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Research Note

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Abstracts

The Democratic Advantage: Institutional Foundations of Financial Power in International Competition

by Kenneth A. Schultz and Barry R. Weingast

Despite their presumed liabilities, institutions associated with democracy serve as a source of power in prolonged international competition by increasing the financial resources that states can bring to bear. The theory of sovereign debt suggests that a state's ability to raise money through public borrowing is enhanced when debtholders have mechanisms for sanctioning state leaders in the event of default. Institutions associated with liberal government provide such mechanisms. All other things being equal, states that possess these institutions enjoy superior access to credit and lower interest rates than do states in which the sovereign has more discretion to default unilaterally. Liberal states can not only raise more money from a given economic base but can also pursue tax-smoothing policies that minimize economic distortions. The ability to finance competition in a manner that is consistent with long-term economic growth generates a significant advantage in prolonged rivalries. These claims are explored by analyzing the Anglo-French rivalry (1688–1815) and the Cold War.

The Dynamics of International Law: The Interaction of Normative and Operating Systems

by Paul F. Diehl, Charlotte Ku, and Daniel Zamora

This article describes the basic components of the operating and normative systems as a conceptual framework for analyzing and understanding international law. There are many theoretical questions that follow from the framework that embodies a normative and operating system. We briefly outline one of those in this article, namely how the operating system changes. In doing so, we seek to address the puzzle of why operating system changes do not always respond to alterations in the normative sphere. A general theoretical argument focuses on four conditions. We argue that the operating system only responds to normative changes when response is "necessary" (stemming from incompatibility, ineffectiveness, or insufficiency) for giving the norm effect, and when the change is roughly coterminous with a dramatic change in the political environment (that is, "political shock"). We also argue, however, that opposition from leading states and domestic political factors might serve to block or limit such operating system change. These arguments are illustrated by reference to three areas of the operating system as they concern the norm against genocide.

Shortcut to Greatness: The New Thinking and the Revolution in Soviet Foreign Policy
by Deborah Welch Larson and Alexei Shevchenko

Why did Soviet foreign policy change during 1985–1991 from viewing conflict between capitalism and socialism as inevitable to favoring cooperation between states in solving global problems? Neither materialist analyses nor ideational accounts explain why Gorbachev adopted the radical new thinking instead of more conventional reform alternatives. We argue that the new thinking offered a means to enhance Soviet status despite retrenchment and accommodation of the West. By promoting principles underlying a new world order, the Soviet Union could achieve greatness based on the exercise of soft power. This explanation draws on social identity theory, which maintains that people are motivated for their social group to have a distinctive, positive identity. Lower status groups may enhance their perceived standing by finding a new domain for comparison or reevaluating an undesirable trait.

Globalization, Taxation, and Burden-Shifting in Latin America
by Erik Wibbels and Moisés Arce

Most researchers interested in the relationship between global markets and public policy focus on advanced industrial democracies. In contrast, we examine competing hypotheses as to globalization's effect on governments by expanding the scope of the discussion to include developing nations. More specifically, we investigate the relationship between international market integration and the evolving burden of taxation on capital, as well as the subsequent response of markets to shifts in tax policy in Latin America since the late 1970s. Consistent with our theoretical expectations, we find that global market forces are more constraining vis-à-vis tax policy in Latin America than in the world's wealthiest nations. Despite these market-based pressures, however, national politics continue to influence tax policy in Latin America in a manner consistent with findings on advanced industrial democracies. As such, developing nations continue to have some room to manipulate policy, though within the context of a more strictly neoliberal context than their counterparts in advanced industrial democracies.

Economic Interests and Regional Trading Arrangements: The Case of NAFTA
by Kerry A. Chase

This article examines lobbying in the United States on the North American Free Trade Agreement (NAFTA). I argue that economies of scale and production sharing across borders create incentives for firms to seek regional trade liberalization.

Statistical analysis demonstrates that sectors with these characteristics were more likely to lobby for free trade in North America; these sectors were also exposed to free trade more rapidly under the tariff-phasing schedule in the NAFTA treaty. However, corporate restructuring to rescale production for the regional market and to increase offshore assembly presented adjustment costs for U.S. workers, which created divisions between labor unions and their employers. I conclude that regional arrangements are an attractive mechanism to liberalize trade for firms in need of larger-than-national markets to take advantage of economies of scale or to develop production-sharing networks.

Reversal of Fortunes: Democratic Institutions and Foreign Direct Investment Inflows to Developing Countries
by Quan Li and Adam Resnick

Does increased democracy promote or jeopardize foreign direct investment (FDI) inflows to less-developed countries? We argue that democratic institutions have conflicting effects on FDI inflows. On the one hand, democratic institutions hinder FDI inflows by limiting the oligopolistic or monopolistic behaviors of multinational enterprises, facilitating indigenous businesses' pursuit of protection from foreign capital, and constraining host governments' ability to offer generous financial and fiscal incentives to foreign investors. On the other hand, democratic institutions promote FDI inflows because they tend to ensure more credible property rights protection, reducing risks and transaction costs for foreign investors. Hence, the net effect of democracy on FDI inflows is contingent on the relative strength of these two competing forces. Our argument reconciles conflicting theoretical expectations in the existing literature. Empirical analyses of fifty-three developing countries from 1982 to 1995 substantiate our claims. We find that both property rights protection and democracy-related property rights protection encourage FDI inflows; after controlling for their positive effect through property rights protection, democratic institutions reduce FDI inflows. These results are robust against alternative model specifications, statistical estimators, and variable measurements.

The Reaction of Private Interests to the 1934 Reciprocal Trade Agreements Act
by Karen E. Schnietz

In recent research on the 1934 Reciprocal Trade Agreements Act (RTAA), there has been no examination of the reaction of private actors to the RTAA. Did producer groups and investors in 1934 believe the Democratic RTAA was the solution to Republican protectionism, as institutional analyses of the RTAA claim, or did they realize the RTAA was no "magic bullet" against a return of protectionism, as skeptics argue? Archival data suggests that many producer groups believed the RTAA would result in durable liberalization, but that fewer understood the likely effects of its specific features. An event study of investor reaction to the RTAA reveals that export-dependent firms experienced a significant, positive stock return increase on news of the RTAA, while heavily tariff-protected firms experienced a significant stock decline, albeit several months later.