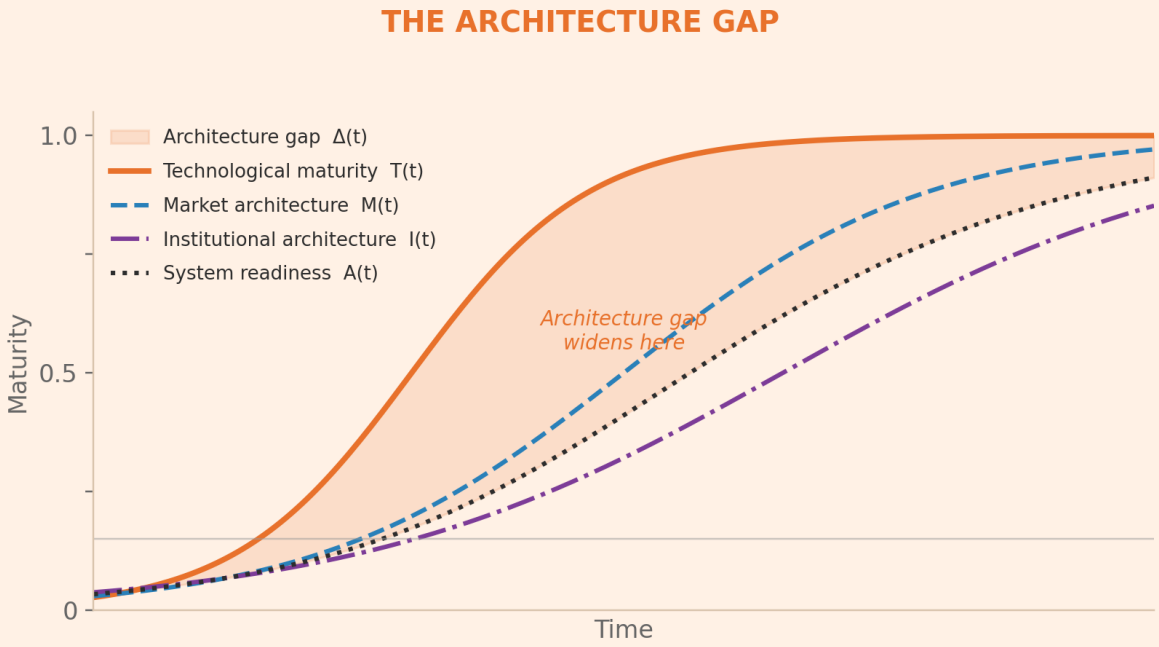

Figure 1: Technology advances fastest, followed by market architecture and institutional architecture. The shaded region shows the architecture gap—the structural misalignment that determines whether markets can form.

THREE DEVELOPMENT REGIMES

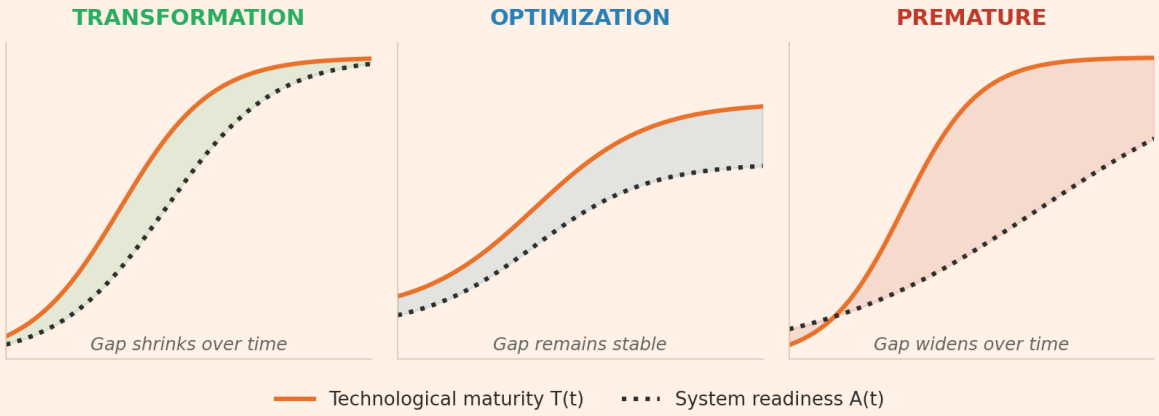

Figure 2: In transformation regimes, institutional adjustment closes the gap. In optimization regimes, it stays stable. In premature regimes, it widens—technological capability accumulates but markets fail to form.

TWO INSTITUTIONAL ARCHITECTURES COMPARED

DIMENSION	TRANSFORMATION ARCHITECTURE	OPTIMIZATION ARCHITECTURE
Adaptive bandwidth	High: frequent feedback, tolerance for experimentation, rapid institutional revision	Low: emphasis on predictability, rule enforcement, procedural consistency
Primary function	Build new economic systems under uncertainty; coordinate structural change	Stabilize and refine existing systems; minimize variance and enforce compliance
Policy mode	Iterative adjustment; decentralized implementation with central oversight	Rule-based governance; judicial enforcement; low discretion
Coordination logic	Align complementary investments across infrastructure, finance, standards, production	Incentive alignment through property rights, contracts, and market signals
Historical examples	Japan 1950s–80s, South Korea 1960s–90s, Taiwan, Singapore, China post-1978	United States, United Kingdom, EU member states, post-colonial transplant economies
Failure mode	Overreach; politicized allocation; failure to transition to optimization when mature	Inability to reorganize under new technological paradigms; persistent architecture gap

THE TRANSPLANTATION TRAP

This reframing explains one of the most persistent puzzles in development economics: why copying institutions almost never works.

After independence, many post-colonial states adopted institutional arrangements that closely resembled Western legal and administrative systems—constitutions, centralized bureaucracies, commercial law, judicial frameworks modeled on European systems. On paper, these looked like the institutions that had worked in rich countries.

But (and this is a big *but*), they were introduced into economies with incomplete markets, limited industrial capacity, weak infrastructure, and enormous coordination demands. And here's the

mismatch: these were optimization architectures—designed to enforce rules, maintain procedural regularity, and stabilize mature systems—dropped into contexts that needed transformation architectures.

They prioritized compliance over coordination, legal consistency over adaptive speed.

India after independence is the clearest example. It inherited one of the most sophisticated legal systems in the developing world, a professional civil service, and parliamentary institutions closely modeled on Britain's. Industrialization proceeded slowly and unevenly nonetheless. Infrastructure, finance, technology adoption, and market formation all evolved at different speeds with no mechanism to pull them into alignment. The institutions were present. The coordination capacity wasn't.

Compare this with South Korea, which didn't inherit Western-style institutional stability but built high-bandwidth coordination architectures from scratch—capable of aligning finance, infrastructure, production, and export markets under conditions of extreme uncertainty. The difference isn't explained by institutional presence or formal quality; it's explained by institutional function.

WHY THIS CHANGES INDUSTRIAL POLICY

Industrial policy has long been treated with skepticism by mainstream economics—and not without reason. Much of the evidence evaluates interventions as isolated treatments: did this subsidy raise exports? Did this tariff protect the right firms? The results are mixed, and the skeptics have a point.

But the framing is wrong. Industrial policy isn't primarily a question of subsidy scale or targeting precision; it's a question of coordination capacity. Policies succeed when the state can align standards, infrastructure, finance, procurement, regulation, and private investment with emerging technologies. When that coordination architecture is missing, every instrument looks like it's failing: subsidies raise activity without building ecosystems, targeting produces stranded assets, and projects get stuck in pilot-scale equilibria.

This reframes what the state actually does when industrial policy works. It's not picking winners, instead it's building the coordination system that allows winners to emerge—sequencing infrastructure, stabilizing early demand, adjusting standards as technologies mature, and reorganizing governance in response to feedback. High-bandwidth states can do this iteratively, whereas low-bandwidth states deploy the same instruments but can't coordinate across subsystems, so the result is fragmentation and waste.

THE PRODUCTIVITY CONNECTION

This framework also changes how you think about productivity. The standard approach emphasizes firm-level efficiency—are resources going to the most productive firms? Are barriers to entry low enough? But this treats misallocation as an outcome rather than a coordination problem.

High-bandwidth institutional systems don't just improve firm incentives. They reorganize the environment firms operate in. Stable interfaces, coordinated complementary investments, and enabled specialization allow productive firms to expand, supply chains to deepen, and learning effects to compound. Productivity growth is a systems outcome, not a firm-level one.

This also explains why productivity slows in mature economies. As institutions become optimized for stability, they lose the capacity to reorganize when new technological paradigms emerge. The slowdown isn't a lack of innovation, it's simply a growing mismatch between what's technologically possible and what the institutional system can coordinate.

THE PARADIGM SHIFT

Development economics has spent decades asking whether countries have the right institutions. The evidence suggests a more productive question: *whether they have institutions capable of changing fast enough.*

The distinction between transformation and optimization architectures isn't normative. It doesn't map onto democracy versus authoritarianism, or state versus market. Democratic systems can exhibit high adaptive bandwidth just as authoritarian ones can be rigid and brittle. What matters is not political form but institutional function: can the architecture coordinate large-scale change under uncertainty, or is it optimized for maintaining stability in a system that already works?

Misalignment happens in both directions. Stability-oriented institutions applied to transformation-phase economies produce stagnation. Transformation-oriented institutions that persist beyond their useful phase produce overreach and politicized allocation. The problem in both cases is the same: a mismatch between what the institutional architecture is designed to do and what the economy actually needs.

Development, therefore, is not convergence toward a fixed institutional template but an endogenous process of institutional evolution. And the countries that will shape the next century of economic history are not those that adopt the institutions of countries that already succeeded. They're the ones that build institutions capable of transforming an economy under uncertainty.

This article draws on the working paper by Sinéad O'Sullivan: ***Institutions as Coordination Architectures: Adaptive Bandwidth*** *This paper develops the formal models, mathematics, and cross-domain evidence summarized here.*

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