# Chapter 3   Populism, Majority Rule, and Economic Freedom

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## 1  Introduction

The past decade has provided vivid testimony to the rise of political populism. Contrary to earlier populist episodes, the phenomenon was not limited to its traditional field of Latin America, but has now firmly established itself as a significant political force in practically all high-income democracies of Western Europe and North America. Although research is only beginning to understand the consequences of its rise to power, an important recent assessment by Funke, Schularick and Trebesch (2023) suggests that the economic and institutional costs of populism in government are potentially high. In the United States, for example, there is already an ongoing discussion of what a possible return of Donald Trump to the presidency in 2025 would mean for the country's political and economic freedoms.

Overall, the rise of populist politicians and their party movements into positions of government responsibility have sparked a fair amount of research on its *determinants* in recent years. Here, a series of influential studies has found that economic globalization in general, and trade with the People's Republic of China in particular, as well as the ensuing effects for inequality and economic insecurity, may all have functioned as important drivers of the populist rise (Autor, Dorn, Hanson, and Majlesi, 2020; Gozor, 2022). In this context, other authors have further highlighted the role of immigration, identity politics, and international institutions (Guiso, Herrera, Morelli, and Sonno, 2019; Guriev and Papaioannou, 2022). Recently, Bergh and Kärnä (2020, 2022) make the important observation, though, that many studies finding globalization and inequality to be drivers of the recent populist success are mostly conducted at the micro-level. At the cross-country macro-level, these authors find no such association.

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In contrast to the vast number of studies on the determinants of populism, and partially due to the (still) rather limited number of available observations, there are not too many comparative empirical studies that have looked at the economic and institutional *outcomes* produced by populist governance. Still, despite their limited coverage, these studies find that, overall, populism in government produces undesirable consequences for the economy and the institutional arrangement of affected countries (Huber and Schimpf , 2017; Absher, Grier, and Grier, 2020; Bennett, Boudreaux, and Nikolaev, 2021, 2023; Funke, Schularick and Trebesch, 2023; Strobl, de Viteri, Rode, and Bjørnskov, 2023), suggesting that we may have reason to be concerned about the rise of populism into positions of power, if the preservation of liberty and creation of wealth is our concern. Regarding economic freedom, the only paper that explicitly deals with the effects of populism on economic freedom is a relatively early contribution by Rode and Revuelta (2015). Along the lines outlined above, these authors find empirical evidence that populism and economic freedom are essentially incompatible, as populist leaders tend to advocate for policies that restrict economic freedom, such as protectionism, an overly expansionary monetary policy, and higher government spending.

Notwithstanding, the study by Rode and Revuelta (2015) does not reflect the most recent populist episode that is mainly right-wing in nature, focusing instead extensively on the left-wing populist regimes of Latin America. Furthermore, it was conducted at a time when the measurement of populism was much more underdeveloped than at present. In a parallel manner, authors such as Weyland (1999) have in the past argued that especially right-wing populism and "neoliberalism" can coexist, essentially making the argument that populist movements may promote economic freedom by challenging established elites and corruption, thereby putting a check on crony capitalism. So, despite the vivid example of Donald Trump's war against free trade, and the dismal record on rule of law that many populist governments on the right present, there is a remote possibility that the most recent episode of right-wing populism may have produced different outcomes for economic freedom. These could be similar to the effects identified by Stöckl and Rode (2021) for financial markets, where these authors find that the negative effects stemming from the election of populist parties is primarily driven by populism on the political left.

Another related issue that has come up is the possibility that the relationship between populism in government and economic freedom may be significantly conditioned by a country's political institutions. For example, some scholars suggest that populist movements in countries with strong checks and balances may be less likely to restrict economic freedom, as these institutions provide a limit on executive power (cf. Levitsky and Ziblatt, 2018; Bennett, Boudreaux, and Nikolaev, 2021, 2023). Here, an instructive example is the case of Switzerland, which has championed one of Europe's most successful right-wing populist parties since the mid-1990s. Because of the Swiss system of forming executives, the Swiss People's Party (SVP) has also participated in numerous governments since that time, but with no apparent negative effect for the country's overall economic freedom ratings. These have remained stable and comparatively high ever since. In part, this may well be due to Switzerland's complex system of checks and balances, which heavily constrains the power of the federal government in Bern.

Following Rode and Revuelta (2015), this chapter reinvestigates the association of government populism and economic freedom, considering the potentially mediating roles of institutional constraints and government ideology. It does so by employing a recent measure of populism by Celico, Rode, and Rodriguez Carreño (2022) that offers a much larger time and country coverage than other comparable indicators. Controlling for a series of other determinants, findings show that populism in government is significantly associated with reductions in economic freedom for a large sample of democratic countries, where OECD countries are, nonetheless, differently affected by populism in government than non-OECD countries. For OECD countries, the association of populism and economic freedom seems to be mediated by political constraints and political ideology to a substantial degree. In contrast, populism in non-OECD countries is generally harmful for economic freedom, and it is not mediated by political constraints and ideology in a significant manner. The heterogeneity of our findings is probably the result of the important institutional guardrails that most OECD countries have in place, which put an important check on the power of populist governments, and that are often absent in many non-OECD countries.

## 2  What is populism: conceptualization and measurement

The concept of populism is arguably one of the most elusive that social science currently has to offer. Everyone seems to have an idea of which parties and politicians are populist, but the term has been applied to such a broad spectrum of actors that it is often not clear what similarities would justify such a categorization, outside that of personal ideological preferences. The economics literature, for example, has often equated populism with regimes employing radical left-of-center economic policies that eventually threaten the stability of the regime itself (Dornbusch and Edwards, 1991; Acemoglu, Egorov, and Sonin, 2013). This view of populism has often been criticized, because it places redistributive objectives at the center of its definition, thus focusing almost exclusively on left-wing populist regimes in Latin America (Hawkins, 2009).

An approach that also encompasses the more recent rise of populism on the right is the ideational definition, which focuses on the dualistic worldview of populism that sees "the people" engulfed in a cosmic struggle with "the elites" that have somehow managed to subvert the will of the people (Müller, 2017; Mudde and Rovira Kaltwasser, 2017). This definition thus focuses on the tendency of all populist movements to identify democracy with a certain party or leader who defends the people's interests against those of a privileged elite, essentially making it an ideological worldview on the functioning of politics. To have the will of the people prevail, some kind of revolution is needed and, as a consequence, populists tend to identify the minority rights of liberal democracy as unjustly protecting the conspiring elites, frequently calling for their abolition (Hawkins, 2009). This type of discourse or policy style is independent of political ideology and can be found both on the political right, and on the left, which usually act as a type of host-ideology (Mudde and Rovira Kaltwasser, 2017). In the case of left-wing populism, the conspiring elite is mostly the "neoliberal" business establishment, while in the case of right-wing populism, it is the "liberal" cultural elite that undermines national identity and culture. While this distinction is important for the definition of populist ideology, it should also be mentioned here that right-wing populists often attack business elites as well.

Practically all attempts to quantify the populism of parties and politicians are based on some version of this ideational definition, which is also the one we will stick to in the following. Existing indicators of populism can generally be divided between demand-side and supply-side measures. The former attempts to capture the populist political attitudes of voters, while the latter tries to quantify the degree of populism employed by political leaders and parties. Overall, the development of supply-side measures is currently much more advanced than that of demand-side measures. Since our own objective is to capture government populism in some form, we only focus on the political supply-side for the purposes of this chapter.

## Capturing supply-side populism

Several measurement approaches to capturing supply-side populism can be distinguished in the academic literature. First, an initial set of attempts mainly used discourse analysis to measure the degree of populist rhetoric employed by political leaders. For instance, Hawkins (2009) developed an early dataset that is based on the textual analysis of political speeches of 215 chief executives from 66 countries. Unfortunately, the coverage of these indicators is usually quite limited. Second, other authors have developed binary or categorical populism measures, such as the *PopuList* (Rooduijn et al., 2019) and the *Timbro Authoritarian Populism Index* (Heinö, 2016). Although these offer wide temporal and geographic coverage, critiques have pointed to the fact that the multidimensional complexity of populism can hardly be explained sufficiently by a zero-one dynamic (Hawkins, 2009). Third, most recently a series of datasets employ surveys of academic experts to qualify the degree of populism employed by political parties for a wide set of different parties and countries (Norris, 2020; Meijers and Zaslove, 2021). Despite the precise definitions and methodological consistency offered by these indicators, these are only available for rather short periods of time.

In this chapter, we employ a populism indicator by Celico, Rode, and Rodriguez Carreño (2022) that employs machine-learning tools to greatly extend the temporal coverage of the measure by Meijers and Zaslove (2021), combining different expert surveys via random forest-regression algorithms. The resulting indicator captures party-level populism on a continuous 0-to-10 scale, covering 1,920 parties in 163 countries from 1970 to 2019. Zero represents pluralist parties, while 10 represents populist parties. Since their underlying base data is available for all countries with a national legislature, Celico, Rode, and Rodriguez Carreño (2022) are able to calculate populism scores for countries in democratic and autocratic countries. It may, in principle, be somewhat a matter for discussion how much the phenomenon of populism is applicable to non-democratic settings. Still, many authors have successfully applied the concept to autocracies in past research (e.g., Mudde and Rovira Kaltwasser, 2017; Funke, Schularick and Trebesch, 2023) and autocratic leaders like Vladimir Putin are vividly demonstrating at present what autocratic populism essentially looks like. In the following, we employ the data for democratic and autocratic countries for illustrative purposes but limit our empirical analysis to electoral democracies only.

**Figurze 3.1** shows the ten most populist parties between 2010 and 2019, which we show separately for OECD and non-OECD countries.[1] Focusing first on the

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1 *Populist parties in OECD countries*: PVV = Party for Freedom; LsNS = People's Party Our Slovakia; AfD=Alternative for Germany; PiS = Law and Justice; SPD= Freedom and Direct Democracy;

Figure 3.1: The ten most populist parties in OECD and non-OECD countries, 2010–2019
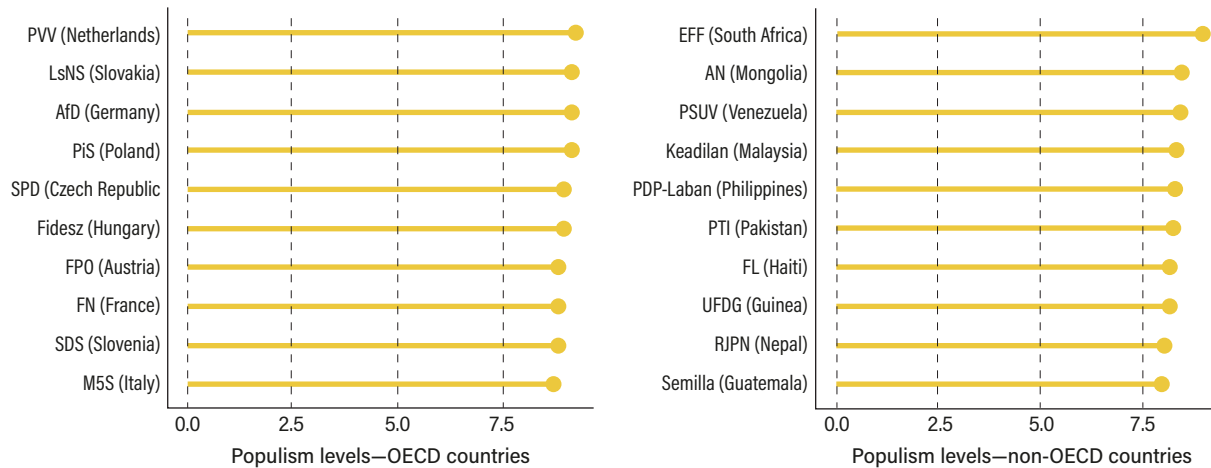


Source: Random Forest Populism Indicators (Celico, Rode, and Rodriguez Carreño, 2022).

left-hand panel for OECD countries, the list contains some very obvious candidates, such as the Dutch Party for Freedom (PVV) under its flamboyant leader Geert Wilders, the Italian Five Star Movement (M5S) founded by comedian Beppe Grillo, or the Alternative for Germany (AfD) that has recently made headlines with its openly revisionist rhetoric concerning Germany's WWII past. Similarly, the Polish Law and Justice Party (PiS), as well as the Hungarian Fidesz party under the leadership of Victor Orban, both of which have gone about dismantling their respective country's system of democratic checks and balances in recent years, figure prominently in this list. In the right-hand panel of figure 3.1, we also find many well-known populist parties in non-OECD countries, such as Julius Malema's Economic Freedom Fighters (EFF) in South Africa, the United Socialist Party of Venezuela (PSUV), founded by former president Hugo Chavez and currently led by the present chief executive Nicolas Maduro, as well as the Philippine Democratic Party–Strength of the People (PDP-Laban), which is chaired by the country's former populist president, Rodrigo Duterte.

Aggregating the party-level populism indicator of Celico, Rode, and Rodriguez Carreño (2022) to the country level is not straightforward. We opt for an approach that considers both the degree of populism presented by a respective party and its relative strength inside a government coalition, similar to the approach taken by Stöckl and Rode (2021). In so doing, we create a measure that is the parliamentary-seat-share weighted degree of populism for all parties that make up a government coalition, employing data provided by the V-Party dataset by Lührmann and colleagues (2022). Of course, this may be a somewhat imperfect proxy for presidential systems of government, where, for example, the chief executive is populist, but whose party does not necessarily enjoy a parliamentary majority. Notwithstanding, these cases should be few. **Figure 3.2** shows

Fidesz = Fidesz – Hungarian Civic Alliance; FPO = Freedom Party of Austria; FN = National Rally; SDS = Slovenian Democratic Party; M5S = Five Star Movement. *Populist parties in non-OECD countries*: EFF = Economic Freedom Fighters; AN = Democratic Party; PSUV = United Socialist Party of Venezuela; Keadilan = People's Justice Party; PDP-Laban = Philippine Democratic Party-Strength of the People; PTI = Pakistan Movement for Justice; FL = Lavalas Family; UFDG = Union of Democratic Forces of Guinea; RJPN = National People's Party, Nepal; Semilla = Seed Movement.

Figure 3.2: The distribution of government populism worldwide (last available election)
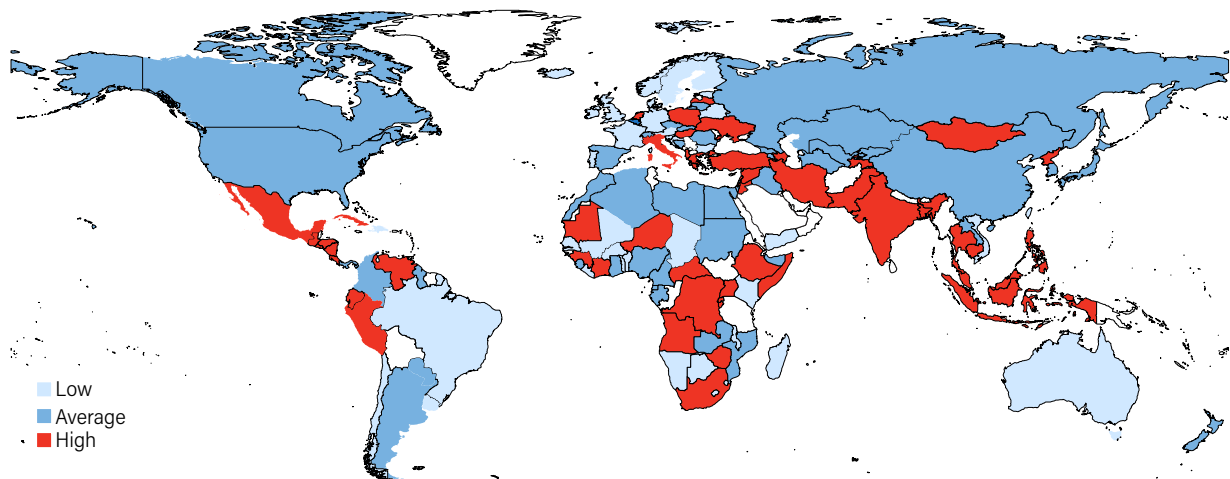


Note: Displayed categories are based on populism in government terciles.

Source: Celico, Rode, and Rodriguez Carreño, 2022; Lührmann *et al.*, 2022; authors' calculations.

the distribution of government populism worldwide, always employing the latest election available. A brief visual inspection shows that many recent episodes of populism in government are quite adequately represented, such as the cases of Italy, Poland, Hungary, Turkey, Venezuela, Mexico, or India. Despite the recent advances of political populism in many Western high-income countries, the figure nonetheless also makes clear to what a large extent the phenomenon is centered on non-Western middle- and low-income countries, extending nowadays also far beyond the limits of Latin America.

**Figure 3.3** shows the evolution of average government populism from 1970 to 2019, where scores are normalized on the value of 1970. It can be seen here that overall populism was comparatively low during the 1980s and 1990s, which were also two decades characterized by considerably less political polarization than others during the twentieth century. It is clearly visible that populism in government has been on the rise again since the early 2000s though, reflecting what Mudde (2004) has prominently called the "populist zeitgeist". Interestingly, this development started long before most other observers seemed to take notice. The figure also clearly shows the last sharp increase in government populism during the 2010s, when the topic first rose to a certain prominence with the larger public, following the success of new populist politicians and parties in the aftermath of the Great Recession.

## 3  Economic freedom, populism, ideology, and political constraints

In the following section, the relationship between populism and economic freedom is analyzed empirically. Economic freedom is measured by the index published in *Economic Freedom of the World: 2022 Annual Report* (EFW) (Gwartney, Lawson, Hall, and Murphy, 2022). Prior research has shown that this measure is related to many other important variables, such as overall income and growth, investment, unemployment, trade, entrepreneurship, democracy, and human rights (Lawson, 2022). Our most basic estimation model has the following functional form:

Figure 3.3: The evolution of populism in government, 1970–2019
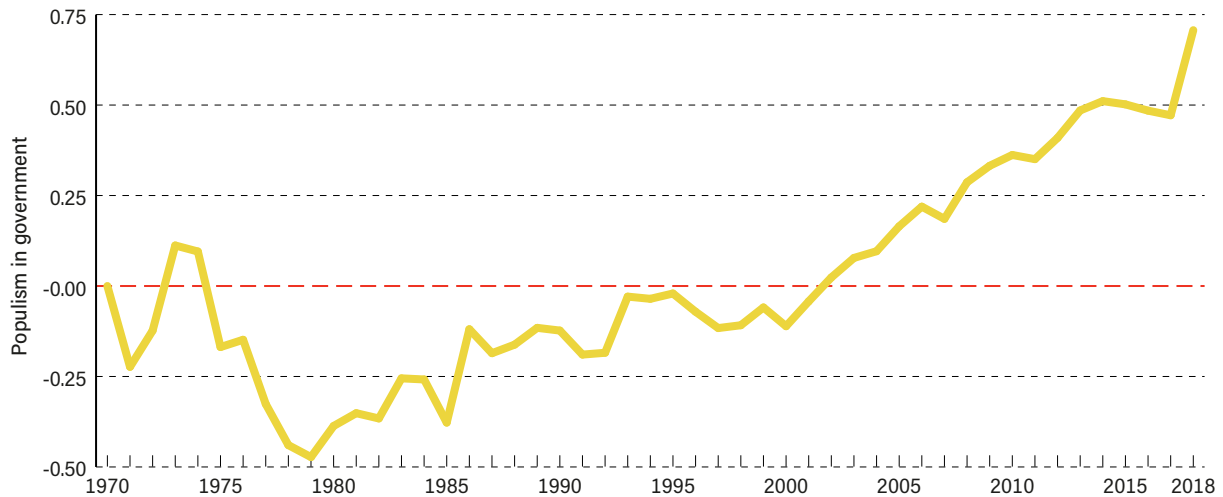


Source: Celico, Rode, and Rodriguez Carreño, 2022; Lührmann *et al.*, 2022; authors' calculations.

$$\Delta EFW_{i,t} = \beta_1 EFW_{i,\,t-1} + \beta_2\,POP_{i,\,t-1} + \beta_3 POLCON_{i,\,t-1} + \beta_4 IDEO_{i,\,t-1}$$
$$+ \beta_4 logGDPpc_{i,\,t-1} + \delta_i + \gamma_t + u_{i,\,t}$$

Following Rode and Revuelta (2015) to a large extent, we employ the annual variation in the five-year rolling averages of the EFW index as our dependent variable to determine the specific outcomes of government populism for following changes in economic freedom, further introducing the initial average EFW index value as a primary control variable. Initial values are always the preceding five-year rolling average. An inverse relationship is expected between the initial average EFW value and the following change in EFW, indicating that countries with a lower initial average EFW rating are likely to liberalize more rapidly in subsequent periods. Although the EFW index is only available on an annual basis starting in the year 2000, we impute annual values for the preceding five-year intervals on a linear basis, allowing us to estimate with the full dataset from 1970 to 2019.

Populism in government (POP) is the seat-share-weighted degree of populism by Celico and colleagues (2022) for all parties that form part of a government coalition, using information on coalitions by Lührmann et al. (2022), where we also calculate the five-year rolling average. Again, following Rode and Revuelta (2015), we expect populism in government to be associated negatively with changes in the EFW index. As highlighted in the introduction, the association between populism and economic freedom may, nonetheless, be mediated by political institutions that establish strong checks and balances on an executive, or by the political host-ideology of the populist government that is in power.

To control for the possibility that the relationship between populism in government and economic freedom may be significantly conditioned by a country's political institutions, we need to capture the degree to which that power is concentrated in a political system. To do so, we introduce the five-year rolling average of the latest available version of the POLCON V index by Henisz (2000) to our estimation model. This index relies upon a simple spatial model of political interaction, incorporating information on the number of independent branches of government with veto power and the distribution of preferences across and within

those branches, in order to derive the extent to which any one political actor is constrained in his or her choice of future policies. The POLCON index ranges on a scale from 0 to 1, where higher scores indicate more constrained institutional settings. It is a little unclear what impact the POLCON index may have by itself for subsequent changes in the EFW, but we expect an interaction term of POP and POLCON to be positively associated with subsequent changes in economic freedom. This would indicate that populism in government can do comparatively less harm to economic freedom in institutionally more constrained settings, such as in the example of Switzerland that was highlighted in the introduction.

In order to examine the possible effects of political ideology in connection with government populism, we further introduce a measure of government ideology calculated from information by Lührmann and colleagues (2022) to our basic model. This index weights government parties' economic positions by their respective electoral performance, with the final index ranging on a scale from −3 to 3, where negative values represent an ideology on the political left and positive values represent an ideology on the political right, while zero represents the political center. Previous findings indicate that, taken by itself, government ideology may be an important determinant of economic freedom (Bjørnskov and Potrafke, 2012, 2013; Jäger, 2017), with left-wing governments generally being comparatively more harmful for the development of economic freedom. In this case, government ideology should enter our equation with a positive sign. To control for the fact that populist governments of different political ideologies may also have different effects on subsequent changes in economic freedom, we introduce an interaction term between variables POP and IDEO. Following the discussion in the introduction, it is somewhat unclear whether we would expect left-wing populism in government to be comparatively more harmful to economic freedom than right-wing populism. On the one hand, the personalist tendencies of populism and its underlying zero-sum logic may mean that it is generally harmful for economic freedom, regardless of its political ideology. On the other hand, populist movements on the right may be comparatively less harmful to economic freedom, or potentially even promote it by challenging crony capitalism, although the latter possibility is rather doubtful as outlined above.

Finally, a range of studies has found that initial average GDP per capita is a fundamental determinant of changes in economic freedom (e.g., Rode and Gwartney, 2012). Therefore, the logarithm of the five-year rolling average of GDP per capita in terms of purchasing power parity is also included in our basic model. This data is taken from the latest version of the Penn World Tables (10,0) by Feenstra, Inklaar, and Timmer (2015). We expect this variable to show up with a negative sign in our regressions, indicating that countries with a lower per-capita income will liberalize their economies comparatively quicker in subsequent periods.

All estimations further include country- and time-fixed effects, in order to account for the specifics of different time periods and different countries. The use of fixed effects together with our empirical strategy, which relates the level of populism to subsequent changes in economic freedom, should somewhat alleviate concerns of unobserved heterogeneity and reverse causality in our findings, at least in the short run. Still, prior research has established an empirical link between comparatively stronger political constraints and higher economic-freedom ratings on the one hand (Pitlik, 2007; Lihn and Bjørnskov, 2017) as well as government populism and the slow but steady erosion of political constraints on

the other (Huber and Schimpf, 2017). It should thus be stressed that our overall findings, and in particular the interaction effects, should be merely interpreted as correlational evidence, and not in a causal manner. **Table 3.1** shows summary statistics for all variables employed in the estimations.

Table 3.1: Summary statistics

| Variable | N | Mean | Std. Dev. | Min | Max |
|----------|------|-------|-----------|--------|-------|
| EFW | 2774 | 6,802 | 1,069 | 2,776 | 8,79 |
| POLCON | 2574 | 0,619 | 0,272 | 0 | 0,889 |
| POP | 2888 | 4,11 | 1,13 | 1,379 | 7,762 |
| IDEO | 2867 | 0,16 | 0,62 | -2,435 | 2,28 |
| logGDPpc | 2862 | 9,412 | 1,02 | 6,62 | 11,40 |

Given the uncertain association of populism and autocratic governance discussed above, we further limit our estimation sample to electoral democracies only, following the definition of Bjørnskov and Rode (2020). These authors elaborate on the minimalist democracy-dictatorship approach of Cheibub, Gandhi, and Vreeland (2010), defining democracies as those regimes where legislative and executive offices are chosen by contested and popular elections. Limiting the sample in this way obviously means that we cannot say anything about the possible correlation of autocratic populism and economic freedom, which is already an interesting research question in itself. It also means that some populist experiences, which become increasingly autocratic over time, may drop out of our sample when the country's institutions no longer satisfy our minimalist definition of democracy anymore. For example, this is the case of Venezuela under the governments of Hugo Chavez and Nicolás Maduro, which Bjørnskov and Rode (2020) count as a civilian autocracy from 2016 onward. Notwithstanding, if we are interested in the association of populism and economic freedom in conjuncture with majority rule, limiting the sample in this way will give us much cleaner and more reliable results.

## 4 Estimation results

Before we go into the description of our findings, briefly consider **figure 3.4**, which gives an overview of the association between government populism and economic freedom in a scatter plot. Here, country-year values are colored differently, depending on whether the corresponding states are OECD members, or not. The figure clearly shows a negative association between government populism and economic freedom, and this seems to be the case for both groups of countries. Notwithstanding, EFW levels seem to be somewhat higher, on average, while overall government populism may in turn be lower, in OECD member countries. Again, the figure makes clear to what a large extent populism and comparatively low economic-freedom ratings may essentially be a phenomenon of non-Western countries, where significant institutional checks and balances are also usually absent. Of course, the observed association might be driven by the high correlation between EFW scores and GDP per capita, for example, which is not controlled for in the graphic. This will be analyzed more formally in the following.

Figure 3.4: Populism and economic freedom
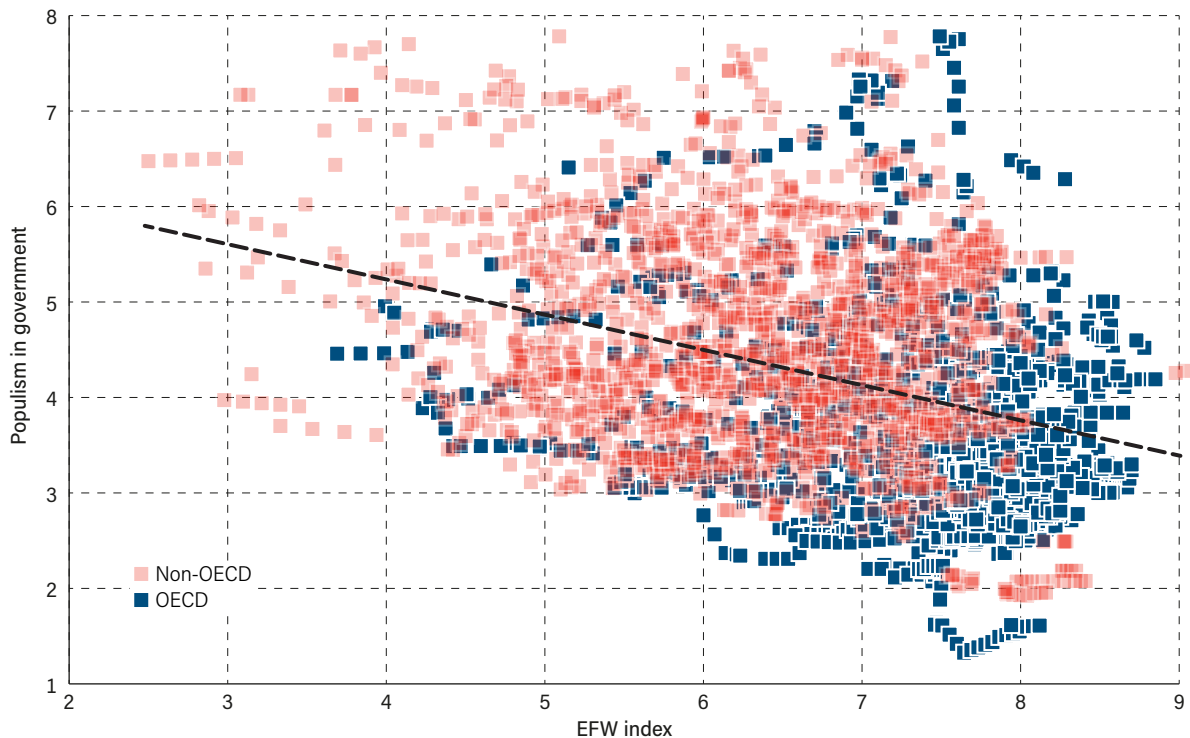


Sources: Celico, Rode, and Rodriguez Carreño, 2022; Gwartney, Lawson, Hall, and Murphy, 2022; Lührmann *et al*, 2022; authors' calculations.

**Table 3.2** shows results from regressing the annual change in economic freedom on its initial level, as well as the full battery of control variables. As indicated by the preceding figure, we show results for the full country sample, but further divide our data between OECD countries and non-OECD countries. Taking first some of the basic controls: table 3.2 shows that the initial average EFW score is negative and highly significant as a determinant of subsequent changes in economic freedom in the full sample, as well for both sub-samples. Thus, the cross-country analysis indicates that countries with lower initial average levels of economic freedom tend to achieve larger subsequent increases in the EFW index. This result is consistent with Rode and Revuelta (2015), as well as the findings by Rode and Gwartney (2012) and others. Coefficients obtained for log GDP per capita are always negative as expected, and the variable is statistically highly significant in the full sample. Notwithstanding, the two right-hand panels of table 3.2 make clear that this association seems to be driven by non-OECD countries, while coefficients are negative but insignificant for the sub-sample of OECD countries. This may essentially reflect the high correlation between two control variables in our OECD sub-sample, where countries with higher initial average EFW ratings also tend to present higher per-capita incomes and, on a comparative level, both these variables tend to score high among OECD member countries.

Coming to our principal variable of interest, it can be observed in models (1) to (3) of table 3.2 that government populism is negatively but insignificantly associated with subsequent changes in economic freedom in the full sample. Model (1) also shows that both the POLCON and ideology variables present the expected positive sign, but are both always insignificantly related to subsequent changes in the EFW index in the full sample. This picture is consistent when we introduce an

## Table 3.2: Estimation results

| | Full sample | | | OECD countries | | | non-OECD countries | | |
|---|---|---|---|---|---|---|---|---|---|
| | (1) | (2) | (3) | (4) | (5) | (6) | (7) | (8) | (9) |
| EFW | −0.040*** | −0.041*** | −0.040*** | −0.037** | −0.036** | −0.039** | −0.046*** | −0.046*** | −0.046*** |
| | (0.009) | (0.009) | (0.009) | (0.014) | (0.014) | (0.014) | (0.013) | (0.013) | (0.013) |
| POP | −0.014 | −0.014 | −0.020 | −0.008 | −0.036** | −0.010 | −0.032* | −0.037* | −0.032 |
| | (0.010) | (0.010) | (0.015) | (0.010) | (0.017) | (0.009) | (0.019) | (0.020) | (0.019) |
| POLCON | 0.024 | 0.021 | −0.028 | 0.107*** | −0.077 | 0.116** | −0.004 | −0.065 | −0.006 |
| | (0.040) | (0.039) | (0.145) | (0.035) | (0.116) | (0.036) | (0.050) | (0.247) | (0.050) |
| POP*POLCON | | 0.002 | | | 0.039* | | | 0.012 | |
| | | (0.007) | | | (0.023) | | | (0.048) | |
| IDEO | 0.000 | −0.010 | −0.002 | 0.027 | 0.027 | −0.014 | −0.013 | −0.015 | −0.022 |
| | (0.013) | (0.035) | (0.015) | (0.017) | (0.017) | (0.036) | (0.020) | (0.021) | (0.059) |
| POP*IDEO | | | 0.010 | | | 0.011 | | | 0.001 |
| | | | (0.027) | | | (0.010) | | | (0.011) |
| logGDPpc | −0.084*** | −0.084*** | −0.083** | −0.055 | −0.051 | −0.052 | −0.088** | −0.087** | −0.088* |
| | (0.029) | (0.029) | (0.029) | (0.044) | (0.043) | (0.043) | (0.035) | (0.036) | (0.035) |
| N | 2367 | 2367 | 2367 | 1104 | 1104 | 1104 | 1263 | 1263 | 1263 |
| Adj.R2 | 0.419 | 0.419 | 0.419 | 0.451 | 0.453 | 0.453 | 0.416 | 0.416 | 0.415 |
| WithinR2 | 0.090 | 0.090 | 0.090 | 0.097 | 0.101 | 0.101 | 0.094 | 0.095 | 0.095 |

Note: Heteroskedasticity robust standard errors in parenthesis: *** $p < 0.01$; ** $p < 0.05$; * $p < 0.1$.

interaction effect of our government populism variable and the POLCON index in model (2), and an interaction effect of government populism and political ideology in model (3). In both cases, the interaction effects again show the expected positive sign, but are always statistically insignificant.

This picture changes when we divide our sample into OECD countries and non-OECD countries in the right-hand panels of table 3.2. Model (4) shows that, taken by itself, the association of government populism and changes in economic freedom is also insignificant for our sub-sample of OECD countries, but this negative association becomes statistically significant at the 5% level upon introducing the interaction effect of government populism and the POLCON index in model (5). The coefficient on the interaction term is now also positive and significant, indicating that populism in government will hurt economic freedom comparatively less in OECD countries that exhibit strong institutional checks and balances on the executive. The left panel of **figure 3.5** is one possible way of interpreting the interaction of both variables in model (2), indicating

Figure 3.5: Marginal impact of government populism on economic freedom by political constraints
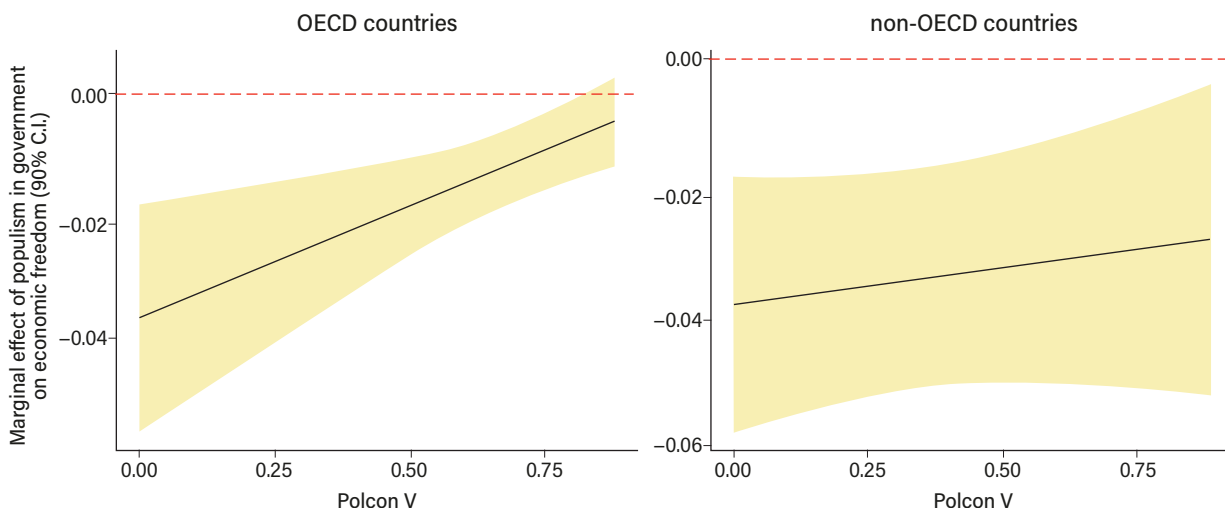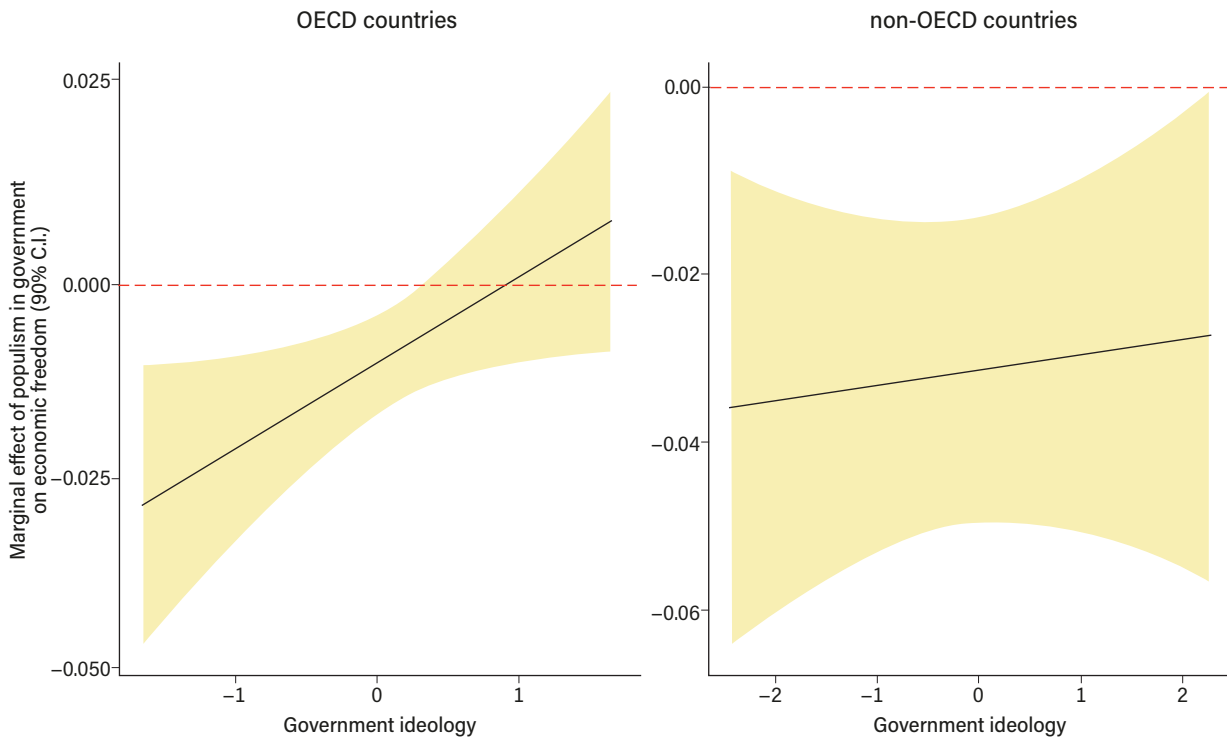


Source: Authors' calculations.

that an increase of one standard deviation in government populism is significantly associated with a reduction in economic freedom for OECD countries that exhibit relatively few institutional constraints on government power, while government populism is inconsequential for economic freedom in countries with strong constraints on government.

Interestingly, model (7) of table 3.2 shows that the association of government populism and changes in economic freedom is, in turn, significant and negative at the 10% level for the sub-sample of non-OECD countries. This would indicate that government populism is associated with reductions in economic freedom in non-OECD countries, regardless of the existence of political constraints. This is further confirmed when introducing the corresponding interaction term in model (8), which is graphically interpreted in the right-hand panel of figure 3.5: here, an increase of one standard deviation in government populism is significantly associated with a reduction in economic freedom for countries that exhibit comparatively lower institutional constraints on government power, but also for those countries that exhibit comparatively higher constraints on government power. The negative association between populist governance and subsequent changes in economic freedom is thus not mediated by political constraints outside of our sample of high-income Western democracies.

To be sure, the heterogeneity of our findings across sub-samples is probably due to the important institutional guardrails that most OECD countries have in place that put an important check on the power of populist governments. These guardrails are often absent in many non-OECD countries, and the unchecked governmental power of these electoral majoritarian democracies is probably what is also reflected in our findings, explaining further why we do not find a significant association between government populism and changes in economic freedom in the full sample. Although we do not want to make any causal claims here, indications are that high-income democracies with strong checks on the power of government may therefore be comparatively better protected against the potentially negative outcomes of populist governments for economic freedom than middle- and low-income democracies, where populist governance resulting from

Figure 3.6: Marginal impact of government populism on economic freedom by ideology



Source: Authors' calculations.

majoritarian elections may pose a real threat to economic freedom. In both sub-samples, the estimated impact of populism on economic freedom is, on average, only about one seventh of a standard deviation. This statistical effect is admittedly small, but it should be kept in mind that our dependent variable measures annual changes from five-year averages in the EFW index, meaning that we should not expect it to be very big either. If these effects cumulate over the time period of one or several legislatures though, they may become quite relevant indeed.

Models (3), (6), and (9) further introduce an interaction effect of government populism and political ideology to the full sample, and both of our sub-samples. While the interaction term is again insignificant in the full sample, **figure 3.6** graphically shows the marginal impact of populist governance for economic freedom, dependent on political ideology for OECD countries and non-OECD countries. In the left-hand panel of figure 3.6 it can be observed that, similar to the impact of political constraints, the association between government populism and subsequent changes in the EFW index in OECD countries is mediated by the political ideology of government to a significant degree. While left-wing populist governments are found to be associated with significant reductions in economic freedom, populist governance on the political right seems to be statistically all but inconsequential for a country's economic-freedom ratings. Similar to the findings by Stöckl and Rode (2021) for financial markets, right-wing government populism in Western high-income countries may, therefore, not necessarily be detrimental to economic freedom. Still, we find absolutely no indications that populist governments on the political right are engaged in the promotion of economic freedom either. In turn, left-wing populism is clearly associated with reductions in economic freedom, on average.

The right-hand panel of figure 3.6 shows that the association between government populism and economic freedom in non-OECD countries is clearly not mediated by political ideology to a significant degree. Albeit marginally insignificant on the far right, indications are that populist governments of any political ideology are associated with reductions in economic freedom ratings for the mostly middle- and low-income countries that make up our sample of non-OECD countries. Interestingly, the distribution of populist governments across the spectrum of political ideologies also seems to be much more extreme in that group of countries, when compared to Western high-income nations in the left-hand panel. Once again, it should be stressed that identification is uncertain but indications are that the impact of government populism on economic freedom in high-income democracies may ultimately depend on the political ideology of the populist government in power. In turn, populist governance is generally a threat to economic freedom in middle- and low-income democracies, disregarding the ideology of the populist government in power.

## Conclusions

This chapter reinvestigates the association of government populism and economic freedom following Rode and Revuelta (2015), who find empirical evidence that populism and economic freedom are essentially incompatible. Still, the study by Rode and Revuelta (2015) does not reflect the most recent populist episode that is mainly right-wing in nature, it does not take into account the potentially mediating role of institutions that restrict the power of the executive, and it was conducted at a time when the measurement of populism was much more underdeveloped than at present. This chapter considers the potentially mediating roles of institutional constraints and government ideology. Furthermore, we employ a recent measure of populism by Celico, Rode, and Rodriguez Carreño (2022) that offers much larger time and country coverage than other comparable indicators.

Controlling for a series of other potential determinants, our results show that populism in government is significantly associated with reductions in economic freedom for a large sample of democratic countries. Here though, OECD countries are differently affected by populism in government than non-OECD countries. For OECD countries, the association of populism and economic freedom seems to be mediated by political constraints and political ideology to a substantial degree. In contrast, populism in non-OECD countries is generally harmful for economic freedom and it is not mediated by political constraints and ideology in a significant manner. The heterogeneity of our findings is probably due to the important institutional guardrails that most OECD countries have in place, which put an important check on the power of populist governments, and that are often absent in many non-OECD countries.

To some degree, our results raise an important question: Is a political system based on unchecked majoritarian democracy really the best method to preserve economic freedom? This is an especially pertinent question at a time when many democratic societies worldwide are becoming increasingly polarized on a multitude of issues, and political populism on the left and right has firmly established itself as a viable political option for electorates to voice their frustrations. Just to make one thing absolutely clear: we are certainly not suggesting that some form

of soft autocratic rule is a better system to preserve economic freedom and wealth creation than liberal democracy. This logic is deeply flawed in itself, because all autocracies present at least a latent propensity towards political repression, which further tends to increase over time, eventually also harming economic liberties. Still, unchecked majoritarian democracy may do as much damage to economic freedom and wealth creation as many repressive autocratic regimes. Following the ideas of Hayek (2020), and to some degree those of Jones (2020), an ideal system of government for the continued development of economic freedom would reflect some combination of majoritarian rule with strong institutionalized checks and balances that limit the power of the central executives. Historically, this balance has been at the center of the idea of liberal democracy. However, in recent years, this constrained view of democracy has been replaced by one based on unchecked majoritarian rule. This change in the meaning and institution of democracy has been true even in Western democratic countries. If this trend continues, its political manifestation in unchecked populist rule may well present the most important threat to individual liberty and economic freedom since World War II.

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