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GLOBALIZATION-DEMOCRACY NEXUS: EMPIRICAL EVIDENCE FROM SOUTH ASIA

Abstract

The paper examines how globalization affects the level of democracy in South Asia. To test this question, conflicting theoretical positions in the literature - globalization enhances democracy; globalization hinders democracy; and globalization does not necessarily affect democracy - are evaluated empirically. The effect of FDI on political rights is measured in 5 South Asian countries using pooled time-series cross-sectional data for the period 1983 to 1999. Several statistical methods are conducted to test the link between FDI and political rights. Based on the results, the study finds that a positive effect on political rights should be expected from an increase in FDI. As a result of this finding, the paper concludes that globalization is likely to promote democratic governance in South Asia.

I. Introduction

The study of globalization and democracy is at the heart of political economy. Understanding how free market reforms and political reforms are related is one of the main challenges facing this field. *Does greater integration into the world economy further*

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or obstruct democratic governance? The existing evidence does not provide a clear-cut support of the links between globalization and democracy. While scholars found both positive and negative effects of globalization on democracy, others argue that globalization is not a significant determinant of democracy.

In Philip Cerny's words, "...globalization and democracy are deeply contested concepts..." [Cerny, 1999:2]. Globalization is a historical process with several dimensions, such as economic, political, social, environmental and cultural[1]. Democracy, on the other hand, could take various forms, i.e. direct democracy, representative democracy, liberal democracy, and procedural democracy[2]. In this paper, I will focus on *economic globalization* defined as the increasing integration of economies around the world, particularly through trade and financial flows [IMF, 2000:5-10]. The definition of *democracy* will be limited to "a political system that supplies regular constitutional opportunities for changing government officials, and a social mechanism which permits the largest possible part of the population to influence major decisions by choosing contenders for political office" (Lipset, 1959: 69-105).

Against such a backdrop, the paper presents an empirical analysis of the relationship between globalization and democracy for South Asia[3]. The regional experience with these two broad international trends has not been well substantiated. In an attempt to fill this void, the paper proceeds as follows. Section II examines the literature dealing with the impact of globalization on democracy. The methodology is described in section III. Section IV analyses the data. The results are discussed in section V. Section VI wraps up the paper.

II. The Globalization-Democracy Debate

Literature on linkage between globalization and democracy is sizable, but it is mostly theoretical. Existing scholarship posits three competing positions - globalization enhances democracy;

globalization hinders democracy, and globalization does not necessarily affect democracy. In what follows, a summary of the arguments from studies supporting each of these theoretical positions is presented.

Globalization Enhances Democracy

In the views of Schumpeter (1950), Platner (1992), Weitzman (1993), Lipset (1994), globalization fosters economic growth, increases the size of the middle class, promotes education, and reduces income inequality, all of which contribute to the growth of democracy. Trade, foreign direct investments and financial capital flows are believed to allocate resources to their most efficient use; democracy is believed to allocate political power to its most efficient use. The outcome in both cases represents the free will of people.

Globalization increases the demand of international business for democracy [Kant, 1795; Bhagwati, 1994; Schmitter, 1996]. Business requires peace and stability to prosper. Since democracies rarely fight each other, commercial interests pursue democracy in order to secure peace and stability. Therefore, authoritarian governments that open their economies face greater pressures from international business for political liberalization.

According to Van Hannen (1990), Diamond (1992), and Kummel (1998), by reducing information costs, globalization increases contacts with other democracies and makes the pro-democratic international non-governmental organizations (INGOs) more effective. With increased economic openness, citizens have greater access to information. More exposure to the media strengthens the effectiveness of transnational advocacy networks and the INGOs to help protect pro-democratic forces in authoritarian regimes and promote democracy.

Globalization strengthens domestic institutions that support democracy [Roberts, 1996; Stark, 1998; Keck and Sikkink, 1998]. Economic openness pleads for the rule of law, civil and human rights so long as the efficient operation of the market requires an enforceable system of property rights and impartial courts. The increased involvement of international business and INGOs in the host economy further promotes the transparency and accountability of domestic institutions and reduces state intervention, which is said to facilitate democracy.

Globalization Hinders Democracy

Lindblom (1977), Gill (1995), Gray (1996) and Cox (1997) argue that globalization reduces state policy autonomy and brings about public policies that please foreign investors instead of the common people. Increased financial capital mobility across countries and relocation of the means of production reduce the ability of states to implement domestic economic policies. Moreover, governments design their policies with a view to competing for foreign capital from the global investors and firms, who are not accountable to the voters. All this indicates a decline in the level of democracy.

Scholars like, Wallerstein ((1974), Przeworski (1991) and Amin (1996) argue globalization widens the economic gap between the North and the South. In this uneven process, the developed countries (DCs) drain capital, technology and skilled labour from the least developed countries (LDCs). This gives rise to widening gap in wealth and social unrest in the LDCs; their elites cling to power and governments become less democratic. Along the lines of the dependency theory, MNCs relocate to the LDCs to enjoy lower wages and labor cost and environmental standards and repatriate profits to the core. The penetration by MNCs distorts the economies in the LDCs and sways the domestic politics in their own favor. All of this obstructs democracy. Similarly, Im (1987), MacDonald (1991) and O'Donnell (1994) in their studies contend globalization enables the fast movement of money between countries, resulting in frequent balance of payment crises and unstable domestic economies. This gives the DCs and international organizations the leverage to impose economic reforms on the LDCs. In the face of resulting social unrest and support for radical opposition groups, weak democracies resort to authoritarian measures in an attempt to reassert power.

In the views of Robertson (1992), Dahl (1994) and Im (1996), globalization deepens ethnic and class cleavages diminishing the national-cultural basis of democracy. Losers from economic openness tend to seek a united identity based on ethnicity or religion. The winners, on the other hand, may promote discriminatory measures to maintain their edge over the losers. Globalization also induces labour migration across borders. The old residents typically attempt to restrict or eliminate the political participation of the immigrants with a view to reducing their competitiveness. All this gives rise to social cleavages and undermines democratic consolidation.

Globalization enables the state and Multinational Corporations (MNCs) to control and manipulate information supplied to the public [Gill, 1995; Martin and Schumann, 1997]. With the help of information technology, the state and the MNCs are better able to monitor people's information sources, provide only certain views. This results in disconnection between actual government decision-making and distorted public knowledge. The government becomes less transparent and accountable to the people leading to the erosion of democracy.

Globalization Has no General Effect on Democracy

Scharpf (1991), Jones (1995) and Wade (1996) contend that the extent to which globalization may affect democracy is exaggerated. The world economy is not as integrated as commonly believed. MNCs have a home bias and foreign direct investment (FDI) concentrate in a few countries. The effect of economic openness on democracy is not large in case of the LDCs since they generally do not participate in the global economy. On the other hand, the DCs are already stable democracies; globalization will not affect their levels of democracy.

Globalization does not necessarily render the welfare state powerless [Vernon, 1971; Kurzer, 1993, Frieden and Rogowski, 1996]. Increased national economic openness is a result of the deliberate choices of states. Modern welfare states still exert considerable control over their own economies because they provide important collective goods under-supplied by markets, i.e. social stability, property rights, infrastructure. They also compensate the losers from economic openness.

In their studies, Haggard and Kaufman (1995), Milner and Keohane (1996), Longworth (1998) are of the opinion that the effects of globalization on democracy may not be uniform. It varies across countries depending on government policies, a country's geopolitical location, the domestic political institutions, the identity of the domestic winners and losers, level of privatization and democracy etc. Although globalization-induced economic crises may expel authoritarian regimes in favor of democracy, these crises, if managed effectively, may instead increase public support for authoritarian leaders.

The above review of the literature is aimed at explaining how the analysis of the relationship between globalization and democracy in South Asia fits into the larger picture. The different theoretical claims need to be evaluated empirically to further the explanation how globalization affects democracy in South Asia, to which I turn next.

III. Methodology

With a view to assessing the effects of globalization on democracy in the South Asian context, the study will focus on Bangladesh, India, Maldives, Nepal, and Pakistan. Bhutan and Sri Lanka are excluded from the analysis due to unavailability of data. The link between the dependent variable - political rights - and independent variable - foreign direct investment (FDI) - is quantified using pooled time-series data for the period 1983 to 1999.

Data for the dependent variable have been collected from Freedom House's annual survey across countries[4]. Indicators to measure political rights include, free and fair selection of executive and legislative branch, fair electoral laws, ability for elected representatives to hold power, ability to organize political parties, ability for the opposition to win, free from elite domination, and input in the decision making process. Countries are rated from one to seven on this measure, with one signifying most free and seven, not free[5].

Data source for the independent variable is the World Bank's World Development Indicators CD-ROM, 2001. FDI indicator will reflect the acquisition of a lasting management interest (10 percent or more of voting stock) in an enterprise operating in an economy other than that of the investor, or the creation of a new subsidiary of a firm in a foreign country[6].

Based on the information collected, I pose the following research question:

Considering the levels of economic integration and democratic performance in South Asia, is it possible to find a systematic relationship between globalization and democratization?

The following model is constructed to test for the link between foreign direct investment and political rights in the case of South Asia:

Political Rights = $\beta_0 + \beta_1$ (FDI) + e

I will employ several statistical analyses to investigate the robustness of the results.

IV. Estimated Results

I first used Ordinary Least Squares (OLS) to test for a simple relationship between FDI and political rights. Political rights have been regressed on FDI. The results are presented in Table 1

Table 1: Model of Political Rights for South Asia (1983-1999)

Variables	Coeff. (st. error)	p-value
Foreign Direct Investment	.0004984 (.0002454)	0.045
Constant	3.099927 (.1716508)	0.000

The table shows that FDI has a positive impact on political rights and is statistically significant from zero. But as Beck and Katz (1995) note, problems associated with OLS include-autocorrelation, heteroskedasticity etc. Although this cross-sectional OLS regression for South Asia finds significant relationship between FDI and political rights, it does not control for cases that are not independent within cases and also for larger error variance.

Therefore, I applied OLS with dummy variables to get a more accurate relationship between the variables[7]. Gross domestic product (billions of local currency) and portfolio investment (millions of US \$) have been incorporated as dummy variables[8]. The findings are presented in Table 2.

Table 2: Model of Political Rights for South Asia (1984-1998)

Variables	Coeff. (st. error)	p-value
Foreign Direct Investment	.0004449 (.0005296)	0.404
GDP	.0000384 (.0000949)	0.687
Portfolio Investment	-.0002658 (.0002738)	0.335
Constant	3.103057 (.2121034)	0.000

The table presents distinct results when compared with the simple OLS procedure. FDI and GDP have a positive relationship with political rights but are not statistically significant from zero.

Portfolio investment seems to have a negative impact on political rights being statistically insignificant from zero. With the help of dummy variables, this procedure could not find any significant relationship between FDI and political rights.

Next I proceeded with fixed-effects model [Generalized Least Squares (GLS)]. It is very similar to the OLS w/dummy variables, only I did not have to create any dummy variable. The results are shown in Table 3.

Table 3: Model of Political Rights for South Asia (1983-1999)

Variables	Coeff. (st. error)	p-value
Foreign Direct Investment	-.0000712 (.000217)	0.744
Constant	3.254631(.1273263)	0.000

The table depicts negative relationship between FDI and political rights which is not statistically significant. The results contrast with that of the OLS w/dummy variables.

The preceding test was a cross-sectional time-series feasible generalized least squares (FGLS) regression. It helps fill in missing data, although my data set has no such problem. The findings are presented in Table 4.

Table 4: Model of Political Rights for South Asia (1983-1999)

Variables	Coeff. (st. error)	p-value
Foreign Direct Investment	.0004984 (.0002425)	0.040
Constant	3.099927 (.1696194)	0.000

The table implies a positive and statistically significant impact of FDI on political rights. This procedure is preferable since it is better with large data and also corrects for variation.

The final model to test was the OLS with panel corrected standard errors (PCSE). It works well when the data has a time series effect. The results are presented in Table 5.

Table 5: Model of Political Rights for South Asia (1983-1999)

Variables	Coeff. (st. error)	p-value
Foreign Direct Investment	.0004984 (.0002283)	0.029
Constant	3.099927 (.1166071)	0.000

The table signifies that FDI has both a positive and statistically significant impact on political rights. It produces very similar results when compared with regular OLS model, but takes into consideration the time series effect.

V. Discussion

This cross-sectional study of 5 South Asian countries explores the effect of FDI on political rights from 1983 to 1999 to predict an association between globalization and democracy. From the above estimated models, we find that the pooled time-series error-correction model is best suited to assess the influence of globalization on democracy over time and across countries. This procedure establishes a high threshold for estimating conventional levels of significance. As suggested by Beck and Katz (1995), the use of OLS with panel-corrected standard errors deals with the problem of panel heteroskedascity and spatial correlation and the lagged dependent variable corrects for serial correlation. In this study, the OLS w/PCSE has been able to establish important linkage between FDI and political rights to support the idea that globalization has a positive effect on democracy for South Asia. Such estimates are more reliable in the sense that the estimation of the standard errors is more efficient and consistent.

Now let us glance through the South Asian sample. Five decades after the end of colonial rule, South Asia still faces problems related to development and governance. The countries across the region have diverse historical, social, political, economic and cultural growth. However, against a wider context of international integration, South Asian states have sought to shape economic development and democratic legitimacy[9]. After years of inward-looking policies and tight regulation, much of South Asia (Bangladesh, India and Pakistan) undertook sweeping economic reforms in the early 1990s. Trade barriers were eliminated and restrictions on foreign direct investment were dismantled. FDI inflows increased from US $ 351 million during 1987-92 to US$2873 million during 1993-98 (World Bank, 2001). This globalization led economic growth did not come without political stability. By the end of last decade (till the military coup in Pakistan in late 1990s), each of these states had emerged as a functioning democracy. Repeated elections ('free and fair') had been held; diverse political interests and groups had organized together as political parties to compete in elections for power.

As per the descriptive statistics (Table 6 in the Appendix), Maldives and Nepal are the lowest recipients of FDI and also rank the lowest ('not free' and 'partly free', respectively, according to Freedom House study) in terms of degree of freedom when compared with other countries in the region. Whereas, India, the largest recipient of FDI, is also the largest working democracy in the developing world. Another point in case is Pakistan. FDI declined from $602 millions to $478 million in 1999 with the overthrow of representative democratic system. As such it follows that the amount of FDI influences the status of political rights.

However, several design issues warrant further research. To begin with, as multidimensional concepts, economic globalization and democracy need to be measured with multiple indicators. Important measures of economic integration include - trade openness, portfolio investment, credit ratings etc. Civil rights and economic freedom are useful determinants of democracy. This approach is believed to deal with the problem of validity. Like any other statistical analysis, my findings leave open questions that can be answered more rigorously with qualitative methods. Therefore, for methodological rigour, qualitative case study analysis is necessary to arrive at more sophisticated understanding of the consequences of economic globalization for political freedom.

VI. Conclusion

With centuries long histories, the processes of globalization and democratization have made remarkable progress after the end of the Cold War. Stakes are high in better understanding the relationship between these two broad trends. Existing literature presents conflicting positions on how globalization affects democracy. The paper has made a systematic empirical effort to assess the controversial effects of globalization on democracy for South Asia. I believe the analysis is critical as the links between globalization and democracy in the South Asian context is not statistically articulated. The results bear important implications for future research as well as for policy debate on globalization-democracy nexus. The findings suggest that a positive effect on political rights should be expected from an increase in FDI. Such influence did show up empirically for South Asia in this study. It provides preliminary support for the globalization-leads-to-democracy perspective. Apparently, the more globalized South Asia becomes, the more democracy it will experience. But such linkage between globalization and democracy could be established from the outcome of the pooled time-series error-correction model based on the inputs chosen as determinants of globalization and democracy. The analysis should be realized as part of a broader-scope research on the effects of globalization on democracy in South Asia. Therefore, further research should be conducted involving an expanded model with a larger sample in order to make generalizations.

Notes

1. On globalization, see, Wallerstein (1974); Cameron (1997); Held et al. (1992).

2. On democracy, see, Huntington (1991); Potter, Goldbalt, Kiloh and Lewis eds. (1997); Diamond (1999).

3. South Asia as a region is defined differently by various agencies. The South Asian Association for Regional

Cooperation (SAARC) defines South Asia as Bangladesh, Bhutan, India, Maldives, Nepal, Pakistan and Sri Lanka. On the other hand, the World Bank definition of South Asia includes the seven SAARC countries and Afghanistan. The United Nations Development Program (UNDP) definition is even broader, which includes Iran. For this paper, I will follow the SAARC definition.

4. Annual Survey of Freedom Country Ratings, 1972-73 to 1999-2000, New York: Freedom House.

5. For a concise meaning of these scores, consult the given explanation in any of the annual Freedom House volumes.

6. See any *World Development Report* of the World Bank for further explanation.

7. Data for this test have been truncated due to unavailability of information for certain years and indicators.

8. GDP is the gross value added, at purchaser's prices, by all resident and non-resident producers in the economy plus any taxes and minus any subsidies not included in the value of the products. Portfolio investment (excluding liabilities constituting foreign authorities' reserves) covers transactions in equity securities (the sum of country funds, depository receipts, and direct purchases of shares by foreign investors) and debt securities (publicly guaranteed and non-guaranteed debt from privately placed bonds). For further elaboration, see World Development Report of the World Bank.

9. A detailed account of the development and democratization processes of the South Asian states is available in Shastri and Wilson eds. (2001).

Appendix

Table 6: Descriptive Statistics

	Bangladesh		India		Maldives		Nepal		Pakistan	
Year	Political Rights*	FDI**	Political Rights*	FDI**	Political Rights*	FDI**	Political Rights*	FDI**	Political Rights*	FDI**
1983	5	0	2	63.0	5	0.00	3	0.0	7	26.1
1984	6	0.2	2	62.0	5	0.00	3	0.0	7	43.3
1985	6	1.2	2	160.0	5	0.00	3	0.0	7	77.6
1986	5	-5.1	2	208.0	5	5.40	3	0.0	4	150.0
1987	4	2.4	2	181.0	5	5.10	3	0.0	4	108.0
1988	4	2.6	2	287.0	5	1.20	3	0.0	4	155.0
1989	4	2	2	350.0	5	4.40	3	0.0	3	177.0
1990	4	3	2	97.0	6	5.60	4	0.0	3	200.0
1991	5	2	2	129.0	6	6.50	4	0.0	4	239.0
1992	2	4	3	315.0	6	6.60	2	0.0	4	343.0
1993	2	7	3	586.0	6	6.90	2	0.0	4	310.0
1994	2	16	4	1,314.0	6	8.70	3	0.0	3	360.0
1995	2	6	4	2,144.0	6	7.20	3	0.0	3	439.0
1996	3	7	4	2,821.0	6	9.30	3	7.0	3	1,106.0
1997	2	16	2	3,557.0	6	11.40	3	28.4	4	712.0
1998	2	249	2	2,462.0	6	11.50	3	11.1	4	602.0
1999	2	198	2	2,155.0	6	12.30	3	8.5	4	478.0

Sources: Annual Survey of Freedom Country Ratings, 1972-73 to 1999-2000.

World Bank's World Development Indicators CD-ROM, 2001.

* Measured on a one to seven scale, with one representing the highest degree of freedom and seven the lowest.

** Millions of US Dollars.

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