Does opportunism pay off?

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Abstract

In Portugal, increases in investment expenditures and changes in the composition of spending favouring highly visible items are associated with higher vote percentages for incumbent mayors seeking re-election. The political payoff to opportunistic spending increased after democracy became well-established in the country.

Keywords: Voting functions; Opportunism; Local governments; Elections; Portugal

JEL classification: D72; H72

1. Introduction

The objective of this article is to determine whether opportunistic mayors can increase their chances of re-election[1] by generating political budgetary cycles around elections. We test the hypothesis that pre-electoral increases in municipal expenditures and changes in their composition, favouring items most visible to or preferred by the electorate, are associated with higher vote percentages for the incumbent mayor. Research is conducted over a dataset comprising all Portuguese mainland municipalities, from 1979 to 2001.

In previous work, Veiga and Veiga (2007) found strong evidence of political budgetary cycles in Portuguese municipalities. They also showed that electoral cycles were stronger for investment items highly visible to the electorate, for example, construction spending on public infrastructure. Given these results, it would also be

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[1] For a literature review on vote and popularity functions see Paldam (2004).

interesting to know if voters reward (or punish) politicians' opportunistic spending policies. Additionally, because democracy was reestablished in Portugal in 1974, during our sample period the country has evolved from a "new" to an "established" democracy. This makes Portugal an appropriate laboratory for analyzing if the determinants of electoral results change as a democracy matures.

There are several other reasons that make Portugal an interesting case for study. First, we have very detailed data on local governments' financial accounts. Second, the mayor is a principal decision-maker in the allocation of resources and the distribution of investment in the municipality. Third, the institutional structure of local governments and the policy instruments available are the same for all Portuguese localities. Finally, election dates are fixed and defined exogenously from the perspective of the local authorities, and all municipalities have elections on the same day.[2]

2. Data, model specification and results

The dataset is composed of data on a set of political, financial and economic variables for 275 Portuguese mainland municipalities, for years from 1979 to 2001.[3] Since this article tries to determine whether or not political opportunism by mayors pays off, only the cases in which they run for re-election are considered.

The two models used in the empirical work are specified as follows:

$$\text{Votes}_{it} = \alpha \text{Votes}_{i,\text{prev.el.}} + \phi \text{YM}_{it} + \gamma \text{GP}_{it} + \beta_1 \text{IE}_{it} + \beta_2 \text{IE}_{i,t-1} + \beta_3 \text{IE}_{i,t-2} + v_i + \varepsilon_{it} \quad (1)$$

$$\text{Votes}_{it} = \alpha \text{Votes}_{i,\text{prev.el.}} + \phi \text{YM}_{it} + \gamma \text{GP}_{it} + \beta_1 \text{IEtm}_{it} + \beta_2 \text{IEdev}_{it} + v_1 + \varepsilon_{it} \quad (2)$$

$$i = 1,\ldots,275 \quad t = 1979,1982,1985,1989,1993,1997,2001$$

where Votes_{it} is the percentage of votes obtained by the incumbent's party in the municipality i, in election of year t, $\text{Votes}_{i,\text{prev.el.}}$ is the percentage of votes obtained in the previous election, YM_{it} stands for *Years Mayor* (the number of years the mayor of municipality i has been in office), GP_{it} is a measure of *Government Performance/Popularity*,[4] IE are levels of real per *capita Investment Expenditures* (in the election year, t; the year before elections, $t-1$; and 2 years before elections, $t-2$),[5] IEtm is its term

[2] During the sample period, there were local elections in 1979, 1982, 1985, 1989, 1993, 1997 and 2001, always in December.

[3] Election dates and municipal electoral results were obtained from STAPE, Portugal. The government popularity index is based on monthly surveys published in the newspaper *Expresso*, from 1986 to 2001. Data on municipal accounts and population, from 1979 to 2001, were obtained from DGAL, Portugal. Data on the total number of employees in firms within each municipality and on their average wages, since 1985, were obtained from the Portuguese Ministry of Labour and Social Solidarity. Finally, the consumer price index was obtained from the OECD's *Main Economic Indicators*.

[4] *Government Performance* is accounted for by the following two interaction variables: *Government's Party*Inflation Rate*; and, *Government's Party∗Government Popularity*. The dummy variable *Government's Party* takes the value of one when the mayor's party is the same as that of the Prime Minister, and equals zero otherwise. By interacting this variable with the *Inflation Rate or Government Popularity*, we account for the possibility that the votes for an incumbent mayor whose political party is in charge of the national government are affected by the performance/popularity of the latter.

[5] Since the first terms were only 3-years long, when working with the full sample it is not possible to include the level of expenditures 3 years before elections. In the estimations, lags that turned out as not statistically significant were sequentially excluded.

Table 1
Investment expenditures

Votes	1979–2001		1979–1989		1990–2001		1986–2001
	1	2	3	4	5	6	7
Votes (previous election)	0.447	0.459	0.445	0.486	0.233	0.220	0.149
	(10.9)***	(11.2)***	(6.71)***	(5.27)***	(3.41)***	(3.18)***	(2.69)***
Years Mayor	−0.836	−0.850	−1.664	−1.672	−0.772	−0.782	−0.837
	(−10.7)***	(−10.9)***	(−9.22)***	(−6.54)***	(−6.77)***	(−6.85)***	(−8.80)***
Government's Party*	−0.172	−0.173	−0.279	−0.206			
Inflation Rate	(−3.75)***	(−3.81)***	(−5.23)***	(−2.70)***			
Government's					0.068	0.070	0.034
Party*Government Popularity					(3.31)***	(3.37)***	(1.95)*
Investment expenditures							
Election year	0.008		0.014		0.013		0.012
	(2.01)**		(1.73)*		(3.21)***		(3.27)***
Term mean		0.017		0.005		0.020	
		(3.88)***		(.34)		(3.21)***	
%Deviation of election year		018		0.017		0.0029	
from the term mean		(1.71)*		(.63)		(2.12)**	
Employment							0.0124
							(1.12)
Real wages							0.0026
							(3.29)****
# Observations	1128	1136	597	486	650	650	839
# Municipalities	275	275	261	259	274	274	275
# Elections	6	6	4	3	3	3	4
Adjusted R^2	0.037	0.037	0.036	0.033	0.040	0.041	0.036

Notes: Panel regressions, for election years, controlling for municipality fixed effects. Votes, the dependent variable, was defined as the percentage of votes obtained by the incumbent. Models estimated with a constant. *T*-statistics based on heteroskedastic consistent standard errors are in parenthesis. Significance level at which the null hypothesis is rejected: ***, 1%; **, 5%, and *, 10%.

mean, IEdev is the percentage deviation of the election year level from the term mean,v_i is the individual effect of municipality i, ε_{it} is the error term, and, α, ϕ, γ, β_1, β_2 and β_3 are parameters to be estimated.

The estimation results of the panel data models described above, controlling for municipality fixed effects, are shown in Table 1. Results for the full sample are consistent with the hypothesis that pre-electoral manipulation of investment expenditures leads to a higher percentage of votes cast for the incumbent mayor. Expenditures in the election year are statistically significant, with a positive sign (column 1),[6] and the same applies to the term mean and to the percentage deviation of the level of the election year relative to the term mean (column 2).[7] There is also evidence of systematic popularity erosion over time (sometimes referred to as a "cost of ruling"), and support for the hypothesis that mayors belonging to the prime minister's party lose votes when inflation is high.

[6] Levels for *Investment Expenditures* in previous years are not statistically significant when included.

[7] In the longer working paper version of this article (Veiga and Veiga, 2006), we also report estimation results for models including budget balances, taxes, total expenditures, and current and capital expenditures. Evidence that opportunism pays off was found for total and for capital expenditures. Since it was for investment expenditures that Veiga and Veiga (2007) found greater evidence of political business cycles, only the results obtained for those are reported in the present paper.

There may be an endogeneity problem in this regression. It is possible that the popularity of the mayor affects the size of the opportunistic cycle: when certain of winning by a large margin, she does not need to engage in the manipulation of expenditures;[8] but, when confronted with a close race, she has the greatest incentive to behave opportunistically. However, even when a mayor does not expect a close race, she may still want to increase expenditures shortly before elections, in order to elect as many deputies as possible in the Town Hall and in the Municipal Assembly. Thus, the endogeneity bias may be small.[9]

In order to determine if expenditure manipulation affected votes in the same manner throughout time, we split the sample into two parts. Results shown in columns 3 and 4 imply that opportunistic spending was not highly vote-productive in the period 1979–1989, as investment expenditures are only marginally statistically significant in column 3 and no effects of opportunism on votes are found in column 4. But, results for the period 1990–2001 are stronger than for the full sample. Thus, electoral manipulation of the timing of spending had higher pay off as the Portuguese democracy became more established after its restoration in 1974. In these estimations, there is also evidence that government's popularity ratings affect the votes obtained by mayors of the government party.[10]

The increasing importance of fiscal performance on voters' decisions over time is in line with Brender's (2003) findings for Israel. It may result from a shift in voters' concerns away from ideological issues to economic ones, as democracy matured, leading to a greater sensitivity of voters to the budget cycle. But, contrary to Brender, who found evidence that the Israeli electorate started penalizing incumbents for loose fiscal policy as democracy matured, our results suggest that the political pay off to opportunistic spending increased after democracy became well-established in Portugal. A possible explanation for this result is that, as the Portuguese democracy matured, politicians learned how to take advantage of electoral institutions and, unlike in Israel, no significant measures were implemented to increase the transparency of local governments' accounts. In this respect, it is worth mentioning that Alt and Lassen (2006), working on a sample of advanced industrialized economies, identified a persistent pattern of electoral cycles on low(er) transparency countries, while no such pattern could be observed in high(er) transparency countries.

The next step of the empirical analysis was to include variables accounting for the economic performance of municipalities. In column 7, municipal *Employment* and average real *Wages* were included along with *Investment Expenditures*. Results for the latter are very similar to those of column 5. While *Employment* does not seem to affect votes, higher *Wages* in the election year lead to greater percentages of votes for the incumbent.[11]

In the estimations of Table 2, investment expenditures are broken up into their seven components. In column 1, only *Other Buildings* and *Miscellaneous Constructions* are statistically significant. These results were expected, as these are the most important and most visible components of *Investment*

[8] Although the incentive for opportunistic behavior may also be small for those who are certain of losing, they generally decide not to run for re-election and, consequently, most of them are not included in our sample.

[9] Since only the mayors who run for re-election are considered, most of the cases in our sample in which there is not a close race correspond to situations in which the mayor is sure of winning. Consequently, our estimates are likely to underestimate the causal relationship between opportunistic cycles and popularity.

[10] The variable (*Government's Party*Government Popularity*) was not included in the previous estimations because popularity data are only available after 1986.

[11] Since data for unemployment and wages are only available after 1985 and that for government popularity after 1986, only the elections that occurred between 1986 and 2001 are covered in this estimation.

Table 2
Components of investment expenditures

Votes	1	2
Votes (previous election)	0.0335 (6.42)***	0.0298 (5.67)***
Years Mayor	−0.0887 (−9.72)***	−0.0889 (−9.71)***
Government's Party*Inflation Rate	−0.0146 (−2.05)**	−0.0185 (−2.64)***
Main components		
Acquisition of land: election year	0.0025 (0.074)	
Housing: election year	0.0017 (1.07)	
Other buildings: year before election	0.0039 (2.95)****	
Miscellaneous constructions: election year	0.0011 (2.46)**	
Transportation material: election year	0.0098 (1.39)	
Machinery and equipment: election year	0.0036 (.75)	
Other investments: election year	0.0021 (0.053)	
Components of *other buildings*		
Sports, recreational and schooling facilities: election year		0.0003 (0.22)
Social equipment: election year		0.0105 (1.97)**
Other: year before election		0.0056 (3.12)***
Components of *miscellaneous constructions*		
Overpasses, streets and complementary works: year before election		0.0030 (2.12)**
Sewage: election year		−0.0023 (−1.05)
Water treatment and distribution: election year		−0.0030 (−1.84)*
Rural roads: election year		0.0019 (2.44)**
Infrastructures for solid waste treatment: election year		0.0047 (1.11)
Other miscellaneous constructions: election year		0.0002 (0.33)
# Observations	934	930
# Municipalities	275	275
# Elections	5	5
Adjusted R^2	0.032	0.033

Notes: Panel regressions, for election years, controlling for municipality fixed effects. Votes, the dependent variable, was defined as the percentage of votes obtained by the incumbent. Models estimated with a constant. *T*-statistics based on heteroskedastic consistent standard errors are in parenthesis. Significance level at which the null hypothesis is rejected: ***, 1%; **, 5%, and *, 10%.

Expenditures. Since we have very detailed data on the municipal accounts, we are able to disaggregate *Investment Expenditures* even further, in order to analyze the three components of *Other Buildings* and the 6 components of *Miscellaneous Constructions*. Results shown in column 2 indicate that votes can be gained by increasing expenditures in the election year (or in the year before, in some cases) in *Social Equipment*, *Other*, *Overpasses*, *Streets and Complementary Works*, and in *Rural Roads*.

3. Conclusions

Results indicate that higher investment expenditures in election years are associated with higher vote percentages for incumbent mayors in Portuguese municipalities. This finding is in line with the evidence presented by Akhmedov and Zhuravkaya (2004) for Russian regions. We also find that opportunistic spending was more vote-productive after Portugal became an established democracy than it had been when democracy was newly established. This may be a result of a lack of transparency regarding local fiscal policies combined with the acquisition of knowledge by politicians, and with a greater sensitivity of Portuguese voters to the budget cycle, as democracy matured.

Electoral manipulation can also be accomplished by altering the composition of expenditures, as suggested by Drazen and Eslava (2005). Our results show that opportunistic mayors should spend relatively more on: *Social Equipment*; *Other*; *Overpasses*, *Streets and Complementary works*; and, *Rural roads*. With the exception of *Social Equipment*, it was exactly for these components of investment expenditures that Veiga and Veiga (2007) found greater evidence of political budgetary cycles.

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