Robbing Peter to have Paul sent to the Gulag: The Relationship between Expropriation and Consolidation in Autocratic politics?

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1 Introduction

In 2017 Mohammed Bin Salman (MBS) 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[Leber and Carothers, 2019]. Those arrested were forced to forfeit supposedly illicit gains, in form of companies, bank accounts and oversease assets. When access codes were not forthcoming, purgees were tortured. The total hall was some 107 Billion, at least according to the organizers statements. Strikingly, the entire affair was conducted with great publicity; purgees were held in the same Ritz-Carlton Riyadh hotel where MBS held a press conference just two weeks prior.

In 2012, King Abdullah the II of Jordan faced a similar dilemma when the monarchy desperately needed to supply a restive urban population with water underlying farms owned by politically connected families [Liptrot and Hussein, 2020]. 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 expropriation was not recorded publically, although it was an open secret among policymakers and locals.

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, 1993b][Tilly, 1993]. This literature finds that democracies expropriate less through political constraints on their executives [Li, 2009].

But not all expropriations are equal; more public methods like nationalization increase the reputation cost, increasing the economic damage. Democratically constrained leaders expropriate less but ban investors from repatriating their profits at the same rate [Graham et al., 2018]. Democratic leaders also prefer more "covert" methods, to appropriate assets without triggering veto points and reduce damage to the economy (Pearlman, forthcoming). Institutional constraints create a cat and mouse game between leaders and societies. Societies and investors attempt to constrain theft while leaders seek loopholes.

But autocrats are constrained more by their elite allies than by the median voter [De Mesquita et al., 2005b]. The dictators close allies can remove the leader with a coup, especially in the early years of a regime. These elite allies have sharply divergent interests from democratic veto players. They stand to benefit greatly from state rents and influence, lose less from economic setbacks and are vulnerable to replacement. This essay asks how these two different constraints affect expropriation type.

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, 1993a]. Because autocratic regimes are lindy [Svolik, 2012], expected tenure is higher late in the regime. Therefore expropriation is highest at the start [Li, 2009]. Alternatively, expropriation may arise due to internal regime politics [Albertus and Menaldo, 2012]. New dictators may expropriation to reassure supporters that the dictator will stay loyal to them.

This paper finds a similar pattern in expropriation strategy, autocrats expropriate more brazenly in their early careers. The autocrat most certain of their position prefers a more subtle expropriation, which protects future revenue from reputation damage and is less transparent to supporters. However, all autocrats continue to expropriate more overtly than democracies. This evidence is consistent with both the revenue maximizing and signalling models.

2 Literature Review

This section begins by reviewing the incentives for and against expropriating foreign assets that regimes face. It then turns to institutional political economy studies. The second subsection reviews models what posit the regime as a single actor. The third turns to models which investigate within-regime contestation.

All leaders need money, and autocrats are no exception. Autocrats also need money to provide public goods to deter revolution [De Mesquita et al., 2005b], but spend less than democracies [Hausken et al., 2004]. Some autocrats are motivated by expensive national or personal projects, leading them to maximize revenue. Tzarist Russia exported during famines to fund industrialization. The Pol Pot regime maximized revenue to purchase arms for a revanchist invasion of Vietnam.

Autocrats also need funds to reward their supporters through patronage

[Pepinsky et al., 2017]. 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, 2008b]. A collapse in the ability to pay supporters often triggers regime collapse [De Mesquita et al., 2005b][Hale and Colton, 2017]. Failure to pay supporters has resulted in the death of several autocrats, including William Tolbert of Liberia and Samuel Doe (who had had himself killed William Tolbert in the preceding wage crisis) [De Mesquita and Smith, 2011].

Expropriation can be highly lucrative. Price shocks increase the probability of expropriation more than political crisis, at least in extractive industries [Duncan, 2006]. Financial crisis restrain expropriation of foreign assets [Jensen et al., 2020]. This result is counterintuitive but financial sensible; the windfall from taking an asset is lower during a crisis, when future years are more profitable. During boom year, the windfall is high relative to future years. International financial institutions restrain expropriation through the threat to withdraw lines of credit, which are crucial to political survival[Jensen et al., 2020]. [Check up on Jensen]

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, 1984]. 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, 2012].

Expropriation does come with costs for a regime [Tomz and Wright]. 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 [Jensen et al., 2020]. Additionally, expropriated assets should be less productive because they have less access to foreign technology [Minor, 1994]. [have the economists expand this]

2.1 Revenue and Constraint

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, 1993b]. 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 subsidizing state businesses. If the asset is given to a supporter, that supporter is appeased but may use the independent resource base to challenge the leader. To formalize this, the leader expropriates if

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

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, the number of years the leader expects to survive and δ the leaders discount function.

Because regimes vary widely in their discount rates, the stationary bandit model explains considerable variation in property rights. The furthest looking autocrats are monarchies, who have long leader tenures, care about their children's wealth and often rely on hereditary and stable support institutions. They protect property rights at a similar level with democracies [Knutsen and Fjelde, 2013]. Single party regimes also have long time horizons due to the secure positions of party leaders and their strong internal communication. Military and non-party regimes last for shorter times and military leaders tend to survive the transition to democracy and keep their ill-gotten gains. Single-party regimes protect worse than monarchies but better than military regimes [Knutsen and Fjelde, 2013]. The property effects are large in practical terms. Moving from a military regime to monarchy has the same effect on the property rights index as a 170% increase in GDP, and from military to single-party is equivalent to a 26% increase.

It is plausible that the expectation of losing power soon would motivate leaders to moderate to prevent punishment from the following regime. **?** showed that such an equilibrium does exist, similar to how some regimes enforce non-execution insiders. Unfortunately this hypothesis directly contradicts Knutsen's stronger evidence and cannot be supported without the dubious assumption taht inequality is a proxy for the regimes wealth.

In contested autocracies, regime institutions such as parties and courts allow the leaders supporters to coordinate and protect one another from the leader [Myerson, 2008a]. Such mutual protection of captains enables credible promises between leader and supporters. Gehlbach and Keefer [2011] proposed that the same institutions allow leaders to credibly commit not to expropriate from the party or court, while continuing predation on outsiders. This relationship is actually revenue maximizing for the leader because it allows concentrated investment without resorting to democracy. The Chinese growth explosion which followed Deng's deconsolidation post-Mao likely resulted from party cadres feeling secure enough to save.

Authoritarian parliaments may also protect investors from state predation. Autocrats sometimes adopt parliaments to make policy concessions with those outside the winning coalitions [**?**]. Parliaments help coopt outsider elites and identify effective policy concessions. Parliaments are associated with higher investment in autocracies [**?**], either by reducing state predation or by improving contract law (protecting investors from their in-country staff). **?** find that parliaments decrease predation on both foreign and national investors, but only in military or party autocracies. The effect is small or nonexistent in personalist regimes.

Autocratic legislatures do have a robust, positive effect on contract law [Jensen et al., 2014]. It appears that legislatures are often too weak to constrain the inner circles expropriations, they can "enable private actors to check one another" [Jensen et al., 2014]. Schuler and Westerland [2018] propose that the relationship between legislatures and predation is a spurious correlation produced by the consolidation process. As leaders eliminate their rivals they close legislatures and expropriate to buy support and quiescence, leading to a non-causal negative relationship.

[add Albertus and Menaldo later]

3 Consolidation, Political Survival and Expropriation

This section lays out an alternative theory of expropriation. New autocrats face constraints from supporters who threaten removal in exchange for benefits. However, such threats cease to be credible once the leader amasses sufficient power to survive a coup with high probability. Expropriation is an appealing strategy for gathering appointments and funding new parties or militia, all while popularizing the leader. We derive the hypothesis in this section.

No one head of state rules alone. There is always some coalition of elite actors who cooperate to elevate their candidate[Svolik, 2012]. We call this group the ruling coalition, although others use winning coalition [De Mesquita et al., 2005a], support coalition or launching organization. Relations between the leader and ruling coalition are fraught because in autocracy there is no overriding arbiter of political disputes; parties must enforce their agreements themselves with coercion or credible threats [Svolik, 2012].

In the vast majority of cases ruling coalitions begin stronger than their leaders, who are only a "first among equals" [Geddes et al., 2018]. However, once chosen both the interests and power of the leader quickly diverge. A power struggle often emerges in which the ruling coalition seeks to bind the leader, and the leader seeks to replace them with loyal cronies. Such replacement extends the leaders tenure, rids them of rent seeking courtiers, and increases their policy control [Geddes et al., 2018].

3.1 Model

This section derives comparative statics for when expropriation is expected across consolidation stages. We will assume that leaders are maximizing their discretionary budget after expenses, possibly to supply public goods, fund pet projects or bad their Swiss bank account.

Consider a consolidated, revenue maximizing leader who receives a rent of one unit from ruling, after the expenses of maintaining a minimum support group. The leader has reduced his coalition by expelling unnecessary members and preventing a threat of overthrow. The leader discounts future payoffs at δ which includes both impatience and the (lower) probability of losing office despite consolidation.

We also assume that expropriation can redistribute assets to produce an immediate windfall, but doing so reduces future tax takes. The leader can expropriate an asset and receive a windfall w to day, but loses C_E in all periods (for simplicity, that includes the first period). The leader refrains from expropriation as long as

$$\sum \delta^t \geq w + \sum (1-c)\delta^t$$

which simplifies to

$$\frac{c}{w} \geq 1 - \delta.$$

In other words, a leader with a constant share of rents and probability of removal only expropriates when the theft has better returns than their discount rate. However, notice that the discount rate contains the removal probability, as in Olson's original "stationary bandit".

In fact, the same is true in negotiations between a support coalition and ruler when the threat of removal is constant. Consider a stable but contested autocracy. The support group can remove the leader with *constant* probability q. The game proceeds as follows: First, the support coalition requests a quantity

$s, 1-s$ of revenue for them and the leader, respectively. Second, the dictator accepts or rejects their offer of revenue. If the dictator rejects the offer, the support coalition chooses to fight or concede. Concession leads to immediate consolidation, giving the support group a reservation wage π_r, where fighting replaces the dictator and grants the desired quantity s if successful and incurs cost f if unsuccessful.

First we observe that if a fight has not occurred, all periods are identical. We therefore solve only a single period by backward induction.

The support coalition decides to fight is

$$u(fight) \geq u(concede)$$

or

$$qs + (1-q)(\pi_r - f) \geq \pi_r.$$

Note that the credibility of this threat is decreasing in both q and s, which is itself decreasing in q. Therefore for fixed reservation wage and fighting costs, a decreasing q will eventually make the threat non-credible. This point is our endogenous consolidation moment. Note also that asking for a smaller s decreases the credibility of the threat, so the support coalition will ask for the largest accepted s.

Assuming threat credibility, the leader chooses to accept if

$$\sum (1-s)\delta^t \geq (1-q)\sum 1\delta^t$$

and the resulting $s*$ is

$$s* = q$$

.

Suppose we add an expropriation component option w w/ cost c, chosen by the support coalition. If the supporter coalition refrains from expropriating they receive

$$u(s) = q1 - \delta$$

.

If the support coalition expropriates in all future instances they receive $q(1-c)$. In the first period the leader will accept

$$(1 + w - c - s{*}{*}) + \delta(1 - c)(1 - q) \geq (1 - q)(1 - c) + w(1 - \delta)$$

which simplifies to

$$s{*}{*} == (1 + w - c)(1 - (1 - q)(1 - \delta))$$

The support group therefore expropriates if

$$(1 + w - c)(1 - (1 - q)(1 - \delta)) + q(1 - c)/(1 - \delta) \geq q/(1 - \delta)$$

$$(1 + w - c)(1 - (1 - q)(1 - \delta)) \geq q * c * (1 - \delta)$$

$$(1 + w - c)/c \geq \frac{q * (1 - \delta)}{1 - (1 - q)(1 - \delta)}$$

In the top equation the primary constraint to expropriation is the difference between $\delta q(1-c)$ on the left hand side and q on the right hand side. This is the loss to future revene from expropriating, which is incurred by the support group, which restrains their expropriation in much the same way as the consolidated autocrat.

The threat of consolidation immediately changes the support groups interest in expropriation. To take the simplest formulation, suppose that consolidation only occurs between the first and second period, and occurs with probability ρ. Neither party can foresee if a consolidation opportunity will arise. The leader now accepts requests if

$$(1-s)+\delta(\rho\sum\delta^t+(1-\rho)\sum(1-s)\delta^t \geq (1-q)\sum 1\delta^t$$

which simplifies to

$$s^*_\rho = \frac{q}{1-\delta\rho} > q.$$

In other words, the leader is less willing to fight in year one because they expect to consolidate later and therefore accepts a larger request in period one to the support coalition. For example, if $q = .8$, $\delta = .95$ and $\rho = .5$ the support coalition can demand 152% of annual rents. Therefore a natural time inconsistency problem develops and gives the leader an incentive to incur debt.

If the support coalition expropriates w at cost c, they can now demand $s^{*}*_\rho$ which satisfies

$$(1+w-c-s)(1-\delta)+\delta(\rho-(1-\rho)(1-q)(1-c)$$

This is a stranger result than anticipated. It implies that if the

H1: Foreign and national expropriation are higher during consolidation episodes

H2: Foreign expropriation declines after a successful consolidation

H3: Pre-consolidation autocrats prefer nationalization, covert theft is more common after consolidation

H4: Consolidation decreases national investor protection in party regimes

H5: Consolidation decreases investor protection by contract law in all regimes

4 Data

Consolidation - Geddes Wright and Franz consolidation index by IRT

Foreign expropriations - Theft database from Kobrin, Miner, Hajzler

National expropriations - idk, any ideas? Maybe the insurance data?

Contract law protections - Use same source as Jensen Malesky and Weymouth

Regime data - REIGN

Regime type classifications - Hadenious and Teorell (note: do not use Geddes because personalist regime coding biased[Knutsen and Fjelde, 2013])

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