Partisan Politics in International Financial Rescues

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Motivation

- Negotiations over international financial rescues are difficult
- States in economic distress need financing, but at what cost?
- Conditions require policy reforms in exchange for loan
Motivation

• When do borrowers’ preferences matter?

• When borrowers encounter “co-partisans” on the IMF EB, they are more likely to get what they want
Focus

• Our focus is on a specific lender: IMF
• The IMF provide a “hard test” of co-partisan hypothesis
• In theory, IMF is non-partisan
  – Yet there is abundant evidence that IMF lending is heavily politicized by large shareholders’ interests
  – Partisanship as additional political factor shaping large shareholders’ lending preferences
Argument

• Partisan politics play out via national-level appointment of Executive Directors (EDs)
  – Executive Board is composed of 24 EDs
  – EB approves all loans
  – US, Japan, Germany, France and the United Kingdom each appoint their own ED
  – G5 EDs are appointed by national governments
    • In the UK, for example, the Prime Minister appoints the British Director
  – Left governments appoint left-leaning directors
Argument

• G5 Directors can be more or less left-leaning, depending on the parties in power at home
• G5 are more lenient with “co-partisan” borrowers
• Borrowers’ preferences are more influential when negotiating with the IMF in the shadow of “co-partisan” approval
Argument

• Focus on loan conditions as the key outcome of negotiations
  – Labor-related conditions
    • “Reduce the 1st grade public sector wage from 91,000 BYR to 77,000 BYR” (Belarus 2008 prior action)
    • “Cut at least 5,500 positions in the education sector” (Bulgaria 2006 benchmark)
    • “The monthly minimum wage is not to exceed 160 BGN” (Bulgaria 2006 performance criteria)
The politics of labor conditions

• Left governments resist labor conditions
• Left-leaning Directors will be sympathetic to demands for less stringent labor conditions
• Hypothesis: Loans negotiated between left borrowers and a left IMF will contain fewer labor conditions, all else equal
Data

• Sample: all non-concessional IMF borrowers from 1983-2012 (N=146-156, 39-42 countries)

• Dependent variable: # of labor conditions
  – Various permutations: % of total conditions, # of labor-related prior actions and performance criteria, count/log of labor conditions, etc.
Data

- Sample: all non-concessional IMF borrowers from 1983-2012 (N=146-156, 39-42 countries)
- Dependent variable: # of labor conditions
- Key independent variables:
  - Partisanship of borrower (chief executive)
    - World Bank DPI classification (1=right; 3=left)
  - Vote-weighted partisanship of the G5 countries
  - Interaction of the two
Results

- Marginal effect of a left borrower on labor conditions is negative when G5 Directors are also left-leaning
Conditional Marginal Effect of Left Borrower by G5 Partisanship (Labor-related conditions, % of total)
Conclusions

• Partisanship affects both the demand for and supply of IMF conditionality
• Loans approved by IMF EB for “co-partisan” borrowers differ from those approved for other countries
• Elections in one country can affect policy reforms in other countries via IMF conditions
Thank you!

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## G5 Partisanship and IMF Conditionality (unconditional)

<table>
<thead>
<tr>
<th>Variable</th>
<th>$G5\ DPI = 1$ (Right)</th>
<th>$G5\ DPI = 1.6$</th>
<th>$G5\ DPI = 2.7$ (Left)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total labor-related conditions</td>
<td>0.1</td>
<td>0.3</td>
<td>3.5</td>
</tr>
<tr>
<td>Labor-related conditions (% of total)</td>
<td>0%</td>
<td>4.2%</td>
<td>11.5%</td>
</tr>
</tbody>
</table>
Conditional Marginal Effect of G5 Partisanship by Left Borrower (Labor-related conditions, % of total)
Implications

• Debate exists in the literature as to whether borrowers interests converge or diverge from those of the IMF
  – Often assumed that a conflict of interest over conditionality exists between the IMF and borrowing governments (e.g. Pop-Eleches 2009)
  – Yet others argue that borrowers and the Fund have convergent interests (e.g. Vreeland 2003)

• We resolve these conflicting expectations by theorizing as to when disagreement is most likely
Implications

• Affinity is too narrowly defined
  – “Geopolitical” affinity: measured by looking at the similarity of UN voting
  – Geopolitical affinity reduces the total number of conditions (e.g. Stone, Vreeland, Dreher, etc.)
  – Ideological affinity also matters

• International negotiations are two-sided
  – Studies often focus more attention on one side (e.g. Rickard & Caraway)
  – We examine the effects of partisanship on both sides
Conditional Marginal Effect of G5 Partisanship by Left Borrower (Labor-related conditions, log)
Labor conditions

• Public sector wages
• Public sector employment
• Privatization
• Minimum wages
• Private sector wages
• Pensions
• Social security
• Labour market flexibility
• Collective bargaining decentralization
Further implications

• Elections in one country can affect policy outcomes in other countries
• IMF transmits national-level partisan politics across the world