POLITICAL INSTABILITY AS A SOURCE OF GROWTH

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Executive Summary

The U.S. government emphasizes the importance of stable political leadership as a necessary condition for economic growth. Contrary to this view, I show that high leadership turnover is strongly associated with high economic growth both in autocracy and in democracy. The effect of "unstable" leadership is stronger in democracies than autocracies because democratic political systems have institutions that promote competition over policy ideas rather than over the distribution of private benefits to cronies. Two institutions are shown to be particularly important in promoting such public goods as a fair legal system, transparent decision making and accounting, a strong national defense, and a healthy, growth-oriented infrastructure. These two institutions are a large selectorate (the set of people with a say in choosing leaders) and a large winning coalition (the set of people whose support keeps the incumbent in office).

Political leaders are eager to stay in office and, contrary to the neoclassical economic model, are not benign agents of the people in whose name they lead. Because autocrats depend on small groups of supporters, they emphasize the use of private benefits to their cronies as the means to gain political loyalty and stay in office. This means that they generally have little incentive to pay attention to the overall quality of their public policies.

Democrats, in contrast, require the support of a large coalition to stay in power. Because private rewards have to be spread thinly to many people, democrats find it easier to compete for office by providing public goods that benefit everyone rather than private benefits for a few cronies. This means that, in democracies, political competition is over policy ideas. Two effects follow from the fact that democratic leaders must build large coalitions: Democratic leaders provide better policies to improve their chances of surviving in office, and because competition is over policy ideas, they are more easily turned out of office in favor of

a political challenger than are autocrats. Thus, autocrats have longer terms in office and produce less-efficient economic growth. The U.S. government emphasis on stable leadership as a necessary condition for growth is mistaken and can lead to global economic contraction rather than expansion.

POLITICAL INSTABILITY AS A SOURCE OF GROWTH

Since the end of the cold war, U.S. foreign policy has appropriately been attentive to issues of economic growth around the world as a central factor in promoting peace, prosperity, and American security. The great diversity in growth rates and in poverty cannot easily be attributed to ignorance by leaders about what makes an economy grow. Market economies have driven socialism into obscurity. Therefore, we must look at something other than competing economic theories to explain national economic failure.

Today the key to economic performance lies within the political institutions of sovereign states. Political arrangements create incentives for political leaders to foster growth or to steal their nation's prospects for prosperity. How to promote prosperity is likely to be one of the most important policy puzzles facing the U.S. government as it looks for ways to ensure national security in a world of great economic inequality.[1]

Typically, economists approach the issues concerning economic reform by assuming that decision makers and citizens have a common interest and that leaders just need information about how best to realize those interests.[2] This view has fostered an understanding about which economic policies promote growth, but this view is inadequate for ad-

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dressing how to improve the prospects for implementing growth-oriented policies. I show here that different rules of governance create highly variable incentives for leaders. Under some arrangements, it is best for leaders to promote growth; under others, they are best off encouraging cronyism and corruption. Many of the world's governments operate in environments that promote economic policies that diminish prosperity and social welfare, not out of ignorance but because it is not in the best interest of their leaders to foster prosperity.

Economists provide economic policy solutions that are tried, tested, and true for promoting prosperity, but they rarely confront the political incentives that block economic reform. I identify the institutional sources for these incentives and suggest changes that they imply in U.S. overseas economic policy.

Stable Government and Prosperity

Peace and prosperity are commonly thought to be associated with stable governance. A recent study by the Congressional Budget Office (CBO), for instance, claims that stable government is a necessary, if not sufficient, condition for economic growth. The CBO's conception of stability appears to focus primarily on national leaders' longevity in office. It reports, for example, that Zambia "has enjoyed a fair degree of political stability since independence in 1964. Until 1991, Zambia was governed by a one-party system" or that "Tunisia is one of the more stable and developed countries of North Africa and the Middle East. Governed by the Destourian Socialist Party since independence in 1957, Tunisia's administration has been flexible and pragmatic in implementing development policy." Egypt also is characterized as stable because "only three presidential administrations have governed Egypt since 1952—those of Gamal Abdel Nasser, Anwar Sadat, and Hosni Mubarak."[3]

This view of stability and growth is a dangerous basis for forming foreign policy. It confuses two entirely separate dimensions of stability, one that can promote growth and one that actually retards growth. If the U.S. government, the International Monetary Fund, and the World Bank were to follow the recommended course of promoting leadership stability, the consequence would more likely produce economic contraction around the world rather than expansion.

Stability can be divided into at least two important dimensions. One is the longevity in office enjoyed by national leaders. The other is the longevity of national political institutions that define the form of governance. For many, especially among economic policy makers, any source of instability is thought to create uncertainty in the marketplace. Such uncertainty raises uncompensated risks associated with investment and so is presumed to retard growth. Taken alone, this view may be correct. However, uncertainty about national politics, and especially about who will be the future leader, is often the product of an open, competitive political system that can lead to substantial economic benefits arising from the efficiency gains created by political competition.

In politics, competition promotes growth when it is over ideas for improving the welfare of a broad base of citizens through the provision of market-enhancing public policies. Leaders' longevity in office typically reflects institutional arrangements that stifle just such competition, instead rewarding cronyism and corruption. I will show that competition for national leadership, rather than stable leadership, is a hallmark of growth.

Institutional change differs from leadership longevity in important ways. A polity can maintain stable institutions of government that create incentives to promote growth, but it can also protect institutions designed to promote corruption. Indeed, from a political leader's point of view, as I show below, institutions of government that facilitate corruption are the easiest path to longevity in office. Institutional changes that move a government from dependence on cronyism and corruption toward fair, transparent competition promote growth. Institutional changes that diminish the protection of property rights, rule of law, and other factors that make for a level, competitive playing field discourage growth. Therefore, the direction of change in political institutions is more important than the presence or magnitude of instability per se when it comes to promoting or retarding economic development. Neither leadership instability nor institutional instability need be the bogeyman of economic development.

I begin with an evaluation of stability and growth and then identify the specific institutional factors that create incentives for leaders to produce growth. I then contrast those institutions to others that reward leaders for creating slow growth, in the process identifying circumstances that make bad policy good politics.

Leadership Stability, Autocracy, and Democracy

Autocracies have more stable leadership than do democracies. Over the past forty years, for instance, the most autocratic governments of the world have averaged only seven leaders (the median number is 6.5). Some countries have managed only one or two leaders in that time span. Fidel Castro, for instance, has led the Cuban government for four decades, running its economy into the ground the whole time. Since the Chinese revolution, that country has only had five leaders (and strong growth for two of the five decades); Russia in the seventy-five years since the death of Lenin, only eight (and poor growth for most of its history). The British and Americans, who have had vastly more leaders since the end of World War II, have highly stable democratic leadership systems. The average number of leaders in the most democratic countries since 1961 is twelve (with a median of 10). Yet the benefits of leadership instability in terms of economic growth are dramatic (see figures 1 and 2). Figure 1 shows the relationship between average national growth rates over the period since 1961 for democracies, comparing growth rates to the number of leaders (provided the leader lasted at least one year). Figure 2 shows the same assessment but for the most autocratic governments (again provided the leader lasted at least one year). Several features are clear.

Growth increases with turnover in leaders in both democracies and autocracies, eventually leveling off. The uncertainty provoked by

Figure 1. Leadership Stability and Growth: Democracies

instability might be thought to scare investors, but those effects are offset by the advantages inherent in political competition, even when that competition occurs in an autocratic environment. Although leadership turnover turns out to be generally beneficial for growth, the benefits are smaller in autocracies than in democracies. Democracies, of course, have more orderly means to turn leaders out of office and so provide greater predictability.

The average growth rates in democracies are higher than in autocracies for most levels of leadership turnover. It is not only competition over leadership that gives democracies an advantage. Other features of democracy create incentives for leaders to provide successful policies and create an environment that makes democratic leaders especially likely to remain in office a shorter time than do most autocrats.

Bad Policies Associated with Long Terms in Office

It is natural to think that leaders who produce peace and prosperity for their citizens are successful, just the sort of leaders people would like to keep around. By contrast, leaders who produce war, famine, pestilence,

Figure 2. Leadership Stability and Growth: Autocracies

poverty, and misery seem like dismal failures who should be turned out of office as quickly as possible. Yet the opposite is true. Leaders who produce poverty and misery keep their jobs much longer than leaders who succeed in making their countries rich and peaceful.

Let us divide the world into the most democratic and the most autocratic governments and compare their track records for producing prosperity. To evaluate prosperity, I examine the average annual growth rates delivered by the approximately two hundred most democratic leaders and the approximately two hundred most autocratic leaders since 1961 (see figure 3).

The difference in growth rates tells a dramatic story. Two countries starting out with the same size economy in 1961 would look radically different in 2000 if they had had different forms of government. Suppose a democracy and an autocracy each had a gross domestic product of $10 billion in 1961 and suppose each grew at the rate typical for its type of government? In the year 2000, the democracy's gross domestic product (GDP) would be $58.6 billion. The autocracy's GDP would be only $28.9 billion. Assuming each maintained its form of government and

Figure 3. Comparison of Growth Rates by Regime Type

that the average performance of these government types did not change, by 2061, a century beyond the start date, the democracy's GDP would be expected to grow to $832 billion; the autocracy's, to $142 billion, a six to one ratio. Apparently a prosperous life for the average citizen seems to be closely tied to democracy and poverty, to autocracy.

Democracy seems to produce prosperity, but what about peace? Here too the evidence strongly favors the idea that leaders in the most democratic states significantly reduce the risks their citizens face of death in war as compared to the risk under the most autocratic leaders. Figure 4 displays the peak level of violent deaths during international conflicts suffered by citizens living under the leadership of the average democrat and the average autocrat over the past two centuries.

Figure 4 makes several facts abundantly clear. War, of course, is rare, and so most leaders, most of the time, rule during times of peace. The most typical experience for citizens is to suffer no deaths in foreign conflict regardless of the government they live under. For those living in an autocracy, however, there is about a fifty-fifty chance that some citizens will die in war. For those living in a democracy, the odds are 70 percent that no deaths will be experienced in foreign conflicts. The odds of living in peace are much better in democracies than in autocracies. Autocracies lead democracies in every subsequent category of

Figure 4. Fatalities in International Conflict

violent death in war. Twenty percent of the most autocratic leaders rule in times when their population suffers more than a thousand fatalities in wartime; the comparable figure in democracies is 15 percent. The odds of lower levels of violent deaths in foreign adventures are almost twice as high under the most autocratic leaders as they are under the most democratic incumbents. The probability that this difference arose by chance is less than one in a thousand.

The lessons of the past show that democracy enhances the prospects of peace and prosperity, though what it is about democracy that promotes these desirable consequences remains an open question. Autocracy seems good at producing the poor, nasty, brutish world that Thomas Hobbes was concerned to avoid more than three centuries ago. Why, then, are there so many autocrats in the world?

Politicians, like everyone else, are concerned with their personal welfare. Peace and prosperity may be good for most people, but are they good for leaders? It seems obvious that leaders ought to desire peace and prosperity, but in politics the obvious is often false. Just how does political life look for incumbents?

Begin with the premise that incumbent leaders want to remain in power. That is, politicians are not benign agents of their citizens, they are not primarily concerned with enhancing national welfare. National welfare is enhanced only if doing so helps incumbents remain in office. Personal welfare, rather than the national interest, is the wellspring of action for all leaders. Therefore, they do what gives them the best chance of staying in office and avoid those actions that place their leadership at risk.

What does political survival look like from the viewpoint of democrats and autocrats? I address the political survival of leaders in three ways. Figure 5 shows the division between the most democratic and the most autocratic leaders for different periods in office over the past two centuries. The figure answers the question, what proportion of leaders who stay in power for a given number of years are democrats and what proportion are autocrats? The striking feature of figure 5 is that once leaders get beyond about eight or so years in office, almost none of the survivors are democrats. The democrats disappear. With rare exceptions, only autocrats hold onto power for a long time. Autocracy is the basis for stable leadership of the sort that the CBO mistakenly thinks promotes economic development. This advantage in leadership stability

Figure 5. Long-Serving Leaders—Autocrats or Democrats?

is true despite the fact that few democracies have term limits and even fewer had them over the span of the two hundred years of leadership reflected in figure 5. Even the United States had no presidential term limit before Dwight Eisenhower became president in 1954.

Figure 6 looks at survival in office from a different perspective. Here the question is what percentage of leaders in democracies and what percentage of leaders in autocracies lasted for particular periods in office? So, whereas figure 5 answered the question, what percentage of those lasting in office ten years were democrats? figure 6 answers the question, what percentage of democrats lasted ten years? The results in figure 6 are striking. Naturally, there is attrition the farther out one gets in political longevity. Although 100 percent of those lasting forty or more years, for instance, are autocrats, only a bit more than 2 percent of autocrats actually hold onto power that long. But two facts jump off the figure. First, nearly half of all democratic leaders are out of office within about one year of coming to power. Such a short tenure only describes the experience of about one-third of autocrats. This is a remarkable difference in stability. Second, virtually no democrats are around for more than eight years, whereas one-quarter of autocrats stay in office for more than eight years. Autocratic systems seem to favor long-term

Figure 6. Autocrats and Democrats—How Rapidly Turned Out of Office?

political survival. The CBO's idea of stable leadership is an unwitting endorsement of authoritarianism.

A third view of political longevity can be gleaned by examining table 1. Here we see the average political life of incumbents in the most autocratic and the most democratic regimes. The difference in their average years in office is so large that it would happen by chance in less than once in a thousand samples. Autocrats survive an average of about seven years; democrats average just less than three years. Of course, the average time in office can be misleading. After all, the longest-lived autocrat, Francis Joseph of Austria, lasted more than sixty-seven years, helping to push the mean up. The Finnish leader Kekkonen endured longest among democrats, surviving in office for twenty-five years. The median longevity, however, tells the same story, albeit foreshortened relative to the mean, as we would expect. Half of all autocrats last more that 3.2 years; half of democrats last no more than 1.7 years.

It is apparent that democrats produce more peace and prosperity than autocrats but last a shorter time in office. Figures 5 and 6 and table 1, when examined in light of figures 1–4, tell a remarkable tale. Despite the seemingly sensible speculation that everyone wants good leaders; that is, leaders who provide peace and prosperity for the people they rule, we see that the reward for providing peace and prosperity is to be thrown out of office. The politicians who offer their citizens poor, nasty, brutish governments are the ones likely to reap the rewards of long political lives. If staying alive politically is a leader's measure of success, then good government often is bad politics. In that sense, the real puzzle is why any leaders provide their citizens with good public policies. Of

Table 1 Average Political Life Expectancy by Type of Government

	N	*Mean (years)*	*Median (years)*
Autocrats	487	6.70	3.22
Democrats	510	2.98	1.69

course, correlation does not prove causation. For that we need an explanation of how government institutions encourage or discourage good policy.

Political Institutions and Policy Incentives

Every political system depends in part on two institutions.[4] One is the size of what I will call the selectorate, and the other is the subgroup of the selectorate who form the winning coalition that keeps the incumbent in power. The selectorate is the set of citizens who have a prospect of becoming members of an incumbent's winning coalition. In a universal adult suffrage political system, such as prevails in most democracies (and in some rigged-election autocracies), any citizen has some chance of rising to political influence. In monarchies, military juntas, and many autocracies, by contrast, only a small portion of the population has any chance to become influential in politics or to gain access to the benefits that involvement in politics can bring.

The winning coalition is made up of a portion of the selectorate. The winning coalition has two special qualities. First, its support is essential for the incumbent to stay in office. If members of the winning coalition defect to a rival and new members cannot quickly be added to replace them, then the incumbent is deposed and the rival comes to power. Second, members of the winning coalition are accorded a privilege not available to those outside this group. Specifically, they share in any of the private benefits that the leadership distributes. Keeping the loyalty of the winning coalition is crucial for any political leader. Is it best to do so by giving them special private privileges (private goods in the vocabulary of economics) or by producing public policies that raise the welfare of the whole society?

Governments raise resources through taxation. These resources are then allocated by the political leadership, presumably in a way designed to help it stay in office by retaining support from the members of the winning coalition. Leaders can invest resources in the production of public goods or they can invest resources in providing private benefits for their supporters. Public goods are enjoyed by all members of society, whether they are members of the winning coalition, members of the selectorate, or citizens in neither group. Private goods are enjoyed only by members of the winning coalition. Public goods include such items as national security, guarantees of property rights, rule of law, transparent regulation and administration, as well as protection of individual rights and freedoms. Private goods include special privileges to selected citizens, including idiosyncratic, personal protection from the law, advantages in business transactions, nepotism, cronyism, rights to corrupt practices, and the like. We can think of the allocation decision between public and private goods as reflecting either a shopping basket of some mix of goods of each type or as a basked of mixed goods, with different degrees of emphasis on the private or public elements of each good that was chosen.

The incumbent leader decides how much public policy to purchase and how many private goods to generate given the available resources. This decision is made with an eye toward staying in office. Members of the current winning coalition continue to support the incumbent leader provided the benefits they receive outweigh those they expect to receive if a challenger replaces the incumbent. That expectation depends on a couple of factors. One is how much the challenger can credibly offer. Of course, this is limited by the available budget of resources, which is no larger for the challenger than it is for the incumbent. However, it also depends on how readily a member of the winning coalition can believe that he will be essential to a new government and so continue to get private benefits if he defects. This risk of exclusion from benefits is closely linked to the size of the selectorate and the size of the winning coalition.

When the selectorate is made up of a large number of people, then the pool from which to draw supporters is big; thus any individual's chance of being essential is smaller when the selectorate is large. By contrast, when the required winning coalition is large, as in an electoral democracy, then many supporters are needed and so each individual's chances of getting access to the winning coalition is good. For example, in majoritarian democracies, the selectorate is large and the winning coalition equals about half the people in the selectorate (suitably adjusted for voter turnout). In an autocracy, the selectorate is typically smaller than in a democracy but still can be large. Tens of millions of Chinese citizens, for example, are members of the Communist Party, which offers special advantages not available to those not in the party. As such, the selectorate is still big relative to the size of the winning coalition needed to keep the incumbents in office. This means that a defector in an autocracy runs a high risk of losing access to the private benefits provided by the leadership. In a democracy, the risk of losing such access is comparatively small, equaling about half.

The allocation of resources that maximizes the incumbent's chances of political survival drives the degree to which she emphasizes good public policy or cronyism and corruption. When the winning coalition is small, a leader only needs the support of a few individuals. Suppose that, under these circumstances, the leader decided to allocate the majority of resources into private goods. Since the winning coalition is small, each supporter receives a relatively large proportion of the available resources. By concentrating on private goods, leaders with small winning coalitions can truly enhance the welfare of their supporters. However, as the winning coalition increases in size, each member's share of the private goods allocation shrinks because these goods are distributed to a greater number of individuals. This reduces the welfare of members of the winning coalition. As the size of the winning coalition increases, the provision of private goods is no longer an efficient mechanism through which to enrich supporters. Rather than continuing to focus on private goods, as the winning coalition grows leaders are better able to enrich their supporters by investing a greater proportion of available resources in public goods. Of course, the increased provision of public goods benefits all in the society, not just the members of the winning coalition. The logic is straightforward. When the winning coalition is large, leaders perforce must be more concerned with the provision of public goods, not out of civicmindedness but because the provision of such goods is compatible with their desire to stay in office.

When the winning coalition is small, the same leaders would be more inclined to provide more private goods and fewer public goods because that is the allocation that would be compatible for them. In this circumstance, a leader who emphasizes good public policy over bribing supporters is likely to lose to a challenger when members of the winning coalition defect to get a better deal. Thus, large winning coalitions, such as exist in a democracy, encourage attention to the quality of public policy. Small winning coalitions, such as typify autocracies, discourage attention to good public policy because such attention raises the risks the incumbent will be turned out of office.

Suppose that one or more members of the current winning coalition defects and the incumbent is removed from office. Because members of the coalition have defected, the challenger now has the opportunity to form a new government. The challenger must draw enough supporters from the selectorate. Since the winning coalition is always smaller than the selectorate, the defectors cannot be certain of making it into the new winning coalition. Many of the defectors may be weeded out, proving inessential to forming a new winning coalition. Consequently, a risk and a cost are associated with political defection. The risk involves the chance of exclusion, and the cost entails being cut off from a future stream of private goods conditional on being excluded from the successor winning coalition. As the size of the winning coalition becomes smaller, or the size of the selectorate becomes larger, challengers are less likely to use the support of any particular individual when forming their winning coalition. Hence, if either the size of the winning coalition shrinks or the size of the selectorate grows, defecting becomes riskier.

When the selectorate is large and the winning coalition is small, defection is risky. Given the large number of people that the challenger could choose as supporters and given that he only needs a small number of supporters, any individual's chance of being in the successor coalition is small. The pool of prospective defectors and other prospective future coalition members is large; thus no defector can be certain of being essential to the successor winning coalition. Therefore, no defector can be certain of continuing to receive private goods in the future since individuals only receive private benefits when they are members of the winning coalition. When the selectorate is large and the winning coalition is small, individuals who defect from the current winning coalition are especially unlikely to gain access to private goods in the future as compared to defectors when the coalition is large relative to the selectorate.

Consequently, systems, like many autocracies, in which the winning coalition is small and the selectorate is relatively large induce a norm of loyalty toward the incumbent leadership. Large selectorates and small winning coalitions help keep supporters loyal by making defection from the current winning coalition unattractive. As the size of the winning coalition grows relative to the selectorate, the degree of loyalty to the incumbent declines because the cost and risk of defection decline. This norm of loyalty is a powerful force in autocracy. It insulates leaders from being turned out of office just because they do a poor job on public policy. They are protected as long as they do not “squander” resources on economic development, keeping those resources to use as bribes to their few essential supporters. In a democracy, the value of individual private goods is small because they must be divided among so many people and thus leaders do not enjoy the same loyalty from their backers. Consequently, they must compete over the provision of successful policies; they do not have a sufficient loyalty advantage through cronyism and corruption. The consequence is that democrats work harder at producing effective policies, enjoy less loyalty, and so get turned out of office more frequently than their autocratic counterparts. For autocrats, bad policy often is good politics because their focus on cronyism and corruption ensures their stable leadership. That is almost never true for democrats.

Conclusions

Economic growth depends on good economic policies, but good economic policies are not always in the best interest of political leaders. The United States should encourage political reform wherever possible to promote competitiveness for office as well as competitiveness in the marketplace.

Market competition is an essential step toward prosperity, but it is not sufficient. When authoritarian leaders face a choice between promoting growth at the expense of losing office or protecting themselves in office at the risk of slowing growth, they can be expected to choose to slow growth. The Chinese leaders did just that when they used force to put down the democracy movement in Tienanmen Square. They are doing that again today through their harsh oppression of the Falun Gong movement. The same pattern can be discerned in Iraq, North Korea, the Congo, the Philippines under Marcos, and everywhere else that leaders depend on bribing supporters to stay in office.

Authoritarianism is especially conducive to political stability, at least in the sense of long-lasting leaders. Sometimes such leaders make use of discretionary resources to encourage growth, but more often they use those resources for their own benefit. When politicians depend on few supporters and the risks for supporters from defecting to a political rival are high, so too are the incidence of corruption and kleptocracy. Neither of these characteristics is conducive to growth, though both are closely tied to political stability.

The International Monetary Fund, the World Bank, and the United States government have frequently shown a reluctance to use their economic leverage to promote political reform. When economic crises arise, the international financial community frequently comes through by bailing out the ailing economy. The idea too often is that, once the financial crisis is past, the politicians will be better able to put their economic and political house in order. This view is prompted by the mistaken idea that leaders are interested in national welfare even if it comes at the expense of their personal political well-being. As nice a thought as this is, it is a poor basis for policy. Economic crises provide the opportunity to pressure corrupt regimes to mend their political ways by changing their institutions as a prerequisite for economic assistance. If we fail to capitalize on these opportunities, we can expect cycles of economic crises, bailouts, forgiven debts, and new economic crises to continue into the indefinite future.

Notes

1. For a detailed study of this issue, see Bruce Bueno de Mesquita and Hilton Root, eds., *Governing for Prosperity* (New Haven: Yale University Press, 2000).
2. See, for instance, G. Debreu, *The Theory of Value* (New York: John Wiley, 1959); Richard Arnott, Bruce Greenwald, and Joseph E. Stiglitz, "Information and Economic Efficiency," *Information Economics and Policy* 6 (1994): 77–88; Bruce Greenwald and Joseph E. Stiglitz, "Externalities in Economies with Imperfect Information and Incomplete Markets," *Quarterly Journal of Economics* 101 (1986): 229–64.
3. Congressional Budget Office, *The Role of Foreign Aid in Development* (Washington, D.C.: Government Printing Office, May 1997), pp. 11–13.
4. This section borrows heavily from the collaborative research I am involved in with James D. Morrow, Randolph Siverson, and Alastair Smith.