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Effects of political rivalry on public investments in education and income inequality

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Abstract

In this paper we intend to empirically examine the impact of political rivalry on four selected macroeconomic variables: public investments in education, school enrollment, GDP per capita and income inequality. We first construct a political rivalry indicator and examine how it varies across different groups of countries. We then perform a series of regressions and find that in lower income countries there is a significant negative impact of political rivalry on the selected variables, while in higher income countries the impact is weaker. This suggests that the channels linking political rivalry to macroeconomic variables differ with the development level.

Keywords: Economic development; Inequality; Institutions; Political rivalry; Public education

JEL classification: E24; H21; H40; H52; I24; O43; P0

1. Introduction

Uncovering the mechanisms of how political institutions may affect and determine economic performance is one of the most challenging research questions in modern economics. Related research on political institutions emphasizes their central role in defining economic policies

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and the resulting outcomes. Studies focusing on political competition and economic interactions argue that policies cannot be viewed as exogenous and, as important determinants of economic incentives, should be regarded crucial in explaining differences in economic performance across countries (e.g., Acemoglu, 2006; Acemoglu & Robinson, 2001; Persson & Tabellini, 1992; Sayer, 2000).

Traditionally, models developed in this research area have usually considered that political competition is beneficial for the economy (e.g., Besley, Persson, & Sturm, 2010; Wittman, 1989), as they associate higher degrees of political competition to the implementation of growth-enhancing policies. However, more recently, some researchers have questioned this perspective, suggesting that political competition may be harmful for economic growth and development, as it reduces the incentives of the political group in power to implement policies that promote economic growth and social welfare (Acemoglu, 2006; Acemoglu & Robinson, 2006; Lizzeri & Persico, 2005).

In particular, Acemoglu (2006) emphasizes the idea that the main objective of the political group in power—the elite, may not be serving the society, but keeping the control of political power for as long as possible, using it for their own benefit. In this case, the elite will implement distortionary policies aimed solely at impeding political rival groups to rise to the power. This political rivalry, i.e., a negative form of political competition, will have a harmful effect on the economy, as implemented policies will be distortionary and will generate inefficiency in resources' allocation.[1]

The present work relates to the increasing literature on the new political economy of growth referring to political rivalry as a key factor affecting economic performance. For example, Rodrik (1999) suggests that disagreements between political groups may inflict the extra cost on the economy, interpreted in terms of forgone investments and growth opportunities. Similarly, Dixit and Londregan (1995) and Acemoglu and Robinson (2001) suggest that contesting political power may induce economic costs due to its growth-retarding effects. In Acemoglu (2006) the political elite's preferences over inefficient policies due to political consolidation reasons compromise long-term investments and lead to poor aggregate economic performance. Sochirca, Afonso, and Silva (2012) specifically study the effects of political rivalry on a number of macroeconomic indicators–education, economic growth and income inequality–finding that all are negatively affected by political rivalry. More specifically, political rivalry reduces human capital accumulation through its negative impact on public investment in education, workers' wages and schooling choice, hinders economic growth by discouraging economic activity and human capital accumulation, and increases income inequality by impeding income convergence and prolonging income inequality over time.

Motivated by the theoretical results in Sochirca et al. (2012), in this paper we intend to empirically examine the effect of political rivalry on four macroeconomic variables: public investments in education, school enrollment, GDP per capita and income inequality. Given that these macroeconomic indicators, reflecting long-term economic development, are determined by specific macroeconomic policies, they are potentially subject to political rivalry influence.[2] With this

[1] Thus, political rivalry may arise in both democratic and non-democratic regimes and its existence is thus independent of the political system, varying only in degrees of intensity and forms of manifestation (see, for example, Acemoglu, 2006).

[2] In choosing these specific variables we also relate to some studies on the relationship between human capital accumulation, inequality and economic growth. For example, Perotti (1996) and Saint Paul and Verdier (1996) show that higher inequality is associated with a lower level of human capital accumulation, which on its turn is associated with lower levels of economic growth. More recently, the cross-country analysis of Easterly (2007) reaffirmed that human