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The Big Idea Series / Democracy Under Attack

Do Democracy and Capitalism Really Need Each Other?

by Laura Amico

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Democracy and capitalism coexist in many variations around the world, each continuously reshaped by the conditions and the people forming them. Increasingly, people have deep concerns

about both. In a recent global survey, Pew found that, among respondents in 27 countries, 51% are dissatisfied with how democracy is working. Further, Millennials and Gen Zs are increasingly disinterested in capitalism, with only half of them viewing it positively in the United States.

In “The Business Case for Saving Democracy,” Rebecca Henderson argues that the failure of each system is married to the other, and that to rebuild a strong free market we are going to have to strengthen democracy. But do other observers agree?

To learn more about the complex global relationships of democracy and capitalism — and why global opinion of the two appears to be waning — Harvard Business Review, with Henderson, reached out to top economists and political scientists who study democracy, and who are from, live, or work in countries that are struggling with it. We asked them these questions: **Do democracy and capitalism need each other? Why or why not?**

Here’s how they answered.



Isabelle Ferreras

Tenured fellow of the Belgian National Science Foundation, professor at the University of Louvain, and a senior research

associate of the Labor and Worklife Program at Harvard Law School

Clearly not: Capitalism, as we can see across the globe, is compatible with all different kinds of political regimes: liberal democratic, communist, autocratic — and now illiberal

democracies, too.

Democracy is a system of government based on the recognition that people are equal “in dignity and rights” and should therefore have equal political rights. This ideal can be applied to entities of any size.

Capitalism is also a system of government, but an unequal one. It grants political rights based on capital ownership. Its core institution is the firm, which is made up of two classes of investor: capital and labor. In capitalist firms, political rights to govern are held by capital investors only, through the legal vehicle of the corporation. The only citizens that matter in the extractive logic of the capitalist firm are those who own capital — in other words, shareholders. They exercise the power and reap the bulk of the financial returns, while labor investors (i.e., workers) are disenfranchised — and the planet’s resources exhausted.

Capitalism is not naturally meant to support the free market. The market is an exchange mechanism that is legally and culturally produced and secured by the state. Its superiority in coordinating supply and demand has been proved, but it is seldom acknowledged that the market economy is compatible with both democratic and capitalist governments at the firm level.

Capitalism and democracy both need markets, not each other.

This confusion has created the illusion that democracy and capitalism go hand in hand, when, in fact, they contradict each other. Today’s political leaders (democratic or not) are scrambling to hide their powerlessness to reduce inequalities or save the planet in the face of transnational capitalist corporations. One result of this is crumbling democracies. We have a clear choice before us: either expand our democratic commitment to include corporations, through democratizing them internally (by including the representation of labor investors along the current

representation of capital investors), or forfeit our democratic rights to those who own capital — a possibility looming on the horizon, particularly in the United States.



Isabel V. Sawhill

Senior fellow in economic studies at the Brookings Institution and author of *The Forgotten Americans: An Economic Agenda for a*

Divided Nation

Capitalism and democracy absolutely need each other to survive, but right now it is democracy that is most threatened.

Capitalism is the right way to organize an economy, but it's not a good way to organize a society. Markets do a good job of allocating resources, fostering dynamism, and preserving individual choice, but they cannot solve climate change, too much inequality, or the plight of workers whose jobs have been destroyed by trade or technology. When government fails to address these or other systemic problems, democracy begins to lose its legitimacy. In desperation, citizens turn to populists on the right or the left. If these leaders then prove unable to keep their promises, trust in government erodes further. Political instability begins to threaten capitalism itself.

We are now seeing that spiral in action. Dissatisfaction with democracy in the U.S. has risen by one-third since the mid-1990s and now includes about half the population, according to the Centre for the Future of Democracy at Cambridge University. It was the white working class, whose counties had been ravaged by a loss of jobs, that elected Donald Trump in 2016. Yes, his

supporters had cultural anxieties (opposition to immigration in particular) in addition to economic ones, but there's no denying the surprisingly strong county-level correlation of votes for Trump with long-term economic distress, very low employment rates, plant closings related to trade, and the location of the opioid epidemic.

Now the U.S. is in the midst of another presidential campaign and the signposts of instability are rising on the left. If Bernie Sanders wins the Democratic nomination this year, it will be clear that it is not just the working class that is fed up but also young people and progressives, who believe the system is corrupt and that only a democratic socialist can save the day. But a Sanders revolution would almost surely disappoint his voters further, since enacting most of his proposals is politically infeasible, leading to more fraying of trust in government.

Fewer than half of 18- to 29-year-olds now support capitalism. They are right that markets without guardrails do not produce a healthy society. But a government that overreaches by trying to replace the market in areas like health care or job creation will not restore that trust. This is the balancing act we face.



Archon Fung

Winthrop Laflin

McCormack Professor of
Citizenship and Self-

Government at the John
F. Kennedy School of

Government, Harvard University

Of course they don't need each other.

Ancient Athens and the revolutionary United States were democratic but not capitalist, and China practices what some call state capitalism without democracy. To be provocative, let me pose a different question: Can democracy and capitalism coexist?

Democracy is a system of government in which people make the laws and policies together as equal citizens. But under capitalism, capitalists tend to like to make the laws and policies. The new Oxford dictionary defines capitalism as “an economic and political system in which a country’s trade and industry are controlled by private owners for profit.” That’s simply not democracy.

In societies that contain elements of both democracy and capitalism, the challenge is to maintain political equality against the economic inequality that capitalism tends to produce. Capitalist democracies with greater political equality tend to look less capitalist; I’m thinking of northern European countries with more-generous social safety protections, stronger unions to counterbalance the political power of businesses, higher tax rates, and more-egalitarian labor market and distributive policies. Indeed, those places are commonly called “social democracies” rather than capitalist democracies. And the places that are more capitalist tend to be less democratic. In the United States, for example, the political scientist Martin Gilens has shown that over many decades, numerous public policies have been very responsive to the wishes of those at the top of the income distribution but not at all to the bottom 80% of Americans.



Reetika Khera

Indian development
economist and associate
professor at the Indian

Institute of Management Ahmedabad

While neither capitalism nor democracy exist in their ideal form, especially today, what democracy promises is more appealing to me than what capitalism promises. For instance, unlike democracy, capitalism does not even strive to achieve equality.

The failings of democracy are all around us. The rise of authoritarian government in India and the revolting levels of social and economic inequality are signs of this. Too often the not-so-invisible hand of crony capitalism is apparent in this. Yet, Indian democracy — even infirm and fragile — has shown its value and provided glimpses of potential to achieve social change: Since the country's independence in 1947, life expectancy at birth has more than doubled, from 32 years in 1951 to 66 years in 2011. Another glimpse: In 2017, a nine-judge bench of the Supreme Court of India reaffirmed the right to privacy as a fundamental right, paving the way for striking down Section 377 of the Indian Penal Code, which criminalized same-sex relationships.

Similarly, the reality of capitalism is troubling. Be it car manufacturers who fudge emissions, banks that move drug money with impunity, or, in India, business tycoons who flee the country when their debtors come knocking, living by the rule of law and equality before the law do not appear to be the norm. When powerful capitalists are not violating laws, they buy influence to shape the law-making process to their advantage (e.g., by scuttling basic worker-protection initiatives) and carry out legal theft. In decades past, the sugar and tobacco industries sponsored friendly research to cover up the ill effects of their products; today we see the tech industry doing something similar, including undermining free and fair elections, the foundation of a functional democracy.

Do democracy and capitalism need each other? Capitalism needs a pretence of democracy more than democracy itself.

Increasingly, I feel that plutocracies pass themselves off as democracies. In plutocracies, capitalism is consolidating its wealth and power while maintaining a charade of democracy.



Manuel Agosin

Professor, department of economics, Faculty of Economics and Business, University of Chile, and former dean of the faculty

(2010–2018)

Capitalism can survive without democracy for a long time, as exemplified by the experiences of China, Russia, Turkey, and other authoritarian states. However, capitalism without democracy usually favors corruption and control over resources through means other than merit, such as party loyalty.

That said, in the short term, we have seen democracies being abused for personal gain in many mostly democratic countries. The many cases of mega corruption that have come to light in democratic countries in Latin America (Lava Jato, or Car Wash, in Brazil, and the Odebrecht cases all over the continent) are ample evidence of this. Even the United States has been far from impervious to the subversion of democracy by a would-be autocrat.

By emphasizing individualism and personal gain, capitalism tends to breed market concentration and a long series of abuses, as the Great Recession clearly showed. Individuals and corporations are continuously tempted to evade or to use

loopholes in the law. The financial sector is particularly prone to this type of behavior, since it allows market participants to reap gains not only by producing services that people need but also by the clever manipulation of “financial engineering.” More often than not, such creativeness produces nothing of value for society; rather, it often engenders conditions that create financial crises down the road.

This is why only a true democracy can correct the ills of capitalism, such as lack of competition and a skewed distribution of its rewards, through the use of state power. Strong democracies have checks and balances that can put a limit to what capitalism can do: courts where cases of uncompetitive markets, corruption, and subversion of democracy can be tried and punished. In fact, the maximum benefits of capitalism can be fully reaped *only* in a democratic society. And so the most pressing challenge for democratic societies is this: how to ensure that finance serves the real needs of citizens rather than lining the pockets of those who are lucky to win at the financial game.



Steven Klein

Assistant professor of political science at the University of Florida; beginning June 2020, lecturer in the

department of political economy, King's College London

The past 30 years have shown that capitalism does not need democracy to take root: In China, the introduction of capitalism has not lead to an expansion of democratic rights, and

authoritarian governments in other countries — like Hungary — have also enthusiastically embraced capitalism.

At the same time, it's clear that capitalism does need democracy to save it from itself. The financial crises in the United States and Europe show how democratic institutions have been called on to come to capitalism's rescue.

Historically, we know that democracy and capitalism can evolve together. Merchant city-states like Florence and Amsterdam had forms of representative government, and in Great Britain, the development of democracy protected the interests of the rising merchant classes against older vested interests. Yet countries like Great Britain only ever saw a partial democratization, with property qualifications to vote, and it was widely thought that universal suffrage would destroy property rights and, by extension, capitalism. Elsewhere, the eventual collapse of democracy in Europe was tied to the needs of capitalism: The German chancellor Heinrich Brüning's austerity policy of the 1930s, an effort to keep Germany on the gold standard and so part of global capitalism, helped propel the Nazis to power.

The organizing principles of democracy and capitalism differ. Democracy rests on the belief that everyone should have an equal say in decisions that affect them. Capitalism doesn't. Instead, it bases production around the profit motive and the capacity to enter and exit relationships based on opportunities. This is the heart of the tug they have on one another: Realizing an ideal of equal voice will mean limiting the ability of individuals and firms to abandon their economic and political relationships even if democratic decisions don't favor them. We know what the outcome of this tension is: Capitalists often turn to authoritarianism before they accede to a new regime of democratic checks. | **THE BIG IDEA**