

# Do Banking Crises Improve Democracy?

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## BACKGROUND

- Economic shocks have consequences on democracy
- Banking crises (BC) have real consequences on the economy as witnessed by the recent financial crisis
- ... And on democracy?
  - Growing literature on political effects of banking crises.
  - **But first attempt to study the impact of BC democracy**

- Why? Based on Acemoglu and Robinson (2001)

- Non democratic countries are governed by a rich elite which coexists with a marginalized society (the poor)
- The poor can contest the power by threatening a revolution, but at a given cost
- However, the cost decreases during BC, and this may force the elite to democratize to avoid a revolution



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## PURPOSE

- **Assess the impact of BC on democracy**
  - Do BC affect democracy?
  - In the same way?
- **Analyze the dynamics of the impact**
  - What is the timing of the change?

## METHOD: Event Study

- Before/After the end of a BC (the event)
- Sub-periods around the end of a BC

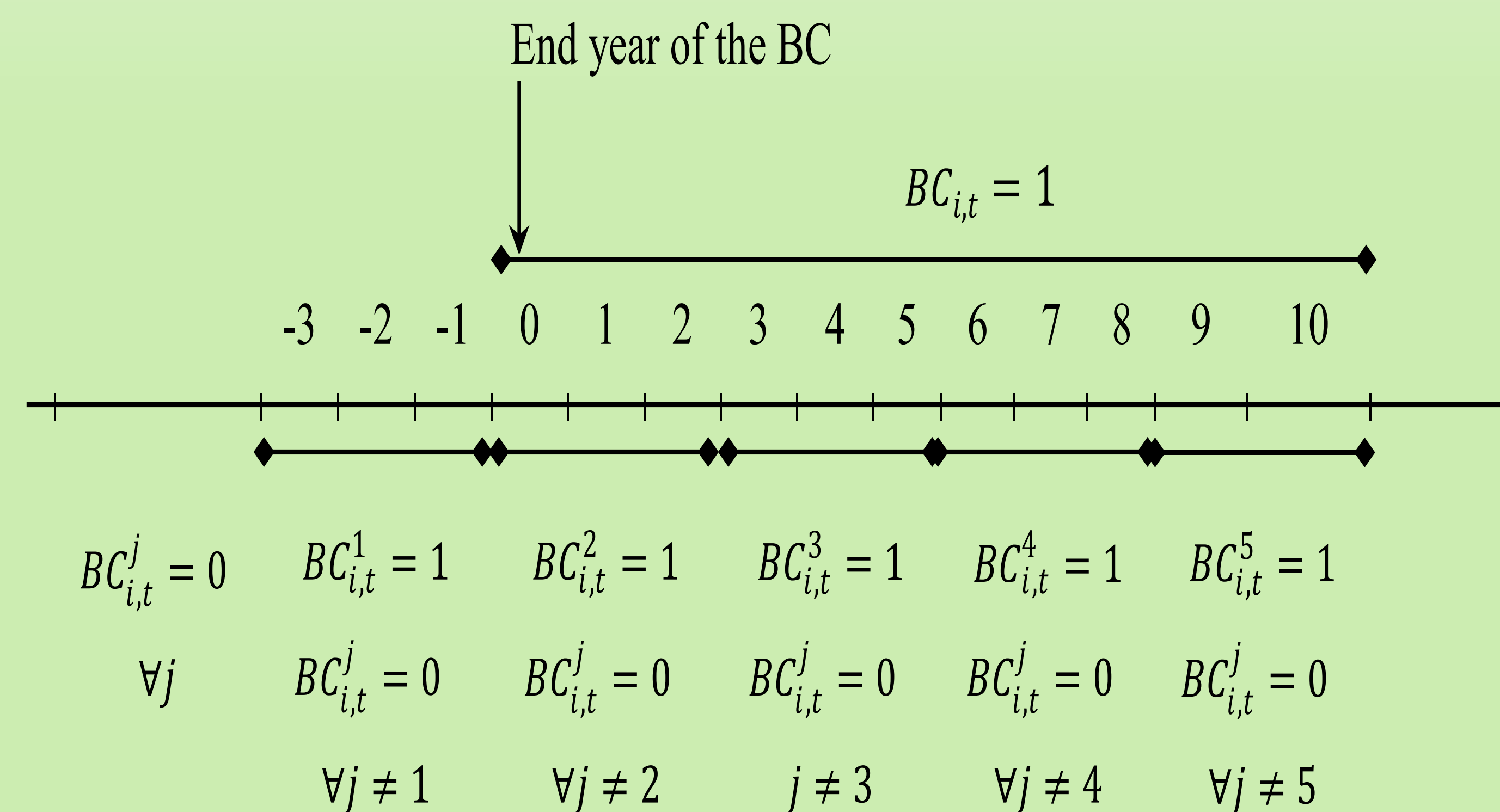


Fig 1. Event Study

## RESULTS

- Estimation by OLS controlling for country and year FE
- Robustness checks using an **alternative measure of democracy**, an **IV approach**, a **System-GMM**

	Baseline	Severe vs Moderate		Demo vs Non demo	
	All countries	Severe	Moderate	Democracies	Autocracies
BC	++++	++++	++++	-	++++

## RESULTS

	Baseline	Demo vs Non Demo	
	All countries	Democracies	Autocracies
BC1		---	
BC2		---	++
BC3	++++	--	++++
BC4	+		++++
BC5	++		++

- +++ (---): indicates positive (negative) and significant at 1%
- ++ (--): indicates positive (negative) and significant at 5%
- + (-): indicates positive (negative) and significant at 10%

## CONCLUSIONS

- Democracy improves in the 10 years that follow a BC
- The bulk of the change materializes from the 3<sup>rd</sup> year
- Severe BC have more consequences on democracy than moderate BC
- The results hold particularly for non democratic countries

## REFERENCES

1. Acemoglu, D., and Robinson, J. A., 2001. A theory of political transitions. *American Economic Review*, 91(4), 938–963.
- \* : <http://www.businessinsider.fr/us/americans-cant-recover-from-financial-crisis-2016-7>