

# The economic costs of populism\*

IMF IEO Seminar

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## Definition of populism:

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- ▶ **Populism is a political strategy**, as defined by Canovan (1981, 1999), Hawkins (2009), Mudde (2004), Müller (2016), Taggart (2000) etc.
- ▶ Populists focus on struggle of **“the people” vs. “the elites”**
  - Then claim to be sole representative of the people
  - Polarization (people/elites) core of campaign/governing
- ▶ **Left vs right:**
  - Left-wing populism is typically economic
    - Campaign against financial elites and for redistribution
  - Right-wing populism is typically cultural
    - Campaign against ethnic/religious minorities & foreigners



## Populism and economics

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- ▶ Populists are in power many countries
- ▶ Much recent work on determinants of populism  
Inglehart and Norris 2016, Herrera et al. 2018, Rodrik 2018, Guriev 2018, Algan et al. 2018, Eichengreen 2018, Guriev/Papioannou 2020
- ▶ But only little work on the economic consequences of populist policies  
Seminal volume by Dornbusch and Edwards (1991) with Latin American focus

## On the determinants

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### Economics vs. culture

- ▶ Economics: import competition and unemployment, robots, crisis
- ▶ Culture: cultural backlash, social capital, moral values, religion, xenophobia

Consequences of populism: populists in power

# Populists in power

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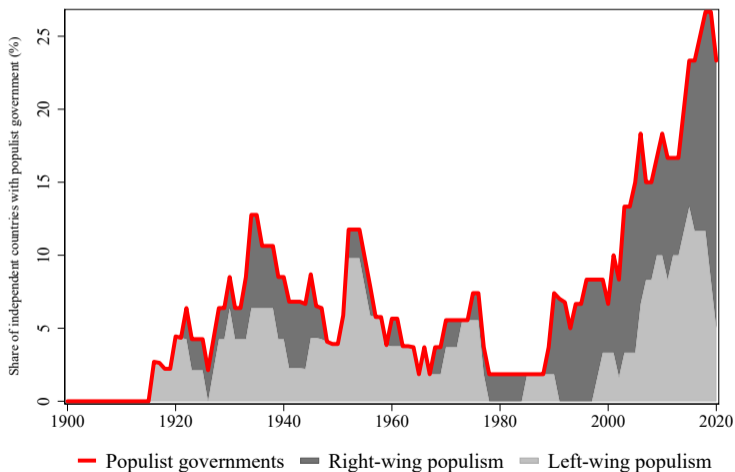
## 1. **Facts on "Populists in Power"**

Use classification of >1,500 leaders as "populist" or "non-populist" (and right-wing vs. left-wing populist), covering 60 countries and 120 years (1900-2018)

## 2. **Study economic consequences of populism**

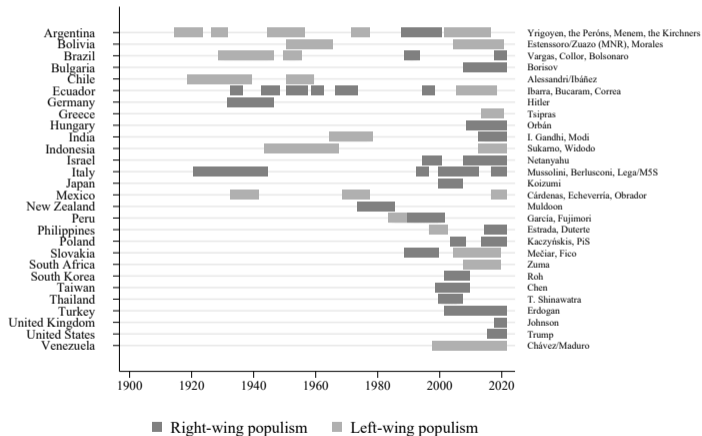
- Broad-based extension of Dornbusch/Edwards (1991)
- Approach builds on Jones / Olken (2005, QJE), Blinder / Watson (2016, AER), Acemoglu et al. (2019, JPE)
- Focus is on effects on GDP, but also study other outcomes

# Populists in power: Share of countries in sample





# Serial populism



## **Populist are good at surviving in power**

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### **Populist leaders often rule for many years**

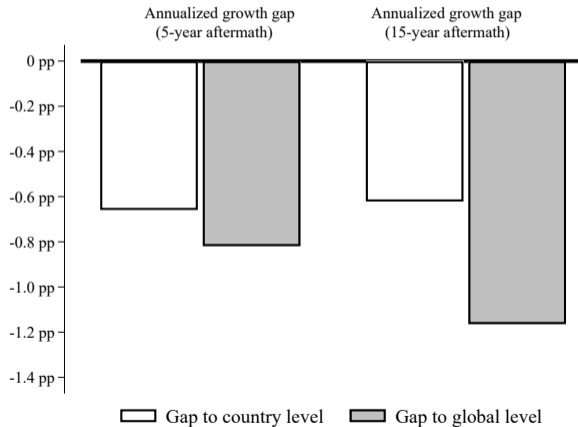
- ▶ Average time in office is 7.5 years compared to 4 years for non-populist leaders (using Archigos)

### **Populists have a high re-election probability**

- ▶ 18 out of the 51 populist leaders show two or more spells in office: 36%
- ▶ Non-populist return to power with a probability of 16%

# Economic performance

# Average annualized growth gap after populists come to power

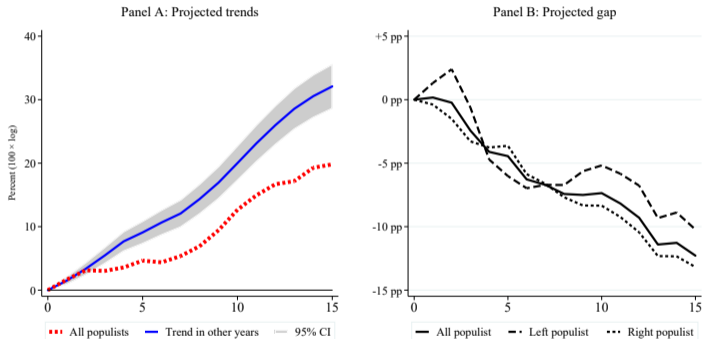


# Event studies

	(a) Simple OLS	(b) CFE & YFE	(c) Macro controls
5-year aftermath			
Populist leader	-0.97** (0.41)	-1.01** (0.41)	-0.81** (0.40)
$R^2$	0.001	0.174	0.235
Observations	4249	4249	3081
15-year aftermath			
Populist leader	-1.04*** (0.22)	-0.81*** (0.25)	-0.73*** (0.25)
$R^2$	0.004	0.174	0.235
Observations	4249	4249	3081

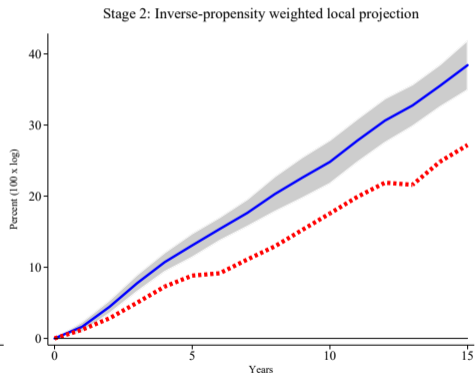
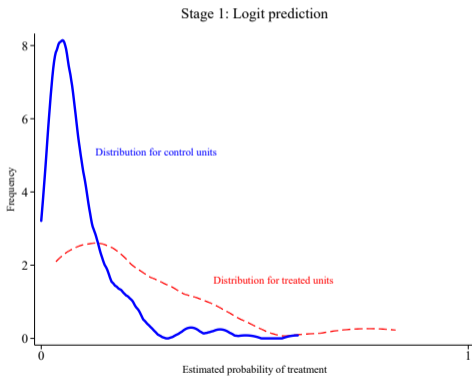
$$g_{it} = \beta_P \text{Populist}_{i,t-k} + \delta X_{i,t-1} + \alpha_i + \alpha_t + \epsilon_{it} \quad (1)$$

# Local projections



$$\Delta_k Y_{i,t+k} = \beta_P^k * Populist_{i,t} + \mu_i^k + \sum_{j=1}^l \gamma_j^k * X_{i,t-j} + \varepsilon_{i,t}^k \quad k = 1, \dots, 15 \quad (2)$$

# Inverse propensity weighted local projections



Synthetic control



## The Synthetic Control Method

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### Key Idea:

- ▶ As control use the (convex) combination of comparison units that best resembles the values of predictors of the outcome variable for the affected unit before the event or intervention of interest

### Advantages:

- ▶ Transparency
- ▶ Avoids extrapolation
- ▶ Accommodates the presence of unobserved factors
- ▶ Does not require outcome data to design the study (Rubin 2001)
- ▶ Permutation methods that produce valid inference regardless of the number of available comparison units, time periods, or level of aggregation data

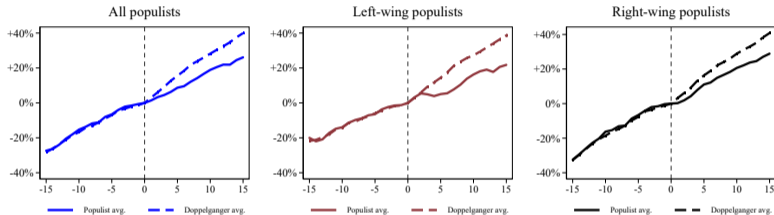
## Synthetic Control Method: Implementation

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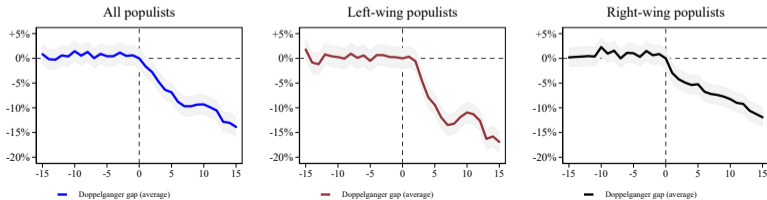
- ▶ Let  $X_1 = (Z_1, \bar{Y}_1^{K_1}, \dots, \bar{Y}_1^{K_M})'$  be a  $(k \times 1)$  vector of pre-intervention characteristics
- ▶ Similarly,  $X_0$  is a  $(k \times J)$  matrix which contains the same variables for the unaffected units
- ▶ The vector  $W^*$  is chosen to minimize  $\|X_1 - X_0 W\|$ , subject to our weight constraints
- ▶ We consider  $\|X_1 - X_0 W\|_V = \sqrt{(X_1 - X_0 W)' V (X_1 - X_0 W)}$ , where  $V$  is some  $(k \times k)$  symmetric and positive semidefinite matrix
- ▶ Various ways to choose  $V$  (subjective assessment of predictive power of  $X$ , regression, minimize MSPE, cross-validation, etc.)

# Synthetic control estimation for real GDP per capita

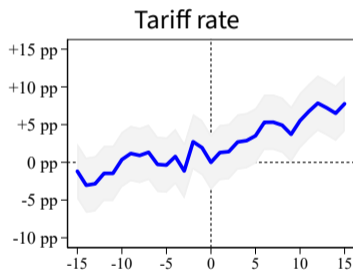
Panel A: Trends



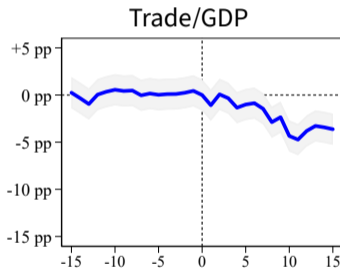
Panel B: Doppelgänger gap



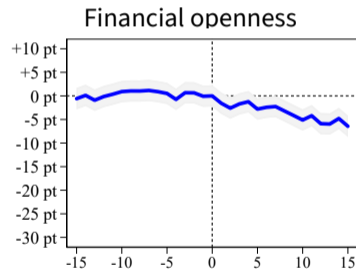
# Trade and financial openness



— Doppelgänger gap (average)  
 1 SD of pre-treat. doppelgänger gap (avg.)



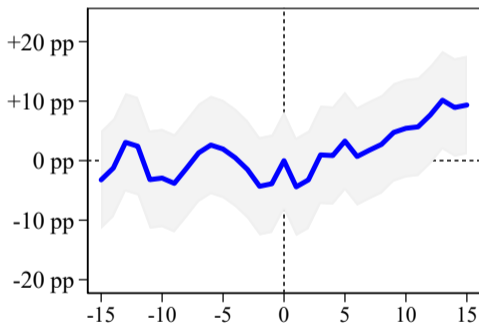
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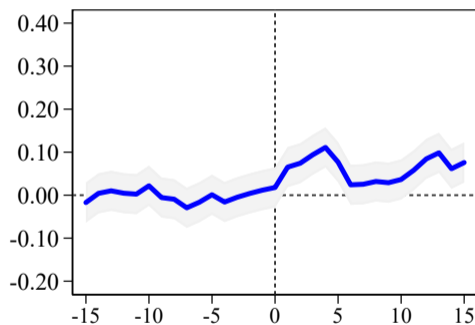
# Macro outcomes

### Debt/GDP



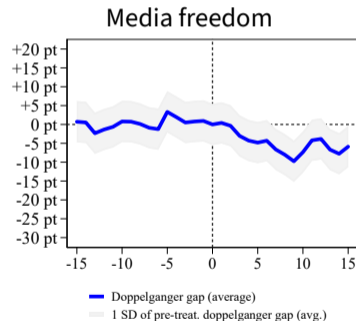
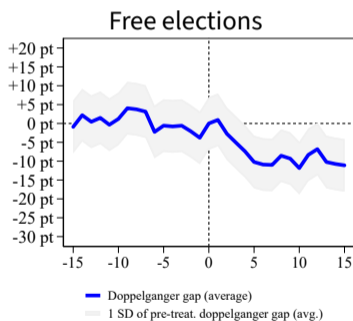
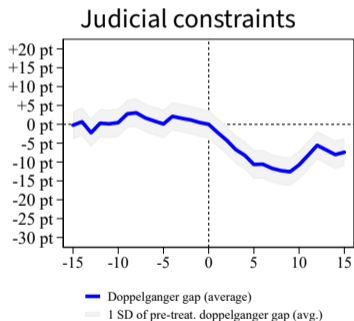
— Doppelgänger gap (average)  
 1 SD of pre-treat. doppelgänger gap (avg.)

### Inflation



— Doppelgänger gap (average)  
 1 SD of pre-treat. doppelgänger gap (avg.)

# Institutions



## Conclusion

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- ▶ Substantial economic cost of populism: about 10% of GDP over 15 years
- ▶ Populism does not improve the fortunes of the “people”
- ▶ Populists typically deliver on their nationalist rhetoric: economic integration falls behind
- ▶ Visible erosion of checks and balances: judicial independence, free and fair elections, press freedom

**Thank you for your attention!**



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