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# INSTITUTIONS AS THE FOUNDATION OF ECONOMIC PROSPERITY: INSIGHTS FROM NEW INSTITUTIONAL ECONOMICS

UDC / UDK: 330.34/.35:330.837
JEL classification / JEL klasifikacija: B52, O43, O40, D02
https://doi.org/10.17818/EMIP/2026/37
Review / Pregledni rad
Received / Primljeno: May 13, 2026 / 13. svibnja 2026.
Accepted / Prihvaćeno: August 26, 2026 / 26. kolovoza 2026.

## *Abstract*

*This paper examines how New Institutional Economics conceptualises the relationship between institutions and long-term economic performance. Drawing on seminal work by Douglass North, Ronald Coase, Oliver Williamson, and later institutional scholarship, it presents a systematic mapping review of literature published between January 1990 and June 2026. Using OpenAlex records, predefined eligibility criteria, bibliometric classification, and structural topic modelling, the review identifies the field's main themes and their evolution over time. It synthesises four channels through which institutions may affect economic outcomes: incentives and transaction costs; factor accumulation and innovation; resource allocation and governance; and income distribution and political power. The reviewed evidence generally links stronger institutional quality to better economic outcomes. The strength and timing of these relationships vary across institutional measures, empirical methods, countries, and enforcement contexts. Administrative capacity, institutional complementarities, informal norms, and political incentives also shape the effectiveness of formal institutional arrangements.*

***Keywords: institutions, economic growth, Institutional quality, economic development***

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# 1. INTRODUCTION

Persistent cross-country differences in income levels remain one of the most robust empirical regularities in modern economics. Despite decades of theoretical and empirical advances, there is still no consensus on the fundamental causes of these disparities (e.g., Banerjee and Duflo, 2011; Rodrik, 2019). Standard explanations based on capital accumulation, human capital, and geography account for proximate drivers of growth but fail to explain why these drivers themselves differ systematically across countries.

In this context, New Institutional Economics (NIE) has emerged as a powerful analytical framework that places institutions at the center of economic analysis. The term was introduced into the social sciences and economics literature by Nobel laureate Oliver E. Williamson (Williamson, 1975). A few years later, the term gained prominence and began to appear in the titles of books, academic articles, research projects, and related scholarly outputs. As a distinct school of thought of predominantly United States origin, NIE experienced a significant rise from the 1980s onward, primarily due to the contributions of its leading figures, the Nobel laureates Douglass C. North, Ronald H. Coase, and Oliver E. Williamson (e.g., Williamson, 1985, 2000; Coase, 1988, 1998; North, 1990; Ménard and Shirley, 2014).

Although NIE initially developed outside the central core of mainstream economic theory – as an alternative to neoclassical economics, it has since attracted a steadily growing number of adherents. This trend intensified particularly after 2000, driven by the contributions of scholars such as Daron Acemoglu, Simon Johnson, and James A. Robinson, who were awarded the Nobel Prize in Economic Sciences in 2024 for their research on the relationships and interactions between institutions and the economic prosperity of nations. Admittedly, the claim that "institutions matter" for economic growth and development represents a longstanding intellectual tradition. Early proponents of classical economic thought, particularly Adam Smith (Smith, 1776/1976) and John Stuart Mill (Mill, 1848/2004), emphasized that well-functioning economic institutions constitute a fundamental determinant of economic prosperity.

Although the primary focus of NIE is on economic and political institutions, the broadly defined research agenda encompasses a wide range of analytical domains, including transaction costs, property rights, contracts, the economic analysis of law, constitutional economics, public choice theory, and principal-agent problems. A common feature across these approaches is that, in contrast to neoclassical economics, they do not treat the institutional framework as exogenously given. Instead, institutions themselves are regarded as objects of inquiry, with particular emphasis placed on examining how specific institutional arrangements shape economic behavior (Richter, 2005).

The most prominent representatives of NIE are leading scholars and Nobel laureates in Economic Sciences, Douglass C. North (1993), Ronald H. Coase (1991), and Oliver E. Williamson (2009) (Royal Swedish Academy of Sciences, 1991;

1993; 2009). The relevant literature also recognizes enduring contributions made by James M. Buchanan (1986), a leading figure in public choice theory, and Elinor Ostrom (2009), who shared the Nobel Prize with Williamson (Richter, 2005; Ménard and Shirley, 2025). More recent representatives of this school include Daron Acemoglu, Simon Johnson, and James A. Robinson, recipients of the 2024 Nobel Prize in Economic Sciences for their contributions to the analysis of the relationships between institutions and economic prosperity.

Our paper is guided by the following central research question: "What insights does the theoretical and empirical literature on NIE provide regarding how institutional structures and institutional quality shape long-term economic performance, through which mechanisms, and under what conditioning factors?" To address this question, the paper reviews and synthesizes the literature on institutions and their corresponding organizations, their significance for economic prosperity, the transmission mechanisms through which they influence economic growth and development, and the determinants of institutional change and persistence. The analysis concludes by considering the implications of these insights for institutional reform and economic policy.

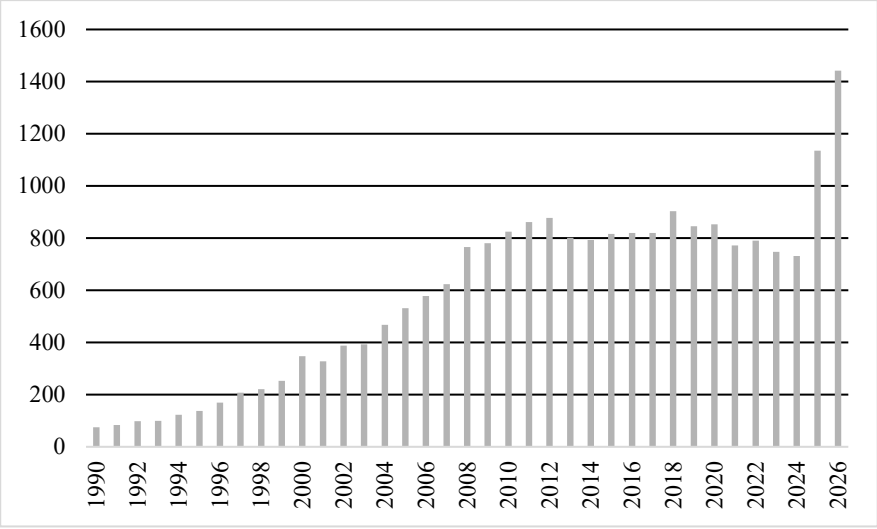
The paper contributes to the literature by providing a structured synthesis of theoretical and empirical insights from New Institutional Economics concerning the relationship between institutions and long-term economic performance. It systematically reviews the relevant literature, clarifies the distinctions between institutions and organizations and between formal and informal institutions, examines the principal mechanisms through which institutions influence economic outcomes, and identifies the factors that shape institutional change and persistence. The paper also draws out the implications of these insights for institutional reform and economic policy.

The remainder of the paper is organized as follows. Section 2 provides a brief systematic literature review of the main trends and branches of NIE. Section 3 investigates the distinction between institutions and organizations and examines the role of formal and informal institutional arrangements in shaping economic interactions. Section 4 outlines several classifications of institutions, including the distinction between formal and informal institutions, economic and political institutions, and different categories of market-supporting institutions. Section 5 analyzes how institutions affect economic prosperity by exploring competing explanations of growth, the transmission mechanisms through which institutions influence economic outcomes, and the determinants of institutional change and persistence over time. Section 6 discusses the implications of NIE for economic policymaking and highlights its complementary relationship with conventional macroeconomic approaches. Section 7 offers concluding remarks and highlights the avenues for future research.

## 2. REVIEW METHODOLOGY

This section employs a systematic mapping review to examine the theoretical and empirical development of New Institutional Economics (NIE). The review was conducted in R using bibliographic records retrieved from OpenAlex, an open-source catalog of global research. Study selection followed three sequential stages: title screening, abstract screening, and full-text assessment. Screening was conducted interactively using the *revtools* package, with records classified as included, excluded, uncertain, or unavailable where appropriate (Westgate, 2019). At the full-text stage, included studies were coded by NIE branch, study type, main outcome, geographical scope, and other mapping characteristics. The final dataset was used to generate publication trends, thematic distributions and tables of the most cited publications and authors. The period under investigation was confined to the period from January 1990 to June 2026. If all publications are considered (articles, books, book chapters, working papers, dissertations, etc.), a sustained expansion of research related to NIE is observed (Figure 1). Annual publication output increased gradually during the 1990s, accelerated after 2000, and remained relatively high after 2010. However, conceptual duplication remains, because the same research output may first appear as a working paper and later as a peer-reviewed journal article. Since some records may represent duplicate versions of the same research output, we refrain from interpreting the sharp increase in 2025 and January to June 2026 as evidence of an unprecedented surge in scholarly interest in NIE.

Figure 1 Annual distribution of publications related to New Institutional Economics, January 1990 - June 2026




*Source: Authors' data based on OpenAlex retrieved on July 27, 2026.*

To limit the scope of the literature review, we only focus on English-language research outputs published between January 1990 and June 2026. The predefined search streams covered key NIE concepts, such as transaction costs, property rights, institutional change, contracts, governance, and collective action. The search identified 5,400 records (Table 1).

Deduplication used OpenAlex identifiers, DOIs, and standardized title-year combinations. We excluded working papers, retracted publications, irrelevant studies, and research that treated transaction costs solely as financial trading costs. Hence, we removed 345 duplicates, leaving 5,055 records for title and abstract screening (Table 1). Preliminary screening excluded 2,472 records and retained 2,583 eligible publications for thematic classification and systematic mapping.

Table 1 Descriptive characteristics of the literature search results

| Indicator | Result |
|---|---|
| Records retrieved from *OpenAlex* | 5,400 |
| Duplicate records removed | 345 |
| Records retained after deduplication | 5,055 |
| Earliest publication year | 1990 |
| Latest publication year | 2026 |
| Records excluded by preliminary criteria | 2,472 |
| Eligible publications | 2,583 |
| Eligible publications (in percent) | 51.1 |
| Mean citations per publication | 139 |
| Median citations per publication | 45 |

*Source: Authors' calculations based on OpenAlex data retrieved on July 27, 2026.*

As presented in Table 2, most publications are devoted to institutional change, economics of transaction costs, and combinations of several NIE branches.

Table 2 Distribution of retrieved publications across branches of New Institutional Economics

| Rank | New Institutional Economics branch | Number of publications | Share of total (%) |
|---|---|---|---|
| 1 | Institutional change | 408 | 15.8 |
| 2 | Economics of transaction costs | 390 | 15.1 |
| 3 | Multiple NIE branches | 353 | 13.7 |
| 4 | Formal and informal institutions | 344 | 13.3 |
| 5 | General New Institutional Economics | 326 | 12.6 |
| 6 | Property-rights theory | 273 | 10.6 |
| 7 | Collective action and commons | 263 | 10.2 |
| 8 | Unclassified | 171 | 6.6 |
| 9 | Contracts and enforcement | 55 | 2.1 |
| | Total | 2,583 | 100.0 |

*Source: Authors' calculations based on OpenAlex data retrieved on July 27, 2026.*

NIE-related studies have mainly been focused on economic growth and development, a dominant research outcome accounting for 39.0% of retrieved publications (Table 3). Governance *per se* absorbs 15.3% of the primary research outcome, whereas productivity and performance represent another 11.2%. In turn, investment, innovation, inequality, and organizational choice receive substantially less attention. The high share of other or unspecified outcomes, 26.2%, indicates the thematic breadth of the NIE literature.

Table 3 Distribution of retrieved publications by primary outcome

| Primary outcome | Number of publications | Share of total (%) |
|---|---|---|
| Economic growth and development | 1,008 | 39.0 |
| Governance | 396 | 15.3 |
| Productivity and performance | 289 | 11.2 |
| Investment | 85 | 3.3 |
| Innovation | 65 | 2.5 |
| Distribution and inequality | 44 | 1.7 |
| Organizational choice | 18 | 0.7 |
| Other or unspecified | 678 | 26.2 |
| Total | 2,583 | 100.0 |

*Source: Authors' calculations based on OpenAlex data retrieved on July 27, 2026.*

The most influential studies in the field of NIE, in terms of number of citations, are presented in Table 4.

Table 4 Five most frequently cited unique publications in the literature corpus

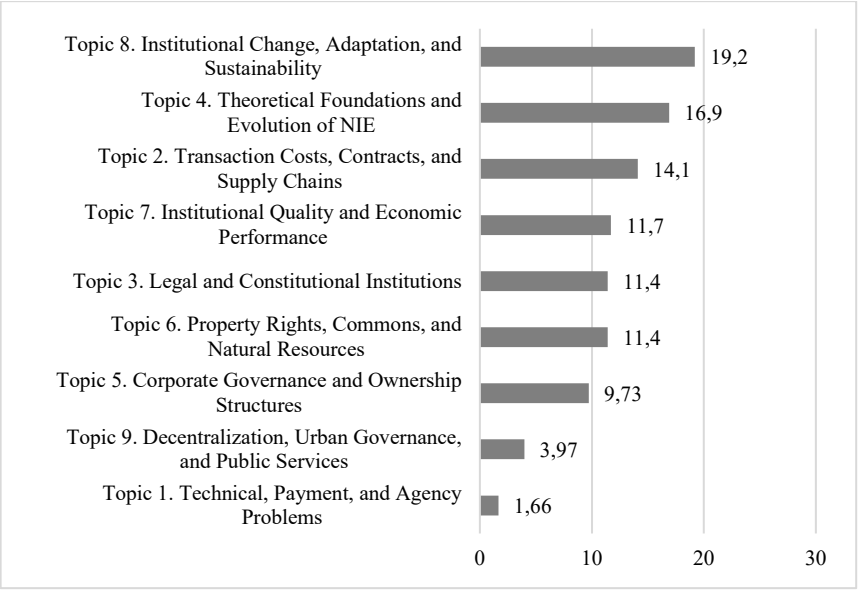
| Rank | Author | Publication | Year | Citations |
|---|---|---|---|---|
| 1 | Douglass C. North | *Institutions, Institutional Change and Economic Performance* | 1990 | 31,256 |
| 2 | Elinor Ostrom | *Governing the Commons: The Evolution of Institutions for Collective Action* | 1990 | 19,189 |
| 3 | Paul Pierson | *Increasing Returns, Path Dependence, and the Study of Politics* | 2000 | 7,758 |
| 4 | Oliver E. Williamson | *The New Institutional Economics: Taking Stock, Looking Ahead* | 2000 | 6,323 |
| 5 | Douglass C. North | *Institutions* | 1991 | 5,062 |

*Source: Authors' calculations based on OpenAlex data retrieved on July 27, 2026.*

Structural topic modelling was also conducted using the *stm* package in R to identify latent themes in publication titles and abstracts (Roberts et al. 2019). The model identified nine important topics: Topic 1. Technical, Payment, and Agency Problems; Topic 2. Transaction Costs, Contracts, and Supply Chains; Topic 3. Legal and Constitutional Institutions; Topic 4. Theoretical Foundations and Evolution of NIE; Topic 5. Corporate Governance and Ownership Structures; Topic 6. Property Rights, Commons, and Natural Resources; Topic 7. Institutional Quality and Economic Performance; Topic 8. Institutional Change, Adaptation,

and Sustainability; Topic 9. Decentralization, Urban Governance, and Public Services. We then estimated the prevalence of each topic across the entire corpus (Figure 2) and evolution over time (Figure 3).

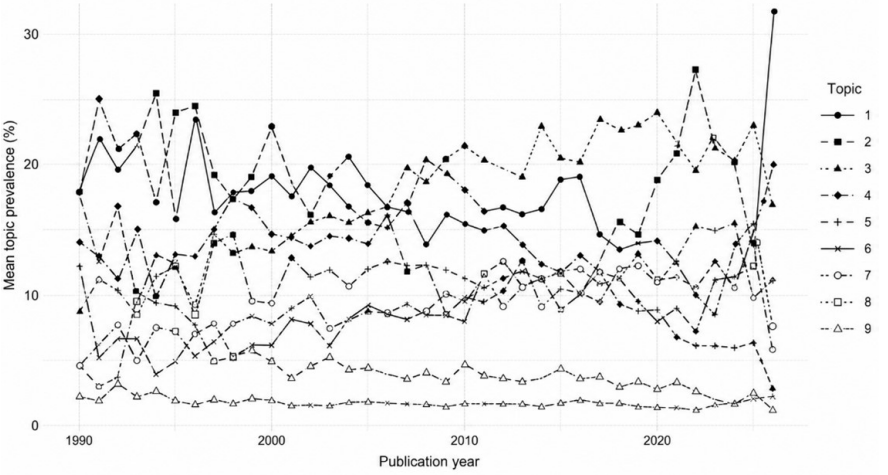
Figure 2 Main structural topics in New Institutional Economics




*Source: Authors' calculations based on OpenAlex data retrieved on July 27, 2026.*

Figure 3 Evolution of New Institutional Economics topics

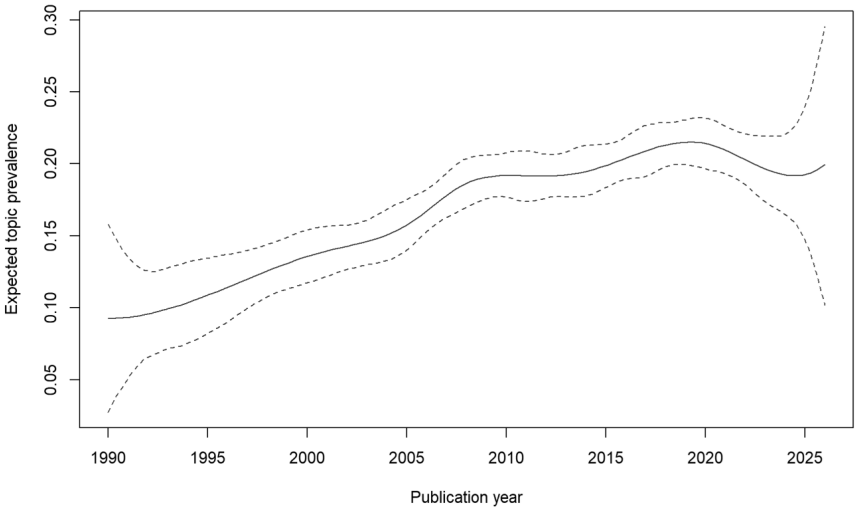
*Annual mean topic prevalence between January 1990 and July 2026*




*Source: Authors' calculations based on OpenAlex data retrieved on July 27, 2026.*

It is also noteworthy to underline the increasing prevalence of Topic 8: Institutional Change, Adaptation, and Sustainability (Figure 4). It might reflect the growing research focus on the role of institutions for sustainable development following the adoption of the United Nations Sustainable Development Goals in 2015, although this observed association merits an investigation on its own.

Figure 4 Change in prevalence of Topic 8 over time




*Source: Authors' calculations based on OpenAlex data retrieved on July 27, 2026.*

In sum, text-processing methods used in the literature review serve only to complement but not to substitute for the qualitative analysis of key ideas and challenges in NIE, a task we pursue in the next sections.

## 3. INSTITUTIONS AND ORGANIZATIONS: CONCEPTUAL FOUNDATIONS

One of the main corollaries of the literature review is that institutions and their evolution exert a decisive long-term influence on the economic performance of societies. "Institutions are the rules of the game in a society or, more formally, the humanly devised constraints that shape human interaction" (North, 1990, p. 3). Additonally, North (1990) introduced an important distinction between institutions and organizations. While institutions refer to formal and informal rules, norms, and enforcement mechanisms that regulate human interaction, organizations consist of groups of individuals who pursue shared objectives. Organizations may be economic (firms, trade unions, cooperatives), political (political parties, regulatory

bodies), or educational (universities, schools, training centers). Hence, if institutions are the rules of the game, organizations are the players (North, 2005).

Ostrom (1990; 2005) defines institutions more broadly, noting that the term is used to denote diverse entities, including organizational forms as well as the rules, norms, and strategies structuring patterns of interaction within and across organizations. She observes that such an inclusive definition generates conceptual ambiguity and complicates the distinction between institutions and organizations. As she emphasizes, one of the central challenges in institutional analysis lies in defining and identifying institutions. Since institutions are fundamentally shared constructs, they reside in the minds of participants, often as tacit rather than explicitly codified knowledge (Ostrom, 2005). Put differently, while the physical structures housing organizations are visible, institutions themselves are often intangible. She illustrates this point with the example of the Banaue Rice Terraces in the Philippines, which have been sustained for over two millennia. To an engineer, these terraces may appear merely as physical constructions. However, they embody a deeply embedded system of property rights and governance rules developed by farmers over generations. In this sense, the terraces materialize the institutional arrangements governing the management of common resources.

The difficulty in distinguishing institutions from organizations is further reinforced by the fact that organizations, as actors in the system, are not only responsible for complying with institutional rules but also contribute to their evolution. Through their practical activities, organizations refine and operationalize general norms, thereby blurring the boundary between the two concepts. A clearer distinction requires recognizing that institutions perform a broader, more universal function. They establish rules, norms, and social structures that guide behavior across domains, effectively providing the framework within which organizations operate. Institutions tend to persist over long periods and across generations, exhibiting greater resilience to change.

These considerations support the existence of institutions alongside their corresponding organizations. For example, law constitutes an institution, while courts represent organizations; property rights form an institution, while judicial bodies enforcing them are organizations; education is an institution, while schools are organizations; transport systems represent institutions, while railways function as organizations. Both institutions and organizations are critical in practice. Effective institutions require not only well-designed formal and informal rules but also efficient organizations that implement and uphold them.

Within NIE, this distinction has led to the emergence of two analytical strands: one focusing on institutions, associated with North, and the other on organizations, associated with Oliver E. Williamson (Ménard and Shirley, 2025). We confine our analysis to the institutional-related strand of the relevant literature.

# 4. THE SCOPE OF INSTITUTIONS

In defining and exploring institutions, it is essential to distinguish between formal and informal institutions. Formal institutions consist of codified rules governing human interaction, including constitutions, laws, and regulations related to politics, governance, and finance. Informal institutions, by contrast, refer to unwritten codes of conduct, social norms, customs, traditions, and moral values. A key criterion for distinguishing between the two lies in the role of the state and the legal system in their enforcement. Formal institutions are enforced through state coercion within national legal systems, primarily by courts. Informal institutions, as a rule, do not require state enforcement. The institutional economics literature consistently emphasizes that informal institutions are not less important than formal ones.

Transition economies illustrate the important difference between the formal adoption of institutions and their effective implementation. Although these countries introduced market-oriented legislation, property rights systems, regulatory institutions, and democratic structures, their effectiveness has often remained. Late-reforming transition economies from the Western Balkans are still constrained by weak administrative capacity, inconsistent enforcement, informal networks, and limited political accountability. Their experience indicates that institutional convergence requires much more than legal harmonization. It also depends on credible enforcement as well as capable and credible public organizations (EBRD, 2003; Fiti, 2004; 2008; Stojkov, 2008; Filipovski and Fiti, 2017; Host et al. 2017; MANU, 2017; Visković and Šeparović, 2017; Stojkov et al., 2024; Podvorica et al. 2025).

Both economic and political institutions are critical for the prosperity of nations. Acemoglu, Robinson, and Johnson (2004; 2021) identify property rights, their enforcement, and market organization as the most important economic institutions for growth and development (Acemoglu et al. 2019). Among political institutions, the form of political authority, democracy versus autocracy, and the constraints imposed on political and economic elites are of central importance. They further distinguish between inclusive and extractive institutions. Inclusive economic institutions secure property rights, ensure contract enforcement, and create incentives for education, saving, investment, and entrepreneurship. They enable broad participation in economic activity and facilitate efficient allocation of talent through markets, while supporting the provision of high-quality public services. Inclusive political institutions allow broad participation in governance, protect the interests of the majority, constrain political power, and prevent the extraction of income and wealth by elites. Conversely, extractive institutions are associated with economic stagnation and decline (Acemoglu and Robinson, 2012).

Another relevant classification is proposed by Rodrik and Subramanian (2003), who identify four types of institutions with strong relevance for economic growth:

- Market-creating institutions: These include institutions that establish and sustain market economies, particularly those related to property rights protection and contract enforcement. They rely on effective judicial systems and courts. Strong rule of law and good governance are essential for a functioning market economy.
- Market-regulating institutions: These encompass institutions responsible for government regulation of market failures. Regulatory agencies in sectors such as energy, telecommunications, transport, environment, and financial services address issues such as monopolies, externalities, and asymmetric information. In such contexts, markets alone fail to allocate resources efficiently, necessitating regulatory intervention.
- Market-stabilizing institutions: These institutions ensure macroeconomic stability, including price stability, mitigation of business cycle fluctuations, and resilience to financial crises. Central banks, fiscal frameworks, and budgetary rules play a key role in this domain.
- Market-legitimizing institutions: These institutions provide social protection, facilitate income redistribution, and mitigate social conflict. They include pension systems, unemployment benefits, and other social safety mechanisms.

As discussed in the next section, the salience of institutions and their relationship with economic prosperity has been extensively examined in the economic literature.

# 5. INSTITUTIONS AND ECONOMIC PROSPERITY

## 5.1. Determinants of Economic Growth and Differences in Levels of Development

Why are some countries rich while others remain poor? Why do some economies achieve sustained growth, while others experience stagnation? What explains persistent disparities in income per capita across countries? These questions lie at the core of growth and development theory. Contemporary economic literature offers several competing explanations. The neo-Keynesian Harrod-Domar model attributes differences in economic performance to variations in savings and capital accumulation, which finance investment (Harrod, 1939; Domar, 1946). The neoclassical growth model of Solow (1956) emphasizes capital, labor, and total factor productivity as the main drivers of growth. Endogenous growth theories, developed by Robert E. Lucas Jr. and Paul Romer, focus on human capital and technological innovation as key determinants (e.g., Romer, 1998).

Another line of explanation is the geography hypothesis, which argues that climate, ecology, and geographic conditions shape technological possibilities and incentives, thereby influencing economic outcomes (e.g., Sachs, 2003). A related perspective is the cultural hypothesis, associated with Max Weber, which

highlights the role of values, beliefs, and work ethics in shaping economic performance (Weber, 1905/2002). A further approach is the ignorance hypothesis, which attributes underdevelopment to poor policy choices and limited understanding among policymakers (Acemoglu and Robinson, 2012).

As Acemoglu and Robinson (2012) argue, these explanations are insufficient to account for large cross-country differences in economic development. They emphasize instead the central role of institutions. Earlier insights by Adam Smith and John Stuart Mill already recognized the importance of institutions, but this perspective gained analytical strength with the emergence of New Institutional Economics.

In this context, North (1990) argues that factors commonly identified as drivers of growth, such as capital accumulation, education, and innovation, are not ultimate causes but manifestations of growth itself. The fundamental cause lies in the quality of institutional arrangements that create incentives for innovation, enable economies of scale, and ensure efficient market functioning.

An integrative perspective, developed by Rodrik and Subramanian (2003), highlights the interaction between institutions, geography, and international trade. Their empirical analysis shows that institutional quality is the only consistently positive and statistically significant determinant of income levels. At the same time, trade can indirectly affect income by improving institutional quality, while geography influences institutions themselves.

The importance of institutions is further emphasized by Allan H. Meltzer, who identifies rule of law, fiscal discipline, openness to trade, and secure property rights as key pillars of economic prosperity (Meltzer, 2003). Similarly, Joseph E. Stiglitz stresses the critical role of legal and regulatory frameworks in ensuring contract enforcement, resolving commercial disputes, maintaining competition, and safeguarding financial stability (Stiglitz, 2002).

As demonstrated in Section 2 conveying the systematic literature review, a vast body of the NIE-related literature (39.0%) explores the relationship between institutional quality and long-term economic growth. Barro (1991) demonstrated a powerful, positive relationship using data from 98 countries. Kaufmann, Kraay and Zoido-Lobaton (1999) provided similar evidence based on a sample of 150 countries. Edison (2003) finds that institutional quality significantly affects income levels, growth rates, growth stability, and the effectiveness of economic policy implementation, particularly in Sub-Saharan Africa. Filip and Setzer (2024), Glawe and Wagner (2025), Dogan (2025) and European Bank for Reconstruction and Development (2003) also underscored the role of institutions for European transition economies.

The evidence from European transition economies also confirms the salience of institutional quality for growth, investment, innovation, and convergence. It does suggest that institutional effects might be conditional and nonlinear, as they depend on the initial level of economic development,

administrative capacity, and complementarity among institutional reforms (Filip and Setzer, 2024; Glawe and Wagner, 2025; Dogan, 2025). The EU integration process of transition economies can support institutional development through legal harmonization, policy conditionality, monitoring, and pre-accession assistance. Yet, formal compliance does not necessarily produce effective institutions, particularly when enforcement capacity and domestic political commitment remain weak (Stojkov, Veljanovski, and Warin, 2024).

By conducting a meta-analysis, Doucouliagos and Ulubaşoğlu (2008) explore the effects of democracy on economic growth on 483 estimates from 84 studies. They do not find a robust direct effect, but identify indirect effects, through human capital, political stability, low inflation rate, and economic freedom. Another study by Efendic, Pugh and Adnett (2011) analyze 40 empirical studies and 112 estimates. Their meta-regression analysis finds strong evidence that institutional quality positively affects output levels, while evidence of its effect on economic growth is less robust. The substantial variation reflects differences in institutional measures, model specifications, and treatment of endogeneity.

Given this heterogeneity, understanding the transmission mechanisms through which institutions influence economic outcomes becomes crucial. The following subsection examines these mechanisms in greater detail.

## 5.2. Transmission Mechanisms Through Which Institutions Affect Growth and Development

Institutional effects often differ across time horizons. In the short term, changes in legal and regulatory arrangements may influence expectations, perceived risk, transaction costs, and business confidence. They may also generate adjustment costs and create uncertainty. Over the medium term, institutional effects typically operate through investment, market entry, foreign direct investment, credit allocation, and administrative performance. Their long-term effects emerge through the cumulative influence of these channels on human capital, innovation, productivity, and structural transformation. Meta-analytical evidence supports these distinctions: Ugur (2014) finds that corruption has stronger adverse effects on growth over longer periods, while Efendic, Pugh, and Adnett (2011) report more robust institutional effects on output levels than on growth rates. Institutional reforms should therefore not be expected to produce an immediate or uniform growth effect.

Proponents of NIE provide robust arguments on the importance of institutional quality, credibility, and effectiveness for dynamics and quality of economic growth. These arguments point to the transmission mechanisms through which institutions shape economic outcomes.

North (1990) demonstrated the fundamental role of institutions through historical analysis. Examining the United States in the nineteenth century, he showed that progress in agriculture, banking, and transport was driven by effective

institutional arrangements. He also argued that strong protection of property rights was a key precondition for the rapid economic growth of England and the Netherlands from the late medieval period to the eighteenth century. In contrast, the absence of institutional innovation contributed to the long-term stagnation of Spain. His work further highlighted the limitations of neoclassical growth theory in identifying the deeper sources of growth, prompting a rethinking of modern macroeconomic frameworks.

According to Acemoglu and Robinson (2012), institutions are fundamental because they: shape incentives for investment in physical capital, human capital, and technology; encourage innovation; improve the allocation of resources toward their most productive uses; influence not only output levels but also the distribution of income, requiring protection of broad segments of society from elite extraction. Their empirical and historical analysis provides strong evidence against geographic determinism. During colonization, European powers implemented different institutional frameworks across regions. In resource-rich colonies, they established extractive institutions that concentrated power and enabled the exploitation of local populations, leaving a legacy of weak institutions and low-income levels. In contrast, in sparsely populated regions such as the United States, Canada, Australia, and New Zealand, settlers replicated European institutional models that protected property rights and constrained elites, laying the foundation for long-term prosperity.

A second key argument is the “reversal of fortune.” Societies that were relatively prosperous in the sixteenth century, such as the Mughal Empire in India or the Inca civilization, are now relatively poor, while regions that were historically less developed, such as North America and Australia, have become among the richest in the world (Acemoglu, Johnson, & Robinson, 2002). This pattern cannot be explained by geography alone but is consistent with differences in institutional development.

The supremacy of institutions is further illustrated by natural experiments such as the divided city of Nogales. Nogales has identical geography and climate on both sides of the border, yet vastly different economic outcomes. The U.S. side benefits from strong institutions, rule of law, and democratic governance, while the Mexican side faces weaker institutions, corruption, and lower living standards. Income per capita is several times higher on the U.S. side, demonstrating the decisive role of institutions.

A similar contrast emerges in the case of the Korean peninsula. South Korea developed a market-based economy with democratic institutions, while North Korea adopted a centrally planned system with weak economic and political institutions. By the early 2020s, income levels in South Korea were estimated to be between 25 and 30 times higher than those in North Korea, reflecting the long-term divergence between inclusive market institutions and centrally planned extractive institutions (e.g., Haggard, Kim and Lee, 2026).

The reviewed literature can be synthesized into four interconnected transmission channels. First, institutions influence incentives and transaction costs through protection of property rights, enforcement of contracts, and predictability of regulation. Second, they affect factor accumulation and technological development by affecting investment in physical capital, human capital, and innovation. Third, institutions influence resource allocation through market organization, corporate governance, public administration, and access to finance. Fourth, they can affect income distribution and political power, which can either reinforce or weaken existing institutional arrangements.

## 5.3. Institutional Change and Persistence

As illustrated in Section 2, a sizeable body of NIE-related literature focused on the institutional changes (15.8%). Douglass C. North devoted substantial attention to the determinants of institutional change and their interaction with economic performance. In his framework, economic and institutional change are mutually reinforcing processes operating under conditions of scarcity and competition. Competitive pressures compel organizations, including firms, to invest continuously in new knowledge and skills to survive. When competition is weak, incentives for such investment, and for institutional change, diminish. Simultaneously, the institutional framework, or institutional matrix, provides the structure of incentives that shapes which types of knowledge and skills are valuable (North, 2025).

North's analysis of the interaction between economic and institutional change is complex and can be synthesized through several key relationships. Competition forces economic actors to invest continuously in knowledge, capabilities, and skills. These investments, primarily in human capital and technology, generate economic change. Economic change, in turn, induces institutional change. At the core of institutional change lies the learning process.The learning system strongly influences beliefs, preferences, and the way individuals perceive reality. Belief systems shape the formation of institutional matrices, defined as the structure of rules, norms, conventions, and beliefs embedded in constitutions, property rights systems, and informal constraints (North, 2025, p. 31).

The institutional matrix feeds back into the system by shaping incentives, which influence the accumulation of knowledge and skills and, ultimately, economic performance. Institutional change is typically incremental, reflecting uncertainty and conflicts of interest among social groups. Although gradual, both institutional and economic changes are continuous. Entrepreneurs seek to improve their competitive position, while political actors attempt to shape institutional arrangements in line with their interests. The dynamic interaction highlights that institutional evolution is path-dependent, driven by learning, incentives, and strategic behavior within a changing economic environment.

A compelling explanation for the slow pace of institutional change is provided by Acemoglu and Robinson (2012), who emphasize conflicts of interest among social groups. Institutions shape the distribution of income not only among individuals but also across groups. Those who benefit from existing arrangements tend to resist reforms.

Consider a setting in which a political elite with weak democratic capacity has captured institutions over a prolonged period. While in power, it holds both de jure and de facto authority and blocks institutional reform. Even after losing formal political power, such an elite may retain de facto influence through economic dominance, especially if wealth was accumulated through privileged or illicit channels. The persistence of power creates strong barriers to institutional transformation.

From this perspective, the linkage between institutions, economic outcomes, and the distribution of power generates what Acemoglu and Robinson describe as a "central mechanism of persistence." This mechanism explains why both economic and political institutions tend to evolve slowly.

While North (1990) focuses on the interaction between economic and institutional change, Acemoglu and Robinson (2012) highlight the interplay between political and economic institutions. Economic institutions determine whether a country achieves prosperity or stagnation, while political institutions determine which economic institutions emerge and persist.

They illustrate this interaction through contrasting examples. In the United States, inclusive political institutions have historically supported inclusive economic institutions. The success of Bill Gates reflects an environment characterized by strong property rights, access to finance, a skilled labor market, and predictable rules. Institutional credibility creates confidence among entrepreneurs that their investments will be protected. Moreover, political institutions ensure stability and constrain the concentration of power, reducing the risk of expropriation.

The same institutional strength is evident in the enforcement of competition policy. In the 1990s, U.S. authorities brought antitrust action against Microsoft under the Sherman Act. The case concluded with a negotiated settlement in 2002, imposing restrictions on business practices. This demonstrates that even the most powerful firms operate within binding institutional constraints.

By contrast, weak institutions in Mexico enabled Carlos Slim to consolidate monopoly power in telecommunications, supported by close ties with political elites (e.g., Arslan, 2025). Barriers to entry and regulatory capture allowed the accumulation of vast wealth at the expense of consumers and competitors.

These examples illustrate why institutional change is difficult. Once established, institutions create vested interests and power structures that resist reform. As a result, inefficient and extractive arrangements can persist for long periods, particularly in less developed economies, and can reinforce cycles of stagnation and inequality.

### 5.4. Critical Assessment of the Reviewed Literature

Even though there is a broad consensus that institutions matter, the reviewed NIE literature contains important conceptual and empirical limitations. Firstly, the concept of institutional quality is multidimensional, as it includes the rule of law, protection of property rights, government effectiveness, regulatory quality, and political accountability. Simply aggregating these dimensions may conceal differences in their mechanisms and economic effects.

Secondly, the empirical research still confronts serious identification problems. The biderectional causality is a case in point. Institutional quality most likely affects the level of economic development, but economic development also provides the resources and political demand required for stronger institutions. The reverse causality complicates attempts to determine the direction and magnitude of institutional effects. Common institutional indicators also rely heavily on expert assessments and perceptions, which may contain biases or measurement errors.

Thirdly, institutional effects appear to be context-specific, as other important factors influence the development outcomes. The same formal institution may produce different outcomes depending on enforcement capacity, informal norms, political incentives, and complementary organizations. A judicial model that functions effectively in Germany may not produce effective outcomes in the Western Balkans. Institutional arrangements that function effectively in advanced European economies may therefore produce weaker results when transferred to European transition countries.

Hence, the NIE literature concentrates heavily on economic growth and development, while giving less attention to distribution, organizational choice, innovation, and the timing of institutional effects. Avenues for future research can better design the distinction among specific institutional dimensions, examine short-, medium-, and long-term effects, and devote greater attention to institutional reversals, transition economies, and implementation capacity.

## 6. THE INFLUENCE OF NEW INSTITUTIONAL ECONOMICS ON ECONOMIC POLICY DESIGN

A structured assessment of the policy relevance of NIE requires attention to three elements: its core theoretical postulates, its position outside the mainstream of modern macroeconomics, and its complementary, rather than competing, relationship with dominant schools of thought.

The central propositions of NIE can be summarized as follows:

Institutions, both economic and political, and their quality, credibility, and effectiveness are fundamental determinants of economic prosperity. In this context, the protection of property rights, contract enforcement, rule of law, good governance, and anti-corruption mechanisms are critical.

Institutions affect economic outcomes through identifiable transmission channels. They shape incentives for investment in physical capital, human capital, and technology, stimulate innovation, improve resource allocation efficiency, and influence both output levels and income distribution. The interaction between institutions, economic growth, and the distribution of economic power generates conflicts of interest among individuals and social groups, leading to a "central mechanism of persistence" and slow institutional change. The development of inclusive institutions reduces transaction costs, which remain a central concern in modern economies.

Economic analysis extends beyond prices and markets to include contracts, contract enforcement, and alternative governance structures. This includes the role of firms as hierarchical organizations alongside markets. The approach is inherently multidisciplinary, integrating insights from political science, law, sociology, anthropology, and evolutionary biology. Economic agents operate under imperfect information and bounded rationality, which increases transaction costs and reinforces the importance of institutional frameworks.

Despite these contributions, NIE remains positioned outside the core of mainstream macroeconomics. The evolution of macroeconomic thought has been dominated by debates between neoclassical and Keynesian traditions, later reflected in the divide between new classical and new Keynesian models. These debates have shaped the primary analytical and policy frameworks used in practice.

However, it is essential to emphasize that NIE does not function as a competing paradigm. Instead, it operates as a complementary approach. While neoclassical and Keynesian frameworks explain short- and medium-term macroeconomic dynamics, New Institutional Economics provides a deeper understanding of the structural determinants of long-term growth and development.

From a policy perspective, this implies that effective economic policymaking cannot rely solely on traditional macroeconomic tools such as fiscal and monetary policy. It must also incorporate institutional design and reform. Policies aimed at improving governance quality, strengthening legal systems, enhancing regulatory effectiveness, and limiting the concentration of economic and political power are essential for sustaining long-term economic prosperity.

In this sense, the contribution of NIE lies not in replacing existing frameworks, but in expanding the analytical foundation of economic policy by embedding it within a broader institutional context.

# 7. CONCLUSION

This paper systematically maps and synthesizes the theoretical and empirical literature on New Institutional Economics (NIE) published between January 1990 and June 2026. The review examines how NIE conceptualizes institutions, distinguishes them from organizations, and explains the mechanisms

through which institutional arrangements may influence economic outcomes. Literature is mainly focused on property rights' protection, contract enforcement, transaction costs, governance structures, political accountability, and the interaction between formal and informal institutions.

The reviewed studies associate institutional quality with investment, innovation, resource allocation, productivity, and economic development. However, the strength and direction of these relationships vary across countries, periods, institutional dimensions, and empirical methods. Measurement limitations, reverse causality problems, institutional complementarities, and differences in enforcement capacity prevent a simple conclusion that institutions alone explain long-run growth or cross-country differences in living standards.

The literature also indicates that institutional change is gradual, path-dependent, and shaped by political and distributional conflict. Formal reforms may produce limited results if administrative capacity is weak, enforcement is inconsistent, or powerful groups resist implementation. This distinction is particularly relevant for the European transition economies, where legal convergence commonly proceeds more rapidly than changes in organizational practices and informal institutions.

These findings support several cautious policy implications. Institutional reform should address the quality of formal rules. Policymakers must focus more on the barriers for enforcement of rules and on the capabilities of implementing organizations. Reform champions must also fully comprehend the political incentives affecting compliance. Reform priorities must reflect country-specific conditions rather than rely on direct institutional transplantation from more advanced economies.

Future research could empirically examine how institutional quality, enforcement capacity, and political concentration interact in shaping economic performance. Attention should be devoted to transitional economies, where formal institutional reforms are frequently hampered by weak administrative capacity and persistent political concentration. Academic studies could also investigate the role that digital governance and artificial intelligence play in institutional effectiveness, as well as the factors that make reform efforts produce enduring effects on economic growth, resilience, and social inclusion. Another important avenue for future research would be to examine the role of reversals in institutional quality (democratic backsliding, institutional erosion, state capture) and their implications for long run economic development. Finally, the NIE literature would benefit from a more comprehensive and updated meta-analytical evidence on the impact of institutions on economic performance, with greater attention to contextual factors.

**Author Contributions:** Conceptualization, T.F. and A.S.; Methodology, T.F.; Validation, T.F.; Formal Analysis, T.F. and A.S.; Investigation, T.F.; Resources, A.S.; Data Curation, A.S.; Writing – Original Draft Preparation, T.F. and A.S.; Writing – Review & Editing, T.F. and A.S; Supervision, T.F.; Project Administration, T.F.

**Funding**: The research presented in the manuscript did not receive any external funding.

**Conflict of interest**: None.

**Acknowledgement of AI or AI-assisted tools use:** We have not used any AI or AI-assisted technologies to prepare this work.

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# INSTITUCIJE KAO TEMELJ EKONOMSKOG PROSPERITETA: UVIDI IZ NOVE INSTITUCIONALNE EKONOMIJE

## *Sažetak*

*U radu se istražuje kako nova institucionalna ekonomija konceptualizira odnos između institucija i dugoročnih ekonomskih rezultata. Oslanjajući se na radove Douglassa Northa, Ronalda Coasea, Olivera Williamsona i kasnijih predstavnika institucionalne ekonomije, provedeno je sustavno mapiranje literature objavljene od siječnja 1990. do lipnja 2026. Pregled se temelji na bibliografskim zapisima iz baze OpenAlex, unaprijed definiranim kriterijima prihvatljivosti, bibliometrijskoj klasifikaciji i strukturnom modeliranju tema radi utvrđivanja glavnih istraživačkih područja i njihova razvoja tijekom vremena. Izdvojena su četiri transmisijska kanala putem kojih institucije mogu utjecati na ekonomske rezultate: poticaji i transakcijski troškovi, akumulacija proizvodnih čimbenika i inovacije, alokacija resursa i upravljanje te raspodjela dohotka i politička moć. Analizirana literatura uglavnom povezuje višu kvalitetu institucija s boljim ekonomskim rezultatima, no snaga i vremenska dinamika tih odnosa ovise o institucionalnim pokazateljima, empirijskim metodama, zemljama i uvjetima provedbe. Rezultati naglašavaju važnost administrativnih kapaciteta, institucionalne komplementarnosti, neformalnih normi i političkih poticaja za djelotvornost formalnih institucionalnih aranžmana.*

***Ključne riječi: institucije, ekonomski rast, kvaliteta institucija, ekonomski razvoj.***

***JEL klasifikacija: B52, O43, O40, D02.***