Journal of Comparative Economics 42 (2014) 839–854

Contents lists available at ScienceDirect

Journal of Comparative Economics

journal homepage: www.elsevier.com/locate/jce

Democratic institutions and regulatory reforms ☆

Mohammad Amin [a,*], Simeon Djankov [b]

[a] Enterprise Analysis Unit, World Bank, 1818 H Street NW, Washington, DC 20433, USA
[b] Harvard Kennedy School and NES, 79 John F. Kennedy Street, Cambridge, MA 02138, USA

ARTICLE INFO

Article history:
Received 1 August 2014
Available online 24 August 2014

JEL classification:
P11
P16
K20
L51

Keywords:
Democracy
Elections
Regulation
Reforms

ABSTRACT

Amin, Mohammad, and Djankov, Simeon—Democratic institutions and regulatory reforms

We use a sample of 144 countries over the period 2003–2013 to investigate the link between democratic institutions and regulatory reforms. Democracy may be conducive to reform, as politicians embrace growth-enhancing reforms to win elections. On the other hand, authoritarian regimes may not worry as much about public opinion and could undertake reforms that are painful in the short run but bring long-term benefits. We test these alternative hypotheses, using data on regulatory reforms from the World Bank's *Doing Business* database. The results provide mixed support for the hypothesis that democracy is good for regulatory reforms. We also show that regulatory reforms are more likely just after parliamentary elections in poor and middle-income countries. *Journal of Comparative Economics* **42** (4) (2014) 839–854. Enterprise Analysis Unit, World Bank, 1818 H Street NW, Washington, DC 20433, USA; Harvard Kennedy School and NES, 79 John F. Kennedy Street, Cambridge, MA 02138, USA.
© 2014 Association for Comparative Economic Studies. Published by Elsevier Inc. All rights reserved.

1. Introduction

The link between political and economic governance has been the subject of debate at least since Aristotle in 4th century BC. In *The Politics*, Aristotle thought that democracy functioned well in the absence of inequality, and so "a city ought to be composed, as far as possible, of equals and similars; and these are generally the middle classes." Two millennia later, Montesquieu supported the view that checks on the powers of government are a pre-requisite for good economic governance and prosperity. More recently, Schumpeter (1942) argued that "modern democracy is a by-product of the capitalist process," while other scholars further developed his theory by finding that the need for democratic institutions does not arise until countries reach a certain degree of economic development, through market reforms (Lipset, 1959).

A separate literature – on development – finds that democracy sometimes assists reformers in making difficult choices that potentially hurt important lobbying groups. Examples include Dewatripont and Roland (1992) and Roland and

☆ We thank Daniel Berkowitz (the editor), Caroline Freund, Andrei Shleifer, the anonymous referee, and seminar participants at the Harvard Kennedy School, the Cato Institute and the Millennium Challenge Corporation for useful comments. All papers in this special issue were reviewed at the same level as regular submissions to the Journal of Comparative Economics.
* Corresponding author.
E-mail addresses: mamin@worldbank.org (M. Amin), Simeon_djankov@hks.harvard.edu (S. Djankov).

http://dx.doi.org/10.1016/j.jce.2014.08.005
0147-5967/© 2014 Association for Comparative Economic Studies. Published by Elsevier Inc. All rights reserved.

Verdier (2003), and Freund and Rijkers (2014) in the context of labor markets. However, Du et al. (2014) find that the rigid regulatory state has played a positive role in the economic transition in China. And Freund and Jaud (2013) identify over 100 transitions to and from democracy, and show that the transition to democracy yields no growth dividend compared to other types of regime change and that countries that democratize slowly do not gain in economic growth from regime change. In contrast, Acemoglu et al. (2014) find a positive effect of democracy on growth, using a similar sample.

Overall, the empirical evidence on the link between democracy and reforms is unclear. Economic history provides us with examples of both authoritarian and democratic regimes that implemented major economic reforms. For example, successful economic liberalization was achieved under the military regimes in Argentina (1966 and 1976), Chile (1973), Brazil (1964), Uruguay (1976), and under authoritarian regimes in China (1978), Vietnam (1993), Saudi Arabia (2006) and Azerbaijan (2008). Reform is also achieved under democratic regimes in Australia (1983), Colombia (1986, 1991, 2006), New Zealand (1984), Spain (1977–1978), Poland (1992), Russia (1992), Estonia (1993), Slovakia (1998–2000), Georgia (2004–2008), FYR Macedonia (2007–2008) and Latvia (2009–2011).

The existing economics literature on the relationship between democracy and reform first developed around the experience of countries with macroeconomic stabilization efforts in the 1970s. It is largely based on case studies (see, for example, Williamson, 1994; Nelson, 1990; Bates and Krueger, 1993). While this literature does not reach a consensus on whether democracy promotes reform, it highlights the argument that reforms are often unpopular because they tend to reduce living standards in the short run. Even reforms that increase overall prosperity (measured in GDP growth) may be unpopular if compensation schemes for the losers are not credible; and if benefits are far in the future and costs more immediate (Fernandez and Rodrik, 1991; Rodrik, 1996).

These problems with democracy are compounded by the fact that democracies offer more channels of protest and influence on policymaking to subordinate groups than authoritarian regimes. And that they create more favorable conditions for the development of strong and independent sectoral and non-government organizations capable of resisting reform efforts (Remmer, 1986). Lastly, democratic rule may fragment decision-making authority among branches of government, allowing opponents of reform to interfere more easily with program design. In contrast, authoritarian governments have less need to respond to either popular opinion or vested interests and hence can more readily base their decision on criteria of economic rationality. They are better able to make long-run plans than are democratic governments tied to electoral cycles; have greater centralization of power that facilitates the implementation of reforms.

However, these supposed advantages of authoritarianism are not without their problems. For example, to the extent that policy information and feedback are vital to the design of reforms, democracies may have an advantage (Remmer, 1986). Autocratic rulers do not have to worry about re-election and hence it is not clear what their incentive to reform is; losers from reforms may comply with their defeat because they believe that the institutional framework that organizes the democratic competition will permit them to advance their interest in the future (Przeworski, 1991).

The literature on democracy and reforms received a new life with the trade liberalization and agricultural liberalization reforms of the 1990s. These gave rich empirical data, including on the relationship between different types of democracies and structural reforms. Examples include Olper and Raimondi (2013) and Giuliano et al. (2013). The findings generally support the view that democracies increase the likelihood of reform, while not finding support for a feedback mechanism.

The most recent line in the literature on economic reforms studies the post-communist experience. Examples include Grosjean and Senik (2011), BenYishay and Grosjean (2014), and Dower and Markevich (2014). These studies find some evidence for the positive effect of democracy on attitudes toward structural reforms like privatization and competition policy.

Still, the empirical literature on democracy and reforms is in its infancy, mostly hobbled by the lack of available panel data that relates changes in political structure to changes in regulatory governance. All existing studies have hence focused on macro-economic or sectoral reforms. In this paper we provide analysis of the link between democratic institutions and regulatory reforms, using data on micro-economic reforms. In particular, we study the relationship between business regulatory reforms, shown in previous studies (for example, Klapper et al., 2006 and Barseghyan, 2008) to expand growth, and the level of parliamentary democracy as a proxy for democratic institutions. The analysis is done on a sample of 144 countries, with data on reforms between 2003 and 2013 drawn from the World Bank's *Doing Business* project.

Our data are less subject to the criticisms on other measures of economic institutions, which suffer from significant endogeneity issues, and measure outcomes rather than institutions (for example, Glaeser et al., 2004). The Doing Business data are focused on specific regulatory or legal reforms, and as such they are a better indicator of underlying institutions. At the same time, they are sufficiently finely measured so as to avoid the possibility of such reforms affecting the development of democratic institutions. In other words, the feedback loop from reforms to democratic development, that has worried researchers using macroeconomic reform data, is less of an issue here.

We experimented with a number of different specifications. While most of these specifications show a strong positive relationship between democracy and reforms, the relationship is somewhat weak in evidence is somewhat weak in some specifications. In this sense, our results for the positive effect of democracy on reforms are mixed. For example, for our main specification, we find robust evidence for the link between democratic institutions and regulatory reforms. The estimates imply that a move from below-average to above-average level of parliamentary democracy increases the probability of reform by as much as 8.6 percentage points, a large effect given that the probability of doing reform by a country in a given year averages 68.3 percent in our sample. Higher-end estimates imply an increase of 20.4 percentage points in the probability of a reform in moving from below- to above-average level of democracy.

Download English Version:

https://daneshyari.com/en/article/5092314

Download Persian Version:

https://daneshyari.com/article/5092314

Daneshyari.com