Special
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Is Democracy Compatible with a Competitive Economy?

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Despite several examples of authoritarian countries that have developed rapidly, with current China being a prominent one, decades of systematic research suggest that democracy does not hurt economic growth or other indicators of national economic competitiveness. To the contrary, the best available evidence suggests that democracy may come with several advantages, also for the economy.

Democracy's virtues in terms of ensuring political and civil liberties and broad popular participation in politics are widely acknowledged. When asked in surveys such as the World Values Survey, large shares of citizens in countries from across the world say that they value democracy and prefer it to alternative regime types such as military rule. While it is true that the world has become less democratic in recent years, it is also true that even countries that are clearly autocratic try to emulate certain democratic features such as multiparty legislatures and elections (though without holding truly competitive such elections). They likely do so, in part, to reap some of the legitimacy benefits that democracies enjoy. If political regime types were to compete in a global popularity contest, democracy would win.

An Authoritarian Advantage?

Despite its virtues and popularity, many citizens, policy makers, and even academics remain doubtful that democracy is the superior regime type in all important respects. One especially persistent notion is that democracy may come with significant economic costs. According to this notion, political freedom and competitive elections may lead to slower development and hamper the competitiveness of the national economy.

Different arguments support this notion. Some arguments, for instance, highlight that more authoritarian regimes – where governments do not have to worry about re-election over the next few years – can more freely pursue longer-term developmental policies such as promoting private and public savings over consumption. Another argument is that more autonomous authoritarian regimes can push through painful, but efficiency-enhancing economic reforms without being slowed down by entrenched interest groups or skeptical and perhaps ill-informed citizens. Similarly, authoritarian leaders can respond more quickly and effectively to sudden, large-scale crises (such as a pandemic or a global recession) that require action. They can even do so without being bound by considerations of how popular their policy responses are and without being held up by legislatures dominated by opposition politicians or politically independent judiciaries worried about the constitutionality of the new measures meant to fight the crisis. While democracies are often stuck in endless debates and cumbersome consensus-seeking, the argument goes, authoritarianism allows for effective and forceful policymaking, and this has important downstream benefits for the economy.

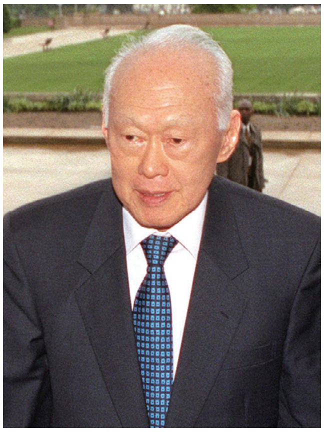
As I have detailed elsewhere, these arguments rest on very strong assumptions that do not necessarily hold up in practice (at least in most countries), and a series of alternative arguments point to other and important economic benefits of democracy. The theoretical case for an authoritarian advantage in generating economic development is not particularly strong.

Yet, the cases made for the economic benefits of authoritarianism have seldom been merely theoretical in nature. Advocates have typically pointed to the experiences of specific authoritarian countries that have displayed rapid economic development over some period of time as evidence. The country examples have shifted over time – in the 1930s, Adolf Hitler's Germany was a prominent one and in the 1950s Josef Stalin's Soviet Union was often invoked – but the inferences drawn from these examples have been similar: the type of policies and outcomes experienced in this country – be it the rapid building of the Autobahn in Germany or fast industrialization and massive capital investments in the Soviet Union – would not have been possible under democracy. Ergo, authoritarianism has an edge over democracy when it comes to improving economic competitiveness and development.

The Lee Thesis & Its Problems

This notion has been particularly powerful in East and Southeast Asia, as several of the most rapidly developing autocracies in the world, at least over the last few decades, have been located in these regions. Since the 1990s, China – a large economy with a very rapid industrialization and growth rate under one-party rule – has been the most visible example. In prior decades (when the Chinese economy remained stagnant and prone to crises), pre-democratic South Korea and Taiwan were regularly invoked as examples of how authoritarian governments fostered (export-driven) industrialization and high growth. Indeed, the notion that an authoritarian regime is required for ensuring economic development is often referred to as the Lee Thesis, named after Lee Kuan Yew, the long-time leader of the authoritarian country with the perhaps most impressive economic success story of them all, Singapore *(Photo 1)*.

Photo 1: Wikimedia Commons



Former Singapore Prime Minister Lee Kuan Yew, originator of the Lee Thesis.

Despite the impressive development of the Singaporean economy, and the more recent growth of the Chinese one, the Lee Thesis as a general proposition does not hold up to closer scrutiny, be it globally or when considering Asia more specifically. There are many important reasons to avoid jumping to general conclusions from observing impressive economic development in a handful of authoritarian countries.

First, there are many other relevant aspects of, say, China's situation that may explain why it has developed so fast over the last few decades than the autocratic character of its political system. For example, China started out far poorer than, say, democratic Japan or France, and poorer economies have much more room to grow fast over a limited period of time than richer ones. Second, many democracies also display impressive patterns of economic development. Take, for example, the previous posterchildren of authoritarian growth, namely Taiwan and South Korea, which have continued their impressive development also after democratization. Third, for every Singapore, there are several Cambodias or North Koreas (or Chinas under Mao, for that matter) – that is, autocratic countries that are mired in poverty and have displayed stagnant economies for decades.

These points indicate that if we are to draw any lessons about the relationship between regime type and economic performance, we need to incorporate much more of the available evidence that history offers us, from across different countries and time periods. And we must try to make systematic comparisons that account for other relevant factors that might explain differences in economic performance across democracies and autocracies. This is exactly what economists, political scientists and other researchers studying the relationships between democracy and different economic outcomes have done and continue to do, and the results from this research literature are typically not in line with the Lee Thesis.

From Anecdotes to Systematic Analysis

Let me start with the relationship between democracy and economic growth, typically measured as percentage growth in GDP per capita. This is the most studied outcome in the broader literature on the economic effects of democracy, with hundreds of statistical and other analyses dedicated to the topic. What can we learn from this body of research?

Depending on factors such as what countries and time periods are included, what type of statistical analysis is used, and how democracy is measured, studies on this particular relationship typically arrive at one of two conclusions. The first one is that there is insufficient evidence to conclude that democracy and autocracy produce different growth rates. The second conclusion is that democracy, on average, leads to higher economic growth than autocracy. Indeed, a larger number of the more recent studies, which draw on more data and typically use more careful research designs than older studies, tend to favor the latter conclusion.

Hence, when summarizing the state of the wider research literature today, the most plausible answer seems to be that democracy typically enhances economic growth, although there is ample uncertainty about exactly how strong and robust the relationship is. At the very least, there does not seem to be a clear trade-off between democracy and economic growth, as suggested by the Lee Thesis. And it is worth noting that this conclusion can be drawn even from studies that do not account for the fact that many autocracies inflate their GDP growth statistics – once this latter pattern is accounted for, the evidence for a democratic growth advantage turns even clearer.

How Autocracy Can Be Really Bad for the Economy

Yet systematic analyses of political regime type and economic growth point to further advantages of democracy, also when looking beyond the "typical relationship". Not only do democracies have systematically higher average growth rates, on average, but they are also much better at avoiding economic crises and have more stable growth over time. While some authoritarian countries perform well economically over limited periods of time, they are also much more likely to experience periods of economic decline, for example as a result of conflict, self-interested and corrupt leaders who prey on the country's resources to their own private benefit, or stunningly misguided economic policies that would never have been accepted by voters in a democracy.

Some types of autocracies, such as personalist autocracies and military regimes, tend to perform worse than other types of autocracies, such as dominant party regimes, but the higher volatility of growth rates and tendency towards crises can be found in autocracies across the board. Some of this is due to the inherently larger importance of individual leaders and leader successions in autocracies (compared to in democracies) for economic outcomes. Some leaders are simply worse at steering the economy than others, and they do more damage in autocracies than in democracies, where leaders have more limited power.

However, autocratic regimes, according to recent research, also display more volatile economic performance within leadership tenures than democracies do. Whenever the international or domestic context shifts and an autocratic leader is faced with different trade-offs between pursuing sound economic policy and his own self-interest (typically related to prolonging his own tenure in power and the welfare of a smaller group of supporters), the autocrat's self-interest typically wins out and this often leads to a quite large shift in policies. Autocrats who have presided over developing economies may thus initiate bouts of intensive repression that stifle investment and creativity or start destructive wars if they perceive that this is to their own benefit, even when the economy craters as a result.

Indeed, the association between autocracy and disastrous economic performances is very clear and robust, and well documented in several studies. As political scientist Adam Przeworski and his co-authors highlighted in a seminal book written more than two decades ago, autocracies dominate the lists of countries with the worst economic performances in different periods of time. As I show in a recent study, this trend has continued also over the last few decades. If you want to minimize the chances of experiencing a contracting economy, democracy is a good prescription.

Short-Term vs Long-Term Gains in Competitiveness

Yet there are recent and systematic studies which suggest that autocracies may have certain predispositions that could create economic, competitive advantages over democracies, at least in some sectors. Notably, several authoritarian countries have amassed very high savings and investment rates, often off the back of policies that were aimed at curtailing different types of public or private consumption. (Such polices would likely be very unpopular and politically dangerous to pursue for democratic leaders facing re-election.) Related to this, autocracies may have advantages when it comes to pushing through massive infrastructure projects. This is because they can more easily ignore those groups who lose out from these projects and they are less sensitive to spending taxpayers' money on, say, expensive and large electrification projects, excessively tall skyscrapers, long bridges, or fancy airports. Hence, John Gerring, Haakon Gjerløw and I, in a recent study, found that autocracies, all else being equal, invest more in industrial infrastructure and generate more rapid industrialization than democracies (even though this does not necessarily transform into higher economic growth) *(Photo 2)*.

Hence, there are some reasons to believe that autocracies could enhance competitiveness, at least in certain industrial sectors and over the medium term, through pushing through large-scale infrastructure projects and amassing savings and capital investments. However, some of this authoritarian investment advantage from higher savings rates and access to domestic capital is offset by democracies, generally, being better at attracting more foreign investment. This is likely, at least in part, to be a consequence of more stable and friendly regulatory environments and better protection of property rights, which reduces risks and increases expected profits for foreign investors. In fact, among all studies published in English-language journals from 2000 and 2020, more studies find that democracy increases rather than decreases physical capital investment overall, although the pattern of findings is mixed. One plausible conclusion is thus that the domestic savings advantage that autocracies might have is (at least) outweighed by other advantages that democracies have in terms of spurring capital investment.

More generally, any national competitive advantages that autocracies may have are likely dominated by such advantages that democracies have. This goes, in particular, for knowledge-intensive sectors, and especially if we consider advantages that are likely to accumulate over the longer term. For example, democracies are generally much better at accumulating "human capital", that is, building up a skilled and effective workforce. This is because democracies tend to provide more education to larger parts of their populations, and democracies are also better at providing their citizens with other important public services such as healthcare. Workers in democracies are not only better paid than their counterparts in autocracies, they are also, on average, healthier, better educated, and (as a consequence) more productive *(Photo 3)*.

Finally, and even more importantly for long-term growth, democracies provide friendlier environments for entrepreneurs, firms, and other economic actors for developing and learning new ideas and techniques that allow them to produce more efficiently. This is especially important, since economists highlight that such technological change is by far the most important ingredient for ensuring productivity growth and thus also long-term economic growth. Investing more in infrastructure or machinery may give economies a medium-term boost, but absent new and more effective organization and production technologies the benefits are likely to taper off. In economies that continuously innovate or adopt new and efficient ideas from abroad, economic growth is more sustainable. Democracies hold a clear edge over autocracies when it comes to generating technological change, according to several studies, and this translates into higher economic growth in the long run.

More Democracy Advantages

In a recent survey of the academic literature from the last 20 years, my co-authors and I summarized the findings from more than 1,200 analyses on the effects of democracy on 30 different social, economic and governance outcomes. The overall pattern of results does not suggest an adverse trade-off between democracy and other outcomes that are widely accepted as normatively desirable. For several of the 30 outcomes that we surveyed,

Photo 2: Wikimedia Commons

An autocratic industrialization experience with adverse economic consequences: backyard furnaces in Xinyang County, China, during Mao Zedong's "Great Leap Forward".

Photo 3: Wikimedia Commons

The Pfizer-BioNTech MrNA vaccine against Covid-19: a result of innovation taking place in democracies.

there is mixed evidence with respect to the relationship with regime type, with no clear indications that autocracy is outperforming democracy, or vice versa. Yet for several other outcomes there is robust evidence from across studies that autocracies clearly outperform democracies. Several of these outcomes may have more or less direct bearing on the competitiveness and development of national economies, and let me start by referencing some of the relevant outcomes for which there is no clear evidence on a relationship with democracy.

For example, the plurality of surveyed studies does not find any systematic relationship between regime type and inflation, and among the remaining studies about equal numbers report a positive and a negative effect of democracy. When it comes to monetary policies as well as fiscal policies that are anticipated to have benevolent macroeconomic effects, there are more studies that report a positive than a negative effect of democracy. But, yet again, the plurality of studies – for both types of policies – shows no systematic relationship with regime type.

Still, there are even more outcomes where there is overwhelming evidence of democracy having a positive effect on outcomes that should, in turn, help promote national competitiveness and economic development (beyond those outcomes already mentioned in the above sections, such as education or technological change).

First, democracy is negatively related to corruption, positively related to property rights protection, and, more generally, associated with a host of business-friendly regulatory and governance outcomes. Democracies thus also tend to have fewer barriers to entry for new firms and more dynamic markets. Second, democracies tend to have more developed stock markets and other financial markets and are associated with lower financial risks. Third, democratic economies tend to pursue policies that promote economic openness and score higher also on more direct measures of international economic interaction. This goes not only for incoming foreign direct investment, which I have already mentioned, but also in the areas of tourism and especially trade. Hence, a majority of studies show that democratic economies are more open and better integrated with the world economy than autocratic ones, and this could, in turn, contribute to explain the discussed findings that democracies have higher productivity growth.

In sum, democracy seems to be clearly beneficial for some economic outcomes that should enhance national competitiveness, whereas for other outcomes there is no clear evidence that regime type matters. Taken together, this implies that there is no clear trade-off between having a democratic political system and building a well-functioning economy that is internationally competitive.

Democracy Is the Safest (& Best) Bet

In well-functioning democracies, ordinary citizens are able to vet and select their leaders in competitive elections. Insofar as many citizens care about the performance and development of the economy, this is likely one mechanism that contributes to democracies, on average, having more competent leaders than autocracies. Yet democracies may occasionally also produce leaders with misguided economic policy ideas and who manage the economy poorly. Then, at least, competitive elections provide a safety valve for making sure that these leaders are thrown out of office after about four years instead of 20.

At present, there is for example much uncertainty and investor angst regarding the direction that policy-making will take in China under President Xi Jinping, with related concerns that a new policy course could even impact negatively on the Chinese growth rate over the coming years. Since presidential term limits were recently abolished and since Chinese citizens cannot easily change their government, as contested elections are lacking, such a policy shift could have severe long-term consequences; the current president is still only 69 years old and can be expected to remain in power for a long time. A democratic system with competitive elections would have contributed to making such a scenario less likely, as voters experiencing a deterioration of the economy are likely to vote for a government change.

Yet democracies do not only contribute to faster development and more competitive economies by allowing for more easily changing leaders who pursue counterproductive policies. In fact, democracy helps ensure a number of conditions that provide fertile ground for increased productivity. For example, democracies protect property rights better and provide regulatory environments that are, generally, more friendly to new businesses. They are also more open to both foreign investors and international trade, providing the economy with new sources of capital and important impetuses for technological upgrading. Further, democracies take better care of their children, by providing them with better healthcare and access to education. This is obviously important for the life quality and opportunities of these children. Yet it is also important for the longer-term competitiveness of the national economy – healthier and more educated children today means a more productive workforce tomorrow. JS

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