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Risk taking and investing in electoral competition

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ABSTRACT

We analyze a two-player electoral contest game between a challenger and an incumbent. First, the challenger decides whether to choose a high-risk campaign (e.g., risky platforms, negative campaigning, an interactive Web technology) or a less risky one. In a second stage, both the challenger and the incumbent raise funds and invest in the electoral contest. The politicians differ in their fund-raising costs. According to theory, a high-cost challenger should choose high risk (gambling for resurrection). If the benefit of winning is sufficiently large, a low-cost challenger should take high risk either to discourage the incumbent or to prevent intense campaigning. Both effects are based on the fact that high risk campaigning reduces incentives to invest in the contest. In case of a rather small benefit of winning, a low-cost challenger should prefer low risk to avoid jeopardizing his competitive advantage. Our experimental findings show that gambling for resurrection plays a role. Taking low risk to preserve a competitive advantage is strongly supported by the data. However, reactions of low-cost challengers when facing high benefits of winning are heterogeneous.

1. Introduction

In many election campaigns we observe strong competition between two players—the challenger and the incumbent. Whereas the incumbent typically has a well-known agenda and follows a safe strategy by trying to benefit from familiarity and office experience, the challenger often chooses a risky strategy to achieve a competitive advantage (e.g., Druckman et al., 2009; Militia et al., forthcoming; Darmofal et al., 2011; Walter and van der Brug, 2013). Such risky behavior includes negative campaigning, the use of interactive Web technologies, introducing personal features, taking clear issue positions, and partisan emphasis.[1] For example, negative campaigning by the challenger can harm the incumbent but may also backfire on the challenger if voters dislike aggressive behavior. The riskiness of clear political positions has been highlighted by a large number of publications in politics and political economy (e.g., Shepsle, 1972; Mayhew, 1974; Alesina and Cukierman, 1990). Taking a clear position is beneficial for the challenger if the majority of voters takes a similar position, but may be detrimental if there are considerable gaps between the challenger's policy preferences and those of his constituencies. When the challenger takes risk, he has to decide whether high or low risk is optimal in his specific situation.

In this paper, we theoretically and experimentally analyze the behavior of a challenger and an incumbent in a stylized electoral competition game. Our theoretical setting is based on the standard rank-order tournament model,[2] which is extended by a

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[1] In their empirical analysis of U.S. congressional campaigns, Druckman et al. (2009) used these measures as proxies for risky behavior of the politicians. The authors define risky behavior as choosing actions that have high variance outcomes.

[2] Rank-order tournaments have been first analyzed by Tullock (1980) and Lazear and Rosen (1981). For more recent work on tournaments see Sheremeta (2010b), Ryvkin (2010), Chowdhury and Sheremeta (2011), Amegashie (2012), Franke (2012), Kräkel (2012), and Lee (2012). For an overview see Congleton et al. (2008a), Congleton et al. (2008b), Konrad (2009), and Long (2013). For an application of tournament theory to electoral competition see Erikson and Palfrey (2000), Meirowitz (2008), and Konrad (2009). The empirical findings of Rekkas (2007) stress the importance of campaign spending in electoral competition.

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risk-taking stage. At the first stage, the challenger has to decide between taking low or high risk. At the second stage, for given risk, the challenger and the incumbent compete by raising and investing funds in a political campaign.[3] Funds are used to persuade the voters of being the right candidate that should be elected. The more funds a politician has raised, the higher will be his likelihood of being elected.

We assume that the challenger and the incumbent differ in fund-raising costs. Often, politicians are associated with different reliability from the voters' point of view, or they have different skills or abilities, which are common knowledge (e.g., politicians differ in vocational qualifications). As a consequence, it is less costly (e.g., less time-consuming) for a leading or more able politician (the "favorite") to obtain financial resources from sponsors when competing against a trailing or less able opponent (the "underdog"). We can think of a situation where the incumbent politician is the natural favorite since he can make use of his previous political experience and his challenger is the underdog (e.g., Ashworth, 2006). However, there also exist situations in which the incumbent is the underdog due to past poor performance. In any case, the heterogeneity of the politicians has important implications for funding by interest groups.

Suppose that the risk taking challenger is the underdog. He should strictly benefit from a high risk since he has nothing to lose but good luck may compensate for the competitive disadvantage. Such behavioral pattern has been called a knife-edge or gambling for resurrection by Rose-Ackerman (1991), Downs and Rocke (1994), Carrillo and Mariotti (2001), and Eriksen and Kvaløy (2014). In our model, the underdog anticipates that in equilibrium he will not collect and invest more funds than the favorite. Thus, his winning probability cannot be larger than that of the favorite. The best the trailing challenger can do is to choose high risk in any situation in order to win the competition by luck. This strategic behavior is summarized as gambling for resurrection in the following.

Accordingly, if the risk taking challenger is the favorite, one would expect that he does not prefer a high risk which can jeopardize his favorable position. Our analysis shows that this guess is not necessarily true. We have to distinguish three different effects: First, there are situations in which risk taking influences the fund-raising efforts and, hence, effort costs of both politicians (cost effect). Following the cost effect, the favorite prefers high risk so that the outcome of the competition is mainly determined by luck. This high-risk strategy undermines overall incentives and, therefore, reduces both players' effort costs. Second, there are other situations in which the fund-raising efforts of both politicians do not react to risk taking—the favorite will always choose high effort and the underdog low effort. In this situation, risk only influences the politicians' likelihood of winning so that the favorite prefers a low-risk strategy to hold his predominant position (likelihood effect). This effect is the counterpart of gambling for resurrection by a risk-taking underdog. Third, if the benefit of winning the election is very large relative to the politicians' effort costs, the favorite will choose a high risk to further discourage his opponent (discouragement effect). In this situation, high risk destroys the underdog's incentives when collecting funds: It does not pay for him to invest in fund raising as he would bear rather high effort costs but the outcome of the electoral contest is mainly determined by luck. However, the favorite still invests in fund raising as he has to bear lower effort costs. Such discouragement will be very attractive for the favorite if the gain of winning the election is rather large (e.g., the politicians compete for becoming president or governor).

Altogether, the three effects point out that the challenger should not always prefer a rather safe strategy when being the favorite. On the contrary, both cost effect and discouragement effect make high risk a rational choice for a favorite. According to the cost effect, high risk prevents both politicians from acting too aggressively during the campaign, which would result into high effort costs. Following the discouragement effect, a risk taking favorite prefers a high-risk strategy in order to further demoralize his already trailing opponent.

The experimental part of the paper tests whether gambling for resurrection, the cost effect, the likelihood effect and the discouragement effect are relevant for real decision makers. Since the challenger is either the favorite or the underdog, we ran six treatments. The three treatments labeled disc_F, cost_F and likel_F consider risk taking by the favorite under the discouragement effect, cost effect and likelihood effect, respectively. In the treatments disc_U, cost_U and likel_U, we use the same parameter constellations as in the three treatments before but now the underdog is the risk taker.

Our experimental results point out that gambling for resurrection plays a role for underdogs when choosing risk. Underdogs most clearly gamble for resurrection when risk taking determines the players' winning probabilities but does not influence equilibrium efforts. This finding is quite intuitive since in the given situation subjects in the lab can fully concentrate on the direct effect of risk on the likelihood of winning without anticipating any spillover effects on the subsequent effort choices. The larger the underdogs' cost disadvantage relative to the favorites, the more often high risk is chosen by underdogs in stage 1. Intuitively, the more desperate the situation of the underdogs the more strongly they rely on the pure chance of winning by luck. Regarding the risk choice, the favorites very often make use of the likelihood effect and choose low risk to maximize their winning probability. They do not select high risk as often as theoretically predicted in the disc_F treatment. The behavior in the cost_F and cost_U treatments reveals two stable patterns: subjects either want to keep control by choosing low risk and high effort or make use of the cost effect by combining high risk with low effort. The subjects' effort choices as reactions to given risk are often in line with theory in the disc_ and likel_treatments. Our data shows that subjects indeed react to different amounts of risk.

Of course, our model and the experiment cannot capture all aspects that influence "real" political campaigns such as historical contingencies or candidate characteristics. Instead we focus on a specific aspect, namely risk taking, and study its impact on behavior of politicians. While we have to be cautious to transfer our findings one-to-one to "real" political campaigns and historical situations, we believe that our results offer valuable insights and help to understand the effects of risk taking in campaigns. Nevertheless, we want to briefly discuss some historical campaigns to give the reader an idea about the situations we

[3] For example, during the 2004 presidential election campaign, President Bush and the Republicans spent $1.14 billion, while expenditures of challenger Kerry and the Democrats amount to $1.08 billion (see Edsall and Grimaldi, 2004). See Houser et al. (2011) on informative advertising in political campaigning. Fink (2012) analyzes the impact of campaign spending in German elections.