

# International Scrutiny and Pre-Electoral Fiscal Manipulation in Developing Countries

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*Pre-electoral fiscal manipulation—spending more or taxing less prior to an election—is an important tool that governments possess to enhance their chances for reelection. Existing explanations of pre-electoral fiscal manipulation focus primarily on domestic characteristics. We extend this line of inquiry by examining international influences on governments' decisions to engage in pre-electoral fiscal manipulation. We find that international scrutiny of the economy and international scrutiny of elections affect pre-electoral fiscal manipulation in cross-cutting ways. Using data from 1990 to 2004 for 94 developing countries, we show that pre-electoral fiscal manipulation is more likely when international election monitors make direct election manipulation more difficult, and it is less likely when governments are subject to international economic scrutiny resulting from an IMF agreement.*

Pre-electoral fiscal manipulation—spending more or taxing less prior to an election—is an important tool that governments may use to enhance their chances for reelection.<sup>1</sup> Recent studies document that it is employed most often in new democracies (Brender and Drazen 2005) and developing countries (Shi and Svensson 2006).<sup>2</sup> Existing explanations for why incumbents in these countries engage in pre-electoral fiscal manipulation focus on domestic characteristics, and scholars have shown that pre-electoral fiscal manipulation is more likely the less consolidated the democracy (Gonzalez 2002), the less transparent the political system (Alt and Lassen 2006), the less independent the media (Brender 2003), the less aware the voters (Brender and Drazen 2005), and the poorer the country (Schuknecht 2000).

Despite widespread recognition of the impact of the international environment on developing countries' fiscal policies (Mosley 2002; Wibbels 2006), scholars have not examined the effect of the international environment on pre-electoral fiscal manipulation among these countries. In this article, we explore how two potentially cross-cutting sources of

international scrutiny influence governments' decisions to engage in pre-electoral fiscal manipulation. Specifically, we argue that international scrutiny of the electoral process increases the likelihood of pre-electoral fiscal manipulation, while international scrutiny of the economy decreases the likelihood of pre-electoral fiscal manipulation.

Politically, developing countries that wish to be considered democratic, as demonstrated through free and fair elections, are increasingly subject to scrutiny of their electoral process from international election monitors. Monitors focus primarily on documenting direct electoral fraud, and publicize information about election quality to domestic and international audiences. Negative reports frequently trigger negative consequences. Elections declared fraudulent by reputable observers have been used to justify reductions in foreign aid, internationally supported post-election domestic uprising, economic sanctions targeted at the regime, suspension from international organizations, and the withholding of other benefits that would have otherwise been awarded following an internationally certified election (Bjornlund 2004; Bratton 1998).

<sup>1</sup>An online appendix for this article is available at <http://journals.cambridge.org/jop> containing supplemental analyses. Data and supporting materials necessary to reproduce the numerical results in the paper are available at <http://hyde.research.yale.edu/research.htm> no later than the publication date.

<sup>2</sup>See Kayser (2005) Franzese (2002), and Drazen (2001) for an overview of this literature.

Because election monitors raise the cost of engaging in obvious and illegal (but more direct) methods of gaining votes, the presence of election monitors should reduce the likelihood of direct election fraud (Hyde 2007). In contrast, pre-electoral fiscal manipulation has the advantage of being a legal and often legitimate means of increasing government popularity prior to an election. Fiscal manipulation rarely provokes criticism from international election observers. Therefore, legal methods of increasing electoral support should become more attractive when more direct methods of stealing an election become more difficult due to election monitoring. Such foreign monitors should make pre-electoral fiscal manipulation more likely.

Developing countries under International Monetary Fund (IMF) agreements also face international economic scrutiny as the IMF determines whether or not these countries meet the conditionality requirements of their programs. Preventing economic manipulation prior to an election is not a particular remit of the IMF. Quite to the contrary, the IMF tries to avoid making big decisions or releasing sensitive information about a country prior to an election. Nonetheless, the IMF does monitor governments' finances and emphasizes the implementation of sustainable macroeconomic policies, generally conceived of as an improvement in the government's budget deficit. A country under an IMF agreement experiences increased attention to government expenditures, which may make it more difficult to engage in pre-electoral fiscal manipulation. As a result, governments under an IMF agreement should be less likely to engage in pre-electoral fiscal manipulation. Our argument is not that IMF scrutiny is the only form of international scrutiny with the potential to reduce pre-electoral fiscal manipulation. Rather, IMF scrutiny is a useful proxy for heightened international attention to a government's fiscal stance.

The central contribution of this article is to examine whether a government's decision to engage in pre-electoral fiscal manipulation is affected by international political and economic scrutiny. The evidence supports the argument that governments are more likely to manipulate the economy prior to an election when international election monitors constrain their ability to engage in direct electoral fraud. In contrast, governments are less likely to engage in pre-electoral fiscal manipulation when the country is under an IMF agreement, as scrutiny by the IMF makes pre-electoral fiscal manipulation more difficult. Taken together, these two effects suggest that pre-electoral fiscal manipulation is most likely when

incumbents are subject to international political scrutiny from election monitors, but are not subject to international economic scrutiny resulting from an IMF agreement. Previous research has demonstrated that developing countries are predisposed to engage in pre-electoral fiscal manipulation. This article builds on this research by showing that among developing countries, international political and economic scrutiny are important factors mediating when governments choose to manipulate the economy in order to enhance their chances for reelection.

### **International Scrutiny and Pre-electoral Fiscal Manipulation**

Politicians enjoy a wide range of tools that can be used to bias an election in their favor. Andreas Schedler has called this set of options the "menu of manipulation" (2002). Some forms of election manipulation are direct and are therefore more certain ways to guarantee an election victory, such as widespread stuffing of ballot boxes, banning opponents from electoral competition, or falsifying vote totals. Other forms of manipulation are less direct and therefore less certain ways to assure an electoral victory, such as monopolizing state-owned media, spreading false information about opponents, vote-buying, or, as highlighted here, increasing public spending or decreasing taxation in advance of the election (pre-electoral fiscal manipulation). Within this set of options, pre-electoral fiscal manipulation is both uncertain (because it does not guarantee victory) and expensive (because it typically requires significant government funds), but represents a legal means by which a government can increase its own probability of victory in the run-up to an election.

Leaders wish to guarantee their reelection while minimizing the cost of doing so, both financially and reputationally. This trade-off between the certainty and costliness of electoral victory influences which options a leader chooses from the menu of manipulation. When leaders are not constrained in their use of election fraud, either normatively by their own commitment to democracy or procedurally through oversight mechanisms that would detect and punish such manipulation, such as those that exist in consolidated democracies, leaders should be more likely to use electoral fraud because it is a more direct and therefore more certain tactic. As constraints on extralegal electoral manipulation are introduced, such as international election monitoring and the

associated enforcement of standards for democratic elections, leaders should abandon direct and obvious electoral manipulation in favor of less certain but legal options in order to avoid international condemnation.<sup>3</sup> As Thomas Pepinsky writes, “political manipulation of the economy may be less costly politically, both domestically and internationally, than electoral fraud. . . . Even a low probability event of public outcry in response to rigged elections is likely to be far costlier for the regime than subtle—and perhaps more welcome—fiscal policy manipulation” (2007, 142). Fiscal manipulation should become a more likely choice for increasing governments’ reelection chances when international election monitors are present.

Until the 1990s, election monitoring was a rare practice, and most governments did not consider inviting international election monitors. Since the early 1990s, most governments in the developing world have invited official delegations of foreign observers to judge the quality of their elections. Refusing to invite observers has become a signal that the government has something to hide, and unmonitored elections are widely viewed with suspicion by international and domestic actors (Bjornlund 2004; Kelley 2008; Rich 2001). To illustrate, in 2003 observers were not invited to elections in Cuba, Guinea, Jordan, Kuwait, Mauritania, North Korea, Oman, Syria, Turkmenistan, and Yemen—countries widely perceived to be nondemocratic. Although election monitoring existed in the 1960s–1980s, it was rare and usually inconsequential. As it spread throughout the developing world, international observers improved their methods of fraud detection and increased their willingness to criticize problematic elections (Bjornlund 2004; Carothers 1997). The increased rigor and comprehensiveness of election monitoring has made direct election fraud more costly. All else held equally, the presence of observers should make pre-electoral fiscal manipulation a more attractive option, leading to Hypothesis 1.

*H1: Pre-electoral fiscal manipulation is more likely when election monitors are present.*

International political scrutiny from election monitors is not the only form of international attention that can influence the government’s decision to manipulate fiscal policy prior to an election. International economic scrutiny, in the guise of IMF monitoring, may have the opposite effect on the use of pre-electoral fiscal manipulation. This influence may occur

in two ways. First, IMF conditionality may constrain governments’ ability to engage in pre-electoral fiscal manipulation. Second, IMF reporting on governments’ fiscal policies plays an informational role that may dissuade some governments from engaging in pre-electoral fiscal manipulation.

Countries that enter into IMF agreements to borrow money are subject to conditionality. One key component of programs’ conditionality is the adoption of sustainable macroeconomic policies, which generally means a reduction in the government’s budget deficit (Fischer 2004). As a result, if implemented, conditionality constrains government finances, making it difficult for governments to engage in the expansionary policies that are the cornerstone of pre-electoral fiscal manipulation. It is unclear, however, that countries actually implement conditionality, and recent studies have found relatively low levels of compliance (Bird 2007). This suggests that government finances may not be as constrained as IMF conditionality implies. That said, even when controlling for compliance rates, countries that are under IMF agreements appear to have an improvement in their fiscal balance (Dreher 2005). Additionally, individual country studies suggest that governments are concerned about IMF agreements constraining their ability to engage in fiscal manipulation (Pepinsky 2007; Treisman and Gimpelson 2001). Even when governments do not fully comply with conditionality, government expenditures may be limited by IMF agreements and the associated international scrutiny of their fiscal balance.

Moreover, recent economic studies have shown that IMF monitoring has an informational role beyond the conditionality of an IMF agreement.<sup>4</sup> As Eichengreen, Kletzer, and Mody argue, “the monitoring that accompanies the core conditionality in all IMF programs helps creditors gain confidence in the likelihood of reduced policy variability” (2006, 1337). Thus, IMF monitoring provides an important signal to international markets about a government’s commitment to sound macroeconomic practices. To engage in fiscal manipulation, governments must either increase spending or decrease revenues, calling into question the soundness of their finances. Therefore, fiscal manipulation may jeopardize a favorable IMF report, potentially reducing the country’s access to international capital, both from the IMF and from international bond markets.

<sup>3</sup>Observers do not eliminate fraud, but make it more costly or more likely to be discovered.

<sup>4</sup>For the theoretic foundation for the IMF’s delegated monitor role, see Tirole (2002). For empirical support of the importance of IMF signaling to international bond markets, see Bordo, Mody, and Oomes (2004) and Mody and Saravia (2006).

A few examples help illustrate this dynamic. Russian President Boris Yeltsin came under criticism from the IMF in 1996 for ordering the transfer of central bank money to government coffers in order to cover his pre-election spending and tax breaks.<sup>5</sup> In contrast to the previous year in which Russia was praised by the IMF for successful implementation of their fiscal austerity program (and received an additional \$525 million loan), the 1996 spending provoked stern IMF warnings and drew attention to Yeltsin's electorally motivated change of course.<sup>6</sup>

Similarly, following an IMF projection that pre-election spending would bloat the budget deficit, the Philippine government sought to reassure investors, arguing that government spending would be "a matter of socioeconomic priority and not a matter of political expediency."<sup>7</sup> In other cases IMF officials have also used high levels of pre-election spending to justify caution in extending post-election loans, as in Sri Lanka,<sup>8</sup> or to apply pressure on governments to cancel pre-election promises of tax cuts, as in Croatia.<sup>9</sup> This pattern of reaction by the IMF is visible to other leaders facing similar forms of international scrutiny.

Additionally, scholars have argued that governments prefer not to be under IMF agreements during elections, and research has shown that governments are more likely to enter into IMF agreements after elections (Przeworski and Vreeland 2000). Entering an IMF agreement early in a government's term increases the likelihood that "the stigma of signing an agreement will be forgiven or forgotten before the next elections" (Przeworski and Vreeland 2000, 394). It also increases the likelihood that the short-term pain of an economic reform program will be forgotten or superseded by the benefits of the reforms by the next election.

Although governments may prefer not to enter into new IMF agreements until after an election, the majority of elections in the developing world are held while countries are already under an IMF agreement. Many countries use IMF facilities for prolonged periods of time (Bird 2007; Conway 2007). In fact, the average time a given country is under an IMF agree-

ment is more than five years, with many countries continuously under IMF agreements for 10 years or more (Vreeland 2007, 56–58). For the developing countries in our study's sample, more than half of all elections were held during periods in which countries were under IMF agreements. Incumbents therefore often campaign during periods in which government expenditures are constrained by IMF scrutiny. It should be more difficult for countries to engage in pre-electoral fiscal manipulation when under an IMF agreement than when not under an IMF agreement. As a result, lower levels of pre-electoral fiscal manipulation are expected when countries are under an IMF agreement, leading to Hypothesis 2.

*H2: Pre-electoral fiscal manipulation is less likely when countries are under an IMF agreement.*

The presence of an IMF agreement should reduce the likelihood of pre-electoral fiscal manipulation. This should only matter, however, if the government would have been likely to engage in pre-electoral fiscal manipulation in the absence of an IMF agreement. Whether or not the government manipulates the economy prior to an election is influenced by other variables, particularly the other options available to the government for increasing its electoral chances. When the government plans to commit direct electoral fraud, it should be less likely to engage in pre-electoral fiscal manipulation. There is less need to persuade voters with indirect tactics like social spending or tax breaks if, for example, opposition parties have been repressed or if planned election fraud means that the election outcome is not in question. The effect of an IMF program on pre-electoral fiscal manipulation should depend on whether election monitors are present. In the absence of election monitors, the constraint imposed upon government finances by IMF conditionality may be irrelevant—they were unlikely to engage in pre-electoral fiscal manipulation anyway. In contrast, pre-electoral fiscal manipulation becomes a more likely policy choice when international election observers are present. Therefore, the constraining effect of an IMF agreement on pre-electoral fiscal manipulation will be much greater when election monitors are present than when election monitors are absent, generating Hypothesis 3.

*H3: The negative effect of an IMF agreement on pre-electoral fiscal manipulation is stronger when election monitors are present.*

Similarly, the effect of election monitors on the use of pre-electoral fiscal manipulation should be

<sup>5</sup>Marielle Eudes. "Yeltsin reaches into central bank's coffers in pre-election spree." June 6, 1996. *Agence France Presse (AFP)*.

<sup>6</sup>"Financial Focus: IMF loan boost for Yeltsin." *Lloyd's List*, September 16, 1995.

<sup>7</sup>"Philippine FY deficit will not be bloated by election spending." Feb. 3, 2003. *AFX*.

<sup>8</sup>Amal Jayasinghe. "Sri Lanka looks to raise new foreign loans as budget slips." May 23, 2004. *AFP*.

<sup>9</sup>"Croatia postpones reduction in value-added tax." May 26, 2004. *Deutsche Presse-Agentur*.

tempered by IMF agreements. Governments experiencing both types of international scrutiny must weigh the increased cost of electoral fraud due to election monitors against the constraints of the IMF agreement. As a result, the presence of election monitors should have less of an effect on the use of pre-electoral fiscal manipulation when the country is under an IMF agreement than when the country is not under an IMF agreement, leading to Hypothesis 4.

*H4: The positive effect of election monitors on pre-electoral fiscal manipulation is weaker when the country is under an IMF agreement.*

Overall, pre-electoral fiscal manipulation is most likely when election monitors are present and the country is not under an IMF agreement. The larger implication is that governments facing both types of international scrutiny will be more constrained in their ability to manipulate elections in their favor, either through fiscal manipulation or election fraud.

## Illustrative Cases

Before evaluating these hypotheses with cross-national quantitative data, we first describe elections in Hungary, Zambia, and Georgia to document these dynamics in greater detail. These cases were selected because they exhibit variation in our central explanatory variables: whether governments were under an IMF agreement and whether elections were monitored. No set of elections in our study includes the ideal conditions for a natural experiment in which all other variables are held constant and IMF agreements and international monitors are randomly assigned to countries. Nevertheless, documentation of overtime variation within these countries supplements the quantitative analysis by underscoring four points: (1) governments use fiscal manipulation to increase their chances for reelection, (2) government use of this tactic has occurred as a response to international scrutiny of elections, (3) IMF scrutiny of the economy constrains the use of fiscal manipulation, and (4) depending on their unique circumstances, governments facing both international scrutiny of their elections and their economy may be willing to risk criticism of their elections in order to avoid suspension of an IMF agreement, or vice versa.

The Hungarian elections of 1994, 1998, and 2002 were all internationally monitored and exhibited low levels of overt election fraud, but varied in IMF scrutiny over time. In 1991, Hungary and the IMF

negotiated an agreement to provide the country with access to \$100 million over three years to ease the country's postcommunist transition. The agreement mandated that the government reduce its budget deficit to 3.5% of GDP prior to the disbursement of funds. By 1993, the government had not met this target, and the IMF had refused to release funds. As a result, the IMF and the government renegotiated the agreement, loosening the deficit requirement in return for incorporating austerity measures in the 1994 budget.<sup>10</sup> This budget hampered the government's ability to engage in fiscal manipulation prior to the 1994 election, which the incumbent government lost to a socialist led left-liberal coalition. Although economic conditions leading up to the 1994 elections were poor and the governing coalition was not popular, the government was constrained by both international political and economic scrutiny, and there is little evidence that it employed fiscal manipulation.

Projecting itself as the party of competent economic governance, in 1996 the new government negotiated a two-year IMF agreement predicated on the implementation of broad structural reforms, including budget deficits not to exceed 3% and early repayment of outstanding loans.<sup>11</sup> The government adhered to the agreement, and the IMF approved access to all installments of the loan. Yet the government chose not to withdraw the funds. Even before negotiating the agreement, Hungary did not need the loan but wanted the appearance of compliance with an IMF agreement. As the finance minister explained, "... we no longer needed the money, only a signal from the IMF that our economic policy is on the right course."<sup>12</sup> This policy of fiscal constraint under IMF scrutiny carried into the 1998 election. The government kept the budget deficit low, although there were some signs of fiscal manipulation, including free public transportation for senior citizens.<sup>13</sup> The IMF also noted fiscal electioneering during local

<sup>10</sup>"Hungary fails to qualify for IMF loans" *AFP*, 6 Feb 1993. "Hungary's 1994 deficit shouldn't exceed 5.6 percent of GDP: IMF" *AFP*, May 7, 1993. "Hungary; Tea, anybody?" *The Economist*, June 12, 1993. IMF (2000a).

<sup>11</sup>On the technocratic basis of the Hungarian socialist party, see Bozóki 1997; Körösenyi 1999; Racz 2003; and Tóka and Enyedi 1999, 198–223. "IMF delegation to visit Hungary to discuss standby deal," *AFP*, Sept. 4, 1995. "Hungary to repay billion dollars in foreign debt ahead of time: bank"; *AFP*, Jan. 10, 1996.

<sup>12</sup>"Hungary Needs No New IMF Loan—Officials," *Hungarian News Agency (MTI)*, Feb 5, 1998.

<sup>13</sup>"Hungarian Election Campaign Full of 'Freebies' for Voters," *Deutsche Presse*, Jan. 20, 1998.

elections held after the national elections, yet the national budget won praise in the same IMF report, as the deficit was smaller than expected.

Taking back power from the socialist-led coalition, conservatives won the 1998 election and chose not to negotiate a new IMF agreement (IMF 1999a). Although the conservative government initially continued its predecessor's economic approach (IMF 2000b), by 2001 the IMF was cautioning the government over its expansionary fiscal policies (IMF 2002).<sup>14</sup> Confident in the durability of Hungary's new reputation for economic responsibility, Prime Minister Viktor Orban rebuked IMF criticism, noting that the country could now obtain credit from a diverse range of financial institutions, and stating that, "[t]he Hungarian economy is strong enough that an IMF report can be taken as but one opinion that is worthy of consideration."<sup>15</sup> Engaging in overt fiscal manipulation prior to the 2002 elections, the government rolled out a series of tax cuts and spending increases, which resulted in a doubling of the budget deficit, reaching a decade high of 9.4%. The IMF was unsparing in its analysis: "[W]ith elections in 2002, fiscal policy was highly politically charged and turned very expansionary, contributing to macroeconomic imbalances and an inordinate burden on monetary policy" (IMF 2003a). The conservatives lost power despite their use of fiscal manipulation, and the new socialist government quickly moved to repair relations with the IMF, reducing the deficit to 5.9% by 2003.

A comparison of the 1991 and 1996 elections in Zambia reveals a similar dynamic, but provides evidence of a government choosing direct election fraud and paying the price of a negative report from election observers in favor of maintaining fiscal austerity under IMF agreements. Caught between international creditor demands for repayment and widespread public pressure for domestic subsidies, Zambian President Kenneth Kaunda's economic policy vacillated throughout the 1980s. IMF insistence that the government reduce maize subsidies repeatedly provoked opposition riots, and in 1987 led the government to abandon IMF-mandated reform programs (Baylies and Szeftel 1992). IMF loan disbursements were suspended until the government resumed its economic reforms in 1989. As before, the reforms provoked widespread public protests and

galvanized the opposition (Bratton 1992; Nasong'o 2005). Facing increased international and domestic pressure, Kaunda promised to hold democratic elections in 1991, and agreed to invite international election observers. In the face of stiff electoral competition, Kaunda attempted to create favorable economic conditions to enhance his popularity, abandoning the IMF-mandated reform package and further loosening fiscal policy (Rakner 2003, 66). The IMF officially suspended cooperation in September 1991, just a month before the election.<sup>16</sup> Despite his efforts, Kaunda lost to Frederick Chiluba after 27 years in power.

President Chiluba quickly negotiated a new IMF program, remaining responsive to the IMF throughout his tenure in office even as his political support deteriorated.<sup>17</sup> Facing a challenge from former president Kaunda in the 1996 elections, Chiluba turned to more direct methods of election manipulation and engineered constitutional amendments that effectively prohibited Kaunda from participating in the presidential election (Baylies and Szeftel 1997; Gould 2002). Kaunda and his party launched an official election boycott, and several major international monitors protested the new rules by refusing to send delegations to monitor the elections, although the elections were still monitored by NDI and the United Nations (Gould 2002, 304). Several donors, including the United States, suspended bilateral aid in response to the election manipulation.<sup>18</sup> The electoral process itself was marred by further controversies over voter registration (Baylies and Szeftel 1997; Donge 1998; Gould 2002). The NDI delegation, the foreign press, and most large domestic monitoring groups reported the elections as flawed (Bratton 1998; Gould 2002). The IMF, on the other hand, did not criticize the government's electoral conduct. Chiluba adhered to agreed policies and Zambia's deficit shrank between 1995 and 1996 (IMF 1999b, 29). Highlighting the conflict between international political and economic scrutiny, several key IMF member-states pressured the IMF to curtail its relationship with Chiluba because of his reliance on election fraud. As a diplomat stationed in Zambia remarked, "the irony is that the problem arose partly because Chiluba was

<sup>16</sup>"Zambia: Out of the maize," *Economist*, Oct., 5 1991.

<sup>17</sup>"Zambia's Ruling Party Faces Split," *Africa News*, June 1995; "Zambian opposition figure warns country still in turmoil," *Deutsche Presse*, July 22, 1995.

<sup>18</sup>"IMF and World Bank aid to Zambia continues," *Deutsche Presse*, July 20, 1996.

<sup>14</sup>"IMF urges Hungary to tighten fiscal policy to lower inflation before EU entry" *AFX European Focus*, May 18, 2001.

<sup>15</sup>"Hungarian Prime Minister Critiques IMF Report," *Deutsche Presse*, June 6, 2001.

'good' by stringently sticking to IMF and World Bank demands for economic reform."<sup>19</sup>

Georgia presents a more nuanced case that nevertheless demonstrates the clear use of pre-electoral fiscal manipulation and government response to international economic and political scrutiny. Legislative elections in October 1999 and presidential elections in April 2000 were internationally monitored by the OSCE/ODIHR. The lead up to the 1999 legislative election saw intensive negotiations between the Georgian government and the IMF, as the Georgians sought to secure the final installments of a three-year IMF program and develop plans for a successor program. Relations between Georgia and the IMF had been souring for some time, and IMF officials were particularly critical of Georgia's increasing budget deficit and pushed the country to limit expenditures and increase tax collection.<sup>20</sup> To smooth IMF relations, Georgian President Eduard Shevardnadze agreed to an \$8 million cut, though acknowledged that this amount was "rather symbolic compared to the expected one."<sup>21</sup> Firm steps were not taken to improve tax collection, and revenues declined after years of steady growth (IMF 2000a). The government's failure to restrain spending led the IMF to break cooperation with Georgia shortly before the legislative election. Domestically, critics blamed Shevardnadze's supporters for the large 1999 deficit, pointing to increases in state funded electricity provision and road construction in the run-up to the vote (Areshidze 2007). The IMF concurred, stating that "increased pressure from the weak fiscal position... and the run-up to the parliamentary elections led to a more rapid expansion of net credit to government in the last four months of 1999" (IMF 2000c). Following the legislative elections, continuing disputes over the 2000 budget led the IMF to extend its freeze in cooperation with Georgia.<sup>22</sup> Shevardnadze, meanwhile, won the presidential election easily. Despite his popularity, however, election observers criticized the elections, and pointed out

<sup>19</sup>"Zambia Falls Off Africa's Development Bandwagon," *Christian Science Monitor*, Aug. 19, 1996.

<sup>20</sup>"IMF examining release of ESAF tranche to Georgia," *Interfax*, Jan. 20, 1999; "IMF team said to set conditions for Georgian budget," Associated Press, Jan. 28, 1999; "IMF 'generally pleased' with Georgian reform, still critical of customs receipts," *Prime-News Agency*, May 19, 1999.

<sup>21</sup>"Georgia cuts budget expenses at IMF demand" TASS, July 9, 1999.

<sup>22</sup>"IMF concerned about Georgian Budget," *Prime-News Agency*, Sept. 23, 1999; "World Bank to hold back loaning Georgia until next spring," TASS, Dec. 14, 1999.

widespread electoral tampering on Shevardnadze's behalf. Even Shevardnadze's party acknowledged that "local governors showed too much zeal" in their electoral efforts.<sup>23</sup>

In early 2001 a newly negotiated IMF agreement overlapped with steady improvement in fiscal conditions between 1999 and 2002 (IMF 2003b). In the lead up to the 2003 legislative elections, however, IMF officials repeatedly expressed concerns about the deteriorating fiscal outlook. They pushed the government to rollback recent reductions in electricity tariffs in order to boost revenue, an unpopular demand Shevardnadze complied with shortly before the election.<sup>24</sup> The incumbent president showed additional signs of fiscal restraint, such as his initial resistance to calls by an opposition-led hunger strike to disburse delayed pension payments (Areshidze 2007). Ultimately the government's failure to make significant cuts to the budget led to a temporary suspension of further IMF loans shortly before the election.<sup>25</sup>

Meanwhile, Shevardnadze's political bloc was facing stiff competition in the legislative elections. Accusations of massive electoral violations by foreign and domestic observers prompted a post-election protest movement led by opposition parties, which was legitimized by international condemnation of government-sponsored election fraud, and eventually led to Shevardnadze's resignation in the 'Rose Revolution.'<sup>26</sup> Opposition leader Mikheil Saakashvili won an overwhelming victory in the January 2004 presidential election and his bloc was victorious in subsequent legislative elections held in March. The minor growth in the fiscal deficit that occurred in 2003 was followed by significant increases in income in 2004, leaving the country with a budget surplus for the first-time in its postcommunist history.<sup>27</sup> Overall,

<sup>23</sup>"Shevardnadze victory flawed, observers say," *Globe and Mail*, April 11, 2000; "His last chance," *The Economist*, April 15, 2000.

<sup>24</sup>"IMF unhappy with Georgia's revenue collection," *Iprinda New Agency*, Feb. 21, 2003; "IMF Against Electricity Tariff Reduction in Georgia," *Central Asia & Caucasus Business Report*, March 3, 2003; "Georgia told to get its act together before next IMF visit," *Prime-News Agency*, June 22, 2003; "IMF Extends Deadline For Georgia to Meet Obligations," *Business Report*, July 8, 2003; "Georgia meets IMF requirement to increase electricity tariffs," *Prime-News Agency*, Aug. 15, 2003.

<sup>25</sup>"IMF Suspends Programs in Georgia," *World News Connection*, Sept. 5, 2003.

<sup>26</sup>On the "Rose Revolution," see Fairbanks (2004), Mitchell (2004), and Wheatley (2005).

<sup>27</sup>Areshidze points out that a significant portion of the revenue increase came from one-time fines paid by public officials and businessmen that were detained during the anticorruption sweeps of the newly installed government (2007, 211-17).

this case illustrates that international political and economic scrutiny constrained Georgian government behavior despite efforts to engage in election fraud and overtime changes in IMF agreements.

## Quantitative Analysis

This section explores the hypotheses presented above with a quantitative analysis of fiscal manipulation in 94 developing countries, 1990–2004.<sup>28</sup> The results are consistent with our expectations: fiscal manipulation is most likely when elections are internationally monitored and countries are not under IMF agreements.<sup>29</sup> The baseline model used in this article is similar to Brender and Drazen's (2005) analysis of fiscal manipulation. This model was chosen for two reasons. First, findings from Brender and Drazen (2005) and Shi and Svensson (2006) represent the alternative hypothesis for this project—that developing countries engage in pre-electoral fiscal manipulation regardless of international scrutiny. Second, Brender and Drazen (2005) adopt a well-accepted array of controls for fiscal policy analyses in developing countries. The estimation technique is ordinary least-squares regression with country and year fixed effects.<sup>30</sup>

The dependent variable, *Change in Government Balance*, represents a change in the central government fiscal balance. It is positive when the budget is in greater surplus (smaller deficit) than in the previous year. Fiscal manipulation should be inversely related to *Change in Government Balance*—the more manipulation, the more negative the dependent variable. Data come from two sources—IMF (2007) and Brender and Drazen (2005). For most countries the IMF publishes government balance data in its *International Financial Statistics*. Brender and Drazen

augment the data missing from these series with data from other IMF publications.<sup>31</sup>

Election data were collected by Hyde and Marinov (2009) and include descriptive information on all elections for national office, even those occurring in the most undemocratic countries.<sup>32</sup> The theory developed in this article presupposes that holding an election implies some risk that the incumbent will give up power. In some elections, however, opposition is banned or otherwise restricted. To exclude elections that are a priori uncompetitive, *Election* is coded from three questions in these data: Was opposition allowed? Was more than one party legal? Was there a choice of candidates on the ballot?<sup>33</sup> *Election* is coded 1 if the answer to all three questions is “yes” and 0 otherwise, generating a list of potentially competitive elections.

Data for *Monitors* are from Hyde (2006) and indicate whether an official delegation of foreign observers was present at a given election. Excluded from this measure are monitors from a priori “friendly” organizations that had never previously criticized an election, as these monitors were unlikely to criticize an election even if fraud were widespread, and therefore were unlikely to increase the costs or risks for election fraud. Thus, an election is only considered monitored if at least one of the monitoring organizations present had previously condemned an election as fraudulent. *IMF Agreement*, coded 1 when a country is under an IMF agreement and 0 otherwise, is included in the analyses to capture the effect of IMF program participation on a government's fiscal stance. Data on IMF program participation are from Vreeland (2003).<sup>34</sup>

Figure 1 presents the mean value of *Change in Government Balance* and the total number of observations in each category for eleven different sets of observations, distinguished by elections, election monitoring, and IMF program participation. In this comparison of mean values, pre-electoral fiscal manipulation is highest when election monitors are present and the country is not under an IMF agreement, which is consistent with our argument.

<sup>28</sup>Countries listed at <http://hyde.research.yale.edu/research.htm>, in the Online Appendix-A (OA-A). We focus on developing countries because most IMF loans are made to developing countries and election monitoring is prevalent. We selected 1990–2004 because election monitoring was relatively rare before 1990 and because IMF conditionality was more comprehensive after 1990.

<sup>29</sup>OA-C shows that the findings are robust to alternative specifications, alternative measures of variables, other data samples, and exclusion of outliers.

<sup>30</sup>See OA-C. Results are not a function of the specific estimation technique. We run a random effects model, models with only country and only year fixed effects, and a model with panel corrected standard errors, all of which provides significant support for our argument.

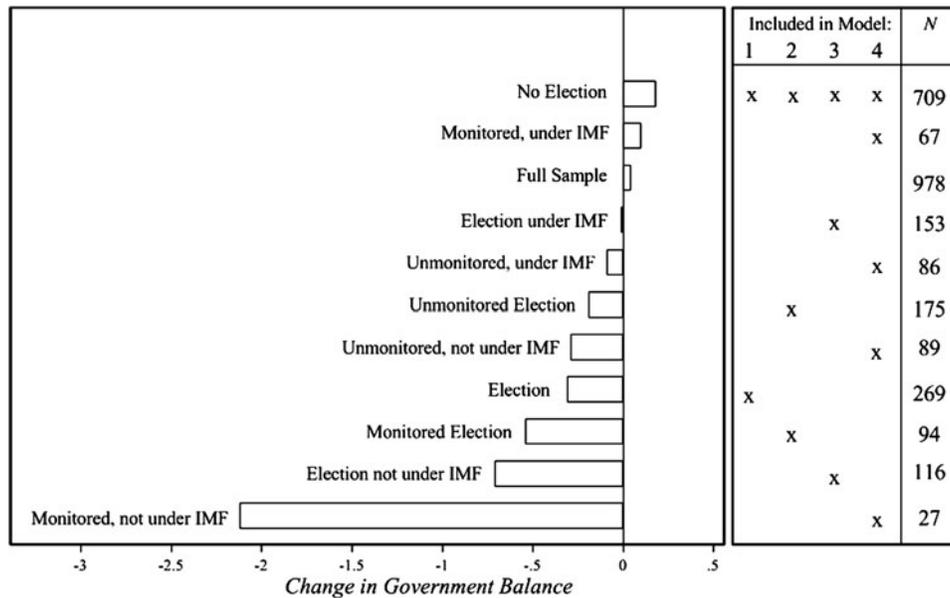
<sup>31</sup>To verify that there is no systematic bias caused by splicing two data sources, we re-run our analyses using each data source separately. The results are comparable but somewhat weaker.

<sup>32</sup>A country may have more than one election in a given year. For consistency, the analysis considers that a given event occurred if it took place in any election during the country-year.

<sup>33</sup>OA-B describes data on elections and election monitoring in greater detail.

<sup>34</sup>IMF program participation post-2000 was provided by James Vreeland.

FIGURE 1 Mean Change in Government Balance across Categories included in Models 1—4



The analyses also include a series of economic and demographic control variables (World Bank 2007). *GDP per capita* (logged) and *GDP Growth* are included to control for income effects. *Trade* is included as a constraint on budget deficits. *Population between 15 and 64* represents the fraction of the population presumed to be of working age. The greater the working age population, the greater the tax base, all else equal. Conversely, the greater the *Population 65 and above*, the greater the demand for government expenditures. *Government Balance, lagged* is included to control for temporal dependence.

Table 1 presents the results. Model 1 shows that elections are associated with a 0.5 percentage point decline in government balance, which supports the alternative hypothesis that developing countries engage in pre-electoral fiscal manipulation unconditionally. Model 1 also suggests that subsequent evidence of international scrutiny's constraining effect does not stem from an analysis biased against the alternative hypothesis.

To test Hypothesis 1, Model 2 includes an interaction between *Election* and *Monitors*. To better gauge support for Hypothesis 1, Figure 2 graphically displays the marginal effect of an election on fiscal manipulation as monitoring varies. When monitors are present, elections are associated with a 0.9 percentage point decline in government balance, which is three times the size of the statistically insignificant decline when monitors are not present. These results suggest governments engage in greater fiscal manipulation when election monitors are present.

To test Hypothesis 2, we include an interaction between *Elections* and *IMF Agreement* in Model 3 and present the results graphically in Figure 2. In support of Hypothesis 2, elections are associated with a 0.8 percentage point decline in government balance for countries not under an IMF agreement, an effect that is twice as large as that for countries under an IMF agreement.

Although Models 2 and 3 provide support for Hypotheses 1 and 2, if the effects of international economic and political scrutiny are interrelated, then Models 2 and 3 are improperly specified. Thus, Model 4 includes a three-way interaction between *Election*, *Monitors* and *IMF Agreement* to evaluate the extent of fiscal manipulation under both types of scrutiny.

If Hypothesis 3—that the constraining effect of an IMF agreement is stronger when election monitors are present—is correct, then fiscal manipulation should be significantly higher when election monitors are present and the country is not under an IMF agreement than when election monitors are present and the country is under an IMF agreement. Conversely, when election monitors are not present, the level of fiscal manipulation should not be significantly different whether or not the country is under an IMF agreement. Based on the results in Figure 2, Hypothesis 3 receives strong support. When monitors are present but countries do not participate in an IMF program, elections are associated with a 1.9 percentage point decline in government balance. In contrast, when international election monitors are

TABLE 1 International Scrutiny and Pre-Electoral Fiscal Manipulation

	Model 1	Model 2	Model 3	Model 4
Government Balance, lagged	-0.58 * (0.03)	-0.59 * (0.03)	-0.58 * (0.03)	-0.58 * (0.03)
Election	-0.52 * (0.22)	-0.31 (0.27)	-0.76 * (0.34)	-0.43 (0.37)
Election x Monitors		-0.61 (0.43)		-1.51 * (0.72)
Election x IMF Agreement			0.44 (0.45)	0.24 (0.53)
Election x Monitors x IMF Agreement				1.19 (0.87)
Under IMF Agreement	0.22 (0.27)	0.24 (0.27)	0.10 (0.30)	0.05 (0.30)
GDP per capita (logged)	-1.84 (1.21)	-1.77 (1.21)	-1.84 (1.21)	-1.71 (1.21)
GDP Growth	0.10 * (0.02)	0.10 * (0.02)	0.10 * (0.02)	0.10 * (0.02)
Trade (logged)	-0.05 (0.69)	-0.02 (0.69)	-0.06 (0.69)	-0.08 (0.69)
Population between 15 and 64	-0.40 (0.34)	-0.11 (0.11)	-0.11 (0.11)	-0.12 (0.11)
Population over 65	-0.12 (0.11)	-0.43 (0.34)	-0.40 (0.34)	-0.43 (0.34)
Constant	17.61 * (8.62)	17.03 * (8.63)	17.57 * (8.62)	17.24 * (8.63)
Adjusted R2	0.40	0.43	0.43	0.43
Observations	978	978	978	978

\*p < 0.05. Standard Errors in parentheses.

absent, there is no statistically significant evidence of pre-electoral fiscal manipulation regardless of IMF program participation.

As with Hypothesis 3, Hypothesis 4—that the presence of election monitors is more likely to increase pre-electoral fiscal manipulation when countries are not under an IMF agreement—receives strong support. When countries are not under an IMF agreement, fiscal manipulation is four times greater when election monitors are present than when election monitors are absent. In contrast, when countries are under an IMF agreement, there is no statistically significant evidence of pre-electoral fiscal manipulation, regardless of the presence of election monitors.

With respect to international scrutiny, countries that face election monitoring but are not under an IMF agreement appear most likely to employ fiscal manipulation. In the absence of election monitors, fiscal manipulation appears less likely, indicating that such indirect means of electoral manipulation are less desirable when direct election manipulation is easier. Similarly, pre-electoral fiscal manipulation is insignificant when a country is under an IMF agreement, suggesting that being under an IMF agreement consistently acts as a constraint on fiscal policy.

## Alternative Explanations

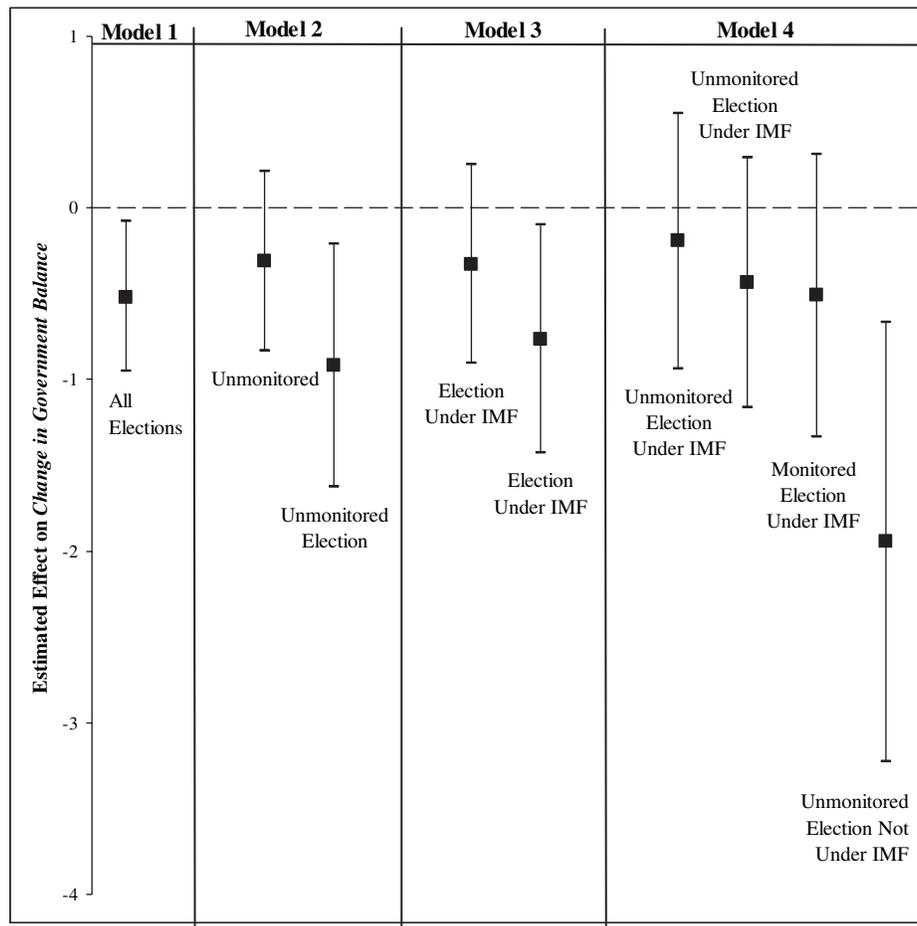
In this section, we consider several alternative explanations that could plausibly account for the effects of election monitoring and IMF program participa-

tion on pre-electoral fiscal manipulation. For each alternative explanation, we reestimate Model 4 with the addition of the variable relevant to the alternative explanation, as described below. For ease of interpretation, Figure 3 graphs the marginal effects and 95% confidence intervals on *Change in Government Balance* for our central variables of interest across all six alternative explanations. The full results are confined to the online appendix.

In the analyses presented above, participation in an IMF program has been treated as exogenous; however, because the IMF and governments negotiate agreements, there is a selection effect to IMF program participation. This effect could confound the analysis if the same factors that lead countries to participate in an IMF agreement also reduce fiscal manipulation. To assess whether the constraining effect of an IMF agreement identified in Model 4 reflects factors associated with countries negotiating IMF agreements, we reestimate Model 4 including an interaction between *IMF Hazard Ratio*, which captures countries' likelihood of participating in an IMF program, and *Election*.<sup>35</sup> If the IMF program participation effect evidenced in Model 4 reflects the likelihood of IMF program participation rather than an actual participation effect, then pre-electoral fiscal manipulation should decline as the *IMF Hazard Rate* increases and there should be no significant electoral effect to an *IMF Agreement*. This is not the case. As

<sup>35</sup>Figure 3's point predictions and confidence intervals are derived from models presented in OA-C. The selection model, presented in OA-D, is based on Nooruddin and Simmons (2006).

FIGURE 2 Estimated Marginal Effects of Elections on the use of Pre-Electoral Fiscal Manipulation



Notes: Full models provided in the Online Appendix C. Markers (■) indicate estimated marginal effects on *Change in Government Balance* from the models specified. Interactions between *Elections*, *Monitors*, and *IMF Agreement* vary across models. Bars indicate 95% confidence intervals.

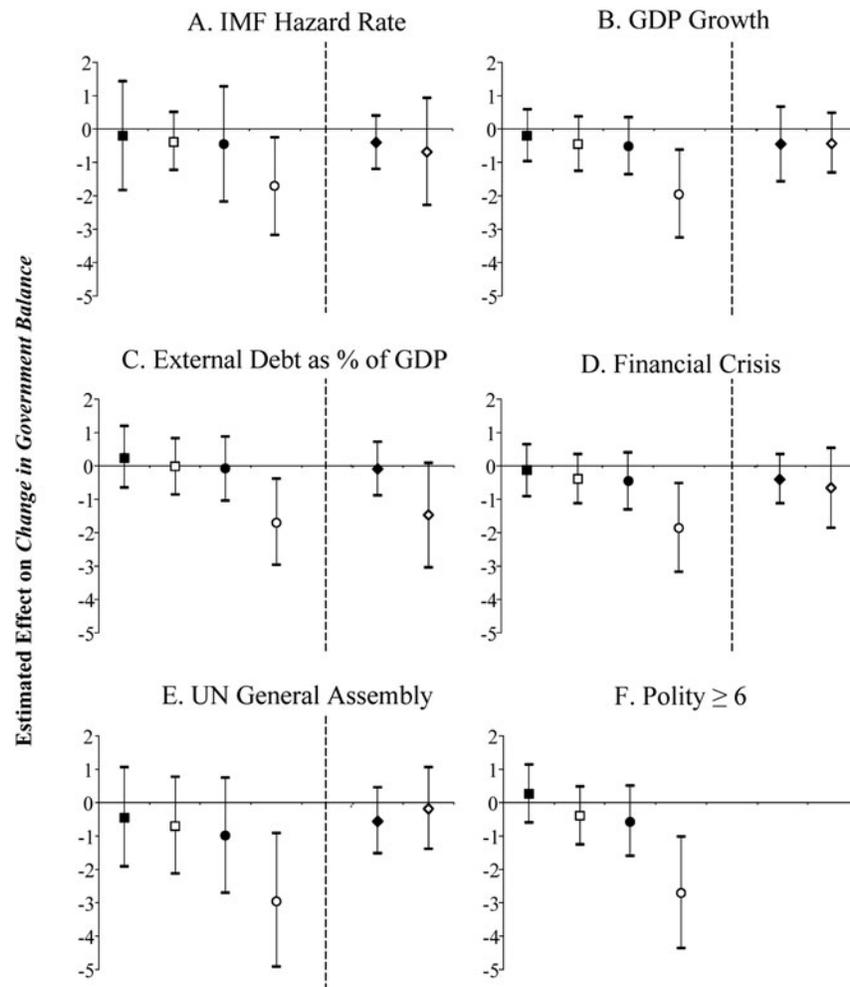
shown in Figure 3 (A), our argument continues to receive statistically significant support, while the likelihood of IMF program participation does not appear to constrain pre-electoral fiscal manipulation.

Alternatively, the ostensibly constraining effect of an IMF agreement may be a proxy for poor economic conditions such as low GDP growth, high external debt, or a financial crisis. Under this alternative hypothesis, governments forgo pre-electoral fiscal manipulation not because they face IMF scrutiny, but because they lack the fiscal wherewithal to engage in manipulation. Poor economic conditions may constrain fiscal manipulation in two ways. First, poor conditions reduce the amount of money governments have at their disposal to manipulate the economy. Second, poor conditions reduce a country's attractiveness to international creditors, thus reduc-

ing the government's ability to borrow internationally to fund fiscal manipulation. To test this hypothesis, we replicate Model 4, including an interaction between *Election* and three alternative proxies for poor economic conditions—*GDP Growth*, *External Debt as a % of Exports* and *Financial Crises*.<sup>36</sup> As can be seen in Figure 3 (B–D), pre-electoral fiscal manipulation does not appear to covary with economic conditions. In support of our argument, across all models including these measures, pre-electoral fiscal manipulation remains greatest when election monitors are present and the country is not under an IMF agreement. There remains no

<sup>36</sup>Data for *Financial Crisis* are from Laeven and Valencia (2008). OA-C includes each variable independently as an alternative specification to Model 4. Our results remain robust.

FIGURE 3 Estimated Marginal Effects of Elections on the use of Pre-Electoral Fiscal Manipulation; Alternative Explanations



Notes: Full models provided in Online Appendix C. In figures A-F, markers indicate point predictions of marginal effects on *Change in Government Balance* when Model 4 is modified, as described in the text for the following variables of interest:

- Unmonitored Election, Under IMF Agreement
- Unmonitored Election, Not Under IMF Agreement
- Monitored Election, Under IMF Agreement
- Monitored Election, Not Under IMF Agreement

In Figures A-E, additional markers indicate marginal effects when each variable (A-E) is:

- ◆ High (95<sup>th</sup> percentile)
- ◇ Low (5<sup>th</sup> percentile)

statistically significant evidence of pre-electoral fiscal manipulation when countries are under an IMF agreement or when monitors are absent.

We also consider the recent finding that the credibility of IMF conditionality, and therefore the constraining effect of IMF scrutiny, may vary depending on countries' political importance to the United States (Dreher and Sturm 2006). If this is correct, then pre-electoral fiscal manipulation should be positively correlated with a country's importance

to the United States. We assess this hypothesis by rerunning Model 4, including an interaction between *Election* and *UNGA Voting Record*, which captures countries' voting congruence with the United States in the United Nations General Assembly (*Ibid.*). As can be seen in Figure 3 (E), there does not appear to be a significant relationship between a country's voting affinity with the United States and pre-electoral fiscal manipulation. Furthermore, controlling for a country's political importance to the United

States does not weaken the effects of international scrutiny on pre-electoral fiscal manipulation.

Finally, country-specific research on political business cycles suggests that fiscal manipulation varies based on countries' democratic consolidation (Gonzalez 2002). To assess whether our results are an artifact of competitive elections in nondemocratic regimes, we rerun Model 4 limiting the analysis to country-years that are nominally democratic according to the widely used *POLITY* dataset's cross-national index of regime type (i.e., receive a *POLITY* score of 6 or above; Marshall and Jaggers 2002). As can be seen in Figure 3 (F), our argument receives support even when limiting the analysis to nominally democratic observations, suggesting that pre-electoral fiscal manipulation is not limited to relatively non-democratic regimes.

## Conclusion

International scrutiny of elections and the economy act as constraints on government behavior throughout the developing world. International election observers make indirect or legal tactics of election manipulation more likely by increasing the costs of overt forms of election fraud. IMF scrutiny of the economy and pressure on governments to maintain a sustainable fiscal policy make pre-electoral fiscal manipulation less likely and should also make direct forms of manipulation such as election fraud more likely. Together, these forms of international scrutiny influence the use of pre-electoral fiscal manipulation in cross-cutting ways, increasing the use of pre-electoral fiscal manipulation when elections are internationally observed and decreasing it when a government is under an IMF agreement. We have explored the consequences of international scrutiny on government use of pre-electoral fiscal manipulation, a tactic that recent scholarship highlights as an important tool that governments use to bias elections throughout the developing world. Our research suggests that scholars are correct in arguing that incumbents in developing countries may have greater incentives to engage in pre-electoral fiscal manipulation, but, by omitting the cross-cutting effects of international scrutiny, they are missing important constraints on these governments' scope for maneuver.

More generally, evaluating whether international scrutiny is "good" or "bad" is not straightforward. Fiscal manipulation may make it difficult to maintain

a sustainable budget, but it is not clear that fiscal manipulation is normatively worse than blatant election theft. Across other areas of election manipulation, increased international scrutiny should have similarly cross-cutting effects. There are many methods of election manipulation, and increasing international scrutiny across multiple issue areas should constrain governments in a manner that makes real electoral competition more likely, a proposition to be explored in future research.

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