

WHERE DOES THE MONEY FOR FINANCING OUR PRESIDENTIAL CAMPAIGN COME FROM?

They want to finance your campaign
They only ask for your soul in return, c'mon!



DIGGING DEEPER INTO BRAZIL'S 2014 CAMPAIGN FINANCE

Explaining contributions and cronyism in terms of economic freedom

Dr. Roberta Muramatsu

Motivation- Warm-up

2009



2013



- ✓ Are Brazilians in need of new (economic liberty) theoretical/empirical approaches to better explain the logic of 2014 presidential campaign finance?
- ✓ Why? Better chance to understand crony relations, systematic corruption scandals and poor performance
- ✓ Time to change, new fresh air....coming from bright young individuals



Why do we care?



A screenshot of a Bloomberg Markets article. The main headline is "Batista Brothers' Latest Deal Drags Brazil Into Fresh Crisis" by Gerson Freitas Jr, dated May 18, 2017. The article lists two key points: Wesley and Joesley Batista have agreed to a plea bargain, and JBS owners wield financial and political influence in the country. A "Most Read" sidebar on the right lists several other articles. Below the article is a video player with two thumbnails: "Brazil's Temer Says 'I Never Authorized the Payment'" and "Brazil Markets Plunge as President Caught in Scandal".

- Brazilian has to deal with a relevant economic downturn.
- Corruption scandals go on and on. Recession. Low investment, low savings, high unemployment. Let's see if we will have 0.3% growth in 2017 (source: IMF July report)

Why do we care?

- Big cartel of construction companies has bought for years privileged contracts with Petrobras (Brazilian quasi-state oil company).
- Implementation of infrastructure projects (ports, airports, nuclear plants, subway lines, railroads, football arenas, etc) in Brazil, Venezuela, Cuba
- Petrobras executives received bribes of 1%-5% of deliberately overestimated/ inflated contracts with government
- Companies regarded as national champions “JBS” (Pilgrim, Swift Armour), Odebrecht, OAS, etc” received subsidized credit (5-6% yearly), long term interest was 14.25%. Unsustainable government expenditure trajectory

Main aim of this talk

- ✓ To show that the Brazilian presidential campaign finance makes a good case for testing the empirical relevance of Austrian Public Choice Economics
- ✓ To claim that integrating perspectives does pay off and inspire our talk about the prospects of economic freedom in Brazil

Lessons from Public Choice Economics

Lincoln would now see government not of, by, and for all the people but of, by, and for some kinds of people. He would see it not as of all the people but as of the political activists. He would see government not as by the people but as managed by the politicians and their officials. And he would see government not as for the ordinary people but as for the organized in well-run, well-financed, and influential business, professional associations, and trade unions. **It is government “of the Busy (political activists), by the Bossy (government managers), for the Bully (lobbying activists)”.** (Tullock et al, 2002)

- Politicians are self-interested. Voters are rational ignorant
- Concentrated benefits and disperse costs. Government fails



Blanks to be filled by Austrian school of ideas

- Criticism of the debate over market failures (against static account)
- Time to address the issues of knowledge problem and coordination in the political arena
- Confusion between theoretical and practical knowledge (Hayek 1974)

“Modern democracies are large scale, in which voter constituents face an exacerbated knowledge problem in making collective choices. This increases the base on which to disperse and they persist due to specific forms of large-scale democratic mechanisms that exacerbate knowledge problems”

(Boettke and Lopez 2002, p. 113)

Insights from the Austrian school

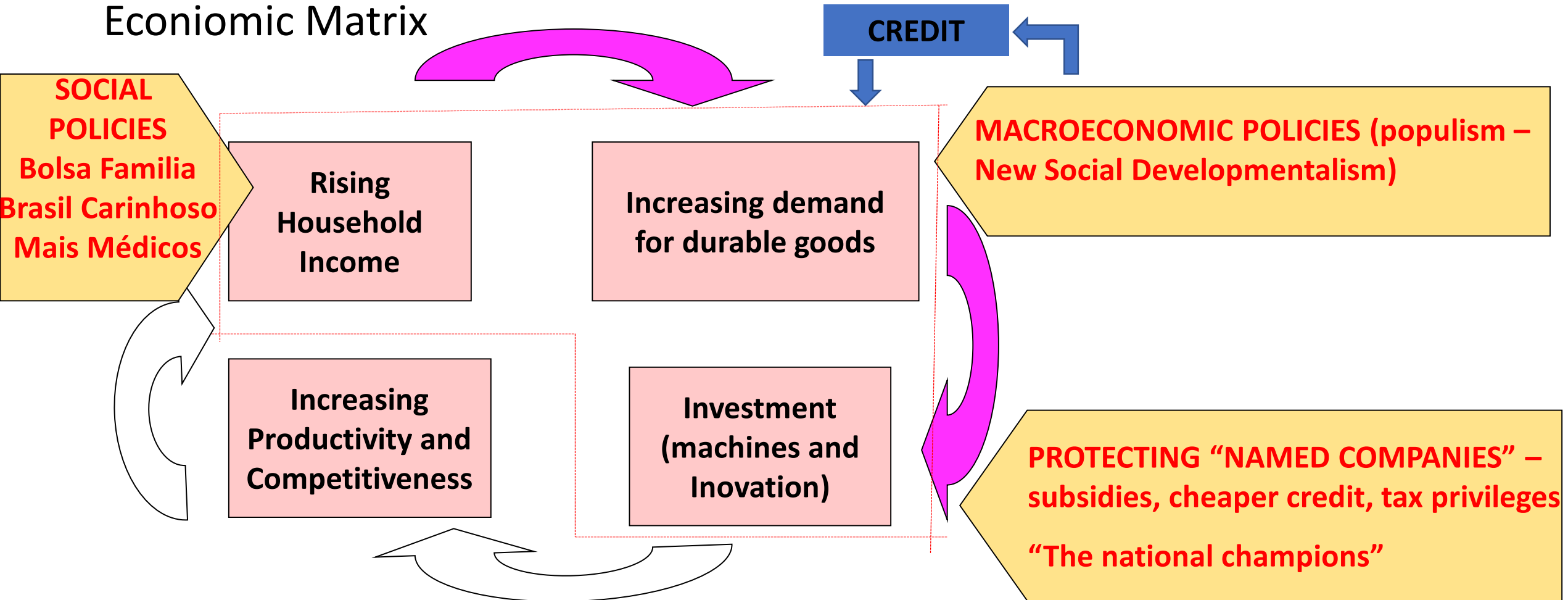
- Politicians are political entrepreneurs
- Wealth destruction mechanisms triggered by rent-seeking behavior/ cronyism
- There is also a supply side of the market for wealth transfer
- Politicians react and change the market for government protection and regulation
- Sellers of wealth transfer services Labor Unions + Big Companies as buyers

Crony relations and corruption as best policy?

- It depends on whether the institutional matrix rewards politicians to produce demands for protective legislation and wealth transfer devices.
- Rent-seeking is institutionalized! BUT privileges cannot be to all, right? Can this last forever?
- Unintended consequences of a long institutional history/ culture of paternalism and patronage

Crony relations as best (possible) policy?

- Brazilian Worker's Party (PT) promised what they could never deliver – a New Economic Matrix



- Unintended consequence: growing government expenditure and less economic freedom. Collapse in 2014 – Dilma's popularity went down the hill (7%) Impeachment in Aug 2016

Crony relations as best policy?

Crony capitalism as a by-product of big government (Holcombe 2013)

-An alliance of three powerful interests:

Big business + Big labor + Big government

- Symbiotic relationship to create pools of rents for particular industries or firms
- Firms share surplus with politically-favored groups and with the politicians themselves through campaign contributions

(Zywicki 2015, p. 8)

Crony capitalism amplifies corruption

What is the logic of paying bribes?

- To avoid costs
- To obtain government benefits
- My bold claim - the best response to a business environment without economic freedom
- Big businesses learn that governments can be a profitable buyer and contractor. Officials can be captured (given to much discretion)
- Paying bribes depend on net benefits, how risky deals are and bargaining power of briber and bribe (Rose-Ackmerman 2016)

What shall we do next?

- Let's try to submit to an empirical test our conjectures
- How? Drawing some inferences from the 2014 Presidential campaign finance behavior
- Corruption scandals accompanied the first stage of Car Wash Operation in 2009, Petrobras, JBS International, BNDES, etc give support to our perspective
- Worker's Party (Lula da Silva and Rousseff) used Petrobras as personal piggy bank to finance elections and bribery

**An assessment of Brazil's 2014 presidential
campaign finance : testing explanatory
relevance of Austrian Public Choice Economics**

Our main empirical sources

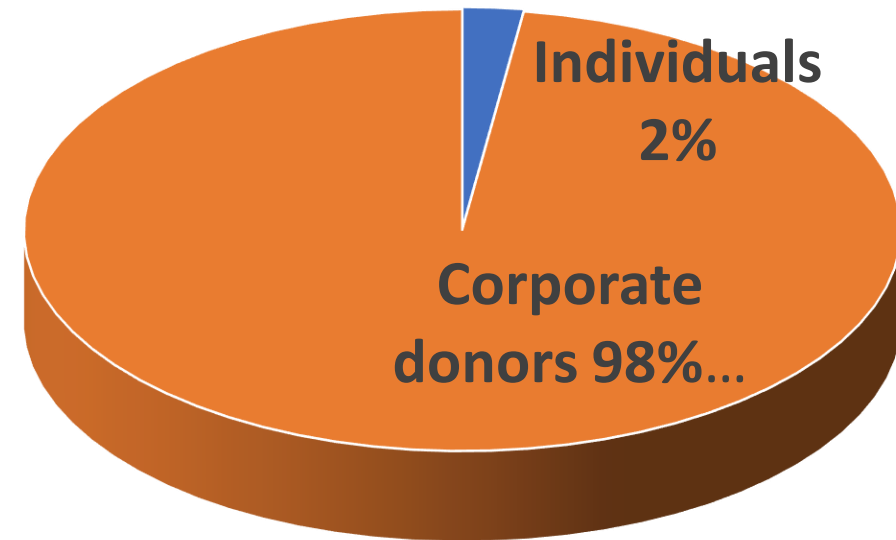
- Electoral data about campaign finance - Superior Electoral Court:
<http://inter01.tse.jus.br/spceweb.consulta.receitasdespesas2014>
- “Carwash” Operation - Federal Public Ministry:
<http://lavajato.mpf.mp.br/lavajato/index.html>
- Federal government expenditure – Federal Government’s Transparency Web Site: <http://www.portaldatransparencia.gov.br/>
- Data source on BNDES (Brazilian Development National Bank):
<http://www.bndes.gov.br/wps/portal/site/home/transparencia/consulta-operacoes-bndes/consulta-a-operacoes-bndes/>



2014 Brazilian Presidential Elections Outlook

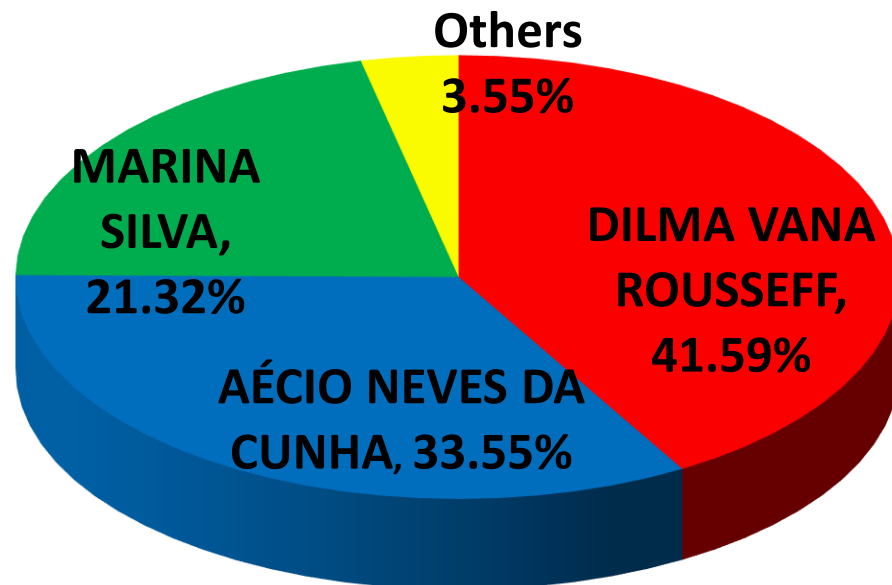
- 11 candidates
- Main candidates: Dilma Rousseff; Aécio Neves; Marina Silva
- Private contributions for Brazil's 2014 presidential campaign finance = R\$ 645 million (about US\$ 272 million)
- Contributors
 - People = 1899 individuals => the top hundred were business men and responsible for 95% of personal contributions
 - Corporations = 421

Share of the value of private contributions: People X Corporations

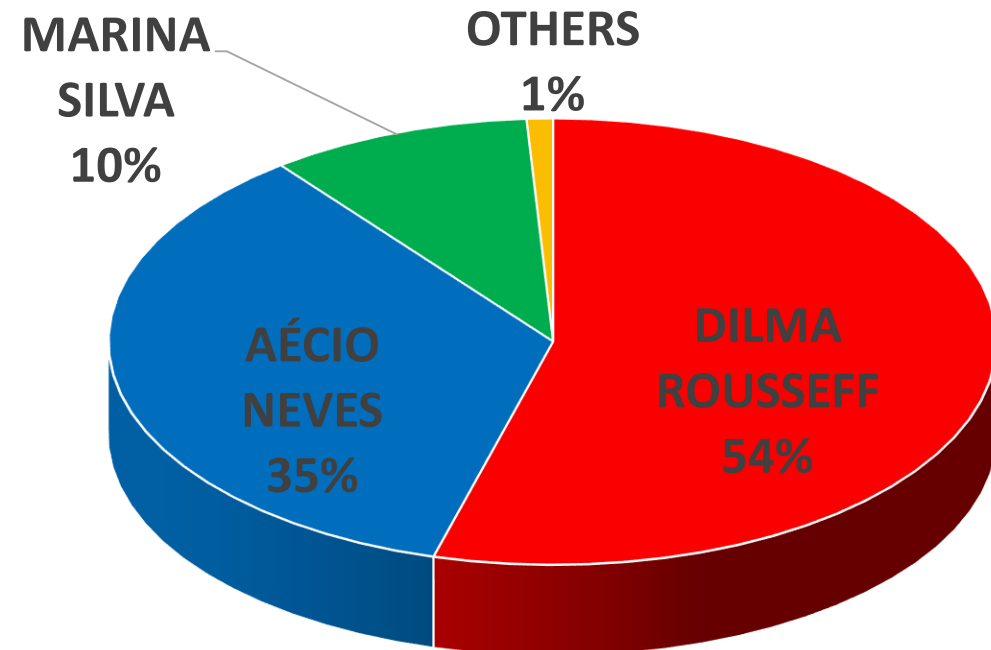


Brazil's 2014 Presidential Elections Outlook

- Share of received votes on first round

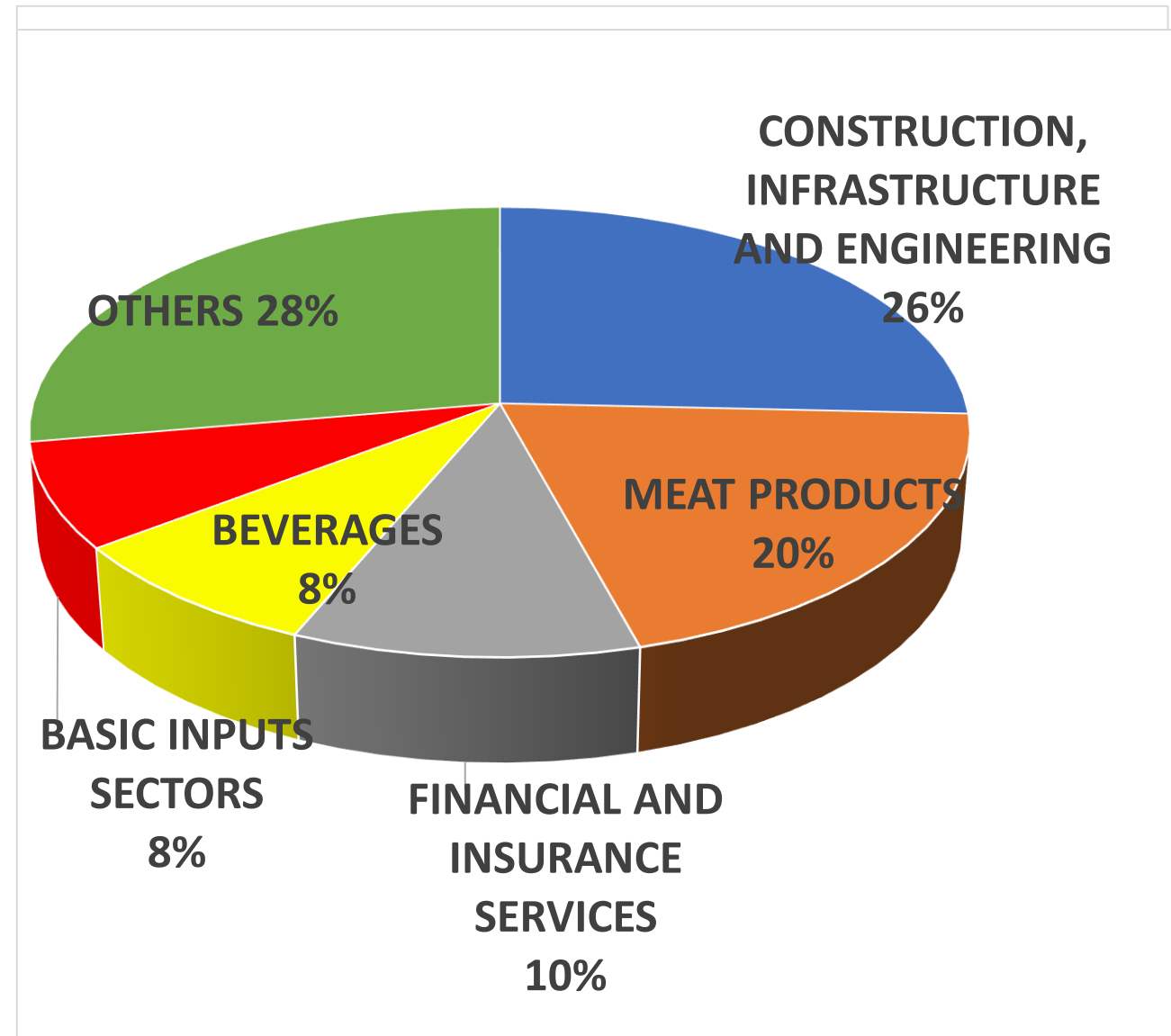


- Share of received contributions on 2nd round



Contributions by business sectors

- Basically the same sectors were the main contributors/donors to all 3 main candidates, with small variations in the individual ranking
- Top five sectors were responsible by 75% of Dilma e Aécio's contributors and 59% of Marina's contributors



Interesting results

- Top 20 corporate donors financed 65% of presidential campaign
- Top 50 donors contributed to 80% campaign
- 10 out of the Top 20 corporate donors contributed to Dilma Rousseff, Aécio Neves and Marina Silva
- Lesson to be drawn: Worth buying good relationship with government in the future

What does the evidence of crony relations underlying 2014 campaign finance tell?

- ❑ 10 out of the 20 biggest donors received R\$ 3.2 bi (US1bi) of federal government from their services
- ❑ Construction, Engineering and infrastructure received 73% of that (Government as contractor)
- ❑ 17 out of the top 20 campaign donors received R\$ 10.5 bi (approx. US3.5 bi) in subsidized credit by the National Bank of Economic and Social Development (BNDES) between 2011-2014.
- ❑ Received value is 28 times more than the total corporate contributions made by Top 20 donors. Profitable business, right?

Car Wash Operation: evidence of cronyism and government corruption



- ❑ More than a Federal Police operation to arrest “doleiros” (black money dealers) that used a carwash/gas station to make transactions with criminal groups in 2009
- ❑ Due to plea bargaining black money dealers confessed that public officials demanded their services (transfer money from bribery to shell companies)

Car Wash Operation: evidence of cronyism and government corruption

- ❑ Investigation came to discover a sophisticated bribery network in what used to be the biggest Brazilian company, Petrobras (run-owned oil company)
- ❑ Given the demand for infrastructure works, construction companies formed a cartel to be the always winners that take it all
- ❑ Many 2014 Presidential campaign top corporate donors (Andrade Gutierrez, Odebrecht, Cervejaria Petropolis, Galvão Engenharia) are involved in CarWash Operation – many executives arrested or wearing an “electronic (ankle) bracelet”

Car Wash Operation: evidence of cronyism and government corruption

- ❑ In 3 years, 199 convicted and 27 arrested. Still many in the list to come
- Ex- Minister of Finance under Lula and Rousseff presidencies – Palloci – 12 years
- Ex Congressman – Andre Vargas (Worker's Party)
- Ex president of the Congress – Eduardo Cunha
- Ex Rio de Janeiro governor – Sergio Cabral
- Ex- senator Gim Argello
- Marcelo Odebrecht – CEO Odebrecht – 19 years
- Carlos Miranda – Rio governor's partner
- Eduardo Meira – owner of Credencial Construction Company
- Joao Henriques – lobbyist and financial operator
- Jorge Zelada – previous International Director of Petrobras Oil Company

Operation Car Wash

LAVA JATO

PETROBRAS EMBEZZLEMENT SCHEME ESQUEMA DE DESVIOS DE RECURSOS DA PETROBRAS

Supply chain director

Service Director

International Director

DIRETORIA DE ABASTECIMENTO

DIRETORIA DE SERVIÇOS

DIRETORIA INTERNACIONAL

INDIGADO PELO PP

INDIGADO PELO PT

INDIGADO PELO PMDB

PAULO ROBERTO COSTA

RENATO DUQUE

NESTOR CERVERÓ

Political party nomination

Indication of Worker's Party

Job through political influence

Construction companies contracted



EMPREITEIRAS CONTRATADAS

EMPREITEIRAS CONTRATADAS

EMPREITEIRAS CONTRATADAS

Propina

Propina

Propina

Bribery

Bribery

Bribery

Bribery

OPERADOR

OPERADOR

OPERADOR

ALBERTO YOUSSEF

JOÃO VACCARI

FERNANDO BAIANO

Propina

Propina

Propina

Bribery

Bribery

Bribery

POLÍTICOS

POLÍTICOS

POLÍTICOS

PP/PMDB

PT

PMDB

Politicians and their parties

Politicians and their parties

Politicians and parties

Source: Brazilian Prosecution Service of the Union (MPF)



Example of how top donors relate to investigations by Car Wash prosecutors

- ✓ One example: Andrade Gutierrez S/A (Construction company) – 2nd top donor

Donor: CONSTRUTORA ANDRADE GUTIERREZ S/A

Ranking 2nd

Legal contributions R\$ 34.602.406,37 (a bit more than US\$10 mi)

Some contracts under the Car Wash Operation

Nuclear Energy Plant of Angra 3; Arco Metropolitano do Rio de Janeiro (highway);

Arena da Amazônia; Usina Hidrelétrica Belo Monte; Ampliação do centro de refino e

processamento da COMPERJ (petrochemical pole in Rio);

Expansão Trensurb; Ferrovia Leste-Oeste; Ferrovia Norte-Sul;

Reforma do estádio “Mané Garrincha”;

Reforma do estádio “Maracanã”; Urbanização da favela de

Otávio Marques de Azevedo (CEO) arrested and agreed to cooperate (plea bargaining).

What Car Wash is uncovering about estimated and final costs of suspicious projects that government with campaign donors contracted

Public contracts under suspicion in the operation "Lava Jato"	Initial estimated cost (R\$ million)	Final estimated cost (R\$ million)	Difference (R\$ million)
Total	97.299,00	264.864,50	167.565,50

Conclusions



✓ Austrian Public Economics adds to our understanding of campaign finance moves in 2014 Brazilian presidential election



✓ Rent-seeking, cronyism and corruption as symptoms of a disease caused by lack of economic freedom and view of government as GODFATHER OR BIG BROTHER

✓ Solution is NOT to argue for PUBLIC campaign finance. We need TRANSPARENT contracts, rule of law and ECONOMIC FREEDOM

Conclusions

- History of incentives to keep predatory political/economic institutions partly explain why Brazilian government corruption destroyed its economic fundamentals



“Feeding a small termite may be a generous act at a negligible cost. If the termites are many, and society only decides the survival of one at a time, in the end, it may feed many. And many termites may erode a house” (Lisboa and Latiff 2013)

That's it for today, folks!



Thanks for your attention!

Email: roberta.muramatsu@mackenzie.br