Frank Bohn (Radboud University)

“Political Forecast Cycles”

Abstract

By forecasting overly optimistic revenues opportunistic governments can increase spending in order to appear more competent prior to elections. Ex post deficits emerge in election years, thereby producing political forecast cycles - as also found for US states in the empirical literature. In our theoretical moral hazard model we obtain three results which are tested with panel data for Portuguese municipalities. The extent of manipulations is reduced when (i) the winning margin is expected to widen; (ii) the incumbent is not re-running; and/or (iii) the share of informed voters (proxied by education) goes up.