Carl Henrik Knursen, University of Oslo & V-Dem co-Principal Investigator

Characteristics of the Private Sector and Democracy

KEY FINDINGS:

- *Investing in capital and technology improvements in the private sector in poor democracies is likely to help protecting them from breakdown.*
- *Regulations on the influence of money in democratic politics, and thereby possibilities for undue exercise of power by business elites, can improve democratic quality.*
- *Diversifying the private sector in natural resource intensive or agricultural economies, can help chances of democratization*

Several studies on democratization and democratic resilience suggest that characteristics of actors in the private sector affect democratic outcomes. With "the private sector", we refer to firms, investors, workers, and other economic agents who engage in production in entities that are not owned, or otherwise directly controlled, by the state or other government units. In most countries today, the private sector accounts for the majority of economic investment and production. Hence, studies concerning how democracy is influenced by the effectiveness, volume, and nature of economic production, or the distribution of income to different groups, are relevant to consider; private sector characteristics affect these features, which, in turn, affect democracy.

One relevant relationship, which is widely discussed in the democracy literature, is the so-called modernization hypothesis (Dahlum 2018). It suggests that economically more developed countries are more likely to become democracies, and stay democratic. In particular, many studies have assessed the link between GDP per capita and democracy. Researchers today agree that higher GDP per capita – which is strongly related to more capital-intensive and technologically efficient private sectors – is positively correlated with democracy, but are in less agreement on why this is so. One predominant position, backed up by several statistical studies (e.g. Przeworski et al. 2000; Rød et al. 2019), is that high GDP per capita mitigates the risk of democratic backsliding, but that it is not clearly related to democratization episodes. In other words, a more capital-intensive and

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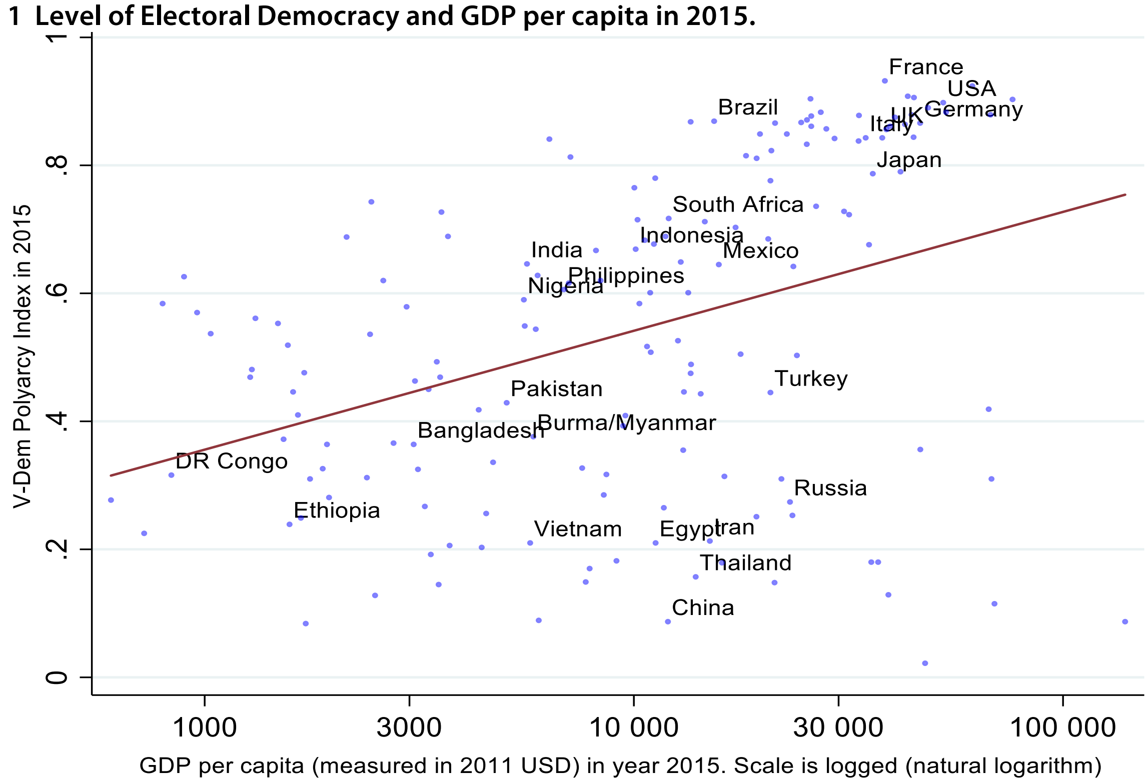
efficient private sector may – for various reasons, including more structural differentiation and trade or the need for better educated workers, who are also better able to organize for defending democracy – help safeguard existing democracies. Investing in capital and technologies that increase the level of development is therefore likely to help protect and stabilize poorer democracies.

One possible reason for the lacking relationship with democratization episodes, is that the higher tax revenues stemming from the higher GDP can be used by autocrats to co-opt threats and increase repression, thereby mitigating risks for regime change (Kennedy 2010). Still, one should note that other studies have found that GDP per capita was positively related to democratization in certain historical periods, especially before WWII, when the international system and production technologies were very different (Boix 2011).

Moreover, the development-democracy relationship may depend on which aspect of democracy we consider. A recent study, using disaggregated V-Dem data, found a clear relationship between development and the electoral component of democracy, but not between development and other components of broader understandings of democracy. The explanation is that development enhances the power resources of citizens and elections provide a focal point for collective action for these citizens (Knutsen et al. 2019).

Fig. 1 Level of Electoral Democracy and GDP per capita in 2015.

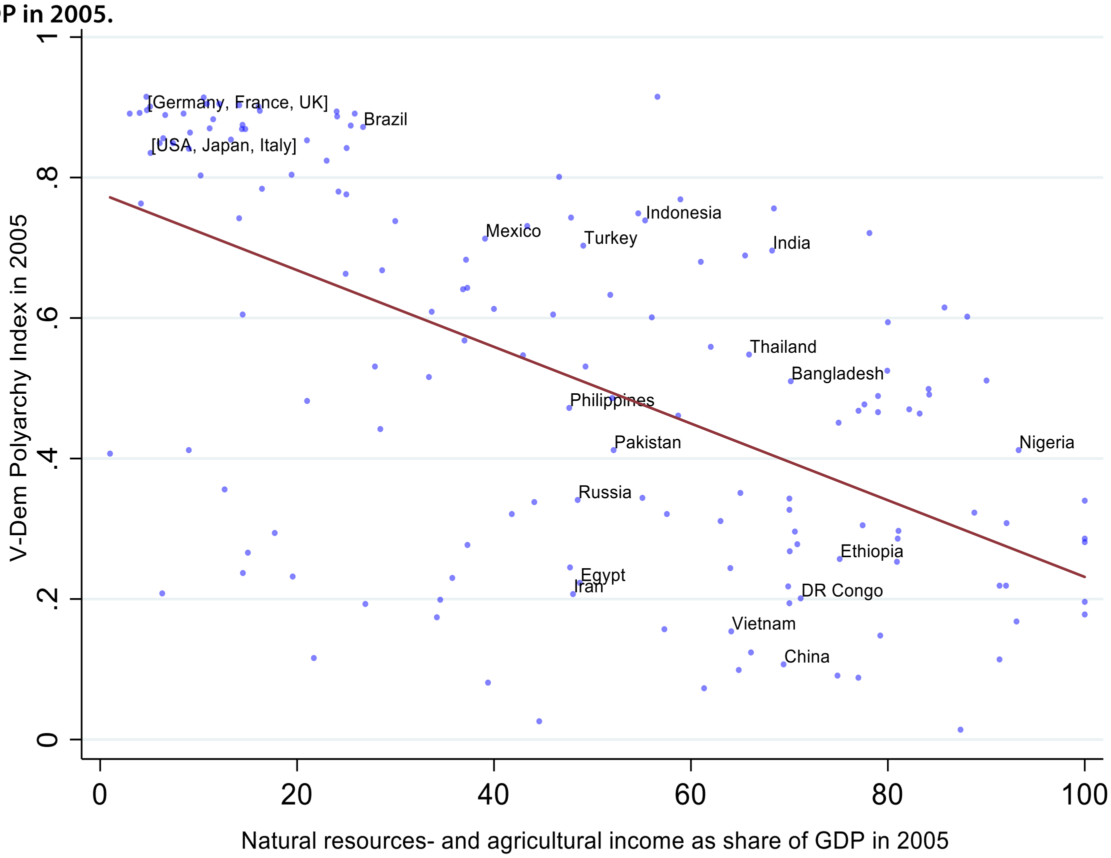


Note: *Data are from V-Dem (Coppedge et al. 2018). Only countries with population above 50 million are labelled. The line represents best fit from a linear regression (Pearson's r = .38).*

Figure 1 shows the placement of countries in 2015, on both GDP per capita (x-axis) and V-Dem's measure of electoral democracy (Polyarchy index; y-axis). The figure exemplifies the fairly strong, though far from perfect, positive correlation between income and democracy. Some large deviations from this overall trend (in the lower-right corner) are very rich but autocratic countries such as United Arab Emirates, Qatar, Equatorial Guinea, and Saudi Arabia. These deviations -- mainly major oil and gas producing countries -- illustrate that not only income level, but also what the source of this income is, matters for democracy. In other words, not only the volume and efficiency, but also the particular type of private (and public) sector production matters.

This point is further highlighted by **Figure 2**, which displays a clear negative relationship (in 2005) between electoral democracy (V-Dem's Polyarchy) and share of economic production coming from either natural resources extraction or agriculture – two sectors that academic studies have highlighted are particularly harmful to democracy.

Fig. 2 Level of Electoral Democracy and Income from Natural Resources and agricultural production as share of GDP in 2005.



Note: *Data are from Coppedge et al. (2018) and Miller (2015). Only countries with population above 50 million are labelled. The line shows best fit from a linear regression (Pearson's r = -.58)*

Natural resources have been found to hurt chances of democratization and democratic survival for several reasons. One is that they represent a source of revenue where assets cannot be moved abroad. Private sector production in areas where capital is immovable may hurt democratization chances because economic elites, under such conditions, will fight hard to avoid democracy and the related higher tax rates (Boix 2003). Another reason is that natural resource dependent economies are often very homogeneous in terms of production structure and number of goods produced. Under these conditions, private sector business owners have more uniform interests, enabling them to organize and coordinate a hold on political power within their narrow circles (Olander 2019).

The same arguments pertain to many agricultural economies. In such economies, elites mainly have immovable assets (land) and are concentrated on a few types of production and thus have convergent interests. The incentive to maintain autocratic regimes are perhaps particularly strong for landowning elites, e.g. plantation owners, who depend on cheap agricultural labor (Albertus 2017). In addition, the type of private-sector workers (i.e., peasants) that exist in agricultural economies are typically less able to mobilize effective challenges against autocratic regimes than workers in industrial or service-intensive economies (Dahlum et al. 2019). Hence, studies find that a high share of national income coming from agriculture, or various other measures of strong land-owning elites such as high land inequality (Ansell and Samuels 2015), predict lower chances of democratization.

Regulations on the influence of money in democratic politics, and thereby possibilities for undue exercise of power by business elites, can improve democratic quality.

Helping to diversify private sector production in autocracies, especially in natural resource intensive or agricultural economies, improve chances of democratization

Could the latter finding reflect, more generally, that high economic inequality – and thus private sector production where capital owners earn a high share of total income – is bad for democracy, independent of whether production takes place in the agricultural sector or manufacturing and service sectors? While plausible arguments suggest that high income inequality mitigates chances of democratization (e.g., Boix 2003), empirical support is mixed, at best. Some studies find that high capital-labor income inequality in the manufacturing sector hurts the durability of existing democracies, but are unrelated to democratization (Houle 2009). Yet other studies fail to find clear support for either relationship (Knutsen 2015).

Recent arguments help shed light on the puzzling lack of a robust relationship with inequality. Ansell and Samuels (2015) propose that certain rich elites, notably urban and industrial business owners, value democracy because it helps protect them from expropriation by autocrats. Albertus and Menaldo (2018) note that business elites may want to substitute autocracy for democracy if they are able to shape institutions and control political processes under the new democracy. When private sector business owners are powerful, they may sometimes work for democratization, but then democratization towards an elite-controlled democracy. Even in wealthy and well-established democracies, high inequality and the strong influence of private business interests in political processes, for example via lobbying parliamentarians or funding presidential campaigns, may mitigate broader popular control over political decision making, and thus the quality of democratic processes (Przeworski 2011). In the end, available evidence (e.g., Knutsen et al. 2019) suggests that a more diversified economy and higher level of development increases the chances of maintaining a high-quality democracy.

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