Rentier Capitalism as Structural Corruption and its Impact on Development and Inequality. An *Ordoliberal* approach

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FIRST DRAFT

Abstract

The paper analyses the concept of "rentier capitalism", studies its impact in contemporary economies analyzing the variety of institutional frameworks in which "rentier capitalism" is embedded and assesses its socio-economic consequences in terms of development, instability and inequality. In the first part the notion of "rentier capitalism" is defined as pertaining to the connection between the meso- and the macro levels of analysis. The different institutional patterns that lead to rent-seeking behavior are analyzed looking at the underlying principles and mechanisms as well as at the different forms of corruption such as client-patron relationships, patrimonialism, captive markets, collusion, etc. "Rentier capitalism" is contrasted with an ideal "inclusive or productive" form of capitalism, based on the principles of "public service" and on the "sovereignty of the consumer," as that proposed by the Social Market Economy. In the second part, some comparative empirical evidence is proposed from a variety of economic system. This part will identify the institutional ideal-types in actual capitalism and the symptoms or specific malfunctioning. The third part considers that these pathologies characterize not only market-state relationships, but also intra-organizational behavior and market-to-market relationships. Therefore, "rentier capitalism" is referred to different contemporary models of economic organization, to show how the patterns of rent-seeking could be developed in economies that present a centralized and authoritarian state ("state capitalism"), and in economies which apparently appear as "free," with a minimal state. Finally, the paper considers the policy dimension dealing with how to limit the development of "rentier capitalism" patterns, as well as promoting a "productive-inclusive" society. This task will be based on the Ordoliberal economic-institutional approach, with its main concepts of "strong and limited state" and "economic constitution".

Key words: patrimonialism; crony capitalism; clientship; constitutional order.

1. Rentier capitalism today

The typical configuration of market economy plus democracy and the rule of law is presently living some regressive times, as shown by the success of many nationalist and paternalistic leaders around the world. The 2018 *Freedom House* index confirms the resurgence of authoritarianism after decades of democracy and market advancement. Since the subprime crisis (2007-08) the number of *authoritarian* or *intermediate* regimes has grown, while the number of *liberal* ones has decreased.

This tendency could be seen as a political consequence of the subprime crisis, which originated in high-income countries, led to a worldwide great recession that left a decade of instability and had severe distributional consequences. However, if this crisis has triggered some reactionary political demand, also a long term trend towards the growth of patrimonialism can be detected, which has prepared the ground to some odd development of the political economy. The result is the diffusion of the so-called *crony capitalism* and of many forms of *rentier capitalism* that are compromising the trust in open and free markets.

The collapse of the communist block in 1989 paradoxically seems to have brought also the seeds of the corruption of free market capitalism. The dissolution of this external constraint led to a relaxation of internal defenses against the degeneracy of the political economy. With the excuse of developing an institutional environment more favorable to free business, we assisted to a push towards deregulation, which in fact has often been a new regulation favorable to some powerful insider. In particular, the relaxation of institutions granting prudential financial regulation and a socially acceptable distribution of income had a relevant impact on the middle classes of the industrialized countries. The most visible consequences have been the so called financialization of the economy (the increased role of finance in the economy) and the rise of uncertainty and instability. This context has favored the diffusion of *neo-patrimonialism* as a basic relational form, often leading to its macro-outcome of *crony capitalism*. Here, we define *neo-patrimonialism* as a form of political-economic governance in which the power tends to be concentrated in the hands of a few leaders and not sufficiently subject to the rule of law, leading also to a confusion between the public and private domains.[1]

Richard Lachmann (2011) argues that the reemergence of patrimonialism in states and firms throughout the world is replacing the confident view in the progress of modernity. Patrimonial practices can be evident in the increasing financial power of Middle-East oil kingdoms or in the case of new states and privatized firms in former socialist countries, ending with the private appropriation of firms by their managers in the United States. Such practices are gaining ground in both political and economic realms. Unexpectedly, this form of exercising power is gaining legitimacy from its "'victims'.[2] The increased uncertainty, in fact, leads people to support odd political-economy practices.

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[1] This notion has been theorized prevalently in politics. Here we extend it to the economic domain. In the specific case of the business enterprise, neo-patrimonialism is the confusion of the entrepreneur and the company. This is a natural fact in small firms and can be sometimes be usefull in specific circumstances for medium-sized companies where flexibility and rapid steering is fundamental. It is here considered a dangerous pathological phenomenon for large organizations. See Eisenstadt (1972).

[2] Lachman arues that "patrimonialism is more than a set of practices for wielding power. It also is an ideological justification for the legitimacy of that power and those practices" (Lachmann, 2011: 205).

> *Patrimonialism is a powerful form of elite privilege, one that allows its holders to achieve autonomy that verges on autarky from rival elites and from non-elites. The reemergence of patrimonialism holds the potential of weakening state capacities, limiting democracy and deepening inequality.* (Lachmann, 2011: 205).

Therefore, patrimonialism may be seen as an answer to uncertainty, but it has some bad impact on political-economic institutions, weakening the rule of law and corrupting democracy, which further increases uncertainty in a perverse loop. This kind of change is normally consistent with the development of the '1% society', that is to say the concentration of wealth and, what is more worrying, of the relevant economic decision-making in the 1% of the population – totally contradicting the view of free markets of neo-liberalism. Such unequal political economy is not an odd or exceptional development of capitalism, but the normal situation when the political economy is not framed by solid institutions as the rule of law and accountability. Fukuyama (2011) looks at the weakening of the political institutional framework arguing that a

> *"common thread links many of our contemporary anxieties about the future, from authoritarian backsliding in Russia to corruption in India, to failed states in the developing world, to entrenched interest groups in contemporary American politics. It concerns the difficulties of creating and maintaining effective political institutions, governments that are simultaneously powerful, rule bound, and accountable."* Fukuyama (2011: 16).

However, there are some anthropological and cultural roots of this adverse evolution (Piattoni, 2001). The confidence in formal institutions of the political economy is a fundamental factor that helps preventing the degeneration of society into corrupted practices. Janine Wedel (2018) studied this lack of faith in formal institutions in the case of former socialist countries. She recounted how people systematically discounted official information conveyed by the state-run news media. We perceive a similar phenomenon in many Western countries which is also connected to the concentration of official information in the hands of a few financial centers.[3] The trust in institutions, including banks, churches, Congress, television news, and newspapers is falling everywhere. People tend to see themselves as outsiders. They perceive a "*division between outsiders and insiders and that the insiders are working on their own behalf, even as they purport to have the public in mind. People feel that the system is rigged against them and that they are being left on the outside, trying to get in*" Wedel (2018).[4]

The weakening of the rule of law is symbiotic to the rise of personal power. That, reinforces the tendency of people to find protection from abuse and discretionary decisions, degenerating often in clientship and patronage. When people are obliged into this system, a positive feed-back between rights degradation and patrimonialism establishes a regime shift. Roniger (2004) argues that "*the principal issue is whether clientelism and patronage affect the principles of modem constitutional democracy, for example, by sliding into what could be called systemic corruption, which cripples institutional trust and public confidence in the political system and in projects that otherwise could empower citizens*" (Roniger 2004: 367).

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[3] We refer to 'institutional trust' (confidence in institutions) and not on simple trust which is irrational and extemporary (Knack, 1999).

[4] Hot Spots, Cultural Anthropology website, April 25, 2018. https://culanth.org/fieldsights/1410-deja-vu-how-today-s-western-democracies-recall-eastern-europe-under-communism

Max Weber argued that "*public administrative organizations characterized by meritocratic recruitment and predictable long-term career rewards will be more effective at facilitating capitalist growth than other forms of state organization*" (Evans and Rauch, 1999: 749). Exposing people to arbitrary power is instead dangerous for the market economy.

Most of the case study literature on *developmental states* focuses primarily on the role state bureaucracies play in eliciting higher rates of private investment.[5] As Evans and Rauch (1999) argue, high quality of government institutions are fundamental for growth.

> *rational, risk-averse entrepreneurs will avoid making long-term investments in plant and equipment if they face a corrupt, unpredictable bureaucracy unlikely to provide complementary public investments. By the same token, shared perceptions of the state bureaucracy as dependable, predictable, minimally competent and committed to long-term growth makes investment appear less risky. (*Evans and Rauch, 1999: 752-753).

According to Rothstein and Teorell (2008), impartiality is a 'public good' defining the quality of institutions. A specific problem is that, precisely because high quality institutions are impartial, they have no obvious interest group that is their natural supporter. Interest groups may be based on economic, ideological or other orientation and strive for getting privileges and favorable regulations from political institutions. Therefore, they suffer from all "*the well-known problems of collective action in creating goods such as various forms of 'free-riding' and others sorts of opportunistic behavior*" (Rothstein and Teorell, 2008). Elionor Ostrom's cases concern relatively small local groups where the agents have known each other for a very long time and have been able to develop norms about reciprocity, trust and social capital that give birth to high quality institutions (Ostrom 1990: 35). The problem is to understand how such institutions can come about in much larger settings where one cannot assume the existence of such norms of reciprocity, social capital or interpersonal trust among the agents (Rothstein, Teorell 2008: 30-31).

Analyses of corruption have traditionally focused on illegal abuses such as bribery and misuse of public funds. However, in recent years increasing academic attention has been paid to the notion of *legal corruption*, as developed by Kaufmann and Vicente (2011).[6] *Legal corruption* involves the *abuse of office for private gain* that is central to traditional notions of corruption, but where the 'abuse' is able to take place legally due to its perpetrators possessing political and legal control. Once this legal corruption was closely bound up with a titled aristocracy (Bailey et al., 2018: 359). Today, it is more frequently related to new forms of patrimonialism.

This arrangement of the political economy has consequences for what concerns corporations and their concentration. Corporations have some natural incentive to become politically connected. Therefore, large influential companies tend to acquire the role of interest groups in the standard theory of rent seeking and distributive coalitions (Tollison, 1982; Olson, 1965; 1982). There are many forms and targets of this influence. According to Mara Faccio (2006: 369) the preferential treatment of government owned enterprises (such as banks or raw material producers) is the most evident case. A common standard is the demand for lighter taxation. However, also the preferential treatment in competition for government contracts and relaxed regulatory

[5] E.g., Amsden (1989); Evans (1996); Johnson 1982; Wade (1990); World Bank (1993).
[6] See also Aidt (2003).

oversight of the company in question are relevant cases. Finally, the search for stiffer regulatory oversight of company's rivals, usually foreign competitors, is also often observable.

This situation is likely to show some stable pattern given by the circular causation instaurating a feedback between advantages gained by companies and the weaknesses of the institutional environment. More specifically, 'State agency capture' and the use of the state for privileges (Neo-patrimonialism) reinforce private company power and profits. At the same time, the weakness of the antitrust policy tends to increase economic concentration, which feeds corruption and institutional discredit. This synergetic perverse dynamics is opposed to 'inclusive or productive' capitalism, where competition is not distorted, granting standard constitutional freedoms. Therefore, economic arrangements have political consequences. Economic actors, when too big or having a dominant position, on the one hand, limit individual economic freedom, on the other hand, shape the agenda and the process of political decision making. In some cases, too powerful private actors may also affect the judiciary power, deeply distortng the rule of law.

In the next section, empirical identification of rentism is discussed. Which are the relations between the characteristics of rentier capitalism with the patterns of "structural" (public-private) corruption and how can be detected are questions discussed in the second section. In the third, the theoretical background of rentism and the meso-macro connection are analyzed. Subsequently, the consequences of patrimonialism for the political institutions are discussed in detail taking the theory of *Ordoliberalism* as a reference to introduce the concepts of "strong and limited state" and "economic constitution" that help to identify the neo-patrimonal organization of the state and the role of private power through economic concentration as bi-directional roots of "rentier capitalism". Some reflection on concentration and centralization is supplied in section five and further developed in relationship with the state in the sixth. Finally, the paper discusses how the patterns of a rentier capitalism could be related or originated both in economies that present a centralized and authoritarian state ("state capitalism"), and in economies which apparently appear as 'free' with a minimal state ('nightwatchman') and a self-regulated conception of the market. The conclusion supplies some reflections on which is the socio-economic impact in terms of economic development of each system (rentier vs productive/inclusive) and how it is possible to deter or limit the development of "rentier capitalism" institutions and patterns, as well as promoting 'productive/inclusive' ones.

2. The identification of rentier capitalism

The institutions that a society develops to coordinate economic interactions are factors that decisively influence economic success and the quality of life of citizens. Poor institutions constitute incentives for different interest groups to engage in redistributive activities resulting in a net transfer of benefits (consisting in both income and power) towards specific individuals, with a net decrease of general well-being. In contrast, institutions promoting productive activities able to produce new wealth and reducing concentrated power are desirable. But the identification of desirable institutions is not easy, as well as their connection with growth is not straightforward.

Mancur Olson (1965; 1982) wrote some classic work in this field arguing that fragmented interest groups and conflict are likely to produce odd institutions (distributive coalitions) relenting growth. Angus Madison (1988) has criticized this too

strict connection between institutions and growth, as other relevant factors, as the distance from the technology frontier and the availability and use of factors of production make the interaction more complex.

Douglass North (1990) has underlined that the profit maximization of firms, that should lead to investments in the skills and knowledge of labor, could easily be turned into a 'rent-seeking' strategy, where investments could be made to change institutions in a favorable way, if institutions allow these opportunities. Therefore, the adequate design of institutions is considered fundamental.

In the well-known book by Acemoglu and Robinson, *Why Nations Fail?* (2012) the authors propose a central distinction between *extractive* political-economic institutions versus *inclusive* institutions. The extractive political institutions would be characterized by the existence of a monopoly of the political power of the elites in the control of the government and the lack of competition and circulation in which they take charge of it. This would result in the 'capture' of the government by private interests that would be able to generate extractive economic institutions, consisting of the extraction of rents (distributed to these elites). On the contrary, inclusive political institutions are characterized by a wide open access to government and pluralistic influence on political decisions, the existence of checks and balances and the rule of law. In this case, what is expected is the development of inclusive economic institutions, which are based on the defense of property rights, the existence of competitive markets, and non-discriminatory access to public goods and services that would generate a certain "levelling of the field of the game" (Acemoglu and Robinson, 2012).

The peculiar aspect of this view is that it excludes corruption, which involves some infringement of the law as bribery and misuse of public funds. However, in recent years some attention has been paid to the notion of 'legal corruption', as developed by Kaufmann and Vicente (2011). 'Legal corruption' means the 'abuse of office for private gain', where the term 'abuse' is not referred to formal legal practices, but points at ideal (rational) forms of economic interaction. In fact, actors perform these corrupted practices legally, because the perpetrators possess political and legal control of the procedures (Bailey et al., 2018: 359). At this point, the term 'corruption' denotes a reference to an ideal legal structure, the rule of law of the liberal state, and not to actual laws and governmental actions. The focus is therefore shifted to the distance between an ideal legal framework and the actual configuration. In this sense we talk of *quality of institutions* (Rothstein and Teorell, 2008). Rothstein and Teorell, (2008) underline the property of *impartiality* of an institution as the fundamental characteristic of 'quality'. This quality is surely not enough, but it is relevant for the analysis of patrimonialism.

Crony capitalism is relatively easy to identify but difficult to measure with precision. *The Economist* has focussed on the concentration of wealth among billionaires operating in heavily regulated industries.[7] This simple indicator is justified by the

[7] The Economist's crony-capitalism index, May 7th 2016. This index builds on work by Ruchir Sharma of Morgan Stanley Investment Management and Aditi Gandhi and Michael Walton of Delhi's Centre for Policy Research, among others. It uses data on billionaires' fortunes from rankings by Forbes. We label each billionaire as a crony or not, based on the industry in which he is most active. We compare countries' total crony wealth to GDP. We show results for 22 economies: the five largest rich ones, the ten biggest emerging ones for which reliable data are available and a selection of other countries where cronyism is a problem (see chart 3). The index does not attempt to capture petty graft, for example bribes for expediting forms or avoiding traffic penalties, which is endemic in many countries. The rich world has lots of billionaires but

assumption that the higher is concentration of wealth, the more intense are likely to be the rent seeking activities, the greater the dimension of crony capitalism. An alternative approach is suggested by Pei (2016: 12-13) and consists of using data from corruption involving officials and businessmen. However, the acts of collusion that constitute crony capitalism are concealed from public view. If the system is stable 'corruption is legal' and no evidence can be traced (apart from some infrequent independent investigation of journalists). Therefore, the empirical evidence based on judiciary acts reveals only a minor part of these phenomena, notably those undergoing in regimes exposed to conflict or political change. The empirical approach consequently has its limitations.

The logics of the 'crony index' is based on the presupposition that some industries are prone to rent seeking. The term rent points to an extra-profit going to the owner of an input of production so that such factor extracts more profit than it would under a competitive market. Cartels, monopolies and lobbying activities are common ways to produce a context favorable to extracting rents. Industries that are vulnerable are those undergoing frequent interaction with public authorities, notably those which enjoy some license: for example network services, the extraction of natural resources, real estate, constructions and defense.

3. Crony capitalism and rent-seeking: theoretical background

The central characteristics of 'rentier' capitalism are the taming of competition and the seeking of specific privileges (such as rigging bids, capturing regulators, creating or sustaining monopolies with abuse of dominant position, development of collusive agreements or cartels within oligopolistic markets, etc). A fundamental element of the administration of the state in a 'rentier' regime is *neo-patrimonialism*, that in this case we define as the *informal use of public agencies for private benefit* (whether there is no formal framework that regulates the actions of the state, or that this framework exists, but is intentionally avoided by informal practices). This *neo-patrimonialism* affects also private organizations when managers or some relevant shareholder uses the company for his own interests. This can become a diffuse culture of management in all kind of organizations.

In Neo-patrimonialism individuals exercise an administrative power, born out of a public or specific delegation, as if such position of power would be a private property. Instead of serving the general interest of the organization they belong, they surrender to particularistic demands in exchange of some benefit. In the case of civil servants, they distribute divisible benefits, public resources such as public contracts, administrative jobs, state aid, investments in local infrastructure, etc., in a restricted, arbitrary and secret way, to individuals or particular groups in exchange for subordination and political support.[8] In the case of private organizations, corrupted individuals obtain private benefits from suppliers or clients damaging the patrimonial position of the organization and its efficiency. This is the penetration of the market

fewer cronies. Only 14% of billionaire wealth is from rent-heavy industries… if we lumped in hedge-fund billionaires and other financiers, too, the share of American billionaire wealth from crony industries would rise from 14% to 28%... Developing economies account for 43% of global GDP but 65% of crony wealth. The final reason for vigilance is technology. In this index they assume that the industry is relatively free of government involvement, and thus less susceptible to rent-seeking. But that assumption is being tested…

[8] See Lachmann (2011) and Van Gool and Beekers (2010).

logics into organizations based on law or rules, transforming a legal position into a marketable good.

Crony capitalism presents a configuration of specific political-economic relations. In particular, entrepreneurs 'need' the state to obtain privileges useful to extract benefits and, often, to smooth competition in their sector. On the other hand, politicians or civil servants 'need' friendly entrepreneurs in order to 'monetize' and appropriate the economic value of their power position (defined as effective corruption). Generally, this operation requires the complicity of medias, other public managers, NGOs, and particularly that of the judiciary and executive powers. This complicity usually takes the form of a network of relationships, assuming the form of a distributive coalition (Olson, 1965) when some coordination exists, or of a diffuse, uncoordinated and fragmented 'marketization' of the state bureaucracy. The whole system assumes the form of a *dysfunctional corporatism*, which benefits the élite (of those having a prominent position in the political economy) against the population. It may defined *corporatism* as it involves a strict coordination of social bodies in the public and private sphere. It is obviously *dysfunctional* as this coordination is not geared to overcome some obstacle to economic development (e.g. approaching the technological frontier, as in Madison, 1983) or some critical social problem, but simply oriented at reproducing an élite with unjustified high income. The result, from a purely economical perspective, is reduced efficiency for the whole economy and a distorted structure of prices. However, social inclusion and social integration are limited, as some effective barrier is built to limit and select the ruling élite. The logics of decision-making is in this way widely corrupted, generating an adaptive behavior that stabilizes the system.

Finally, this arrangement of society corrupts the whole democratic political-economic system. 'Rentier' capitalism has therefore relevant and persistent repercussions on equality. The performance-based justice of competitive markets indicates that the greatest benefit should go to the bidder that generates the best value proposition for consumers, taking into account that there is a certain equality of opportunities. The imperfections of markets (limited information) imply that firms develop some relational capabilities to reach and capture clients. This activity has positive social outcomes up to a certain point (that beyond which it limits competition). However, such relational competences have in any case perverse social outcomes when addressed towards the regulators or to administrative officials. In presence of a predominant rent-seeking, or *extractive institutions*, *privileges* are formed based on a different kind of performance, which is not transformed in the general well-being of the population. Therefore, in this context, individuals have incentive to invest in different skills and develop competences that are not so valuable from the viewpoint of society. This clashes with the bases of the republican system of government and democracy that was developed in modernity under the principle of *civil equality*, of *equality of rights* and therefore of *equality before the law*.

Concluding, the development of 'Rentier Capitalism,' and the consequent institutional discredit, is based on the synergy of two fundamental legal-economic factors: a) the capture of public administrative or legislating bodies for specific privileges; b) the taming of competition by specific structuring of the legal frameworks of markets. The result is a distortion of the economic space in favor of some specific interest. This distortion has been theorized as sometimes useful for specific developmental policies, but it can become a cancer for civil society and the open economy.

In order to develop further our argument we will distinguish at least two main configurations or models of rentier capitalism: one based on exclusion by a compact

self-limited élite (what we call *Booty capitalism* reinterpreting Hutchcroft, 1994) and the other based on diffuse patron-client relationships, deeply corrupting society at any level (*State capitalism*, following Bremmer 2009).

4. Neo-patrimonialism relaying on patron-client relationships

We have seen how n*eo-patrimonialism* is a form of socio-economic organization in which relations of a patrimonial type prevail in a political and administrative system that is formally built on the basis of rational-legal guidelines. This can be inserted in a simple case of self-contained élite practicing 'legal corruption' but it could also be the apical part of widespread dysfunctional social relationships. A quite diffuse socio-economic interaction practice, usually characterizing less developed regions (but not exclusively), is the *patron-client* relationship.

Patronage or clientship, if seen from the bottom-up, refer to a type of social structure in which vertical ties are formed between individuals of unequal power and socio-economic status in order to obtain mutual benefits through some kind of multi-dimensional and relational exchange. It implies mediated and selective access to resources from which others are excluded. This access is conditioned by subordination, compliance or dependence to the rationing individual. Patron-client ties derive their legitimacy from the voluntary nature of entry, as well as from the expectations of reciprocity in the exchange of goods and services. However, the relationship is essentially asymmetric in its structure and in its results. The client 'buys' protection and access to resources, but renounces to his autonomy as a citizen by recognizing the master in a position of dominant authority and offering his loyalty and services. The patron-client relationships constitutes a way of organizing crucial questions of the institutional order: a) power relations and their social legitimacy, and b) the structure and flow of resources (distribution of wealth and income).[9]

This specific pathological form of interaction develops in situations of high uncertainty. The latter can be caused by the underdevelopment of markets, but often, it is caused by administrative discretionary behavior. From a micro-economic perspective, when people action plans are heavily exposed to administrative decisions or to the predatory action of some powerful private actor (think of mafias), they may decide to increase the probability of success of their action strategies by affiliating, promising loyalty, to a *patron*. The patron should be so powerful to give a certain order to the allocation of resources or to 'adjust' market economic interactions thanks to a variety of means, from charismatic authority to violence. The patron should be also able to affect administrative behavior affiliating politicians or public managers into his network.

From the point of view of the client, the benefits of affiliation overcome the costs of the lost freedom. Often, benefits are material, while costs are not immediately visible or monetarily cheap. This exchange is convenient when there are a lot of resources to be rationed, but the mechanism works well mainly because of the artificial creation of uncertainty and to the artificially rationing of resources. This is normally due to the corrupted environment, but this form of interaction may become normal and legitimate

[9] See Günay (2008), Eisenstadt (1972), Eisenstadt and Roniger (1980), Roniger (2004), Resico (2015).

in the view of individuals by habituation, reducing the administrative costs for the patron.[10]

Therefore, client exchange may be voluntary and consented as market exchange even if subject to habituation. Client and patron enjoy mutual benefit, but the patron is often artificially increasing uncertainty for the client, so to rise the costs of non-affiliation. The scheme is totally informal and asymmetrical and the individual evaluation is affected by the fear of retaliation. The content of the exchange is open and often concerns some discretionary or illegal action. It also is thick in the sense that it involves personal relations and duration, sometimes irreversibility. The exchange is also characterized by functional flexibility (resources, access, loyalty, votes, support, etc.). The exclusivity of this tie generates a form of privilege, or at least, the client is induced to think so. On the contrary, free market contractual exchange tend to involve more equality, specificity, non personality of spot relationships and free the partners after the conclusion of the exchange. The market exchange is normally producing inclusive social relations (although it depends on a variety of factors) while the clientship-based exchange reproduces a hierarchical society (Günay Sevgi, 2008).

As concerns rentier capitalism, when administrative relationships fall under the patron-client relationship instead of the rational-legal case of formal subordination to a superior, the legislative and executive powers of the state may fall under the influence of external patrons. That may be due to personal connections in contexts of low institutional trust, but could also be systematic intrusions of special external interests (Resico 2015: 60-75). In some cases, the whole political parties may be part of some client affiliation (Piattoni, 2001). Clientship and patronage serve in this way as a rent seeking strategy of private interests. In this way, neo-patrimonialism is directed from outside the public administration.

5. Business concentration and centralization

A society based on patron-client relationships is reinforcing some 'dominating relations' that 'genuine' market does not. Wilhelm Röpke argued that the

> *"market and power do not go well together, and anyone who wished to use his strong position vis-it-vis some buyer or seller to establish a dominating relationship of more than transitory duration would find it difficult to do so unless he could count on government support. As long as there exists a genuine market, economic power will remain precarious, and co-ordination will not easily be transformed into subordination. On the other hand, it is one of the most damning things to be held against collectivism in any shape or form that, with the exception only of the few who hold the power to plan and direct, it presses men inescapably into vertical and personal relations of subordination and so robs them of freedom"* (Röpke, 1944: 237-238).

We are not pointing at a specific causality between rentism, neo-patrimonialism and clientship, however, if uncontrasted, these phenomena tend to consolidate some unitary model of crony capitalism that is difficult to extirpate.

In the last two decades, more than 75% of US industries experienced an increase in concentration levels, with the Herfindahl index increasing by more than 50% on average. During this time, the size of the average publicly listed company in the United States tripled in market capitalization: from $1.2 billion to $3.7 billion in 2016 dollars (Grullon, Larkin, and Michaely 2019; Craig et al. 2018). This phenomenon is the result

[10] This is when people have no confidence in any alternative arrangement.

of two trends: On the one hand, the reduction in the rate of birth of new firms, which went from 14% of existing firms in the late 1980s to less than 10% in 2014 (Decker et al. 2016); on the other hand, a very high level of merger and acquisition activity, which for many years in the last two decades exceeded $2 trillion in value per year.[11] (Zingales 2017: 113-130).

Luigi Zingales has noted that in the last three decades in the United States,

> *"the power of corporations to shape the rules of the game has become stronger for three main reasons: First, the size and market share of companies has increased, which reduces the competition across conflicting interests in the same sector and makes corporations powerful vis-à-vis consumers' interest. Second, the size and complexity of regulation has increased, which makes it easier for vested interests to tilt the playing field to their advantage. Finally, there has been a demise of the antibusiness ideology that previously prevailed among Democrats, and this has reduced the costs of being perceived as too friendly to the interests of big business for both parties"* (Luigi Zingales, 2017: 124-125).

We may add that, in the case of the new rapidly growing internet companies, the operation domain of these organizations has been international (the web, which is not related to a territory, but is a specific space), only in part affected by U.S. regulation. These companies have rapidly acquired some global monopoly power thanks to both the acquisition of competitors and the lock-in effect of consumers' socialization and habituation into these technologies. Such companies have always taken advantage of the absence of specific regulation and have always considered existing national rules as 'relative', doing some rule shopping, that is to say, deciding witch country legislation they would follow and for which matter. On the other hand, they have contributed to shape standards and to define new forms of property rights in their field, taking advantage of this privilege.

As a consequence, there is an increasing danger of states' capture from these large organizations. Jan Tulmir (1989) affirmed that in these circumstances the narrow focus on the problems of private economic power constitutes a severe limitation of the analysis.

> *"Not only is the power of the state much greater and more dangerous than any feasible accumulation of private economic power, in any practical context the two are difficult to distinguish. Franz Böhm, Ernst Mestmäcker and Wernhard Möschel repeatedly point out that economic power, as it grows, will be increasingly able to direct political power into its ends. What deserves at least equal emphasis is the fact, or the strong presumption, that already in its emergence, private economic power depends on public, political power"* (Tulmir, 1989: 138).

The Ordo-liberal view, which is a well-developed theory of economic institutions, emphasized competition policy to avoid this progressive capture of the state by big business. Möschel Wernhard (1989) noted that in such perspective a structural parallel exist between the political constitution on the one hand and free trade on the other. The common point is the problem of limiting power. As the first task of a political constitution is to tie governmental power to the law, similarly the first task of an economic constitution is to solve the problem of private economic power. Some legal principles must be developed with respect to the acquisition and exercise of private economic power in a way that it remains consistent with the fair functioning of the economic system.

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[11] Institute for Mergers, Acquisitions & Alliances, at https://imaa-institute.org/mergers-and-acquisitions-statistics/

> *"Holders of economic power jeopardize the economic legitimization of free trade if they make use of the competence of individual planning in order to eliminate the price system; they destroy the basis of private autonomy if they replace freely negotiated contracts with a unilateral act of will…"* (Wernhard, 1989: 151-52).

The idea of Ordo-liberalism is therefore that the state and business should remain separated. Moreover, the size of corporations is to remain limited to the point that they have no political influence. Anti-trust activity had to grant the latter point. The political-economic constitution had to establish the former. On the other hand, Ordo-liberalism has said little specifically of the cases in which crony capitalism is well installed and patron-client relationships have devastated the civil society (Banfield, 1958).

6. State-business relations and economic systems

Standard economic theory, consistent with the neoclassical thought (or 'Washington consensus', as it was called when transforming into economic policy orientations) tended to assume the institutional framework as given, not only in its theoretical approach, but also in its economic policy recommendations, leading to relevant policy mistakes.[12] At the same time, and aiming to repair this flaw, the *New Economy of the Institutions* was developed with contributions from the history of economics by, among others, Douglas North (1990) to study the role of both formal and informal institutions. More recently, Acemoglu and Robinson (2012) distinguished between *inclusive* and *extractive* institutions. These instruments allow a first approach the issue of the *quality of institutions*. However, as a way of proceeding, outlining some ideal-type configuration of capitalism is useful, following the way of Walter Eucken (1950).

Current economic systems can be divided in four categories according the relationship between the state and the relevant private groups. In the first two cases, the state operates in a neo-patrimonial way favoring the extraction of resources. The first case is mentioned by Ian Bremmer (2009) with his concept of *state capitalism*[13] and points at situations in which the state controls key production sectors or co-opts entrepreneurs of the existing ones (broadly the cases of China and Russia). The second is *booty capitalism* (Hutchcroft, 1994) in which private groups 'capture' public agencies. This may evolve through concentration and inequality in laissez-faire economies, in cases where a self-regulated market economy is assumed to work (note that this system can coexist with different categories usually used as the 'free market' or the 'regulated market', which lose their explanatory capacity from our point of view). In the first case of neo-patrimonialism, the state co-opts the semi-private groups and in the second, private groups coopts the state, but in both the results are sub-optimal configurations of *crony capitalism*.

[12] It also tends to conceive economic policy as a too strict consequence of theoretical activity (Colander and Freedman, 2019).

[13] The conceptualization of *state capitalism* was first discussed by Rudolf Hilferding in 1940 much in a similar way.

Tab.1 Synoptical scheme of models of state-economy configurations

Model of capitalism	Polit.-economic governance	Function	Power
State capitalism	patrimonialism	rentism	the state
Booty capitalism	patrimonialism	Rentism + clientship	tycoons
Developmental state	strong state	market enhancing	élites
Social market economy	rule of law	market preserving	balanced

On the other hand, there are two other types of capitalism, both defined by an impartial bureaucracy acting autonomously form private interests according to the principle of legality. In the first, the state acts in connection or interrelation with competitive economic sectors in order to support growth or overcome obstacles to development and is defined as the *developmental state* (Evans, 1995) expressing a *market enhancing* role (Aoki et al., 1997). In this model, the state encourages certain sectors to increase their productivity and become competitive, by providing them with the appropriate framework for their operation. In Aoki et al. (1997) the state accords some contingent rents in specific sectors to attract investments and improve productivity. This *developmental state* works well when the development path is already traced and the country is trying to catch-up with leading economies. In the second model there is more balance between state and market and we are in the presence of developed market economies that operate within a framework of the rule of law, enforced by a strong and limited state. This is the case of the *Social Market Economies*.

Both *rentier capitalism* is characterized by an institutional framework rooted in neo-patrimonialism (the first two cases above). This model is characterized by the accumulation of economic and political power, although formally remaining a market economy (or better a pseudo-market), in practice we assist to the existence of privileges, increasing inequality, and prevailing 'law of the jungle' in the political and economic social field. That is, individuals having more power or connections with patrons have the greatest advantages.

On the other hand, we have taken as a reference the *Social Market Economy*, where the institutional framework is characterized by an 'impartial' state, that is to say, a "strong although limited" state. In this case, the 'rule of law' is guaranteed so that citizens are 'equal before the law' and in the market, which is the condition for the existence of genuine social justice. The result of each individual is then due to 'merit', maybe to some good luck, but not to privilege. Equality before the law is a necessary condition to effective *rule of law*, it also guarantees the 'dignity of the human person', with each of its attributes. In the case of the Developmental State – and we add in the Social Market Economy – Evans (1995) talks of *embedded autonomy*, that is, a political configuration characterized by a strong and impartial state that has multiple proactive links with the economy and society. Likewise, it is based on the existence of a competitive market economy, an adequate institutional framework and a reinforcement of the primary distribution to reach an equitable socialization of economic growth.

In the *Social Market Economy* growth and distribution are shared objectives in the private sector. The public sector must regulate sensible sectors and provide public services. The tendency to market self-regulation needs to be reinforced by the explicit

institutional framework. The State should keep the political leadership in the economy to achieve a good regulation and guaranteeing equality of opportunities. The bureaucracy is of Weberian kind. All that assures the *embedded autonomy* (Evans 1995).

From a historical perspective, the patron-client relationship has characterized traditional economies since ever (the feudal system being an expression of this organization). Given its culturally sedimented properties, it has been a bond to be broken by modern political economies, but this development often failed and often we find hybridized systems with 'extractive economies' trying to 'modernize their state and markets but only formally or superficially. Either because the process is partial, truncated or simply it finds no legitimacy due to an inadequate middle class, unable to abandon the umbrella of clientship in presence of very strong powerful actors. Typical examples are the so called developing countries, in particular those that underwent the process of decolonization.

A second group of countries clearly maintaining characteristics of a *rentier capitalism* are those that, having been 'Planned economies' on the orbit of communism, underwent a liberalization process, which did not end in well-functioning market economies with democratic political systems, but which carried out a partial or deficient, pragmatic-authoritarian liberalization that led to systems with several of the characteristics of what Ian Bremmer has called *state capitalism* (Bremmer 2009). The main examples are Russia and China. Some of these countries have simply fell in the hands of a few insiders that drove privatizations and restructuring but have been prey of systemic corruption.

Finally, in a third historical group we can include market economies excessively dominated by *laissez-faire*, in which a disequilibrating liberalization process has been carried out with neglect of the relevance of the impartial institutional framework, with negative consequences on 'equality before law' and on inequality. In these countries the concentration of wealth and income tends to increase, together with the influence on the economic and political power that it implies, where the 'privileges' achieved reinforce unequal results. In these systems, the progressive development of a neo-patrimonialist logic that deteriorates both the principle of 'equality before the law' and the 'rule of law' can rapidly worsen their position. That is, there is a gap between the formal and declared rule of law so that real practices in the governmental and judicial process do not produce the results of a real and effective 'rule of law'. This may be the case of the U.S. in the last thirty years.

7. The strong and limited state of *non-rentist* capitalism

A *non-rentist* economy, which is not oppressed by inherited inequality, could be an *inclusive* economy. The political economy should be a virtuous mix of cooperation and competition where there is no domination of an actor over the others. We have pointed out the two main historical alternatives:

1. 'Developmentalism', that means the creation of a competitive business class through an autonomous state. This has been the case of Japan and 'Asian tigers', may be of France, even if some negative drawback is evident as in the case of the Japanese high public debt.
2. Private groups gain independence from the state but respect the state's regulatory functioning and its necessary autonomy. The law keeps the economy in a state of fair market competition. We do not find so many cases in history: Britain at the times of the *Glorious Revolution*, post Second World War Germany (with some external aid

from the U.S.), Scandinavian countries, some brilliant small open economy as Austria or Switzerland.

In both cases, we found, consistent with the ordoliberal conception, the key function of a *strong and limited state*.

In this concept, strength is understood in the sense of the legitimacy of origin and exercise of force, that is the 'moral' sense of strength. For this reason, in this system the factual concentration of power, of resources or functions is adversed, rather, the guarantee of independence from the influences of particular interest groups is pursued. This independence is what allows this type of state to act with the objective of achieving the feasible common good or public interest. The category of Weberian 'rational-legal' state, implies that access to the administration is based on merit criteria and impartiality. For this reason it is an adequate foundation of the 'rule of law', able of acting in a manner consistent with the principle of 'equality before the law'. For this reason, it can promote equal rights and opportunities in the economy and society. We could also describe it as a state in which there is the presence of an 'embedded autonomy' (Peter Evans 1995), that is to say that the independence and autonomy from pressure groups is assured, but at the same time the health of society is granted by systematically detecting substantive needs and contributing to their satisfaction. This type of state is the one that has been considered necessary for the functioning of the *Social Market Economy*. The existence of this type of state requires, of course, internal support from politicians and state officials, but also external support from interest groups and public opinion, particularly a low level of social conflict and a high level of agreement and compliance on rules.

On the contrary, in a country in which *patron-client* governance dominates autonomy, conditions become favorable for the *neo-patrimonial* accumulation of power and resources. In that situation, it becomes difficult to maintain rational-legal logics in administrative structures that grant social rights and a variety of life opportunities.

The connotation of *limited state* is understood in a classical sense. Limited by law, that is to say by the Constitution, the existence of an effective division of powers, checks and balances, etc. *Strength* is understood in the sense of legitimacy 'of origin' and 'of exercise'. It is not a strong state because of the concentration of power, resources or functions, but because of the guarantee of relative independence from the pressures of particular interest groups. This last characteristic is what makes it possible to act in the direction of the public interest or common good. In this sense, the state must not be captured by any specific pressure group (Streit, Wohlgemuth, 2000).[14] At the same time, the market should not be bent to achieve results that it is not able to deliver, as public goods (Nik-Khahand Mirowski, 2019).

In the Weberian view, public-administrative organizations characterized by meritocratic recruitment and predictable, long-term career rewards are more effective obtaining economic growth (Evans and Rauch, 1999: 749). Such organization helps the private division of labor by reducing the uncertainty of individual legal-economic positions, which foster investment plans.

Wilhelm Röpke wrote relevant pages on this subject.

> *"Menawhile where it is a matter of freedom and the retention of one´s personality we require counterweights not only against the state but also weights to counterbalance the forces of private pressure groups. Thus the danger threatens not only from collectivism but likewise from other development which is rendering the individual in his economic existence dependent upon*

[14] Particularly the Finance-Media sectors, but also the Agro-Industry, trade unions or social movements, drug trafficking, etc. are critical in many countries.

powerful groups of that kind. His Independence jeopardized by proletarianisation, by concentration of private economic power, by increasing organization and monopoly, by cartels and associations, by agglomerations of financial interests, by corporativism, by the private planning economy of vested interests, in short by "business collectivism," where the farmer is no longer a free individual since he is dependent upon the cogwheels of his organization, neither is the doctor nor the politician nor whosoever it may be. This is a state of affairs which fully corresponds to the feudalism of the Middle Ages. It amounts to an authoritarian decentralization and the parallel is so complete that the old baronial courts have their analogy in the private courts of modern economic organisations… so the private collectivism of the present day, if it is not revised, is but a step to state collectivism." (Röpke 1944: 113-114).

Wilhelm Röpke insisted also on the notion of *centralization* as opposed to the decentralized system of decision making typical of a market economy. Röpke referred to the notion of centralization in a way similar to Hilferding, that is to say, the concentrtion of economic decision-making in a few hands due to the concentration of the economy into large organizations. He feared the social costs from centralization of economic activities (Röpke 1944: 174), not only due to information problems but to the impairment of decision-making and social life. He also warried the political consequences of such concentrated economic decision-making.

Peter Evans (2011) argued that capable public bureaucracies are more important than they are commonly thought to be, particularly by liberal and conservative scholars. Relevant public services, that are fundamental inputs of production that serve as capability-expanding for private actors cannot be delivered without a competent, coherent public bureaucracy, public services will not be delivered. The ability of the state to identify and pursue collective goals coherently, rather than responding to the subjectively defined immediate demands of individual members of the élite or pressure groups is essential. Evans (2011) defines 'Embeddedness' as the dense sets of interactive ties that connect the apparatus of the state, administrative and political, to civil society. This property is important and must be focussed on a broad cross-section of civil society rather than simply on business elites. Finally, the problem of state effectiveness is a political problem that has the state-economy relationships at its heart (Evans, 2011: 9-10). Any effective reform of public administration should begin by a severance from pressure groups and by the selection of high quality public managers.

8. Conclusion: The unlikely optimal path of unregulated capitalism

The present study is not framed in the *Public Choice* perspective, but ought much to the political economy of Buchanan and Tullok (1962) on pressure groups.[15] We are always in presence of both market and government failures. The problem discussed here is how they match to form a more or less viable regime of growth and distribution. A desirable regime is not such for simply the rates of GDP growth or per capita income. Constitutional republican values, comprehending inclusion, are important factors of well-being in themselves and the best predictors of long run sustainability. No strict inverse relationship neo-patrimonialism and growth can be theorized, as the ways of obtaining growth are manyfold, including oil extraction, the reliance on slavery of simply a favorable context. But in the long run, the lack of cultural change (out of client-

[15] Interestingly Ciampini (2018 p.238) states an influence and quotation from Buchanan of a paper by W. Röpke (Röpke 1959) focused in the workings of pressure groups over economic policy and state structure.

patron relationships) or the falling back into it are fundamental for the regression of modern economies based on equality before the law and democracy.

We have proposed a simple taxonomy of political economy regimes according to their historical generation and to the level of civil autonomy. We have argued that the risk of falling bak into a rentier capitalism is always present into our societies. At the same time, it is very hard to get out of a context dominated by both patrimonialism and clientship. The circularity of causation between political-bureaucratic corruption and civic corruption is a very dangerous situation. Only big coalitions, often moulded by deep crisis and grievous events, may help breaking this vicious circle.

The state-market dispute as the best governance mechanisms is an odd theoretical debate that has confused deep issues at stake. The issue is studying the best form and role of the state in the political economy, according to the specific cultural context. It is of a fundamental importance paying particular attention at the destabilizing loops of some kind of intervention that alter the structure of state-economy match building the fundamental mechanisms that drive the political economy into a path of social regression. Cultural policing is fundamental to assure that republican values hold firmly into society. One of the worst mistakes performed in Western societies by public authorities is the renunciation to the civilizing role of institutions, the progressive betterment of civil society education to a progressive autonomy, mutual respect and cooperation to the common good.

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