Aiding Elections? Foreign Aid and Donor-Country Election Cycles

Michael Batu (University of Windsor)
Darren Larue (University of Windsor)

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by

Michael Batu
Department of Economics
University of Windsor
401 Sunset Avenue
Windsor, Ontario
Canada N9B 3P4
mbatu@uwindsor.ca

Darren Larue
Department of Economics
University of Windsor
401 Sunset Avenue
Windsor, Ontario
Canada N9B 3P4
larued@uwindsor.ca

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Abstract

We provide empirical evidence for a causal donor election cycle effect on some types of foreign aid. Our identification strategy exploits the variation in foreign aid for donors with fixed election dates, making elections clearly exogenous.

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1. Introduction

Called "political election cycle effect", Nordhaus (1975) pioneered the idea that incumbent politicians often employ expansionary fiscal policies before elections to increase their re-election chances. Drazen (2008) offer two explanations for this phenomenon: first, voters like low taxes and high government expenditures, and therefore elect incumbents who provide them; and second, voters respond to good economic conditions by being more likely to vote for the incumbent. Regardless of the explanations, because voters do not observe all government expenditure, there is an incentive for politicians to increase spending in areas that voters can observe (Annen and Strickland, 2018). For the case of spending on foreign aid, the motivations for strategically spending before an election are slightly different and somewhat complicated. First, voters in the donor country may view the capacity to provide foreign aid as an indicator of the incumbent government's ability to influence the world globally (Annen and Strickland, 2018). Second, incumbents can use foreign aid spending to attract certain types of voters. For instance, foreign aid spending intended for the promotion of women's rights may appeal to voters who care about gender quality issues. Indeed, we find evidence to support the view that governments increase spending for certain types of aid before an election.

Our work is related to the literatures on the determinants of foreign aid and political election cycles. Here, we cite a few relevant papers. Faye and Niehaus (2012) looked at political

aid cycles by linking aid flows with elections in recipient countries. They show that donors use bilateral aid to influence elections in recipient countries. Rashky and Schwindt (2012) found that a donor country's decision on the channel and type of post-disaster assistance is mainly driven by the quality of institutions in the recipient country, as well as strategic trade and natural resource interests, where humanitarian aspects play only a minor role. In contrast to these papers, we carefully consider that political election cycles may be endogenous to foreign aid. By exploiting the variation in foreign aid for countries with fixed election dates, we find a significant causal election cycle effect for some types of aid.

2. Empirical strategy

Our hypothesis is that incumbent governments would increase the allocation for aid categories that would raise their re-election chances. For instance, politically important categories like infrastructure aid or production aid may increase prior an election. This hypothesis can be empirically tested by running a regression with log of foreign aid share with respect to total ODA ('aid') as the dependent variable and an election dummy ('election') as the main explanatory variable

$$\text{aid}^{j}_{i,t} = \beta_0 + \beta_1 \text{election}_{i,t-1} + \gamma X + \mu_i + \gamma_t + \varepsilon_{i,t} \tag{1}$$

where i indexes the donor country, j indexes the type of aid, and donor and year fixed effects are μ and γ, respectively. The *election* dummy variable assumes a value of 1 if an election occurs in the previous year. The parameter β_1 captures the political election cycle effect which we expect to be positive and statistically significant. The vector X include control variables like party affiliation and lag real income per capita of the donor country.

It is possible that the election dummy variable is endogenous to foreign aid. For instance, donor governments may choose the date of their elections to correspond with high levels of voter support generated by social issues or the strength of the country's economy (Annen and Strickland, 2018). If not taken into account, the endogenous relationship between foreign aid and elections may lead to biased estimates for β_1. Hence, as in Annen and Strickland (2018), we address the endogeneity problem by running regressions with two samples, donors with constitutionally fixed election dates and donors without fixed election dates.

3. Data

Our data on the national elections in donor countries comes from the National Elections Across Democracy and Autocracy (NELDA) database. The NELDA dataset includes information on more than 2600 election events in 157 countries from 1945-2012 (Hyde and Marinov, 2012). In line with the current literature, we focus on elections where the leader of the country's government is elected. We obtain the data on Official Development Assistance (ODA) from the OECD's DAC database. Our study focuses on the following categories of ODA:

- Debt relief is any form of debt reorganisation which relieves the overall burden of debt (i.e. debt forgiveness, rescheduling, refinancing).

- Infrastructure aid covers assistance for networks, utilities and services that facilitate economic activity.

- Humanitarian aid is used for the purposes of disaster prevention and preparedness, reconstruction relief, relief coordination, protection and support services, emergency food aid and other emergency/distress relief.

- Multi-sector aid is intended for projects which straddle several sectors, with a concentration on the environment, gender projects and urban and rural development.

- Production aid is applied to all directly productive sectors.

- Program aid is support for the implementation of macroeconomic reforms (structural adjustment programmes, poverty reduction strategies); general programme assistance (when not allocable by sector).

- Social infrastructure aid covers efforts to develop the human resource potential and ameliorate living conditions in aid recipient countries.

Foreign aid data used in our study are expressed in per capita and in 2015 constant prices. Additional donor variables such as unemployment and real GDP were sourced from the OECD statistics database. The descriptive statistics for the seven categories of ODA, elections, and control variables are summarized in Table 1.

4. Results

Table 2 Panel A presents our regression results for equation (1) using the full sample of countries. In all the regressions we obtain a positive coefficient for the election dummy variable, which is consistent with our hypothesis of different types of foreign aid being affected by political election cycles. Most of the estimated coefficients for the elections dummy are significant at the 1% level. Of the different types of aid, social infrastructure aid is the most responsive to election cycles while program assistance is the least responsive. The results indicate that foreign aid for social infrastructure increases by 12 percentage points one year before an election. In contrast, humanitarian aid increases only by 2 percentage points one year before an election.

It is possible that the results in Panel A are biased because of the endogenous relationship between foreign aid and elections. Hence, we ran a separate regression shown in Table 2 Panel B for equation (1) but only for countries with fixed elections. Notable is the reduction in the size of the estimated coefficient for the election dummy compared to the estimates in Panel A. The reduction in the size of the coefficients suggests an upward bias. Debt relief aid, humanitarian aid, production aid, and program assistance aid lost their statistical significance in the fixed election sample relative to the results from the full sample. The estimated coefficient for elections for other types of aid remained positive but only significant at the 5 percent level.

Income of the donor country is one of the most important determinants of aid. Also, it is well known that left-leaning spend more than right-leaning governments. Hence, we include lagged real GDP per capita and the political party affiliation variable in the donor country in the regressions. As shown in Table 3, including GDP and political party in the regressions failed to change the signs of the estimated coefficients for the full donor sample and the estimated coefficients are significant at the 1% level. However, some of types of aid lost their statistical significance. As in Table 2, only economic infrastructure aid, multisector aid, and social infrastructure aid remain statistically significant at the 5% level.

5. Conclusion

This paper enriches the literature on the political determinants of different types of aid with the literature on political election cycle effect by arguing that donor countries increase the amount of humanitarian assistance to recipient countries in the years prior to an election to increase voter support. The results of the regression analysis appear to support this theory.

As in Annen and Strickland (2018), we want to emphasize that although we find election cycle effect in the different types of aid, this effect only explains a tiny part of the total variation in humanitarian aid observed in the data.

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Table 1: ODA descriptive statistics.

Variable	Observations	Levels (in mil. 2015 USD)		Share of ODA	
		Mean	Std. Dev.	Mean	Std. Dev.
Debt Relief	287	492.84	900.45	0.14	0.16
Economic Infrastructure	321	613.91	1145.00	0.12	0.09
Humanitarian	320	329.27	778.56	0.09	0.06
Multi-Sector	320	338.74	461.87	0.10	0.06
Production	321	303.60	428.81	0.09	0.04

Program Assistance	314	205.78	403.16	0.05	0.05
Social Infrastructure	321	1,567.56	2,631.33	0.41	0.12

Source: OECD.

Table 2: Elections and types of foreign aid.

Dependent variables (in logs):	Debt relief	Economic infrastructure	Humanitarian	Multisector	Production	Program assistance	Social infrastructure
PANEL A: Full sample							
Election Dummy	0.025	0.051***	0.022**	0.037***	0.030***	0.009	0.121***
	(0.019)	(0.014)	(0.009)	(0.009)	(0.007)	(0.006)	(0.029)
N	281	281	281	281	281	281	281
Adjusted R^2	0.631	0.555	0.684	0.578	0.620	0.498	0.685
PANEL B: Fixed elections only							
Election Dummy	0.018	0.0251**	0.015	0.027**	0.008	-0.005	0.091**
	(0.027)	(0.014)	(0.013)	(0.014)	(0.008)	(0.007)	(0.049)
N	126	126	126	126	126	126	126
Adjusted R^2	0.508	0.639	0.823	0.712	0.718	0.605	0.734

Note: All regressions include donor and year fixed effects. Robust standard errors in parentheses. Significance levels: * 10%; ** 5%; *** 1%.

Table 3: Elections and types of foreign aid with additional controls.

Dependent variables: (in logs)	Debt relief	Economic infrastructure	Humanitarian	Multisector	Production	Program assistance	Social infrastructure
PANEL A: *Full sample*							
Election Dummy	0.011***	0.046***	0.021***	0.034***	0.027***	0.006***	0.091***
	(0.020)	(0.014)	(0.008)	(0.009)	(0.007)	(0.006)	(0.021)
Party Affiliation Index	0.000***	0.000***	-0.000***	-0.000***	-0.000	0.000***	0.000***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
Change in real GDP per capita (t-1)	0.016**	0.001	0.008***	0.009***	0.005**	0.004***	0.046***
	(0.005)	(0.003)	(0.002)	(0.002)	(0.002)	(0.001)	(0.007)
N	268	268	268	268	268	268	268
Adjusted R^2	0.556	0.560	0.733	0.624	0.635	0.549	0.765
PANEL B: *Fixed elections only*							
Election Dummy	0.006	0.026**	0.015	0.024**	0.009	-0.006	0.068**
	(0.027)	(0.014)	(0.012)	(0.013)	(0.007)	(0.007)	(0.044)
Party Affiliation Index	0.000	0.000***	-0.000***	-0.000***	-0.000***	0.000***	0.000***
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
Change in real GDP per capita	0.029***	0.001	0.004	0.005	0.003	0.002	0.033***
	(0.009)	(0.004)	(0.002)	(0.003)	(0.002)	(0.001)	(0.010)
N	120	120	120	120	120	120	120
Adjusted R^2	0.674	0.657	0.840	0.753	0.749	0.631	0.803

Note: All regressions include donor and year fixed effects. Robust standard errors in parentheses. Significance levels: * 10%; ** 5%; *** 1%.