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The transparency curse: Private information and political freedom[☆]



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ABSTRACT

I offer a model of the sustainability of authoritarian rule in which the transparency of productive economic activity enables the ruler to distinguish productive economic activity from preparations for rebellion. The less transparent the productive technology the greater the economic side effects of maintaining authoritarian rule, and the stronger the incentives to liberalize the regime. Using a cross section of countries I provide evidence that, consistently with the theory, democratic government Granger causes internet penetration.

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1. Introduction

Authoritarian governments often display hostility to innovation. During Summer, 1933 industrialist Carl Bosch complained to Hitler about the damaging effects on German competitiveness of widespread dismissals of Jewish professors in physics and chemistry. Hitler replied that “Germany could get on for another hundred years without any physics or chemistry at all” (Evans, 2003, p. 426). Indeed history is replete with examples of governments that repress productive activity out of concern about domestic threats to their survival—most dictatorships impose some form of press censorship, notwithstanding the economic costs of restricting the flow of information. In the realm of telecommunications and the internet Kedzie (1997) describes the ‘dictator’s dilemma’: “How to benefit from the global economy without relinquishing domestic control.” He notes that the former Soviet Union severely restricted telephone connections with the outside world, while Saudi Arabia and Singapore wrestle with the tradeoff between the economic benefits of expanded internet connectivity and the threat this poses to their authority. In a cross sectional statistical analysis Kedzie (1997) shows that higher levels of democracy are associated with greater telecommunications density, and especially with more extensive internet penetration, a finding confirmed by Milner (2006).

Authoritarian regimes’ aversion to technology goes beyond xenophobia. Not only did the former Soviet union restrict international telephone connections, it also placed limits on intra-regional connections within its borders, and it even

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limited the publication of telephone directories (Pool, 1983)—despite the potential economic costs of such a restriction identified by Jipp (1963). Fleck and Hanssen (2006) note that in Ancient Greece the most productive use of the hilly land in Athens and Argos, city states that liberalized, was olive cultivation, which poses severe monitoring difficulties for third parties. In contrast, on the plains of Sparta and most other city states, cropland could be turned to grain production, where monitoring problems were much easier to solve. Indeed, the regularity that monitoring problems are more severe for perennial crops than they are for annuals persists to the present day (Milgrom and Roberts, 1992). Fleck and Hanssen note further that after Athens was occupied, in the wake of the battle of Chaeronea, olive cultivation lapsed. Fleck and Hanssen argue this decadence of olive tree cultivation stemmed from the conquerors' inability to extract rents from confiscated orchards because, unlike owner/cultivators, the conquerors had to delegate harvesting to slaves. Turning to the modern world, in a cross-national, multi-industry study of technology adoption Comin and Hobijn (2004) find that the implementation of “successor technologies” (e.g. motor ships, which succeeded steam ships, or basic oxygen furnaces that came after furnaces using Bessemer processes) takes place more quickly in countries with more democratic governments.

In this paper I argue that the tendency of authoritarian regimes to limit productive activities is a central feature of their existence: activities that could mask preparations for a rebellion pose a threat to the survival of an authoritarian regime. I present a model in which citizens have private information about their productivity in an autonomous economic activity. There is also a less productive but easier to monitor activity that they could use instead. The difficulty of discerning whether workers are plotting forces authoritarian governments to choose between facing the hazards of allowing citizens to use the productive technology or interfering with the productive sector of the economy to attenuate the risk of being overthrown. The less transparent the activity is, the more dangerous and difficult it is for the government to maintaining authoritarian control rather than liberalizing.

The model identifies conditions under which governments will prefer to relinquish authoritarian control, as did Spanish monarch Juan Carlos, rather than to maintain a remorseless grip on power, as in the case of the Communist Party of Cuba. The authoritarian government is most likely to step down when hidden actions and innovation are important, and least likely when economic activity uses known and easy to monitor technologies.

This paper has the seemingly paradoxical implication that transparency of the production technology, a trait we are accustomed to think of as favorable in a free society, can actually facilitate the persistence of authoritarian rule. This apparent anomaly arises because transparency allows an autocratic government to extract resources more efficiently while suppressing rebellion. The mechanism identified here is somewhat reminiscent of the “resource curse” that posits a link between another favorable condition, large endowments of extractable resources, and the persistence of authoritarian rule. Hence one might refer to the process identified in this paper in which easy to monitor economic activities provide a stable base for authoritarian rule as the “transparency curse”.¹

This model contrasts with the mechanism identified in North and Weingast (1989), in which democracy promotes investment and growth by guaranteeing that investors are represented in future governments, thereby making the commitment not to renege on bonds nor to abrogate property rights more credible. Applications of their insight span a gamut of diverse settings, from the post First World War expansion the franchise in Western Europe (Ticchi and Vindigni, 2003), to the adoption of new technologies (Comin and Hobijn, 2004). Notably, Acemoglu and Robinson (2006) argue that extension of the franchise is crucial to locking in governments' commitment to egalitarian income redistribution.

Another strand of the political economy literature is characterized by Fernández and Rodrik (1990) who note that individuals threatened by reform, or by innovation, will lobby to block the change. While that paper is couched in terms of a proposed Pareto improving tariff reform it applies equally well to cases in which users of a *status quo* production process lobby to block the introduction of a successor technology. Comin and Hobijn (2004) link the Fernández and Rodrik model with regime type by arguing that it is easier for incumbents to bribe a dictator to block innovation than it is to successfully lobby a democratic government. Applying the framework of Diermeier and Myerson (1999) one could characterize the Fernández and Rodrik argument as asserting that the “hurdle factor” is equal to 1 for dictatorships, while it is higher for the various forms of democracy.

Looking through a similar lens at the politics of innovation Acemoglu and Robinson (2000) show that interest groups may lobby to prevent technologies that will undermine their political rights, as opposed to harming their economic position as in the Fernández and Rodrik framework.

In the model developed here the limitations on economic activity in an authoritarian context originate with the government, and not with reluctant investors, as in the North and Weingast (1989) model, nor with active lobbying by industry to block innovation as in Fernández and Rodrik (1990) and Acemoglu and Robinson (2000). This leads to somewhat different empirical implications, and I consider these at greater length in the discussion section of the paper.

The next section sets forth a simple information theoretic model of the political economy of production and rent extraction by the government, section three presents an informal discussion of the Perfect Bayesian Equilibria (Fudenberg and Tirole, 1991) for this model, while section four discusses applications of the formal model to understanding regime choice. Section five contains an empirical analysis of the model's implications for the adoption of the internet. A formal statement and proof of the results appears in the Appendix.

¹ In the discussion section of this paper I argue that, given the relative ease with which governments can monitor many extractive activities, the resemblance between the resource curse and the transparency curse is more than superficial.

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