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Inclusive institutions and the need for institutional reforms: Lessons from the 2024 Nobel laureates in economics

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Article Info	Abstract
Short Paper Main Object: Economics Scope: Iran Received: 23 October 2024 Revised: 01 November 2024 Accepted: 03 November 2024 Published online: 04 November 2024 **Keywords:** development, institutional reforms, institutions, Iran, Nobel Prize in Economics.	In 2024, Daron Acemoglu, Simon Johnson, and James Robinson were awarded the Nobel Prize in economics for their research on the role of institutions in economic development. Their studies highlight that inclusive institutions, which promote broad participation in both the economy and politics, are essential foundations for development. In contrast, extractive institutions that serve the interests of specific groups hinder economic and social progress. Iran's current state, characterized by inefficient, extractive institutions that protect minority interests, disrupts the country's development process. Drawing from the Nobel laureates' findings, it is clear that institutional reforms to enhance transparency, eliminate rent-seeking, and increase public participation are essential for setting the country on a path to development. In Iran, key obstacles to development include policies that favor specific groups over the general population, limited political participation, and the lack of an accountable party system. These economists stress the importance of reforming political and economic institutions to enable inclusive, participatory governance that can foster economic growth.

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Extended Abstract
Introduction
In 2024, Daron Acemoglu, Simon Johnson, and James Robinson received the Nobel Prize in economics for their groundbreaking research on institutions and their impact on economic welfare and development. This award not only honors their efforts to deepen our understanding of institutions' roles, but also underscores the relevance of their findings for countries like Iran, which seek to navigate their current challenges and advance toward economic growth and development.

To better understand this message, we must first briefly examine the concept of institutions. Institutions can be defined as the "rules of the game" in any society, encompassing a set of laws, norms, and structures that govern individuals' behavior in economic, social, and political interactions (Hodgson, 2006). Institutions are formal and informal frameworks aimed at regulating human behavior and reducing transaction costs arising from uncertainty among exchange parties (North, 1990). When institutions are effective, trust between exchange parties increases, reducing transaction costs. This facilitates economic, political, and social exchanges at lower costs. Inefficient institutions, conversely, heighten uncertainty and transaction costs, impeding economic and social development.

Aims
The purpose of this article is to understand the necessity of reforming political and economic institutions to analyze the status of economic and political institutions in Iran and their impacts on economic development.

Discussion
Types of institutions: Formal and informal
Institutions are traditionally divided into formal and informal categories. Formal institutions include laws and regulations officially enacted by governments and legislative bodies. These laws monitor exchanges and create the necessary legal framework for building trust between parties. Informal institutions, on the other hand, consist of norms, values, customs, traditions, religion, and other cultural elements that shape social expectations and behavior without requiring formal laws (Hodgson, 2006; North, 1990).

The role of political competition and transparency in institutions
Studies show that a key factor in forming inclusive institutions is the presence of political competition and transparency within the political system. Societies with political competition and open-access systems, characterized by greater governmental transparency, create more efficient institutions. Political competition and open-access order

promote broader societal participation in politics and economics, preventing power from becoming concentrated in the hands of rentier parties. Such environments allow individuals and various societal sectors to participate in decision-making processes, leading to inclusive institutions that facilitate sustainable economic growth and development (Acemoglu & Robinson, 2012).

Roots of inclusive and extractive institutions

To understand the effects of institutions on development, they can be divided into inclusive and extractive categories. Inclusive institutions guarantee property rights and promote public participation in politics and economics. These institutions support long-term investments and lay the groundwork for sustainable growth and social development. In contrast, extractive institutions primarily aim to preserve power and wealth for a specific group or rentier parties. Such institutions weaken property rights, restrict participation, and prioritize short-term control over resources for the benefit of select groups (Acemoglu et al., 2001). A study by Acemoglu, Johnson and Robinson (2001) demonstrates that institutions—especially property rights, and rule of law—are essential for fostering an environment that promotes investment, efficient resource use, and overall economic performance. Countries with higher-quality institutions protect private ownership and limit undue government interference, often achieving higher income and development levels. In their research, they compare extractive institutions focused on short-term resource extraction (such as colonial institutions in Congo) with inclusive institutions that promote long-term participation and growth (as in settler colonies like the United States and Canada).

For example, during Belgium's colonial rule in Congo, the political and economic system focused on extracting natural resources (like diamonds and copper) and exploiting native labor. Colonial institutions operated solely for the benefit of colonizers, neglecting infrastructure development or support for local growth. In contrast, settler colonies like the United States developed institutions that recognized private property rights and allowed individuals to participate economically and politically. These institutions fostered long-term investment, industrial growth, and sustainable economic development.

While extractive institutions are generally designed to exploit resources and maintain control among elite groups, inclusive institutions strive to secure property rights for all and encourage broader political and economic participation. Ultimately, these differences lead to significant disparities in economic development levels across countries. The Nobel laureates' research clearly illustrates that economic development can only occur under inclusive political and economic institutions.

Critical junctures and their impact on institutional development

Critical junctures are key historical moments where the existing political and economic order is challenged, creating an opportunity for major changes. At these moments, countries face choices that can determine their long-term fate. For example, the Industrial Revolution in Britain and the fall of the Berlin Wall are recognized as critical junctures that fundamentally changed these countries' development paths. Such changes led to the establishment of inclusive and democratic institutions that fostered sustainable economic growth. In other words, at these moments, countries can either move toward positive reforms and create more inclusive institutions or remain on a path where ruling elites maintain power and wealth, reinforcing extractive institutions that ultimately lead to stagnation and poverty (Robinson & Acemoglu, 2012).

The importance of path dependency

Path dependency suggests that once institutions are established, they tend to persist and become more entrenched, making changes over time difficult. This concept is particularly relevant in societies that have chosen extractive and inefficient institutions during critical junctures, as reforms in these societies often encounter significant resistance. Over time, those who benefit from the existing system work to preserve it, creating vested interests that make change more challenging. For instance, countries that have followed specific institutional paths at historical turning points often struggle to deviate from these paths and implement fundamental institutional reforms (North, 1990; Robinson & Acemoglu, 2012).

A notable example of path dependence following critical decisions at historical turning points is the stark contrast between South Korea and North Korea. The critical juncture for these two nations occurred in the mid-20th century, in the post-World War II and Cold War era, when the Korean Peninsula was divided in 1945 following the defeat of Japan in World War II. North Korea came under Soviet influence, while South Korea was aligned with the United States. The Korean War in 1950 further deepened these divisions, setting the two countries on distinct paths.

While South Korea moved toward more inclusive institutions and underwent widespread economic and social reforms, North Korea followed a closed path, establishing a socialist authoritarian regime based on extractive institutions and centralized state control. From the 1960s onward, South Korea embraced institutional and economic reforms, progressing toward industrialization and attracting foreign investment. In turn, South Korea developed institutions that protected private property and promoted broad economic participation.

Conversely, North Korea maintained a closed, one-party system focused on government control over resources and strict social

Countries Studies, Vol 3, No 1, Spring 2025

regulation, continuing its path dependency without implementing meaningful reforms. These extractive institutions allowed the government to maintain complete control over resources and society, suppressing any economic or social activities outside the state's framework.

Path dependency in North Korea has resulted in a closed political system that resists change. Over the decades, those benefiting from this system have worked to preserve it, reinforcing institutions that prevent the entry of global economy, innovation, and reform. Meanwhile, South Korea adopted more inclusive institutions, transitioning toward an export-based economy and attracting foreign investments.

These differences are directly reflected in the two countries' development levels: South Korea is one of the world's most advanced economies, with high living standards and democratic institutions, while North Korea remains impoverished and internationally isolated. This example demonstrates how institutional choices at critical junctures and subsequent path dependence can shape a country's long-term development trajectory. This case underscores the challenges of path dependency in implementing fundamental institutional reforms and why decisions made at critical junctures—such as the Korean War—can have enduring and difficult-to-reverse impacts (North, 1990; Robinson & Acemoglu, 2012).

In the remainder of this paper, we will explore the message of the 2024 Nobel laureates' research for Iran's economy, following the framework presented above.

Methods

In this study, a comparative institutional analysis approach and an applied-theoretical research method are used to examine and analyze the status of economic and political institutions in Iran and their impacts on economic development. The research approach is based on the theoretical framework presented by Daron Acemoglu, Simon Johnson, and James Robinson regarding the role of inclusive and extractive institutions in the economic development of countries. This framework has been used as a comparative basis for analyzing the institutional status of Iran. The methodology steps are as follows:

1. **Review and Interpretation of relevant theories.** In the first step, a thorough review of literature and theories related to inclusive and extractive institutions from the works of Acemoglu and colleagues (2001), and Robinson and Acemoglu (2012) was conducted to develop the theoretical foundations of the study. These theories helped form an analytical framework in which institutions are categorized as either inclusive or extractive. Their roles are analyzed in terms of reducing or increasing transaction costs, creating or hindering investment incentives, and improving or restricting property rights. This conceptual framework, which

is also emphasized in the economic institutionalism literature (North, 1990; Hodgson, 2006), has been employed as a tool to assess existing institutions in Iran.

2. **Adapting theories to Iran's context.** In the next phase, the theories of inclusive and extractive institutions were applied in a comparative manner to examine Iran's economic and political institutions. Initially, by reviewing legal and administrative structures, such as property laws and constraints on government power, Iran's status was situated within the inclusive-extractive theoretical framework. Analytical and observational data on the current state of Iranian institutions, including domestic and international economic and social reports and secondary analyses, were used to analyze institutional effectiveness or inefficacy.
3. **Inference and analysis of outcomes.** In this step, the main consequences of these institutions for Iran's economic development were identified based on the characteristics of extractive institutions outlined in Acemoglu and colleagues' theory. To draw inferences, the study examined how current institutions affect public trust and participation, then predicted the probable outcomes of continued ineffective institutions in Iran based on empirical evidence and comparisons with other countries. The inference method was both deductive and inductive, using historical and comparative evidence based on Iran's current conditions and comparisons with countries with inclusive and developed institutions.

This research, while theoretical, is designed as an applied study to provide insights for policymakers and economic planners. The aim is to analyze existing economic and political institutions in Iran and clarify the consequences of maintaining extractive institutions, thereby offering recommendations for institutional reforms and a transition toward inclusive institutions.

Findings

The current economic issues in Iran can be analyzed from an institutional perspective. The country's political and economic institutions are often described as "extractive"—structures that benefit a small elite while neglecting broader economic participation and transparency. This situation leads to uncertainty, diminished public trust, and discourages long-term investments in human and physical capital essential for sustainable development. Moreover, the current inefficiencies have driven a significant exodus of human capital, known as the "brain drain" in recent decades, which now includes skilled workers, specialists, and technicians, and continues to intensify yearly.

One of the primary factors behind the current disorder—considered by Nobel laureates as the main obstacle to development—is the legacy of unfavorable institutions resistant to reforms. This resistance is largely due to vested interests among groups benefiting from the status quo who block any positive change. According to the theory of Acemoglu and Robinson, exclusive and non-inclusive institutions not only hinder economic development but also lead to political and social crises. For Iran, institutional reforms must therefore aim at increasing inclusiveness and facilitating participation across all societal groups in economic and political processes.

Another problem is the lack of prioritization of public economic interests in policymaking. While development programs have set targets like 8% growth, policies in practice have consistently failed to achieve these goals. Acemoglu and his colleagues emphasize that strong and inclusive institutions can create a positive cycle, gradually leading to economic growth and the strengthening of civil society. Eliminating rent-seeking behaviors and promoting transparency in economic processes can encourage innovation and long-term investment, resulting in sustainable development.

A major challenge in Iran is the absence of a responsive party system. Without competition and accountability, politicians seldom answer for their performance, reducing public political and economic participation. Nobel laureates argue that democratic and inclusive governance is fundamental to economic development because only through participation and accountability can a resilient and sustainable economy be achieved.

Iran's domestic and foreign policies have largely been influenced by the interests of specific rentier groups, which has limited constructive international interactions. Inefficient domestic institutions have not only constrained economic development but have also severely damaged international relations, intensifying sanctions and international tensions. Consequently, domestic institutional reforms could facilitate more effective international engagement and help rebuild global economic relations.

For sustainable growth and development, Iran needs profound institutional reforms. The first step is to establish inclusive economic institutions that ensure participation from all sectors of society. These institutions should create a free and fair competitive environment and support small and medium-sized enterprises. Facilitating private and foreign investment and reducing state and quasi-state monopolies are also essential in this direction.

Additionally, improving the economic environment requires transparency and corruption reduction. Widespread corruption in government institutions has eroded public trust and hindered new investment. Strengthening an independent judiciary and fighting corruption indiscriminately could rebuild public trust and create a safer investment climate.

Another essential reform is to reduce dependency on the oil-based economy. Iran's reliance on oil resources has made the country vulnerable and limited economic diversification. This issue, often referred to in theory as the "resource curse", has weakened civil society, democracy, and social capital. The government's budget independence from tax revenues over decades has disconnected policymaking from a people-centered economy, placing non-economic priorities at the forefront of policymaking. Moving toward a knowledge-based economy and developing innovative industries such as information technology, tourism, and pharmaceuticals could promote economic diversification and reduce oil dependency.

Finally, more constructive engagement with the world and reducing international tensions through diplomacy and economic relations rebuilding could enhance exports, attract foreign investment, and strengthen Iran's position in global markets. Furthermore, domestic policy reforms that ensure active political participation could drive economic growth and civil society development. Inclusive and accountable governance in economic policymaking can contribute to Iran's sustainable social and economic development.

Conclusion

The outlook for Iran's economic development depends on the country's ability to implement inclusive institutional reforms. Although the current situation is extremely complex due to sanctions, structural issues, and inefficient institutions, gradual and continuous reforms aimed at strengthening inclusive institutions can lead to significant improvements in the economic environment. By moving toward greater transparency, eliminating rent-seeking behaviors, and strengthening property rights, new investments and public trust are likely to increase, paving the way for sustainable and long-term economic growth.

Through these reforms, Iran could approach a hopeful development trajectory, in which the economy relies on knowledge and innovation and reduces dependency on natural resources. At the same time, constructive relations with other countries and reduced international tensions could facilitate export growth and attract foreign investment, both of which are essential for economic growth and prosperity.

In summary, the research of the 2024 Nobel laureates in economics teaches us that institutional reforms should move toward creating transparent and inclusive institutions that serve the interests of the majority and ensure fair competition. For example, lifting internet censorship—a long-debated issue in Iran—could be recognized as a key reform in this direction. Open internet access would not only boost internet-based businesses but also enhance transparency, innovation, and economic capabilities. Furthermore, based on extensive evidence and studies, such reforms can lead to sustainable economic growth and poverty reduction (Bergantino et al., 2024). The current censorship laws, as inefficient institutions, only impose high transaction costs on people and businesses and hinder the creation of a dynamic and competitive economic environment.

Ultimately, Iran can only return to the path of development and progress if political and economic institutions move toward inclusiveness and accountability, and the ruling elites prioritize the interests of society as a whole rather than specific groups. The Nobel laureates' main message is clear: institutional reform is the key to development, and such reforms must serve the public rather than exclusive interests. Thus, building inclusive and efficient institutions can become the central focus of policymaking in Iran, leading to improved quality of life and enhanced social welfare.

Conflict of interest

The author declared no conflicts of interest.

Ethical considerations

The author has completely considered ethical issues, including informed consent, plagiarism, data fabrication, misconduct, and/or falsification, double publication and/or redundancy, submission, etc.

Data availability

The dataset generated and analyzed during the current study is available from the author on reasonable request.

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