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Democracy and Economic Development: A Comparative Analysis

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Abstract Modern-day economics is greatly influenced by the political landscapes, and the modern politics are largely reliant on the economic situation of countries. Both the terms are interlinked and each variable has complemented the other at every historical instance since the industrial revolution. The paper sketches multi-variate analysis on the different aspects of democracy and economy with regards to institutional development and the new political economy. The paper further tries to find the positive and negative implications of democracy on economic development and vice versa. The study will also provide arguments on the successes and failures of economic institutions on the democracy. The antithesis from the realist sociologists and political scientists is provided in each section in the literature review. The paper further analyzes how geography, demography, and history shape democratic and economic institutions, and why democracies never drive economic development in some countries and bear fruitful results in the other countries. The study will then conclude with the analysis on what kind of democratic institutions are favorable for economic development and what kind of political institutions impede economic development.

Keywords: Democracy, Modern Politics, Industrial Revolution, Economic Institutions, Geography

1 Introduction

Democracy and economic development are two of the most important concepts in the modern world and have either been idealized as entirely intertwined or completely estranged by sociologists, political scientists, and the masses from various schools of thought for a long time. In definition, democracy is a system of government in which power is vested in the people, usually through regular free elections. Economic development, on the other hand, refers to the process of improving the economic well-being and quality of life for a community or country. The relationship between these two concepts is a complex one, with some arguing that democracy promotes economic development while others argue that it hinders it. The idea of democracy can be traced back to ancient Greece, where it was first implemented in the city-state of Athens. However, it wasn't until the 18th century that democracy began to gain traction as a form of government. The American Revolution and the French Revolution were both instrumental in spreading the idea of democracy throughout the world. Since then, democracy has become the dominant form of government, with most countries now claiming to be democratic in some form or another. Economic development, on the other hand, has been a more recent concept, with the term first being used in the early 20th century. Theoretically, it refers to the process of improving the economic well-being and quality of life for a community or country. This can be achieved through various means, such as increasing GDP, reducing poverty, and improving access to healthcare and education. Economic development is often seen as a necessary condition for achieving social and political stability, as well as improving the overall standard of living.

2 Literature Review

The relationship between democracy and economic development and the way they shape the economic and political landscape of countries has been a subject of much research and debate in the academic community. Historical occurrences indicate that both are deeply intertwined. The post-World War II period in Western Europe clearly indicates how democracies strengthened economic growth in those countries. After the war, Western European countries such as Germany and Italy transitioned to democracy and experienced rapid economic growth, known as the "economic miracle." This was due to a combination of factors, including the protection of property rights, the rule of law, and a stable political environment provided by democracy. The success of these countries in achieving economic growth and development while maintaining democratic governance is long being used as an example of how democracy can promote economic development. Another example is South Korea, which transitioned to democracy in the 1980s and experienced rapid economic growth. South Korea's democratic government was able to create a stable political environment, which attracted foreign investment and promoted economic growth. In the Arab world, Tunisia transitioned to democracy in 2011 after the Arab Spring, and since then has experienced economic growth and development. The democratic government has been able to create a stable political environment, which has attracted foreign investment and promoted economic growth. It illustrates how democracy can change fortunes of third-world countries when applied with continuity.

On the other hand, there are many examples where democracy has hindered economic development. One such example is Argentina, where the democratic government has struggled to achieve economic stability and growth. The country has been plagued by political instability, corruption, and a lack of long-term planning, which has hindered economic development for a long time. Another example is Venezuela, where the democratic government has struggled to achieve economic stability and growth. Despite having vast oil reserves, the country has experienced hyperinflation, a shortage of basic goods, and a decline in the standard of living. This can be attributed to a combination of factors, including government mismanagement, corruption, and a lack of property rights protection. African countries are known for their intermittent military rules and many theorists suggest that democracy has failed in most of the countries in Africa. For example, Zimbabwe is among the relatively democratized countries in Africa, however, the lack of democratic governance has led to economic decline and poor living standards for citizens.

2.1 Political & Economic Institutions

Institutions are defined as "the set of rules and norms established by society to structure exchanges in the economic, political, and social domains" (Abrutyn and Turner, 2011). These institutions are further classified into two categories: formal and informal.

Formal institutions are written rules and regulations that are officially enforced by the state or its organs. These include laws, economic policies, and political regulations that govern society. They are explicit and are legally binding, meaning that individuals are held accountable for their actions and can be punished if they violate these rules. Examples of formal institutions include the judicial system, government agencies, and financial institutions.

Informal institutions, on the other hand, refer to the customs, conventions, and norms that are implicit in society. These are not written down and are instead passed down through tradition and socialization. They are not legally binding and are instead upheld by social norms and the expectations of the community. Examples of informal institutions include traditions, customs, and social norms that shape behavior and decision-making within a society.

2.1.1 Formal Institutions

Acemoglu et al. (2005) in their research, divide formal institutions into two types: economic institutions and political institutions. Economic institutions refer to the rules and regulations that govern the economy such as property rights, contract enforcement, and the rule of law. They shape the incentives and opportunities for economic actors and shape how markets function. Political institutions, on the other hand, refer to the rules and regulations that govern the political sphere such as elections, political parties, and the separation of powers. They shape how power is distributed and exercised within a society and how public policies are made and implemented. The distinction between economic and political institutions is important as they interact with each other and shape the overall functioning of a society. There are many types of political and economic institutions. The political institutions comprise presidential systems, parliamentary systems, federal systems, and authoritarian systems. Types of economic institutions include market-based systems, planned economies, and mixed economies as the widely adopted systems.

2.2 The Political Economy

The political economy is a modern concept of analyzing and interpreting the interactions between the economic and political spheres. The "new political economy" integrates political decisions or indecisions with the national and regional economic affairs. The public management, which is a purely administrative affair is summed up with economic factors, such as unemployment and purchasing power parity. The success or failure is gauged on the satisfaction levels of the citizens in that country or region. The theory develops an understanding of how policies by the governments make or break the economic growth. The theoretical framework of political economy also aims to understand the choices of leaders when making collective choices.

The politicians, bureaucracy, and sometimes, the military generals are the main actors that are responsible to drive political economies of their respective countries. The study will generalize politicians as the main custodians of driving national and regional political economies. Politicians are individuals who are elected or appointed to hold positions of power and influence in government. Politicians make decisions and implement policies that shape the direction and growth of a country's economy. They are also responsible for cohesion within the government, creating laws, management of government institutions, and acting as binding forces between different colliding groups or institutions. Moreover, politicians must represent national interests in international relations on behalf of the citizens. Politicians also play a central role in shaping public opinion and are responsible for communicating their vision and policies to the citizens. Politicians may belong to various categories, such as liberals, who deliver progressive policies, support free markets, and limited government intervention in the economy. The conservative politicians, however, uphold traditions, seek powerful military, and do not interfere excessively in the free markets. The authoritarian politicians favor governance with an iron fist, suppress civil liberties, quash human rights, and control the markets. Populism is the newer challenge to both the democracy and economic development. Populist leaders offer impracticable solutions for the fundamental political and economic ills and gain instant popularity among the masses. They create distrust among the citizens and often follow an anti-elitist, anti-corruption narrative. These politicians shape the economic policies of the country.

2.3 How Democracies Favor Economic Development:

2.3.1 Individual & Collective Rights

The protection of individual and collective civil rights relates to the quality and strength of national institutions. Among many, the democratic institutions offer the best guarantee for property rights (Acemoglu and Johnson, 2005). Scholars believe that democratic systems establish institutions that provide a framework for protecting and enforcing property rights. Also, democratic governments are able to effectively manage conflicts that may arise in a dynamic economy, and the democratic systems have all-encompassing mechanisms in place to limit predatory behavior by both the state and private actors. However, they also note that the positive democratic effects on individual and collective property rights are dependent on the sustainability of the political institutions. It is also known from history that new or unstable democracies may see a deterioration incivil liberties and property rights.

2.3.2 Political Stability

Political stability is among the vital elements for promoting economic expansion and drawing in investments. An unsteady political climate creates ambiguity about future decisions and deters potential investors from committing to projects. Studies indicate that the type of political regime plays a significant role in determining political stability, with democratic institutions being viewed as the most reliable for maintaining stability (Apergis, 2017). One of the main advantages of democratic governments is their transparent process for the rotation of parties in power. Unlike autocratic regimes, which frequently resort to unconstitutional practices in controlling the state of affairs and clinging to the power, democratic governments are open to suggestions and debates on the national and administrative issues that discourages extremism and unlawful modes of governance. This leads to peaceful and predictable transfers of political power, which helps to maintain stability.

Democratic regimes also have institutional limitations that restrict the power of political decision-makers, providing visibility and stability in economic policies. This is in contrast to autocratic regimes, where economic policies can be unpredictable (Siegle et al., 2004). Democratic systems provide a sense of continuity and reliability, reducing the potential for upheaval during transitions of power (Ghardallou and Sridi, 2019). This can result in longer time horizons for government policies and better economic choices, which can attract both domestic and foreign investors. While democratic institutions are not a guaranteed solution, they are considered the best guarantee for political stability and economic growth. More notably, the stability of the political administration is a crucial factor in the successful implementation of democracy and its associated benefits. Inexperienced political institutions, such as new democracies, may see deterioration in the structure of property rights. Therefore, the permanency of the political order is crucial for the successful implementation of democracy and its associated benefits.

2.3.3 Standard of Living

In democratic regimes, the development of human capital and standard of living is enhanced through greater public spending on necessary facilities i.e., education and health (Ghardallou and Sridi, 2019). This is due to the state financing of these areas, which is heavily influenced by redistribution policies. According to the Saint-Pail and Verdier’s endogenous growth model (1993), these policies, shaped by political competition and the preferences of the median voter, lead to a greater focus on the needs of the population and an increase in redistribution requests. These requests improve the supply of public goods, including the education system, and lead to improvements in the quality of life and health of citizens. In contrast, autocratic governments tend to avoid redistribution and may even oppose the provision of public services, prioritizing personal gain over the well-being of citizens. This results in a lower standard of living and less access to education for the population. Democracies also promote innovation, which ultimately raises the living standard. It drives long-term growth and decentralize the power system to enhance public spending on technology and innovation, which will result in advancement and create more opportunities in the system. New ideas dismiss the older ones and result in broader thinking patterns in the decision-makers as well as the public (Halperin et al., 2005). The technological advancements adopted by the Western European countries resulted in economic productivity, which ultimately caused democracies to flourish. All these factors then contributed to raising human standard of living in those countries. In authoritarian regimes, civil liberties are curtailed, which repress innovation and create barriers in the way of science and technology (Knutsen, 2011). Competition is constricted and institutions stagnate in the long-term, which in turn halts economic development.

2.4 How Democracies Impede Economic Development

Democracy and economic development is not always taken in positive and utopian context. The fruits of democracy and its relationship with short- and long-term economic growth have been questions infinite times by various sociologists, political scientists, and dictators as well. The argument holds that autocratic governments are better able to focus on long-term goals and implement policies that align with optimum economic choices. They are not constrained by the need to negotiate with pressure groups and can make decisions that benefit society as a whole. In contrast, democratic governments are often focused on short-term objectives and re-election, and may not have the capacity to implement significant reforms. Additionally, democratic regimes are subject to popular demands for immediate consumption, which may reduce the scope of opportunities, such as investments and exports. Critics argue that this can result in a deterioration in property rights and a lack of incentives for investment, which can negatively impact growth. Others argue that an "enlightened dictatorship" would be a better political regime, one that supports economic freedoms while repressing individual political freedoms.

For example, China has been able to achieve significant economic growth under an autocratic government. Under the leadership of Deng Xiaoping, China was able to implement policies that were favorable to investors and were purely market-oriented. These policies, despite the autocratic institutions led to rapid economic growth and modernization. Similarly, Singapore has also been able to achieve high levels of economic development under an autocratic government, with policies that focus on long-term growth and development. On the other hand, democratic countries like Pakistan, Venezuela, and Zimbabwe have struggled with economic development due to populist policies that have led to a lack of investment and a deterioration in property rights. These examples suggest that autocratic governments may be better able to achieve economic development, while democratic governments may struggle to implement policies that support long-term growth.

3 Methodology

The modern-day literature provides unprecedented knowledge and research material on the nexus between democracy and its impact on development. With various interpretation and schools of thought on the subject, the literature reviewed multivariate studies and analyses regarding the subject. To compare and contrast the positive and negative impacts of democratic institutions, the joint historical cross-national analyses are extracted from the most recent research journals. The other models from which the results were extracted include various models on exogenous economic growth, related theoretical models on democracy and political processes, causal analyses, and conclusions from square-autoregressive models. The research articles were compiled from various sources, including Google Scholar, JSTOR, Journal of Knowledge Economy, American Political Science Review, Cambridge University Press, Taylor & Francis, and more. Statistical data is not included in the study as it would have made the study lackluster. Instead, the study summarized various theoretical & quantitative models, and compiled them with the most recent or fitting examples. The research design included comparative analysis of democracy and economic development, institutions responsible to enhance or impede the variables involved, novel studies linking both the subjects, causal relationships between the two fields of study, along with advantages and disadvantages of democratic institutions in propagating economic development.

4 Results & Analysis

Democracy and economic growth are extremely important indicators to analyze the nation’s accomplishments and failures. It has been largely established that democracy promotes economic development by providing a stable political environment and protecting property rights. In democratic countries, citizens have the freedom to pursue economic opportunities, and the government is accountable to the people, which reduces the risk of corruption and abuse of power. Additionally, democratic countries tend to have stronger institutions and a more transparent legal system, which can attract foreign investment, promote technological innovation and economic growth. On the other hand, some others believe that democracy can hinder economic development by leading to political instability and corruption. In partially democratic countries of Africa and South Asia, there is often a constant struggle for power, which can lead to policy uncertainty and a lack of long-term planning.

In some completely democratized countries with liberal values, such as in the United Kingdom, it is said to have vested too much power on the shoulders of the general population, which led to hinder the economic stability and social security, as witnessed in the Brexit referendum. Additionally, populist leadership policies, such as high taxes and wealth redistribution can also discourage private investment and slow economic growth in democracies worldwide. Furthermore, democracy can also lead to a lack of decisive leadership, which can lead to slow decision-making and a lack of progress on important economic issues. In addition, economic development also has a causal relationship with democracy. Economic growth can lead to increased political participation and representation, as citizens have more resources and access to education, and are more aware of their rights and liberties. However, economic inequality can lead to decreased political participation and representation, as citizens who are struggling economically are less expected to protect their civil and collective rights, and may not have the resources to participate in the political process.

Conclusion

Democracy and economic development are closely linked and often work together to improve the overall well-being of a society. Economic growth can accelerate democratic institutional growth and vice versa. This is often seen in developed countries where democratic institutions are well-established and the economy is strong. However, in developing countries, the relationship between democracy and economic development can be more complex. In some cases, economic development may proceed faster in countries with authoritarian regimes, as these governments have more control over economic policies and can make decisions more quickly and efficiently. However, in the long run, democratic institutions are necessary for sustainable economic development. Authoritarian governments can often lead to economic inequality and lack of transparency, which can stifle innovation and investment. Additionally, the lack of political freedom and human rights in authoritarian regimes can lead to social unrest and instability, which can ultimately harm economic growth. On the other hand, democratic societies are more likely to promote economic growth and development in the long-term. Democratic governments are accountable to their citizens and are more likely to respect individual and collective rights, promote social justice and provide equal opportunities for all citizens. This in turn creates a more stable and conducive environment for economic growth and development. In order to achieve long-term economic growth and development, it is important to establish and maintain democratic institutions. This will ensure that economic policies are implemented in a transparent and accountable manner and that citizens have a say in the decisions that affect their lives.

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