

# The welfare advantage of democracy: Evidence, theory and anomalies

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## *1. Evidence: Democracy's welfare advantage*

If measured by per capita income or by multidimensional indices such as the Human Development Index, wealthy countries are on average more democratically governed. This is the case if we define democratic countries as countries whose political regime is characterised by the existence of inclusive political competition through free and fair elections of government and parliament, freedom of opinion and a free press as well as freedom of association (Dahl 1971). The above-mentioned finding holds even under more nuanced conditions, when the degree of democracy of a country is measured by independent democracy indices such as the Freedom House Index, the Bertelsmann Transformation Index or the Varieties-of-Democracy-Index. All depict positive correlations between the level of democracy and societal welfare.

Yet, correlation is not causation, and thus it is not of much surprise that academics have been discussing intensively the direction of causality between societal wealth and political order. In other words, is it democracy that follows socioeconomic wealth as supporters of traditional modernisation theory have proposed? Or is it democracy that outperforms autocracies in welfare terms due to advantages of the outlined democratic arrangements?

Today, the evidence has shifted strongly towards the second hypothesis. In the last two decades, a variety of studies – many of them based on more refined econometric methods for cross-country analyses that better

cope with problems of reverse causality as well as experimental case study research – leave little doubt on the direction of causality. The overarching majority of results points into the direction of a democracy dividend (e.g. Doucouliagos & Ulubaşoğlu 2008). By controlling for many context variables, research shows that increasing levels of democracy tend to produce higher levels of economic growth (Acemoglu et al 2019), economic productivity, health, nutrition and other measures of economic prosperity and social well-being. Higher levels of democracy also lead to lower levels of mortality by natural catastrophes and pandemics and come along with a lower level of famine (McMann & Tisch 2021). Even in comparatively poor countries, democracy outperforms authoritarian regimes. Thus, while there is of course evidence that autocratic regimes might also provoke periods of socioeconomic growth and well-being, the systemic comparison of political regimes shows that democracies outperform autocracies.

Moreover, the evidence assembled so far even tends to underestimate the democracy advantage. This is because authoritarian governments have more space for cheating about their socioeconomic performance. Democratically governed societies are equipped with free media and independent research. Therefore, it will be much harder for governments in democratic settings to lie systematically about their economic performance for legitimation gains. In contrast, such constraints do not exist in authoritarian regimes, where independence of media and research is not given and leaders have much more opportunities to manipulate data about socioeconomic and environmental policy performance. For instance, cross-country studies do not only find that authoritarian regimes systematically report less economic data to international organisations. The comparison between a) official statistics and b) more objective data such as geocoded, satellite-based growth data reveals that authoritarian regimes tend to report overestimated data about their economic performance (Magee & Doces 2015).

## 2. *Theory: Explaining the democracy dividend*

However, those empirical findings are in need of convincing theoretical arguments, particularly in times where many established democracies in Europe and North America face serious threats and some of the most promising emerging democracies in Eastern Europe, Latin America and Africa have had to face a backslide to authoritarianism.

Since the path breaking work of Mancur Olson (1993), theories around a democracy dividend focus on the different incentives of authoritarian

respectively democratic regimes when it comes to the provision of public goods necessary for sustained prosperity of a society. In this regard, the main argument departs from the not far-fetched idea that political leaders and their political associations or closest allies are self-interested and like to stay in power.

If settled and equipped with the necessary power, political leaders will not only be able to tax the population. They will also define informal and formal regulations according to their interests and those on whom their political survival depends. The amount of taxes and the rules and regulations in turn will define how state resources are spent and how the production of public as well as private goods is institutionally shaped. Thus, a government and its distribution coalition heavily influences public good provision in all relevant policy fields such as education, health, economic, judicial, trade or environmental protection.

The constraints faced by democratic regimes compared to autocratic ones make them use their power to provide a mix of private and public goods that tends to serve better the comprehensive interests of a society. Democratic regimes will invest more in non-excludable public goods that benefit the broader population because they rely on the support of majorities. Under the constraint of inclusive electoral competition and the incapability to suppress a free press, political associations and innovative debates around solutions for pressing policy challenges by civil society, democratic governments face strong incentives to invest more in public good provision than autocratic regimes.

In contrast, in an authoritarian setting, where government suppresses fair elections, free media and political associations, there is much less need to respond to the interests of an encompassing majority of the population. Instead, authoritarian governments have much larger degrees of freedom to distribute private goods in form of privileges to themselves and their comparatively narrow group of allies in turn for their loyalty. The formal regulation of monopolies and cartels as well as organised cronyism and corruption are well-known instruments to distribute privileges in turn for political support in narrow distribution coalitions (Faust 2007).

As neither an independent press nor independent judiciary nor an organised opposition can effectively counterbalance such self-interested rentier behaviour, authoritarian regimes in comparison to democratic regimes will not only suffer from productivity losses due to collectively inefficient economic regulation. They will also invest less money and regulatory effort for creating social and environmental public goods, which are beneficial for encompassing majorities, such as an inclusive education and health system or clean water or air.

Moreover, authoritarian regimes are threatened by an endogenous instability problem which aggravates the problem of public good provision explained above. As authoritarian regimes by the means of repression have access to a comparatively high amount of privileges, they face a more serious potential threat of being overthrown: be it by a rebellion of the masses or a clever coup d'état by a rival group. In contrast, the succession mechanism in democracies works by stabilising an incentive scheme that favours public-good oriented behaviour because even the electoral victory of an opponent again has to be based on an encompassing majority. Therefore, the endogenous instability or uncertainty of authoritarian leaders and their narrow coalition will reduce the time horizon under which they will use their discretionary powers to maximise their rent extraction. Authoritarian regimes will not only show irrational collective behaviour because of their ability to serve a narrow coalition but also due to their expectation of a comparatively short time horizon.

### *3. Anomalies: Attractive autocracies and the globalisation paradox*

The logic of a democratic welfare dividend explains the empirical evidence that democracies on average outperform autocracies in most indicators of social, economic and environmental well-being. However, two empirical puzzles merit further attention, namely surprisingly successful autocracies and the potential decline of the democracy advantage in times of globalisation.

As numerous examples have illustrated in history, the vast majority of autocracies has been enriching small elite circles and bringing misery and violence to the majority of its population. A few other small and authoritarian regimes have been based on natural resource abundance and could afford to distribute an important legitimacy-enhancing amount of resources among the population, while at the same time installing an impressive repression apparatus. All these cases are in accordance with the outlined theoretical arguments as the overall welfare performance of such regimes has been poor or mediocre at best.

More interesting are therefore autocracies such as contemporary China and 20<sup>th</sup> century Mexico, which are large and less resource-rich but have witnessed longer periods of economic success. These autocracies were able to counter their authoritarian disadvantages by increasing their support base through authoritarian corporatism and/or by temporarily solving the succession challenge.

Perhaps the most illustrative example is Mexico. Throughout several decades of the past century, the Mexican authoritarian regime was not only based on a highly institutionalised corporatist party structure that organised political influence by many societal interest groups, thereby broadening the political distribution coalition. Moreover, it also institutionalised a succession mechanism that gave the president only one term in office while at the same time allowing him to select his successor. As long as inclusive corporatism and the particular succession mechanism remained in place, the country experienced a period of socioeconomic modernisation. Chinese authoritarianism from the 1990s until recently had similar features, causing rapid modernisation from a very low starting point. An authoritarian but corporatist party structure and some federal arrangements broadened the distribution of the regime, and the party's leadership was capable to install a stable succession mechanism. With the centralisation of power during the last years, however, those mechanisms have vanished. Thus, like in the Mexican case at the end of its economic "miracle", China is currently confronted with autocratic sclerosis that most probably will weaken its socioeconomic performance.

Both examples show that under specific circumstances authoritarian regimes may be capable of copying some of the institutional advantages of democracy to a certain extent. However, authoritarian corporatism and institutionalised succession mechanisms are often not flexible enough to respond to the consequences of societal modernisation and are vulnerable to attempts of elite groups or single leaders to narrow the broadened distribution coalition for their own interest.

The second anomaly is related to the potential threat of globalisation to the democratic dividend. For many citizens in existing democracies, both the disappointment with the functioning of democracy and the discontent with socioeconomic (and environmental) performance have increased. While public good provision is often perceived as unsatisfactory, the level of inequality of income and wealth distribution has been rising within many democracies as did the share of the population reaping high incomes from both labour and capital. Economic elites have become increasingly autonomous from the rest of society and their closeness to political elites has been increasing, thereby threatening democratic mechanisms and favouring narrow distribution coalitions.

One explanation for this phenomenon is the globalisation paradox, formulated by Dani Rodrik (2011). The paradox consists of the impossibility to achieve economic globalisation, national sovereignty and democracy at the same time. Beyond the many virtues of globalisation, global markets – just like national markets – need to be regulated to avoid uncontested

cartelisation and monopolisation or negative externalities. However, as is discussed most prominently for the financial sphere, global markets currently often lack the necessary regulatory underpinnings to avoid these market failures and are not sufficiently legitimised by democratic arrangements. One positive example is the European Union. Here, the construction of – some say: not yet complete – democratic governance mechanisms at the supranational level has accompanied the establishment of a broader European market. In many globalised markets this is not the case, and little or no democratic control mechanisms constrain the decisions of those who manage global affairs: be it in the realm of international organisations or of private business.

Consequently, the congruence between the jurisdiction of national democratic arrangements and the geographic scope of markets that are in need of public-good-oriented regulation has eroded substantially. If national citizenries or their democratically elected parliaments and governments are simply not capable to take impactful decisions over pressing policy issues because those decisions are made outside their jurisdictions, the previously explained virtues of democracy will have little effect. Instead, rather narrow policy coalitions can be built outside the democratic jurisdiction and will shape markets with the usual and negative consequences for encompassing majorities. As Rodrik (2011) argues, if we do not want to waive the virtues of democratic government for encompassing majorities, we will have to choose between less globalisation and a substantial democratisation of global governance mechanisms. In any case, we will only be able to secure prosperity for the population at large – whether at local or at global level – if we construct and preserve polities which serve the collective interest through political rights and civil liberties congruent with the basic features of democratic governance.

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