

THE ECONOMIC COSTS OF PARLIAMENTARY POPULISM: EVIDENCE FROM EUROPEAN REGIONS

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ABSTRACT

Populist parties now hold parliamentary seats in nearly all EU member states; however, their economic impact remains underexplored. While existing research focuses on populist executives, we examine whether populist parliamentary presence affects regional economic performance. Using a panel of 239 European NUTS 2 regions (1996 – 2022) and System GMM estimators to address endogeneity, we find that a permanent 1 percentage point increase in populist vote share reduces GDP per capita by 0.74% in the long run. The results suggest a populist trap in left-behind regions, as parliamentary populism shifts the legislative agenda away from growth-oriented long-term reforms, creating institutional frictions and policy uncertainty. Counterintuitively, we find that populist support that remains outside parliamentary representation is not associated with lower growth rates. Our findings reveal that the economic costs of populism begin well before populists take office.

1. INTRODUCTION

The last few decades have been marked by the rise of populist parties all over the world, which have seen almost uninterrupted electoral support. While political scientists have long studied populism, economists only began to address it after the Great Recession, when the rise of European populist parties brought this issue to the forefront of research and public debate. According to The Guardian (2019), an estimated 2.5 billion people live in countries whose leaders are at least somewhat populist⁴. In 2022, populist parties had parliamentary representation in 26 out of 27 EU member states⁵. This growing presence, and its evolution across the EU, is visualized in **Error! Reference source not found.**

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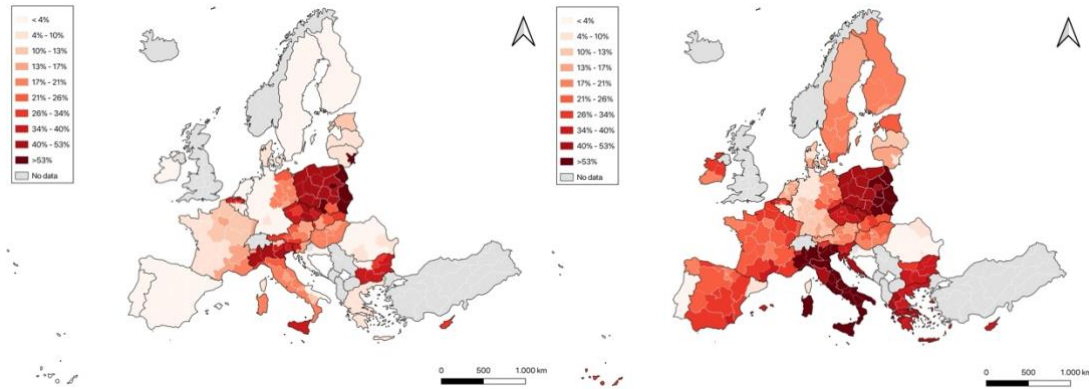
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⁴ This figure is based on an analysis of political leaders' speeches in 40 countries, scored on a 0–2 populism index, where somewhat populist corresponds to 0.5–1.

⁵ All the parties, classified as populist in The Populist 3.0 database (Rooduijn et al., 2023), used in this work are: Austria (FPÖ), Belgium (VB), Bulgaria (ITN, Vazrazhdane, GERB), Croatia (MOST, Domovinski Pokret), Cyprus (ELAM), Czech Republic (ANO, SPD), Denmark (DF), Estonia (EKRE), Finland (PS), France (RN, LFI), Germany (AfD, Die Linke), Greece (SYRIZA, Greek Solution), Hungary (Fidesz), Ireland (Sinn Féin), Italy (FdI, Lega, M5S), Latvia (NA), Lithuania (LVŽS), Luxembourg (ADR), Netherlands (PVV, FvD), Norway (Fremskrittspartiet, Rød Valgallianse), Poland (PiS), Portugal (Chega),

This presence has now become the norm rather than the exception. Researchers have studied the economic (Funke et al., 2023) and institutional (Magud and Spilimbergo, 2021) consequences of populism, focusing on the decisive role of populist leaders (e.g. Grier and Maynard, 2016; Absher et al., 2020). However, the economic literature has largely ignored the consequences of their parliamentary presence, focusing instead on populists in government. Yet we argue that the mere parliamentary presence of populist parties erodes economic performance by altering policy-making. In other words, the ‘Populist Zeitgeist’ (Mudde, 2004; Schwörer, 2021) may alter the behavior of parties in a multiparty system, leading them to adopt populist discourses and policies, in turn, affecting economic performance. We therefore estimate whether, and to what extent, the parliamentary presence of populist parties affects long-run regional economic performance in Europe.

Figure 1 Share of votes to populist parties 1995-2022



Note: The figure displays the regional vote share for populist parties at the NUTS 2 level in 1995 (left panel) and 2022 (right panel). Populist parties are identified following the classification provided by The PopuList 3.0. Regional vote shares are obtained by merging this classification with electoral data from the EU-NED database.

Source: Own elaboration based on data from EU-NED (Schraff et al., 2023) and The Populist 3.0 (Rooduijn et al., 2023).

To this end, we employ a theoretical framework adapted from the growth models of Barro and Sala-i-Martin (2004) and Acemoglu (2009), explicitly incorporating components related to public use of resources and institutional efficiency. Empirically, we test this model by constructing a comprehensive dataset spanning 239 NUTS 2 regions across the European Union for 1996 – 2022. By controlling for regional variations rather than country-level aggregates, our approach captures the heterogeneous economic dynamics that support this phenomenon. We employ a dynamic panel data model estimated via System GMM to address endogeneity concerns and isolate the specific impact of populist

Romania (AUR), Slovakia (Sme Rodina), Slovenia (SDS, LEVICA), Spain (VOX, UP, CUP, EH Bildu), and Sweden (SD), while Malta had none.

parliamentary presence on long-term regional economic performance. Anticipating our main result, we find that a permanent 1 percentage point increase in populist vote share is associated with a long-run decline in regional GDP per capita of about 0.7%. Our identification strategy addresses endogeneity arising from reverse causality and omitted variables through internal instrumentation. We interpret our estimates as internally consistent dynamic effects within the GMM framework.

While the effects of populist executives are well documented, the implications of parliamentary populism remain largely unexplored. In particular, we suggest that the continuous increase in populist vote share entails economic and institutional consequences, albeit of a lesser magnitude than those found in the literature focusing on populist leaders (Funke et al., 2023; Absher et al., 2020). By shifting the focus from executives to parliaments and from countries to regions, our analysis uncovers the economic costs of populism that arise well before populists take office. In this sense, Funke et al. (2023) note that there is still a particular lack of rigorous research on the macroeconomic consequences of populism, especially in advanced economies. We aim to fill this gap.

The remainder of the paper is organized as follows. Section 2 reviews the literature on the definition, causes, and economic consequences of populism. Section 3 outlines the theoretical growth model and describes the data and estimation strategy. Section 4 presents the empirical results. Finally, Section 5 offers concluding remarks and policy implications.

2. CONCEPTUALIZING POPULISM: A REVIEW OF THE LITERATURE

Defining populism remains a contested endeavor in political science due to its inherent conceptual fuzziness, multidimensional nature, and cross-ideological manifestations (Dornbusch and Edwards, 1991; Magud and Spilimbergo, 2021). Yet the definition has evolved over the years (Guriev and Papaioannou, 2022). Two frameworks serve as the primary reference points for operationalizing the concept: *the economic perspective* rooted in Dornbusch and Edwards (1991) and the *ideational approach* spearheaded by Mudde (2004)⁶.

⁶ This framework was further developed in Hawkins and Rovira Kaltwasser (2017) and Mudde and Rovira Kaltwasser (2017).

Dornbusch and Edwards (1991) characterize populism as an economic approach that, while disregarding macroeconomic risks and external constraints, deliberately prioritizes short-term growth and income redistribution. This definition, often referred to as *economic populism* (Sachs, 1989), is best applied—as the authors suggest—to the case of Latin American countries⁷, where populism has predominantly been a left-wing phenomenon, particularly during the second half of the twentieth century (De La Torre, 2014; Huber and Schimpf, 2016), with policies that generated a short-lived boom followed by macroeconomic crisis (Ball et al., 2019). Conversely, Mudde (2004) conceptualizes populism as a 'thin-centered ideology' that separates society into two homogeneous and antagonistic groups—'the pure people' and 'the corrupt elite'—and holds that politics should be an expression of the *volonté générale* (general will) of the people⁸. The latter, being ideological in nature, broadens the definition to encompass the new forms of populism that have emerged in the twenty-first century, typically attaching themselves to host ideologies like nationalism, socialism, or nativism (Mudde and Rovira Kaltwasser, 2017)⁹. Norris and Inglehart (2019) point to the frequent overlap of these new populist movements with authoritarian values.

The literature on populism is typically divided into three strands: (i) the general characteristics of populist leaders—i.e., definition and identification (Rooduijn, 2014; Norris and Inglehart, 2019); (ii) the causes of their electoral success and/or rise to power (Stankov, 2018; Rico and Anduiza, 2019); and (iii) the economic, institutional and social consequences of their rule, i.e., what next? (Houle and Kenny, 2018; Ball et al., 2019).

The last strand examines the economic, social and institutional consequences of populist rule. While most research has focused primarily on Latin American cases¹⁰ (Dornbusch

⁷ The policies implemented in countries such as Argentina, Bolivia, Venezuela, and Chile, are considered part of the populist cycle (Sachs, 1989).

⁸ This definition is not far from what Aristotle pointed out as one of the distinctive features of *demagogues*, which would later become part of one of the common denominators of populists (Rooduijn, 2014). In the words of Aristotle “there is an error common both to oligarchies and to democracies: in the latter the demagogues, when the multitude are above the law, are always cutting the city in two by quarrels with the rich” (Politics, 1310a). We can, therefore, encompass demagogues, given the elements pointed out by Rooduijn (2014), as a special case of populism, thus reconciling the classical and modern conceptions of populism.

⁹ It is worth noting that Laclau (2005) defines populism in a very different fashion. He conceives it as political logic and strategy of mobilization, a discursive model based on dialectical confrontation, not necessarily tied to any fixed ideological content, unlike the ideational approach.

¹⁰ Such as Rafael Correa from Ecuador, Hugo Chavez (on whose presidency, see Grier and Maynard (2016)) and later Nicolás Maduro from Venezuela, Evo Morales from Bolivia, Fujimori from Perú, the Kirchners from Argentina, among many others. Houle and Kenny (2018) have studied the political and economic consequences of these democratic populist regimes using data from 19 Latin American countries and find

and Edwards, 1991; Houle and Kenny, 2018; Absher et al., 2020; Grier and Maynard, 2016), recent work has extended this analysis to other, mainly Western, countries (Guriev and Papaioannou, 2022; Mudde and Rovira Kaltwasser, 2017). Within this branch, recent research has emphasized the political and institutional outcomes (changes in democratic quality (Huber and Schimpf, 2016) and weakening of judicial independence (Funke et al., 2023)) rather than the purely economic ones (Funke et al., 2016; Levitsky and Ziblatt, 2019)¹¹, which remain comparatively understudied.

Regarding the economic findings of populist rule¹², Absher et al. (2020) use a multi-treatment synthetic control model to estimate the durable effects of left-populist regimes in Nicaragua, Venezuela, Bolivia and Ecuador. They conclude that, on average, these regimes reduced real per capita incomes by over 20% and find no trade-off between lower growth and greater income redistribution. Similarly, Funke et al. (2023) study the economic consequences that populist leaders had on the national economy during their term in office. Drawing on a global panel that comprises 1482 leaders from 60 countries, 51 of whom were identified as populists, from 1900 to 2020, they document that GDP per capita is, on average, 10% lower after 15 years compared to non-populist counterfactuals. These costs are linked to institutional erosion (i.e. changes in the national Constitution to remain in power, weakening the checks and balances, nationalization of industries), protectionism, and unsustainable fiscal policies (i.e., debt and inflation) and are invariant to left/right ideology. This dynamic echoes the marked '*walking stick*' pattern identified in Ball et al. (2019), common to Latin American populist regimes, where a short-lived boom undermines the country's long-term productive capacity and macroeconomic stability (persistent inflation, higher deficit, crowding out of private investment).

Regarding the drivers of this phenomenon, Funke et al. (2016) show that systemic financial crises in advanced economies lead to a systematic increase in the electoral

mostly negative outcomes, e.g. erosion of the checks and balances and institutional constraints on executive power, and no more redistribution than non-populist governments, even under iconic leftist governments like Chávez's.

¹¹ In the Latin American context, Huber and Schimpf (2016) find that populists' impact on democratic quality is double-edged. While incumbent populist leaders have a negative effect on it, weakening democratic institutions such as government's checks and balances, and freedom of press and speech; opposition populists may have a positive effect: extending the political agenda to new issues and including the social demands of marginalized groups—as Evo Morales did with the indigenous people (Mudde and Rovira Kaltwasser, 2013)—though it fades as democracy consolidates.

¹² For an excellent and extensive literature review regarding the recent rise of populism and its consequences in a variety of countries, please see Guriev and Papaioannou (2022).

support for far-right parties, parliamentary fractionalization, and diminished majorities. Surprisingly, they show that these crises do not significantly boost support for far-left parties. In a similar vein, Guiso et al. (2017) show that economic insecurity is the key driver behind the demand for populist parties, both directly—through disillusionment with traditional platforms—and indirectly, via the erosion of political trust and growing hostility toward immigrants. Their analysis also shows that insecurity depresses participation among mainstream voters, thereby creating electoral space for populist entrants, underscoring the key role of abstention. On the supply side, moreover, populist parties emerge more readily when economic insecurity is widespread and political opposition fragmented, and choose their ideological orientation strategically, depending on where political space is greatest. In this framework, populist success becomes the equilibrium outcome of a dual crisis—of markets and institutions—leaving voters unprotected and elites unable to respond. Building on this evidence about the effect of crises on the populist surge, *Figure 2* plots the vote-share in each country of the sample by election year from 1995 to 2023¹³. The Great Recession (2008 – 2009) and the COVID pandemic (2020 – 2021) are shaded in grey. In this period, only six out of thirty countries depicted recorded a drop in the populist vote—Luxembourg, Cyprus, Denmark, Iceland, Austria, and Latvia— although in all of them populist parties continue to be represented in Congress.

Populism is also conceived as a discursive style or strategy that constructs confrontations between those two groups (Laclau, 2005), which may or may not be homogeneous—as in the case of Latin American inclusionary populism (Mudde and Rovira Kaltwasser, 2013). Therefore, the ambiguity in determining who is the ‘pure people’ and who is the ‘corrupt elite’ creates room to adapt the definition to parties that employ dialectical and Manichean discursive strategies—through ‘us-vs-them’ narratives—on both sides of the ideological spectrum (Müller, 2016). For example, during the twentieth century most of those branded as populist were on the left wing of the spectrum (Dornbusch and Edwards, 1991), whereas in the twenty-first century they are mainly located on the right wing (Funke et al., 2016; Herkman, 2022). The former confronts the corrupt capitalist and business elite with the common people and the working class; while the latter tend to have openly Eurosceptic positions, as well as nationalistic and xenophobic tendencies, thus

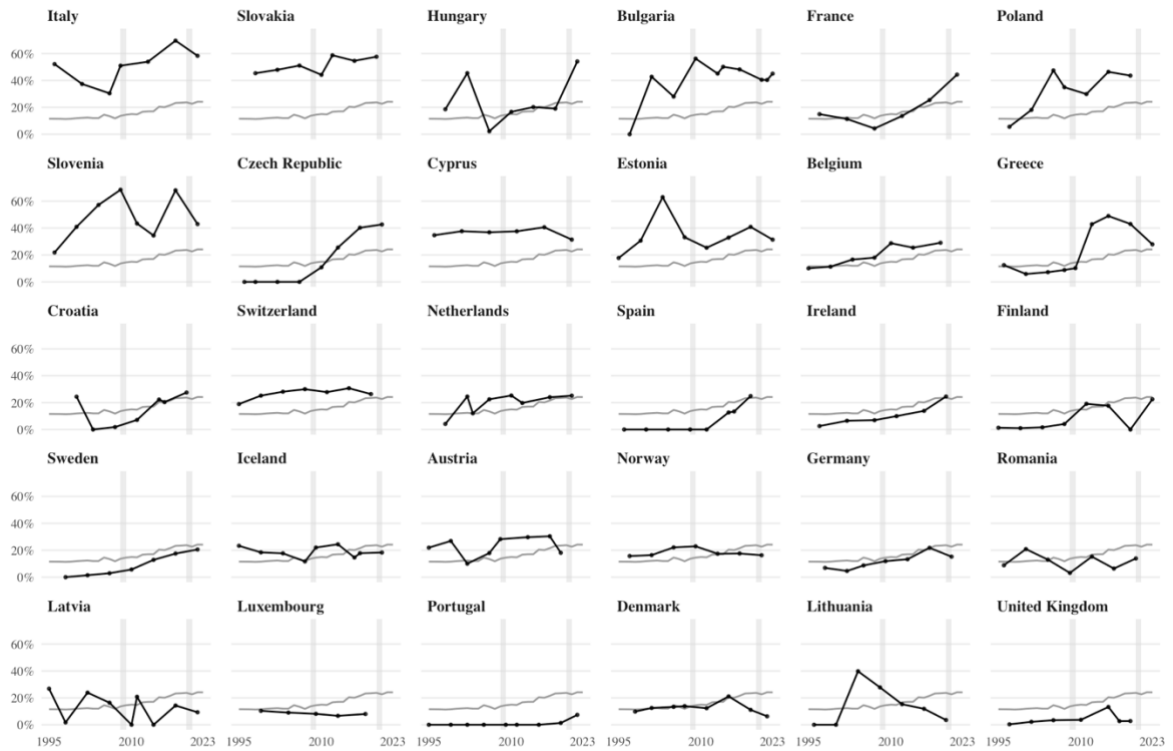
¹³ Note that each dot represents an election year in the country, in some countries the first and last observation in the graph correspond to periods after 1995 and/or before 2023

identifying the corrupt political class – or immigrants – as ‘*them*’, and the pure people, i.e., the nationals or locals as ‘*us*’¹⁴ (Müller, 2016). Other populist leaders have followed a nativist or ethnic perspective—ethnopolit parties—with a highly redistributive, nationalist and interventionist-oriented policy, e.g. Evo Morales (Madrid, 2008).

However, none of these strands systematically examines whether parliamentary populism produces measurable economic effects at the regional level, nor do they account for the territorial heterogeneity in the growing support for contemporary populist options illustrated in **Error! Reference source not found..** This growth in regional support for populist parties is addressed in the seminal paper by Rodríguez-Pose (2018), who frames the rise and success of populist leaders as a *political backlash*, a systematic retaliation by ‘left-behind’ places who leverage electoral (democratic) mechanisms to punish incumbent governments (Wuthnow, 2019). Building on this framework, we argue that the macroeconomic effects and institutional instability associated with executive populism (e.g. Funke et al., 2023; Absher et al., 2020) are ultimately the aggregate and visible manifestation of deeper regional discontent. By focusing on the executive branch, current work has overlooked the fact that the continuous increase in populist vote share is deeply rooted in the socioeconomic decline of ‘left-behind places’ (Rodríguez-Pose, 2018). Therefore, the NUTS 2 level of analysis allows us to capture this regional heterogeneity and provides the appropriate scale to study the economic costs of parliamentary populism.

¹⁴ This type of dichotomization and Manichean discourse is central to populists who present themselves as outsiders vis-à-vis the political establishment (Mudde, 2004), and who claim, by virtue of this self-imposed condition, to represent the will of the ‘people’ better than any other (Levitsky and Ziblatt, 2018).

Figure 2 Trends in Populist Vote Share across European Countries (1995–2023)



Note: The figure displays the evolution of electoral support for populist parties in national parliamentary elections (1995 – 2023). Parties are those tagged as Populist in The PopuList 3.0, merged to ParlGov by party ID to retrieve vote shares; tags are activated using PopuList start/end years. We keep the last election in each year. The solid black line depicts the national vote share for each country, while the grey line represents the aggregate EU trend, calculated as a population-weighted average using annual population data from Eurostat. Shaded vertical bands indicate the periods of the Great Recession (2008–2009) and the COVID-19 pandemic (2020–2021). Countries are ordered descendingly by their vote share in the most recent election. Turkey and Malta excluded

Source: Own elaboration based on data from The PopuList 3.0, ParlGov, and Eurostat.

3. ECONOMIC MODEL AND METHODS

3.1. AN EXOGENOUS GROWTH MODEL WITH PUBLIC GOODS AND INSTITUTIONAL QUALITY

To identify how the presence of populist parties in congress affects economic growth, we develop an original extension of exogeneous growth models (Barro and Sala-i-Martin, 2004; Acemoglu, 2009) in which public spending is productive but subject to congestion, and its growth impact depends on institutional efficiency. According to this framework, once populist parties enter parliament, they can distort policy-making by increasing chronic deficits and weakening institutional efficiency, thereby reducing long-run regional growth.

Assume the economy is endowed with a finite number of N identical and competitive firms that benefit from public goods G as a positive externality to production. As in Barro and Sala-i-Martin (1992), we assume the value of public goods suffers full depreciation

(the State needs to keep a steady flow of public expenditure to maintain the same value of G across periods). Therefore, the simplest Cobb-Douglas production function that face each firm i can be depicted as

$$Y_i = (AL_i)^{1-\alpha} K_i^\alpha \left(\frac{G}{AP} \right)^{\frac{\lambda-1}{\lambda}} \quad (1)$$

where Y_i is the gross output of firm i , A is a measure of the global state of technology, which is shared among all firms, L_i is the number of workers employed by firm i , and K_i is the value of rented physical capital stock. The parameter $\lambda > 0$ determines the output elasticity of firm i regarding public goods G . The ratio G/AP measures the net contribution of public expenditure G discounted from the congestion problem derived from increasing total population weighted by technological progress AP ¹⁵. Besides, effective public goods also suffer from inefficiencies derived from bad institutional quality, where $0 < \lambda < 1$ implies a crippling impact of the public sector on economic growth, $\lambda = 1$ a neutral impact, and $\lambda > 1$ a net positive impact.

Besides, $0 < \alpha < 1$, then equation (1) exhibits constant returns to scale in private inputs L_i and K_i . Therefore, the Euler theorem fulfills the following national accounting fact

$$Y_i = \frac{\partial Y_i}{\partial L_i} L_i + \frac{\partial Y_i}{\partial K_i} K_i = wL_i + RK_i \quad (2)$$

Where, given that all firms produce identical final goods, they also produce the *numeraire* good. Therefore, (2) implies that the value of production of each firm equals the gains of labor and capital hired by that firm, as well as the fact that under perfect competition, each factor is rewarded according to the market value of its marginal productivity.

The public sector obtains public funds from two sources: public debt B ($\dot{B} > 0$ is the creation of new public debt due to public deficit), and income tax collection $T = \tau Y$, where $0 \leq \tau \leq 1$ is the income tax rate. The budgetary constraint of the Public Sector equals

¹⁵ Barro and Sala-i-Martin (1992) assume that congestion occurs at the GDP level.

$$G = \dot{B} + T \quad (3)$$

On the other hand, households devote their disposable income after taxation to consumption C and investment in capital stock I or public debt $\dot{B}$ according to the constraint

$$C + I + \dot{B} = Y - T \quad (4)$$

Rearranging we have

$$I + \dot{B} = S \quad (5)$$

Where $S = Y - T - C$ is savings from households. Assuming that investment in public debt is a ratio $-1 \leq \phi \leq 1$ of gross savings, then $\dot{B} = \phi S$, and we can rearrange (5) into

$$I = (1 - \phi)Y \quad (6)$$

Furthermore, using the fact that $T = \tau Y$, then $S = s(Y - T)$ where s is the exogenous saving rate as in the original Solow-Swan model, gross investment in physical capital stock can be read as

$$I = ((1 - \tau)s - \phi)Y \quad (7)$$

Since public debt and physical capital are perfect substitutes in the investment portfolio of households, we assume that ϕ is adjusted by the public sector according to its desired level of chronic public deficit relative to GDP.

Since all firms are identical, each firm is endowed with $1/N$ units of private sector labor force L and capital stock K . Using this fact in (1), aggregate gross output equals

$$Y = \sum_i^N \frac{1}{N} (AL)^{1-\alpha} K^\alpha \left(\frac{G}{AP} \right)^{\frac{\lambda-1}{\lambda}} = (AL)^{1-\alpha} K^\alpha \left(\frac{G}{AP} \right)^{\frac{\lambda-1}{\lambda}} \quad (8)$$

Finally, using the facts $\dot{B} = \phi Y$ and $T = \tau Y$ in (3), yields the equilibrium level of public goods provision

$$G = (\phi + \tau)Y \quad (9)$$

Substituting (9) into (8), using $n = L/P$ as the ratio of employment over total population, $\tilde{k} = K/(AP)$ as the stock of capital per capita per effective person, and $y = Y/P$ as gross output per capita, leads to the final per capita GDP equation

$$y = An^{(1-\alpha)\lambda} \tilde{k}^{\alpha\lambda} (\phi + \tau)^{\lambda-1} \quad (10)$$

Assuming that physical capital accumulation is explained by the Solow-Swan model's equation of motion, and the remaining variables and parameters evolve at an exogenous rate, as well as $\lambda < 1/\alpha$, the level of output per effective person $\tilde{y} = y/A$ around the steady state $(\tilde{y}^*, \tilde{k}^*)$ equals¹⁶

$$\tilde{y}^* = n^{\frac{(1-\alpha)\lambda}{1-\alpha\lambda}} \left(\frac{(1-\phi)(1-\tau)s}{\delta + g_P + g_A} \right)^{\frac{\alpha\lambda}{1-\alpha\lambda}} (\phi + \tau)^{\frac{\lambda-1}{1-\alpha\lambda}} \quad (11)$$

Here, δ denotes the depreciation rate of physical capital stock, while g_P and g_A are the growth rates of population and technological progress. Observe that, for $1 < \lambda < 1/\alpha$, the steady state of the economy is concave with respect to the tax rate τ and the chronic public deficit rate ϕ . Conversely, when bad institutional quality prevails ($0 < \lambda < 1$), equation (11) is strictly decreasing in the aforementioned variables. In this framework, if

¹⁶ Steady-state physical capital per effective worker equals $\tilde{k} = n^{\frac{(1-\alpha)\lambda}{1-\alpha\lambda}} \left(\frac{(1-\phi)(1-\tau)s}{\delta + g_L + g_A} \right)^{\frac{1}{1-\alpha\lambda}} (\phi + \tau)^{\frac{\lambda-1}{1-\alpha\lambda}}$.

the mass of voters is large enough to allow the entry of populist parties into parliament, it reduces the efficiency with which public resources are transform into productive public capital (lowering λ). This inefficiency may manifest through different channels, such as clientelistic spending that boosts aggregate demand without enhancing productive capacity, misallocation of fiscal resources, or reduced quality of public investment. When $\lambda < 1$, tax revenues and deficit-financed expenditure fail to generate productive public capital, crowding out resources that could otherwise be allocated to productive investment.

3.2. ESTIMATION STRATEGY

The standard first-order Taylor approximation to average per capita GDP growth around the steady state of a panel of N regions in $z < T$ subperiods equals (e.g. Barro and Sala-i-Martin, 2004; Acemoglu, 2009)¹⁷

$$\frac{\ln y_{it} - \ln y_{it-z}}{z} \approx g_{Ai} - \beta(\ln y_{it-z} - \ln y_{it}^*) \quad (12)$$

where $\ln y_{it}$ is the natural logarithm of per capita GDP of region i in period t , z is the span of time of each subperiod, and g_{Ai} is the steady-state per capita average growth rate of economy i . Additionally, $\beta = \left(\partial \frac{\ln \tilde{y}_{it} - \ln \tilde{y}_{it-z}}{z} / \partial \ln \tilde{y}_{it} \right) \Big|_{\ln \tilde{y}_{it} = \ln \tilde{y}_{it}^*}$ is the parameter of implicit speed of convergence which must fulfil $0 < \beta < 1$ to have a stationary series in (12) around g_{Ai} .

We also approximate the natural logarithm of equation (11) using a first-order Taylor approximation around the unknown steady-state values $(X^*) = (\lambda_i^*, n_i^* s_i^*, g_{pi}^*, \phi_i^*, \tau_i^*)$. This leads to

$$\ln y_{it}^* \approx \ln A_{it} + \ln \tilde{y}_i^* + \sum_m^M \frac{\partial \ln \tilde{y}^*}{\partial x_m} (X^*) \cdot (x_{mit} - x_{mi}^*) \quad (13)$$

¹⁷ Due to alphabetic limitations, we use i in this subsection to identify each region, while N is the total number of regions.

Since each partial derivative $\partial \ln \tilde{y}^* / \partial x$ is evaluated in the steady state of the economy, we assume that $E \left(\frac{\partial \ln \tilde{y}^*}{\partial x_m} (X^*), x_{mit} \right) = 0$. Then, equation (12), using equation (13), can be rearranged into the two-way fixed effects linear regression

$$\ln y_{it} = u_{it} + \tilde{\beta} \ln y_{it-z} + \chi \lambda_{it} + \sum_m^{M-1} \rho_m x_{mit} + \varepsilon_{it} \quad (14)$$

Where $u_{it} = u_i + \gamma_t \approx -z\beta \left(\ln \tilde{y}_i^* - \sum_m^M \frac{\partial \ln \tilde{y}^*}{\partial x_m} (X^*) \cdot x_{im}^* + \ln A_{it} \right)$ is the linear combination of region (u_i) and time (γ_t) fixed effects. Additionally, $\sum_m^{M-1} \rho_m x_{mit}$ works as a set of control variables which are standard in growth regressions, and ε_{it} is a random noise term normally distributed.

The parameter of convergence is now weighted by the number of chosen subperiods z , that is $\tilde{\beta} = 1 - z\beta$. Since the speed of convergence implies $\beta = (1 - \tilde{\beta})/z$, and time will be measured in natural numbers, i.e. $z: \{1, 2, 3, \dots, \text{Max } z\}$, then $1 \leq z < T$, the estimated $\tilde{\beta}$ must be also positive and bounded between 0 and 1 to fulfill the stationarity condition $0 < \beta < 1$.

Our major analysis is associated with parameter χ . Our model does not theoretically constrain χ to a specific value; thus, institutional quality may exhibit positive, negative, or null impacts on the long-term growth rates of EU regions¹⁸. Additionally, we also aim to identify χ exploiting data on populism support. According to Huber and Schimpf (2015) and Vittori (2022), populist parties can deteriorate, improve or have a null impact on the quality of liberal-democratic regimes depending on their political power and relevance.

Finally, since the Within Groups estimator is likely to be inconsistent and biased downwards due to dynamic panel data (Nickell, 1981; Bond, 2002), we consider the System GMM estimator (Arellano and Bover, 1995; Blundell and Bond, 1998) using past information on the levels and differences of the regress and regressors to minimize sample bias and increase estimates precision (Bond, 2002).

3.3. DATA

¹⁸ For a discussion on endogenous institutional quality, see Acemoglu and Robinson (2008).

We build a comprehensive panel dataset covering 239 NUTS 2 regions in 27 European countries for the period 1996 – 2022 (5,513 observations). We rely on NUTS 2 regions for several reasons. First, focusing on subnational-level rather than country-level (NUTS 0) data allow us to capture regional heterogeneity in growth. Policies enacted at the national level often affect prosperous and lagging regions in asymmetric ways, fueling discontent and the sense of being “left-behind” (Rodríguez-Pose, 2018). Second, NUTS2 regions are also meaningful political units because electoral competition, party organization and voter mobilization often follow regional lines, making this the appropriate scale at which parliamentary populism originates. Furthermore, aggregating at the country level risks overlooking the place effect in vote (Gutiérrez-Posada et al., 2021), thereby masking the unequal regional economic trajectories that underpins the electoral success of populist parties (Dijkstra et al., 2020). Consequently, the regional scale provides the necessary variance and a sufficient large panel to estimate dynamic growth models, while controlling for time-invariant regional heterogeneity.

Our primary outcome variable is the natural logarithm of real GDP per capita (in constant 2015 euros). Regional economic and demographic data (GDP, population, employment, gross investment, taxation) are obtained from the Annual Regional Database of the European Commission 2024 (ARDECO) (Auteri et al., 2024), while country-level public deficit figures are extracted from Eurostat’s Government Finance Statistics (EDP and ESA2010) (Eurostat, 2024). *Table 1* outlines the variable definitions, while *Table 2* provides summary statistics for all variables.

Political data are constructed by merging The PopuList 3.0 (Rooduijn et al., 2023) and the EU-NED datasets (Schraff et al., 2023). Using an Expert-informed Qualitative Comparative Classification (EiQCC), The Populist 3.0 identifies political parties from 31 countries according to the ideational approach from 1989 to 2020¹⁹. Parties are classified as populist if they exhibit people-centrism, anti-elitism and claims that politics should express the the *volonté générale* of the people (Mudde, 2004; Hawkins and Kaltwasser, 2017). The EU-NED dataset provides disaggregated electoral results at the NUTS 2 level, including regional vote counts and electoral census. We construct four measures of populist support:

¹⁹ The dataset contains parties that have won one seat or at least a 2 per cent of the vote in national parliamentary elections and are either populist, far right, far left (Rooduijn et al., 2024). Parties not included in the database are not considered either populist, nor far right or far left.

- i. Populist vote share (*pop*): Votes for populist parties in region i during national elections in year t divided by the electorate in region i , year t . With this measure we capture the aggregate electoral strength of populist parties in each region, irrespective of its territorial concentration.
- ii. Parliamentary populist vote share (*pop_par*): Votes for populist parties already in the parliament (in country c) in region i during national elections in year t by the electorate in region i in year t . This measure directly captures legislative influence, acknowledging that parties with parliamentary representation can materially affect policy through agenda-setting, committee work, and coalition bargaining.
- iii. Non-parliamentary populist vote share (*pop_nopar*): Votes for populist parties who are not in the parliament (in country c) in region i during national elections in year t divided by the electorate in region i in year t .
- iv. Territorially-adjusted populist vote share (*pop_pns*): To account for the fact that populist support may be geographically concentrated in specific regions, we also weigh the shares of votes by a standardized political nationalization score (PNS) in the lines of Jones and Mainwaring (2003) and Bochsler (2010). The PNS acts as a Gini coefficient for territorial distribution of votes, adjusted for the effective number of electoral units *à la* Bochsler²⁰ using regional population. The final PNS for populist votes in country $j \in [1, J]$ is defined as:

$$PNS_{jt} = 1 - \left(\frac{\sum_{i,j}^{N_j} \sum_{-i,j}^{N_j} |pop_{ijt} - pop_{-ijt}|}{2N_j \sum_{i,j}^{N_j} pop_{ijt}} \right)^{1/\ln E_j} \quad (12)$$

Where N_j is the number of regions and E_j is the effective number of electoral units based on population. The score equals 1 when (i) there is only one region in the country ($N_j = 1$)²¹; (ii) when the populist support is perfectly uniform across all regions in country j ($pop_{ijt} = pop_{-ijt}$), and decreases as the vote distribution becomes more polarized or

²⁰ The number of effective electoral units equals 1 when the country has only one region, or when population is identically distributed across regions. This number penalizes parties in countries with less concentrated population, increasing the number of electoral districts with a significant influence on the final result of elections, requiring parties to have a widespread clout across regions in order to attain more *de facto* political power.

²¹ Which is not the case in any country of our sample.

territorially concentrated; (iii) when the number of effective electoral units $E_j = \left(\sum_{i_j}^{N_j} inhab_{i_j} \right)^2 / \sum_{i_j}^{N_j} inhab_{i_j}^2$ increases

Table 1 Variables and their definitions.

Variable	Name	Definition	Source
lny	Log of per capita GDP	Natural logarithm of GDP at constant prices (million EUR2015) divided by total population on 1st January (millions of persons)	
n	Employment to population ratio	Total Employment (workplace based, millions of employed persons) divided by total population on 1st January (millions of persons)	
s	Investment rate	Gross Fixed Capital Formation at constant prices (million EUR2015) divided by GDP at constant prices (million EUR2015)	
ginhab	Population growth	First time difference of the natural logarithm of total population on 1st January (millions of persons)	
pd	Public deficit	General government deficit with respect to GDP	
tx	Tax rate	Current taxes on income and wealth (million EUR) divided by households' net disposable income (million EUR)	
pop	Populist support	Total votes supporting populist parties during national elections divided by the electorate (%)	
pop_pns	Weighted populist support	Populist support weighted by the political nationalization score	
pop_par	Populist support in parliament	Total votes supporting populist parties already in the parliament during national elections divided by the electorate (%)	
pop_nopar	Populist support out of parliament	Total votes supporting populist parties not present in the parliament during national elections divided by the electorate (%)	

Data sources: ARDECO, Eurostat, QoG, The PopuList 3.0 and EU-NED datasets.

Table 2 Summary statistics

Variable	Mean	SD	Min	Max
lny	9.986	0.633	7.859	11.566
n	0.445	0.083	0.172	0.937
s	0.216	0.050	0.066	0.783
ginhab	0.002	0.008	-0.053	0.062
pd	0.030	0.032	-0.069	0.321
tx	0.123	0.060	0.010	0.420
pop	0.169	0.166	0	0.756
pop_pns	0.104	0.119	0	0.624
pop_par	0.116	0.152	0	0.756
pop_nopar	0.053	0.104	0	0.705

Note: This is an unbalanced panel data with 5513 observations from 239 NUTS 2 entities between 1996 and 2022 (28 periods).

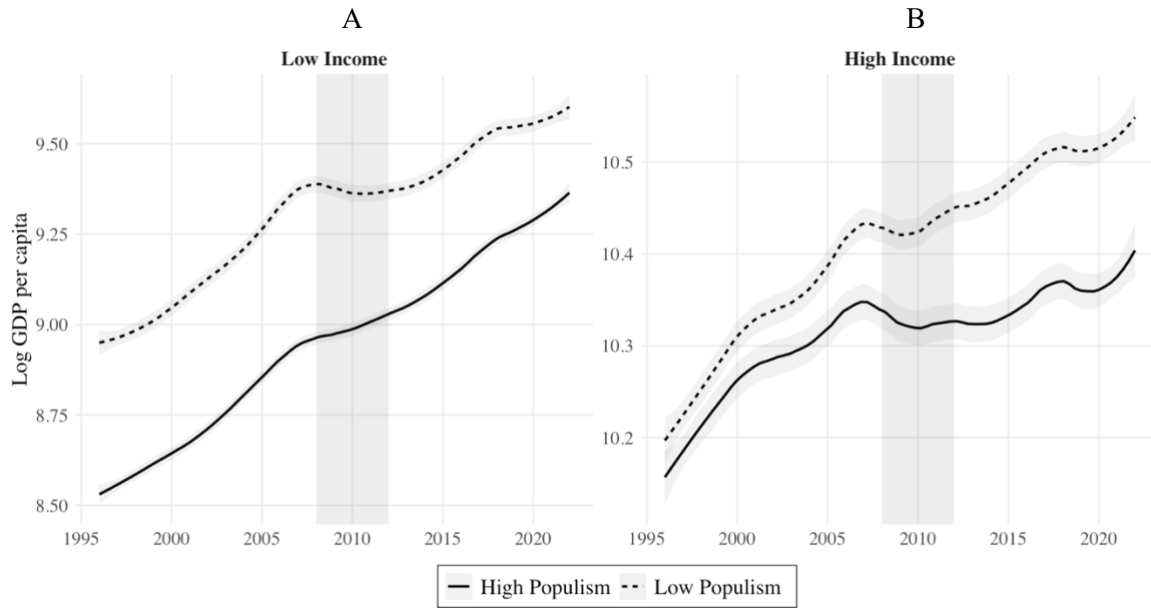
A key feature in our data is the subnational intra-country heterogeneity in populist support (as shown in *Figure 1*). Even with the same institutional and macroeconomic (within-country) context, regions differ significantly in their exposure to populist politics. This variation is visualized in **Error! Reference source not found.** (Panel A and B), which plots the unconditional relationship between populist vote share and average GDP per capita trajectories (1996 – 2022). To ensure meaningful comparisons across development stages, we first classify countries into quintiles based on their average GDP per capita over the period 1996 – 2022, isolating Low-Income (bottom 40%, Q1 + Q2) and High-Income (top 40%, Q4 + Q5) countries. Within these country groups, regions are classified as *High* or *Low Populism* based on whether their mean vote share (1996 – 2022) exceeds the within-group median²².

Panel A (Low-Income Countries) reveals that regions with high populist support tend to systematically lag behind their low-populism counterparts through the entire period, suggesting a persistent association between economic performance and populist voting.

Panel B (High-Income Countries) shows a more dynamic pattern with growth trajectories evolving evenly until 2008, suggesting a structural break following the Great Recession. Low-populism regions subsequently recover, whereas high-populism regions stagnate. The failure to recover from economic shocks in left-behind regions seems to fuel sustained populist support, creating a potential reinforcing cycle of economic decline and political discontent (Rodríguez-Pose, 2018).

²² Table A.1 shows the number of NUTS 2 regions in each country classified in each group.

Figure 3 GDP Trajectories by Populist Support and Income Level



Note: The figure displays average log GDP per capita trajectories for NUTS 2 regions, classified by average national income levels (1996 – 2022). Panel A comprises regions in low-income countries (bottom 40%, $Q1 + Q2$), while Panel B covers high-income countries (top 40%, $Q4 + Q5$). Regions are classified as High or Low Populism based on their average populist vote share in national elections (1996 – 2022) relative to the within-group median. In the low-income group, High Populism (30 regions) is predominantly driven by Poland, Hungary, Bulgaria, and Slovenia, whereas Low Populism (30 regions) is concentrated in Czechia, Romania, Slovakia, Croatia, Lithuania, Estonia, Latvia, and Malta. In the high-income group, High Populism (58 regions) primarily includes regions from France, Austria, Denmark, and Finland, while Low Populism (58 regions) is dominated by Germany, Sweden, and Luxembourg. The exact composition of each group is displayed in Table A. 1 in the Annex. The shaded gray area indicates the Great Recession (2008–2012).

Source: Own elaboration based on data from ARDECO and The PopuList 3.0.

4. RESULTS

Table 3 shows the main results of the Within (M1) and system GMM estimators (M2-M6). Specification M2 assumes that regressors other than the time lag of the dependent variable are strictly exogenous, while specifications M3-M6 expand the system of equations considering potential endogeneity in covariates. Additionally, specifications M4-M6 change the populism variable to check for heterogeneous results.

As expected, the Within estimator underestimates the coefficient measuring the inertia of the series, with a value of 0.695. In contrast, the GMM estimates range between 0.8 and 0.906. In this sense, the Within estimator overestimates the speed of convergence to the long-term growth rate of GDP per capita, yielding a value of 0.076, while that of the

GMM system range between 0.05 and 0.024²³. The overestimation of speeds of convergence is a common result of biased estimates result from misspecification and endogeneity issues (Islam, 2003). Then, we dismiss those results of the Within estimates. Focusing on the System GMM estimates, the no rejection of serial autocorrelation²⁴ in specification M2 violates the necessary condition for an accurate estimation of equation (14) (Bond, 2002). Conversely, specifications M3-M6 soundly reject the existence of serial autocorrelation. This result, alongside the Hansen test of overidentifying restrictions, as further evidence against the assumption of strict exogeneity in the chosen covariates and instruments, as expected. Then, we also dismiss specification M2 as non-valid.

Furthermore, the estimated coefficient for the lagged dependent variable (0.898; M5, *Table 3*) in our preferred System GMM specification, lies within the credible range defined by the downward-biased Fixed Effects estimate (0.695; M1, *Table 3*) and the upward-biased Pooled OLS estimate (0.909; full results are omitted for brevity but available upon request). This supports the validity of our instrumenting strategy, confirming that the System GMM estimator effectively addresses dynamic panel bias without suffering from finite sample biases (Bond, 2002).

Regarding the control variables, the results are consistent with the predictions of the theoretical model framework outlined in *Section 3*. The share of employment (n) and the investment rate (s) show a positive and significant coefficients across all specifications. Higher labor participation and physical capital accumulation are key drivers of regional development, confirming the standard Solow-Swan predictions. A contemporary increase of 1 percentage points (p.p.) in any of these variables increases per capita GDP between 0.3% and 0.5%. Furthermore, fiscal pressure over households (tx) also presents a positive impact, ranging between 0.354% and 0.412% after experiencing a 1 p.p. increase. This suggests that the distortionary effect of taxes on private consumption and investment is compensated by a more active role of the public sector via productive public expenditure. Conversely, public deficit (pd) shows a strong negative influence on per capita GDP, decreasing it between 0.4% and 0.51% after an increase of a percentage point in the share

²³ Recall that equation (14) estimates average growth rates for 5-year subperiods of time, then the implicit interannual speed of convergence equals $\beta \approx (1 - \partial \ln y_t / \partial \ln y_{t-4}) / 4$.

²⁴ The AR(5) test shows that first-differenced residuals are correlated with their fifth-order lags, that is, $E(\Delta \varepsilon_{it}, \Delta \varepsilon_{it-5}) = E(\varepsilon_{it} - \varepsilon_{it-1}, \varepsilon_{it-5} - \varepsilon_{it-6}) \neq 0$. By construction, this is always true for the AR(1-4), since $\Delta \ln y_{it} = \Delta f(\cdot) + \sum_{z=0}^4 \Delta \varepsilon_{it-z}$.

of public expenditure minus revenues over aggregate GDP. This is consistent with our hypothesis that chronic deficits crowd out private investments and increase the risk premium, as captured by equation (11) of our model. To sum up, and following the model proposed in Section 2, it seems that fiscal pressure is below the optimal levels of taxation for the average EU NUTS 2 region, whereas the public deficit has likely exceeded its sustainable threshold.

Table 3 Estimated results

	Within	System GMM estimates				
	(M1)	(M2)	(M3)	(M4)	(M5)	(M6)
lny fourth lag	0.695*** (0.029)	0.800*** (0.047)	0.891*** (0.013)	0.884*** (0.013)	0.898*** (0.012)	0.906*** (0.012)
n	1.029*** (0.148)	1.350*** (0.255)	0.469*** (0.073)	0.455*** (0.071)	0.465*** (0.073)	0.505*** (0.076)
s	0.187*** (0.065)	-0.366 (0.261)	0.336*** (0.088)	0.328*** (0.089)	0.360*** (0.087)	0.374*** (0.082)
ginhab	-1.754*** (0.376)	0.751 (1.669)	-0.821** (0.377)	-0.911** (0.378)	-0.950** (0.388)	-0.543 (0.404)
pd	-0.289** (0.119)	0.818** (0.408)	-0.511*** (0.084)	-0.498*** (0.085)	-0.468*** (0.081)	-0.405*** (0.084)
tx	-0.506*** (0.186)	1.084** (0.544)	0.354*** (0.113)	0.412*** (0.116)	0.380*** (0.117)	0.355*** (0.109)
pop	-0.079*** (0.017)	-0.243*** (0.068)	-0.045** (0.023)			
pop_pns				-0.122*** (0.033)		
pop_par					-0.075*** (0.022)	
pop_nopar						0.148*** (0.026)
Cum. impact of populism	-0.259*** (0.064)	-1.212*** (0.351)	-0.418** (0.200)	-1.049*** (0.252)	-0.738*** (0.207)	1.582*** (0.403)
AR4 test first differences		-6.08*** (p=0.00)	-4.80*** (p=0.00)	-4.95*** (p=0.00)	-4.89*** (p=0.00)	-4.87*** (p=0.00)
AR5 test first differences		-2.05** (p=0.04)	-0.05 (p=0.96)	-0.01 (p=0.99)	0.04 (p=0.97)	0.02 (p=0.98)
Hansen overid. test		73.33*** (p=0.00)	236.30 (p=0.99)	236.56 (p=0.99)	236.26 (p=0.99)	236.70 (p=0.99)
Year FE	YES	YES	YES	YES	YES	YES
Observations	5513	4557	4557	4557	4557	4557

*Standard errors in parentheses. * $p < .10$, ** $p < .05$, *** $p < .01$. Instruments for equation in differences: first lag of all explanatory variables. Instruments for equation in levels: first lag of the first difference of all explanatory variables. The cumulative impact using $1/(1 - (1 - \partial \ln y_t / \partial \ln y_{t-4})/4)$.*

Considering the main hypothesis of the present work, *Table 3* shows robust evidence of populist support as a relevant determinant of economic growth. Estimates suggest that a 1 p.p. increase in the share of votes devoted to populist parties lowers contemporary per capita GDP by 0.045%. This change is larger when we account for the actual representativeness of these votes, whether by taking into account territorial polarization –a 0.122% reduction in per capita GDP– or considering the presence in the parliament –a 0.075% decrease. These short-run effects are modest because legislative influence materializes gradually through budget composition, agenda-setting and regulatory delays, which accumulate over time.

Counterintuitively, the results for the extra-parliamentary populism (M6, *Table 3*) suggest that an increase in populist support without parliamentary representation fosters economic growth, raising per capita GDP by 0.148%. This pattern is consistent with models of electoral discipline (Barro, 1973) and with probabilistic-voting frameworks where incumbents respond strategically to electoral threats (Lindbeck and Weibull, 1987; Dixit and Londregan, 1996). Rising populist support tightens the re-election constraint, forcing mainstream parties to reduce 'political income'²⁵ and align policy closer to the public interest to secure survival. However, once populists gain legislative power (i.e., seats in the parliament), the effect reverses (M4 and M5, *Table 3*), consistent with the materialization of institutional frictions and persistent deficits.

Regarding the long-term dynamics, while the immediate contractionary effect of parliamentary populism is estimated at 0.075%, the long-run cumulative impact is substantially larger. A permanent 1 percentage point increase in populist vote share leads to a cumulative reduction in per capita GDP of approximately –0.74% (M5, *Table 3*). These results confirm our main hypothesis, the mere presence of populist parties with representation affects regional economic growth, persistently, although more gradually but less than what has been found by other authors when it comes to populist leaders (Absher et al., 2020; Funke et al., 2023).

5. CONCLUSIONS

This paper builds on the recent literature regarding the economic consequences of populism but shifts the focus from the executive branch to the legislature, and from the national aggregate to the regional scale. While previous research has studied the economic

²⁵ Defined as rents extracted through inefficient government expansion or factor overpayments.

costs of populist leaders (e.g., Houle and Kenny, 2018; Ball et al., 2019; Absher et al., 2020; Funke et al., 2023), the macroeconomic impact of their mere parliamentary presence has remained unexplored.

Using a comprehensive panel of 239 European NUTS 2 regions over the period 1996 – 2022, we employ System GMM estimators to address endogeneity and provide evidence that populist parties do not need to govern to erode economic growth. Our empirical analysis shows a significant negative relationship between the electoral support for populist parties and regional economic performance, robust to different model specifications. Specifically, we estimate that a permanent 1 percentage point increase in populist vote share leads to a cumulative reduction in per capita GDP of approximately 0.74%. This suggests that the economic impact is a cumulative process rather than a one-off shock.

This cumulative erosion of economic performance should not be interpreted simply as a penalty associated with electoral preferences per se, but rather as a significant missed opportunity for structural reforms—therefore representing a high opportunity cost in terms of long-term reforms to foster growth. The entry of populist parties into parliament is often associated with a shift in the legislative agenda away from competitiveness and liberalization policies (Abou-Chadi and Krause, 2020; Schwörer, 2021; Rodrik, 2018). Instead of fostering an environment focused on long-term growth, political capital is redirected towards short-term redistributive conflicts or identity politics (Schumacher and van Kersbergen, 2016), keeping regions in a lower-growth equilibrium.

Our finding on extra-parliamentary populism, which we find to be associated with a positive contribution to regional growth (0.148%), may support this interpretation. It may suggest that the electoral threat of a rising populist wave initially acts as a discipline mechanism, incentivizing mainstream incumbents to improve policymaking efficiency to recapture the dissatisfied electorate. This aligns with Schumacher and van Kersbergen (2016), who argue that the prospect of losing votes to a populist party motivates mainstream party responses. However, once these forces gain parliamentary presence, this disciplining effect appears to be outweighed by the institutional friction and policy uncertainty described in our theoretical model. Thus, the economic cost arises not from the expression of populist sentiment itself, but from the specific gridlock and misallocation of resources that occur when these parties obtain legislative leverage.

Symmetrically, a second interpretation may pose that this positive effect may capture the economic recovery that follows when populist parties *lose*

Finally, our findings have profound implications for the European Cohesion Policy. The results suggest the possibility of a *populist trap*: the economic decline of 'left-behind' regions fuels the rise of populist parties which, once in parliament, implement or force policies that further erode regional growth potential (Rodríguez-Pose, 2018). Breaking this vicious cycle may require a focus on improving the institutional quality (Rodríguez-Pose, 2013).

While our analysis is robust to endogeneity concerns, we are aware of some limitations. First, our macro-level approach does not disentangle the specific micro-channels of transmission (e.g., the flight of human capital or the contraction of FDI). Second, we treat populism as a unified ideational shock, but future work could explore whether right-wing and left-wing populisms affect the economy through different mechanisms. Nonetheless, the cost of populism is measurable and pose a significant economic challenge for regional development.

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ANNEX

Table A. 1 Classification of Countries by Income Level, Populism Group, and Number of NUTS 2 Regions

Low Income Countries		
Populism group	Country	NUTS 2 regions
High Populism	Poland	15
	Hungary	8
	Bulgaria	5
	Slovenia	2
Low Populism	Czechia	8
	Romania	8
	Slovakia	4
	Croatia	2
	Lithuania	2
	Poland	2
	Bulgaria	1
	Estonia	1
	Latvia	1
	Malta	1
High Income Countries		
Populism Group	Country	NUTS 2 regions
High Populism	France	21
	Austria	9
	Germany	8
	Belgium	6
	Denmark	5
	Finland	4
	Netherlands	4
	Sweden	1
Low Populism	Germany	30
	Netherlands	8
	Sweden	7
	France	6
	Belgium	5
	Finland	1
	Luxembourg	1

*Note: Country and regional composition underlying **Error! Reference source not found.** Each row indicates the number of NUTS2 regions from a given country contributing to each trajectory. Countries are grouped by income quintiles based on 1996 national GDP per capita (Low Income: Q1+Q2; High Income: Q4+Q5). Within each income group, regions are classified as High or Low Populism according to whether their mean populist vote share (1996-2022) exceeds the within-group regional median. Countries with regions in both categories reflect significant intra-country variation in populist support.*