Double Trap: Institutions and Economic Development

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Abstract

The empirical growth literature has established that institutional quality is a deep determinant of economic growth. We examine whether institutional quality in low income countries converges to the level witnessed in high income countries, or whether they are trapped in convergence clubs that stagnate or even deteriorate over time. Using the log-t-test suggested by Phillips and Sul (2007), we find evidence of multiple equilibria in institutional quality, with several countries stuck in poor quality institutions traps. We further find that per capita incomes of some of the developing countries are also stuck in low-level traps. Finally, using bivariate probit estimations, we establish that poor institutional traps are major determinants of low income traps. These results indicate that these countries are caught in a double trap where their incomes are stuck in low-level traps from which it is difficult to escape, because the institutions that enable growth are also stuck in low-quality traps.