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CORRUPTION UNDER AUSTERITY

In this paper, we study how policies limiting the spending capacity of local governments may lead to a reduction in corruption. We exploit the extension of one such policy, the Domestic Stability Pact (DSP), to Italian municipalities with less than 5,000 inhabitants that occurred in 2013. Using a 'local Difference-in-Differences' approach, we show that the extension of the DSP led to a substantial decrease in recorded corruption rates. This effect emerges only in areas in which the DSP put a binding cap on municipal capital expenditures, in line with the hypothesis that investments and procurement are naturally prone to corruptive phenomena. We also show that i) the reduction in corruption is linked to accountability incentives; ii) and it is not just a mechanical consequence of the decrease in investments, by pointing out evidence of an improvement in the corruption-proofness of public spending. We then estimate the impact of the extension of the DSP on local welfare, finding a null effect. Overall, our findings suggest that budget constrains might induce local governments to curb expenditures in a way that dampens their exposure to corruption without depressing local welfare.

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