Political Economy

- How do economic factors shape political outcomes?
  o How do economic institutions affect politics?
  o Unemployment, inflation, and economic growth affect government policies and survival
  o Do market dynamics undermine or enhance democratic consolidation?
- How do political factors shape economic outcomes?
  o How do political institutions affect economic policies?
  o Do democratic institutions advance or hinder market functions?
  o How do states regulate markets?

Role of Ideology

- Social democracy v. liberalism
  o Normative debate over how political institution should regulate economic activities
  o Empirical debate over how well markets function with or without regulation
- How do ideologies influence political and economic aims?
  o Ideologies define what values are sought (equality v. freedom)
  o Ideologies influence interpretation of outcomes
    ▪ Do states with extensive regulation and taxation grow faster or slower than others?
    ▪ Do states have more or less inequality than others?
    ▪ What are the effects of inequality?
“Modernization” and Development Pathways

- Do stages of development influence political outcomes?
  - Early developers: US, UK, France
  - Middle developers: Germany, Japan
  - Late developers: Russia, China
  - Late, Late (experimental) developers: India, Mexico, South Africa, Iran

- Modernization
  - Generic view: state will move toward higher levels of economic development, especially industry rather than agriculture
  - Teleological view: states are progressing toward industrialized, market democracies
    - Process may be uneven
    - How to assist modernization?
  - Criticisms of teleological view
    - Rules out alternative political and economic systems
    - Developmental pathways are more varied
CPE: Early Developers/ Advanced Industrialized Democracies

Ideological Tension Between Social Democracy v. Liberalism
- SD: equality and egalitarian values
- L: equality of opportunity and limits on state infringement on citizens’ liberty
- Struggles over which ideology should prevail

Future of the Social Welfare State
- L: welfare state too large
- SD: welfare state should be reformed, not eliminated
- What “welfare” should be withdrawn?
  - National health-care systems
  - Unemployment insurance
  - Retirement pensions
  - Income subsidies
  - Housing construction and subsidies
  - Agricultural subsidies
  - Higher education subsidies and loans

Graying of populations
How to provide pensions and health-care to retirees?
- retirees as % of pop. increasing
- workers as % of pop. decreasing
- tax burden on workers will increase given current benefit levels
- Policy options
  - cut benefits
  - raise taxes
  - increase # of workers: encourage immigration
Political Effects on Economic Policies and Outcomes

Do democratic policies produce higher inflation levels?

- Hypothesis is that public will demand more government spending and high-employment policies
  - Governments will spend excessively and trade higher inflation for lower unemployment
- recent study (Desai, et al) finds that inflation levels vary based on inequality, 1960-1999
  - low inequality countries have lower inflation rates
  - high inequality countries have higher inflation rates
  - when Gini coefficient is below, .40, then democracy restrains inflation
- In part, poor will demand greater government spending when income inequality is high

Do democracies tax more than dictatorships?

- concern was that democracies were less capable of taxing than authoritarian regimes
- advanced democracies do tax more than advanced dictatorships
  - 31.5% of GDP in democratic countries with per capita income > $7,000
  - 18.5% of GDP in non-democratic countries with per capita income > $7,000
  - but most rich non-democracies are rentier states
- overall, democracies in general do not tax much more than non-democracies
Labor and Welfare Reforms in Germany
- in Germany, Schroder’s “Agenda 2010” program (SDU)
  - small firms can fire employees at short notice
  - long-term unemployed will face penalties for refusing lower-paying jobs
  - income tax cut but tobacco tax raised
  - Liberal*-oriented Christian Democratic Union (CDU) wanted greater restrictions on collective bargaining rights
  - Bundestag vote was close (306 v. 291)
- Germany has 12% unemployment
- Germany is violating EU Euro-zone rules that budget deficits do not exceed 3% of GDP (3.3% for 2002)
  - France exceed deficit in 2002 at 3.2% and in 2003 at 4.1%
- Public divided: CDU preferred over SDU in recent polls
  - 58% said reforms were wrong, and 93% said they were insufficient to solve the problems

Service Economy and Trade-offs
- declining manufacturing employment as % of economy
- weakens labor unions in manufacturing sectors
- mass service employment often temporary and with lower wages

Taxation Systems
- US has more progressive tax system v. Europe
- … but US devotes less to income redistribution
- 1991-97: US taxes drew 31% of capital income v. 20-24% in Europe
- 25-33% of GDP is devoted to social transfers in Europe v. 14% in US
- Europe trades more regressive taxes for more state-directed income redistribution