

Fiscal Policy and Inequality

17. Elections as Selection and Incentive Device

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- ▶ There are two main problems
 - ▶ Moral hazard (incentives): Policymakers may act opportunistically.
 - ▶ Political selection: Policymakers may differ in their quality or motivation.
- ▶ Political agency models are motivated by the idea that elections serve to address these problems

Outline

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 - ▶ For passing out goodies (e.g. delivering programs)
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- ▶ Evidence
 - ▶ Do voters reward good politicians?
 - ▶ For passing out goodies (e.g. delivering programs)
 - ▶ For being good types (e.g. not being corrupt)
 - ▶ Do politicians respond to these incentives? (e.g., by becoming more honest)
 - ▶ Can we distinguish incentives from selection in practice?

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Baseline Political Agency Model

Evidence on Elections as Selection and Incentive Device

- Voter Responses to Targeted Transfers

- Voter responses to information on corruption

- Politician Responses to Voter Accountability

Wages and Politician Performance

Politician choices and incentives

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- ▶ What is a ?
 - ▶ Effort. e.g., passing a new bill takes a lot of work. He'd prefer to play golf.
 - ▶ Lack of corruption. Politician prefers to steal, but public doesn't want him to
 - ▶ Lack of crony capitalism. Politician prefers to give jobs

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- ▶ The greater the temptations of slacking off in office (the greater the r), the more likely he will choose the low action
- ▶ What happens if politicians cannot run for reelection (term limits)? Then we get low action for sure.
 - ▶ This is one empirical test we will use

Types of politicians

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 - ▶ Opportunistic types will do whatever they think is optimal, that is, choose $a = 1$ when

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Model Timing: Two Periods

- ▶ First period.
 - ▶ Politician chosen at random from the distribution of candidates.
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 - ▶ All else chose $a = 0$. (Why?)

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- ▶ Impact on opportunistic type:
 - ▶ Given this voter strategy, opportunistic type will choose $a = 1$ (the good action) in the first term, in order to be reelected and get the office rewards in the second term.

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 - ▶ **Selection:** since voters select for good types, good types are more likely to be in office and bad types are less likely to be in office.
 - ▶ **Incentives:** since voters reward the good action, opportunistic types are more likely to choose the good action.

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Political Agency in Practice

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- ▶ From the voters'side:
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- ▶ What are the policy implications?

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Do voters reward politicians who appear to do better?

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- ▶ Setting
 - ▶ Mexico
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 - ▶ 505 villages were randomly treated (i.e., received benefits) either 21 months or 6 months before the 2000 Mexican presidential election
 - ▶ Examine the impact on electoral turnout and vote for the incumbent

Specification

- ▶ They run the regression

$$\Delta y_i = \theta + \beta \text{treatment}_i + \varepsilon_i$$

where treatment is a dummy variable that is 1 if you received the program for longer.

- ▶ Is β consistently estimated? Why or why not?

Turnout Results and Vote Share

TABLE 3 Impact of Progresa on Turnout and Party Vote Shares

ITT Estimates of the Assignment to Early versus Late Treatment				
	(1) Turnout	(2) PRI	(3) PAN	(4) PRD
Treatment	0.053* (0.030)	0.037** (0.015)	0.007 (0.012)	0.002 (0.014)
Constant	0.580*** (0.172)	0.233*** (0.086)	0.191*** (0.072)	0.166** (0.074)
Controls	yes	yes	yes	yes
# Villages fixed effects	yes	yes	yes	yes
Observations	417	417	417	417
R-squared	0.116	0.288	0.197	0.318
IV Estimates of Early Progresa Coverage				
	Turnout	PRI	PAN	PRD
Early Progresa	0.156* (0.087)	0.108** (0.045)	0.021 (0.035)	0.006 (0.040)
Constant	0.702*** (0.154)	0.414*** (0.080)	0.146** (0.069)	0.140** (0.068)
Controls	yes	yes	yes	yes
# Villages fixed effects	yes	yes	yes	yes
Observations	417	417	417	417
R-squared	0.095	0.275	0.192	0.317

- ▶ Turnout increased in places that received the program longer
- ▶ Vote share for the incumbent party (PRI) increased in places that received the program longer

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 - ▶ This has happened in Indonesia.
 - ▶ Suggests incumbents will target programs to those people who are likely to be marginal in turnout
 - ▶ Politicians tend to rebrand programs to try to get credit
 - ▶ Progresa was rebranded Oportunidades by the new administration – same program, new name

Happiness and Incumbent Vote Share

- ▶ Bagues and Esteve-Volart, *Journal of Political Economy* (2016):
 - ▶ Incumbent politicians tend to receive more votes when economic conditions are good.
 - ▶ Exploit the exceptional evidence provided by the Spanish Christmas Lottery.
 - ▶ Winning tickets are typically sold by one lottery outlet, winners tend to be geographically clustered.
 - ▶ Incumbents receive significantly more votes in winning regions.
 - ▶ Temporary increase in happiness making voters more lenient toward the incumbent, or with a stronger preference for the status quo.

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 - ▶ Bad (incompetent, dishonest) types
- ▶ In the model, when voters learn about a politician's type, it affects their voting behavior
 - ▶ Is this true in practice?

Does the electorate respond to information about corruption?

Ferraz and Finan (2008): Exposing Corrupt Politicians: The Effects of Brazil's Publicly Released Audits on Electoral Outcomes

- ▶ Setting: municipal governments in Brazil
- ▶ Empirical idea:
 - ▶ Starting in 2003, the central government randomly selected 26-60 municipalities each month for audits, the results of which were made publicly available

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 - ▶ They then show that the effects are bigger if the media is stronger (information is more likely to get out)

Re-Election Rates by Corruption Level, with/without audit

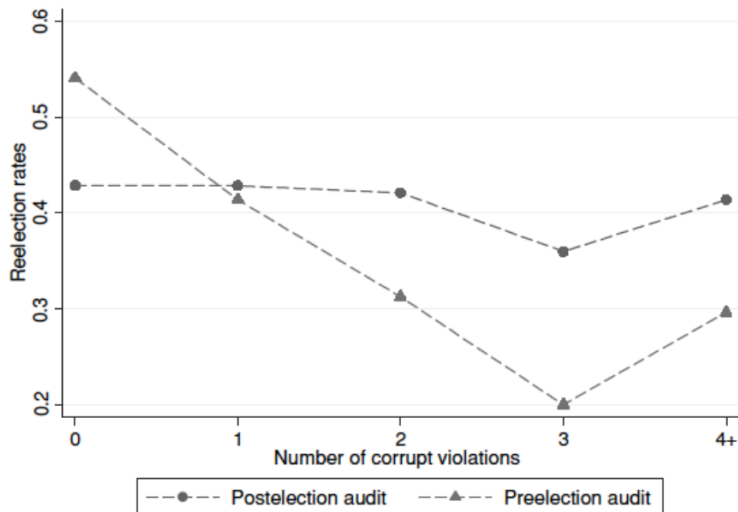


FIGURE III
Relationship between Reelection Rates and Corruption Levels

Bottom line of this paper

- ▶ Voters respond when given information about politician's performance

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- ▶ Voters respond when given information about politician's performance
- ▶ Do you view this as different from the paper on cash transfers?
 - ▶ How?

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- ▶ The final step in our analysis:
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- ▶ This paper asks: are politicians less corrupt if they are up for re-election?

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 - ▶ Mayors in Brazil have a two-term limit

The Next Step: How Politicians Respond

Ferraz and Finan (2011): Electoral Accountability and Corruption: Evidence from Audits of Local Governments

- ▶ The final step in our analysis:
 - ▶ Do politicians behave differently given that voters reward them for good behavior?
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- ▶ Setting: same municipal elections in Brazil
- ▶ Empirical idea:
 - ▶ Mayors in Brazil have a two-term limit
 - ▶ Compare first-term mayors (who face re-election) with second-term mayors (who don't).
 - ▶ Convincing?

Overall Results

TABLE 4—THE EFFECTS OF REELECTION INCENTIVES ON CORRUPTION

Dependent variable	Share of audited resources involving corruption							
	OLS (1)	OLS (2)	OLS (3)	OLS (4)	OLS (5)	OLS (6)	Matching (7)	Tobit (8)
Mayor in first term	−0.019 [0.009]**	−0.020 [0.010]**	−0.020 [0.010]**	−0.024 [0.011]**	−0.026 [0.011]**	−0.027 [0.011]**	−0.028 [0.010]**	−0.042 [0.012]**
R^2	0.01	0.08	0.10	0.12	0.14	0.20	n/a	n/a
Observations	476	476	476	476	476	476	476	476
Mayor characteristics	No	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Municipal characteristics	No	No	Yes	Yes	Yes	Yes	Yes	Yes
Political and judicial institutions	No	No	No	Yes	Yes	Yes	Yes	Yes
Lottery intercepts	No	No	No	No	Yes	Yes	Yes	Yes
State intercepts	No	No	No	No	No	Yes	Yes	Yes

- First-term mayors (who can run for re-election) are less corrupt than second term mayors (who cannot run for re-election)

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- ▶ This paper shows that politicians respond to re-election incentives, as they behave better when they can run for re-election
- ▶ Highlights role of elections in achieving accountability

Outline

Baseline Political Agency Model

Evidence on Elections as Selection and Incentive Device

- Voter Responses to Targeted Transfers

- Voter responses to information on corruption

- Politician Responses to Voter Accountability

Wages and Politician Performance

Do politicians' wages affect principal-agent problems?

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 - ▶ Selection: high wages may motivate different types of people to run for office

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 - ▶ By contrast, CEOs who manage billion-dollar companies are paid on the order of \$5 million - \$10 million
- ▶ Singapore is the main exception:
 - ▶ Pay is \$1.7 million USD, explicitly set to be comparable to top private-sector salaries, as a way of signaling high ability

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$$w + u_i > v_i$$

- ▶ Suppose that:
 - ▶ within the interested group, one person is randomly selected to become a politician
 - ▶ we care about some combination of v_i (correlated with competence) and u_i (correlated with idealism, public service)

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 - ▶ Do people with high private-sector returns tend to have higher or lower intrinsic motivation?
 - ▶ This is an empirical question; we'll have to look at the data.

Ferraz and Finan 2011, Motivating Politicians: The Impacts of Monetary Incentives on Quality and Performance

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 - ▶ Regression discontinuity design : salary caps are a function of municipal size
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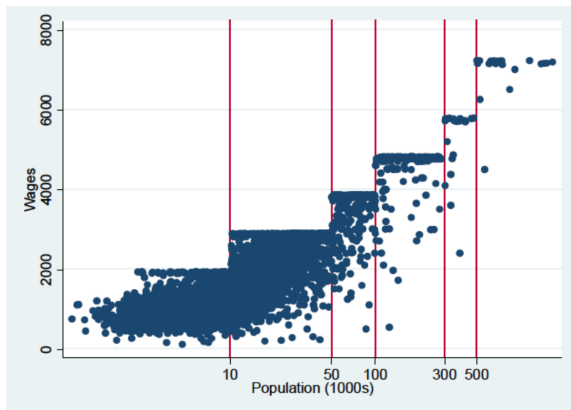
Politican Wage caps in Brazil

Table 1. Constitutional Amendment No. 25, 2000

Population bracket	Cap on salary as a percentage of state legislators salary	Value of maximum allowed salary in 2004	Cap on legislative spending as a proportion of revenues	Average legislative spending as a proportion of revenues	Cap on salary spending as a proportion of legislative spending
0 to 10,000	20%	1927.1	8%	3.6%	75%
10,001 to 50,000	30%	2890.6	8%	3.0%	75%
50,001 to 100,000	40%	3854.2	8%	2.8%	75%
100,001 to 300,000	50%	4817.7	7%	2.6%	75%
300,001 to 500,000	60%	5781.2	6%	2.7%	75%
500,000 plus	75%	7226.6	5%	2.6%	75%

- Constitutional amendment establishes salary caps for municipal legislators that depend on local population

First Stage: Population Cutoffs and Wages



- Actual wages of legislators vary with the population of the municipality

2SLS Estimation

- Estimate the following IV model:

$$w_i = \alpha_0 + \alpha_1 f_i + g(P_i) + \mu_i$$

$$y_i = \beta_0 + \beta_1 w_i + g(P_i) + \varepsilon_i$$

controlling for the different population cut-offs f_i and a flexible function $g(\cdot)$ of population P_i

Salaries Increase Effort

Table 5: The Effects of Wages on Legislative Performance

Dependent variable:	Number of Bills Submitted		Number of Bills Approved		Functioning Commission		Public events	
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
<u>Panel A: IV estimates</u>								
Wages	0.807 [0.238]***	0.672 [0.230]***	0.584 [0.125]***	0.515 [0.122]***	0.065 [0.025]***	0.062 [0.026]**	0.074 [0.033]**	0.06 [0.034]*
<u>Panel B: Reduced-form estimates</u>								
Salary caps	0.72 [0.220]***	0.621 [0.211]***	0.487 [0.109]***	0.429 [0.105]***	0.043 [0.020]**	0.04 [0.021]*	0.034 [0.029]	0.026 [0.029]
R-squared	0.18	0.2	0.15	0.17	0.02	0.03	0.03	0.04
Municipal characteristics	No	Yes	No	Yes	No	Yes	No	Yes
Observations	3544	3544	3544	3544	5093	5093	5093	5093

- In municipalities with higher legislator wages, legislative performance is higher

Evidence of Positive Selection

Table 7. The Effects of Wages on Political Selection

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
<u>Panel A:</u> Dependent variable	Years of schooling	No formal schooling	Some primary school	Primary school	Some high school	High school	Some college	College	High skilled occupation
Wages	0.495 [0.155]***	-0.023 [0.008]***	-0.016 [0.015]	-0.014 [0.012]	0.009 [0.008]	0.004 [0.016]	0.021 [0.007]***	0.017 [0.013]	0.043 [0.018]**
Observations	5091	5093	5093	5093	5093	5093	5093	5093	5093
<u>Panel B:</u> Dependent variable	Average terms of experience	1 term of experience	2 terms of experience	3 terms of experience	4 terms of experience	5 terms of experience	6 terms of experience	7 terms of experience	Male
Wages	0.154 [0.056]***	-0.047 [0.019]**	-0.007 [0.015]	0.03 [0.012]**	0.021 [0.008]**	0.005 [0.005]	0.003 [0.002]	0.000 [0.003]	-0.005 [0.010]
Observations	5093	5092	5092	5093	5092	5093	5093	5093	5093
Municipal characteristics	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes

Disentangling Selection from Incentives

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 - ▶ Do legislators perform better when they get paid more? (incentives)
 - ▶ Do we get better legislators when we pay more? (selection)
- ▶ I have some work on judge salaries trying to disentangle this.

The case of judge salaries: Incentives

- ▶ Ash and MacLeod (2015) look at impacts of changing the salary on appellate court judges in U.S. states:

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 - ▶ Panel data approach, looking at the within-judge impact to isolate incentive (as opposed to selection) effects.
 - ▶ Increases in salaries are associated with higher-quality work product: the decisions are cited more often by later judges.
- ▶ Consistent with a positive incentive effect of salaries, reducing the need to engage in outside activities that distract from judging.

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 - ▶ Judges selected under higher salaries actually have *lower* work quality
 - ▶ consistent with a lower intrinsic motivation for judges motivated by money
- ▶ Shows that the positive-selection effect from Ferraz and Finan (2011) is domain-specific.