The Economic Effects of Political Institutions

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Introduction

Political Institutions are enduring practices or organisations with an explicitly political orientation that encompass the constitutional elements of a polity[1]. It is widely claimed that **Democracy** (Fig.1), **Political Rights** and **Civil Liberties** have an impact on the economic development of countries. Objective Political Institutions such as the **Electoral Rules** (Fig.2) employed in translating votes into seats in Parliaments -Majority Rules, Proportional Representation and Mixed Systems- could influence economic policies and ultimately economic growth. Political Institutions vary across countries and they might be one of the reasons why there is an uneven level of economic performance across and within different regions around the world. The extant literature on these caveats is still inconclusive, motivating my academic interest in solving them.

Objectives

This doctoral thesis aims at uncovering the effects that Political Institutions exert on the economic performance of countries by tackling these three unsolved questions:

- Have Political Institutions the same effect on the different industries of an economy?
- What are the economic aftermaths of Electoral Rules?
- Which is the kind of Political Institutions that promote inequality? (Under construction)

Methodology

Placed in the empirical strand of the **Political Economy** literature, this thesis pleads for the **New Institutional Economics'** propositions [2]: Institutions do matter! and the economic theory provides suitable tools to the study of institutions and its economic aftermath. I combine theoretical foundations with statistical analyses, such as **panel data models** which include temporal, cross and within-country information.
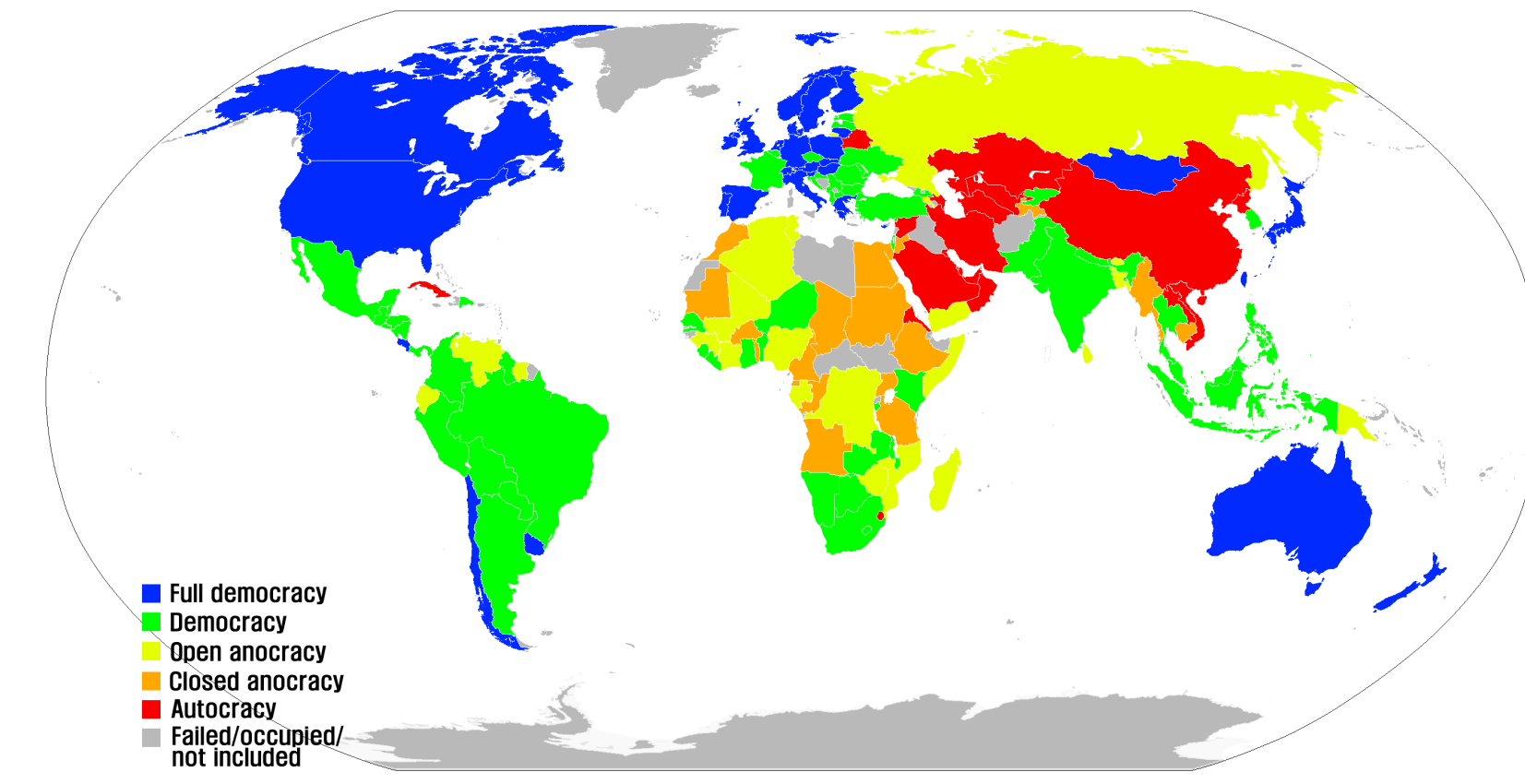

Figure 1: Democracy in the World 2013 (Polity IV Project)

1st Hypothesis

Higher levels of Democracy, Political Rights and Civil Liberties are widely associated with higher economic competition and innovation. The ultimate effect of these institutional changes might be growth-enhancing only for those industries that are **technologically advanced**.
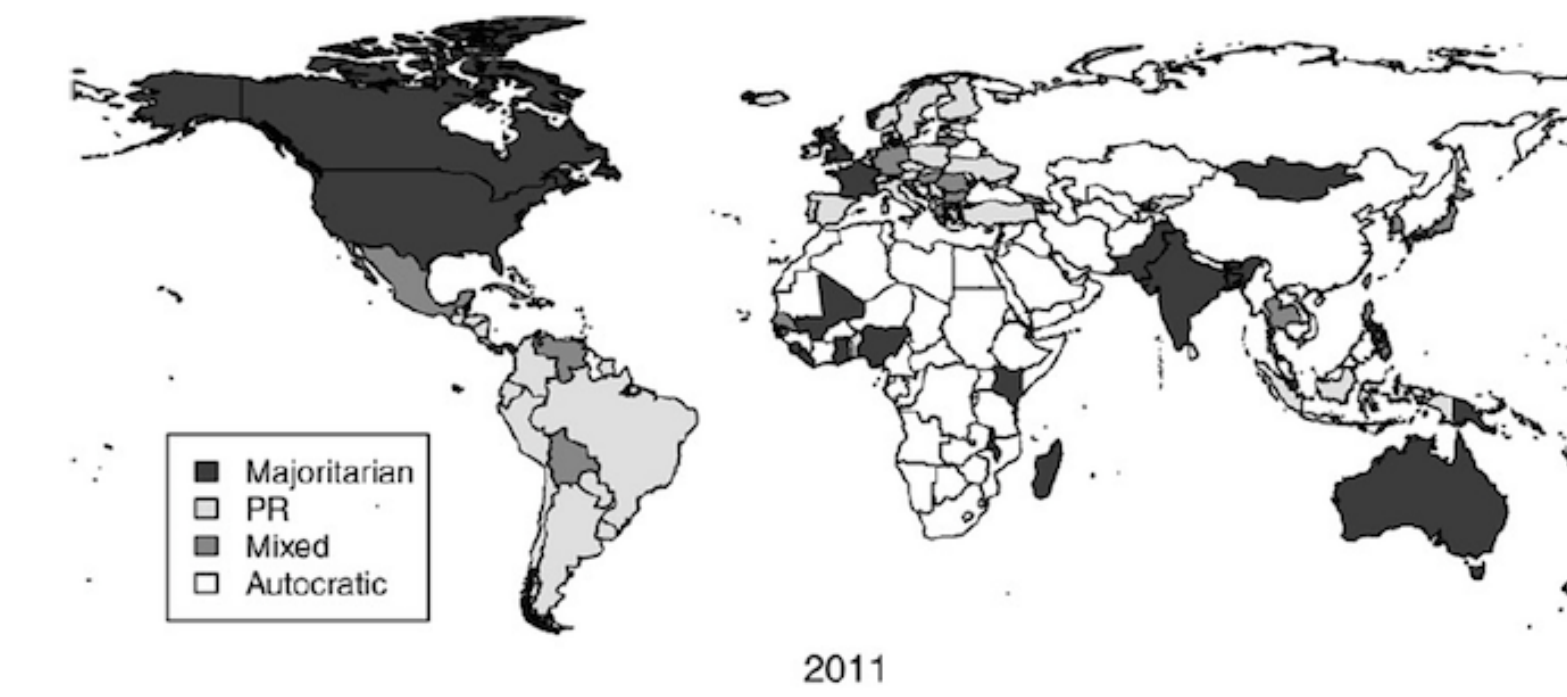

Figure 2: Electoral Rules around the World (Bormann & Golder, 2013)

2nd Hypothesis

Since they need less percentage of the vote share to win the elections, Majority Rules politicians might promote certain **special interest groups** -such as big industries- instead of engaging in more general public projects -health, education or casework projects.

Main Findings

- Changes towards freer, more democratic Political Institutions have a positive effect on technologically advanced industries, but reduce growth rates of backward industries.
- Majority Rules systems favor those manufacturing industries that employ a large number of workers. The differential effect of the three Electoral Rules systems is blurred in large countries.

Econometric Growth Models

Employing information on 100 countries and 61 manufacturing industries over the 1990-2010, I specify econometric growth models to study the effect of Political Institutions (PI_{ct}) and Electoral Rules (ER_{ct}) on growth rates of industries (G_{ict}). I use the Polity2 index for Democracy (PolityIV Project) and the Political Rights and Civil Liberties indeces (Freedom House), and control for different levels of socio-economic development as well as geodemographic factors that vary over time (X_{ict}).

❶ Dynamic growth model

$$G_{ict} = \beta_0 + \beta_1 G_{ic,t-1} \beta_2 Tch_{ict} + \beta_3 PI_{ct} + \beta_4 Tch_{ict} * PI_{ct} + X_{ict}\beta_j + u_{ict} \quad (1)$$

❷ Random and Fixed-effects model

$$G_{ict} = \beta_0 + \beta_1 Emp_{ict} + \beta_2 ER_{ct} + \beta_3 Emp_{ict} * ER_{ct} + X_{ict}\beta_j + u_{ict} \quad (2)$$
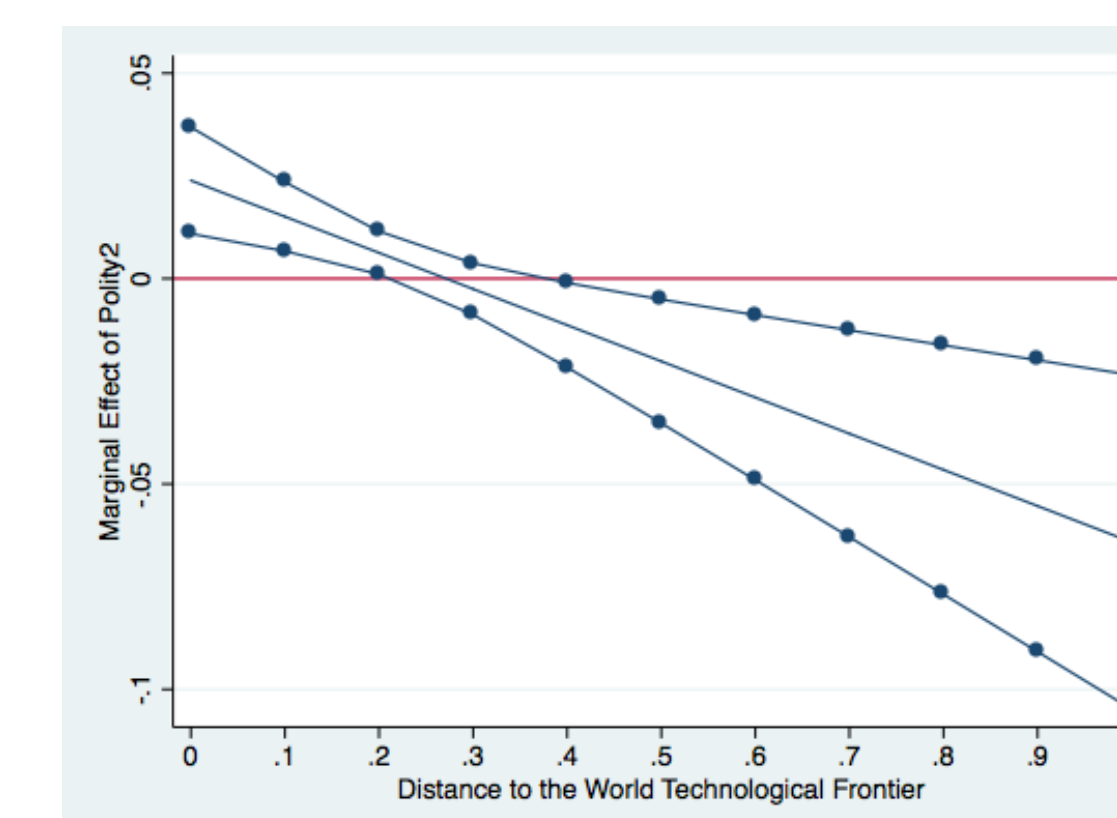
Results

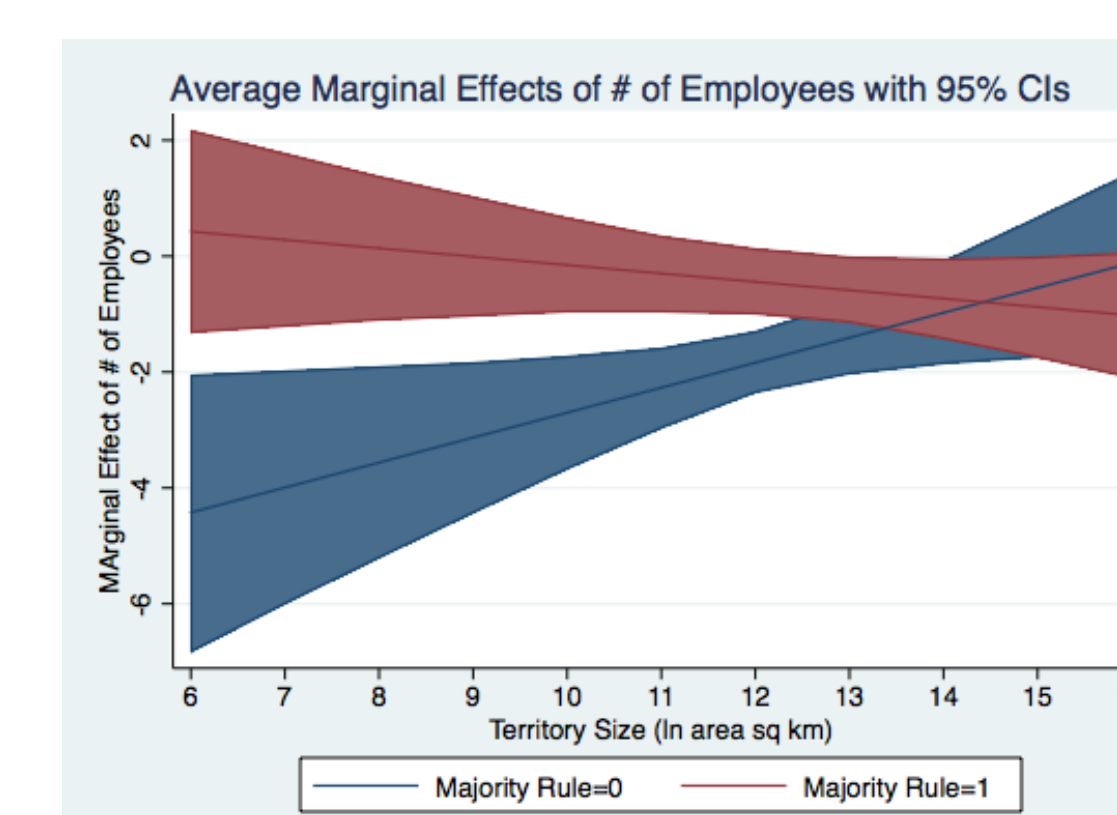Figure 3: Dynamic Polity2 effects depend on Technology

Figure 4: Differential effects under Electoral Rules

Conclusion

Certain industrial characteristics seem to play a crucial role in the economic aftermath of Political Institutions. Using more suitable econometric techniques than previous attempts to study the differential effect of Political Institutions[3], I find that higher levels of democracy favor technologically advanced industries. However, backward industries are harmed by higher democracy levels. Majoritarian electoral rules seem to promote those industries that gather a great part of the workers in manufacturing industries. However, other industries do not benefit from this electoral institution. Consistently with extant findings [4], my results suggest that majority rule politicians might be more responsive to cater special interest groups at the expense of the general public.

References

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Acknowledgements

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