# THE POLITICAL ECONOMY OF LIBERAL DEMOCRACY[*]

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This paper develops a taxonomy of political regimes that distinguishes between three sets of rights—property
rights, political rights and civil rights. The truly distinctive nature of liberal democracy is the protection of
civil rights (equal treatment by the state for all groups) in addition to the other two. The paper shows how
democratic transitions that are the product of a settlement between the elite (who care mostly about property
rights) and the majority (who care about political rights), generically fail to produce liberal democracy. Instead,
the emergence of liberal democracy requires low levels of inequality *and* weak identity cleavages.

Democratic rule has never been so prevalent. Since the fall of the Berlin Wall in 1989, the number
of democracies has risen rapidly and cross-national tabulations suggest that, for the first time in
history, more countries now qualify as democracies than as non-democracies (Figure 1).

While the spread of democracy is something to cheer about, it is clear that this democratisation
has not been accompanied by the spread of the full panoply of rights that we associate with the
established democracies in the West. In a wide variety of democracies, citizens and minority
groups are routinely victims of civil rights violations, subject to harassment and discriminated
against in the courts as well as the supply of public goods such that they do not face equal treatment
by the state.[1] This infringement of civil rights, even though elections remain in principle free and
competitive in democratic countries has puzzled many commentators.[2]

We argue that this failure to protect minority rights and provide civil rights is a readily
understood consequence of the political logic behind the emergence of democracy. Instead, we
make the argument that what requires explanation is not the relative paucity of liberal democracy,
but its existence—rare as it may be. The surprise is not that few democracies are liberal, but
that liberal democracies exist at all. In order to see this, we develop a framework that begins by

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[1] The 2014 Civil Rights and Political Liberties Report (Bertelsmann Stiftung, 2014) reports that in Hungary, 'Roma
and other minorities have become frequent targets of harassment and of hate speech', while in Croatia, the judicial
system 'displays an institutional bias in favor of ethnic Croat suspects'. Similarly, Israel exhibits a wide range of civil
rights violations 'related to minority rights such as those accorded non-Jewish citizens, particularly Arab citizens', while
in Turkey, the Kurdish minority is discriminated against and face 'lengthy pre-trial detention and excessively long and
catch-all indictments'.

[2] As shortcomings of these democracies have become more evident, it has become commonplace to talk about a
'democratic recession' (Diamond, 2015). Fareed Zakaria coined the term 'illiberal democracy' for political regimes
such as these (Zakaria, 1997) and this has been elaborated by Levitsky and Way (2010) who use the term 'competitive
authoritarianism' to describe such regimes. Zakaria and others note that mass franchise emerged in much of the Western
world only after the entrenchment of liberal thought that emphasised individual rights and placed limits on state coercion.
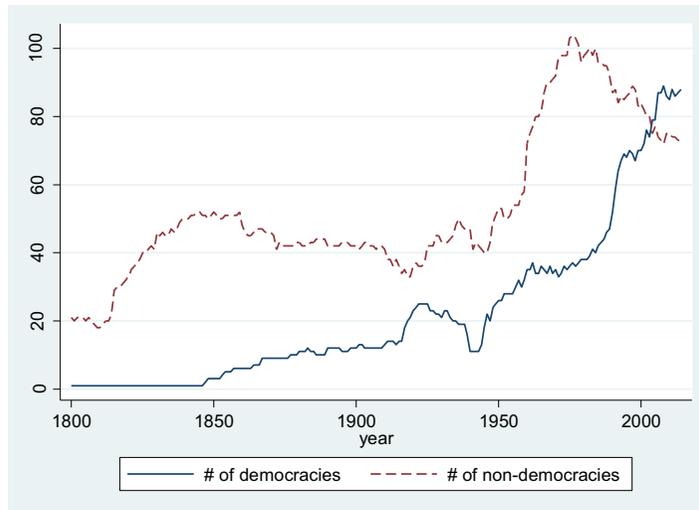
Fig. 1. *Numbers of Democracies and Non-Democracies since 1800.*
*Notes:* Data are from Polity IV (http://www.systemicpeace.org/inscrdata.html). 'Democracies' are countries that receive a score of 7 or higher in the Polity's democ indicator (which takes values between 0 and 10), while 'non-democracies' are countries with a score below 7.

disaggregating the full set of rights we associate with modern capitalist democracies. We focus on three key components: property rights, political rights and civil rights that are defined as follows:

- Property rights protect asset holders and investors against expropriation by the state or other groups.
- Political rights guarantee free and fair electoral contests and allow the winners of such contests to determine policy subject to the constraints established by other rights.
- Civil rights ensure equality before the law as well as non-discrimination in the provision of public goods such as justice, security, education and health.

In our model, each set of these rights has a clear, identifiable beneficiary. Property rights benefit primarily the wealthy, propertied elite. Political rights benefit the majority—the organised masses. And civil rights benefit those who are normally excluded from the spoils of privilege or power—ethnic, religious or ideological minorities.

This disaggregation of rights allows us to provide an analytical taxonomy of political regimes. These political regimes are classified according to the precise bundle of rights that are provided. For instance, in many dictatorships, it is only the property rights of the elite that are protected, while classical liberal regimes protect property and civil rights but not necessarily electoral rights. Similarly, electoral democracies protect property and political rights but not civil rights, while liberal democracies protect all three sets of rights.

Indeed, we take the distinctive feature of a liberal regime to be the restraints placed on those in power to ensure equal treatment of minority groups by the state—in any and all domains where it plays a role. We formally capture these aspects of civil rights, by examining the extent to which an individual's group affiliation affects his public good payoff—be it due to an an absence of

equal treatment before the law or due to discrimination by the state in legal, educational or other domains.

The second key feature of our framework is its emphasis on two societal cleavages. First, there is the divide between the propertied elite and the poor masses. This is largely an economic divide and is determined by the division of land, capital and other assets in society. Second, there is an 'identity' cleavage between what we call a majority and a minority—that may arise from ethnic, religious, linguistic or regional affiliations. Or it may be ideological—as with secular modernisers versus religious conservatives in Turkey, and Western-oriented liberals versus traditionalists in Russia. These two cleavages may align (as they did in South Africa), but more often than not, they will not. Their divergence is what allows us to make an analytical and substantive distinction between electoral and liberal democracy.

In our framework, the government not only taxes its citizens and provides public goods but also (depending on the political regime) makes decisions of whether to selectively discriminate in favour of (or against) any group. Our benchmark model begins with a right-wing autocracy being the historical status quo—the usual scenario throughout the long arc of history. In an autocracy, the propertied elite who control the autocracy protect their (own) property rights and do little else. In the nineteenth and twentieth centuries, processes such as industrialisation, world wars and decolonisation led to the mobilisation of groups that challenged the power of the elites (see Ziblatt, 2006). In line with much of the existing literature (see Acemoglu and Robinson, 2006), it is the threat of a revolution that gives the elite an incentive to obtain a political settlement. Indeed, democracy, when it arose, was typically the result of a quid pro quo between the elites and the mobilised masses.[3] The elites acceded to the masses' demands that the franchise be extended (usually) to all males regardless of property qualifications. In return, the newly enfranchised groups accepted limits on their ability to expropriate property holders. In short, electoral rights were exchanged for property rights.

Our first set of results demonstrates that this political settlement that led to democratisation often excluded the main beneficiary of civil rights—the dispossessed minorities. These minorities have neither resources (like the elite) nor numbers (like the majority) behind them. So they do not have something to bring to the table and cannot make any credible threats. Accordingly, the political logic of democratisation under the threat of revolution dictates the provision of property and political rights but not civil rights. The majority benefits if it receives a preferred treatment by the state (at the expense of the minority), be it in the enforcement of contracts or access to education, law enforcement and other public goods. This makes the majority favour electoral over liberal democracy. Indeed, this is consistent with the emergence of liberal democracy when there is no clear, identifiable cleavage—ethnic, religious or otherwise—that divides the majority from the minority. This may account for the emergence of liberal democracy in early twentieth-century Sweden or more recently in South Korea and Japan.

However, the majority–minority cleavage can work in the other ways too that mitigate the bias against liberal democracy. We show that under some conditions, this cleavage can make the elite favour liberal democracy. We identify two such conditions. First, the elite may support liberal democracy when the income/class cleavage is very deep. This is because the rate of taxation is generally lower under liberal democracy: the majority reaps fewer benefits from redistributive taxation that is required to finance public goods when they have to share public goods with the minority. Second, when the elite's identity aligns with that of the minority, the elite have a direct

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[3] See Acemoglu and Robinson (2006) and also Dahl (1971), Przeworski (1991), Rueschemeyer *et al*. (1992), among others.

stake in civil rights too. In such a case, the elite will seek both property and civil rights as part of the political settlement with the majority. An example of this is the position of the white minority government in South Africa prior to the transition to democracy in 1994.

Finally, we pull together our results to argue that liberal democracy requires quite special circumstances: mild levels of income inequality as well as weak identity cleavages. This is so despite the fact that we give the elite 'agenda-setting' power by allowing it to move first and force the majority to move second. When the class or the identity cleavage is large, either the elite or the majority (or both) prefer alternative political regimes, and the prospects of liberal democracy are thwarted.

There are two main (related) innovations in this paper. First, we unpack the concepts of 'democracy' and 'liberalism' and give civil rights an analytical standing co-equal to property rights and political rights. The conventional treatment of democracy in the political economy literature focuses on the conflict between a wealthy elite and the organised masses (see for example Przeworski, 2005; or Acemoglu and Robinson, 2006). This approach tends to bundle civil rights with political rights. It provides an explanation for the origins of electoral democracy but has little to say on the provision of civil rights, when it takes place. In contrast, standard accounts of the emergence of liberalism tend to bundle civil rights with property rights (Marshall, 1949; Fawcett, 2014). They evade the puzzle of why a society run by liberal elites would provide broad civil rights when the beneficiaries of such rights are predominantly among the non-elites. The political basis for the provision of civil rights has been obscured by both kinds of bundling. In both cases, the result has been the failure to ask the question: where do civil rights come from?

Our focus on civil rights gives rise to our second conceptual innovation—namely, giving prominence to the 'identity' cleavage. This is in sharp contrast to the literature (see below) that focuses on income inequality as a catalyst for democratisation. While inequality is important in our analysis, by giving the identity cleavage a key role in our framework, our framework throws light on not just the comparative politics of democratisation (Horowitz, 1993) but arguably also the recent upsurge of both left and right-wing populism (Rodrik, 2018).

Together these conceptual innovations help provide a parsimonious taxonomy of political regimes, both democratic and non-democratic. We accomplish this by distinguishing among three groups (elite, majority, minority) and three kinds of rights (property, political, civil) associated with various modes of taxation and public-goods provision (who determines the tax rate, who pays the taxes and how the public good is targeted). These distinctions allow us to capture a rich variety of outcomes. The resulting taxonomy should be of independent interest, beyond our focus on liberal democracy.

It is perhaps worth emphasising that our 'interest'-based exploration of the foundations of liberal democracy contributes to (and stands apart from) a large corpus of influential work across a variety of fields. This work has almost exclusively focused on the primacy of 'ideas' in both the creation and the diffusion of liberal democracy. This includes work in political philosophy (Rawls, 2009; Sen, 1999), history (Israel, 2013; Siedentop, 2014) and political science (Fukuyama, 2014).

There is a very large literature on the drivers of democratisation (for an excellent survey, see Ziblatt, 2006). An influential strand emphasises the role of income inequality. Higher inequality increases the threat of revolution. Acemoglu and Robinson (2006) analyse how by offering credible redistribution, democratisation staves off the threat of such a revolution. A different tack is taken by Boix (2003), who focuses on how democratisation is most likely when inequality starts declining, since the elite have less to fear from redistributive taxation. In contrast to its emphasis on inequality, a second important strand in the literature focuses on inter-elite

competition (see also Iversen and Soskice, 2009; and Milan Svolik, 2012). For instance, Llavador and Oxoby (2005) show how elements in a divided elite may strategically use the extension of the franchise to ensure that its preferred policies get implemented (at the expense of the competing elite). Similarly, Lizzeri and Persico (2004) demonstrate conditions under which the elites willingly extend the franchise in order to give better incentives to politicians. Finally, Ticchi and Vindigni (2010) argue that the threat of interstate competition gives countries an incentive to democratise.

This paper is directly related to the small literature that addresses the issue of partial and imperfect democratisation. Acemoglu and Robinson (2008) show how democratisation (in the form of elections) may not change things on the ground. This is because the elite make investments to ensure that the (democratic) government policymaking apparatus remains captured. Similarly, Bidner *et al.* (2016) show how allowing elites a probabilistic share of spoils in the future provides them with an incentive to hold elections, without giving its citizens any of the accompanying rights, i.e., a 'minimalist' democracy. Besley and Persson (2011) develop a framework that shows how in the absence of strong executive constraints, cohesive institutions and state capacity are unlikely to develop.

Our introduction of the identity cleavage makes the present paper quite different and pushes us away from the singular emphasis on class and economic variables for democratisation (see Rokkan, 1970 on European democratisation). Not surprisingly, our framework speaks to challenges of democratisation, in most of the developing world—where ethnic, tribal and linguistic cleavages are present (see Horowitz, 1993). Indeed, these identity cleavages are closely associated with discrimination by the state of politically excluded minorities (see Posner, 2005; Baldwin and Huber, 2010; Alesina *et al.*, 2016; and Hodler *et al.*, 2015, among others).

The outline of the paper is as follows. In Section 1 we first present our taxonomy of political regimes, based on the threefold distinction of rights we just discussed. We next sketch a simple formal framework to help us think through the circumstances under which liberal democracy is adopted. Section 2 examines political transitions. In Section 3 we provide a brief overview of the historical backdrop and case studies of liberal democracy before concluding in Section 4.

## 1. The Framework

We proceed by describing the details of our framework. In the first instance, we describe our taxonomy of political regimes. Informed by this taxonomy, we develop a model that describes the basic structure of the economy and group-specific payoffs. Next, we describe our assumptions about how allocation decisions (on taxes and public-goods provision) are made in different political regimes. Using these two building blocks, we then derive analytically the payoffs that the groups receive under each regime. We will discuss the equilibrium selection of political regimes, that is, how society ends up in one particular political regime in the next section.[4]

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[4] Our framework bears some surface resemblance to Besley and Persson (2011), who study a model with two groups—the government and opposition—and analyse the equilibrium determination of different forms of violence or repression versus civil war. Besley and Persson's treatment of 'repression' as the one-sided infringements of human rights of government opponents represents an extreme form of our violation of minority rights. Also, as in the present paper, their government controls fiscal instruments, which can be of the redistributive or public-goods types. Our paper differs in that we have three players and characterise the set of peaceful political equilibria rather than varieties of violence.

Table 1. *A Taxonomy of Political Regimes.*

| | | Property rights | | | |
| | | No | | Yes | |
| | | Political rights | | Political rights | |
| | | No | Yes | No | Yes |
| Civil rights | No | (1) Personal dictatorship or anarchy | (2) Dictatorship of the proletariat | (5) Right-wing autocracy | (6) Electoral/illiberal democracy |
| | Yes | (3) n.a. | (4) Democratic communism | (7) Liberal autocracy | (8) Liberal democracy |

### 1.1. *A Taxonomy of Political Regimes*

We define liberal democracy as a regime in which civil rights are provided in addition to electoral and property rights. Our view of the provision of civil rights draws heavily on the civil rights movement and associated legislation in favour of equal treatment of blacks in the American South (see Branch, 2013). Accordingly, we view the provision of civil rights as equal treatment of individuals or groups by the state. In other words, what sets liberal democracy apart from electoral democracy in our framework is that an elected government cannot discriminate against specific individuals or groups when it administers justice, protects basic rights such as freedom of assembly and free speech, provides for collective security, or distributes economic and social benefits.[5]

Our taxonomy of political regimes, based on the combinations of property/political/civil rights allows us to distinguish among different types of political regimes. For simplicity, let us assume that we can treat each of these rights in a binary, all-or-none fashion—they are either protected or not. This gives us eight possible combinations in all, shown in Table 1.

A regime in which none of these rights is protected is either a personal dictatorship or an anarchy where the state has no authority (box 1). If property rights are protected but there are no political or civil rights, the regime is under the control of an oligarchic elite and can be described as a right-wing autocracy (box 5). A regime that provides political rights but not property or civil rights would be controlled by the effective majority, resembling perhaps Marx's dictatorship of the proletariat (box 2). A regime that provides only civil rights, on the other hand, is hard to imagine—the only box for which we are at a loss for label (box 3).

Consider now political regimes that provide two out of our three sets of rights. When property rights are missing but political and civil rights are provided (box 4), we get a democratic version of communism—what Marx had in mind for the long run (even though communist regimes turned out quite differently in practice). When political rights are missing but property and civil rights are protected (box 7), we have what we might call a 'liberal autocracy'. Until the extension of the franchise to most males in the late nineteenth century, Britain stood as an example of this

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[5] The equality before the law and the ability to have unbiased adjudication before the courts is an important dimension of civil rights. However, so is equal treatment by the state when it comes to access to public goods such as education, police and public transport. Indeed, much of the civil rights movement in the United States turned on the question of the difficulty of unbundling equal protection under the law (guaranteed by the 14th Amendment) from absence of equal access to public goods such as parks, drinking water, public transport and especially education (see Ogletree, 2004; and Branch, 2013). Nevertheless, a plausible case can be made that among the various dimensions of public-goods provision, in the context of civil rights, perhaps equal treatment before the law is *primus inter pares*.

type of regime. There are few if any contemporary variants (see below). When civil rights are missing but property and political rights are protected, we have electoral or illiberal democracies. As we argued above, a large share of today's democracies, particularly in the developing world, are in this category. Finally, a political regime that provides all three sets of rights is a liberal democracy (box 8).[6] Our focus will be on the circumstances that permit the emergence of this kind of regime, as distinct from electoral democracies.

### 1.2. *Groups and Civil Rights: the Identity and Income Cleavage*

We consider a country where the total population has a mass of $1 + \eta$ and total output is normalised to one. This population is divided across three groups in society. The propertied elite have mass $\eta$, while the non-elite are divided into a majority group and a minority with population shares $n$ and $(1 - n)$ respectively, where $n > 1/2$.[7]

These group divisions are a consequence of two kinds of cleavages in society—an income cleavage and an identity cleavage. The income cleavage distinguishes the wealthy (propertied) elite from the lower income non-elite. This is essentially an economic or class divide. The second cleavage separates the majority from the minority on the basis of some salient identity marker. This marker may relate to ethnicity, religion, language, region or ideology. Obviously, there may be more than one such cleavage but we shall focus on a single identity cleavage, distinct from class/income, to keep things tractable. We will call these two the class and identity cleavages, for short. The identity cleavage can align with or cut across the class cleavage: the elite may share an identity with either the majority or the minority.

These three groups are labelled with the subscript $i$, with $i$ taking one of the three possible values $e$ (elite), $a$ (majority) and $b$ (minority). Members of each group $i$ have preferences $u_i$ that are given by their (after-tax) income $y_i$ and a public good $\pi_i$:

$$u_i = y_i + \pi_i. \tag{1}$$

Here we capture the magnitude of the income cleavage by examining intergroup differences in income. Since the economy's total output has been normalised to 1, the elite's pre-tax/transfer share is given by $\alpha$ and the non-elite's by $(1 - \alpha)$, where $\alpha > 1/2$. In the absence of any taxes or transfers, the income of the elite equals $y_e = \alpha$ and the non-elite majority and minority's is given by $y_a = y_b = (1 - \alpha)$. Accordingly, the size of the income (class) cleavage is given by the gap between $\alpha$ and $1/2$.

The second term $\pi_i$ captures an individual's payoff from a positional public good that captures the magnitude of the identity cleavage. To see this, we index the type of public goods by $\theta \in [0, 1]$, where the three groups' ideal types are given by $\theta_i, i \in [e, a, b]$. The larger the size of

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[6] Our distinction between electoral democracies and liberal democracies relies on the presumption that free and fair elections—the hallmark of electoral democracy—can be separated from equal treatment and non-discrimination—the hallmarks of liberalism. In other words, there may be elections with (in principle) the majority group being in power. However, in practice policymaking may not reflect these majoritarian preferences. Of course, we agree that this distinction between what is *in principle* conceptually distinct and what is *in practice* observed is likely to be fuzzy, but we take it as a caution about the fuzziness in practice between electoral and liberal democracies. We treat electoral democracy as a particular kind of imperfect democracy, where the electoral majority gets to trample on the rights of the minority.

[7] We note a sleight of hand that simplifies our exposition in what follows. Technically, in all our subsequent computations we need to divide total elite income $\alpha$ by its mass $\eta > 0$. It is convenient for expositional purposes to assume this mass $\eta$ is arbitrarily close to (but less than) one, though the median voter remains a member of the majority non-elite (which has mass of one).

the identity cleavage between, for example, the minority and majority, the further apart will the 'ideal' location of these two groups, i.e., larger $|\theta_a - \theta_b|$.

In our framework, this term also captures a core dimension of civil rights. A key principle of civil rights is non-discrimination or equal treatment by the state. We can capture this principle as one where there is equal treatment before the law or in terms of non-discrimination in the provision of public goods. Of course, these two facets of civil rights are closely related. The more expansive interpretation of civil rights in terms of non-discrimination by the state in public-goods provision derives from the civil rights movement in the United States, where Martin Luther King and his allies demanded equality of access of public goods such as education, housing and transport. The alternative narrower but sharper interpretation of civil rights is when we restrict focus more narrowly about *equal treatment before the law*—be it the police, the courts or the justice system. Our formalisation captures both these (related) dimensions of civil rights.[8]

We assume that there is a deadweight loss associated with the provision of public goods. Denoting total expenditure on the public good by $r$, the utility derived from the public good is thus expressed as:

$$\pi_i = r - \{1 + |\theta_i - \theta|\}\frac{\gamma}{2}r^2, \tag{2}$$

where $\gamma$ parameterises the magnitude of the deadweight loss relative to the direct benefits associated with public goods provision. Note that deadweight loss is minimised, but not eliminated when $\theta = \theta_i$. We shall normalise the majority's preferred public good by taking $\theta_a = 1$. By incorporating the idea of an identity cleavage, the above formulation provides a parsimonious way to capture both of the notions of civil rights delineated above. For instance, consider the idea of equal treatment before the law. With positive probability, all citizens face the prospect of a contractual (or any other) dispute that affects their payoffs. Expected payoffs are higher if a citizen (especially belonging to a minority group) can be guaranteed fair and equitable treatment by the law.[9]

### 1.3. *Political Regimes: Policy Decisions and Group Payoffs*

All political regimes correspond to an allocation of political power that is constrained by an associated set of group-specific rights. These group-specific rights constrain policy choices made by the government and include (*i*) political rights and the likelihood that the group in power face elections, (*ii*) property rights—who will be taxed and how much and (*iii*) the civil rights of any (especially minority) group.

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[8] Besley and Persson's (2011) formalisation of executive constraints has a similar flavour. In their formalisation, for every dollar of transfers that the incumbent makes to its group it has to give $\omega$ dollars to the other group, where $\omega$ belongs to the interval [0, 1]. Hence, if $\omega = 1$, there is full equality and perfect executive constraints and corresponds to our case of civil rights in terms of perfect symmetry in treatment of each group when $\theta = \bar{\theta}$.

[9] For example, suppose an economic interaction between an individual from group $A$ with another citizen from group $B$ generates a surplus $s_{ij} > 0$. In the case of a contractual dispute between the two parties, both the parties will face the legal system that may or may not guarantee equal treatment. In other words, equality of the law would mean that the division of the surplus will be unaffected by their group membership. However, if there is no equal treatment of minority group members under the law, we may expect that in response to a disagreement between two citizens the police and the courts will side with the individual who belongs to the majority group. We can show that the more biased are the courts (further away from the ideal point of the minority group $B$), the larger the share of the surplus extracted by the majority at the expense of the minority, i.e., large $|1 - \theta|$, the smaller is $(1 - \beta)s_{AB}$ (a simple application of asymmetric Nash Bargaining solution will deliver this—see Muthoo, 2001).

In order to illustrate the key differences across the political regimes as well as rank them in a plausible way, we make a few simplifying assumptions. In particular, we assume that the political regime in place determines (*a*) how the public good is financed (whether through general taxation or the extraction of a surplus from the non-elite), (*b*) the level of expenditures on the public good and (*c*) the type of public good provided. This specification provides us with a parsimonious framework to distinguish between different kinds of political regimes, especially whether they discriminate in favour of a group in terms of *both* how they finance a public good as well as what kind of public good is provided by the state. This enables us to have a comprehensive view of deviations from equal treatment by the state under a given political regime.

Accordingly, in a *right-wing autocracy* (*RA*) the relative absence of executive constraints/civil rights, enables the elite to discriminate against the populace and tax/extract surplus from them. A liberal autocracy is very similar in that the elite remain in the driving seat. However, they are also somewhat constrained in that the elite cannot discriminate against any particular group either in terms of taxation or the nature of public good provided.

In contrast, in a democracy the group in power is the numerical majority (group *A*). However, this power will translate into very different policy and public good outcomes depending on the constraints in operation—we may end up with either an electoral democracy, a liberal democracy or indeed democratic communism. First, in an electoral democracy, it is the majority's prerogative to select an economy-wide tax rate. And the majority can also choose the type of public good, disregarding the minority's wishes completely. In contrast, in a liberal democracy, the majority retains control over the tax rate, but they cannot discriminate against the minority. If the political regime is one of democratic communism, the majority can further extract a surplus from the elite (over and above any economy wide tax). Other details about the political regimes will be provided below.

### 1.3.1. *Group payoffs in different political regimes*

We can now derive the payoffs that each group will obtain in any political regime that is adopted. We focus in detail only on regimes in which property rights are protected and briefly discuss payoffs in the absence of property rights at the end of the section.

Consider first the *RA* case (box 5 in Table 1). This is the regime in which property rights are the only rights protected. We assume the elites can extract a share $\sigma$ of the non-elites' pre-transfer income $(1 - \alpha)$, for a total expenditure on public goods of $r = \sigma(1 - \alpha)$. They can also select their preferred type of public good, $\theta = \theta_e$. The rate of extraction $\sigma$ is determined by maximising the elite's utility function $u_e^{RA} = \alpha + \sigma(1 - \alpha - \frac{\gamma}{2}[\sigma(1 - \alpha)]^2)$, where *RA* stands for 'right-wing autocracy'. This yields:

$$\sigma^{RA} = \frac{1}{\gamma(1 - \alpha)}. \tag{3}$$

Substituting this expression back in $u_e^{RA}$ gives us:

$$u_e^{RA} = \alpha + \frac{1}{2\gamma}. \tag{4}$$

The non-elites are excluded from public goods in this political regime. It is only their income that is affected, which is reduced by the amount extracted by the elites:

$$u_a^{RA} = u_b^{RA} = (1 - \alpha) - \frac{1}{\gamma}. \tag{5}$$

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Move next to the *electoral democracy* case (*ED*, box 6). The level and type of public-goods provision are now chosen by the majority. Civil rights are not protected in an *ED* and subjects belonging to the minority identity no longer face equal treatment by the state. Accordingly, we model this as the majority being free to select public goods targeted solely at their preferences ($\theta = \theta_a = 1$). The minority can be discriminated against by the majority (who control the state). To finance the expenditure on public goods, the majority in turn set an economy-wide tax rate ($\tau$) by maximising their utility $u_a^{ED} = (1 - \alpha)(1 - \tau) + \tau - \frac{\gamma}{2}\tau^2$. This yields:

$$\tau^{ED} = \frac{\alpha}{\gamma}. \tag{6}$$

Substituting this back to $u_a^{ED}$, we get the equilibrium payoff for the majority:

$$u_a^{ED} = (1 - \alpha) + \frac{1}{2\gamma}\alpha^2, \tag{7}$$

which is clearly larger than in the *RA* regime (equation (5)). The payoffs for the other two groups (the elite and the minority) can be solved by substituting (6) into their respective utility functions. This yields the following results:

$$u_e^{ED} = \alpha - (2\alpha - 1)\frac{\alpha}{\gamma} + \frac{\theta_e}{2\gamma}\alpha^2; \tag{8}$$

$$u_b^{ED} = (1 - \alpha) + \frac{\theta_b}{2\gamma}\alpha^2. \tag{9}$$

We note a couple of things about this political regime. First, as long as there is an identity cleavage (i.e., $\theta_b \ll \theta_a = 1$), the minority end up doing worse under *ED* compared to the majority (compare eqs. (9) and (7)). This is the result of the state (controlled by the majority) discriminating against the minority. The deeper the identity cleavage, measured by $1 - \theta_b$, the higher the cost the minority suffers in the absence of civil rights.

Second, the elite suffer two distinct costs in the *ED* political regime relative to *RA*. They now both pay net taxes and consume fewer public goods. The first of these effects is captured with the middle term in equation (8). (Recall that $\alpha > \frac{1}{2}$.) The second effect can be observed by comparing the public-goods terms in equations (8) and (4).

We now turn to the *liberal democracy case* (*LD*, box 8). In this political regime, the majority can still choose $\tau$ freely to maximise their utility, but they cannot discriminate in public-goods provision. In other words, quite irrespective of the group they belong to, all citizens receive equal treatment by the state in a *LD*, resulting in identical payoffs such that $\pi_a = \pi_b = \pi_e$. This is equivalent to assuming that the public good is located such that $|1 - \bar{\theta}| = |\bar{\theta} - \theta_b| = |\bar{\theta} - \theta_e|$.[10] Under this assumption of equal treatment, the expression for the majority's utility in this case is given by $u_a^{LD} = (1 - \alpha)(1 - \tau) + \tau - \frac{\gamma}{2}\tau^2(2 - \bar{\theta})$. The tax rate that maximises this is:

$$\tau^{LD} = \frac{\alpha}{\gamma(2 - \bar{\theta})}. \tag{10}$$

Note that $\tau^{LD} < \tau^{ED}$, since the majority now derives fewer benefits from expenditures on public goods, which, in a liberal democracy, they have to share with the minority (cf. equation (6)).

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[10] Of course, we can relax this insistence of equal treatment under an *LD* and allow for some (appropriately weighted) social welfare function $\bar{\theta}$. In this case, we assume that the type of public good provided lies somewhere between the ideal types of the majority and minority: $\theta = \bar{\theta}$, with $\theta_b < \bar{\theta} < 1$. For example, $\bar{\theta}$ might be a population-weighted average of the two groups' preferences $\bar{\theta} = n + (1 - n)\theta_b$.

Plugging (10) in the utility functions of the three groups, we then derive the equilibrium levels of utility of the three groups:

$$u_e^{LD} = \alpha + \frac{\alpha}{\gamma(2-\bar{\theta})}\left[1 - \frac{3}{2}\alpha\right], \tag{11}$$

$$u_a^{LD} = (1-\alpha) + \frac{\alpha^2}{2\gamma(2-\bar{\theta})}, \tag{12}$$

$$u_b^{LD} = (1-\alpha) + \frac{\alpha^2}{2\gamma(2-\bar{\theta})}. \tag{13}$$

We should note that the expressions derived above are for payoffs of each of the groups when they are equally treated by the state (in terms of the impact on $\pi_i$).[11]

These expressions have straightforward interpretations. First, note that the majority are worse off in the *LD* political regime compared to the *ED* political regime (compare eqs. (12) and (7)). This is a direct implication of the provision of civil rights to (or sharing of public goods with) the minority in the former case. The presence of a minority reduces the gains to the majority from taxing the elite in *LD*. To that extent it ameliorates class conflict.[12] Second, it can be checked that the minority are better off if the political regime is *LD* instead of being *ED*, for the same reason (equation (13) versus (9)). The greater the identity cleavage between the majority and the minority $(1-\theta_b)$, the larger are both of these effects.

So far, we have discussed three out of the four regimes in which property rights are protected. The remaining possibility is the combination of property rights with civil rights, a regime that we called *liberal autocracy* (*LA*). In this case, we assume elites are the ones that set the tax/extraction rate (as in *RA*), but they do not exclude non-elites from the benefits of the public good, and they tax themselves as the rest of society. The tax rate that will be adopted in this political regime equals:

$$t^{LA} = \frac{1-\alpha}{\gamma}, \tag{14}$$

which is smaller than the extraction rate under right-wing autocracy (*RA*, see equation (3)). This tax rate is also smaller than the outcome under *ED* (see equation (6), recalling that $\alpha > 1/2$). The associated utility levels for the three groups are:

$$u_e^{LA} = \alpha + \frac{(1-\alpha)^2}{\gamma\Delta}\left[1 - \frac{1}{2\Delta}\right], \tag{15}$$

---

[11] More generally, if instead their payoffs were given by some (appropriate) social welfare function of the two groups' payoffs ($\bar{\theta}$), the expressions would be:

$$u_e^{LD} = \alpha - \frac{(2\alpha-1)\alpha}{(2-\bar{\theta})\gamma} + \frac{3 - 2\bar{\theta} - |\theta_e - \bar{\theta}|\alpha^2}{2\gamma(2-\bar{\theta})^2}.$$

The expression for the majority group A is the same as (12) and group B obtains:

$$u_b^{LD} = (1-\alpha) + \left[\frac{3 - 3\bar{\theta} + \theta_b}{(2-\bar{\theta})}\right]\frac{\alpha^2}{2\gamma(2-\bar{\theta})}.$$

[12] There is some literature that discusses how identity cleavages may soften class-based politics: voters who view themselves as members of a particular, say, ethnic group may vote alongside other members of the group, many of whom may also be rich. See Roemer (1998) and Shayo (2009). In our framework, the causal channel is different, and operates through diminished incentives for public-goods provision.

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$$u_a^{LA} = (1 - \alpha) + \frac{(1 - \alpha)^2}{2\gamma \Delta}[3\alpha - 1], \tag{16}$$

where $\Delta = \{1 + |\theta_e - \theta_i|\}$ the direct payoff from the 'location' of the public good. Moreover, since this is an *LA* and the majority and minority community face equal treatment before the courts and in public sphere, both groups have the same payoff:

$$u_b^{LA} = (1 - \alpha) + \frac{(1 - \alpha)^2}{2\gamma \Delta}[3\alpha - 1]. \tag{17}$$

The non-elites prefer *LA* to *RA* since they get some public goods in the first case. But from the perspective of the majority *ED* dominates both, since it is the majority that sets the tax rate under *ED*. The best possible outcome for the majority under *LA* occurs in the limit case when the elites and the majority have the same identity ($\theta_e = 1$) and there is perfect equality $\left(\alpha = \frac{1}{2}\right)$. In that case, it can be checked that the majority do equally well under *ED* and *LA*. But under all other circumstances, $u_a^{ED} > u_a^{LA}$. The gains to the majority from moving from *LA* to *ED* are increasing in the wealth and identity gaps.

Unlike the majority, the minority can be better off under *LA* compared to *ED*. This is because the minority does not do that well with the public good when the majority selects its type and discriminates against the minority. When the identity cleavage runs deep, this raises the possibility that the elite may co-opt the minority against the majority and forestall the emergence of *ED* by offering *LA* instead.

To complete the description of the various political regimes, we need to specify also what happens when property rights are not protected (boxes 1–4). For purposes of the discussion that follows, we do not need to describe each one of these cases separately. We just need to say something about the payoffs in case the non-elite succeed in expropriating the elite. For concreteness, let us call this the *dictatorship of the proletariat* case (*DP*). We assume a portion $\varphi$ of the economy's productive capacity is destroyed or becomes useless in the process. The elite finds themselves expropriated with their utility being driven to zero, while utility levels for the non-elite depend crucially on the deadweight loss parameter $\varphi$:[13]

$$u_e^{DP} = 0, \tag{18}$$

$$u_a^{DP} = 1 - \varphi, \tag{19}$$

$$u_b^{DP} = 1 - \varphi. \tag{20}$$

### 1.3.2. *Political transitions and the timing of the game*
The focus of our analysis is on the constellation of interests that underlie the transition from a righ-twing autocracy (*RA*) to an electoral or liberal democracy (*ED* or *LD*). Accordingly, we now describe conditions under which a political transition away from a political status quo may take place.

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[13] For simplicity, we posit the payoffs to the majority and the minority to be the same in the DP regime. This is because the relative utility levels of the majority and minority are not important for our results since the reservation level of utility under DP is essentially a normalisation. For example, if the utility of the minority in DP is lower, there would be a larger range of parameter values for which the minority would prefer not to join the majority in an attempted revolution. To allow for this, we would need to introduce and carry around yet another parameter—without providing us with sufficiently new insight.

We assume that, under some structural conditions, there is a narrow window of opportunity that makes revolution and change possible. These structural conditions that facilitate revolution may come in a variety of forms. They include economic crises (see Haggard and Kaufmann, 1995) such as a bad harvest or a negative economic shock from the global economy (e.g., Indonesia after the Asian currency crisis), military defeat (e.g., Argentinian defeat at Falklands in 1983), or something unexpected and random (e.g., when Tunisian street vendor immolates himself and catalyses the Arab Spring). We capture these exogenous factors that affect the prospect of a successful revolution by a random variable $\chi$ drawn from a distribution $G(.)$. If $\chi \geq \hat{\chi}$, then structural conditions are conducive to a regime change. Therefore, if $\chi \geq \hat{\chi}$, we assume that the number of participants in the revolution must exceed the threshold level $n^* \leq 1$ before a revolution can be launched. For simplicity, we further assume that $(1 - n < n^*)$, so that the minority can never mount a revolution on their own.[14] Once initiated, a revolution has a fixed probability $\rho$ of success. If the revolution is successful, the elites are expropriated and the payoffs are as shown in eqs. (18)–(20) (observe that these terms capture the deadweight loss of a revolution). If the revolution is unsuccessful, the majority obtains a utility of 0 (and the elite continue to reap $u_e^{RA}$).

### 1.3.3. *The timing*

The elite observe the prospect of revolution $\chi$ and assess whether or not it is sufficiently high to make the status quo political regime (*RA*) vulnerable to a revolt. After observing the prospects of regime overthrow (i.e., if $\chi \geq \hat{\chi}$), the elite may offer the other two groups a new political regime from the set $\{LA, ED, LD\}$ or may stick to the status quo *RA*. The majority group move next, and they either accept the political regime offered by the elite, or they mount a revolution. Finally in the third period, the minority gets to make a decision about whether to join the revolution or to stay put. If the majority accepts the offer of the elite, the political regime is adopted. However, if the majority does not accept the political regime on offer, it launches a revolution that is successful with positive probability. In the last period, payoffs of the elite, majority and minority are determined as described in Table 1.

In making the assumption that the game ends with the new political regime in place and payoffs realised, we sidestep an important issue. In particular, we implicitly assume that once a political regime is adopted, it is politically sustainable over time. This is for several reasons. First, this simplifying assumption allows us to analyse in the most transparent manner the constellation of interests that make different regimes possible. Second, it helps emphasise that even if we ignore issues of sustainability, liberal democracies emerge only in an unlikely set of circumstances. Indeed, we conjecture that accounting for the effect of credibility and time inconsistency of agreements will only further narrow the set of parameters under which liberal democracy arises. We discuss this further in Subsection 2.2.

We now have all the detail we need to carry out an equilibrium analysis of the sequential game described above. In what follows, we analyse the set of conditions under which a democratic transition is possible and focus on whether a liberal or electoral democracy is likely to emerge. We discuss these issues in the next section.

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[14] Our maintained assumption is that the minority is too small/powerless to overthrow the elite on its own. If it were not, then the minority would be effectively transformed into what we call the 'majority' in our model. Hence, one way to think of our minority–majority distinction is that it is less about sheer numbers and more about potential threat to the elite. See Besley and Persson (2011) for a model where the 'minority' has the potential to destabilise the incumbent government—*on its own*. In Besley and Persson, this threat can lead to repression by the government, which is costly. In our model, electoral democracy (in which the minority is discriminated against) does not entail any costs to the majority or the elite.

## 2. Political Transitions to Electoral or Liberal Democracy?

This being a finite period sequential game, we solve for the equilibrium backwards. In doing so, we illustrate the subset of political regimes that are feasible and likely to arise in any political equilibrium, where we define a feasible political regime as one where (*a*) the payoffs to the elite and the majority are at least as high as they would have obtained had they not participated, i.e., the participation constraints have to be met, and (*b*) it is not dominated by an alternative regime that is preferred by both the majority and the elite. The latter condition rules out regime types that are Pareto-inferior from the perspective of the two groups, who can do better by moving to that alternative.

Given that we have already derived the payoffs for the elite, the majority and the minority under alternative political regimes, this is quite straightforward (see equations (4)–(20)). We are especially interested in examining how the equilibrium is affected by the interaction of the identity cleavage with the class/income inequality. Accordingly, to illustrate this as transparently as possible and depict it graphically, we assume that the elite share an identity marker with the majority ($\theta_e = \theta_a = 1$), while the majority–minority identity cleavage is large ($\theta_b = 0$). Finally, Figures 2–4 show how the utilities of the three groups vary with $\alpha$ and are drawn assuming $\gamma = 2$, $\varphi = 0.3$, $\rho = 0.5$ and $\bar{\theta} = 0.5$. We shall use these figures to examine the equilibria for different ranges of the income/class cleavage. This is a useful benchmark that simplifies the characterisation of possible equilibria and captures the key economic trade-offs at work.

We need to distinguish between two scenarios. The first is the case where the elite face a credible threat of revolution from the majority group alone (either because the minority is politically 'passive' or too small to matter, i.e., $n \geq n^*$). In the second case, a successful revolution requires participation by both the majority and the minority (i.e., $n < n^*$).

### 2.1. *Case 1: Political Transition with a Politically Passive Minority $n \geq n^*$*

In this case the minority do not have any strategic importance as a driver of political change. It is only the preferences of the elite and majority that count towards any negotiated settlement.

Accordingly, in the last period, the minority gets to choose whether to join the revolution or not. However, because the majority have the numbers to mount a revolution on their own and the minority's decision affects neither the elite's nor the majority's actions (remember that $(1 - n) < n^*$), its decision is of no consequence. So the equilibrium outcome is invariant to what happens at this last stage.

Moving back one stage, observe that in period two the majority will accept any regime that yields utility higher than its expected utility when it attempts a revolution, $\rho u_a^{DP} (= \rho(1 - \varphi))$. This reservation level of utility is shown in Figure 2 by the flat line. When $\alpha$ is beyond a threshold $\alpha_a^{max}$ (around 0.8 in our example), there is no such political regime that yields a higher payoff for the majority group, and they will prefer to attempt a revolution. In other words, when the income/class cleavage is sufficiently deep, even if the elite were to offer *ED*, this would not satisfy the majority's participation constraint, and the majority would be better off trying to mount a revolution.

Figure 2 captures the payoffs that each group gets from alternative political regimes. We observe here that there is a minimum threshold $\alpha_a^{min}$ below which the majority will accept any of the offers in the set $\{ED, LD, LA\}$. The choice between each of these regimes is driven by the degree of inequality as well as the magnitude of the identity cleavage. The size of the identity
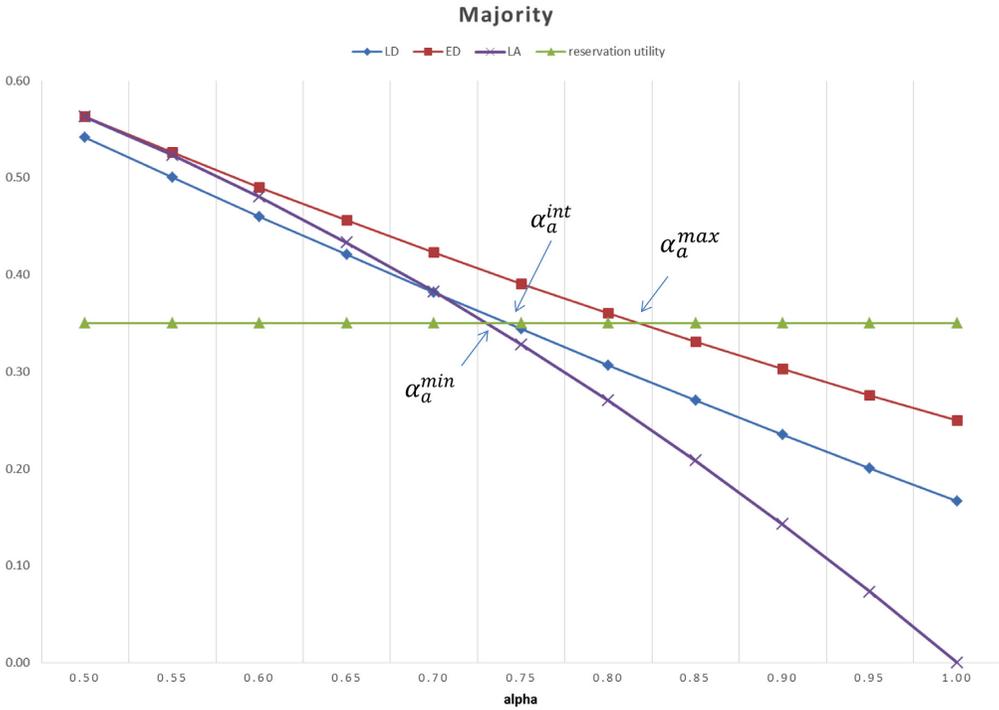
**Majority**



Fig. 2. *Utility of Majority under Different Political Regimes.*

cleavage determines the cost to the majority of ensuring equal treatment by the state for all groups. Further, the degree of inequality also affects the choice of political regime since higher inequality increases the payoff to the majority from choosing *ED* over *LD*. Between $\alpha_a^{min}$ and $\alpha_a^{max}$, there is also an intermediate threshold $\alpha_a^{int}$ which defines the following two additional zones: between $\alpha_a^{min}$ and $\alpha_a^{int}$, the majority is willing to accept either *LD* or *ED* but not *LA*; and between $\alpha_a^{int}$ and $\alpha_a^{max}$, the majority is willing to accept only *ED*.

Now, we move to the first stage of the game where the elite decide on whether to retain the status quo (*RA*) or introduce a regime change. The necessary condition for any regime other than *RA* to emerge in equilibrium is

$$\rho u_a^{DP} > u_a^{RA}. \tag{21}$$

On substituting from (5) and (19), we obtain $\rho(1 - \varphi) > (1 - \alpha) - \frac{1}{\gamma}$. When this inequality is violated, non-elites can never credibly threaten to revolt as their expected utility would be reduced relative to the status quo. Higher inequality (i.e., larger $\alpha$) as well as a lower deadweight cost $\varphi$ (e.g., organisational cost of revolution) will make revolution more likely. This suggests that the elite are more likely to be willing to abandon *RA* in favour of an alternative regime when the class/income cleavage is higher.

Now observe that $u_a^{DP} = 0$ (equation (18)). Therefore, as long as at least one of the three regimes {*LA*, *ED*, *LD*} yield utility to the elite that exceeds $(1 - \rho)u_e^{RA}$, the elite always prefer to stave off revolution by introducing a new political regime. Whether they can successfully do so, however, depends on whether the majority can reap a utility that exceeds its reservation
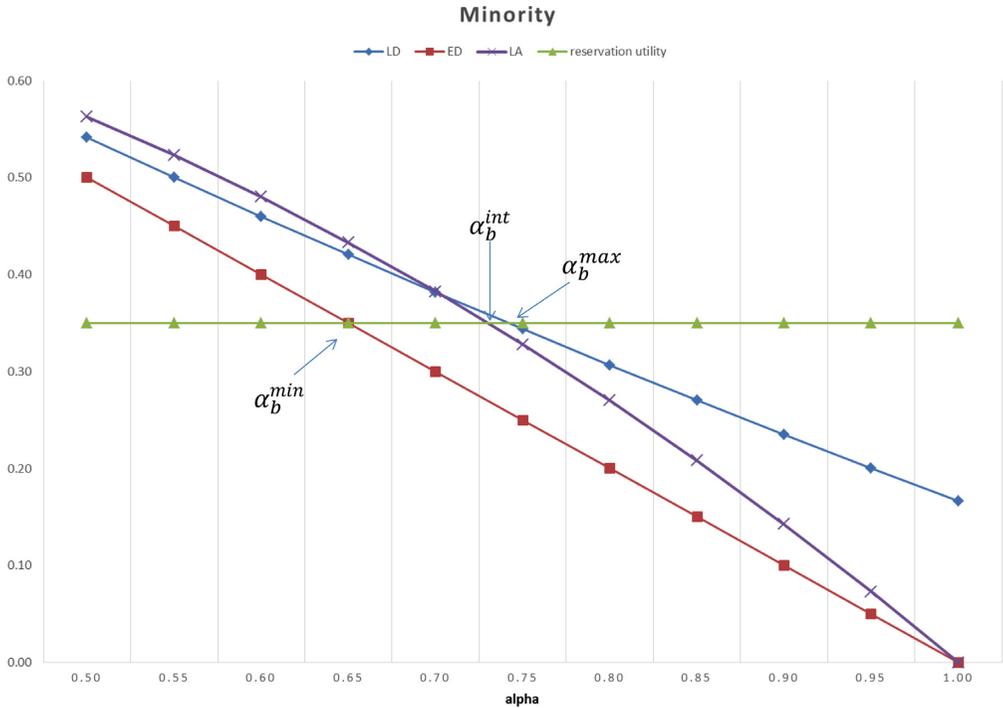
Fig. 3. *Utility of Minority under Different Political Regimes.*

utility under an attempted revolution, $\rho u_a^{DP}$. If such a regime exists, there will not be a revolution attempt on the equilibrium path of the game. Otherwise, the elite cannot prevent a revolution, and with probability $\rho$ the equilibrium ends up in *DP*.

However, if the elite obtain a higher utility from staving off the threat of a revolution, it chooses between the regimes $\{LA, ED, LD\}$ that which yields it the greatest utility, given the choices of the majority described above. Note from Figure 4 that the elite always (at least weakly) prefer *LA* to the other two regimes. The ranking of *ED* and *LD* in turn depends on whether $\alpha$ is larger or smaller than the critical level $\alpha_e^*$. When $\alpha < \alpha_e^*$, the elite prefer *ED* to *LD*. When $\alpha > \alpha_e^*$, the elite's preference switches to *LD*. We note also that $\alpha_e^* < \alpha_a^{min}$ (cf. Figures 2 and 4).

We now turn to the case where $n < n^*$.

## 2.2. *Case 2: Political Transition with a Politically Active Minority $n < n^*$*

Now the majority needs the minority to tag along in order to induce the elite to accept a regime other than *RA*. This transforms the minority into a strategic actor. Given that the minority has some power now, this means they are more likely to get an outcome favourable to them.[15]

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[15] However, greater power need not increase the likelihood of democracy, liberal or otherwise. While the minority is generically better off in *LD* than in *ED*, it is possible that the minority may prefer a *LA* even more. This latter possibility is more likely the deeper the identity cleavage between majority and minority. This creates room for the minority to enter an alliance with the elite as opposed to the majority.
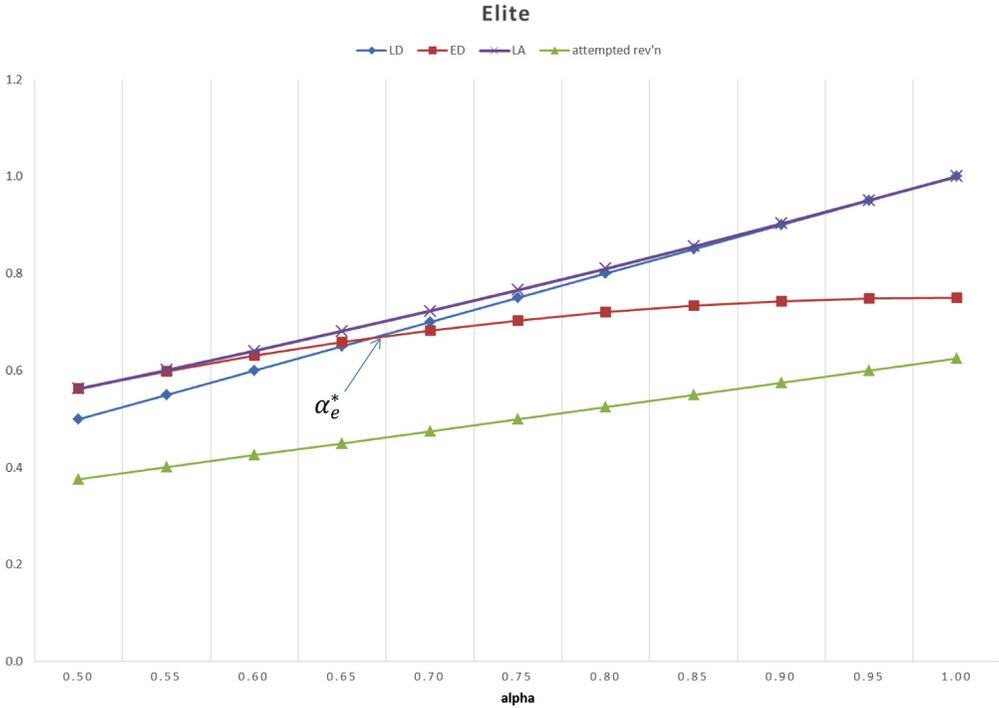
Fig. 4. *Utility of Elite under Different Political Regimes.*

Working backwards again, the minority gets to make the decision of whether or not to join the revolution, if the majority has already launched one. They will join if and only if they are not offered a regime that improves their utility compared to the expected utility they get under an attempted revolution. And, in the previous stage, the majority will launch a revolution only when they know the minority will subsequently join them.

From the perspective of the elite, in the first stage of the game, the constraints are now looser than in the previous case with $n \geq n^*$. That is because the threat of revolution can be thwarted by offering enough to either the majority or the minority. So the elite will do at least as well here as in the previous case.

Despite these differences, under the parameters we selected—and in particular the assumptions that $\theta_b = 0$ and $\bar{\theta} = 0.5$—it turns out that the equilibrium is unaffected when the size of the majority falls short of the minimum threshold required for revolution. This is mainly because *LD* and *LA* yield identical payoffs to the majority and minority, eliminating the advantage that the elites would have in general by being able to split the 'coalition'. We briefly discuss the details.

Revolution now requires that it be the dominant strategy for both the majority and minority. The range of $\alpha$ for which this is true is given by $\alpha > \max[\alpha_a^{max}, \alpha_b^{max}]$. In other words, in general the elite can avoid revolution for a broader range of income/class cleavages. Under our parameters, $\alpha_a^{max} > \alpha_b^{max}$, so the operative limit remains the majority's upper threshold.

At the lower end of the range for $\alpha$, there is scope for the elite to co-opt the minority by offering *LA*, as we discussed earlier. As can be seen from Figure 3, for $\alpha \leq \alpha_b^{int}$, this strategy works and

prevents the minority from teaming up with the majority. Since liberal autocracy produces identical payoffs to the minority and majority under our parameters, we have $\alpha_b^{int} = \alpha_a^{min}$, and the boundary for *LA* remains unchanged as well.

Consider next what happens when $\alpha_b^{int} < \alpha \le \alpha_a^{max}$. Note first that $\alpha_b^{max} = \alpha_a^{int}$, as both of these refer to utilities under *LD* where the outcomes are identical for the majority and minority under our parameters. With this in mind, there are two zones in this interval: (*i*) $\alpha_b^{int} < \alpha \le \alpha_b^{max} = \alpha_a^{int}$, and (*ii*) $\alpha_b^{max} = \alpha_a^{int} < \alpha \le \alpha_a^{max}$. In the first of these, the majority prefers both *ED* and *LD* to revolution, while the minority prefers only *LD* to revolution. In the second, the majority prefers *ED* to revolution, while the minority strictly prefers revolution. The elites will then offer *LD* in the first zone and *ED* in the second.

Hence, the equilibrium configuration of the regimes is identical to the previous case and is as stated in the proposition below. Having described the set of optimal decisions in both the case where $n \ge n^*$ and $n < n^*$, we are now in a position to describe the equilibrium of the game for different degrees of inequality. These are summarised in the proposition below.

PROPOSITION 1. *Under the sequence of moves described above and the parameter assumptions stated, the equilibrium configuration of the political regimes is as follows:*

(*i*)  *when $\alpha \le \alpha_a^{min}$, the elite offer LA and the majority accepts it;*
(*ii*)  *when $\alpha_a^{min} < \alpha \le \alpha_a^{int}$, the elite offer LD and the majority accepts it;*
(*iii*)  *when $\alpha_a^{int} < \alpha \le \alpha_a^{max}$, the elite offer ED and the majority accepts it;*
(*iv*)  *when $\alpha > \alpha_a^{max}$, the majority mount a revolution regardless of what the elite offer.*

We now discuss aspects of the above proposition by focusing on specific scenarios in order to illustrate the forces at work. Since the intuition behind the key tradeoffs is easiest to convey in the case where the minority is a passive player, in what follows we stick to case 1 above.

## 2.3.  *(a) The Narrow Gate: Inequality, Identity and LD*

When the elite share an identity marker with the majority ($\theta_e = 1$) and the majority–minority identity cleavage is large ($\theta_b = 0$), then *LD* emerges under a narrow set of circumstances. Here, notice that when the income/class cleavage is large (but not so large as to induce the majority to revolt), we get *ED* as the equilibrium outcome rather than *LD* (zone (*iii*)). This is so even though the elite prefer *LD* to *ED* for larger $\alpha(> \alpha_e^*)$. In this zone, it is the participation constraint of the majority that binds, and it is their preferences that dictate the outcome. For low $\alpha$, on the other hand, the elite can get away with *LA* and do not need to offer *LD*. Hence, the proposition highlights an interesting implication of our analysis. It shows that the *region in which LD emerges as an equilibrium is squeezed from below by the availability of LA (which satisfies the elite's incentive constraint) and from above by ED (which satisfies the majority's participation constraint).*

Furthermore, observe that when the identity cleavage between majority and minority gets smaller, the majority's preference for *ED* over *LD* becomes weaker. In Figure 2, the *LD* schedule moves closer to the *ED* schedule, expanding the zone in which *LD* is the equilibrium and shrinking the zone in which *ED* emerges. In the limit, when $\theta_a = \theta_b = 1$ (no identity difference among the non-elite), the two schedules overlap completely. Both of these cases render *LD* more likely. Hence, the emergence of liberal democracy requires *both mild inequality (low $\alpha$) and the absence of large identity cleavages (proximity between $\theta_a$ and $\theta_b$).*

2.4. *(b) The Impact of Inequality in the Presence of Identity Congruence between Elites and the Majority ($\theta_e = 1$)*

In this case, the comparison between $u_e^{LD}$ and $u_e^{ED}$ depends on the magnitude of the class cleavage. For relatively mild levels of inequality $\left(\frac{1}{2} < \alpha < \frac{2}{3}\right)$, $u_e^{LD} < u_e^{ED}$, and elites prefer electoral democracy. When the income/class gap is bigger, $u_e^{LD} > u_e^{ED}$, and elites prefer liberal democracy. The intuition is as follows. When inequality is mild, the elite get taxed relatively little, and the fact that they get their preferred variety of public good in *ED* makes up for the higher tax rate that they face. When inequality is high, on the other hand, it is the tax rate that matters more, and the elite would rather have the lower taxes in *LD*, even if that means that the they do not get the advantages of discriminating against the minority.

2.5. *(c) Identity Congruence and Elite Support for LD ($\theta_e = \theta_b \ll 1$)*

Consider an extreme version of this scenario where $\theta_e = 0$. In this case, under *ED* elites would be discriminated by the state, so they unambiguously prefer *LD* to *ED*. And this is true regardless of the depth of the class cleavage. More generally, the closer the elite and minority identities are aligned and the deeper the identity cleavage, the more likely that the elites prefer *LD* to *ED*. Indeed, we can see this in Figure 4, where observe that $\alpha_e^*$ moves to the left (becomes smaller) as $\theta_e$ gets closer to 0. If, for whatever reason, *LA* is ruled out, this makes *LD* an equilibrium for lower levels of $\alpha$ than in our benchmark case. This case speaks directly to the political transition in South Africa in 1994 that we discuss in the next section.

2.6. *Further Remarks*

We briefly discuss two important assumptions that undergird our framework.

(*a*) *Uncertainty and multiple cleavages:* our framework treats the identity cleavage as unchanging and given. This is, of course, quite different from the actual practice of politics, where there may exist a multiplicity of possibly cross-cutting cleavages—revolving around ethnicity, race, religion or nationality. Furthermore, the salience and magnitude of these identity cleavages may be altered by political entrepreneurs who may send messages about who is a native or an outsider, disseminate stereotypes about racial and religious minorities, and so on. In other words, at least part of these cleavages are 'socially constructed' with new cleavages being created, just as old social fissures disappear (see Jain *et al.*, 2014; Mukand and Rodrik, 2018). In this case, our exogenously given majority group A and minority group B may be unstable. An individual who is in a majority group today may (with some probability) end up being in a minority group tomorrow. If that were the case, then that would change decision-making calculus for each of the three groups. For example, the majority may be more inclined to moderate its demands if it knows that there is the possibility that it may end up in the losing minority group in the future.

Indeed, this is consistent with the observation made by Lijphart (1969, p. 218) that uncertainty on this dimension may temper the maximalist demands of today's majority (see Dixit *et al.*, 2000 for a formal analysis). We further discuss this possibility in Section 3 where we discuss the country experiences.

(*b*) *Credibility and commitment:* we now return to our simplifying assumption that political agreements are politically sustainable. Our focus in this paper has been on the constitutive

bargains that lie at the origin of different political regimes, liberal democracy in particular. It goes without saying that such bargains can obsolesce over time. Class and identity cleavages evolve as a result of exogenous developments in the economy and society as well as political strategies pursued by groups contending for power. Commitments made during negotiated pacts and written into law and enshrined in institutions may prove unsustainable when one of the groups—the elite or the majority—perceives clear gains from rewriting the rules through opportunistic behaviour. Problems of self-enforcement are endemic in political systems.

So, in practice, governments often go back on promises of civil rights. Some examples are the internment of Japanese immigrants during the Second World War or the Indian government reneging on some of its promises to the native princely states. These dynamic considerations of credibility of agreements can undermine the adoption of *LD* and should be explored. However, explicitly sidestepping these dynamic considerations also has an upside. In particular, it helps us transparently illustrate that the *set of conditions under which liberal democracy may arise is circumscribed by factors in addition to those of the dynamic credibility of political agreements—namely, the size of identity and class cleavages.* Nevertheless, in the next section we discuss some instances of how this dynamic credibility of political agreements was ensured in practice. The credibility of political agreements can be ensured by not just the contemporaneous evolution of values (Besley and Persson, 2019), 'ideas' of liberalism (see Mukand and Rodrik, 2018), but also by the military as guarantor (as in post-Pinochet Chile) or the prospect of economic collapse and capital flight in moderating majority's demands (as in post-1994 South Africa).

## 3. Liberal Democracy: History and Country Vignettes

### 3.1. *History*

It is common nowadays to treat 'liberal democracy' as a single political package. But its two ingredients have different origins, social bases and political implications (Plattner, 2010; Ryan, 2012; Fukuyama, 2014). In the West, liberalism preceded the provision of political rights. Early liberals were the propertied elites and landed gentry whose primary objective was to prevent the crown from exercising arbitrary power over them. It was the rule of law they were after— not the sharing of power with the masses—whose judgement was perceived to be fickle and untrustworthy (Fawcett, 2014).

The fact that early liberals in the West were in large part the wealthy property-owning elite led to the bundling, in the minds of subsequent analysts, of two kinds of distinct rights: property rights and civil rights. When Western liberals eventually came to accept democracy, it was, as Fawcett (2014) portrays it, a grudging concession. Liberals made peace with democracy over the three decades prior to the First World War with industrialisation well under way which made the class cleavage salient. This was buttressed by state-supported cultural homogenisation through a policy of nation building in many European countries (Weber, 1976; Alesina and Reich, 2017). They gave their support to the expansion of the franchise and yielded to popular sovereignty over domains such as education and ethics in which they previously had a monopoly. In return, they hoped that popular forces would accept 'liberal limits on the authority of the people's will' which often required protection of property and civil rights (Fawcett, 2014, p.144). Thus was

born liberal democracy. However, it required the civil rights movement in the United States for this peculiarly British conception to get transformed into our current understanding of liberal democracy. Historically, subordinated groups across the world were 'profoundly influenced by American ideas of civil rights liberalism and its commitment to defend equality' (Kymlicka, 2007, p. 90).

This peculiarly British history does not fit the experience of other especially non-Western countries very well. In particular, the elite would often turn out to be interested primarily in property rights. Civil rights were for others, chiefly ethnic, religious or other minorities. In these countries, mass politics arrived typically as a consequence not of industrialisation, but of decolonisation or wars of national liberation. It wasn't economic change and the rise of factories that spurred social mobilisation but national struggles against colonisers or foreign enemies. Moreover, mass politics arrived in these newly independent countries before there was any attempt at cultural homogenisation through nation building. So the relevant cleavages were from the very beginning based on ethnicity or nationality rather than class or economic status. This was reinforced by the fact that colonisers had often codified and deepened pre-existing identity cleavages and allied themselves with some, often minority ethnicities against others in order to facilitate their rule (see discussion in Blouin and Mukand, 2019). The nationalist movements of the developing world more or less all claimed to be democratic in some fashion—even those who ascribed explicitly to socialist or communist ideology. But theirs was a democracy that was based largely on identity cleavages. It was explicit about the 'people's' right to rule over ethnic–religious–linguistic minorities or defend against a presumed external enemy. It was unlikely to promote liberal practices and prone to deteriorate into electoral democracy or worse.

### 3.2. *Evidence*

Against this historical baseline, we now examine the evidence. However, before we turn to examining specific country experiences, we briefly describe some supportive cross-country evidence. Figure 5 shows that countries tend to do much better in providing political rights than in providing civil rights. In Appendix A (available online), we provide a measure of liberal democracy and use it to examine some of the cross-national patterns. These results do not go beyond establishing some broad patterns in the data, but they seem to be supportive of our framework. Electoral and liberal democracies appear to be associated with different patterns of income and identity cleavages, a finding that validates our analytical distinction between these two types of democracies. Moreover, the data are consistent with the model's prediction that high levels of identity cleavages are particularly damaging to civil rights and liberal democracy, as opposed to political rights and electoral democracy. Finally, low income inequality and weak identity cleavages taken together tend to be associated with civil rights and liberal democracy. Of course, given the nature of the cross-country exercise, we must be cautious in how much weight we give these results.

We now turn to specific country examples that usefully complement our cross-country exercise. Indeed, they highlight some of the mechanisms delineated in our theoretical framework. At the outset we should clarify that in many of the cases we discuss below our classification of country experiences is for expository convenience and should not be considered watertight.
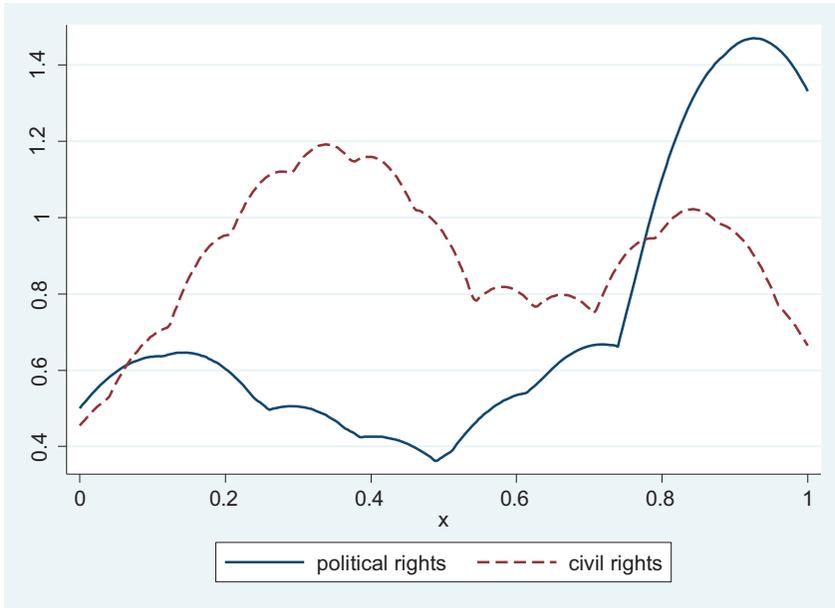
Fig. 5. *Distribution of Political and Civil Rights across 196 Countries 2014.*
*Notes:* Based on raw scores from Freedom House (2015). 'Political rights' refer to free and fair elections
(A1 and A2); 'civil rights' combine measures of independent judiciary (F1), rule of law (F2) and equal
treatment (F4). See text for explanation.

### (i) Identity congruence of elite with the minority ($\theta_e \approx \theta_b \ll 1$)

One set of conditions under which the elite want civil rights in addition to property rights is
when the elite and minority group are one and the same (i.e., share the identity marker).[16]

Perhaps the most striking such instance is South Africa's transition to democracy in 1994,
thanks to a negotiated settlement between the African National Congress (ANC) and the white
minority government. This was a landmark pact, as the elites who ran the apartheid regime
had so much to lose. They had long controlled not only the instruments of power but also the
economic wealth of the country. There was a huge economic gap between the whites and the
disenfranchised blacks. Expanding the franchise might have been expected to produce vastly
redistributive policies, if not outright expropriation of the assets of the white minority.

The key in South Africa was that the whites were a distinct minority on the identity dimension.
In terms of our model, the elites were keenly interested in protecting not just their property rights
but also their civil rights. As the distinguished South African jurist Richard Goldstone (1997)
put it, 'without some guarantee of protection for the rights of minorities, the previous ruling
white minority government would not have relinquished power to an inevitably black-controlled
majority government'. Not surprisingly, a bill of rights was part of the political settlement in 1996
that enshrined civil rights in the constitution and prohibited discrimination, while leaving room
for affirmative action. This political agreement was perceived to be credible not just because of
Mandela's stature as guarantor, but also because of the prospect of flight of capital and high skilled

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[16] Acemoglu *et al.* (2004) show how the corrupt elite manage to remain in political power by bribing and dividing
those politically opposed to them—in some cases even allying with a numerical minority.

labour if the agreement collapsed. In the event, South African democracy produced only moderate amounts of redistribution. The ANC government did institute measures that gave blacks a greater share of ownership of the capital stock and produced a black wealthy elite, but the economic interests of the whites were largely unaffected, an outcome that Inman and Rubinfeld (2012) attribute to the peculiar federal arrangements that were negotiated during the transition. More to the point, in the context of the present analysis, is that South Africa emerged largely as a liberal democracy—despite operating under considerable strain.

In a very different context and a completely different time, we have the classic instance of the 1689 English Bill of Rights. In this case the landlords and wealthy merchants who prevailed over the king in Britain's Glorious Revolution sought to protect themselves from the king in both the religious sphere and the economic sphere. They feared James II would impose his Catholicism on them as much as they worried about the crown's ability to expropriate them through exorbitant taxes. So, in Britain, property and civil rights were entrenched together (see Fawcett, 2014).

*(ii) Identity congruence of the elite with the majority ($\theta_e \approx \theta_a = 1$)*

In this case, a change in political regime is only feasible when there is inequality. At first glance, this scenario seems indistinguishable from Acemoglu and Robinson (2006), where the prospect of revolution results in democratisation. However, this congruence of identity between the elite and the majority may result in either an electoral *or* a liberal democracy. Our framework suggests that a liberal democracy is more likely if inequality is relatively low and the population has been sufficiently homogenised due to industrialisation (see Rodrik, 2016) or policies of nation building, as in nineteenth-century France or Nyerere's Tanzania. In the absence of such factors, we are much more likely to see the emergence of electoral democracy, as is commonplace across the developing world in countries such as Kenya, Brazil, Turkey and Sri Lanka, among others.

Consider the case of South Korea that underwent a striking transformation from a right-wing military dictatorship in the 1980s to a Western-style liberal democracy today. Korea is a country that is remarkably homogeneous in terms of language and ethnicity (if not religion). The main identity cleavage on which the authoritarian regime relied to mobilise domestic support was the military threat posed by the communist regime of North Korea. But this cleavage became less salient over time, as a consequence of the differential economic progress of the two halves of the Korean peninsula. Second, Korea experienced significant industrialisation, with more than a quarter of the labour force in manufacturing by 1987—indeed, these unions played a leading role in the emergence of democracy. This is reminiscent of the Western experience in the nineteenth century, where democratic mobilisation took place against the background of the Industrial Revolution. In sum, we would argue that the emergence of liberal democracy in South Korea has much to do with the relative absence of identity cleavages and the leading role played by the labour movement in mobilising against the military/industrial elite (see Chaibong, 2008).

It is worth pointing out that the process of industrialisation in culturally homogenising the sizeable working class is very similar also in other Asian liberal democratic countries such as Taiwan and Japan. In Taiwan, after the KMT formed a rightwing military dictatorship, the main ethnic divide was between the *waishengren* (mainlanders), who immigrated into Taiwan and were 15% of the population and constituted the military elite, and the *benshengren*, who were native Taiwanese of Hoko, Hakka and other ethnicities. There was a concerted (and successful) plan by the dictatorship to educate, indoctrinate and re-Sinicise the *benshengren*. It was only after this plan of homogenisation had been successfully implemented, that political space opened up for adoption of liberal democracy (Shih, 2012).

Chile's prolonged political transition to a liberal democracy from Pinochet's right-wing autocracy was somewhat different. Here an amalgam of interests that represented the economic elite (including the mostly rural landed gentry) and the military (especially Pinochet) wanted their interests protected when the 1980 constitution was written up. The elite made sure that their rights were respected by putting safeguards in the new constitution. These safeguards included overrepresentation of (typically conservative) rural areas in the legislature, a special quorum to pass bills as well as immunity for the military. Together these provisions ensured that there was no scope for 'tyranny by the majority' by the left-wing Concertacion coalition that may get elected. It ensured adequate political presence of the right-wing Alianza coalition that could not be politically wiped out (Angell, 2007). Indeed, even when the *Concertacion* won the elections in 1990, it was certainly kept in check both because of the constitutional safeguards and by the implicit threat of violence that the military always carried. Over time these constitutional safeguards became entrenched, and a genuine liberal democracy has emerged in Chile.

### (iii) Cross-cutting cleavages and liberal democracy

Ethnic, religious and linguistic identities are at the heart of political conflict and violence throughout the developing world—be it Sri Lanka, Nigeria or Rwanda. However, such cleavages may be much more benign if individuals have a *multiplicity* of local and cross-cutting cleavages. In some conditions, political entrepreneurs can make some of these identity cleavages more or less salient and thereby alter the nature of political coalitions. As mentioned in Subsection 2.1, this uncertainty about what identities may be salient tomorrow allows for the possibility of shifting coalitions. Therefore, uncertainty about whether today's majority will remain tomorrow's majority may temper maximalist demands of today's majority and lead to greater accommodation of the minority and the possibility of an *LD*.

Indeed, the puzzle of democracy in India (albeit an imperfect liberal one) is, arguably, this multiplicity of identities (see Varshney, 1998). As argued by Lipset (1994), 'the cross-cutting cleavages of impoverished India linked to allegiances of caste, linguistic and religious groupings have contributed to the institutionalization of democracy'. These multiplicity of local and regionally specific cross-cutting identities has allowed for the possibility of shifting political coalitions. Arguably, this has prevented (so far) the consolidation of the Hindu majority into a bloc that permanently excludes other minorities.

Similarly, Mauritius is one of the only examples of a successful political transition to a multiethnic liberal democracy in Africa (Brautigam, 1997). At independence, the country was divided into a South Asian majority and a significant minority of European planters and Creole voters. However, the South Asian majority was also further divided not just between Muslims and Hindus, but also across plantation workers, small-scale sugar farmers and petty traders. These cross-cutting cleavages opened up the space for the possibility of shifting coalitions, so no group could be guaranteed a permanent majority.

The bottom line is that in these diverse polities, political coalitions may shift, and today's majority coalition may end up in the minority coalition tomorrow. In these cases there is a nature dynamic towards accommodation of the minority and the emergence of a liberal democracy.

Another way of illustrating this point is by examining Lebanon and the collapse of its political system. Lebanon may be an odd country to bring up as an example of liberal democracy in view of hard times which have befallen the country's political system, but prior to the civil war, which lasted from 1975 to 1990, it was a model democracy in a region sorely lacking in liberal politics. In terms of identity cleavages, Lebanon is a mosaic of religions and ethnicities. The

country is divided between Christians and Muslims, with each major religion in turn divided among different denominations (Maronite, Greek Orthodox, Shia, Sunni). It has a history of providing each religious community its own autonomy going back to the millet system under the Ottomans. The modern consociational regime was created in 1943 by a national pact between the Muslim and Christian communities. What is distinctive about this regime is that public offices were explicitly apportioned among religious denominations. At the apex of the political system, the presidency was allocated to a Christian Maronite, the premiership to a Muslim Sunni and the speakership to a Muslim Shiite. This principle extended downwards to other government positions.

The reasons behind the decline of Lebanon's democracy are also telling and consistent with our framework. The principal cause behind the civil war was the influx of Palestinian refugees from Jordan, which altered the demographic and political balance between Muslims and Christians. There had not been a census since the 1930s, and there was already a sense that the existing distribution of political power was short-changing the Muslims. With the influx of Palestinians, the fragile consociational regime became unsustainable—there was now no ambiguity that one group was the de facto numerical majority and also had the political and military means to back it up (buttressed no doubt by the external intervention by the Israelis and Syrians).

## 4. Discussion

The emergence of liberalism has been discussed to date mostly in the realm of the history of ideas (see also Rodrik, 2014). The political economy literature on democratic transitions, meanwhile, has largely conflated electoral democracy with liberal democracy. Our aim in this paper was to partially fill in the blind spots that were created as a result. We have stressed that liberal democracy is a special beast. It does not arise if it is not based on a particular political configuration. Liberalism must have political legs—in addition to normative appeal—to get any mileage. And the political–strategic conditions that are generally held responsible for the rise of democracy tend to produce electoral rather than liberal democracy.

The crucial building bloc of our analysis is a taxonomy of political regimes, based on a tripartite division of rights: property rights, political rights and civil rights. We have argued that these rights operate across two fundamental types of cleavage in society: an elite/non-elite cleavage that is largely economic or class-based, and a majority/minority cleavage that typically revolves around the politics of identity. Property rights are important to the elite; political rights empower the majority; and civil rights protect the minority. Liberal democracy requires all three sets of rights, while the bargains that produce electoral democracy generate only the first two. Democratic transitions rely on the resolution of conflict between the elite and the masses. Our central message is that in the presence of additional cleavages—identity cleavages in particular—this resolution does little, in general, to promote liberal politics. The stars must be aligned just right for liberal democracy to emerge. The rarity of liberal democracy is not surprising.

Our exploration of the interest-based strategic foundations of liberal democracy is only a first step. We have ignored a powerful force in the origin and persistence of liberal democracy— namely the role of ideas. Ideas of liberalism, multiculturalism, inter-ethnic accommodation and equality (enshrined in the Universal Declaration of Human Rights in 1948) all have played a role (Kymlicka, 2007). The transmission of these ideas may be through education, the media or a by-product of globalisation. Indeed, the liberal democratic impulse may well have been

reinforced by external intervention (e.g., divestment in South Africa) or undermined in other cases (Majumdar and Mukand, 2015). Exploring the ideational foundations of liberal democracy would also help throw light on the rise of populism and the erosion of liberal democratic norms that we see across the globe.

We close the paper with a comment on the economic consequences of different types of democracy. As we highlighted in our model, liberal democracies provide more inclusive public goods compared to electoral democracies. We can conjecture that their economic performance should be correspondingly superior. In future work, it would be interesting to examine whether, for example, how long-term growth rates differ across the two types of democracies. In particular, the inconclusiveness of empirical findings to date on the growth effects of democracy may have something to do with the lack of differentiation in the literature between electoral democracies and liberal democracies.[17]

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Additional Supporting Information may be found on the online version of the article:

**Online Appendix A. Empirical evidence and cross-national evidence**
**Replication Package**

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[17] See Acemoglu *et al.* (2014) and Pozuelo *et al.* (2016) for two recent papers with contrasting findings. Indeed, the Table A8 in Acemoglu *et al.* (2014) shows that civil liberties seem to be more robustly correlated with growth than are political rights.

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