Bilateral Financial Bailouts

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Abstract. Why do governments provide bilateral bailouts to countries that experience financial crises above and beyond what the IMF provides? I argue that governments face a trade off. On one hand, they want to prevent the spread of the financial crisis to their own country by providing additional liquidity. On the other hand, governments experience pressures from domestic constituents who are oftentimes opposed to bailouts. Politicians aim to balance these countervailing pressures. Whereas they are more likely to provide bailout when their economy is exposed to negative spillover effects, elections may have a detrimental effect on bailouts, particularly if the home countrys economy is not doing well. I test my hypotheses using a new data set on bilateral bailouts by OECD countries between 1990 and 2010. My statistical analysis finds robust support for the importance of domestic economic and political factors in international cooperation during financial crises.

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1 Introduction

Over the last two decades, financial crises have become more frequent, virulent, and global.[1] The 1990s and 2000s have witnessed an array of financial crises in emerging and developed market economies such as Mexico (1994), East Asia (1997-1998), Russia (1998), Brazil (1999), Turkey (2001), and Argentina (2001), culminating in the global financial crisis of 2007-2008. Financial rescues of these crisis economies have increasingly been delegated to the International Monetary Fund (IMF). The IMF pools resources from its member countries and lends it to countries that experience a financial crisis and lack access to the international capital market to solve their balance of payments difficulties. Despite these multilateral financial rescues that are organized through the IMF, crisis countries oftentimes receive additional bailout packages from individual countries. For example, during the Asian financial crisis Thailand received an IMF rescue package as well as bilateral bailouts from various countries, notably Japan and other Asian economies. Participation in such bilateral bailouts varies considerably. Whereas Thailand received large bilateral bailouts from a number of Asian economies, it did not receive a bailout from the United States, even though the US had offered a bailout to South Korea during the same period, and to Mexico in 1995.

Why do some states provide bilateral bailouts to crisis countries even though they already contribute to the IMF rescue? And why is there so much variation in the provision of bilateral bailouts? In this paper, I provide a political economy theory of bilateral bailouts.[2] I argue that governments face different, sometimes countervailing pressures when deciding whether to provide a bilateral bailout.[3] On one hand, home country politicians have incentives to provide a bailout in order to prevent negative externalities, such as a decline in economic growth due to falling exports to the crisis country. Such incentives increase the greater the exposure of the home country to the risks of negative externalities. By providing additional liquidity, a home country can help improve the immediate situation in the crisis country, and minimize the risks of costly spillovers. On the other hand, home governments have to take into account the preferences of domestic constituents who are frequently opposed to bailouts, particularly if the economy is not doing well and the bailout would redistribute resources that could potentially be used to foster economic growth at home.

[1] A financial crisis is defined as a sovereign debt crisis, which is "the failure of a government to meet a principal or interest payment on the due date . . . [including] instances in which rescheduled debt is ultimately extinguished in terms less favorable than the original obligation" (Reinhart and Rogoff, 2009, 11).

[2] In this paper, I focus on financial bailouts. Below, I discuss other forms of financial rescues as an important venue for future research.

[3] To distinguish potential donor governments from the crisis government, I call them 'home government.'

To test my theoretical hypotheses, I collect a new data set on bilateral bailouts provided by OECD countries between 1990 and 2010. Using logistic regressions, I find support for my theoretical argument. The more exposed a home country is to a crisis country either economically or financially, the more likely it provides a financial rescue. However, close elections reduce the likelihood of a bailout, particularly if a country's economy is not doing well itself. The effects of both economic exposure and domestic politics are robust to a number of different model specifications.

These findings provide some interesting insights to the question of financial bailouts. First, much of the literature has focused on explanations of international bailouts that highlight economic interdependencies and their effects on policy making.[4] My paper subsumes these arguments and highlights the importance of voter preferences and domestic elections for such an explanation. In particular, I show that the redistributional consequences of bilateral bailouts can lead to situations in which governments fail to rescue countries in crises even though they have strong economic incentives (and pressure) to do so. Second, this paper provides a first step into a quantitative analysis of political economy explanations of bilateral bailouts across a number of home and crisis countries, supporting some of the qualitative evidence for economic explanations, and my domestic electoral politics explanation.

2 Motivation

Since its inception, the IMF has enabled governments to pool resources to provide financial rescues of countries that experience financial crises. Despite the fact that most industrialized countries are shareholders of the IMF, many IMF bailouts have been supplemented with additional bilateral bailouts. Existing explanations for bilateral bailouts generally focus on the effects of economic interests on policy making. Initial research on this topic argued that the primary rationale for bilateral bailouts is to preserve the openness of the world economy.[5] Broz (2005), for example, analyzes US congressional voting on the financial rescue of Mexico and several Asian economies in the 1990s, and shows that congress members were more likely to vote in favor of an international financial rescue when they represented districts with high skilled workers (who benefit from globalization according to the Stolper-Samuelson theorem).

Newer approaches also try to account for the variation in the provision of bilateral bailouts. In his qualitative analysis of the Asian Financial Crisis, Lipscy (2003) convincingly argues that cross-temporal variation in the incentives to provide bailouts mainly depended on the importance of the crisis country's economy for the

[4] Frankel and Roubini (2001); Broz (2005, 2012); Lipscy (2003); Copelovitch (2010*a*,*b*).

[5] Kindleberger (1986); Frankel and Roubini (2001).

home country. Consequently, when the financial crisis likely has negative externalities for the home country then incentives to provide bilateral bailouts should increase.[6]

Whereas there is an increasing body of knowledge that suggests that economic pressures should be important in the home government's decision-making calculus, much less research effort has been devoted to the redistributional effects of bilateral bailouts. Home governments who provide bilateral bailouts have to redistribute domestic resources (or borrow) toward the crisis economy. For example, in the course of the Greek debt crisis, members of the Eurozone have transferred €127 billion Euro to Greece – mounting to about 1.3% of the Eurozone's GDP in 2011.[7] Eventually, most of these loans will be repaid. However, in the short term the home government has to transfer these resources to the crisis country. If the crisis country defaults, or is granted a debt relief (as is currently discussed for Greece), then the home government also loses these resources in the long term. The potential long term costs increase if one takes into account overall debt held by sovereign governments as well as bank and private lending that the crisis country may not be able to repay over time or, in the worst case, ever. For example, as of 2011 Greece owed $38 billion just to French banks and $1.91 billion to the French government (BIS, July 2012). Overall, $407 billion of Greek debt are held by domestic and international investors, as well as sovereign countries.

At the same time, the current Eurozone crisis indicates that bailouts are highly salient and widely discussed topics in home countries. In particular, the redistributional effects (or concerns about redistributional effects) have led to much opposition by domestic publics in the EU.[8] Bechtel, Hainmueller, and Margalit (2012*a*) find that only 3% of respondents in Germany strongly favor the European bailouts (24% somewhat support bailouts). 61%, on the other hand, are either somewhat against or strongly against the bailout. Burden-sharing thereby seems to be the most salient issue in the public and political debates.[9] If domestic public opinion toward bilateral bailouts is negative, and voters take this into account when they decide whom to vote for in the next election, this may have an impact on a home government's decision of whether to provide a bailout.

In the next section, I develop a political economy theory of bilateral bailouts which takes into account electoral dynamics. I argue that governments balance various domestic interests when deciding whether or not to provide a bilateral bailout. Whereas economic exposure increases incentives to bail out the crisis country, the bailout implies a redistribution of budgetary resources that could otherwise be spent to stimulate the domestic economy. If the home economy is not doing well, then governments face pressures to decline a bailout, particularly before elections.

[6] See also Katada (1998); Bordo and Schwartz (1999); Broz (2012).

[7] The IMF provided billion €22 billion. Another €30-38 billion might be necessary as of 2014.

[8] Katada (1998); Bechtel, Hainmueller, and Margalit (2012*a*,*b*).

[9] Bechtel, Hainmueller, and Margalit (2012*b*).

3 Theory

The theory is based on standard assumptions in the political economy literature. I assume that incumbents are opportunistic actors who want to maximize their time in power. They are influenced by consumers and producers in various sectors of the economy. Domestic constituents can influence the government through two channels. First, they can vote for or against the government during elections. When deciding whether to reelect the incumbent they will try to forecast the incumbent's future policies by observing her past behavior. In their assessment they discount the past, such that events closer to the election will be more important in the voters' decision-making calculus. Second, they can form interest groups and lobby the government directly to pursue policies in their favor.

The theory focuses on the decision of a *home country* to bailout a country that currently experiences a financial crisis and is in need of a financial rescue (*crisis country*). I define a *bilateral bailout* as the provision of liquidity in form of a loan to help solve a financial crisis. I assume that the crisis country already experiences the financial crisis, and that it has received an IMF bailout, and accepted IMF conditionality. This allows me to focus on the decision-making calculus of the home government to provide additional liquidity for the crisis country. Indeed, most countries that had a financial crisis in the last three decades – as defined by the extant literature – received IMF loans.

To discuss government interests toward the bilateral financial rescue of a crisis country, I have to analyze the effects of a financial crisis in a crisis country on individuals in the home country. In financially and economically open economies, financial crises usually have negative effects for individuals in other countries even if these countries do not face a financial crisis themselves. First, financial crises carry the risk of sovereign default of the crisis country. A sovereign default occurs when the crisis government loses the ability to repay its debt to its creditors. A sovereign or bank default incurs economic problems for foreign banks that hold some of the crisis country's government debt. These banks will lose their foreign assets and may slide into economic difficulties themselves. These difficulties may lead, in the worst case scenario, to a default of the foreign bank. Even if a sovereign default does not lead to a default of the foreign bank, it usually decreases the confidence of investors in the foreign bank. The exposure of the bank intensifies significantly the more of the crisis country's debt the bank holds. For example, Japan and EU countries held the majority of unsecured claims against the investment bank Lehman Brothers (the US government only held about 10%). The decision of the US government to let Lehman Brothers go bankrupt wiped out confidence in interbank markets of OECD countries, and was a major factor in the spread of the US banking crisis to Asian and European economies.[10]

[10] Welfens (2008).

Second, financial crises are usually accompanied or followed by economic recessions. This will lead to a slow down in the home country's consumer demand. Declining consumer demand will have economic effects on foreign firms that operate in the crisis country as well as on foreign companies that export to the crisis country. Multinational corporations will lose important markets and have to scale down production. This naturally also affects the economic welfare of the company in the home country with consequences for the company's profits as well as employment. National firms in the home country that export have similar concerns. If the demand for their products slows down in the crisis country, then exports will fall, with negative effects on the profitability of production and employment. These negative effects intensify if the financial crisis leads to a devaluation of the crisis country's currency, because it (a) further lowers the demand in the crisis country for now costlier imports from the home country, and (b) increases export competition on third markets for the home country due to the ability of the crisis country to sell its goods for less. For example, debates about the Eurozone bailouts have been accompanied by discussions about the effect of these countries' exit from the Eurozone on Germany's economy. Since Germany is a main exporter to its Eurozone partners (about 71% of German goods were shipped to European countries in 2011, and 59% to EU members), it is not only expected to loose significant market shares due to a decline in consumer demand in the crisis countries.[11] If the crisis countries were to leave the Euro, and consequently experienced a depreciation of their currency against the Euro, Germany would expect to loose additional market shares against the new rivals.[12]

The discussion suggests, first, that financial crises may have negative externalities for other countries, and second, that the negative externalities are particularly felt in countries that are greatly exposed to the crisis country economically and financially. That is, the more interlinked the home country's financial and trade sectors are with the crisis economy, the greater is the expectation that a worsening of the crisis may lead to a spillover of the crisis to the home economy. The effects are felt throughout the home country's economy. On one hand, employers will experience losses in profits, and potential bankruptcies. On the other hand, employees in the exposed sectors will experience a greater likelihood of getting laid off due to economic hardship of their companies. Declining consumer demand then may also have negative effects on other sectors of the economy, particularly if the home country is sliding into a financial and economic crisis itself.

Home governments whose trade and financial sectors are greatly exposed to negative externalities from the crisis country should therefore strive to prevent any crisis spillover. The most straightforward solution is to contribute to an improvement in the financial and economic situation in the crisis country, or at least to prevent a de-

[11] Data from DStatis (Statistical Office of Germany).

[12] The Guardian, May 2012, "Eurozone Crisis: If Greece Goes, Germany's Prosperity Goes with it."

terioration of the situation. By doing so, home governments can minimize the risk that a crisis country goes into bankruptcy, thereby unfolding the processes that lead to the negative spillover effects. IMF loans to the crisis country may alleviate some of the concerns, but the size of these multilateral loans may not be large enough to comfort foreign investors and to prevent a deepening of the crisis (or even an improvement of the crisis at least in the short term). The IMF provides resources that are usually enough to cover "the most obvious sources of payment difficulties. It works only if additional sources of financial pressure do not materialize."[13] Rapid and abundant liquidity provision may be the key to successfully stop the downwards spiral that carries such costly international negative externalities. It increases confidence about the ability to repay debts among investors, and thereby ensures continued access of the home government to the international capital market. In the light of great economic exposure, liquidity provision may therefore seem the best solution even though it may have detrimental effects in the long term.[14]

Home country politicians whose trade and financial sector are greatly exposed to the crisis country should thus have incentives to supplement IMF bailouts with a bilateral bailout:

Hypothesis 1 *The greater a home country's economic exposure to a crisis country, the more likely is a bilateral bailout in addition to an IMF rescue package, ceteris paribus.*

Hypothesis 2 *The greater a home country's financial exposure to a crisis country, the more likely is a bilateral bailout in addition to an IMF rescue package, ceteris paribus.*

Whereas a bailout may minimize expected economic costs for the home country, it may also increase a home government's immediate political costs owing to the financial costs of a bailout. As discussed above, bilateral bailouts imply that financial resources are diverted away from the government budget. The home government can finance a financial rescue threefold. First, it could raise taxes. Second, it could borrow. Finally, it could redistribute budgetary resources. All three strategies reduce the economic welfare of the home country's population at least in the short term, because they divert resources available for the provision of domestic public good to the crisis country.

These negative effects of a bilateral bailout to taxpayers become more severe when the home economy itself faces low or negative economic growth. Employees become increasingly concerned with the government's ability to stimulate the domestic economy and to provide domestic public goods. If the domestic economy

[13] Roubini and Setser (2004, 19).

[14] For example, bilateral bailouts may increase moral hazard problems in recipient countries. Home governments are well aware of this. As a consequence, most bilateral bailouts include the requirement to fulfill IMF conditionality.

is not doing well, companies scale down by reducing wages, cutting benefits, or releasing their employees. Individuals that face significant pay or benefit cuts are now more reliant on the government to provide some compensation through, for example, tax cuts or increase in publicly provided social benefits and services. Individuals that already were laid off now rely on the government's ability to provide unemployment benefits and to stimulate the economy in order to increase employment in the medium run. In other words, in a home economy that low or negative economic growth, individuals should be more likely to oppose a bilateral bailout. This is particularly true if one assumes that individuals cannot fully comprehend the potential beneficial economic effects of preventing a crisis spillover through a bilateral bailout.[15] Interestingly, individuals who will be most concerned about the distributional effects of bilateral bailouts during times of economic downturn are exactly those which are most exposed to the crisis country.

Home country governments will thus face increasing pressure from domestic constituents who oppose a bilateral bailout. The ability of the government to signal economic competence to its voters before elections depends on its ability to increase the voters' domestic welfare, by for example increasing economic growth, before elections. Providing a bilateral bailout may achieve this goal. However, the effect is not felt immediately and whether the bailout has positive externalities for the home country depends on the likelihood that the crisis country's government also pursues (the appropriate) economic reforms. Pursuing expansionary fiscal policies, on the other hand, underlies full control of the home government and provides economic benefits for voters immediately.

The home country government therefore faces a trade off between providing a bilateral bailout to mitigate the negative economic effects on its economy in the long term, and providing more resources to stimulate the domestic economy in order to signal economic competence to its voters. The incentives to provide a bailout should be greater if the government does not face an upcoming election. The further away elections, the less likely voters will use their votes to punish the government for its pro-bailout policies at the ballot. However, if the government faces elections during the crisis, it will have to take into account the pressure exerted by the large, yet unorganized, group of constituents. In these situations, the government faces a time inconsistency problem, whereby it has an incentive to refuse the bailout in the short term even the refusal to provide a bailout may increase the long-term economic costs of a country.

Hypothesis 3 *Upcoming elections in the home country decrease the likelihood of a bilateral bailout that supplements an IMF rescue package, particularly if the home country's economy is not doing well, ceteris paribus.*

[15] Bechtel, Hainmueller, and Margalit (2012*a*); Rickard (2012). I test this directly below. If there is no electoral effect then this is most likely due to individuals being able to analyze the economic effects of bilateral bailouts.

4 Research Design

To test my theoretical hypotheses, I analyze a home government's decisions to provide a bilateral bailout to a given crisis country between 1990 and 2010. I focus my analysis on financial crises since the 1990s since most loans made in the period after the collapse of the Bretton Woods system in the 1970s and 1980s attempted to prevent devaluation of a currency or the abandonment of a pegged exchange rate.[16] By focusing on the period from 1990, I can compare loans that were granted after the peg had failed. By the end of the 1980s, the IMF also started to provide its packages first (it used to provide its packages after the bilateral packages were in place before that).[17]

By home country, I refer to states that consider offering bilateral loans to a country experiencing a financial crisis. Usually these states are large countries with resources sufficient to mitigate economic hardship via relatively large rescue packages (almost all bilateral rescue packages are greater than one billion dollars). For this reason, I include the 23 members of the Organization for Economic Cooperation and Development (OECD) which have been members prior to 1990 into my sample of home countries. Whereas this does not include the potential population of countries providing bilateral bailouts – for example, Russia, Poland, and the Faroe Islands offered bilateral bailouts to Iceland in 2010 – it includes most countries that have offered bilateral bailouts in the sample period, and it prevents me from selecting sample observations on the dependent variable.

By crisis country, I refer to states that experience a financial crisis according to the definitions used in Reinhart and Rogoff (2009). For the purpose of this analysis, I further restrict the universe of crisis countries as all countries that received an IMF loan at least five times their IMF quota in a given year. The advantage of restricting the sample of financial rescues to those supplementing existing IMF rescues is that the cases are more comparable. A home country's calculus is more complex in the absence of an IMF rescue package because the government has to decide whether to provide additional conditionality. In fact, since 1990s most bilateral loans have been in conjunction with IMF loans.[18] For example, during the Icelandic financial crisis, the IMF had informally approved a financial rescue package. However, the Icelandic governments had problems securing bilateral loans, because the IMF loan had not been approved by the Executive Board yet.

In addition, I limit my sample of crisis countries to countries that receive a loan that is at least five times their IMF quota. Generally, the maximum that countries can borrow from the IMF is a multiple of the country's IMF quota. The exact

[16] Bordo and Schwartz (1999).

[17] Meltzer (1991).

[18] This excludes the Malaysian financial crisis in 1997-98 (the Malaysian government refused an IMF rescue package), as well as the Ecuadorian financial crisis in 1998-99 (the IMF and Ecuador could not agree on a package deal until 2000).

amount varies by agreement, and the IMF can exceed these maximums in exceptional circumstances. Limiting the number of countries to the set of crises that received large IMF bailouts in terms of their quotas thus ensures that countries receiving routine loans for temporary liquidity relief are excluded.[19] For example, between 1997 and 2003 the average size of a non-concessional IMF loan is about 1.21 times a country's IMF quota, but sizes varied between 0.15 and 19.38 the times of the country's IMF quota.[20] Including the most current crises even increases the maximum to 32 for the IMF bailout for Greece in 2010.

Whereas some of the crisis countries' quotas do not reflect their economic size (Korea is one example), using this definition tracks very closely with the sample of crises countries presented by Reinhart and Rogoff (2009) and Roubini and Setser (2004) and excludes only a few countries which experienced financial crises according to their definition and received an IMF bailout. For example, Latvia experienced a financial crisis between 2008-10, and received a bailout from the IMF in 2008, but the size of bailout was less than five times of Latvia's IMF quota in that year.[21] The exclusion of countries that did not receive an "oversized" IMF loan may induce an upward bias in the empirical results. Since oversized loans point to more serious financial crises, with potential systemic impact, potential donor countries should have greater incentives to act. This then provides a hard test for Hypothesis 3. Greater pressure to provide bilateral bailouts could reduce the potential negative impact of close elections. Consequently, if I find a negative effect of close elections on bilateral bailouts, I would be more confident that such an effect exists in a larger sample.

The unit of analysis is the home country–crisis country dyad. For example, Germany as the home country and Thailand as the crisis country constitute one such dyad. Iceland, Ireland and Turkey are OECD members and each experienced a crisis. Since they cannot offer bilateral bailouts to themselves, I dropped them from the sample as home countries for the corresponding crises, thereby leading to a total number of dyads of 296.

4.1 Dependent Variable

The theory allows predictions about the likelihood that a home country provides a bilateral bailout to a crisis country. Data on bilateral financial rescues are not readily available from the IMF or other international organizations. I compiled an original dataset containing the dollar amounts that each OECD country contributed to crisis states. Data sources include newspapers such as the New York Times and Financial

[19] http://www.imf.org/external/np/exr/facts/howlend.htm [accessed January 2013]. See also Copelovitch (2010*a*, 70) and Roubini and Setser (2004).

[20] Copelovitch (2010*a*).

[21] Other financial crises that are excluded due to a bailout amount that was too low are Russia (1998), Pakistan (1998), and the Ukraine (1998).

Times, governmental reports, and the data provided by Bordo and Schwartz (1999); Roubini and Setser (2004). Every positive data entry on a bilateral bailout is supported by at least two different sources of information. Whereas the dollar amounts are not fully reliable (in a few cases different amounts were reported by different sources), the occurrence of a bilateral bailout is consistent across different sources. The dependent variable is coded 1 if a given home country provided an bilateral bailout to a given crisis country, and 0 otherwise. In Appendix C, which includes a variety of sensitivity analyses, I demonstrate that the findings are substantially the same if I use bailout amounts instead.

One difficulty in coding the dependent variable is the question how to treat the regional bailouts from the EU to Greece and Ireland in 2010. Since EU members provided the resources necessary to set up the EU bailout, it could be important to code them as bilateral bailout for each EU member. A serious drawback of such a coding rule is that EU members experienced considerable pressure to participate in the regional bailouts. Outside of the EU, many of them would most likely not have provided a bilateral bailout. In addition, Ireland received bilateral bailouts from Denmark, Sweden, and the United Kingdom even though all these countries provided resources toward the EU bailout package. Since coding EU bailouts as bilateral bailouts may considerably bias the results, I do not code the EU bailouts as bilateral bailouts for each EU member for the main model. In Appendix C, I show that the main results are robust to excluding Greece and Ireland from the sample.

Table 1 displays the 13 crisis countries in my sample, as well as information about the crisis years, the timing of the first IMF bailout, the size of the IMF loan (in billions of US dollars), the number of bilateral bailouts, as well as the overall size of bilateral bailouts (in billions of US dollars).[22] It illustrates that there is variation in the number of bilateral bailouts. For example, whereas South Korea received 11 bilateral bailouts during its financial crisis 1997-98, the Ukraine received no bilateral bailouts during its financial crisis in 2008-10.

4.2 Independent Variables

According to Hypothesis 1, a home country should be more likely to provide a bilateral bailout, the greater its trade exposure to the crisis country. I measure the degree of trade exposure as the home country's total trade with the crisis country (the sum of exports and imports) as a share of the home country's total GDP for the year when the IMF rescue package was initiated (*Trade Exposure*).[23] Data are from

[22]IMF loan amounts are from the respective IMF country reports on the IMF's web site, and report the first loan in cases where there were several subsequent loans within the same crisis.

[23]Note, since the decision to provide bailouts are generally taken in a very short period of time, I measure all independent variables for the year in which the IMF bailout was granted. Evidence for the IMF bailout decisions supports this view: "Programs approved by the end of the second quarter of a calendar year will normally have been designed on the basis of information about the macroeconomic picture for the preceding calendar year, while arrangements approved in the second

Crisis Country	*Period*	*Intervention*	*IMF Loan*	*BL Bailouts*	*BL Loans*
Mexico	94-95	3/95	21.4	2	24.3
South Korea	97-98	7/97	22.4	11	19.3
Thailand	97-98	8/97	4.3	2	5.4
Indonesia	97-98	10/97	12.1	4	9.7
Brazil	98-99	11/98	19.4	1	5.3
Turkey	99-02	12/99	23.7	0	0
Argentina	99-02	12/00	22.1	1	1
Uruguay	02	8/02	2.6	1	1.4
Brazil	02	9/02	33.61	0	4.8
Ukraine	08-10	11/08	16.5	0	0
Iceland	08-12	11/08	2.1	7	–
Greece	09-	4/10	30.0	0	0
Ireland	08-12	11/10	17.8	3	7.8

IMF and Bilateral (BL) loan amounts are displayed in billions of US$

Table 1: Crisis Countries and IMF Loans.

the OECD. Note, using the log of the amount of exports from the home country to the crisis country as a measure does not change the results.

According to Hypothesis 2, a home country should be more likely to provide a bilateral bailout, the greater its financial exposure to the crisis country. I measure *Financial Exposure* as the logged amount of crisis country's debt held by the home country in millions of constant US$. Data are from the Bank of International Settlements (BIS).

According to Hypothesis 3, home countries should be less likely to provide bilateral bailouts if the economy is not growing, and elections are close. First, I measure economic well-being of the home country as the home country's economic growth (*GDP Growth (Home)*). Data are from the World Bank. Second, to test for the effect of close elections I use the proximity (in months) of elections for those elections that occurred within one year of the date of the IMF rescue (*Election Indicator*).[24] Following Franzese (2000) I scale the continuous election indicator so that it takes values between 0 and 1. A score of 1 means that the home country held an election within one month of the beginning of the crisis, and a score of 0 means that the next

half of the calendar year will generally be based on information that extends through the first half of the same year" (Knight and Santaella, 1997, 413). Since only two of the loans analyzed in this paper occurred in the first half of the calendar year (and the bilateral bailouts usually occur in conjunction or a couple months after the IMF bailout), it is more appropriate to measure the independent variables in the year of the IMF loan.

[24]Whereas IMF bailout dates are readily available, it was not possible to ascertain a number of bilateral bailout dates. Using the IMF bailout dates as point of departure for the measurement is possible because in all cases where I found information, the bilateral loans were provided in conjuncture or shortly after the IMF bailout (usually within a couple of months).

election did not occur for at least 12 months after the crisis began. Data on elections are from the Database of Political Institutions (Beck, Keefer, and Clarke, 2010).

I control for a variety of factors that may influence the likelihood of a bilateral bailout. First, I use the home country's unemployment rate (*Unemployment*). Data are from the World Bank. Second, I control for the effect of a home and crisis country's wealth on the likelihood of a bilateral bailout. *Per Capita GDP (Home)*) is measured as the per capita GDP of the home country in thousands of constant US$. *Per Capita GDP (Crisis)* is measured as the per capita GDP of the crisis country in thousands of constant US$. Data are from the World Bank. Lastly, cultural and geographic proximity between the home and crisis states might also affect financial rescues, so I include the logged distance (in miles) between the home and crisis state (*Distance*). Data are from Gleditsch and Ward (2001). Appendix A provides descriptive statistics.

I control for further explanatory variables in the sensitivity analysis, which is discussed in Appendix C. First, one could argue that governments face a collective action problem when deciding whether to provide bilateral financial bailouts. They may be less likely to bailout a crisis country if the IMF and other countries already pledged resources that are deemed sufficient for a successful rescue. I include the logged amount of total bilateral loans in billions of US$ (*Total Bilateral Loans (log)*), as well as the logged amount of the IMF loan in billions of US$ as a percentage of the crisis country's debt ratio (*IMF Loan (log)*) Second, home governments could be less likely to provide a bilateral bailout due to bailout 'fatigue'. Repeated financial crises may signal that the crisis government is not willing or able to implement the economic and financial reforms necessary to provide long-term stability. Bailout fatigue is notoriously difficult to measure. I approximate the idea of bailout fatigue by generating a variable that counts the number of crisis in the ten years prior to the financial crisis (*Bailout Fatigue*). Data are from Reinhart and Rogoff (2009). Third, I test whether the type of the financial crisis affects the robustness of my results. Following Reinhart and Rogoff (2009), I use currency crises, sovereign debt crisis, stock market crash, or banking crisis as potential categories. Note, most financial crises fit in several of these categories. Data and definitions for each crisis type are from Reinhart and Rogoff (2009). Fourth, I control for the impact of FDI. *FDI (% Home GDP)* is measured as the amount of FDI from the home country to the crisis country as a percentage of the home country's GDP. Data are from the OECD. Fifth, I include a variable for the partisanship ideology of the home government. *Ideology* tests whether the home government consistent mainly of parties with right-of-center parties. Data are from DPI. Sixth, I control for the amount of debt a crisis country holds as percentage of its GDP (*Debt (% Crisis GDP)*). Data are from Abbas et al. (2010). Finally, I control for the political affinity between the crisis country and the home country using the voting affinity of both states in the United Nations General Assembly (*Political Affinity*). Data are from Strezhnev and Voeten (2012).

4.3 Model Specification

Since the home country's choice to initiate a bilateral bailout is a dichotomous choice, I estimate the following equation using logistic regression:

$$\begin{aligned} Pr(\text{Bilateral Bailout}_{ij} = 1|X_{ij}) = P(\beta_1(\text{Trade Dependence}_{ij}) \\ +\beta_2(\text{Financial Dependence}_{ij}) + \beta_3(\text{Election Indicator}_j) \\ +\beta_4(\text{Controls}_{ij}) + \gamma_k + \epsilon_{ij}) \end{aligned} \tag{1}$$

where *Bilateral Bailout*$_{ij}$ indicates the financial bailout of of crisis country i by home country j. *Trade Dependence*$_{ij}$, *Financial Dependence*$_{ij}$, and *Election Indicator*$_j$ are the main variables. *Controls*$_{ij}$ represents a vector of control variables that are expected to affect bilateral bailouts. Regional fixed effects for the home countries are represented by γ_j. They capture regional-level characteristics that are shared across home countries in the same region and may affect the likelihood of bilateral bailout. Finally, ϵ_{ij} is the error term. In addition, I use robust standard errors to control for heteroscedasticity.[25]

To examine the effect of close elections on the likelihood of a bilateral bailout when the home country's economy is not doing well (Hypothesis 3), I include an interaction term into the logistic regression:[26]

$$\begin{aligned} Pr(\text{Financial Rescue}_{ij} = 1|X_{ij}) = P(\beta_1(\text{Trade Dependence}_{ij}) \\ +\beta_2(\text{Financial Dependence}_{ij}) + \beta_3(\text{Election Indicator}_j) \\ +\beta_3(\text{Election Indicator}_j * \text{GDP Growth (Home)}_j) \\ +\beta_4(\text{Controls}_{ij}) + \gamma_k + \epsilon_{ij}) \end{aligned} \tag{2}$$

Finally, I standardize all continuous explanatory variables in order to ease interpretation of the coefficients.

Appendix C provides results of different model specifications. First, I test for the robustness of the main results when using the bailout amounts as a dependent variable. *Bailout (% GDP)* is measured as the amount of the bilateral bailout provided in billions of US$, in percent of the home country's GDP. Second, I provide the results of models with home country fixed effects. Third, I exclude home countries that have never provided any bilateral bailouts. Fourth, I exclude Ireland and Greece from the sample as they also received a bailout from the European Union. Finally, I analyze whether greater levels of economic and financial exposure mitigate the negative effect of elections on bilateral bailouts.

[25] Clustering standard errors by crisis or home country does not affect the results.

[26] Note, the individual term for *GDP Growth (Home)* is incorporated into $Controls_{ij}$.

5 Empirical Results

Table 2 presents the main findings of the logistic regression. Model 1 includes the main independent variables and several controls (including regional fixed effects). Model 2 adds an interaction between GDP growth and the election indicator in order to test Hypothesis 3. Since log-odds ratios are difficult to interpret, I derive average marginal effects for all coefficients, and use these for the substantive interpretation throughout the text. The average marginal effects for Table 2 are presented in Appendix B.

	Model 1	Model 2
Trade Exposure	1.560**	1.577**
	(0.434)	(0.441)
Financial Exposure	0.880*	0.835
	(0.515)	(0.531)
Election Indicator	-0.803**	-0.531*
	(0.374)	(0.315)
GDP Growth (Home)	0.135	0.228
	(0.411)	(0.447)
Election * Growth		0.728**
		(0.319)
Unemployment (Home)	0.357	0.471
	(0.392)	(0.445)
Distance (log)	0.548	0.585
	(0.566)	(0.621)
Per Capita GDP (Crisis)	1.457**	1.526**
	(0.434)	(0.453)
Per Capita GDP (Home)	1.578**	1.580**
	(0.702)	(0.751)
Constant	-17.244**	-17.600**
	(1.736)	(1.774)
Fixed Effects	Region	Region
Specification	Logit	Logit
Observations	170	170
Pseudo R2	0.453	0.468
Wald Test	213.199	234.688

Independent variables are standardized

Standard errors in parentheses

* p<0.10, ** p<0.05

Table 2: The Political Economy of Bilateral Financial Rescues

The models fit the data very well. The Wald χ^2 is statistically significant indicating that I can reject the null hypothesis that together the independent variables have no effect on the likelihood of a bilateral bailout. Turning to the substantive effects, I find that greater financial or trade exposure corresponds with an increased likelihood that a home country will offer a bilateral bailout to a crisis country. Additionally, proximate elections in the home country are associated with a lower probability of bailouts when the home country's economy is doing poorly.

Providing support Hypothesis 1, I find that trade exposure has a positive and significant impact on the likelihood of a bilateral financial rescue. A one standard deviation increase in trade exposure between the home and the crisis country leads to a 10.2% increase in the likelihood that a given home country decides to bailout a particular crisis country, *ceteris paribus*. I find similar effects (although substantively smaller and not robust) for financial exposure. Supporting Hypothesis 2, a one standard deviation increase in the logged amount of bank holdings increases the likelihood of a bilateral bailout by 5.7%. These findings suggest that governments are more attracted to bilateral bailouts when the home country's economy is greatly exposed to the crisis country's economy, particularly through trade, and when negative spillover effects are likely. These findings support my theoretical argument and are in line with qualitative findings by Lipscy (2003) and others.

The results also provide clear support for the importance of domestic electoral politics. If the home country's incumbent faces an election within one year, then the closer this election, the less likely is a bilateral bailout. The effect of the election indicator is statistically significant, and also substantively interesting. A one standard deviation increase in the closeness of elections in the home country leads to a 5.2% decrease in the likelihood of a bilateral bailout, even though the model does not take into account regional elections or a delay in the provision of bailouts.

Model 1 indicates that elections have an independent negative effect. Above, I argued that elections should only impact the government if the economy in the home country is not doing well. To test Hypothesis 3, I analyze the effect of the election indicator on the likelihood of a bilateral bailout for different values of *GDP Growth (Home)*. Model 2 presents the main results when the interaction effect is included. Since interaction effects are difficult to interpret from regression tables, I graphed the non-linear average marginal effects of the election indicator for various sample values of *GDP Growth (Home)* in Figure 1. The x-axis shows the values for the standardized variable *GDP Growth (Home)*, and the y-axis shows the non-linear average marginal effects of the election indicator (indicated by the solid line). I also graphed the 90%-confidence intervals as indicated by the two dashed lines.

Figure 1 provides support for the conditional effect of elections as described in Hypothesis 3. Whereas close elections have a detrimental effect on bilateral bailouts when economic growth in the home country is very low, this negative effect does not persist for higher levels of growth. Specifically, for low GDP growth in the home country, the average marginal effect of the election indicator is negative and

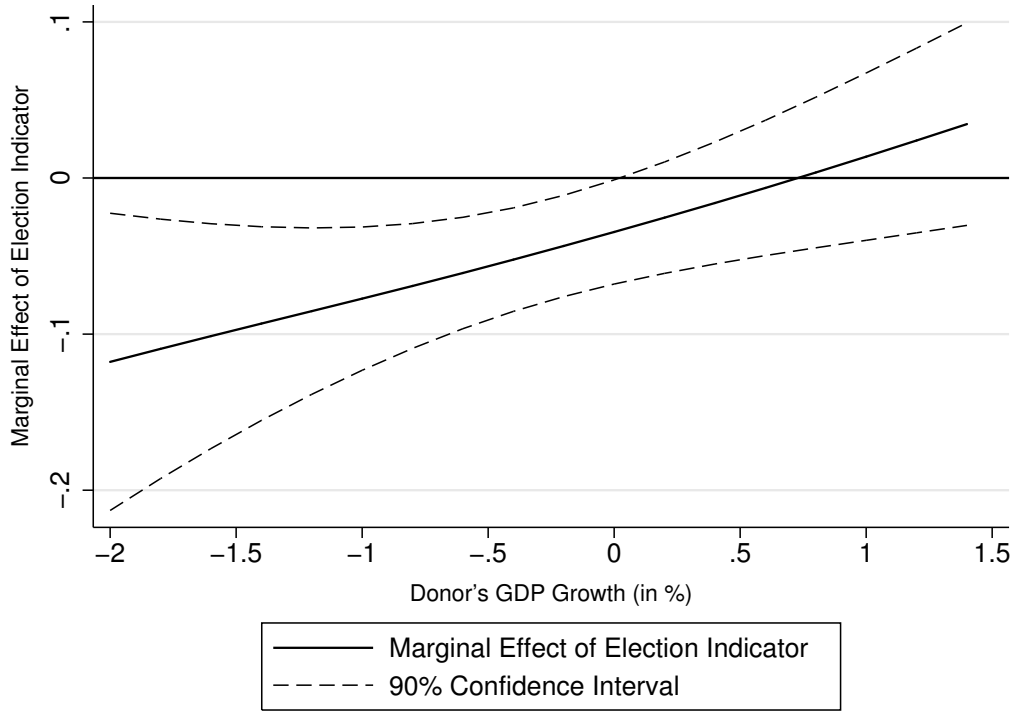

Figure 1: Effect of Elections on Bilateral Bailouts for Different Levels of the Home Country's GDP Growth

statistically significant. The size of the effect varies between a minimum -3.7% (for a sample value of standardized GDP growth of –0.2) and a maximum of -12.7% (for a sample value of standardized GDP growth of –2).

The effects of the control variables provide additional insights into the causes of bilateral bailouts. First, growth does not have a significant positive effect on bilateral bailouts, but just acts as conditioning variable. Similarly, unemployment rates in the home country as well as the distance of the crisis country from the home country are not significantly related to the likelihood of bilateral bailouts. A home country's economic wealth contributes positively to the likelihood that a bilateral bailout is offered. A one standard deviation increase in the home country's GDP per capita increases the likelihood of a bilateral bailout by 10.3%. In addition, bilateral bailouts are more likely for wealthier crisis countries. A one standard deviation increase in the crisis country's GDP per capita increases the likelihood of receiving a bilateral bailout by 9.5%.

Empirical results are oftentimes fragile to different model specifications. To analyze the robustness of my main results I estimated a number of models with additional independent variables and alternative model specifications (see description in the research design). The findings as well as a discussion of the effects can be found in Appendix C. In sum, neither the inclusion of a number of additional control variables nor changes in the sample or model specification have substantive effects on the main independent variables. The only exception is *Financial Exposure*, which turns insignificant (but still with a positive coefficient) in a number of robustness specifications, thereby indicating that trade exposure is a more important factor in a government's decision making calculus. Most importantly, the electoral effect is persistent over these model specifications and negatively affects the likelihood of bilateral bailouts even when trade exposure is at its highest levels. Appendix C also provides an interpretation of some of the substantive effects that provide further insights into the logic of bilateral bailouts.

In sum, the analysis provides support for argument that governments balance various, often contradicting domestic interests when deciding whether to provide a bilateral rescue packages to a country in financial trouble. Home governments indeed face a time inconsistency problem. Whereas they have incentives to provide bilateral bailouts to mitigate the negative externalities of financial crises in other countries, particularly when their economy is greatly exposed to spillover effects, and therefore decrease the long term economic costs, electoral politics provide short term incentives to forgo bilateral bailouts.

6 Conclusion

In this paper, I analyze the domestic electoral politics of bilateral bailouts. I argue that governments have to balance different domestic pressures. On one hand, the

greater the economic or financial exposure to the crisis country, the greater is the pressure to provide a bilateral bailout. If the home economy is not doing well, then such pressures are countered by greater demands for a redistribution of such resources towards the domestic economy. The closer elections in the home country, the more important are these demands to the incumbent government, and the less likely is a bilateral bailout. The findings of logistic regression models robustly support the theoretical argument.

Whereas my paper provides a first step towards a theory of the domestic politics of bilateral bailouts, there are many questions that I could not address due to space constraints, and that would provide interesting venues for future research. For example, I used a measure of national legislative elections as a conservative strategy to test the effect of domestic politics on bilateral bailouts. I would expect that the effect of domestic politics to be much larger if one would also control for (important) regional elections, or if one would also analyze possible delay strategies. As another example, the analysis did not include some factors that the public opinion research highlights to be important. Future research could analyze factors such as a country's overall attitude toward globalization, in order to provide a more fine grained analysis of the relationship between public opinion and the provision of bilateral bailouts. Finally, whereas my paper focuses on the likelihood that a bailout is provided, governments have pursued other strategies to financially rescue crisis countries. An important question is therefore under which conditions governments choose particular strategies. My analysis provides some initial insight for such a theory. Whereas bilateral bailouts are highly public and salient in the home countries' population – and therefore oftentimes influenced by electoral politics – other policies, such as currency swaps or privately financed haircuts, are either less public or less salient, and therefore a potential solution when bailouts would be costly politically.

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Appendix A: Descriptive Statistics

Variable	*Mean*	*Std. Dev.*	*Min.*	*Max.*	*N*
Bilateral Bailout (Dummy)	0.1081	0.3110	0	1	296
Trade Exposure	0.0023	0.0027	0.0000	0.0205	266
Financial Exposure	7,158	15,830	0	141,612	199
Election Indicator	0.1675	0.3027	0.0000	1.0000	296
GDP Growth (Home)	2.837	2.387	-3.548	11.488	296
Unemployment (Home)	6.9	3.2	2.2	20.1	278
Distance (Miles)	4,849	2,715	309	11,639	296
Per Capita GDP (Crisis)	11.2083	12.9640	1.2705	42.6937	296
Per Capita GDP (Home)	30.4212	13.2327	3.4276	95.6361	296

Appendix B: Average Marginal Effects Estimates for Main Models Reported in Table 2

	Model 1	Model 2
Trade Exposure	0.102**	0.101**
	(0.026)	(0.028)
Financial Exposure	0.057*	0.053*
	(0.031)	(0.033)
Election Indicator	-0.052**	-0.050**
	(0.022)	(0.019)
GDP Growth (Home)	0.009	0.009
	(0.027)	(0.028)
Unemployment (Home)	0.023	0.030
	(0.027)	(0.030)
Distance (log)	0.036	0.037
	(0.037)	(0.040)
Per Capita GDP (Crisis)	0.095**	0.097**
	(0.027)	(0.029)
Per Capita GDP (Home)	0.103**	0.101**
	(0.047)	(0.050)

Interaction term omitted in Model 2

Independent variables are standardized

Standard errors in parentheses

* p<0.10, ** p<0.05

Appendix C: Sensitivity Analysis

Empirical results are oftentimes fragile to different model specifications. To analyze the robustness of my main results I estimate a number of models with additional independent variables and alternative model specifications (see description in the research design section). The tables present estimation results of Equation (1) which excludes the interaction effect. I chose this model, because it provides the most conservative estimates. Results for the model estimations with interaction effects generally provide stronger election effects. I will discuss them in this section when appropriate.

Tables 3 and 4 present estimation results of the main model with additional independent variables that could have an effect on the relationship between the main independent variables and the dependent variable. As discussed above, I include a measure for the logged total amount of bilateral loans provided by OECD countries (Model 1), the amount of the IMF loan provided to the crisis country as percentage of the crisis country's debt (Model 2), dummies for the different crisis types – currency crises serve as base category – (Model 3), and the number of previous crises experienced by the crisis country (Model 4). In addition, I include a measure for FDI flows (Model 5), for right-of-center home governments (Model 6), for crisis country's debt (Model 7), and for political affinity (Model 8).

First, the inclusion of none of these measures affects the relationship between the main independent variables and the dependent variable. The only exception is *Financial Exposure*. The effect is not robust (in terms of significance) when controlling for bilateral loans, the type of crises, government ideology, and political affinity. Whereas the coefficient is consistently positive, the sensitivity analysis indicates that financial exposure may not be a consistent factor in a home country's decision-making calculus (in addition, using bank holdings as percent of home country's GDP has no significant effect on bailouts).

Some findings are of interest themselves. First, the analysis indicates that bilateral bailouts are significantly more likely the greater the loan provided by the IMF (Model 2). This indicates that there is no substitution effect. Rather, an IMF loan might signal that it is less risky to provide bilateral bailouts. This is also in line with the finding that bailouts are less likely the greater the crisis country's debt as percent of GDP (Model 7; note, the election effect becomes significant when interacted with economic growth). Second, bailouts are significantly more likely when the crisis country experiences a banking crisis instead of a currency crisis (Model 3). Third, Model 4 provides some initial support for bailout fatigue. Finally, FDI has a negative effect on the likelihood of a bailout. However, the effect is most likely due to collinearity issues. It turns insignificant if the two dependency variables are excluded from the model, and is also not significant when measured as total FDI flows.

Table 5 presents the results of different model specifications. I provide results

	Model 1 (BL Loans)	Model 2 (IMF Loan)	Model 3 (Crisis)	Model 4 (Fatigue)
Trade Exposure	1.723*	1.399**	1.619**	1.739**
	(0.903)	(0.624)	(0.489)	(0.457)
Financial Exposure	1.215	1.214*	1.168	1.240**
	(0.965)	(0.658)	(0.711)	(0.570)
Election Indicator	-1.305**	-1.367**	-0.859**	-0.857**
	(0.654)	(0.571)	(0.427)	(0.406)
GDP Growth (Home)	0.155	-0.733	-0.112	-0.062
	(0.457)	(0.630)	(0.439)	(0.466)
Unemployment (Home)	-0.313	-0.006	0.019	0.352
	(0.587)	(0.526)	(0.469)	(0.410)
Distance (log)	0.021	0.371	0.607	0.871
	(0.641)	(0.531)	(0.555)	(0.581)
Per Capita GDP (Crisis)	1.634**	1.953**	1.217**	1.367**
	(0.699)	(0.604)	(0.361)	(0.380)
Per Capita GDP (Home)	0.602	1.860*	1.010	1.494**
	(0.830)	(0.962)	(0.736)	(0.718)
Bilateral Loans (log)	0.835			
	(0.734)			
IMF Loan (% Debt)		1.611**		
		(0.426)		
Stockmarket Crash			0.011	
			(0.796)	
Sovereign Debt Crisis			-0.981	
			(0.785)	
Banking Crisis			2.067**	
			(0.862)	
Fatigue (Home)				-0.834**
				(0.339)
Constant	-15.899**	-18.783**	-18.603**	-17.894**
	(2.248)	(1.819)	(1.741)	(1.657)
Fixed Effects	Region	Region	Region	Region
Specification	Logit	Logit	Logit	Logit
Observations	124	170	170	170

Independent variables are standardized

Standard errors in parentheses

* p<0.10, ** p<0.05

Table 3: Robustness: Additional Independent Variables

	Model 5 (FDI)	Model 6 (Ideology)	Model 7 (Debt)	Model 8 (Affinity)
Trade Exposure	1.739**	1.361**	1.534**	1.755**
	(0.457)	(0.418)	(0.501)	(0.533)
Financial Exposure	1.240**	0.742	1.302**	1.006
	(0.570)	(0.461)	(0.659)	(0.748)
Election Indicator	-0.857**	-0.876**	-0.777	-1.055*
	(0.406)	(0.379)	(0.538)	(0.636)
GDP Growth (Home)	-0.062	0.405	-0.361	0.182
	(0.466)	(0.425)	(0.475)	(0.481)
Unemployment (Home)	0.352	0.269	0.320	0.704*
	(0.410)	(0.417)	(0.489)	(0.395)
Distance (log)	0.871	0.547	0.438	-0.177
	(0.581)	(0.572)	(0.353)	(0.638)
Per Capita GDP (Crisis)	1.367**	1.362**	2.080**	1.507**
	(0.380)	(0.387)	(0.765)	(0.489)
Per Capita GDP (Home)	1.494**	1.895**	1.386*	1.481
	(0.718)	(0.849)	(0.817)	(0.917)
FDI (% Home GDP)	-0.012**			
	(0.005)			
Ideology		0.765		
		(0.817)		
Debt (% Crisis GDP)			-2.143*	
			(1.122)	
Political Affinity				-0.221
				(0.539)
Constant	-17.048**	-17.936**	-17.734**	-14.938**
	(1.727)	(1.666)	(1.526)	(4.673)
Fixed Effects	Region	Region	Region	Region
Specification	Logit	Logit	Logit	Logit
Observations	170	158	170	144

Independent variables are standardized

Standard errors in parentheses

* p<0.10, ** p<0.05

Table 4: Robustness: Additional Independent Variables

of estimations that use home country fixed effects instead of regional fixed effects (Model 1), an estimation that excludes all donors that have never provided a bilateral bailout (Model 2), an estimation that excludes Ireland and Greece (Model 3), and an estimation that uses the total amount of the bilateral bailout (logged) instead of a dummy variable (Model 4). None of these specification changes affect the main independent variables. When using the bailout amount (Model 4), *Financial Exposure* turns insignificant further raising doubt about the variable's robustness.

	Model 1 (Home FE)	Model 2) (Donor)	Model 3 (EU)	Model 4 (Bailout)
Trade Exposure	2.126**	1.440**	1.860**	0.014**
	(0.570)	(0.426)	(0.540)	(0.006)
Financial Exposure	1.357*	0.904*	1.514**	0.000
	(0.799)	(0.531)	(0.658)	(0.003)
Election Indicator	-0.966**	-0.781**	-0.775*	-0.004*
	(0.487)	(0.380)	(0.478)	(0.002)
GDP Growth (Home)	0.295	0.262	0.240	0.003
	(0.516)	(0.414)	(0.478)	(0.005)
Unemployment (Home)	0.776*	0.347	0.791**	-0.002
	(0.454)	(0.447)	(0.388)	(0.002)
Distance (log)	0.671	0.494	0.201	-0.007
	(0.728)	(0.566)	(0.403)	(0.006)
Per Capita GDP (Crisis)	1.850**	1.527**	1.730**	0.009**
	(0.585)	(0.474)	(0.503)	(0.005)
Per Capita GDP (Home)	2.310**	1.316*	1.802**	0.000
	(0.917)	(0.765)	(0.797)	(0.004)
Constant	-4.620**	-18.574**	-15.085**	-0.002
	(0.962)	(1.734)	(1.425)	(0.017)
Fixed Effects	Home	Region	Region	Region
Specification	Logit	Logit	Logit	OLS
Observations	170	139	162	161

Independent variables are standardized

Standard errors in parentheses

* p<0.106, ** p<0.05

Table 5: Robustness: Fixed Effects

Finally, it could be that the electoral effect diminishes if the home country is more exposed to the crisis economy. To test this, I estimate a model with a triple interaction between *Election Indicator*, *GDP Growth*, and *Trade Exposure*. I then calculate the non-linear average marginal effects of *Election Indicator* for different values of *GDP Growth*, at high levels of *Trade Exposure*. In other words, I replicate Figure 1, but holding *Trade Exposure* at its 95^{th} sample percentile.

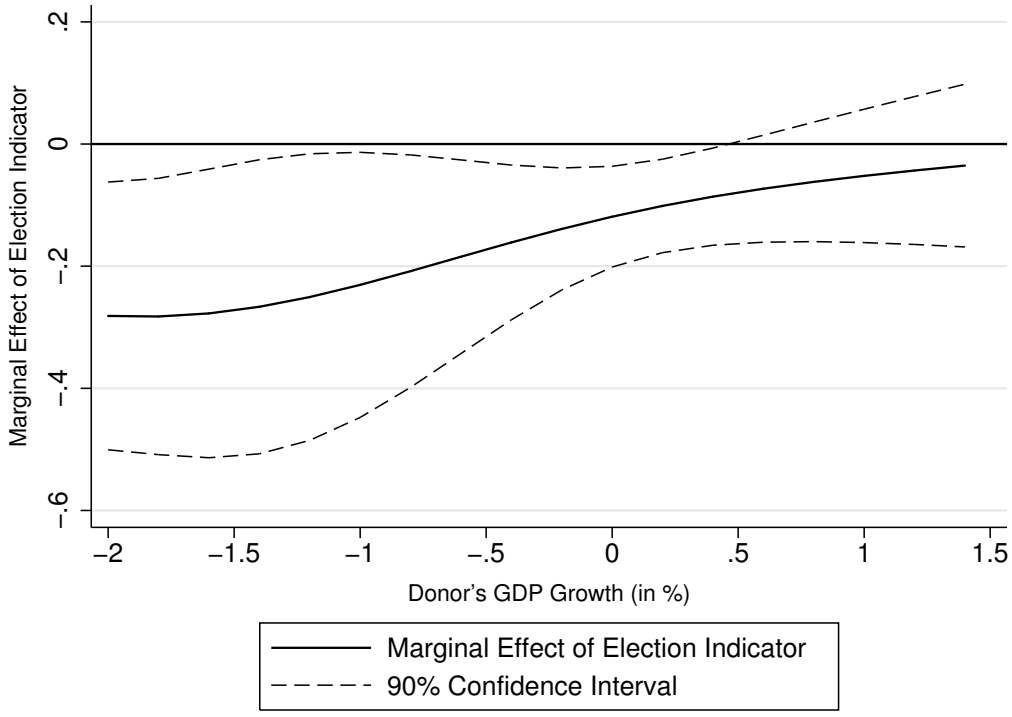

Figure 2: Effect of Elections on Bilateral Bailouts for Different Levels of GDP Growth for High Trade Dependence

Figure 2 shows that the confidence intervals around the average marginal effects of *Election Indicator* are clearly wider compared to the confidence intervals in Figure 1, particularly for low levels of GDP growth. This implies that there are more cases in which home governments decide to provide a bilateral bailout despite close elections and low economic growth, because they experienced high levels of economic exposure. Nevertheless, the electoral effect is persistently negative and significant, indicating that on average close elections have a negative effect, particularly if GDP growth is low (and even if economic exposure is great). Consequently, whereas economic exposure matters greatly to increase a home government's incentives to provide a bilateral financial bailout, it has less power to sway a home government in favor of a bailouts if elections are close and the economy is doing badly. The time inconsistency problem caused by electoral concerns does can only be marginally be reduced by greater economic exposure.