Abstract

The thesis provides a comparative estimation of the electoral cycles’ influence on the monetary policies among a group of developed and developing countries. We use a non-linear central bank’s reaction function which captures the regime switching behavior of the monetary authority depending on the proximity of elections. Moreover, we compare the reaction function with partial adjustment, which controls for policy inertia, with a non-inertial policy rule with serially correlated errors which takes into account other shocks determining the central bank to deviate from its policy rule. The estimation was performed via OLS, 2SLS and 3SLS, the preference being given to the last one due to correction of endogeneity problem and efficiency gains. Robust evidence about election induced monetary policies was found in 2 out of 10 developed economies and 4 out of 10 developing economies. In these countries, the central banks tend to be less inflation averse and/or less counter-cyclical (or even pro-cyclical) during electoral periods in comparison with normal times. Additionally, we find that the legislative framework, in these countries, incorporates significant deviations from the best practices of central bank independence. Finally, following the dynamic inconsistency problem, we document a strong inflationary bias in the economies with politically sensitive monetary policies. It confirms the imperative importance of central bank’s reputation, insulation of monetary policy from the fiscal one and the necessity of an adequate legislative design to ensure the full independence of the monetary authority.