Review of Austrian Economics, 12: 175–200 (1999)


# Entry Barriers in Politics, or: Why Politics, Like Natural Monopoly, Is Not Organised as an Ongoing Market-Process

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**Abstract.** In the paper "Entry Barriers in Politics, or: Why Politics, Like Natural Monopoly, Is Not Organised as an Ongoing Market-Process," an analytical framework for dealing with processes of political competition is presented. The idea goes back to Tullock's model of democracy as franchise-bidding for natural monopoly. To this, basic insights of New Institutional Economics and Austrian Ecomomics are added. It is shown that incomplete contracts which arise in economic bidding schemes, characterise political competition. At the same time, they create leeway for political entrepreneurship. The same is true for various barriers to entry in politics. These barriers affect a trade-off between political stability and contestability which is discussed in view of incentives and opportunities for politicians to engage in positive-sum, long-term investments in political reforms.

**JEL Classification:** D72, D78, L10.

## 1. Introduction

In 1965, Gordon Tullock published a short paper on "Entry Barriers in Politics" in which he sketches a theory of democracy based on the analogy of an auction mechanism for allocating rights to a natural monopoly. In this paper, Tullock not only anticipates the famous proposal for dealing with natural monopoly made by Harold Demsetz (1968), but he also presents a model which is quite suitable for analysing processes of political competition under democratic rules of the game. And yet, Tullock's basic idea has remained largely neglected within the economics of politics.[1]

It is the main intention of the present paper to show that Tullock's basic view of political competition as a process of bidding for political monopoly can be usefully applied and further substantiated in order to highlight and discuss elementary aspects of democratic systems. The model of democracy as a franchise bidding scheme and a closer look at a variety of barriers to entry in politics readily discloses why politics, like natural monopoly, is not organised as an ongoing market process. The title of our paper alludes to Weingast and Marshall's *"The Industrial Organisation of Congress; or, Why Legislatures,*

*I gratefully acknowledge comments and suggestions on an earlier version of major parts of this paper from Ivan Baron Adamovich, Harold Demsetz, Thráinn Eggertsson, Uwe and Annette Mummert, Dennis C. Mueller, Werner Mussler, Thomas Ulen, Gordon Tullock and Stefan Voigt. I also thank two anonymous referees for helpful suggestions. The usual disclaimer applies.

*Like Firms, Are Not Organised as Markets"* (1988)—one of the few and best known applications of IO and transaction cost economics to the realm of politics. Their analysis is, however, limited to explaining properties of the internal organisation of the US-Congress (and especially the workings of its committee system). As e.g. Moe (1990) has observed, political institutions which structure the relationships between politicians and voters have so far been neglected by this approach. Our paper suggests some ventures into this neglected field.[2]

In Section 2 we shortly present the main reasons why political relations differ substantially from market relations and why the provision of political goods and services by the state (democratic or not) is based on specific elements of "natural monopoly." In Section 3 we present and enlarge Tullock's basic idea of democracy as bidding for franchise monopoly. We not only show basic structural similarities to a Demsetz bidding scheme. We also argue that most qualifications of Demsetz's proposal which were put forward by Williamson (1976) and Goldberg (1976) apply *a fortiori* to political "competition for the field." Many of these qualifications relate to questions of contestability of the bidding contest and hence to entry barriers. In Section 4 we argue that democratic elections are characterised by the very same kinds of barriers as Demsetzian auctions—and, again, most barriers to enter *political* incumbency are much more pronounced. In Section 5 we illustrate the practical relevance of looking into entry barriers in politics by discussing their effects on incentives and opportunities of political entrepreneurs to engage in long-term, positive-sum political reforms. The basic result—a fundamental trade-off between political stability and political contestability—is summarised in the conclusion.

## 2. The state as natural monopoly

Political relations differ from typical economic relations in two major, interrelated respects: 1) the forced consumption and indivisability of the goods provided and 2) the monopolistic organisation of the provision. The first peculiarity makes politics categorically different from economic *market exchanges*; the second makes it fundamentally different from economic *competition processes* (Buchanan 1993, 1997:178). While both qualifications are well known to economists, notions like "political market" and "political competition" keep being used not only as short-cut metaphors, but also as wide-reaching analogies. In this paper we are mainly concerned with pointing at necessary qualifications of the political *competition* analogy within an econonomic theory of *democracy*. At a more fundamental level these qualifications also relate to elementary peculiarities of politics in general which must be regarded a non-market exchange phenomenon with the state (democratic or not) possessing as "natural" kind of monopoly. We now provide a very brief sketch of the latter issues.[3]

Unlike private goods, most political goods cannot (or need not) be appropriated privately in return for other private goods or means of exchange. There is a high amount of "free consumption" and "forced comsumption" of political goods due to their high degree of publicness or indivisability.[4] In any political system, there are, in other words, "political external effects" (Buchanan and Tullock 1962:89f). These effects can be "positive" if political goods and services are made freely available to all or some individuals or "negative" if people who would never have voluntarily chosen these political goods (which turn into "bads") are forced to endure them and also to pay taxes for their provision (Hirschman 1970:101). Hence, in any political system there are "free riders" as well as "forced riders" and by necessity almost every person in the polity would have prefered a mix of political goods and taxes different from that which is actually provided. Whereas a single consumer in an economic competitive market setting can (a) avoid forced consumption by simply abstaining from consuming it and paying for it, (b) adapt to changed preferences or prices (hence: scarcities) by simply consuming more or less of the private good and (c) increase her individual well-being by turning to a supplier of a preferred partitionable private cost-benefit offer, a single citizen cannot similarly avoid forced consumption of political goods.[5] All three differences reflect the fact that modern states command a monopoly of force.

The very existence of the state (democratic or not) as an organisation that commands a monopoly of force is argued to be based on (a) scale advantages in the use of violence and/or (b) barriers to the use of legitimate coercion as a necessary input for the production of political goods. These explanations provide rather obvious analogies to definitions of natural monopolies in standard economics: (a) economies of scale (e.g. Bain 1956, 1962) and (b) "barriers to the use of resources" (e.g. Demsetz 1982, 1989a:27)—both of which entail that (with given technologies and within a given area) only one producer can in the long run cover the costs of production.[6]

Economies-of-scale type explanations play a decisive role in the theory of the emergence of the state by Douglass North (1981:21):

> "a state is an organization with a comparative advantage in violence, extending over a geographic area whose boundaries are determined by its power to tax constituents. The essence of property rights is the right to exclude, and an organization which has a comparative advantage in violence is in the position to specify and enforce property rights."

For North, the "scale advantage" of the state is due to the specialisation of any kind of organisation in the use of violence for enforcing any kind of property rights. It is not clear, however, if this theory of the state sufficiently explains the very cause of the exclusiveness of the rights to govern and the range of state activity not only for archaic, but also for modern societies. At least as a complement, an analogy with natural monopoly explanations based on "barriers to the use of resources" (Demsetz 1989:87) or "cost advantages due to ownership of resources" (von Weizsäcker 1980:26ff) could be useful. Such explanations of state monopoly would provide an analogy to Israel Kirzner's (1973:103) definition of monopoly as "position of a producer whose exclusive control over necessary inputs blocks the competitive entry into the production of his products." In terms of Max Weber's theory of the state, the monopolised necessary input for the state's production of protection and justice would be "the means of legitimate coercion."[7] The availability of legitimacy of violence defines the monopolistic character and range of state action. At least in modern times and within civilised societies, the authority of monopolistic state coercion is only as a last resort based on scale advantages in the use of crude violence as such; in the first instance it relies more on the exclusive recourse to legitimacy as a necessary input for the production of laws and regulations that are widely used and accepted.[8]

Both explanations of state monopoly are largely independent of the particular system of government. But they do also hold for democratic governments. Even though democracy, as a method for assigning political leadership, relies on peaceful competition among rival contenders (parties and candidates), it does not do away with the monopoly of legitimate coercion. As Tullock (1965:464) observed, also in a democracy "we can have only one cabinet, governor, mayor, president or majority in a legislature. The scale advantage which acts as a barrier to entry is the majority voting rule which provides that the 'entrepreneurial group' which obtains half the customers can drive the other entrepreneurial group out of the market." Before we discuss different kinds of barriers to entry in democratic politics, we will now present the basic model of democracy as bidding for political monopoly.

## 3. Democracy as a franchise bidding procedure

### *3.1. Structural similarities*

Political competition among parties and candidates, as well as the interaction between voters and politicians, bear almost no resemblance to *ongoing* market *processes*. In their basic structure, democractic elections are much more similar to periodic auctions of a licence to exclusive monopoly rights. This is the core idea of Tullock (1965): (1) There is a "natural" monopoly of government. (2) Periodic auctions of the right to use the monopoly rights of government may prevent some abuses of the monopoly of government. (3) The workability of this pre-stage competition depends, *inter alia*, on barriers to entry in politics.

Thus, Tullock identified for the political realm what later became a hotly debated issue in the IO literature: franchise bidding for natural monopolies. Its underlying idea is that a "franchise system that awards the franchise to that company which seems to offer the best price-quality package would be one that allows market competition between bidding rivals to determine that package. The restraint of the market is then substituted for that of the regulatory commission" (Demsetz 1968, 1989:82). In other words: while natural monopoly precludes competition of simultaneously producing firms ("competition within the field"), the right to operate the monopoly can be competitively determined ("competition for the field"). This—it is hoped—will preclude monopolistic behaviour of those who win the bidding contest and who have to defend their position in coming bidding rounds.

The basic rationale of democratic elections is similar: There cannot be, in one jurisdiction, various producers "offering" (in the sense of enforcing) alternative laws and policies at the same time. There is a monopoly of force. However, the right to operate this monopoly is competitively allocated among various contenders who bid for votes of their citizen-"customers." This—it is hoped—will reduce incentives to act opportunistically during incumbency since incumbent political entrepreneurs will have to win coming "bidding rounds" (elections) in order to keep enjoying political power and office.

So far, Tullock's model captures the basic structure of political competition and provides straightforward analogies with Demsetz's (1989:89) mechanism of "rivalry for incumbency" in the following structural respects:

- based on declarations and *promises*
- made by *potential* producers
- *one* (group of) candidate(s) is given the
- *exclusive* right to provide certain goods and services
- for a specified *period of time* and a specified *area*.

These are the basic *structural* similarities between a Demsetz-mechanism and democracy as a method for allocating political property rights. A closer look at the matter, however, will show that (a) there are already considerable problems with successfully applying the original Demsetzian mechanism to economic monopolies and (b) these *material* complications apply even more strongly to political competition for votes and political principal-agent relations.

Demsetz's (1968,1989) contention that monopoly rents could rather easily and completely be reduced through simple price-cutting auctions without affording further regulation of the use of the franchise has provoked criticism by Oliver Williamson (1976) and Victor Goldberg (1976) who point at complications and "severe contractual disabilities" (Williamson 1976:73) that arise as soon as one allows for "conditions of uncertainty" (ibid.:79). These real-life conditions create problems of (1) assessing the quality and efficiency of the contenders "for the field," (2) ensuring good performance of the winning party that has become sole producer "within the field," and (3) making "competition for the field" sufficiently contestable. The first two kinds of problems mainly involve principal-agent problems and problems of incomplete contracts between those who give the license and those who get the licence to produce for a given time as sole providers of utilities. For an analogy of political "competition for leadership," these problems can be easily translated into a host of principal-agent problems between voters and politicians. In this paper, we concentrate on the third kind of complication: contestability and entry barriers. Some comparative observations concerning the first two problems, however, are in order, to allow to depict some peculiarities of political competition.

### *3.2. Material differences I: political award criteria*

Williamson (1976:81) made the point that "although franchise awards can be reduced to a lowest price criterion, this is apt to be artificial if the future is uncertain and the service in question is at all complex." Obviously, the winning bidder's promise to supply cheaply is "scarcely a well-defined commitment unless the quality of service is well specified..." (ibid.:80). Such problems of complex and insufficiently defined "price-quality packages" as criteria for the selection of the "fittest" competitor apply also—but with much greater force—to political elections:

While in the original Demsetz-setting the "lowest price criterion" may be insufficient, in the Tullock-arena of political elections it is virtually non-existent. Even if political entrepreneurs would compete on something like a "lowest tax criterion" for comparable qualities and quantities of political services, the voters' task to compare political cost-benefit packages seems considerably more demanding than that of an economic franchise-giving agency. First, many political actions are not directly related to tax expenditures; hence political offers cannot easily be compared by using taxes as common denominators. The "measuring rod of money" can more effectively be used in economic than in political exchanges. In addition, in the original Demsetz scheme a comparatively fixed and small number of services to be provided is given to the bidders, whereas political parties and candidates compete with far more complex packages of promises in a wide open field of issues.

It is right here that political entrepreneurship during "competition for the field" enters the stage. In political reality, there is no pre-defined political "issue space." Hence, there is no compelling reason why politicians should not act as entrepreneurs who would differentiate their offers, propose new problem-solutions, or shape public opinion. From a principal-agent point of view, of course, such leeway is exactly at the heart of the problem because now we find that it is not citizens or voters who act as agenda-setters and determine the political services to be rendered and then simply select the political agents who would do it most "cheaply." It is political parties who set the agendas while voters can only voice some general preferences on a limited set of obscure promises. Finally, electoral promises are much less operational and binding than contractual provisions in the Demsetz bidding scheme. Hence the "contractual disabilities" to be discussed next.

### *3.3. Material differences II: incomplete electoral contracts*

As a second qualification of Demsetz's proposal, Williamson and Goldberg claim that after "competition for the field" has produced its winner, many issues would remain for further regulation. The licence is a "relational," "incomplete" contract. Uncertainties about future developments, complex attributes of the (experience-)goods to be supplied, and bounded rationality of the acting individuals prevent the conclusion of fully-contingent licence-contracts. At the same time, it could well be in the interests of principals (customers) to have some built-in flexibility in the contract to allow their agents to react to unforeseen changes in technologies, preferences, relative scarcities etc. (Goldberg 1976:437f ). The control of the use of such entrepreneurial leeway, however, once again makes some kind of regulating agency necessary.

Contractual disabilities of this kind again become all the more obvious on the execution level of a political monopoly. The "contract" between voters and politicians is not just "incomplete"; it is at best implicit. Elections only assign power (seats) to parties and candidates, thereby (pre-)determining who should govern. They do not give binding instructions *how* to govern. The political principal receives no claim on any particular political service as a result of his or her vote. The winning political party is under no legal obligation to perform any particular act as a consequence of its electoral promises. Indeed, the party in power can, if it likes, do just the opposite. And again, this is the very basis for the political entrepreneur to act as Schumpeter wishes, including the pushing through of political innovations which the principals "never thought of and would not have approved of in advance" (see Schumpeter 1942, 1987:278).[9]

At the same time, these severe contractual disabilities create enormous leeway for post-election opportunism of elected agents to pursue policies that a minority or even a (badly informed or weakly interested) majority of principals would never have approved of at all. From this perspective, there certainly is a need for a political equivalent of the "licence agency" that Williamson and Goldberg demanded in order to heal shortcomings of incomplete licence contracts. At this stage, Tullock's basic analogy leads us right into the centre of the perennial question "*quis custodiet ipsos custodes*?" The problem is to find a powerful and independent political agency for the control of political agents who command an overriding democratic legitimisation to act as agents of the voting public. And then the question still remains unresolved: who controls these controllers?

Democratic nations that subscribe to the rule of law have found a more or less satisfying solution to this problem: In the execution of particular policies politicians are controlled by the rule of public law and constitutional law. The rule of law can regulate at least some of the countless contingencies that are not covered by electoral "franchise-contracts."[10] However, one fundamental peculiarity of the regulation of politics remains: the rules of the game—including constitutional rules—are produced and can be changed by the group of "players" that ought to be controlled; political competition is fundamentally self-regulated.

One might expect that political "self-regulation" would not lead to excessive opportunism of incumbents, since the licence to govern is temporary and has to be gained again in new rounds of open "competition for the field." Such an argument would rely on the benefits of *potential* competition equal to those expected by Schumpeter (1942, 1987:85) who argues that "competition of the kind we now have in mind ... disciplines before it attacks. The businessman feels himself to be in a competitive situation even if he is alone in his field." The same argument can be applied to the incumbent government which after the elections finds itself alone in the field of national policy-making: the threat of losing in the next elections would "discipline before it attacks." This is the rationale of the "principle of anticipated reactions" (Sartori 1987:152ff ) according to which incumbents are continuously influenced by the anticipation of voters' reactions. An "invisible hand" optimism in politics, however, would rest on a number of dubious assumptions and analogies. An important subset of such assumptions relates to the "contestability" of political competition and hence to entry barriers in politics, a subject to which we now turn.

## 4. Entry barriers in politics

Williamson's (1976:83) third major qualification of Demsetz' model relates to entry barriers when he argues: "Lest meaningful competition at the contract renewal interval be upset, participation in contract execution should not place winners of the original competition at a substantial advantage over nonwinners." Once again, very similar problems arise with respect to bidding for political monopoly as we discuss entry-barriers in politics. Table 1 shows the different categories of barriers to entry (1) as they occurred in the discussion of the Demsetz-model of bidding for franchise monopoly and (2) as they occur in the context of a Tullock-model of bidding for political monopoly.

During democratic "competition for the field" we find a host of political analogies to "barriers to entry for the bidding" (von Weizsäcker 1980:32) which were already discussed in the context of the Demsetz-model. As a structuring device, the classical distinction between "innocent" and "strategic" entry barriers can also be applied to entry barriers in politics. According to Salop (1979:335) an "innocent entry barrier is unintentionally erected as a side effect of innocent profit maximization. In contrast, a strategic entry barrier is purposely erected to reduce the possibility of entry." The political analogies should be obvious. As another category we introduce the rules of the game of electoral competition—which can

*Table 1.* Barriers to entry in politics and bidding for natural monopoly.

| | Barriers to entry in bidding for franchise monopoly (Demsetz) | Barriers to entry in bidding for political monopoly (Tullock) |
|---|---|---|
| Given rules of the game | Licence period | Incumbency period |
| | | Party admission |
| | | Share thresholds |
| | | Plurality voting |
| "Innocent" barriers | Reputation (good will) | Reputation (good will) |
| | Experience (tacit knowledge) | Experience (tacit knowledge) |
| | Idiosyncratic relations to the licencing agency | Idiosyncratic (ideological) relations to voters |
| | Specific investments | |
| "Strategic" actions | | Specific investments |
| | | Manipulations of rules |

be both "innocent" or "strategic." As long as they are taken as given by the players and not opportunistically changed by the winners, they remain quite "innocent." If they are manipulated by those in power in order to reduce contestability, however, they turn into instruments of "strategic" entry barring (see below).

### *4.1. Rules of the game*

Political competition entails the citizens' collective choice of rulers and the rulers' choice of politics. Both are choices "within rules," or institutionally constrained choices (e.g. Vanberg 1993). The rules of the political game describe political property rights, and some also act as barriers to entry to the political bidding. Four examples may illustrate the point:

(a) An elementary legal barrier to entry for political bidding is erected by the periodicity of elections, i.e. the low frequency with which new parties or candidates are allowed to enter new elections. Parties in opposition, and even more so parties that have not yet entered parliament, are excluded from the use of legitimate rights to produce political goods until the next election. The basic rationale of incumbency is the same in Demsetz' bidding and in Tullock's democracy: to produce stability of expectations and thus encourage agents and principals alike to engage in long-term investments. On the other hand, one wants to oust incompetent holders of licences as quickly as possible in new rounds of "competition for the field," which may also facilitate taking in new opinions of citizens. Thus, one would expect that the more frequently bidding for political monopoly is repeated, the higher will be the responsiveness and "contestability" of monopolistic government and the lower the degree of political stability and "governability" of the polity. Surprisingly, this trade-off has hardly been dealt with in public choice models. We discuss its relevance in more detail in Section 5.

Other rules of the game come to mind which act as legal barriers to entry and affect trade-offs between "contestability" of political "competition for the field" and political stability "within the field." Whereas incumbency periods influence the *frequency of contests*, the following rules mainly influence the *number of contestants*:

(b) The admission of parties and candidates to political elections is often subject to legal "barriers to entry for the bidding," such as the requirement of a minimum number of members and supporters or of loyalty to the country's constitution.
(c) The entry of small parties to representative assemblies is often blocked by requiring minimum shares of votes (such as the German 5% threshold).
(d) Plurality voting systems such as the British "first-past-the post-" rule act as an almost insurmountable barrier to entry for small or new parties (especially if minority-interests are distributed quite equally throughout voting districts).[11]

These rules of the game tend to reduce the number of possible coalitions and thus the costs of searching and bargaining a multi-party government. They also help increase political stability and the sustainability of governments. However, they may as well act as frustratingly high barriers to entry for new parties, to the representation of political minorities and to the introduction of new political ideas, styles etc. These arguments apply most strongly for plurality vote systems, which tend to greatly increase political stability or "governability," as compared to complex and fragile political coalitions which sometimes have to yield to radical parties and to bridge large ideological gaps. However, plurality rules also increase the likelihood of large disproportionalities between votes and seats and the frustration of new parties and political movements.[12]

### *4.2. Innocent barriers*

"Innocent" barriers to entry in politics relate to the simple fact that "we can have only one cabinet, governor, mayor, president or majority in a legislature" (Tullock 1965:464). Only the winners of the political franchise are entitled to actually "produce" and provide political goods and services, whereas members of the opposition can hardly do more than offer dissenting opinions, critique and proposals. At least three kinds of barriers result:

(a) Incumbents often enjoy some goodwill-advantage because the quality of new bidders' offers can be even less easily and reliably assessed (Tullock 1965:463). Winners of exclusive long-term rights to produce also acquire the exclusive possibility to build up a reputation as a consequence of "the investment in an honourable long history" (Demsetz 1982, 1989a:38). For voters, candidates and programmes that compete for "the field" have essential attributes of experience goods (Telser 1976:337f ): the quality of the offer can not be assessed prior to "purchase" (election). It will be revealed only *ex post* by experiencing actual performance. The usual reaction of consumers (voters) is then to rely on past experience. In this case, outsider-competitors have a systematic disadvantage as long as consumers (voters) are somewhat risk-averse. Incumbents can build up goodwill or create loyalty as an asset that newcomers cannot as easily achieve if they find no way to prove their actual qualities as incumbents.[13] Some empirical studies of voting behaviour have found support for an "incumbency advantage" of this kind.[14]

(b) Williamson (1976:81f ) claims that "idiosyncratic" relations between the award giving agencies and the incumbents of their choice could also act as barriers to entry. He expects that "publicly accountable decision makers acquire political and psychological stakes in their own decisions and develop a justificatory rather than critical attitude towards them." Such bias should at first sight not be expected from voters as "political franchise award givers." Voters are not in the same sense "publicly accountable decision makers." The individual voter is anonymous and has no decisive influence on the result—so why should she feel responsible for her "choice" and be biased in her assessment of it? In fact, however, studies show that voters feel committed to their political choices and take "justificatory attitudes" towards them. In politics as in other areas, individuals try to avoid "cognitive dissonance."[15] Their selective search for, interpretation and storing of information and opinions aims at confirming personal political views. For the voting citizen, the unreflected persistence of voter-loyalty, the "uncritical" adherence to fixed ideologies and even stubborn holding of erroneous views is "cheap," since "wrong" voting remains inconsequential. In addition, political parties, interest groups and mass-media deliver (for free) ideologically pre-selected information, argumentation and other aids for cognitive self-confirmation.[16]

(c) More or less "innocent" barriers to effective and radical change can result from specific investments. If incumbents have invested in specific, long-term capital (including human-capital investments), which cannot easily be transferred to alternative uses, changing the staff in charge becomes a costly and risky affair (Williamson 1976: 84ff ). Similarly, political incumbents' investments in projects that are hard to reverse and in skills that are hard to transfer establish barriers against the opposition's entering government *and* changing its policies. Inexperienced newcomers face problems of achieving the necessary knowledge and skills—including non-transferable "tacit knowledge" in the sense of Polanyi (1967)—that is needed for handling bureaucracy, diplomacy and other political affairs. This complication may not only add to an incumbency advantage to the extent that it influences voters' assessments of competing candidates. It also helps to explain why new entrants in positions of political power do not radically change the personnel of political agencies—at least in the lower and middle ranks. Such conservatism is needed for new ministers and political leaders to make use of the political know-how and routines established by their forebearers.

### *4.3. Strategic barriers*

Various kinds of barriers can also be deliberately erected in order to protect investments in particular laws, regulations and programmes. The emergence of such devices has been analysed by Terry Moe (1990:227ff ) who argues that incumbents create structures for their conduct that often involve self-binding commitments. Such acts of self-binding are basically intended to bind rival political entrants and keep them from destroying political creations and investments. Incumbents try to protect their political legacy (including privileges of their political clients), by using strategies that are not just unavoidable by-products of incumbency. Hence, they cease to be "innocent entry barriers" in the sense of Salop (1979) and become obviously "strategic." Some examples:

(a) Incumbents can induce the executing bureaucracy to establish and rely on complex, almost irreversible, idiosyncrasies and routines. This strategy involves, among other things, "for today's authorities to specify, in excruciating detail, precisely what the agency is to do and how to do it, leaving as little as possible to the discretionary judgement of bureaucrats—and thus as little as possible for future authorities to exercise control over, short of passing new legislation" (Moe 1990:228).[17]
(b) Alternatively, the present government can erect legal amendment-barriers by giving a policy the status of constitutional law. This, of course, requires that the present majority be large enough to amend the constitution—or that (parts of) the opposition can be convinced (e.g. by using log-rolling mechanisms) to support such lasting changes.
(c) To include (parts of) the opposition by way of various forms of co-optation in order to create lasting political compromises can be an effective device to protect given policies from being overturned by future authorities. Again, log-rolling at the expense of unrepresented "latent" groups can be used to secure particular projects and privileges for a time after the next elections (Shepsle and Weingast 1981).[18]
(d) Programmatic continuity can also be achieved through the inclusion of vested interest groups in political decisions and in the administration of policies. This may lend political programmes an allure of additional legitimacy (due to the so-called "consent" of all concerned). In addition, the power base against which political reform would have to struggle is hereby enlarged.
(e) Further examples of "strategic barriers to change" involve manipulative changes of the rules of the game that bar outsiders and increase the rents of insiders. The group of insiders may now include all or most established political competitors within the "political class" engaged in cartelised attempts to reap their rents, while the general public and unorganised or non-opportunistic political activists stay outside (Frey 1994:340). Again, this is due to the above-mentioned fact that the rules of political competition emanate from decisions of the political competitors themselves. The incumbent majority—if necessary in collusion with (parts of) the opposition—is enabled to "make laws about elections, ... set rules governing voter qualifications, campaign contributions, the form of the ballot, the role of political parties, and virtually anything they want to regulate about how the public can legitimately 'control' them" (Moe 1990:223). Given that the political freedom to compete is thus guaranteed by no external power but by the competitors themselves, the rules of the game cannot be expected to be very open for outsiders and newcomers.[19]

## 5. Entry barriers and the political economy of policy reform

Similar to discussions within the IO-literature, also in politics entry barriers can be regarded as crucial for stimulating or frustrating innovation, investment and entrepreneurship. Do legal barriers to entry in politics protect and encourage or discourage political entrepreneurs' investments in necessary long-term reforms? How do "innocent" barriers affect the entrepreneurial activity of politicians? Can political practices for protecting agencies and programmes stimulate political investments in sustainable reforms or do they rather increase political sclerosis? These are big questions which cannot all be answered in one paper. As a first step, however, we can provide some reflections which may signal the usefulness of our analytical framework and point to fields of further research.

### *5.1. The problem of sustainable investments in market-oriented reforms*

It is necessary to begin the following discussion by mentioning that political innovation and political entrepreneurship should not be taken as normative concepts. Again, crucial differences to the respective economic counterparts arise: In the economic sphere, new production processes, goods or services can be assumed in principle to be beneficial to the economy as a whole. But not in politics. The reason is that, in a market economy, innovation means additional variations that can be selected by market participants; it enlarges the choice set, so that people are free to choose from a greater tableau of alternatives. In a polity, new policies tend to simply replace old ones and their "consumption" remains just as unavoidable as before. New policies do not create new opportunities; they create winners and losers and hence cannot, as such, be related to something like political "progress."

With this caveat in mind, we now concentrate on one possible expression of political entrepreneurship: the pushing-through of fundamental political reforms assumed to be of a positive-sum kind. Arguably, policies to transform post-socialist societies and developing countries into systems that adhere to market co-ordination and the rule of law, as well as policies aimed at a reduction of protectionism and rent-seeking belong to this category. Positive-sum reforms would aim at establishing or strengthening non-discriminatory general rules of market co-ordination and open entry to economic competition, while abandoning or weakening special privileges, subsidies or other exemptions from the general rules of the game. As Williamson and Haggard (1994:531) observe, such reforms "are like an investment that should ultimately benefit the majority by enough to make them happy they made it, but that in the short run will—like all investments—involve sacrifices." What makes these reforms politically risky is a combination of the following unfavourable conditions:

- the benefits may be substantial, but they are not as visible as the costs;
- the benefits may be long-term, but they also appear only in the long-run, while costs (sacrifices) become visible much earlier;
- the beneficiaries may have a large majority, but they are also diffuse or even unknown while the costs are readily evident and concentrated on a special group;
- the potential beneficiaries would thus often belong to an unorganised (latent) group, while the potential losers would make up parts of a powerful group which for attaining its favours has already formed a powerful rent-seeking organisation.

Hence, for incumbents to become re-elected by a majority of voters, it is not sufficient for them to invest in policies that would actually benefit a majority of voters. If politicians should expect re-election on the basis of investments in positive-sum reforms, they must find additional incentives or opportunities. Many of these incentives and opportunities depend on the properties of entry barriers in politics, a subject to which we now turn.

### *5.2. Basic virtues of entry barriers in politics*

Entry barriers create frictions—in economic and in political competition. The absence of such frictions is essential to what is called "perfect competition"—a model assumed to describe the basic virtues of competition and to prescribe conditions which should be created by politicians seeking welfare improvements.[20] These contentions were early (but never wholly successfully) refuted by some, mostly "Austrian," economists. Friedrich Hayek argued that "perfect competition' means indeed the absence of all competitive activities" (1947, 1948:96) since the model describes an unattainable state of rest based on assumptions which prevent the taking into account of essential preconditions and virtues of competitive processes as procedures of spontaneous knowlegde-creation and dissemination. With equally compelling thrust Joseph Schumpeter (1942, 1987:105) showed that "perfect competition" is inadequate for describing and prescribing dynamic capitalist systems, because "[t]he introduction of new methods of production and new commodities is hardly conceivable with perfect—and perfectly prompt—competition from the start."

An "Austrian" view of *political* processes would be quite similar. Some real-life frictions, complications and barriers which prevent perfect political competition may well have some important functional properties. Let us here deal with one such issue that easily comes to mind. Just like the famous contention of Schumpeter (1942, 1987) that firms which enjoy at least some temporary monopoly status will find innovation more attractive, one can argue that some entry barriers in politics are necessary to increase the capability and hence the likelihood of wide-scale political innovations and far-sighted reforms. The thrust of this argument is on the political risks of market-oriented reforms sketched above. Risky long-term investments (economic or political) may be more likely if entrepreneurs can deploy some practices to protect their investment.

For *economic* inventors and reformers, one way of protecting returns on investment and hence encouraging innovation is patent protection. This way, of course, is not open to political innovators. For such a case, Schumpeter (1942, 1987:88) provides a substitute: "if a patent cannot be secured ... other means may have to be used in order to justify the investment" and he goes on to propose exactly that class of means which is used in politics to encourage investments: "long- period contracts secured in advance ... in order to tie prospective customers to the investing firm." (ibid.) The four or five year licence to govern that politicians achieve in democratic elections can be interpreted as a long-period relationship that ties citizens to the winning government and gives the government time to invest, to stand through the usual hard times following the introduction of reforms and hope still to be there to reap the electoral benefits when the positive sum effects of the reforms would start to show.[21]

Still, such periods of protection from direct contestability have not been able to prevent an often lamented short-sightedness of democratic politics. For some political activities, four or five years of incumbency may not suffice for politicians to expect the timely "amortisation" of long-term investments in reforms. This argument can also be found in Schumpeter (1942, 1987:287) arguing that "government's dependence upon the voting of parliament and of the electorate ... forces upon the men at or near the helm a short-run view and makes it extremely difficult for them to serve such long-run interests of the nation as may require consistent work for far-off ends.” The politician who is exposed to excessive struggle for power and office would “be likened to a horseman who is so fully engrossed in trying to keep in the saddle that he cannot plan his ride” (ibid.). The longer the protected incumbency, one can argue, the longer will the horseman have time to master his horse and the more wide-reaching will be his ride. The longer the period until the next elections, the longer the “honeymoon” of a new government can last during which initial problems and sacrifices can be more easily sustained because they might be forgotten by the next election or can still be blamed on inherited miseries of predecessors.[22] Thus, longer terms of incumbency could, *c.p.*, enhance incentives for politicians to invest in long-term policies. The *ceteris paribus*, however, is not a small one, as we will see in due course.

Other rules of the game which act as barriers to political competition can help to prevent “ungovernability” (see Kavanagh 1980:223ff ) or the erosion of the political entrepreneurs’ power bases during difficult times. They include the use of plurality vote systems or (in systems of proportinal representation) the creation of grand coalitions, the prerequisite of a constructive vote of non-confidence before parliament can dismiss a cabinet, and the errection of barriers to entry of small parties. All these obstacles, by supporting the survival of incumbents, might lend courageous reforms a better life-expectancy.[23]

Political reformers not only need time; they also need resources. The most important political resource in the early times of comprehensive reform is citizens’ loyalty or goodwill. Loyalty, as Hirschman (1970:chap. 7) points out, creates “barriers to exit” which induce the voter-citizen to refrain from or to postpone her turning to another jurisdiction (or, for that matter: to the opposition-party) in the case of a decline in the performance of her organisation (local government, party). Thus preventing the rash and massive withdrawal of political resources (tax-money, public opinion and votes), loyalty creates political stability.

The mutually reinforcing combination of stability and loyalty can be an asset for both, citizens and politicians, but for different reasons. For citizens the continuity of government combined with a confirmed belief in the general trustworthiness of incumbents helps reduce uncertainty as to the general tendency of political development. Since private investors and partners in long-term contracts appreciate secure political “data” and political stability, some barriers to entry in politics may increase the prospects of economic growth.[24] For incumbent politicians, trust, loyalty and goodwill yield political credit which helps them through wide-reaching reforms during an initial period of “blood, sweat and tears.”[25] There is a clear analogy to what von Weizsäcker (1980:85) describes as a virtue of the “seemingly conservative extrapolation principle” of consumers in highly innovative industries: “If his experience ... was good with the products of a supplier in the past, he will have trust in the new products of the same supplier. This then greatly accelerates acceptance of new products and hence greatly increases the incentive to develop new products in the industry.”

Incentives to develop new potential problem-solutions and to discover their problem-solving potential, however, may also be seriously reduced by many of the barriers to entry we have presented above. We now discuss the negative side of political entry barriers.

### *5.3. Entry barriers and stifled political discovery processes*

Democracy, if compared to autocractic political systems which do not rely on the competitive bidding for incumbency, can be argued to provide some analogy to the virtues of economic "competition as a discovery procedure" (di Zerega 1989).[26] In particular, democracies more than other political *régimes* provide legal conditions and political incentives for engaging in an open exchange of political views and opinions (Hayek 1960:108ff). Even if the "marketplace of ideas" is far from being perfectly open and competitive (Weissberg 1996), the fact that incumbents and opposition politicians are forced to convince voters about their own political projects and that they are free to criticise the views of their contenders yields incentives to provide, scrutinise and disseminate political information—information which in autocratic systems often enough remains undiscovered or hidden. To be sure, there are many obvious reasons why even democratic politics cannot mimic the workings of market competition in the economic sphere. Two of the most fundamental ones reflect the nature of politics (democratic or not) as outlined in Section 2; the third refers directly to barriers to entry in democratic bidding for political power:

1) The interaction between suppliers and demanders of political goods is not equivalent to voluntary market exchange. As a consequence, political coordination lacks a meaningful analogy to the system of relative prices which would act as signals that allow individuals to adapt to circumstances about which no single mind can ever have sufficient knowledge. Hence, it is not only that in politics the incentives for citizens to become informed about political issues are comparatively weak. What is more important (and less accounted for in the Public Choice literature), is that in politics there is no adequate tool for mimicing the qualities of a flexible system of relative prices as devices for the discovery and use of local knowledge and skills in society (see Wohlgemuth 1995a).
2) The prospects for the creation of new problem-solutions, the discovery of failures and the delimitation of the scope of these failures are more restricted in the realm of political learning processes than in the creative and selective environment of market competition. Within one jurisdiction or "natural" monopoly of government, there is only one set of political problem solutions being tested at a time; hence political evolution is basically limited to learning from consecutive trials and errors. Competitive market processes, in turn, allow for an ongoing spontaneous parallel testing of the adequacy of many competing real-life entrepreneurial trials at a time (Vanberg 1993:15f).
3) What is more directly relevant in the context of democracy as bidding for political leadership is the question of contestability. If competing political services cannot be tested simultaneously, competing political suppliers ought at least be able to enter easily. Consecutive political learning would be accelerated if opposition parties find good opportunities to propose and enact new problem-solutions and replace old unsuccessful governments. From this perspective, low barriers to entry and exit in politics would seem to create rather favourable conditions for political competition to act at least somewhat like a procedure for the discovery, selection and propagation of new political problem solutions. In this respect, one is tempted to argue that barriers to entry in politics are rather too high.

Let us now follow up the last argument. As an analogy to the older Schumpeter hypothesis (1912, 1934:66) that "new combinations are, as a rule, embodied ... in new firms which generally do not arise out of the old ones but start producing beside them" one can infer that competition for the natural monopoly of government does, as a rule, hardly ever allow new political combinations to see the light of day. And indeed, the contestability of the political "market" is in this respect extremely low when compared to typical economic markets. Within the field of party politics, new "firms" rarely appear and, even among the few established parties, one party can cling to power for a considerable time. As e.g. Demsetz (1982, 1989b:291f) observes: "In the twenty year period from 1932 to 1952, with the exception of one Congress, the Democrats in the US firmly controlled both the administration and Congress, and, even after losing the presidency to Eisenhower in 1952, again with the exception of one Congress, they continued to control Congress until 1980. In no major unregulated US industry has one firm been dominant so long."[27]

One obvious reason for this relates to the differences of award criteria. With usual market competition, if a firm gains, say, 20%, or as a newcomer some 4% market share, this can often be called a success. By contrast, in politics only with a "market share" of over 50% of the seats can a group of political entrepreneurs (say, a coalition of parties) have innovative policies "produced" at all. In this respect problems of entry of political innovators are very similar to those of admitting innovative producers in socialism, where the "man with the new idea will have no possibility of establishing himself by undercutting" (Hayek 1940, 1994:247) and his new idea cannot be proved until he has convinced the central planners that his way of producing is cheaper or that his new product is useful. Similarly, the political "man with the new idea" cannot start producing new politics until he has convinced a majority of voters to elect him to office (Mitchell 1984:167).[28] In addition, capitalist markets hold out the prospect of considerable material rewards for entrepreneurs as a premium for personal risk-taking. Political entrepreneurs, by contrast, do not become very rich as a consequence of taking risks. And indeed, political agencies seem to reward and thus create and/or attract people with a high level of risk-aversion.

Our discussion so far does not amount to a critique of democracy. This is just the way politics works under the rule of monopolised legitimate coercion and how it ought to work if we take into account that the risks of failed political innovations and reforms have to be shared by the citizens collectively. However, as we have seen, various other kinds of entry barriers in politics are the result of institutional design and hence of politics itself. This does not make their lowering very probable in view of self-interested incumbents, but it allows useful comparative assessments of different political systems. In this respect it seems plausible to assume that lower entry barriers in politics for people and parties with new ideas would stimulate "competition for the field" and thus induce incumbents "within the field" to be more active, creative and innovative themselves. In this line, Tullock (1965:464) wanted to make sure "that the entry barrier is low enough so that this potential competition is a real restriction on the activities of the present occupant of the monopoly." And indeed, if one attaches great weight to problems of how to oust an incompetent government, how to avoid sclerotic routines of administration and how to stop increasing interweavings of incumbents and rent-seeking interest groups, lower barriers to changes of government and policy seem most advisable. Under these circumstances, increased contestability of political power could accelerate the pushing through of positive-sum reforms, on the general desirability of which the public at large may since long have formed a favourable opinion, but which have been blocked by incumbents being trapped in long established rent-seeking arrangements.

One indirect way to break these barriers to change and reform would be to shorten the incumbency period, thus increasing the bidding frequency and the actualisation of potential competition. If the cards are reshuffled more frequently, one could argue, opposition parties would have a better chance to enter the electoral contest with new ideas and conquer the political apparatus with new policies. As a consequence, incumbents might also be more urgently challenged to enter the next bidding with new ideas.[29] Under conditions of political scelrosis, other institutional designs which support easier political entry and exit and hence reduce the stability of political incumbency might also be welcome. Multiparty systems and lower representation-hurdles may now, in addition to their providing better representations of voter preferences, also appear more attractive because they make the creation of "new combinations" of parties, policies and potential problem-solutions more probable.

### *5.4. Breaking barriers with outside-competition: the virtues of inter-jurisdictional competition and direct democracy*

Our explanations of government as natural monopoly in Section 2 apply fully only within a single, closed political system of purely representative democracy. As soon as we extend our view to (a) international superstructures of open borders between nations, (b) federalist substructures within a nation, or (c) procedures of direct democratic rule, new dimensions of competitive activity and contestability enter the picture.

The first two ways of securing competition "from outside" relate to what is called institutional competition among jurisdictions which compete *simultaneously* and as producers of basically the *same* category of goods: legitimate political decisions (Wohlgemuth 1995b). At the same time, citizens as users of alternative institutional arrangements can "exit" the domain of local politics and "enter" competing jurisdictions (Tiebout 1956). Inter-jurisdictional competition is driven by owners of mobile resources who—mainly by allocating capital—take advantage of institutionally (co-)determined differences of expected net-yields within different jurisdictions. To the extent that such implicit "choice of rules" is open to citizens, the natural monopoly of state legislation is compromised: Within the respective jurisdictions the monopoly of force is still on place and subject to bidding for exclusive licence ("choice of rulers"); but citizens are no longer strictly confined to a "forced consumption" of all political goods. Their exit provokes incumbent political entrepreneurs of different jurisdictions to engage in a parallel bidding for mobile resources.

Lower exit barriers for citizens as demanders of politics therefore can be recommended as an effective alternative to lower entry barriers for potential suppliers of politics. The former exposes incumbents to competition *within* the field of rival jurisdictions where they find their equals in equally incumbent policy-makers. Politicians now face opportunities to discover and incentives to introduce new elements of the institutional infrastructure which might attract foreign resources. In addition, competition within a federal system is also apt at lowering barriers to entry for the national opposition. Federalism offers opportunities for voters to observe the opposition at the federal level "on the job" of producing real political goods (and not just criticism). This lowers the incumbency advantage barrier, since voters can now assess the political capability of opposition-parties (and often the top-contenders for presidency) under real-life conditions. Parties holding office in states are in a better position to challenge federal incumbents.[30]

What makes institutional competition a recommendable alternative to changing barriers to entry (e.g. by changing the political constitution) is that it can achieve increased political contestability without much endangering political stability and thus the incentives to risk long-term, positive-sum reforms. Indeed, institutional competition may even improve the opportunities and capabilities of incumbents who try to install and keep up such reforms. Inter-jurisdictional competition can be argued to make politicians and the public at large more sensitive to positive models and negative examples of the policies pursued elsewhere. At the same time, international and federal rivalry in trying to attract valuable mobile resources creates good arguments for engaging in market-oriented reforms. In addition, the ominous threat of outside competition (or "globalisation") can be used by incumbents as a kind of a scape-goat if politicians point at forces outside their reach which necessitate radical change.

Very similar arguments can be put forward as recommendations for direct democracy. First of all, referenda and popular initiatives greatly and in most cases beneficially increase the contestability of political incumbency. Direct democracy can be a singularily effective tool for giving citizens a chance to break the barriers to change which are result from the self-regulation of the *classe politique*. Especially popular initiatives can break the agenda-setting and self-protecting cartel of politicians while giving *private* institutional entrepreneurs a chance to articulate and sometimes even realise alternative ideas. As the Swiss example indicates, referenda provide incentives for citizens to become informed on particular political problems and to enter the political field with their own ideas—thus sometimes producing decisions that incumbents would not even have thought of before (Bohnet and Frey 1994).[31] Direct democracy offers opportunities to work as a discovery procedure and an instrument to brake scelerotic inertia of politics; its prospects are less ambiguous than the attempts at lowering barriers to enter parliament which were discussed above.[32] As with institutional competition, direct democratic competition also can be used to support long-term investments in positive-sum political reforms. Such reforms, if backed and perhaps even initiated by the people directly, can be expected to find considerably more binding force and lasting support than usual parliamentary decisions. The ability to refer to an explicit and focused consent of a majority of the governed is perhaps the most effective protection a political entrepreneur can command to ensure the viability of political investments in positive-sum reforms. In addition, direct democracy seems to be a favourable condition for creating "loyalty" of its citizens—which, as we argued above, represents a crucial resource for political entrepreneurs who invest in long-term positive-sum reforms.[33]

## 6. Political stability vs. political contestability

Our disussion of the political economy of policy reform finds its exact counterpart in Williamson's (1976) discussion of Demsetz's model of "bidding for franchise monopoly."

With the intention to strengthen the principal-agent relations and cure contractual disabilities of the licence, Williamson (1976:83f ) advocates "recurrent short-term contracts:"

> "short-term contracts facilitate adaptive, sequential decisionmaking. The requirement that contingencies be comprehensively described and appropriate adaptations to each worked out in advance are thereby avoided. Rather, the future is permitted to unfold and adaptations are introduced, at contract renewal intervals, only to those events which actually materialize. Put differently, bridges are crossed one (or a few) at a time, as specific events occur ... the adaptive, sequential decisionmaking procedure economizes greatly on bounded rationality .. Opportunism is thereby curbed as well."

The very same argument can be easily translated into a demand for shorter election "renewal intervals" if adaptive, sequential decisionmaking or the curbing of opportunism is given priority on a political agenda. Things look very different, however, if political stability and the capability to engage in long-term reforms are regarded as more problematic. Under this premise, the time to invest in the building of long and lasting "bridges" may afford long-term horizons. Exactly this argument is also acknowledged by Williamson (1976:81), who notes that "a leading reason to make the contract long term is to provide the supplier with the requisite incentives to install long-lived assets." For our model of bidding for political monopoly, this means that a fundamental trade-off between political contestability and political stability seems to exist. This trade-off can be translated into different assessments of barriers to entry in politics:

In terms of "competitive pressures," lower barriers to entry increase the contestability of the political "market" or openness of the electoral race to challengers and thus tend to

- enhance incumbents' incentives to adapt to changing preferences of voters;
- increase the chances of removing agents who are unable to fulfill past promises;
- encourage political entrepreneurs outside government to enter the arena of political discourse or the field of political action with new "combinations."

On the other side, and mainly in terms of political "market opportunity," higher barriers to entry would increase the stability of political expectations, and thus tend to

- enhance the incumbents' capability to engage in long-term planning and
- to risk reforms that could benefit a large unorganised majority in the long run, while directly and immediately hurting a small but organised minority;
- increase the citizens' (and foreigners') stability of expectations, which contributes to their willingness to invest in long-term economic ventures.

As usual with trade-offs of this kind, optima cannot be specified once and for all since this would afford knowledge of quite complex causal relations and, above all, it would force one to weigh the importance of competing values (like: adaptability and stability). Just as optimal patent lifetimes cannot generally be identified *ex ante*, so in the political realm optimal election frequencies or optimum heights of other barriers cannot be determined generally and *ex ante*. However, there is also a less ambiguous and less conditional recommendation in terms of (meta-) policy conclusions. If conditions for political entrepreneurship and reform are to be created (or analysed), it would not suffice to have recourse to our table of barriers to entry in politics. It may be even more rewarding to investigate into additional institutional arrangements that create incentives for politicians to act as courageous reformers, while still enjoying the incumbency protection which yields the capability to act with a long-term perspective. We optimistically suggest institutional competition to have such an effect: it encourages piecemeal reforms and at the same time it allows to make use of the particular learning and discovery opportunities inherent in a parallel competition within the field of competing jurisdictions. Similar benefits might be achieved with the introduction of referenda and initiatives which could impel incumbents either actively to propose or *nolens volens* to accept institutional reforms—once again on a piecemeal basis and with opportunities to make use of revealed preferences and skills focused on a particular policy.[34]

## 7. Summary

The main findings and propositions of this paper can be summarised as follows:

1) Political interactions are fundamentally different from economic market exchange. The organisation for the provision of political goods (the state) can be regarded as a natural monopoly which is based mainly on the exclusive control over means of legitimate coercion.
2) Democracy differs from other forms of government in that it provides a competitive procedure to allocate rights to the use of the monopoly of power. Models of franchise bidding can and should serve as reference models, since they capture better than others the fundamental structure of political competition.
3) The working properties of this political "competition for the field" heavily depend on legal, "innocent" and "strategic" barriers to entry in politics. These barriers not seem to have been sufficiently analysed and accounted for in economic models of political competition.
4) Barriers to entry (and change) in politics provide important conditions for political entrepreneurship. On the one side they create the necessary political stability for political and private investors to engage in long-term investments; on the other side, they drastically reduce the contestability of the political monopoly.
5) Positive-sum, long-term reforms meet two kinds of unfavourable conditions: a) unstable governments that suffer from lacking governability which may be due to inappropriatly low barriers to entry in politics; b) sclerotic governments that suffer from lacking contestability which may be due to inappropiatly high barriers.
6) In terms of (meta-)policy conclusions one can find several good arguments in favour of either higher or lower barriers depending on how one perceives present political necessities.
7) The trade-off between demands for stability and demands for contestability seems less pronounced in cases of inter-jurisdictional competition and direct democracy. Both variant expressions of political competition can be recommended as tools for reducing

the amount of incumbents' monopoly power, as procedures for the discovery and use of new political knowledge and problem-solutions, and as conditions that support political reformers.

## Notes

1. At best, some elements of Tullock's idea are implicit parts in accounts of Brennan and Buchanan (1980), North (1981), Moe (1990), Palmer (1995), Bartolini (1995) or Tietzel (1998).
2. We concentrate on those relationships that represent the core of the democratic method, namely "that institutional arrangement for arriving at political decisions in which individuals acquire the power to decide by means of a competitive struggle for the people's vote" (Schumpeter 1942, 1978:269). Thus, we do not discuss "rent-seeking competition" in the sense of Tullock (1989), competition among interest groups in the sense of Becker (1983) or "markets for regulation" in the sense of Wittman (1995). There are many elements that make these political interactions look much similar to an ongoing market process—because some form of reciprocity or give and take is obviously present. At the same time, however, many elements of incomplete contracts and barriers to entry that will be discussed here, would apply as well to the competing efforts of pressure groups.
3. For more detailed analyses, see, e.g. de Jasay (1991); Coleman (1990) or Udehn (1996).
4. It would be misleading to assume that politicians exclusively and sufficiently act as providers of those goods the market presumably fails to provide. Rather, public good-characteristics are artificially (politically) attached to goods that may as well have been provided privately. Some political goods (e.g. rents, subsidies) are even created with the intention to exclude most citizens from enjoying favours which are granted exclusively to a special interest group. Thus, we agree with de Jasay (1991:60f ): "For the present, it suffices to note that certain goods, even if they could be supplied by exchange mechanisms, are as a matter of fact provided by non-market, collective choices instead ... The goods so provided are de facto public, in the manner of the proverbial bird that waddled and quacked like a duck, and was one."
5. The individual citizen can, however, decide to "exit" the jurisdiction and hence choose among different packages of political costs and benefits. Inter-jurisdictional competition will be discussed in Section 5.
6. We do not want to conceal the fact that "the theory of natural monopoly is clearly unclear" (Demsetz 1968, 1989:77). Indeed, problems of identifying a natural monopoly in reality by using static or dynamic criteria are formidable. Fortunately, there is no need for us here to discuss such problems. We only have to compare some very basic aspects of natural monopolies with typical conditions of political competition.
7. Weber (1921, 1972:29) speaks of "Mittel legitimer (das heißt: als legitim angesehener) Gewaltsamkeit."
8. This view corroborates the "first principle of government" proposed by David Hume (1777, 1987:32): "Upon .... opinions ... of public interest, of right to power, and of right to property, are all governments founded. There are other principles, which add force to these, and determine, limit, or alter their operation; such as self-interest, fear and affection: But still we may assert, that these other principles can have no influence alone, but suppose the antecedent influence of those opinions above mentioned."
9. For a more detailed discussion of Schumpeter's notion of political competition for leadership and political entrepreneurship, see Wohlgemuth (2000) or Mitchell (1984).
10. It is a typical reaction to the problem of incomplete contracts to substitute procedural "constitutional" rules for detailed contractual commitments, see Goldberg (1976:428): "As the relational aspects of the contract become more significant, emphasis shifts from detailed specification of the terms of the agreement to a more general statement of the process of adjusting the terms of the agreement over time—the establishment, in effect, of a 'constitution' governing the ongoing relationship."
11. See also Riker (1982) or Myerson (1995:82): "plurality voting tends to create barriers to entry against third parties (because votes for those third parties could be 'wasted')."
12. In the United Kingdom, the party with an absolute majority of total votes did not reap a majority of seats in 1951 and 1971 (Roberts 1987:294). In 1983, the Liberal Party received only 3.5% of the seats with 25.4% of total votes; compare this to the Labour Party which in the same election the Labour Party transformed only a few more votes (28%) into nine times as many seats—while the Conservative Party reduced its share of votes by 1.5%-points and gained 58 additional seats! (see also Leduc 1987).

13. See von Weizsäcker (1980:71ff ) or Bain (1956, 1962:115ff ). This argument also explains why political advertising expenditures are no barrier to entry. The argument is the same as that made by Demsetz (1982, 1989a:29): "Entry by new firms might be even more difficult if such expenditures were disallowed because consumers would then be left to rely in *only* a company's history."
14. The empirical findings are ambiguous, however. Some studies of voting behaviour support a systematic incumbency advantage (e.g. Reed and Schansberg 1992; King 1991; Bernhardt and Ingberman 1985). Other studies yield stronger indications for a "cost of ruling," i.e. the depreciation of voter support during one election period (see Nannestad and Paldam 1994:235f ).
15. The theory of cognitive dissonance goes back to Boulding (1956) and Festinger (1957). Akerlof and Dickens (1982) brought it to the attention of economists and summarised the basic ideas as follows (ibid.:307): "First, persons not only have preferences over states of the world, but also over their beliefs about the state of the world, Second, persons have some control over their beliefs ... they can also manipulate their own beliefs by selecting sources of information likely to confirm 'desired' beliefs. Third, ... beliefs once chosen persist over time." Political applications are provided by Brady, Clark and Davis (1995). See also Hirschman's (1970: chap. 7) theory of unconcious loyalist behaviour as a barrier to exit.
16. Voters also find reinforcement of their own views because they tend to associate disproportionately with like-minded individuals. As a result, they often may have an exaggerated sense of the typicality of their opinions (Huckfield and Sprague 1995:46ff ).
17. Sometimes the "outsourcing" of policies can have a similar effect of removing political tasks from public debate and electoral change. The delegation of such tasks to widely independent bodies such as central banks, regulation agencies, or supra-national organisations works in this direction, when competence is a key resource and the prestige for sticking to credible commitments a key incentive.
18. Frohlich and Oppenheimer (1978:83) also report the use of patronage jobs in order to buy off competitors.
19. Many more examples of "institutional manipulation" are presented in Dunleavy and Ward (1981).
20. See Machovec (1995) for a comprehensive account of the academic and political career of the perfect competition model.
21. Fixed incumbency periods also give citizens time to make plans and invest, see Kuran (1988:144).
22. See Nannestad and Paldam (1994) for empirical indications of voters' myopia; see Williamson and Haggard (1994) for empirical cases supporting the "honeymoon hypothesis."
23. Alternatively to protecting the survival of momentary incumbents, one can directly aim at protecting particular reform projects. As we have seen, this can be done by giving the reform a higher legal status (e.g. of constitutional law), by including (parts of ) the opposition in the decision making or by entrusting bureaucracy with the execution of reform projects in a way which can hardly be reversed.
24. Effects of political (un)certainty on private investments are discussed e.g. by Dixit and Pindyck (1994). Comparative country studies also show positive relations between political stability and investment. Even the single variable "frequency of changes in government" produces good correlations (Cuckierman et al. 1992). Using multidimensional indicators for "credibility of laws, regulations and policies" Brunetti et al. (1997) also show positive relations to private investment and growth.
25. More material forms of "credit" can also have an effect. Especially conditional foreign aid can help reformers to survive initial hard times, as Sachs (1994) points out with reference to the transformation of former socialist countries and reforms in post-war Germany and Japan. Conditional aid may not only increase the rewards of market-based reforms but also lower their political costs if outside organisations (like the Worldbank or the IMF) can be used as scape-goats.
26. The original view of "competition as a discovery procedure," of course, goes back to the seminal article of Hayek (1968, 1978). diZerega, much more than Hayek himself, applies this concept to democracies.
27. More extreme cases can be found in European countries with a high amount of "concordance"-elements. In the first decades of post war Austria, both major parties built pacts to share power and frame all parliamentary decisions beforehand in joint "coalition committees." After some years of mainly socialist rule, Austria has since 1987 returned to traditional forms of grand coalitions. Even more strict and encompassing power sharing rules are typical for the Swiss systems—combined, however, with low barriers to *citizens*' entry in politics as a consequence of direct democracy (see below).
28. Viewed as a multi-stage process it is more realistic to argue that the "man with the new idea" would first have to convince his party and fraction to adopt the new ideas in a new programme or parliamentary initiative and

then convince voters to elect or (re-)elect his party. Thus, intra-organisational barriers to the introduction of novelty also have to be taken into account.

29. A less obvious way to increase potential political competition is suggested by Tullock (1965:464) who proposes "to raise the rewards of office to a level where they would be worth more than the organizational costs of an opposition group properly discounted by the risks involved." As an alternative, Tullock proposes to directly "pay a potential opposition group" (ibid.: 465). How (and by whom) such calculations and payments can be properly performed in reality is not explained.
30. The corresponding argument in the IO-literature is that "the transfer of goodwill from one product group to another reduces the entry cost for a firm which acquired goodwill in a different market. This again reduces the economies of scale effect of goodwill for any particular market and hence the corresponding potential barrier to entry" (von Weizsäcker 1980:123).
31. Frey (1994:341) reports that "among the 250 referenda held in Switzerland betwen 1848 and 1990, the majority's will deviated from the stated will of parliament in 39 percent of the cases."
32. Adamovich and Wohlgemuth (1999) discuss the virtues of direct democracy and federalism as discovery procedures and controlling devices. Referring to the Swiss case, interdependent relations between exit, voice, and loyalty are shown.
33. Empricial studies indicate a positive influence of direct democracy on citizen-loyalty (inferred, e.g., from citizens' tax-morale or their reluctance to engage in tax-arbitrage), see Frey and Bohnet (1993), Pommerehne and Weck-Hannemann (1996), Feld (1997).
34. Unfortunately, the paradigm case of Switzerland is not wholly encouraging in this respect. As Borner et al. (1994) argue, one of the greatest problems of Swiss politics is its inability to risk substantial necessary reforms. As a consequence of conservative interest groups' ability to finance and organise vetoing referenda, they argue, Switzerland has developed an all-embracing consensual and corporatistic system which produces much more inertia and sclerosis than a more competitive democracy would have done. The lower barriers to "voice" in Switzerland seems to have provoced the reaction of incumbents' cartelisation.

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