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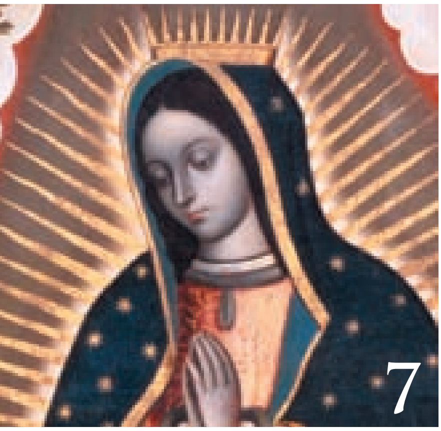

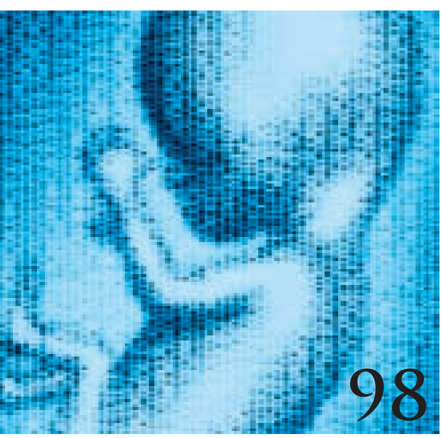

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REVIEWS

NOTES & LETTERS

Capitalism and Democracy

Hilton L. Root

How and why did democracy's good name become a norm of contemporary international society? In a terse, clearly written philosophical treatise, Michael Mandlebaum, Christian Herter Professor of American Foreign Policy at the Johns Hopkins School of Advanced International Studies, claims that its golden reputation comes from the successful fusion of two separate political traditions, one elevating individual freedom and the other popular sovereignty. During the 19th century, most Western elites viewed rule by the people as inclined to demagogy and hence an enemy of economic liberty, private property, religious and political rights. The fusion that transformed individual freedom and popular sovereignty from being perceived as opposites into being hailed as complements explains the extraordinary surge of democracy during the last quarter of the 20th century.

Democracy's Good Name: The Rise and Risks of the World's Most Popular Form of Government
by Michael Mandelbaum
PublicAffairs, 2007, 336 pp., $27.95

Supercapitalism: The Transformation of Business, Democracy, and Everyday Life
by Robert B. Reich
Knopf, 2007, 288 pp., $25

Mandelbaum expounds two major causes for this transformation, one direct and one indirect. The indirect cause was the global success of the Anglo-American countries. The world's powerhouse economies, democracies all, have long been led first by Britain and then by the United States. As these nations grew more prosperous and more powerful, their political institutions and practices came to be admired and imitated, exerting "democratic exemplarism" for others to follow. British and American wealth and power has given democracy a boost that no rival political system can match, forming the nucleus of a socially cohesive cluster of democratic transplants all over the globe in which representative government and prosperity are strongly correlated.

The direct, even more compelling causes are economic liberty and the working of the free market. Mandelbaum refers to these dynamics as the most influential and universal school of democratic politics and liberty. As he explains it, the skills and attitudes that arise from the play of the free market are transferred from the economy to the polity. It is in the marketplace where people form

> the habit, and the expectation, of exercising, through individual choice, a measure of control over the larger economic system in which the individual participates. It is natural for them to carry over into the larger political system in which participants in the market also reside: and this habit, and this expectation, encourage the practice, essential to democracy, of popular sovereignty.

Moreover, Mandelbaum points out, free markets create the wealth that underwrites democratic political participation. Wealth creates and sustains organizations and groups independent of the government: business, trade unions and professional associations. Thus, as Milton Friedman used to argue, Mandelbaum contends that democracy requires private centers of economic power to counterbalance central state authority. Backed by the "examplarism" of Anglo-American wealth and the lure of the international economy, the impulse toward democracy has become the "political equivalent" of a law of gravity, a force drawing the world toward a common political destiny.

Mandelbaum is an optimist and, to some extent, a functionalist. He avoids getting tangled up in arguments over democracy promotion, tending to the view that the maturation of free markets around the world (he worries that the Middle East might be an exception) will ultimately produce that outcome anyway.

Mandelbaum is deeply knowledgeable in political theory and philosophy, and in a sense his thesis in *Democracy's Good Name* harkens back to some of the oldest and most cherished beliefs of Anglo-American liberalism. The problem is that what *ought* to be, here meant both as social science expectation and moral norm, is not what actually *is*.

It falls to Robert Reich, the former Secretary of Labor and now professor of public policy at the Goldman School of Public Policy at Berkeley, to explain that democracy's glittering good name is today being tarnished by the same forces that Mandelbaum sees behind its remarkable rise. What has long worked, at least in most instances, within societies does not seem to be working in the same way at all—and has in fact gone topsy-turvy—now that economic relations are scaled up to global proportions. Global markets, Reich asserts, have unleashed economic forces that are becoming too powerful for democratic institutions to control. The free market has created "supercapitalism", and it is killing democracy. Instead of leading to free societies, supercapitalism is constraining the power of people to achieve their civic and personal goals.

Even the places where democracy originated are not immune from the corroding effects of supercapitalism, according to Reich. The global free market is eroding individual liberty and effective popular sovereignty in the Anglo-American world itself, the world where huge business organizations, exactly the kind that Mandelbaum's free markets have sired, are so powerful that they overwhelm the capacity of democratic institutions to constrain them. Neither governments nor citizen groups have the endowments to absorb the surge of supercapitalism, as its superlobbying trumps all means deployed to protect citizen rights.

Worse, supercapitalism is spilling over national boundaries with abandon. New forms of superlobbying that are constitutionally tolerated in the United States appear as a specter of corruption to many European and non-Western nations. The market in its current form, argues Reich, is giving democracy a bad name, not a good one.

In Reich's account, the irresistible logic of supercapitalism is that people's desires as consumers and investors overwhelm what they can get from their governments by way of equity and public goods. Moreover, many of the public goods that citizens require to thrive, such as public education, environmental protection and social insurance, are in scarce supply because neo-liberal states increasingly lack the revenue to offer citizens assurances of equity or security. The logic of the market, which endows global brands with tools that poorly organized and diffuse citizens or civic society lack, is increasingly setting the rules of the game.

The future of both the market and democracy, Reich concludes, will be determined by efforts to place capitalism back under the regulation of the citizens it is supposed to serve. He proposes several mechanisms to prevent corporations from endangering the societies from which they emerged, not least laws to protect shareholders from having their money used by corporations essentially without their consent. First and foremost among his proposals, Reich calls for the repeal of the corporate income tax to eliminate the fiction that corporations are citizens. Taxing shareholders directly, he argues, will restore civic values because shareholders will place their interests as citizens above their interests in any particular business enterprise.

Reich's larger goal is to constrain corporations from hiding behind the illusion that their legal personality is a license to speak either as or on behalf of citizens. It is illusory, he contends, to think that firms can be good citizens when they owe their first and foremost allegiance to their shareholders. Social responsibility can never replace responsibility for company performance, expressed as returns to capital invested. Believing that the promise of corporate democracy is illusory, Reich would change the tax terms of corporate contributions to charity, as well.

If Reich is correct, unless U.S. citizens become more aware of the dangers their democracy faces and take corrective action, America itself will cease to be an impressive model that commands the attention of others. And, after all, other models of political and economic organization are starting to vie for center stage: Both China and Russia are exhibiting strong economic growth, largely through participation in the global economy, without building democratic institutions. Democratic convergence has yet to result from pro-market reforms in China, where the Communist Party is welcoming wealthy business leaders into its ranks. A compliant middle class is a cornerstone of a repressive, re-centralizing regime in Russia, as well. How can that be if Mandelbaum's basic thesis—that market economics will lead to political democracy—is right?

Perhaps it is not right, or at least not right yet. The fact of growing middle classes in both China and Russia is not translating into sentiment for democratic reforms because, as Bruce Bueno de Mesquita and George Downs have argued, citizens will forgo venues for expression and coordination in exchange for opportunities to consume.[1] Leaderships in authoritarian "market" states cynically avert threats to their incumbencies by eliminating channels for civic organization and information dissemination by opposition groups, even as they encourage citizens to boost their economic status. Evidently, as the marginal cost of political expression goes up, citizens accept consumerism as a substitute, trading the right to assemble and speak out for access to the latest designer kitchen utensils and electronic gadgets. If today's free-market autocrats can create and distribute economic surpluses without making political concessions to their populations—and without letting local forms of supercapitalism erode their political control—then who is to say that Michael Mandelbaum, or Milton Friedman, for that matter, will long remain at all persuasive?

Western corporate collusion in the entrenchment of small cliques of wealthy families creates enemies for global capitalism.

And the liberal view becomes even less persuasive as one moves from the intersection of domestic politics and economics to the larger pull of globalization. In democratic India, for example, the developing world's other emerging powerhouse economy, measures of economic freedom fall well below middle-income country averages. Meanwhile, an important component of democracy, local self-government, is making progress without country-level democracy in China. Individual economic freedom has consistently gained greater protection from authoritarian East Asian regimes than from democratic South Asian ones.

Despite being a democracy, India is also less open to the world economy than China, which suggests that developing-world democratic institutions can be a barrier to full engagement in global economic opportunities. That reverses the causality Mandelbaum posits: At least at the global level, the correlation between free markets and plural politics breaks down, and it seems to do so from both ends. Democratic politics often do not support open markets, and open markets do not always reinforce the tendency to democratic government.

We can begin to explain this apparent contradiction of social science and common sense by recognizing that the slow, organic rise of democratic governance and the more recent installation of democratic regimes in the post-colonial epoch are not at all the same things. Again consider South Asia, where democracy has the longest history in the developing world.

Democracy throughout South Asia—in Sri Lanka, Nepal and Bangladesh as well as in India and Pakistan—has been derailed by dynastic politics, where trust depends on personalities rather than institutions. Winning elections is based on patronage and upon the selective dissemination of resources as private goods to party loyalists. Political parties typically lack respect for parliamentary duties and, in Nepal and Bangladesh, for example, typically boycott meetings just as they do in Iraq. In other words, instead of democratic habits of the heart shaping society over generations, local culture has instead shaped democratic habits, such as they are.

Where democracy has enabled a culture of impunity for those who can afford it, citizen

[1]Bueno de Mesquita and Downs, "Development and Democracy", *Foreign Affairs* (September/October 2005).

cynicism often nurtures extremism. Mandelbaum acknowledges the danger of extremism in democracies, because radicals enjoy the protections of due process. But in South Asia extremism thrives for different reasons: because democracy has failed to provide the mass of citizens with basic endowments of health, sanitation, literacy and public security. Thus, patronage-based elite-class democracy can be a breeding ground for political violence—even Maoism, as in Nepal, and terrorism, as in Sri Lanka.

Mandelbaum as theorist and philosopher does not offer a single quantitative test of his theory that free market reforms create a pathway to liberalized political expression. That is not unusual or particularly problematic; political theory and philosophy is a perfectly respectable pursuit, and it has its own rigorous rules of evidence, even in the absence of quantitative social science. But Mandelbaum also fails to provide a realistic explanation for the incentives of the principal actors in his model, offering no assessment on the conduct of multinational corporations. He sees them as they should behave, not as they actually are behaving.

Other political scientists have been busy testing time-honored Anglo-American tenets, and have found them curiously unable to explain reality. For example, Quan Li and Rafael Reuveny have discovered that openness to trade does not make a dynamic contribution to institutional reform in non-democracies; indeed, it correlates negatively with democratic institutions in a wide cross-sample of regimes. The level of democracy decreases as levels of trade openness increase, as the China and Russian cases cited above would suggest.[2] Other studies have suggested that the increased inequality often associated with foreign direct investment disrupts democratic stability.[3] World Bank data on governance reveals that as the world has become more democratic, governance as measured by transparency, rule of law and corruption deteriorates.

These disappointing correlations track faithfully with Reich's basic analysis. Young, still-developing democracies lack the resources and the institutions to counteract the enormous lobbying power of global business. Young democracies have few mechanisms to prevent large corporate contributions from influencing political outcomes. Even mature democracies, after all, often fail to meet this challenge.

When Anglo-American type firms expand their operations overseas, Mandelbaum's theory would assume the values and habits of the governance standards required in their home markets are promoted in new markets overseas. However, U.S. corporations overseas do not typically behave as corporate good citizens because the American investor seeking overseas partners in under-institutionalized markets is often best satisfied by selecting well-connected partners. Such partners are often firms owned by entrenched elites with insider connections to political officeholders. These connections, in turn, offer impunity from public scrutiny and the supervisory standards of competitive capitalism, such as sanctions against mismanagement or the seizure of collateral in bankruptcy cases.

Should we be surprised that democratically governed Western firms will seek out politically convenient partnerships? In markets where the courts cannot be counted on to protect property rights, or where tax collection is discriminatory, for example, investors would be spurning their fiduciary responsibility to their shareholders if they behaved otherwise. That is why, as Reich notes, "the move toward improved corporate governance makes companies less likely to be socially responsible."

Western corporate collusion in the entrenchment of small cliques of wealthy families is the unintended consequence of making the right decisions for shareholders, but it creates enemies for global capitalism. This enmity is a negative global good that weakens system-wide legitimacy. Moreover, the same enmity helps to explain why many outside America view U.S. democracy activism as a form of guiltless imperialism. As they see it, such activism opens the door for the supercapitalist, come to despoil the hapless masses. Most Western observers believe trade is a democratizing force because, through

[2] Li and Reuveny, "Economic Globalization and Democracy: An Empirical Analysis", *British Journal of Political Science* (2003).

[3] Charles Boix and Louis Gariciano, "Democracy, Inequality and Country-Specific Wealth", unpublished manuscript (2001).

stiffer international competition, it tends to force productive assets into the hands of those who can make best use of them. In theory, anyway, trade should drive down corruption, nepotism, gate-keeping and market distortions of all kinds. In fact, economic elites in many nominally democratic countries run markets so highly distorted that trade functions to make them still richer and no more efficient at the same time. Western supercapitalism, as Reich argues, has made it easier for them to do so.

There is thus a gaping whole in Mandelbaum's analysis: The behavior of key international agents such as multinational corporations in emerging regions is simply not consistent with his case. The expectation that market capitalism will create social foundations for the spread of Western-style democracy fails to anticipate the capture of weak democratic institutions in emerging states by wealthy minorities. Many of the business deals that benefit these wealthy minorities are fashioned from a combination of foreign policy and government power. They almost invariably involve what amounts to insider trading between government officials in the capital city, abetted by increasingly close connections and movements between domestic and transnational capital, often at the expense of the majority of people. Reich doesn't use the analogy, but this qualifies as a form of carpetbagging on a global scale.

In short, the free market school for democracy is not doing as well as Mandelbaum asserts, or as most of us would like. Reich's concerns about the dangers posed by global supercapitalism, both within countries and to the global economy writ large, seem at least for the time being to be a more persuasive account of what is going on. Mandelbaum may be proven right in the long run, and rather a lot of U.S. policy presumption is riding on whether that turns out to be so. But even if it does, the long run doubtlessly involves many a daunting detour. So put a candle in the window, and let's all hope for the best.

Hilton L. Root *is professor of public policy at George Mason University. His latest book,* Alliance Curse: How America Lost the Third World, *will be published in spring 2008 by the Brookings Institution Press.*