



# When voice fails: Potential exit as a constraint on government quality

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## ABSTRACT

Poorly governed (e.g., repressive) countries tend to be located near other poorly governed countries, and well governed countries near other well governed countries. Researchers, by identifying country characteristics (e.g., ethnic fractionalization) that may influence government quality, have provided one potential explanation: Neighboring countries tend to be similar with respect to those characteristics. In this paper, we draw on Hirschman's notion of "exit" as a disciplining device in order to provide a different, though complementary, explanation: The ability of a ruler to implement policy that displeases the country's populace is constrained by opportunities for residents to relocate to other countries nearby. To generate testable predictions about the effects of potential exit on government quality, we develop a simple theoretical model. We test the model's predictions using cross-sectional and panel data, controlling for other determinants of government quality. The evidence we present – which includes discussion of historical examples such as ancient Greece and the Soviet Bloc – supports the model's predictions.

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"There is no prince that will thus lightly lose his subjects."

– John Bunyan, *The Pilgrim's Progress* (1678, p. 222)<sup>1</sup>

## 1. Introduction

Hirschman (1970) famously pointed out that unhappy populations may respond by exercising "voice" or "exit." In well governed democracies, voice typically takes the form of voting or protest. Voice can also take the form of revolt, especially in countries where citizens cannot rely on democratic institutions to make their voices heard. Acemoglu and Robinson (2000, 2001) have shown how the threat of revolution may, in some circumstances, lead to more broadly representative government. In their model, it is *potential*, rather than actual, revolution that influences government quality.<sup>2</sup>

The objective of this paper is to examine whether potential exit has a similar effect.<sup>3</sup> The idea is that even the most repressive rulers will likely have segments of the population (e.g., fellow tribe members, co-religionists, soldiers, doctors, scientists, or star athletes) whom the rulers desire to keep. The possibility of citizen departure thus sets a lower bound on the depths to which the government will descend. *Ceteris paribus*, a country that is very difficult to leave can be governed very badly – "exit" is not a credible option. However, a country with a well governed, easy to reach neighbor cannot be too poorly run without generating an exodus (unless the rulers take measures to make exit more difficult). Consequently, a nation cannot be too much worse than the best of the alternative countries, less an adjustment for the cost of getting there. We label this phenomenon "neighborhood constraints."<sup>4</sup> The implication of neighborhood constraints is that nearby countries will tend to be

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<sup>1</sup> The words are spoken by Apollyon, ruler of the temporal "City of Destruction," to Christian, who seeks to escape to the "Celestial City."

<sup>2</sup> Acemoglu and Robinson (2000, 2001) show how a ruling elite can forestall revolution by promising to redistribute wealth, but must first overcome a time-inconsistency problem: The elite has the incentive to renege once transitory revolutionary fervor has passed. By extending voting rights to the disenfranchised, the elite can reduce its ability to renege ex post, thus rendering its ex ante commitment credible.

<sup>3</sup> Interestingly, the possibility of migration may make the threat of revolution more credible (for example, attempting revolution is less costly if failed revolutionaries can escape to a well-run neighboring country). In other words, as Hirschman (1970, p. 83) hypothesized, the ability to exit may increase the effectiveness of voice.

<sup>4</sup> We should emphasize that the "neighborhood constraints" considered here differ from what has been termed "neighborhood effects" (e.g., Brock & Durlauf, 2002; Manski, 1993) in that this paper's neighborhood constraints involve unidirectional relationships running from better-governed to worse-governed countries, while neighborhood effects typically refer to the influence of an aggregate (e.g., a neighborhood) on an individual member of the aggregate (e.g., a resident). A closer parallel to our notion of neighborhood constraints may be found in the literature on interjurisdictional tax competition, as we discuss below.

alike in the quality of their governments, even in the absence of other similarities, unless there exist substantial barriers to movement.

To investigate this phenomenon systematically, we begin by constructing a simple theoretical model, in which each country has a stylized ruler and a representative citizen – more specifically, a representative citizen of the type the ruler desires to keep from leaving. The citizen's decision to stay in the country depends on the quality of government in that country, the quality of government in countries to which the citizen can move, and the cost of relocating to those countries.<sup>5</sup> The ruler has a preferred level of government quality to provide to the citizen; this preferred level is exogenously determined. Regardless of whether the preferred level is high or low, the ruler will not set quality so low that the citizen leaves. The possibility of relocation thus sets a lower bound on government quality – a government will be no worse than the citizen's best alternative, adjusted for relocation costs. (Whether the constraint imposed by this lower bound is *binding* depends, of course, on the ruler's exogenous preferences in relation to the lower bound.) The model yields two econometrically testable predictions about expected government quality: (i) it increases as the quality of government in the best alternative destination rises, and (ii) it decreases as the cost of relocating to the best alternative destination rises.

We test the model with cross-sectional and panel data. Our focus is on how badly a government can get away with treating its citizenry. There are various forms such “badness” might take: ignoring the public's preferences when setting policy, depriving citizens of civil rights, arbitrarily seizing people and property, and so forth. No single measure will capture all these dimensions, but the measures we have chosen reflect important aspects of them. In the cross-sectional analysis, we use three measures: (i) the Voice and Accountability indicator, developed by Kaufman, Kraay, and Zoido-Lobaton (2002a, 2002b) for the World Bank, (ii) the Political Rights index from the Freedom House (2002), and (iii) the Civil Liberties index from the Freedom House (2002). In the panel analysis, we use both of the Freedom House indices, which allow us to examine changes in government quality over a 30-year period.<sup>6</sup>

Identifying the appropriate measure of relocation costs is more challenging. Of greatest concern is the measure's *exogeneity* with respect to the policies implemented by the country's ruler. For reasons illustrated in the model, rulers who prefer to provide low levels of government quality may enact policies that make departure difficult (as did the USSR). Thus, seemingly obvious measures of relocation costs such as visa requirements or the price of an airplane ticket are not appropriate for use in our econometric analysis. We focus instead on the effect that *neighboring* countries have on each other; a neighboring country is less costly to get to than is a more distant country, all else equal. Within the set of neighboring countries, our principal proxy for relocation costs is the length of the shared border – the longer the shared border, the easier it generally is to enter a neighboring country. In addition to its exogeneity to this application, an important advantage of the border length variable is that it is precisely measured and comparable across countries throughout the world and over time, in a way few other measures would be.<sup>7</sup>

The empirical results support the model's predictions. In the cross-section, we find that government quality is positively related to that of the best alternative destination among the neighbors, and negatively related to our proxy for relocation costs. The results hold when we control for plausibly exogenous influences on government quality: ethnic fractionalization, linguistic fractionalization, religious fractionalization, the size of the Catholic population, the size of the Muslim population, and distance from the equator.<sup>8</sup> We also control for GDP in the neighboring country, to capture economic influences on migration incentives. In the panel, including country fixed effects (thus controlling for *any* long-lived country-specific factors) and year dummies, we find that increases in government quality in the best alternative among neighboring countries are associated with increases in own government quality. In addition, regressing government quality on its past value and on past values of government quality in the best alternative destination, we find that countries located near substantially better governed alternatives subsequently improve more than do other countries of similar quality. Thus, even though we cannot control perfectly for all of the other potential causes of geographical clustering, we find that a variety of econometric approaches generate evidence consistent with our model's predictions.

The model makes two additional predictions, neither of which can be easily tested econometrically with available data. First, a ruler who decides to maintain a very low level of government quality in the presence of a well governed neighbor will expend resources to prevent citizens from leaving. Second, neighborhood constraints lead to government quality that is higher on average across *all* countries than would otherwise be the case. We discuss these predictions in the context of several specific examples of good and bad government.

Perhaps the closest parallel to our notion of neighborhood constraints can be found in empirical studies on interjurisdictional tax competition (e.g., Baicker, 2005; Case, Hines, & Rosen, 1993). These studies document a strong relationship across neighboring states in levels of government expenditure.<sup>9</sup> Similarly, we document a strong relationship across neighboring countries in levels of government quality. The same factors that prevent one state from levying high taxes when low tax states are nearby may prevent one regime from being very repressive when less repressive regimes are nearby. For example, one of the explanations offered for the cross-state relationship in tax rates is “yardstick competition,” enforced by voters (Besley & Case, 1995). Although those subjected to tyrannical rule typically lack the ability to vote a ruler out of office, they may have the ability to vote with their feet. Thus, the basic mechanism emphasized in this paper is similar to Tiebout (1956) competition. However, the reader should be aware that our application is very different from the typical Tiebout analysis. Our model is not one of citizens with heterogeneous policy preferences sorting themselves among alternative governments with alternative policy regimes. Instead, we focus on how the ability of citizens

analyze in this paper. Thus, one may think of border length as a quasi-instrument for underlying (and unobservable) relocation costs.

<sup>8</sup> In the main specifications of our cross-sectional analysis, we do not control for each country's “legal origins” (La Porta, Lopez-de-Silanes, Shleifer, & Vishny, 1999), because legal institutions are endogenous within our framework – for communist and ex-communist countries, low government quality and communist legal origins were simultaneously determined. Nevertheless, we do conduct robustness tests in which we control for legal origins variables. In our panel specifications we include fixed effects, which control for factors – like legal origins – that are constant over time. Finally, in another robustness test, we exclude communist and transition countries from our panel analysis to be sure the downfall of communism does not drive our panel results. See Section 4.

<sup>9</sup> The studies define “neighbors” in various different ways. For example, Case et al. (1993) use three separate measures: common borders (our measure), similar income levels, and similar racial composition.

<sup>5</sup> Note that our argument does not require that the destination country wish to receive immigrants, nor that it have any particular desire to improve the quality of the other country's government. See Hatton and Williamson (2004) for a discussion of the political economy of immigration restrictions.

<sup>6</sup> See Section 3, Appendices A and B for a more detailed discussion of these variables.

<sup>7</sup> While border length may on occasion change as a result of government policy (see, e.g., Alesina, 2003; Spolaore & Wacziarg, 2005), it is difficult to see how it would be caused in any systematic way by the measures of government quality we

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