

**Local Parties and Local Politics:  
Electoral Fragmentation and Municipal Budget Choices in Bolivia<sup>1</sup>**

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**ABSTRACT:** Recent work on the effects of fiscal federalism suggests that the effect of decentralization on public good provision and fiscal restraint are largely determined by the social and political context in which the decentralization occurs. This paper extends this work by showing that the outcome of decentralization is contingent upon the patterns of political competition that develop in the local political arena following decentralization. Political competition may generate incentives for efficiency or inefficiency. Following Chhibber and Nooruddin (2004), we expect that both extremely low and extremely high levels of electoral fragmentation in sub-national elections will generate incentives for clientelism, corruption, and indebtedness. Investments in public goods, in contrast, will tend to be highest when a moderate number of parties seek office. Patterns of government employment and revenue trends in Bolivian municipalities following political and fiscal decentralization reforms in the mid 1990s conform to the expected pattern. Thus while the development of competitive local elections plays an important role in shaping the outcome of decentralization, the type of competition that develops determines the nature of that effect.

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A recent trend in public administration has been the increased decentralization of public finance, taxation authority, and policy implementation from national governments to provincial and even municipal entities (See Gerber and Kollman 2004). As a result, sub-national government expenditures have tripled since 1972 (author's calculation from World Bank 2000) and local governments now provide the majority of public infrastructure (such as sewage, water, electricity, and roads) in most countries (Shah 1997, 9). Often these reforms have entailed the creation of new local administrative units and the implementation of elections to select local officials for the first time (Grindle 2000).

Decentralization can result, however, in either improved government efficiency and responsiveness or in the creation of local authoritarian "brown areas." The specific outcome of empowering local governments depends upon the calibration of incentives for sub-national officials using fiscal instruments and the explicit delimitation of authority (see Oates 1999). A general consensus has also emerged that competitive local elections induce governments to behave "responsively," which is then linked to increased efficiency in the allocation of resources, lower levels of fiscal mismanagement and waste, and increased investment in public goods (e.g. Manor 1999, Crook and Manor 1998, Agrawal and Ribot 1999, Hiskey 2005, c.f. Cleary 2007).

In this article, however, we propose an additional and largely overlooked factor that determines the outcome of decentralization reforms: the nature of the competitive environment facing politicians. Elections can either create incentives to emphasize public goods, restrain the predatory use of the state, and maintain fiscal balance, or not. Politicians' strategic choices are dictated by the demands placed on them by their constituents and the nature of the constituency

coalition necessary to win election. Building on work by Bueno de Mesquita et al (2000) and Chhibber and Nooruddin (2004), we argue that the impact of fiscal and political decentralization on the provision of public policy and on fiscal management is thus contingent upon the type of local party systems that develop following decentralization, a factor which has received very little attention in the debate surrounding federalism. Local governments will be more likely to emphasize clientelism and allow financial mismanagement if electoral competition is either limited or extremely fragmented. Sub-national governments operating in a moderately fragmented environment will be more likely, in contrast, to emphasize public good and exercise fiscal restraint. These predictions are tested in the context of Bolivia's 1994 decentralization.

### **The Contingent Effects of Decentralization**

Advocates of administrative and political decentralization argue that it leads to public policy provision that is efficient and responsive to constituent preferences. A variety of mechanisms have been cited that potentially lead to these effects. For example, decentralized policy provision and revenue collection may create incentives for governments to compete with other localities for investment (Tiebout 1956, Oates 1972, Jones Luong 2003),<sup>2</sup> allow localities to receive the mix of goods that they desire instead of uniform policy (Oates 1999, Faguet 2004), or enhance government transparency (Crook and Manor 2000). Political and economic decentralization also enhance democracy by providing avenues to power for new political actors, increasing the influence and organizational capacity of civil society, and increasing trust in government (Diamond 1999, chapter 4; Grindle 2000; Vetter 2002).

Despite these grandiose expectations in the abstract, however, decentralization in practice has a mixed empirical record. Imperfect monitoring creates incentives for both the center and provinces to either shirk their responsibilities or to encroach on the other level of administration

(Bednar 2004). Local government officials often lack training and expertise (Barrilleaux et al 1992). If decentralization occurs without clear mechanisms for monitoring public officials, it can create “brown areas” where local political elites are unchecked and graft and clientelism flourish (Weingast 1995, Treisman 2000, O’Donnell 1999, Bardhan and Mookherjee 2000, Prud’homme 1995). And if local governments do not invest in capital creation nor practice fiscal discipline, decentralization can undermine macroeconomic reforms undertaken by the national governments (e.g. Remmer and Wibbels 2000) and slow economic growth (e.g. Wibbels 2001, Davoodi and Zou 1998, Zhang and Zou 1998). Differences in the investment choices made by local governments also impact the quality of life for residents in them; while decentralization in Bolivia has resulted in reduced poverty, these gains were reduced in municipalities that had public sector debts and which did not focus investment in public good provision (Singer n.d.).

As a result, there is an ongoing debate over whether federalism represents a “Panacea or a Pandora’s Box” for government performance (Gurgur and Shah 2000). However, recent work suggests that federalism offers both “Promises and Perils” (Rodden 2005) depending upon the way it is implemented and the incentives that local government officials have to respond to demands for efficient policy outcomes. Local governments can be induced to exercise fiscal constraint, for example, if constitutional rules prevent central governments from bailing out local government debts, thus creating hard budget constraints (See Roden 2005 for a review). Similarly, sub-national governments have greater incentives to cater to local constituents if they raise their revenues through locally-generated taxes instead of through transfers from the central government (Hines and Thaler 1995, Remmer and Wibbels 2000, Rodden and Wibbels 2002).

Finally, the election of local officials can provide a direct way for citizens to ensure governmental accountability and responsiveness. Elections are not sufficient to ensure that

programs will be managed in accordance with local wishes (Agrawal and Ribot 1999, Cleary 2007), but they are commonly cited as a necessary condition to ensure that local citizenry can induce politicians to be responsive to their needs while sanctioning politicians who engage in negative practices (e.g. Echeverri-Gent 1992, Fiszbein 1997, Blair 2000, Crook and Manor 1998, Manor 1999). Specifically, it is commonly claimed that localities in which elections are competitive will outperform those in which competition is restricted (e.g. Beer 2003, Hiskey 2003). Local governments who oversee rising corruption are replaced (Henderson and Kuncoro 2006) while the threat of electoral sanction, made credible by the existence of a strong opposition, induces local governments to focus on good management. If the threat of electoral defeat is removed, corruption and mismanagement flourishes (Wise 2006).

Competitive elections, however, may not always lead governments to provide public goods or behave responsibly. Instead, elections may induce politicians to manipulate financial markets (Veiga and Veiga 2007), engage in corruption to fund campaigns (Gingerich 2006), or expand the public employment lists to reward supporters (Remmer 2007). Electoral competition only provides incentives for politicians to act with anticipation of electoral evaluation-the content of those actions is a function of the social and political context in which elections are conducted (Austin-Smith 2000). Thus to understand the trajectory of decentralization, we need to consider the context in which it is enacted and the subsequent incentives for local government behavior. Specifically, we argue in the next section, the impact of political and economic decentralization should be a function of the nature of the type of party competition that exists in a locality.

### **Local Electoral Competition and Policy Choices**

Generally speaking, there are two ways for politicians to build and maintain a winning coalition (See Kitschelt 2000). First, they can develop a reputation for providing some public

goods that benefit the entire society (though some may benefit more from them than others do). Alternatively they can focus on providing private goods targeted at supporters and swing voters. The choice is determined by what parties perceive is necessary to hold office. Voter preferences, the resources at the incumbent's disposal, and the demands generated by the electoral system and other elements of the electoral environment combine to generate incentives to emphasize one strategy over the other (Perrson and Tabeini 2000). Specifically politicians will tend to emphasize clientelist goods if private goods are relatively cheap and if the voters who are pivotal in a given electoral context value this type of goods (Kitschelt and Wilkinson forthcoming). In addition, recent work by Bueno de Mesquita et al (2000) and Chhibber and Nooruddin (2004) suggests that the number of competitors vying for office should generate incentives to build coalitions through public goods or private goods.

Bueno de Mesquita's theory focuses on the differential cost of providing public goods and private goods given the size of the coalition needed to remain in power. Because private goods can be targeted directly at the groups necessary to provide a winning coalition while public goods require sufficient investment to provide benefits to supporters and opponents alike, it is relatively cheap, they argue, to maintain a small coalition with selective goods (see also Weingast, Shepsle, and Johnson 1981, Lyne 2000, Kitschelt and Wilkinson forthcoming). But as the necessary share of the electorate to win office increases, the increased cost of providing selective goods to an ever expanding set of recipients become so great as to become infeasible except for the richest of governments, thus forcing greater emphasis on public goods and building reputations for competence. The larger the necessary coalition, the lesser incentives governments have to maintain patronage networks.

This theory of government policy choice was originally used to explain differences in the policies adopted by democracies and dictatorships. However, as Chhibber and Nooruddin (2004) recently argued, the concept of coalition sizes can be directly extended to differences in electoral coalition types. The minimum number of votes needed to win election facing each candidate given the electoral system and the number of competitors, what Lijphart (1994) called the “effective threshold,” is similar to Bueno de Mesquita et al’s concept of the selectorate. Because increases in the number of parties seeking office reduces the threshold for winning office, we should expect that as the number of candidates or parties seeking office becomes very large, the necessary winning coalition shrinks and parties have incentives to investment in clientelism instead of public good provision. In contrast, moderately fragmented elections should require that parties build a sufficiently large electoral coalition and thus encourage parties to court support through public goods.

Observations of real-world politics do not lead us to expect, however, that elections dominated by a very small number of parties or perhaps a single party should generate less clientelism and selective exchange than those with slightly higher levels of fragmentation. For example, V.O. Key argues in his classic work on Southern Politics that elections dominated by a single party tend to be, “uncomplicated by substantial social and economic issues” and yield “issueless politics” (1949, 308). One implication of this type of politics is that “government [is] especially susceptible to individual pressures and especially disposed toward favoritism” and “highly unstable coalitions must be held together by whatever means is available” (*ibid* 305). So while high levels of fragmentation leads to less programmatic competition and more use of clientelism to hold together small coalitions, low levels of electoral competition and extremely large coalitions seem to yield the same result.

The reason for this convergence is that one-party systems have many of the organizational features common to extremely fragmented systems. One result of channeling all political competition into a single party is that diverse political factions organized around different ideologies or, more often, personalities are forced to coexist and compete for the single nomination. And then “the party organization therefore becomes merely a framework for intraparty competition” (Key 1949, 388).<sup>3</sup> In this process, faction leaders and office holders need to protect their nominating base, which creates incentives for them to divert the resources of the state. Moreover, party leaders are forced to use state resources to maintain unity among those various factions. Hence factional conflict within otherwise large parties can undermine partisan incentives to serve their larger electoral coalition.

Thus the expected relationship between electoral fragmentation and investment in public goods can be compared to the classic story of the “three little bears.” If an electoral arena has *too little* electoral competition, the government will emphasize clientelist exchange over investment and will ignore fiscal discipline and fighting corruption. But if the partisan environment becomes *overly fragmented*, governments will have incentives to maintain small coalitions via targeted goods. The result is that governments will refrain from using the resources of the state to maintain clientelist networks only occur if the election is “*moderately fragmented*” with enough parties to make the election competitive enough to generate organized competition but few enough to provide incentives for parties to cobble together a large electoral coalition. In other words, we expect a curvilinear relationship between clientelism and the number of parties competing for office in a locality. The opposite pattern should hold for public goods, which should predominate at moderate levels of party competition.

One weakness of the above story is identifying the “just right” level of competition. Some scholars have argued that two-party competition produces this happy medium of competition-induced organization and large winning coalitions. States in India (Chhibber and Nooruddin 2004) and Argentina (Remmer and Wibbels 2000) with two-party systems spend more on the public goods of development and electricity provision and less on salaries than those provinces where much fewer or many more parties. But two large parties might also each be so large that they are prone to factional competition within themselves even at the level of a locality. Hence we chose in the statistical models below to not constrain any level as ideal but instead estimate whether there is a curvilinear relationship between electoral fragmentation and various indicators of public good and clientelist investments.<sup>4</sup>

### **Additional Explanations for Clientelism**

There are three additional sets of factors that the extant literature suggests should influence governments’ propensity toward good management and public goods investment: fiscal factors, socio-economic factors, and partisan factors. The literature on fiscal factors, especially the importance of local governments generating their own revenue is outlined above. Hence we control for the origin of government revenues in the models below. In addition, electoral loyalty will be relatively cheaper in poor societies (Londregan and Poole 1993, Bates 1981, Ware 1987, Kitschelt 1995) and those with low levels of social capital (Putnam 1993, Krishna 2002). Ethnic divisions provide natural clienteles for targeting through club goods that can ensure the support of the entire group (Banarjee and Somanathan 2001, Chandra 2004). Thus we control for the level of development and ethnic divisions. Finally, while the hypotheses regarding electoral dynamics outlined above should hold irregardless of which parties are actually seeking office, one might expect different outcomes depending upon which party governs. For example, sub-

national governments controlled by members of the government coalition receive pressure from the national party leadership to not undermine the government's fiscal programs and thus might contract less debt than those municipalities governed by the opposition (Remmer and Wibbels 2000, Rodden and Wibbels 2002).<sup>5</sup>

### **The Context: Decentralization in Bolivia**

While Chhibber and Nooruddin's framework has been tested previously, an advantage of the current work in which we analyze a subset of Bolivia's 314 municipal (county) governments is that the units of analyses in previous studies, states/provinces, are relatively limited in number and in the variation of key features expected to impact the choice of targeting strategies (e.g. size, wealth, number of ethnic divisions) and the degree of electoral fragmentation. By moving to the municipal level, we achieve greater variation in both the political and social variables that allows for a tougher and more complete test of the theory outlined above.

Bolivia is also an ideal case to test this argument because its decentralization is recent and in most parts of the country precedes the development of electoral competition. Prior to 1994, Bolivia was a limited federation. The nine provinces all had some policy-making responsibility but the central government could override their initiatives, controlled their budgets, and provincial governors were appointed by the president. Municipal governments only existed in urban areas while rural areas were unincorporated; 42 percent of Bolivians did not live under formal local government (Grindle 2000, 96). Moreover, most local also did not have independent revenue bases; 92% of revenues earmarked for development were spent in the 9 department capitals, 86 percent of which was spent in the three largest cities: La Paz, Cochabamba, and Santa Cruz (Barbery Anaya 1997, 4)

In 1994, however, President Gonzalo Sanchez de Lozada of the MNR enacted two major decentralization laws.<sup>6</sup> The Popular Participation Law (*Ley de Participacion Popular* or LPP) created a total of 311 (now 314) municipalities and reorganized governance structures within them to make municipal presidents elected and allowing civil society to participate in budgets. It also mandated that 20% of national tax revenues be transferred to municipalities on the basis of their population. The coparticipation (*comparticipación*) transfers form the primary basis of local government revenue.<sup>7</sup> The second major law, the 1995 Law of Administrative Decentralization placed municipalities in charge of providing infrastructure for health and education and gave them discretion, in partnership with the departments, for most other areas of development policy.

Municipal government is made up of two entities: the municipal council (*consejo municipal*) and the mayor (*alcalde*). The municipal council is made up of between 5 and 11 members depending upon the population of the municipality and is responsible for approving municipal laws and the budget. Alcaldes are responsible for implementing the law and for forming the budget proposal for the municipal council to consider. Alcaldes are the public face of the municipal government, and several have used it as a stepping stone to launch national careers and even presidential candidacies.

Members are elected to the council according to open-list PR with seats assigned according to the d'Hondt largest average formula. If one of the candidates for the municipal council receives 50% of the vote, then that candidate is declared alcalde. If no such majority winner exists, then the alcalde is chosen by a vote of the municipal council.

The devolution of political and economic control to local governments has had many benefits. The political reforms have increased political contestation; the number of women and

people of indigenous origin running for both local and national office increased following the 1994 reforms (Grindle 2000). With coparticipation, the total amount of resources controlled by municipal governments is 17 times greater than prior to the reforms (Faguet 2004, 4). These revues are also much more equally distributed across the country than prior to the reforms.

Fiscal and political decentralization changed more than how resources were distributed across the country; there is evidence that decentralization has resulted in significant changes in government spending patterns. Faguet (2004) shows that government spending on education and sanitation greatly increased and spending on resource extraction and transportation decreased following the LPP. He further argues that these changes have not occurred randomly but have been driven by public demands; the largest increases in spending on education, for example, have occurred in areas where educational spending per student prior to decentralization were especially low. Hence in many ways decentralization has improved government policy provision consistent with the expectations of Tiebout or Oates.

However, decentralization's effects have not been entirely positive. One of the most troubling results for many members of the international and national financial sectors has been the increase in Bolivian municipal indebtedness. Since the implementation of the LPP, the 311 municipalities have accumulated over \$123 million U.S. in debt (Ministerio de Desarrollo Sostenible y Planificacion 2000). While municipal debt represents only 2% of Bolivia's GDP and 6% of Bolivia's total government debt, the debt owed by Bolivian municipalities is now essentially equal in magnitude to the coparticipation transfers municipalities receive annually.

In response to the growing indebtedness of local governments, the central government has been forced to create a plan to help municipalities restructure their debt similar to those imposed by IFI's; municipalities can have their debt bought out if they limit further debt to 20%

of their annual revenue, cut current expenses (which often involves reducing social programs), and improve tax collection.<sup>8</sup> However, there remain large problems in monitoring the spending patterns of local governments, meaning that many governments continue to accumulate larger debts than Bolivian law allows.<sup>9</sup> The scale of municipal indebtedness also varies across the country. The median municipality has a per capita debt of only \$1 U.S. per capita but in over 25% of municipalities the per capita debt valued over \$5 U.S. and the most indebted municipalities have debts valued at \$100 U.S. per capita. But given that the *coparticipacion* transfers amount to approximately \$27 U.S. per capita, even small amounts of debt represent a substantial drain on municipal resources in the future.

A second problem that has emerged has been the rise of local government corruption. The head of the Anti-Corruption Agency (*Delegada de Lucha Contra la Corrupción*) in Bolivia, Lupe Cajías, recently commented that while accusations of corruption against the central government have gone down under the new administration, accusations of corruption against local officials have increased (*La Razon* Aug 16, 2004). For example, in April 2004, the leader of the UCS party, which was a member of the governing coalition following the 2002 presidential elections, spoke of the need for funds to contest the upcoming municipal elections and said “I ask the mayors and the rest to take something; I do not tell you to rob, but take something” (“*Le pido a los alcaldes y a todos los demás que saquen algo, no digo que roben pero saquen algo*”) (Paz S. 2004).

In general, there is a growing recognition that “the Popular participation law has been implemented in different ways from municipality to another” (Theévoz and Luján 2000, v). While in some areas it has resulted in increased participation and efficiency as well as increased spending in the poorest areas (Pérez de Rada and Zilveti 2000), other municipal governments

have failed to generate even complete budgets from year to year much less full local development plans as required by Bolivian law (Ayo Saucedo 1999, Gray Molina 2000). The failure of municipal governments to provide services undermines support for both specific local governments and also the national democratic system (Hiskey and Seligson 2003) and also impacts poverty reduction efforts (Singer n.d.).

In addition, one unanticipated result of decentralization has been an increase in political fragmentation. Bolivia's multiparty system has become increasingly fragmented in recent years with the rise of populist parties (Gamarra and Maloy 1995) and municipal elections are more fragmented than national elections. Electoral fragmentation varies substantially throughout the country, however, and we expect that differences in local party systems will affect policy.

## **Data and Methods**

The most commonly used indicator of coalition building via patronage and clientelism is the size of the public sector or spending on public employee salaries, since in the absence of civil service requirements public sector employment is a large source of patronage (e.g. Remmer and Wibbels 2000, Calvo and Murrillo 2004, Remmer 2007). Unfortunately, we have been unable to obtain data on public sector salaries for Bolivian municipalities. As a proxy, we use municipal current expense (*gastos corrientes*) spending per capita for the 1998-1999 fiscal year because the majority of these expenditures are on employee salaries and bonuses (Unidad de Desarrollo Institucional Municipal 2000, 177-80). Our expectation is that current expense spending will be highest in municipalities with either very low or very high levels of party competition, reflecting the greater prevalence of patronage politics in those contexts.

For our indicators of public goods, we use per capita government spending on sanitation infrastructure in the same fiscal year.<sup>10</sup> While in some countries, these programs are havens for

patronage employment (Pachon and Sanchez-Torres 2004), the majority of the spending in Bolivian municipalities has been on infrastructure that did not exist in rural areas prior to fiscal decentralization (Faguet 2004, Pérez de Rada and Zilveti 2000). These variables also are of interest because high levels of municipal investments in sanitation following decentralization have resulted in reduced poverty rates and illness (Instituto Nacional de Estadísticas 2002). We expect that governments in municipalities with very high or very low levels of electoral fragmentation will have fewer incentives to invest in sanitation infrastructure than those with moderately sized electoral coalitions.

For our measure of electoral fragmentation, we use Laasko and Taagapera's (1979) measure of the effective number of parties that received votes (ENPV) in the 1999 municipal elections. If  $v_i$  is the proportion of valid votes that party  $i$  received in a given district, then the effective number of parties by votes (ENPV) in that district is:  $\frac{1}{\sum_{i=1}^n v_i^2}$ . The average Bolivian municipality in 1999 had 5.25 effective parties, but there was a great deal of variance in the amount of electoral fragmentation: the least fragmented municipality of Santa Rosa del Abuna, Pando had 1.08 effective parties (the Acción Nacional Democrático (ADN) party received 95% of the vote) while in Mecapaca, La Paz the vote was divided between 12 effective parties and no party received more than 12 percent.

To capture the predicted curvilinear relationship between fragmentation spending patterns, we include both the effective number of parties and its square. Our expectation is that increases in the effective number of parties (ENPV) will initially be associated with less spending on current expenditures (i.e. the coefficient for ENPV will be significant and negative) but that as the election becomes extremely fragmented the observed financial irregularities will increase (i.e. the coefficient for ENPV<sup>2</sup> will be significant and positive). For the models of

spending on sanitation, we expect that the relationships will be in the opposite direction; e.g. ENPV will have a positive sign and its square will be negative.

In addition to testing our central thesis about the effect of the electoral context, we also test whether the degree of competitiveness of a race, measured as the margin of victory between the first and second place parties, has an impact on local government policy. The standard expectation in the literature is that investment in public goods decreases and clientelism increases as the margin of victory gets larger and the race less competitive.

Following previous studies, we control for a few other political, social, and fiscal factors that vary across municipalities; the data sources are listed in the appendix. We include a dummy variable that takes on the value of 1 if the mayor was from one of the governing parties (ADN, MIR, UCS, and CONDEPA), with the expectation that being in the government might provide them with incentives to emphasize fiscal performance. We also control for the socioeconomic conditions in the municipality by including the municipal population's size, the percentage of municipal inhabitants living in poverty, the effective number of ethnic groups according to respondents' self identification, the percentage of municipal residents who have completed at least secondary school. Following the literature on fiscal federalism, we include the share of total government revenues (excluding borrowed funds) that local governments raised through their own tax collection effort. All fiscal variables are measured for the 1998-1999 fiscal year. Social-demographic variables were measured in the 2001 census. In very few of the models do any of these factors achieve statistical significance, though F-tests not reported here show that the social factors are generally jointly significant.

In addition to these controls, we include dummy variables for 8 of Bolivia's nine departments (using Beni as the excluded case) to allow the model to catch any excluded factors

related to geographic patterns of development, industry, or partisan histories. Even after including these dummies, however, Breusch-Pagan tests reveal remaining heteroskedasticity in all models. We use thus use White robust errors; adjusting for heteroskedasticity results in larger standard errors for ENPV and ENPV<sup>2</sup>.

## **Empirical Results**

Our general hypothesis predicts that spending on selective goods should be highest in areas where electoral fragmentation was either especially low or especially high. The significant positive coefficient for ENPV and negative coefficient for ENPV<sup>2</sup> in the model of current expenditure spending in Table 1 (below) confirm that hypothesis. Initial increases in partisan competition result in a decrease in spending on current expenditures. At high levels of fragmentation (more than 6.9 effective parties), increases in party competition lead to increased spending on current expenditures, which are primarily public sector salaries.

(Table 1 about here)

Besides being statistically significant, the effect of electoral fragmentation on spending on gastos corrientes is substantial. If party competition in a municipality were to increase one standard deviation from 1.5 effective parties to 3.5 effective parties, current account spending is predicted to decrease by \$6.3 U.S. per capita. Given that the municipality only receives \$27 U.S. per capita via coparticipación, the effect of moving \$6.3 dollars represents a sizable proportion of available resources. For the average municipality, this would result in reductions in current account spending by \$85,463 U.S. Alternatively, increasing one standard deviation from 7 parties to 9 parties results in a predicted increase in current spending of \$1.5 U.S.

The second model in Table 1 tests whether the margin of victory affects current spending in a similar manner. While the coefficient for the margin of victory is in the expected positive

direction, its effect does not approach statistical significance. Party fragmentation has the same curvilinear relationship with Gastos Corrientes even when controlling for the margin of victory (column 3). The type of competition that exists in a municipality this seems to be a more important determinant of budgetary choices than the degree to which an election was simply competitive.

We also expect that investment in public goods should be higher in municipalities with moderate levels of fragmentation compared to municipalities with either extremely low or high numbers of parties competing. The results in Table 2 for per capita spending on sanitation (below) again are consistent with our hypothesis; ENPV and ENPV<sup>2</sup> have a statistically significant impact on municipal budgeting for sanitation and that impact is in the opposite direction than it had on current accounts. Increases in the number of parties away from one party dominance results as predicted in increased spending on utilities, with the marginal impact of those increases declining until there are approximately 7 effective parties receiving votes. After that point, increases in the number of parties results in a decreased level of utility investment. Putting these results in context, increasing the number of parties getting votes from 1.5 to 3.5 would increase per capita spending on sanitation by \$2.3 U.S. while increasing the number of parties from 7 to 9 would result in reduced spending of \$0.54.

(Tables 2 about here)

In the second column of Tables 2, margin of victory is used to predict spending patterns instead of the number of parties. In contrast to current account spending, the margin of victory is a statistically significant predictor of spending on sanitation; close races do appear to generate more public sector investment than less competitive races. However, that effect becomes

insignificant electoral fragmentation is reintroduced in the third model table 2, suggesting that the local party system captures any effect of competitive elections.

Two other results from Table 2 deserve comment. First, in the first two models of Table 2, population is negatively associated with spending on utilities at the 0.10 level or better, reflecting the lack of infrastructure in the smaller, more rural communities prior to decentralization and the subsequent increases in spending noted by Faguet (2004). In addition, the effect on sanitation spending in Table 2 of having an alcalde from a party that was a member of the presidential coalition is statistically significant but has a negative coefficient. This is the only time in the models analyzed here where we find any effect for the alcalde's party.

One variable with a surprisingly lacking effect in either Table 1 or 2 is the percentage of municipal government revenue generated by local taxation efforts. The weakness of this mechanism is likely a function of the high degree of municipal reliance on transfers from the central government through coparticipación revenues. The median municipality generates only 1% of its revenues via its own tax collection and licensing efforts. At these levels, the threat of withholding tax revenues absent good government performance is unlikely to wield a large impact on government officials who are not lacking in resources.

The above results suggest that patterns of electoral competition in Bolivian municipalities have shaped investment choices by the regime. Both very low and very high levels of electoral fragmentation are associated with more investment on patronage and less investment on broad public goods.

### **Additional Impacts of Local Electoral Environments: Corruption and Debt**

A challenge for architects of municipal governance structures is not only to induce politicians to avoid investing in patronage instead of public goods; local governments must also

be given incentives to eliminate corruption and to avoid contracting debt. These two negative outcomes can be tied to a similar electoral logic as the one governing clientelism.

The spoils of corruption, for example, do not only accrue to the official actually taking the bribe. These officials often exist within a larger networks of supervisors who must receive either material payoffs or some other form of reward-e.g. campaign contributions of time, money, or supporters for their electoral campaigns in order to be to be convinced to look the other way and beneficiaries from which officials taking bribes can rent support with the ill-gotten resources. The result is that corruption provides money that can lubricate a clientelist machine of political support or a favor/reward (allowing some corrupt activities within some reasonable bounds) that can be given to supporters in exchange for electoral resources. Under those conditions, political parties might be the beneficiaries of ongoing corrupt practices. Allowing some degree of corruption keeps dissident factions within the overall party by providing access to a trough, allows a way to payoff groups whose continued access to special services becomes contingent upon continuity in government, results in networks whose continuity might be easier to maintain than an issue coalition, and provides resources to bankroll a political campaign.

This is not the only way for clientelism to be maintained of course; not all clientelism is corruption. Revenues can be raised through the budgetary allocation process and officials can be given discretion over appointments and service provision in exchange for political support instead of a material payoff. But the networks created by the two types of activities seem similar. In addition, not all corruption is clientelism; officials might simply pocket the resources and not create extended networks and supervisors might turn the other way out of ignorance, a lack of capacity to control lower officials, or desire for a material payoff instead of forging a more extensive political arrangement. But if corruption is in part clientelism, then political parties

begin to have incentives to ignore it or even to actively encourage it to facilitate their control of electoral office. Corruption thus becomes a way of building machines that can win elections and elections the reason for allowing corruption in the first place.<sup>11</sup>

We are not the first to suggest that corruption levels might be correlated with the factors previously linked to the broader phenomenon of clientelist linkages. This is actually a fairly common implicit assumption, as many theories that purport to be about club goods use measures of corruption as their indicator of interest (e.g. Persson and Tabellini 2003) and corruption and clientelism are often lumped together as part of a larger phenomenon (Kang 2002, della Porta and Vannucci 1999, Piattoni 2001, Morgenstern and Manzetti 2003). Here we thus propose that local governments in Bolivia with high and low levels of fragmentation will be more corrupt.

To test this intuition, we use a dataset containing the results of in-depth audits of 124 municipal governments conducted between 1996 and 2001 by the non-partisan National Comptroller's Office. The target of the audits was to identify the use of municipal resources for "economically damaging practices." The specific policies lumped under this heading vary greatly, but the most commonly cited examples were the spending of state resources outside of normal procedures of documentation (reimbursements for trips that there was no documentation of, advances to employees without receipts, sale of state property without records on a recorded bidding process), payment of salaries to individuals who have not been officially hired by municipal governments, and payment for projects that were not completed or occasionally not even ever started. In general, it measures the misuse of government funds for personal gain.

Thankfully, the amount of economically damaging practices discovered by the auditors is relatively minimal; the median municipality only had \$2 U.S. being spent per person on graft and in only three cases did discovered graft per capita exceed \$10 U.S. But if a government's only

source of revenue is the coparticipation tribute distributed by the federal government, then their *per capita* operating budget is roughly \$27 U.S. Hence the loss of even \$2 per capita, much less \$10, is substantial in terms of the decreased services governments can provide to the citizenry at large. In addition, these audits are likely to under-measure the problem.

After excluding cases for which no data about government revenue sources was available, we are left with 118 cases for which we can analyze this variable. A preliminary analysis of these cases shows that the likelihood of a municipality being included in this sample of cases is not a function of any of the political nor fiscal variables under consideration nor of the municipality's population but is a function of the percentage of the municipality's inhabitants who are classified as poor. Specifically, poorer municipalities were significantly less likely to be audited. Rerunning the statistical models in Table 3 of the levels of graft per capita across these municipalities (below) with a selection model, however, does not change the conclusions.

(Table 3 about here)

Looking at the results in Table 3 (below), we see that again our expectations are confirmed as the coefficients for ENPV and ENPV<sup>2</sup> have the expected sign and achieve standard levels of statistical significance. Increases in the number of parties receiving votes away from one-party domination initially reduce graft but at extremely high levels of fragmentation graft again is higher. The predicted switching point is about 5 parties, slightly lower than in the previous model. Also as in Table 1, the effect for the type of competition does not change with the inclusion of a measure of the degree of competition in the third model in Table 3 but the latter variable is not statistically significant either by itself nor when controlling for the number of parties. Hence changes in the number of parties competing have a larger effect on the amount of graft and corruption in a municipal government than election closeness.

(Table 2 about here)

The effect of fragmentation on observed graft is fairly large. Moving from 1.5 to 3.5 parties reduces graft by \$1.4 U.S. while moving from 7 to 9 increases graft per-capita by \$1.8 dollars. Again, in the context of per-capita budgets of \$27, preventing the loss of 5 percent of the budget by moving from 1.5 to 3.5 parties would represent substantial savings.

Finally, it is often argued that differences between locality' emphasis on clientelism or public goods have implications for fiscal management and indebtedness. As politicians have an incentive to use municipal spending to shore up their political base and a political disincentive to emphasize broader public goods such as management efficiency, one likely result of clientelist will be lower levels of budget discipline (Kitschelt and Wilkinson, forthcoming). This is especially true inasmuch as voters are motivated by getting access to goods and not the overall state of the budget. Hence selective good provision and budget deficits often covary. Remmer and Wibbels (2000), for example, find that Argentine Province indebtedness was a function of increased spending on public sector salaries, which is an indicator of patronage (see also Sawers 1996). Thus we expect that local government debt will be highest in municipalities with either very high or very low levels of electoral fragmentation.

In Table 4 (below), then, we model the debt accumulated by local governments in the election year as a function of electoral competition in that municipality. This model is slightly different than those in previous models, however, because there is both anecdotal and, as the model shows, statistical evidence that the nine department capitals (La Paz, Sucre, Santa Cruz etc...) as well as the large suburb of El Alto enjoy easier access to formal credit from domestic and even international banks and thus can contract more debt than other municipalities, the majority of whose debts are IOU's to private firms and even individuals to whom the

government owes payment for rendered services (Morales 2002, Vasquez 2002). Hence we include a dummy variable for whether the municipality was one of those 10 major cities.

(Table 4 about here)

Again, our main expectation is that initial increases in the number of parties should result in an increase in debt but debt will also increase at extreme levels of fragmentation. The estimated coefficients for ENPV and ENPV<sup>2</sup> have the expected signs and are statistically significant at 0.055 or better. For municipalities with less than 6.7 effective parties, increases in the number of parties competing results in less debt being contracted by the government. At higher levels of fragmentation, the result of adding new parties to the electoral mix is to increase indebtedness. In addition, in an analysis not reported here we tested whether increased levels of debt were associated with higher levels of spending on gastos corrientes or of graft. In each case the expected result was obtained, thus reaffirming our initial hypothesis that one result of clientelism in local governments was increased debt.

Again, the marginal effect of changes in electoral fragmentation is quite large. All else being equal, an increase from 1.5 to 3.5 parties seeking office results in a reduction in per capita debt of \$7.8 U.S. To put that in perspective, the average municipality in our study had a per capita debt load of \$11 U.S., so for the average municipality this increase in electoral competition would result in cutting their indebtedness by over half. If fragmentation increases from 7 to 9 parties, however, our model predicts that debt will increase by \$2.6 U.S. For the average municipality, that would result in an increased total debt burden of \$35,036.

Looking at the other variables in Table 4, we see that increases in district magnitude also lead to increased levels of debt (reflecting either the result of changing the threshold or, more likely, the importance of population size for the ability to contract debt) and the large cities are,

on average, 96 Bolivianos (1990 units) or 19 U.S. Dollars per capita more indebted than less powerful municipalities. Again, we find no effect for the margin of victory on policy outputs.

Thus the results confirm that corruption and government debt follow the same electoral logic as clientelism, initially decreasing as the number of parties increases but then increasing again as number of parties becomes large.

## **Discussion and Conclusion**

The results in this essay confirm our starting intuition: competitive local elections themselves are not sufficient for decentralization to yield increased investments in public goods and enhanced government efficiency. The specific nature of the local electoral environment has been shown to determine the degree to which local governments invest their limited resources in clientelist networks instead of broader government services. The result of extremely high or low levels of partisan fragmentation across institutional contexts is high levels of graft and state patronage, which then get translated into budget deficits and local government debt. The result of moderate numbers of parties seeking office is increased investment in public infrastructure and less clientelism, graft, and mismanagement. So while the paper confirms that steps away from political competition dominated by a single party will result in increased levels of investment and less graft and debt, it also warns against local elections becoming overly fragmented.

By implication, decentralization's efficiency enhancing properties are contingent and will be most likely to be manifest if electoral fragmentation at the local level is moderate. Absent this condition, decentralization does lead to local governments potentially undermining the central government's attempts to limit public debt and establish macroeconomic stability just as Remmer and Wibbels (2000) showed with the Argentine Provinces. The result is that as the

amount of revenues being transferred to local governments in Bolivia and other countries continues to increase, government efforts to maintain macroeconomic stability are going to have to become even more stringent at the national level.

These results should not be interpreted as calling for limits on political contestation at the local level. The above theory about electoral incentives for public or club goods assumes that competition is free and fair and that parties have incentives to pursue votes. Absent open and fair political competition, even moderate political fragmentation will not give governments incentives to be responsive.

The results in this paper should raise a red flag, however, for advocates of political and financial decentralization because there is consistent evidence that one of the side effects of fiscal decentralization is increased partisan fragmentation at the local level, even though the mechanism that explains this change is not yet well established (Grindle 2000, Chhibber and Kollman 2004, Ryan 2004). For most political observers, these changes are interpreted as positive for democracy because they represent increased competition as well as often allowing for groups that have traditionally be excluded from the political process (e.g. Indigenous organizations) to gain a foothold in politics. What the results in this paper warns is that these changes might have a negative effect on the quality of local governance and policy.

One surprising finding across models is that the estimated point where electoral fragmentations' effect switches was much higher than the 2-3 party competition emphasized by other studies (e.g. Remmer and Wibbels 2000, Chhibber and Nooruddin 2004). While this may be a result of the parabolic functional form chosen for the analysis, it also might reflect the organizational weakness of many Bolivian parties at the local level. Bolivian parties are noted for their lack of ideological content and internal organization and one impact of this is that

clientelism is used as the glue that hold these parties together (Gamarra and Maloy 1995). Hence the development of strong internal party organizations might occur at higher levels of party competition than Key predicted with regard to the U.S. Or this result might be a result of Bolivia operating in a multi-member electoral system while the other studies emphasized single member elections. But more research is necessary to understand why this result obtains.

Obviously, much work remains to be done on this topic and tease out the various ways in which political competition effects the outcome of decentralization. But it is our hope that the results presented here will push more scholars to look beyond merely asking if elections exist induce accountability to look at how the context under which those elections are contested yields divergent policy outcomes.

## Appendix: Data Sources

Electoral Data for the 1999 elections and outgoing Mayor's Partisanship:

- Corte Nacional Electoral ([www.cne.org](http://www.cne.org))
- Ministerio de Desarrollo Humano 1996. Las Primeras Elecciones. La Paz: Ministerio de Desarrollo Humano.

Fiscal Variables (Debt, Spending on Gastos Corrientes and on Sanitation, Tax base) for Fiscal Year 1998-1999:

- Unidad de Desarrollo Institucional Municipal, Viceministerio de Planificación Estratégica y Participación Popular, Gobierno de Bolivia. 2000. Participacion Popular en Cifras. La Paz: VPEPP.

Local Government Corruption:

- Unidad de Desarrollo Institucional Municipal (2002); Ministerio de Desarrollo Sostenible y Planificación, Viceministerio de Planificación Estratégica y Participación Popular, Gobierno de Bolivia. 2002. Sobre Auditorias a gobiernos municipales de Bolivia, Periodo 1994-2000. La Paz: MDSP.

Socioeconomic data:

- Instituto Nacional de Estadísticas, Gobierno de Bolivia. 2002. Bolivia: Mapa de Pobreza. La Paz: INE. [http://www.ine.gov.bo/PDF/PUBLICACIONES/Censo\\_2001/Pobreza/PBolivia.pdf](http://www.ine.gov.bo/PDF/PUBLICACIONES/Censo_2001/Pobreza/PBolivia.pdf).

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Table 1: The Effect of Electoral Competition on Per Capita Spending on Gastos Corrientes

	[1]	[2]	[3]
ENPV	-24.975* (11.025)	--	-31.801* (13.496)
ENPV <sup>2</sup>	1.802* (0.827)	--	2.252* (0.965)
Margin of Victory	--	0.312 (0.455)	-0.444 (0.298)
District Magnitude	4.453 (9.769)	3.818 (8.341)	5.203 (10.490)
Government Coalition	2.550 (9.019)	3.488 (9.090)	1.142 (8.802)
Population	0.000 (0.000)	0.000 (0.000)	0.000 (0.000)
% Living in Poverty	-0.343 (0.298)	-0.325 (0.279)	-0.309 (0.310)
Effective Number of Ethnic Groups	-14.523 (9.848)	-15.181° (8.299)	-14.453 (9.630)
% Revenues Raised Through Local Taxes	-10.899 (29.051)	-15.364 (35.141)	-9.614 (30.858)
% Secondary Education	-13.244* (5.465)	-24.610° (14.258)	-10.270° (6.718)
constant	-24.975* (11.025)	0.312 (0.455)	-31.801* (13.496)
N	250	250	250
F	2.21**	2.25**	2.07**
R-squared	0.116	0.100	0.118
Root MSE	60.397	60.788	60.440
<p>* p&lt;0.05, ** p&lt;0.01, ***p&lt;0.001                      Robust standard errors in parentheses                      Results for departmental dummies excluded from the table</p>			

Table 2: The Effect of Electoral Competition on Per Capita Spending on Sanitation

	Coef.	Coef.	Coef.
ENPV	9.053* (3.883)	--	8.239* (4.034)
ENPV <sup>2</sup>	-0.651** (0.226)	--	-0.600 (0.261)
Margin of Victory	--	-0.237° (0.125)	-0.054 (0.130)
District Magnitude	-0.955 (1.768)	-0.459 (1.888)	-0.865 (2.008)
Government Coalition	-5.319*** (1.547)	-6.149* (2.998)	-5.478° (2.901)
Population	-0.001° (0.000)	-0.001° (0.000)	-0.001 (0.000)
% Living in Poverty	0.184 (0.220)	0.163 (0.235)	0.183 (0.244)
Effective Number of Ethnic Groups	1.875 (2.138)	2.206 (2.311)	1.908 (2.348)
% Revenues Raised Through Local Taxes	20.221° (10.469)	20.538 (15.781)	20.309 (15.318)
% Secondary Education	20.557 (30.316)	16.986 (30.882)	19.936 (32.323)
Constant	-37.569 (27.218)	-11.995 (27.358)	-35.021 (32.676)
N	213	213	213
F	2.100**	2.200**	1.950*
R-squared	0.102	0.092	0.103
Root MSE	20.979	21.048	21.030
<p>* p&lt;0.05, ** p&lt;0.01, ***p&lt;0.001                      Robust standard errors in parentheses                      Results for departmental dummies excluded from the table</p>			

Table 3: The Effect of Electoral Competition on the Amount of Graft Per Capita Discovered by Government Audits

	[1]	[2]	[3]
ENPV	-1.418* (0.723)	--	-1.441* (0.729)
ENPV <sup>2</sup>	0.146* (0.061)	--	0.148** (0.052)
Margin of Victory	--	-0.006 (0.019)	-0.002 (0.032)
District Magnitude	0.044 (0.220)	0.119 (0.217)	0.045 (0.253)
Government Coalition	-0.167 (0.432)	-0.042 (0.466)	-0.170 (0.421)
Population	0.000 (0.000)	0.000 (0.000)	0.000 (0.000)
% Living in Poverty	-0.015 (0.028)	-0.028 (0.032)	-0.015 (0.022)
Effective Number of Ethnic Groups	0.038 (0.289)	-0.181 (0.305)	0.040 (0.378)
% Revenues Raised Through Local Taxes	1.030 (1.381)	1.816 (1.713)	1.027 (1.338)
% Secondary Education	-2.592 (4.026)	-4.620 (4.824)	-2.572 (3.657)
Constant	7.359° (4.157)	5.906 (3.969)	7.406* (3.512)
N	118	118	118
F	3.830***	2.740***	3.600***
R-squared	0.374	0.244	0.374
Root MSE	2.055	2.248	2.066
<p>* p&lt;0.05, ** p&lt;0.01, ***p&lt;0.001  Robust standard errors in parentheses  Results for departmental dummies excluded from the table</p>			

Table 4: The Effect of Electoral Competition on Per Capita Government Debt

	[1]	[2]	[3]
ENPV	-31.551* (16.024)	--	-31.883° (16.510)
ENPV^2	2.381* (1.216)	--	2.402* (1.217)
Margin of Victory	--	0.574 (0.565)	-0.021 (0.665)
District Magnitude	18.171* (8.071)	20.821* (8.331)	18.179* (8.104)
Major City (Department Capital + El Alto)	96.014** (35.197)	87.080* (35.899)	95.956** (35.745)
Government Coalition	-0.687 (6.859)	0.443 (7.556)	-0.745 (7.708)
Population	-2.383 (3.624)	-5.248 (3.530)	-2.340 (3.776)
% Living in Poverty	-0.505 (0.369)	-0.543 (0.363)	-0.503 (0.364)
Effective Number of Ethnic Groups	-4.336 (5.208)	-4.485° (5.275)	-4.349 (5.398)
% Revenues Raised Through Local Taxes	-6.844 (33.150)	-5.709 (34.070)	-6.888 (33.890)
% Secondary Education	-71.494 (46.281)	-67.905 (46.346)	-71.636 (45.870)
constant	94.070 (74.133)	23.242 (64.154)	94.754 (77.213)
N	261	261	261
F	2.820***	2.620***	2.700***
Prob > F	0.000	0.001	0.000
R-squared	0.334	0.320	0.334
Root MSE	51.549	51.967	51.655
<p>* p&lt;0.05, ** p&lt;0.01, ***p&lt;0.001                      Robust standard errors in parentheses                      Results for departmental dummies excluded from the table</p>			

## Notes

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<sup>1</sup> This paper has benefited from previous comments from discussants at the 2003 Meeting of the Midwestern Political Science Association and by participants at the Comparative Politics Workshop at Duke University and the Duke-UNC Working Group on Political and Economic Regimes in Latin America. Data collection was made possible by financial support from Karen Remmer and the Duke University Political Science Department.

<sup>2</sup> Competition between sub-national units might also potentially have adverse effects on policy by generating a “race to the bottom” (e.g. Brown and Oates 1985).

<sup>3</sup> For recent works on the internal politics of one-party systems, see Richardson (1997), Richard and Patterson (2001), Green (2001), and Magaloni (2006); these works reach similar conclusions about the issue-less nature of politics in these countries. For factional politics more generally and the importance of state resources for maintaining parties, see Leigh (2000), and McCubbins and Thies (1997).

<sup>4</sup> Remmer (2007) also finds that support for the governor in Argentine provinces also has a curvilinear effect on patronage; governors elected with oversized coalitions or extremely small ones engaged in more patronage than those with moderate levels of support.

<sup>5</sup> More generally, differences in parties’ coalitions and ideologies may also result in generally different policy emphases (Plotnick and Winters 1985). Ideological divisions in Bolivia are extremely weak, however, (Gamarra and Maloy 1995), and hence it is not surprising that controlling for the alcalde’s ideology in analyses not reported here did not predict any of the outcomes of interest.

<sup>6</sup> For a more extensive discussion of the process of decentralization in Bolivia, see Grindle (2000, 94-146), Ameller Terranzas (2002), O’Neill (2004), or Faguet (2001).

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<sup>7</sup> In 2002, the National Dialogue Law (Ley del Dialogo Nacional) created a second system of transfers to municipalities to fund anti-poverty programs, with the poorest municipalities receiving the most revenue (Morrison and Singer forthcoming).

<sup>8</sup> Interview with Angelica Soto Mayor and Jorge Brit Pozo, Ministry of Finance UPF, 11 Jun 2002, la Paz Bolivia.

<sup>9</sup> Interview with Interview with Mario Costas, Contaduria General del Estado, June 19 2002; Interview with Juan Antonio Morales, President of the Central Bank of Bolivia June 10, 2002; Interview with Armando Mendez, Vice President of the Central Bank of Bolivia June 14, 2002. All in La Paz, Bolivia

<sup>10</sup> While due to space constraints we only present here the results for spending on sanitation, a similar curvilinear relationship between electoral fragmentation and spending decisions occurs within the sample for expenditures on energy infrastructure and education.

<sup>11</sup> For an interesting discussion of how some Bolivian political parties sell jobs in the bureaucracy to raise campaign funds, see Gingerich (2006)