



## Political support for enterprise restructuring and voting in Serbia

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### ABSTRACT

We examine political support for enterprise restructuring as reflected in voting and two elections in Serbia after 2000. There is no evidence that employment in the firms slated for restructuring influenced voting. However, restructuring appears to have resulted in a decline in support for pro-reform parties. Demographic factors had a crucial effect on voter behavior.

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### 1. Introduction

Political support is a necessary condition for sustainable reform in democracies. Its absence can give rise to two types of political constraints: (1) *Ex-ante* political constraints prevent the initiation and implementation of specific reforms because a government without political support seeking re-election would not be expected to embark upon reforms. (2) *Ex-post* political constraints can result in discontinuation, reversal or even annulment, of previously implemented reforms. Clearly, in democracies, sustainable reform is simply impossible without political support from the electorate. Thus, reforms are endogenous to the political process. Our objective is to examine, from a political economy perspective, reform policy toward real-sector enterprise restructuring in Serbia after 2000. Toward this end, we probe the link between political support and government decisions relating to restructuring.

### 2. Overview of theoretical and empirical contributions

Reforms in general do not result in Pareto improvement; rather, there are winners and losers. This gives rise to uncertainty because individuals cannot be sure about their position as gainers or losers after reform (Fernandez and Rodrik, 1991). Whether, and to the extent to which political parties will deliver on their election promises is another source of uncertainty. In such circumstances, those expecting to emerge as losers would be motivated to vote for anti-reform parties, as an *ex-ante* attempt to prevent reform from taking place. If reforms have taken place, those who have lost would attempt to stop, reverse or annul the reforms by voting for and bringing to power anti-reform parties, thereby imposing *ex-post* political constraints on the reforms. From a normative perspective, the question is how to specify a reform strategy that will provide the necessary political support for all reform steps (Dewatripont and Roland, 1992; Wyplosz, 1993). The pace of job losses in the state sector and job creation in the private sector matter (Aghion and Blanchard, 1994; Tichit, 2006).

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We identify three types of voters in the labor market:

- (1) Employees in state-owned enterprises, for whom comprehensive reform is not advantageous, since it would result in job loss. Therefore, they would be expected to vote for anti-reform parties in the belief that they would stop reforms, continue with subsidies to their firms, and preserve their jobs and social status. The only unknown element for them is the extent to which such an arrangement is sustainable — those voting for anti-reform parties do not know whether they will succeed in their aims, but, in principle, there is no incentive for them to vote for pro-reform political parties.<sup>1</sup>
- (2) Employees in private firms supporting reform, which they consider as a basis for advancement in their sector, and consequently for improving their own position. They have no incentive to vote for anti-reform political parties since this would lead to further deterioration in the private firms' business environment (higher tax burden, exacerbated conditions for business operations, new subsidies for state-owned firms, etc.); and in their own position, irrespective of their private firms' situation, due to the increase in compulsory income redistribution (providing compensation to the losers as a result of transition), and, in turn, increased personal tax burden.
- (3) One option for the unemployed, irrespective of whether they lost jobs in the state-owned or private sector, or have never been employed, is to vote for pro-reform parties. As the unemployed well know, their only sustainable employment is in the private sector (Rodrik, 1995), and, therefore, they support pro-reform parties that favor creating as many jobs as they can in the private sector as rapidly as possible. If this were so, it would have very significant consequences for the political economy of reform. There would only be *ex-ante*, and no *ex-post*, political constraints. The only important concern for reformist governments would be to initiate reform (restructuring, privatization and bankruptcy of state-owned firms), thereby creating unemployment. Thus, the unemployed would be at the forefront in providing political support, and, consequently, the problem of political reform sustainability would not exist. Contrary to such behavior, the unemployed would conceivably vote for anti-reform parties. There are two basic motives for this. First, they hope that the new authorities will stop, reverse or even annul the reform, thus giving them back their old jobs. In the case of privatization or liquidation of state-owned firms, the probability of this is small. Secondly, income redistribution, i.e., transfers to those who have lost their jobs, through generous unemployment benefits, prolonged coverage, among other increased welfare measures, is a more convincing reason. Obviously, the unemployed have motives to vote both for and against pro-reform parties, so some of them and their households may behave in one way, while others vote differently. The relative frequency of such behavior probably varies in different cases, and data can only be obtained *ex-post* empirically.

In identifying these three categories of voters, we also need to consider why people choose to vote, and for whom they choose to vote. Voter turnout in the two elections that we consider was 57.7% and 60.5% respectively. To explain rational voting behavior, we need to assume that utility from voting is not only based on the expected benefit from being decisive (an instrumental view of rational voting). We assume that individuals also vote expressively in support of their self-interest and may be influenced by expressive rhetoric of political parties.<sup>2</sup>

In prior empirical studies (Fidrmuc, 2000; Warner, 2001; Jackson et al., 2003; Valev, 2004; Kim and Pirttila, 2006; Smeets and Warzynski, 2006), the results regarding the relation between restructuring/unemployment and political support for pro-reform parties are ambiguous. There are a few explanations for such findings. First, the regression models used were based on the implicit assumption that constituencies vote predominantly on the basis of economic issues. However, voters' decisions are influenced by several factors, some of which are not related to economic variables. Secondly, even if the assumption that voters' decisions are based on economic variables were true, their rationality might be bounded. These decisions are taken against the backdrop of uncertainty, in terms of whether and to what extent a particular individual would be a loser or winner, and whether the parties for which he or she votes, if they come to power, would deliver on their promises. Thirdly, the assumption of voter's bounded rationality does not necessarily indicate a bias of his/her error. The possibility that the error might be randomly distributed can be rejected due to asymmetry of the complexity of political programs and communication with the constituency. Pro-reform political parties generally have relatively sophisticated economic programs, including on complex issues, such as foreign trade liberalization, European integration, and restructuring various economic sectors. To be accepted, programs should be based on substantial information and sound understanding of transition processes and at least superficial knowledge of basic economic concepts. By contrast, anti-reform party programs and rhetoric are much easier to understand, so it is reasonable to assume that voters' rationality would be more bounded in the case of pro-reform parties.

The above observed constraints are relevant for understanding the relationship among economic variables, political support, and election results in Serbia. Milanović (2004) conducted the only econometric research to date on the underlying factors for the December 2003 parliamentary election results. He demonstrated that the recorded results for anti-reform political parties (in this case, the Serbian Radical Party) were better in municipalities with a higher proportion of refugees (including internally displaced persons), as well as a lower proportion of ethnic minorities in the total population, and a lower level of education, as measured by number of school years completed. The only economic variable with statistically significant impact on the election results was found to be *per capita* GDP, i.e., development level of a particular municipality — the higher it is, the fewer the voters for anti-reform political parties.

<sup>1</sup> Employees in state-owned enterprises who are dissatisfied with their position can move to new jobs in the private sector. There is no need to vote for pro-reform parties while they are still employed and intend to stay in the government sector.

<sup>2</sup> On expressive voting and expressive rhetoric as expressive behavior, see Hillman (2010). We also assume that individuals vote for their preferred party and not strategically (voting for a likely winning party) nor communicatively (voting for a sure loser party), see Sobbrío and Navarra (2010).

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