Sneaky Stealing: Why do autocrats choose to appropriate overtly or covertly?

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1   Introduction

In 2017 Mohammed Bin Salman became the Crown Prince and defacto ruler of Saudi Arabia. He immediately purged 200 wealthy businessmen and princes, including billionaire Al-Waleed Bin Talal and his rivals in the defense sector. Those arrested were charged with corruption and forced to forfeit supposedly illicit gains. Torture was sometimes used to gain access to overseas assets, and in total some 107 Billion dollars in wealth was expropriated. Most strikingly, the entire affair was conducted with great publicity. The purgees were held not in their homes but in the Ritz-Carlton Riyadh, where MBS held a press conference just two weeks prior. One of the targets successfully escaped a month prior, only to be conspicuously assassinated in Turkey. Altogether, these episodes alienated MBS from the royal families traditions, Turkey and even the United States.

This episode was a stunning departure from dispute resolution in the Arab Monarchies. In 2012, King Abdullah the II of Jordan faced a similar dilemma when insider loyalist families possessed farming concessions on an aquifer the monarch desperately needed to supply a restive urban population. But unlike

MBS, Abudllah the II had been ruling for 13 years and had no need for an extravagant and dangerous show. Abdullah the II privately declared the farms contracts expired and ordered them closed after an acrimonious but internal disagreement. The regime kept the disagreement as quiet as possible.

Investment is crucial to economic growth, and many developing countries compete for foreign direct investment (FDI). Because leaders can seize invested assets, states and investors face a credibility problem. Expropriating assets is lucrative, but investors will refrain if they expect expropriation. Academics have long studied how political institutions affect the rate of expropriation (North and Weingast, 1989; Olson, 1992; Tilly, 1993). This literature finds that democracies expropriate less through political constraints on their executives (Quan Li).

Two models have been proposed to explain patterns of expropriation in autocracies. The stationary bandit model predicts that autocrats should expropriate more when they expect a short tenure (Olson, 1989). Because autocratic regimes are lindy (Svolik, 2012), expected tenure is higher late in the regime, leading to low expropriation (Quan li, 2006). Alternatively, expropriation may arise due to internal regime politics (Albertus and Menaldo, 2012). New dictators may use expropriation to reassure supporters that the dictator will stay loyal to them.

Two new papers have shown that not all expropriations are equal. While constrained leaders expropriate less, they ban investors from repatriating their profits at the same rate (Graham et al. 2017). Democratic leaders also prefer more "covert" methods, to appropriate assets without triggering veto points (Pearlman, forthcoming).

Why did MBS choose to expropriate his rivals publicly, which Abdullah the II buried the affair? This essay proposes that autocrats choose to overtly expropriate as a costly signal of loyalty to their launching coalitions. Even when

all actors would prefer a quiet expropriation, the overt act provides reassurance to the launching organization that the autocrat is primarily concerned with their interests.

Previous accounts have argued that autocrats choose overt expropriation because it is easier and more lucrative than forced sales or regulations. I argue that the financial dimension does have causal power but the signalling needs also explain a significant part of the variance. Institutional constraints create a cat and mouse game between leaders and societies. Societies and investors attempt to constrain theft while leaders seek loopholes.

In what follows, we show that autocrats hide their expropriations more when they face low constraints from regime insiders. (summarize results)

This paper argues that contrary to the financial model, as autocrats consolidate they expropriate more covertly. The autocrat most certain of their position prefers a covert confiscation, relative to the early and vulnerable. However, all autocrats continue to expropriate more overtly than democracies. This evidence is consistent with a signalling model of expropriation as a solution to the autocrats credibility problem.

2   Literature Review

This section reviews the literature on when and why autocrats expropriate foreign investment.

All leaders need money, and autocrats are no exception. Autocrats also need money to provide public goods to deter revolution (Bueno De Mesquita, 2005), but spend less than democracies (Hausken et al. 2004). Like all politicians, many autocrats are motivated by expensive personal projects, leading them to maximize revenue. Tzarist Russia exported during famines to fund industrialization. The Pol Pot regime funneled state revenue into buying arms

3

for a revanchist invasion of Vietnam. Such an autocrat will behave a revenue maximizer in peripheral policy areas.

Unlike democratic leaders, autocrats need money to reward their supporters throughout the patronage system (Pepinsky, 2007). While some regimes motivate elite support through "protection pacts", these are a minority of modern autocracies (Slater, 2010). Autocrats mainly motivate their allies to keep them in power with the promise of future payments (Myerson, 2008). A collapse in the ability to pay supporters often triggers regime collapse (Bueno de Mesquita et al. 2005; Hale and Colton, 2008). Failure to pay supporters has resulted in the death of several autocrats, including William Tolbert of Liberia and Samuel Doe (who had himself killed William Tolbert in the preceding crisis) (Bueno de Mesquita, 2011).

Expropriation can be highly lucrative. Price shocks increase the probability of expropriation more than political crisis (Duncan, 2008), consistent with a revenue maximising leader who discounts future payoffs. The effect of price shocks strongly suggests that opportunism plays a significant role (Hajzler, 2007). [add other determinants here]

Expropriation of FDI was most popular in the 1960s to 70s. Decolonization increased developing countries defacto power, while the rents from past investments had been negotiated in the colonial period (Kobrin, 1994). Expropriation was attractive countries needing to fund aggressive industrial and social development programs, while the long term costs of expropriation were poorly understood. However expropriation collapsed in the 1980s (Minor, 1994). The most profitable asset classes (minerals) had been exhausted and states were learning to regulate without ownership. Also the resulting state-owned-enterprises performed poorly. The 2000's saw a modest resurgence of expropriations (Hajzler, 2008).

4

Expropriation does come with costs for a regime (Tomz and Wright, 2008). Future investors are hesitant to invest in expropriating states. Expropriation may also limit the leaders access to foreign credit. In particular the IMF and the World Bank use leverage from credit to deter debtors from expropriating FDI (Jeneson et al. 2019). Additionally, expropriated assets should be less productive because they have less access to foreign technology (Miner, 1994). This has not been proven empirically, but the wage premium that foreign-owned firms pay in developing countries suggests they have higher productivity.

2.1 The Stationary Bandit Model

One might naively assume that a revenue maximizing regime with no constraints would immediately expropriate all available assets. However, if regimes are selfish this does not imply they impatient (Olson, 1993). High taxation and theft decreases the incentives for investment and production that drive growth, decreasing the autocrats future tax take. Olson theorized that a stationary bandit with a discount function $\delta > 0$ has an incentive to leave some investment in place. The optimal take is strictly decreasing in the leaders expected tenure. A leader who expects to lose power this period (a roving bandit) should tax at the highest possible rate.

Expropriation offers short term gains in revenue and control to the leader. The revenue from the output can provide public goods, payoffs to supporters, or fund the leaders pet projects. In the long run, expropriation imposes costs from reduced investment, foreign support and often the need to subsidise poor-performing state businesses. If the asset is given to a supporter, that supporter is appeased but gains an independent resource base to challenge the leader. To formalize this, the leader expropriates if

$$\omega > \sum_{n}^{k} = 0\delta^t - \alpha,$$

where ω is the windfall from expropriating, k is the leaders future years in office, δ is the leaders discount function and α is the value of not expropriating. The future payoff is increasing in k.

I propose that covert expropriation reduces both ω and α, but the proportional reduction in windfall is smaller than the reduction in costs. Thus a leader with a longer expected tenure both expropriates less and chooses to do so covertly.

2.2   The Credibility Model

Albertus and Menaldo propose an alternative model of expropriation in their paper "If you're with us, you're against them" (2012). They argue that expropriation is not motivated by commitment to investors but commitment to regime insiders.

In autocratic politics independent authority can resolve disputes between regime insiders (Svolik, 2012). Both the autocrat and her supporters may make agreements, and may later break those agreements, with only each other to enforce them. Underlying all such agreements is "violence, the ever present arbiter ultimate arbiter of disputes". In the absence of enforcement, regime insiders must highly value credible signal of each other's intention.

No head of state rules alone, so some coalition of elite actors must cooperate to place their candidate on the throne. This coalition is called the launching organization (LO). In exchange for their support, the LO expects some portion of policy control and rents will be distributed among them (Svolik, 2012).

The autocrat may intend to keep the LO as her core support base or to replace them with loyal cronies. If the autocrat has similar policy preferences,

6

the cost of sharing power with this particular set of captains is low. However, the dictator may secretly have sharply divergent preferences from the launching organization or desire a higher share of the rents. Such an autocrat can consolidate power by replacing the LO with loyal cronies. Critically, over time the probability of a successful coup declines over time as expectations solidify and the autocrat acquires experience. Eventually a coup is so unlikely to succeed that supporters never attempt it, allowing the autocrat to reshuffle their winning coalition. For example, Saddam Hussein replaced much of the ruling ministers with loyalists from his home village of Tikrit.

During the early years of the autocracy the LO requires information about the intentions of the autocrat. Asking will not work, because any autocrat will claim to prefer their current captains. The dictator may make promises today, but repudiate such cheap talk once de facto power shifts. The LO needs instead a credible signal of loyal intentions, a signal which would be prohibitively costly for a replacement-planning autocrat. For example, a replacement-planning autocrat would prefer not to destroy the power base of her intended replacements. The LO may therefore demand that the autocrat expropriate the possessions of would-be replacements and distribute them among non-elites, leaving on the LO as viable supporters. Or the LO may demand that the autocrat alienate foreign supporters, which an overt expropriation would achieve.

An expropriation is just such a signal. Expropriation removes a rival power-base to the LO, which a disloyal autocrat would not do. In the case of foreign investment a public expropriation also alienates potential international supporters of the autocrat. It may even constrain the autocrats ability to flee by angering foreign powers.

A covert expropriation provides a similar financial windfall but much less signalling value. Members of the launching organization may not notice the

act, particularly if they are non-elites. Covert expropriation also does less to alienate the international community from the autocrat.

The alternative explanation of overt expropriation is simply that it is cheaper, but creates more enemies. A forced sale would be less efficient as the company must receive some compensation, and the state is not the direct recipient. This theory predicts that the most constrained autocrats will prefer covert expropriation, while a consolidated autocrat should expropriate publicly.

2.3 Hypothesis

From this literature, I derive the following hypothesis about the form of expropriations.

1. Covert expropriation increases with leader tenure.

Coups are much more common in the first years of a ruling spell. Early on the launching organization has less information about the leaders behavior and more opportunity to remove the inexperienced ruler. Each year of tenure is associated with a 4% reduction in probability of removal (Li, 2009).

Longer tenure simultaneously increase the leaders expectation of her tenure and reduces the need for overt expropriation to signal loyalty. The models make identical predictions for this relationship.

2. Price shocks are more strongly associated with covert expropriations than overt.

Price changes are strongly associated with expropriations, particularly in the mineral industry (Duncan, 2006). When prices are high relative to their expectation, a one-time windfall is more attractive relative to the steady gains of continued investment. If covert expropriation is more financially motivated than overt, price shocks should predict covert expropriation more strongly than overt.

3 Data

The ideal dataset for this claim would cover all expropriations in developing autocracies. However, there does not exist a viable dataset on national company expropriations which includes data on the method of expropriation. Furthermore, data on national company expropriations would be biased by the regimes ability to punish complaining owners. Fortunately, foreign companies face no such silencing allowing us unbiased data on their expropriations.

This paper uses a dataset of 618 expropriations of foreign direct investment (FDI) by developing countries from 1960 to 2006. The original data was collected by Kobrin et al. (1980). It has been updated by Minor (1994) and Hajzler (2010).

The majority of the expropriations occurred prior to 1980, with a small resurgence after 2000. Previous research suggests that in the 1980's opportunities for theft were exhausted, while states became disillusioned with the modest returns and audience costs of expropriation.

Following Perlman (forthcoming) an overt expropriation as "[t]he taking of foreign property directly by the government under the due process of local law. This generally entails an act of parliament or an executive order for which proper authority exists" (Kobrin, 1980, 68). The asset moves directly into the control of t he government. These seizures are usually highly public and the state has little wiggle room to avoid responsibility.

Covert expropriation can take place several ways. In an intervention some private actor takes over control of the investors asset and the state makes no intervention to protect the asset. The state may force the investor to sell the company to the government at some below-market price. Finally the state may use the threaot of coercion to force the investor into an unfavorable contract renegotiation. Each of these methods porvides the state with plausible denia-

bility about the expropriation, hiding the act from both internal and external observers.

Firure 1 plots the count of expropriations by type per year.

4   Results

First, I restrict the dataset to only include non-democracies, as classified by Geddes, Wright and Frantz. This retains 491 of the original 618 expropriations (democracies expropriate much less often).

In the first regression I condition on expropriation the regress on a dummy variable with overt as one. My first dependent variable of interest is tenure years, which has a strong inverse correlation with coup risk (Svolik). All three specifications find a statistically significant relationship between years in office and type of expropriation. An autocrat who has been in office for 10 years is 16 percentage points more likely to expropriate covertly than overtly. This first result directly contradicts the financial model, as the most secure autocrats expropriate more covertly.

Polity score is in the expected direction but is not significant, which is expected because the sample is restricted to autocracies. Controlling for sector, region and decade fixed effects creates no change.

<div align="center">Table 1 about here</div>

For my second set of regressions I examine coup risk, as calculated by Curtis (2016). Again we see that more secure autocrats prefer covert expropriation, controling for all fixed effects.

The effect remains when controlling for national legislatures, which do have an independent effect of restraining autrocrats.

Table 1:

	(1)	(2)	(3)
		Dependent variable:	
		overt	
tenure_years	−0.016***	−0.016***	−0.016***
	(0.005)	(0.005)	(0.005)
polity2_P4	−0.007	−0.007	−0.007
	(0.006)	(0.007)	(0.007)
gdppc_WDI_PW	−0.00000***	−0.00000**	−0.00000***
	(0.00000)	(0.00000)	(0.00000)
Constant	0.627***	0.560***	0.417***
	(0.049)	(0.070)	(0.088)
Sector Fixed Effects?	No	Yes	Yes
Region Fixed Effects?	No	Yes	Yes
Decade Fixed Effects?	No	No	Yes
Observations	389	387	387
R^2	0.051	0.065	0.088
Adjusted R^2	0.044	0.040	0.053
Residual Std. Error	0.485 (df = 385)	0.486 (df = 376)	0.483 (df = 372)
F Statistic	6.951*** (df = 3; 385)	2.613*** (df = 10; 376)	2.556*** (df = 14; 372)

Note: *p<0.1; **p<0.05; ***p<0.01

Table 2:

| | *Dependent variable:* |
| | overt |
	(1)	(2)	(3)
couprisk	−4.700	−8.338*	−10.574**
	(4.442)	(4.477)	(4.478)
polity2_P4	−0.035***	−0.026***	−0.017*
	(0.008)	(0.008)	(0.009)
gdppc_WDI_PW	−0.00000	0.00000	0.00000
	(0.00000)	(0.00000)	(0.00000)
Constant	0.629***	0.551***	0.629***
	(0.062)	(0.098)	(0.099)
Sector Fixed Effects?	No	Yes	Yes
Region Fixed Effects?	No	Yes	Yes
Decade Fixed Effects?	No	No	Yes
Observations	148	146	146
R^2	0.126	0.260	0.314
Adjusted R^2	0.107	0.205	0.246
Residual Std. Error	0.399 (df = 144)	0.378 (df = 135)	0.368 (df = 132)
F Statistic	6.895*** (df = 3; 144)	4.734*** (df = 10; 135)	4.639*** (df = 13; 132)

Note: *p<0.1; **p<0.05; ***p<0.01

Table 3:

	overt		
	Dependent variable:		
	(1)	(2)	(3)
tenure_years	−0.017***	−0.015**	−0.016**
	(0.006)	(0.006)	(0.007)
v2xlg_legcon_VDEM	−0.358**	−0.589***	−0.486***
	(0.148)	(0.166)	(0.181)
polity2_P4	−0.007	0.001	−0.001
	(0.007)	(0.008)	(0.008)
gdppc_WDI_PW	−0.00000***	−0.00000*	−0.00000*
	(0.00000)	(0.00000)	(0.00000)
Constant	0.694***	0.805***	0.661***
	(0.070)	(0.101)	(0.136)
Sector Fixed Effects?	No	Yes	Yes
Region Fixed Effects?	No	Yes	Yes
Decade Fixed Effects?	No	No	Yes
Observations	228	228	228
R^2	0.103	0.163	0.181
Adjusted R^2	0.087	0.121	0.123
Residual Std. Error	0.479 (df = 223)	0.470 (df = 216)	0.469 (df = 212)
F Statistic	6.433*** (df = 4; 223)	3.829*** (df = 11; 216)	3.131*** (df = 15; 212)

Note: *p<0.1; **p<0.05; ***p<0.01

Subnational elections may have a restraining effect, but the confidence intervals are much too large to confirm.

Table 4:

	Dependent variable:		
	overt		
	(1)	(2)	(3)
tenure_years	−0.018***	−0.015**	−0.016**
	(0.006)	(0.006)	(0.007)
subnat_elec_VDEM	−0.332**	−0.226	−0.235
	(0.132)	(0.165)	(0.167)
v2xlg_legcon_VDEM	−0.349**	−0.541***	−0.434**
	(0.147)	(0.169)	(0.184)
polity2_P4	0.006	0.008	0.005
	(0.008)	(0.009)	(0.010)
gdppc_WDI_PW	−0.00000***	−0.00000*	−0.00000**
	(0.00000)	(0.00000)	(0.00000)
Constant	0.867***	0.891***	0.750***
	(0.098)	(0.119)	(0.150)
Sector Fixed Effects?	No	Yes	Yes
Region Fixed Effects?	No	Yes	Yes
Decade Fixed Effects?	No	No	Yes
Observations	228	228	228
R^2	0.128	0.170	0.189
Adjusted R^2	0.109	0.124	0.128
Residual Std. Error	0.473 (df = 222)	0.469 (df = 215)	0.468 (df = 211)
F Statistic	6.531*** (df = 5; 222)	3.680*** (df = 12; 215)	3.074*** (df = 16; 211)

Note: *p<0.1; **p<0.05; ***p<0.01

When vertical accountability mechanisms are included, the effect of tenure does decline. There could be a correlation between long survival of an autocrat and vertical accountability, which biased upward the earlier beta1 estimates.

Table 5:

	overt		
	Dependent variable:		
	(1)	(2)	(3)
tenure_years	−0.007	−0.012*	−0.013*
	(0.005)	(0.007)	(0.007)
v2x_veracc	−0.187***	−0.149*	−0.140*
	(0.040)	(0.078)	(0.080)
v2xlg_legcon_VDEM		−0.357*	−0.283
		(0.205)	(0.214)
polity2_P4	0.003	0.005	0.002
	(0.006)	(0.008)	(0.009)
gdppc_WDI_PW	−0.00000***	−0.00000**	−0.00000**
	(0.00000)	(0.00000)	(0.00000)
Constant	0.549***	0.726***	0.602***
	(0.050)	(0.109)	(0.139)
Sector Fixed Effects?	No	Yes	Yes
Region Fixed Effects?	No	Yes	Yes
Decade Fixed Effects?	No	No	Yes
Observations	389	228	228
R^2	0.103	0.177	0.193
Adjusted R^2	0.094	0.131	0.132
Residual Std. Error	0.472 (df = 384)	0.467 (df = 215)	0.467 (df = 211)
F Statistic	11.049*** (df = 4; 384)	3.855*** (df = 12; 215)	3.157*** (df = 16; 211)

Note: *p<0.1; **p<0.05; ***p<0.01

Table 6:

	overt		
	Dependent variable:		
	(1)	(2)	(3)
tenure_years	−0.015**	−0.015**	−0.012*
	(0.006)	(0.006)	(0.007)
v2x_veracc	−0.196***	−0.196***	−0.168**
	(0.072)	(0.072)	(0.079)
v2x_ex_military	−0.240	−0.240	−0.299*
	(0.175)	(0.175)	(0.175)
v2xlg_legcon_VDEM	−0.099	−0.099	−0.396*
	(0.183)	(0.183)	(0.205)
polity2_P4	−0.003	−0.003	0.006
	(0.007)	(0.007)	(0.008)
gdppc_WDI_PW	−0.00001***	−0.00001***	−0.00000**
	(0.00000)	(0.00000)	(0.00000)
Constant	0.663***	0.663***	0.822***
	(0.092)	(0.092)	(0.122)
Sector Fixed Effects?	No	Yes	Yes
Region Fixed Effects?	No	Yes	Yes
Decade Fixed Effects?	No	No	Yes
Observations	228	228	228
Log Likelihood	−149.865	−149.865	−142.707
Akaike Inf. Crit.	313.730	313.730	313.414

Note: *p<0.1; **p<0.05; ***p<0.01

5 Overt Expropriation and Tenure in Office

In the next section I cease conditioning on the expropriation decision. Unfortunately, I am waiting for a data request to select only country-years where some FDI existed to be exporpiatied.

6 Expropriation and Survival

In this final section I look at the effect of expropriation on autocrat survival. This section is also awaiting data.

Causal Inference Ideas - Use price shocks in minerals to achieve exogenous variation in expropriations - Then split up by type of expropriations - Look at the .

Idea. Add value by using an instrumental variable approach to achieve external variation in exprorpriation. Use commodity price shocks as an instrument for expropriation. Then check influence on political survival.

Or I could use the price change dummy. So I again break apart the exprorpriations by type. In my model, covert expropriations are more about money, and overt are more about loyalty. Therefore price shocks should cause covert expropriations and vulnerability should cause overt expropriations. Use Roderick Duncan's data