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Political competition, electoral participation and public finance in 20th century Latin America

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ABSTRACT

Rational choice models predict that political competition and political participation have opposite effects on the size of government. We investigate these theories using data from a panel of 18 Latin American countries during the 20th century. Our research builds evidence for the prediction that reforms enhancing political competition tend to limit the size of government, while reforms increasing political participation tend to increase the size of government. Furthermore, we find that reforms which remove literacy requirements from franchise laws are associated with governmental expansion, while changes in women's suffrage laws have no impact on the size of government. Our findings demonstrate the empirical relevance of the distinction between political competition and participation.

1. Introduction

The role of political institutions as the drivers of specific policy choices and more profoundly, as determinants of economic development, has been the subject of intense theoretical and empirical investigation in recent years (e.g., Acemoglu and Robinson, 2006; Boix, 2003; Persson and Tabellini, 2003; Klomp and de Haan, 2009). At least since Dahl (1971), the idea that political institutions are pivotal players in ensuring economic and social outcomes has enjoyed widespread support. Yet, explaining how political institutions wield their influence has remained a nebulous endeavor. We know that institutions regulate the exact parameters of citizenship rights, determining who votes and how. We know that institutions regulate the degree of competition among factions for political power. And we know that institutions determine the autonomy of the legislature and court system. What we don't understand fully is how the different design of these political institutions impact economic and social outcomes.

Crucial to building more clarity in our understanding of these fundamental issues is the distinction between electoral participation and political competition. This distinction is implicitly or explicitly embodied in many definitions of democracy (e.g., Powell, 1982; Przeworski et al., 2000) but is also employed in analysis of broader regime types, as demonstrated, for example, by Wintrobe's work on dictatorships (Wintrobe, 1998). Electoral participation and political competition also figure prominently in theoretical research. In Meltzer and Richard (1981), for example, the political inclusion of hitherto disadvantaged or

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disenfranchised groups is shown to increase the demand for distributive public spending and to *expand* the size of government. A contrasting view is provided by Becker (1983) and Wittman (1989) who stress the role that political competition plays in *limiting* the size of government.

This paper builds new empirical evidence on these theoretical propositions. We show that electoral participation and political competition have very different implications for the size of government and for the tax structure. We contribute to the existing empirical literature, which isolates the effects of either political competition or electoral participation,[2] by studying the two dimensions jointly.

The setting for our study is the particularly fecund political climate of Latin America. Indeed, 20th century Latin America provides an almost perfect laboratory for testing hypothesizes about political institutions. For example, since independence, Peru has changed or modified its constitution 13 times; Chile has modified its constitution 11 times, while Brazil and Colombia have made 8 and 12 changes, respectively. These institutional fluctuations not only reflect shifts in the allocation of voting rights and thereby the scope for electoral participation; but, they indicate repeated vacillations between highly competitive democratic environments and highly autocratic or dictatorial environments with severely limited competitive frameworks. These factors make Latin America an ideal political terrain for exploring through statistical assessment the impact of electoral participation and political competition on fiscal outcomes, in particular on the size of government and on the tax structure.

Our study is two-pronged, first estimating the impact of different competitive and participatory frameworks on fiscal outcomes. Our second objective is to go into more detail about restrictions on electoral participation and to study the impact of electoral literacy requirements and women's suffrage limitations. We believe exploring the outcome of these transitions statistically makes contributions to the ongoing debate about the role of political institutions, and provokes urgent questions about institutional and electoral design. However, we acknowledge the importance of peculiar, local specificities demonstrated in the histories of the 18 countries we study.

Literacy requirements were the most obdurate of Latin American electoral restrictions. By the late 19th century, most countries in Latin America were at least nominally democracies, but with much more restricted voting franchise requirements than, for example, the USA and Canada (Engerman and Sokoloff, 2005). Restrictions could include wealth or income requirements, but most frequently, laws contained literacy qualifications. While most wealth or income requirements were abolished in the late 19th and early 20th century, literacy requirements remained in place in some countries until the 1980s (Engerman et al., 1998). In countries such as Peru, Bolivia and Ecuador, which have sizable, predominant Native American populations with high levels of illiteracy, these restrictions likely served the purpose of keeping an elite in control, and excluding the massive marginalized population from political influence. In a political climate of such divisive restrictions, we build statistical explanations to show how literacy tests restricting the franchise effected fiscal outcomes.

Suffrage restrictions also excluded vast portions of the population from the electoral process well into the 20th century by virtue of their gender. The first country to grant women the right to vote was Ecuador in 1929, followed by Uruguay and Brazil in 1932. Nearly three decades later, Paraguay followed suit in 1961. Restrictions on female participation in the political process in other contexts, e.g., the USA (Lott and Kenny, 1999) and western Europe (Aidt and Dallal, 2008) have been found to affect fiscal outcomes. We examine if similar patterns can be found in Latin America.

Our analysis is based on a panel data set with information on fiscal outcomes (for central government) in 18 Latin American countries for the period 1920 to 2000. We employ the Polity IV index to measure political competition (Marshall and Jaggers, 2007), and turnout in elections and referenda to measure electoral participation (Vanhanen, 2000, 2003b). These choices allow us to track political reforms over long periods of time and exploit the often substantial variation in electoral participation and political competition *within* the 18 Latin American countries. The Polity IV index is sometimes interpreted as a measure of democracy more generally, but, as we shall detail in Section 2, a careful reading of the Polity IV manual suggests that it is more accurate to interpret it as a measure of political competition. Many studies, e.g., Boix (2003, chapter 5), Mulligan et al. (2004), Persson and Tabellini (2006), Kenny and Winer (2006) use a “world” sample that includes as many countries as possible to study the link between fiscal structures and political institutions. The advantage of this is that the variation in institutional differences is maximized, but at the same time, countries included in a world sample represent very different economic, geographical, social and cultural experiences. We believe that the focus on Latin America has the advantage of making the sample more homogenous, as these countries share common cultural and linguistic roots.

We draw three main conclusions from our analysis. First, our fixed effect estimates strongly support the hypothesis that electoral participation and political competition have opposite effects on the size of government. A country that instigates reforms enhancing political competition experiences a fall in government expenditure and taxation in percentage of GDP in the order of 1.7–2.0 percentage points. In contrast, a country that, through franchise reform or otherwise, experiences an increase of 50% of the population who can participation in elections, subsequently witnesses an increase in government expenditure and taxation as a percentage of GDP by approximately 2.0–2.3 percentage points. Second, we find indirect evidence that part of the reduction in the size of government associated with enhanced political competition can be attributed to a reduction in spending on securing and maintaining authority. In short, in environments bereft of political competition, we suggest direct costs are incurred to the government by the elite's attempt to maintain power and control, be it through military or policing measures. Once a more pluralistic, competitive political environment is achieved, the costs of repression diminish. Third, we find that much of the increase

[2] See e.g., Hettich and Winer (1991), Hettich and Winer (1988), Husted and Kenny (1997), Boix (2001), Rogers and Rogers (2000), Aidt et al. (2006), Kenny and Winer (2006), Aidt and Jensen (2009a,b).