

RELATIONSHIP  
BETWEEN  
REGIME TYPE  
AND ECONOMIC  
OUTCOMES

A RELATED  
QUESTION: THE  
SIZE OF THE  
STATE AND THE  
GOVERNMENT

# RECITATION 6

## THE VARIABLES WE ARE INTERESTED IN

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- Regime type = Democracy / dictatorship: how are they defined?
  - How would you define them? Is the designation of the leader through elections enough to say we are in a democracy?
  - How they are actually defined:  
using indexes, such as Polity Index or Freedom House index take into account: existence of elections, but also degree of actual electoral competition, openness of leader's recruitment, existence of an opposition, degree of political participation, civil liberties, etc.  
Democracy index 2011 (The Economist): "Free and fair elections and civil liberties are necessary conditions for democracy, but they are unlikely to be sufficient for a full and consolidated democracy if unaccompanied by transparent and at least minimally efficient government, sufficient political participation and a supportive democratic political culture."

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- Economic outcomes: which outcomes do we take into account?
  - Growth
  - Variance of growth ( $\sim$  riskiness)
  - Poverty / inequalities? - we have seen this in the model, but not in empirical papers

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Figure 1

# 1ST DIRECTION OF CAUSALITY: REGIME TYPE → ECONOMIC OUTCOMES

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- What are the main findings? What are the underlying mechanisms? Which identification strategies used?
- 1st outcome: Level of growth
  - AJR, settlers: democracy, including protection of property rights → growth
- 2nd outcome: Variance of growth:
  - higher variance of growth rates under autocracy than under democracy
  - why?
    - good and bad leaders matter more in autocracies; good dictator / autocratic system can impose the politically difficult policies (cf. China today).  
Jones and Olken - deaths in leaders while in office but then: why are some leaders better than others? It depends on expected tenure time (Olson 1993): if longer, invest in public goods that increase productivity and yields in 2nd period; if shorter, tax everything in 1st period. How can we identify this impact? (Papa 2012)
    - democracy is better than autocracy to reduce variance from shocks outside the political system (Easterly 2011)

## 2ND DIRECTION OF CAUSALITY: ECONOMIC SITUATION $\rightarrow$ REGIME CHANGE / TYPE

RELATIONSHIP BETWEEN REGIME TYPE AND ECONOMIC OUTCOMES

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- What are the main findings? What are the underlying mechanisms? Which identification strategies used?
- Possible mechanisms: suppose initial autocracy; remember model seen in class; democracy can happen in 2 cases
  - after revolution: we didn't call it democracy, but that's the idea
    - happens if  $\mu$  (amount due to do a revolution) becomes smaller and autocrat can't commit to redistribution in the second period
    - $\mu$  can get smaller due to specific circumstances (cf. recent Arab revolutions) or because income has grown
  - controlled democratization:
    - if  $\mu$  gets smaller, autocrat wants to be able to commit to do some redistribution
    - controlled democratization is a way to commit
  - in both cases : income growth  $\rightarrow$  reduction of relative  $\mu \rightarrow$  revolution or controlled democratization

## 2ND DIRECTION OF CAUSALITY: ECONOMIC SITUATION → REGIME CHANGE / TYPE

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- Another mechanism for income growth → revolution → democratization:
  - Tocqueville, *The Old regime and the Revolution*
  - French revolution did not happen in the most backward state; on the contrary, equalization of conditions had started
  - economic situation improves → privileges of the nobles perceived as less acceptable and less obvious because were contradicting underlying movement → freedom
  - in short: taste of some equality created desire for more
  - cf. Tunisia today?
  
- Empirical Evidence:
  - AJRYared, Income and democracy: use *changes* in income and changes in democracy
  - no statistically significant relationship

# MILTON FRIEDMAN'S ARGUMENT: FROM THE TYPE OF REGIME TO ITS SIZE

- Great book: Capitalism and freedom
- Same question: relationship between economic and political freedom?
  - economic freedom = free market = absence of barriers put by the government on economic choices: choice of health care or retirement plan; license necessary to get certain jobs; quotas to international trade; minimum price
  - political freedom = being free to go wherever one wants, characteristic of democracies
- Theory:
  - economic freedom is itself a component of freedom (cf. indexes for democracy)
  - economic freedom → political freedom
  - mechanism: economic freedom → dispersion of power, separation between economic and political power → political freedom

# MILTON FRIEDMAN'S ARGUMENT: FROM THE TYPE OF REGIME TO ITS SIZE

- For Friedman, political freedom depends on both regime type **and size of the government**
  - too big government decreases economic freedom and political freedom
  - BUT: necessary function of the government: protection of nation against war and of economic freedom → tension

# HOW DO WE GET SUFFICIENTLY BIG GOVERNMENT IN THE FIRST PLACE?

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- Beyond regime type, there is the question of state and government size
- If regime matters, it is because state and government are sufficiently big
- How do they become big?

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- How does state become big?    how can state collect taxes?
- Fundamental positive role of war
  - war favored state formation in Europe: it required the creation of centralized and efficient structures to collect taxes; these structures didn't disappear when war ended
- Things can be a little more complex:
  - What about Africa? Interstate vs. intrastate war
  - prerequisites for institutional development aided by war (cf. failed development of states in Latin America)
    - state must be forced to turn inward in order to meet the financial challenges of war
    - Adequate administrative mechanisms must be in place to manage the explosion in revenues and expenditures
    - The central state must have already established sovereignty over its territory and must be supported by enough local actors (which see war as the best means with which to defend and reproduce their privileges) as to make domestic extraction profitable

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