

# PARTISANSHIP AND CONVENTIONS: AN ANALYSIS OF THE IMPACT OF PARTY ALIGNMENTS ON EMPLOYMENT LEVELS IN BRAZILIAN COMPANIES BETWEEN 2000 AND 2020

Helena Morais\*

Aleff Lopes†

Marco Flávio da Cunha Resende‡

## ABSTRACT

The goal of this research is to examine the impact of political alignment among mayors, governors, and the President on local economic activity in Brazil, with a primary focus on labor demand by companies. This analysis is framed within the post-Keynesian school's concept of conventions. The paper first provides an overview of post-Keynesian literature discussing the development of conventions and their implications for modern economies. We then demonstrate through an empirical analysis a positive effect of political alignments on variations in the formal employment rate at the individual firm level. The findings suggest that examining the Keynesian idea of conventions provides a valuable insight into the uncertainties and complexities inherent in microeconomic decision-making processes. This is especially pertinent in the Brazilian context, where political affiliations significantly influence the formation of regional economic conventions. Overall, this study sheds light on the determinants of employment levels in Brazilian companies and highlights the crucial role of political coordination in promoting economic stability by mitigating uncertainty and fostering the emergence of optimistic conventions.

**Keywords:** Expectations; Conventions; Economic policy; Partisan Alignment; Political coordination.

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\* Faculty of Economic Sciences (FACE) and Centre for Development and Regional Planning (Cedeplar), Federal University of Minas Gerais (UFMG), Belo Horizonte - Minas Gerais, Brazil. [helenarfm@cedeplar.ufmg.br](mailto:helenarfm@cedeplar.ufmg.br)

† Faculty of Economic Sciences (FACE) and Centre for Development and Regional Planning (Cedeplar), Federal University of Minas Gerais (UFMG), Belo Horizonte - Minas Gerais, Brazil. [anfl@cedeplar.ufmg.br](mailto:anfl@cedeplar.ufmg.br)

‡ Faculty of Economic Sciences (FACE) and Centre for Development and Regional Planning (Cedeplar), Federal University of Minas Gerais (UFMG), Belo Horizonte - Minas Gerais, Brazil. [resende@cedeplar.ufmg.br](mailto:resende@cedeplar.ufmg.br)

## 1 Introduction

The economy is ontologically a political field of study (Erber, 2011). To depart from this assumption means acknowledging that the discipline cannot be viewed as purely technical or neutral. The state of the economy is intrinsically connected to the social and political dynamics within which it operates. Such an assumption adds significant complexity to the analysis of economic decision-making, as social systems, as opposed to exact systems, are subject to uncertainties. The social world is not deterministic. As Keynes (1973) asserted, economics is a "moral science" dealing with human behavior and its complex relationships<sup>1</sup>.

In addressing issues of uncertainty and coordination, modern societies employ certain norms that, at the behavioral level, are shaped by conventions (Erber, 2011). In an economic context, conventions represent collective rules of behavior adopted and enduring over time, shared and accepted by economic agents. Conventions play a crucial role in the formation and coordination of expectations, as they provide insight into agents' anticipated responses to specific economic stimuli.

The formation of conventions does not occur in isolation but results from both the direct information accumulated by individuals and interactive processes. It encompasses their knowledge, whether codified or tacit (Erber, 2011), as well as pre-existing conventions. However, despite their relevance in the economic environment, conventions are dynamic. They can undergo changes and evolutions, reflecting the volatile nature upon which expectations are formed in uncertain environments Fraga and Resende (2022).

The goal of this research is to investigate whether conventions can be strengthened depending on the political conditions in which an individual company operates. Under the hypothesis that the political context can stimulate the formation of optimistic conventions and thus expand job opportunities, the study measures the effect of party alignments among mayors, governors, and the President of the Republic on the percentage variation in employment in Brazilian companies between 2000 and 2020. The results indicate that, overall, companies located in municipalities with higher ideological alignment among the three leaders of the executive branches tend to expand employment more intensely than those in municipalities with low party alignment, corroborating our hypothesis.

The paper is divided into four sections, in addition to this introduction. Section 2 provides a brief review of post-Keynesian literature on convention formation and its implications for the functioning of modern

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<sup>1</sup> In a letter written to Harrod in 1938, Keynes argues that "I also want to emphasise strongly the point about economics being a moral science [...] it deals with motives, expectations, psychological uncertainties." (Keynes, 1973, p. 300).

economies. Section 3 presents the methodology used to estimate an econometric model (where the dependent variable is the annual percentage variation in individual company employment, and the independent variables are the levels of political convergence), along with a description of the databases used. The results are presented in Section 4, and Section 5 draws the study's conclusions.

## 2 Literature Review

In the 1930s, the world witnessed the Great Depression, an unprecedented economic crisis. During this period, extremely high unemployment rates were registered, particularly in the United States and Britain. The crucial issue in public policies became the problem of persistent and long-term unemployment. Matters related to the labor market, wage rigidity, and the persistence of unemployment rates played a central role in the economic discussion, giving rise to modern macroeconomics (Margo, 1993).

Keynes was a prominent figure in this debate and presented a new paradigm for economic science in his seminal work of 1936, *The General Theory of Employment, Interest, and Money*. Having a good knowledge of the classical theory, Keynes (1988) argued that his theory was "general" precisely because it opposed orthodox economics, which applied only to specific equilibrium cases, that were rarely observed. In contrast to that school of economic thought, Keynes observed that in the capitalist system, the free functioning of the market did not automatically generate full employment equilibrium. Instead, crises of underconsumption occurred periodically and lasted indefinitely. The General Theory can be considered a theory of employment grounded in demand and, consequently, in income (Bresser-Pereira, 1976).

The breaking point of the automatic market adjustment mechanisms is the existence of uncertainty in a strong sense, also known as fundamental or radical uncertainty. The most critical decisions of economic agents are always subject to bets about the future (bets regarding future income or the future yield of an investment, for example) (Carvalho, 2014). In contrast to the concept of risk, radical uncertainty is non-probabilistic, meaning it is not calculable with complete confidence.

According to Keynes (2013), expectations about the future are built from evidence or premises gathered from the present and the past, referred to as Direct Knowledge. The "evidence" are premises from which a conclusion about the future is drawn, termed by Keynes as Indirect Knowledge, corresponding to the expectation about the future (Resende, 2023). At the moment of decision-making, not all premises are available, and thus, the information necessary for probabilistic calculations regarding the future is not entirely present.

The information is incomplete because there are Crucial Decisions (Experiments) in the economy that change the environment in which they occur, as is the case with investment. If the environment changes, then initial conditions change, preventing the repetition of the event and probabilistic calculation. In other words, Crucial Decisions alter the statistical properties of economic processes (mean, variance, and autocorrelation of data), making them non-ergodic and preventing a sample of present and past data from providing complete information about the future (Resende, 2023). The absence of ergodicity in the economy, provided by Crucial Decisions, leads to the insufficiency of premises (evidence).

Keynes (2013) studied probability as a branch of logic, seeking decision methods that would be rational given the logical result that would follow from the premises. Given the insufficiency of information for probabilistic calculation, the decision based on logic that links premises and conclusions would be the probable decision. "(...) the probable is the hypothesis on which it is rational for us to act" (Keynes, 2013, p. 339).

For Keynes, there is an "arational" element in the agent's decision-making process, i.e., an element that cannot be analyzed or understood through reason. Since information is always incomplete, the agent has to complete existing premises with imagined premises. Because part of the premises is imagined, and the agent is aware of this, the "weight of arguments", elaborated by Keynes (2013), becomes relevant, and substantial uncertainty emerges. The agent knows they are substituting information (which does not exist at the moment of decision-making) with imagination to complete their set of premises.

Therefore, imagined premises do not change the probability of the event occurring but alter the weight of arguments, affecting the agent's confidence in the expectation formed from the conclusion derived from the premises (Resende, 2023). The greater the number of premises, including the imagined ones, the greater the weight of arguments, and the higher the confidence in the knowledge of the future (conclusion) derived logically from the premises, reducing the degree of uncertainty – hence, uncertainty is gradable. The arational element of the decision-making process is the confidence that decision-makers have in their own calculations and the relevance they attribute to the information used to make them, bringing subjectivity into the expectation formation process (Carvalho, 2014). It is the confidence in the premises and, consequently, in the expectations resulting from them that Keynes (1988) referred to as the "State of Expectations."

From the formulation of the idea of uncertainty, the main concepts in post-Keynesian theory are derived: liquidity preference, precautionary saving, the principle of effective demand, and the idea of conventional behavior (Carvalho, 2014).

## 1.1 The Centrality of the Investment

Investment is the most crucial component of Aggregate Demand (AD) due to its catalytic role in stimulating economic growth and income generation. It is also the most volatile component of AD, as it is sensitive to uncertainty and associated with long time horizons. Consequently, investment is the driving force behind economic cycles.

Through investments, companies enhance their productive capacity, leading to increased employment and wages, subsequently fueling consumption and, consequently, elevating aggregate demand (Carvalho, 1988; Botte, 2019). Considering the inherently volatile and subject-to-expectation character of the investment, it plays a fundamental role in determining effective demand (Oreiro et al., 2010). Investment not only provides immediate stimulus to consumption and production but is also responsible for long-term changes in the economy's productive capacity and growth potential in the future (Resende and Terra, 2020; Carvalho, 2014). In other words, investment plays a dual role in the dynamics of the capitalist economy, simultaneously representing short-term demand growth and long-term supply capacity expansion.

From a post-Keynesian perspective, fundamental uncertainty is considered a determining factor in investment decisions (O'Sullivan, 2009; Campos & Chiarini, 2014; Libanio et al., 2020). In an uncertain context, agents' expectations about the future become less clear and predictable, adversely affecting their willingness to take risks and invest (Ferrari Filho & Terra, 2011). Faced with uncertainty and a lack of knowledge about the future, economic agents may seek security by favouring liquidity for precautionary purposes, rather than allocating resources to capital investment. Moreover, fundamental uncertainty makes the existence of automatic market mechanisms that mitigate deviations from the economy's optimal long-term trajectory unfeasible (Dequech, 2000; O'Sullivan, 2009; Terra & Goudard, 2018).

The decision to invest is heavily dependent on entrepreneurs' expectations of future profitability and is subject to fluctuations in entrepreneurial confidence regarding the future. A confidence crisis, for example, can trigger a negative sequence of multiplier effects that directly influence AD and, by extension, economic activity as a whole. Therefore, investment is an autonomous variable whose endogenous fluctuations can alter the current state of the economy (Palley, 1997; Fazzari et al., 2008; Farmer, 2017; Chaib & Lima, 2019).

Investment entails assuming long-term financial commitments based on expectations of future returns. In an uncertain scenario, the expected rate of profit may be deemed insufficient to compensate for the risk incurred, leading to a decrease in current investment. This phenomenon may be exacerbated by the post-Keynesian view that investment is an irreversible decision involving capital goods with a long lifespan, increasing

the potential impact of a postponed or canceled investment decision on future economic performance (Oreiro et al., 2010; Ferrari Filho & Terra, 2011; Castro, 2019). Therefore, if uncertainty looms over expectations, agents may adopt a wait-and-see approach, postponing, canceling, or reducing current investment. As highlighted by Carvalho (2014); Terra and Goudard (2018); Resende and Terra (2020), one way to mitigate uncertainty and stimulate private investment is through the formation of conventions.

## **1.2 Conventions in the post-Keynesian perspective**

Conventions are considered one of the main mechanisms that economic agents use to deal with fundamental uncertainty (Resende and Terra, 2020). From a post-Keynesian perspective, conventions are shared beliefs that encompass norms, practices, and shared assumptions guiding economic agents' decision-making over a certain period. These conventions direct behavior in the face of an unpredictable future and are collective rules based on expectations formed through interactions among agents (Dequech, 2022). Such norms may be rooted in past experiences, empirical rules, or simply observations of the decisions of other economic agents, providing a reference framework for decision makers to formulate their expectations (Plihon, 1995; Carvalho, 2014; Arestis et al., 2019).

By anchoring their volatile expectations in optimistic conventions, agents can reduce the perception of uncertainty and make investment decisions with greater confidence, potentially amplifying investment levels and stimulating economic activity. Conversely, when the expectation of a discouraging future becomes a shared belief, investment decisions may be indefinitely postponed (de Melo Modenesi et al., 2013; Corsi & Sornette, 2014; Nader, 2018; Resende et al., 2021; Fraga & Resende, 2022).

Conventions do not eliminate fundamental uncertainty but allow agents to mitigate it to a certain extent by affecting the confidence with which expectations are formed. It is also crucial to note that conventions can become self-fulfilling, reinforcing the expectations they created. Therefore, from the post-Keynesian approach, agents base their decisions on their own subjective and non-quantifiable expectations, influenced by conventions, i.e., shared beliefs (Resende and Terra, 2020; Resende et al., 2021).

Several factors influence and shape conventions, including economic and social policies, institutional configurations, technological changes, and media-related news (Resende and Terra, 2020). One of the key factors shaping conventions is economic policy, which plays a significant role in their construction and coordination. The government must aim to convince private agents that its policies are suitable for stimulating profit, private investment, and economic growth, creating expectations for a safe and stable economic environment, (Erber, 2011; Carvalho, 2014; Nader, 2018).

According to Resende and Terra (2020), sustaining investment and economic growth partially relies on the capacity of optimistic conventions to anchor private agents' expectations. The role of the state is strategic, as its policies and actions shape conventions. The government's power to influence conventions arises from its exclusive ability to issue currency, stipulate and collect taxes, implement public policies, establish laws, and influence the institutional structure of society. Macroeconomic policies, such as fiscal, exchange rate, and monetary policies, are tools the government can use to influence agents' expectations.

In this context, Resende and Terra (2020, p. 472) point out that Keynesian and post- Keynesian policy prescriptions include: (i) dividing the public budget into current and capital budgets; (ii) linking the capital budget to a medium/long-term, pre-announced, and countercyclical plan of public investments; (iii) conducting public investment in direct partnership with the private sector; (iv) the government should act cooperatively and complementarily with the private sector, aiming to create conventions favorable to private investment; and (v) coordinated macroeconomic policies are crucial to influencing expectations and shaping optimistic conventions about the future.

In summary, the government plays a strategic role due to its ability to anchor expectations and form optimistic conventions among agents through persuasion. Clearly, the ability to persuade agents depends on the degree of confidence they place in government policies, observing the political cohesion of the government and its ability to implement the previously announced agenda. That is, the first step in persuading agents to sustain an optimistic convention is to ensure that signals within the government itself are coherent and clear so that agents have confidence that government guidelines will not be abruptly altered.

One way to ensure this internal coherence is through political alignment between different levels of government. The general hypothesis of this work is that when there is political alignment among the executive branches (federal, state, and municipal), optimistic conventions are likely to be potentiated. In this sense, it is assumed that heads of executive powers, by sharing a similar political-economic agenda, can collaborate and implement such an agenda more assertively, signaling to agents that macroeconomic policy is credible and capable of ensuring and sustaining profit. Therefore, by observing the effective implementation of such policies, agents can be persuaded to form optimistic conventions, which consequently stimulate economic activity and increase regional employment levels.

### **1.3 Possibilities of coordinating economic policies involving the executive branch in the Brazilian Federation**

The 1980s marked a period of increased prominence for municipalities in the Brazilian Federation, driven by the decentralization of tax revenue and the emergence of the “municipalist” movement, both responses to the economic crisis and the country’s democratization after the dictatorship. During this period, despite resistance from hegemonic forces, constitutional amendments (such as 23/1983 and 79/1984) catalyzed fiscal decentralization (Santos, 2005). As a result, municipalities increased their share of available revenue from 9% to 15% between 1980 and 1994, and states also saw a relative increase in their fiscal revenues. The Federal government lost ground, with a reduction in its share of own and available revenues. This scenario led to an inter-regional decentralization of available revenue, expanding the autonomy and responsibility of municipalities in managing locally applied resources (Affonso, 1996).

Fiscal federative discoordination, arising when the policies of the central government, states, and municipalities are not aligned, stems from multiple factors. Disputes over control of public spending among the federal executive, the legislature, and subnational governments, as well as conflicts regarding the division of competencies and fiscal revenues among different levels of government, are examples of such factors. Intra-regional heterogeneity further exacerbates the situation, fuelling fragmenting and centrifugal forces nationally, especially in the absence of horizontal or vertical coordination among governments (Affonso, 1996; Abrucio & Franzese, 2007).

In order to promote the formation of optimistic conventions, coordination between the Federal, state, and municipal levels can be facilitated through various strategies. Encouraging dialogue and negotiation among different levels of government can help resolve disputes over command power regarding public spending and fiscal revenues, as well as reduce potential fiscal wars. In this sense, it is imperative to create mechanisms for intergovernmental coordination and cooperation to mitigate the challenges arising from uncoordinated decentralization, promoting a more stable political-economic environment where private sector economic calculations become more sustainable (Affonso, 1996; Abrucio & Franzese, 2007).

The recent COVID-19 pandemic highlighted the wide range of dysfunctions that can emerge when there is no coordination and alignment between governments. Notably, the Brazilian federal executive’s lack of coordination in health policies resulted in an atmosphere of disarray, exacerbated by the absence of a clear definition of roles and competencies among federated entities. This matter had to be discussed in the Supreme Federal Court (Fernandes & Mafort-Ouverney, 2022). In summary, the instability caused by the

pandemic was exacerbated by the lack of political coordination, whether due to incapacity or inaction. The result was an increase in uncertainty (Resende et al., 2021; Resende, 2023).

Conventions play a mediating role in the economy, influencing the investment decisions of agents. The state, as the most significant social entity and holder of various exclusive activities, such as currency issuance and law creation, has the power to shape such conventions and, consequently, expectations. State intervention during the health crisis, even if uncoordinated intra-regionally, highlighted the relevance of the governmental role in economic stabilization and mitigation of adverse crisis effects (Resende et al., 2021; Resende, 2023).

Before 2019, Brazil had some successful examples of coordination between the three levels of government. In the health sector, for example, the Federal Ministry of Health establishes general guidelines. State health departments then adapt these guidelines to each state's specific context, and municipalities are responsible for the practical application of these guidelines, considering local specificities. In education, the federal Ministry of Education establishes educational guidelines and standards, which state and municipal governments then implement. States can develop curricula in compliance with these guidelines, while municipalities are responsible for school administration and curriculum implementation. In public safety, the federal government, through the Ministry of Justice, sets national guidelines and strategies for combating organized crime, drug trafficking, and border crimes. In turn, state governments, through public security departments, coordinate the civil and military police, focusing on state-level security issues. Additionally, municipalities have the prerogative to establish municipal guards under their jurisdiction, primarily to protect public assets, services, and installations. These are examples in which the context, cooperation, and alignment between the three levels of executive power do not result in exacerbated conflicts and overlaps, given the well-defined role of each entity.

However, when it comes to economic matters, coordination may face obstacles if there are divergences in the conduct of economic policies. A president with a liberal orientation, for example, might resist adopting expansionary fiscal policies, while a governor with social-democratic inclinations might advocate for more public spending. Moreover, mayors of municipalities with diverse ideological inclinations might struggle to implement economic policies aligned with federal and state levels. These differences can lead to a lack of cooperation and the adoption of misaligned policies, harming the effectiveness of state interventions and potentially leading the economy to grow below expectations.

In other words, the (mis)alignment of public policies among federal, state, and municipal spheres affects conventions and the formation of private expectations, with effects on private investment decisions, economic growth, and the generation of employment and income. Decisions about the magnitude or composition of State

expenditures, for example, can influence local AD and have repercussions on the country's overall development goals, as observed in Brazil in 2009. In that year, the Brazilian federal government created fiscal stimulus measures, while subnational governments reduced their expenses, resulting in a reduction in the net expansive effect on the economy (Fardoust & Ravishankar, 2013).

Additionally, the discursive incongruence among public agents with different ideological inclinations can also generate signaling failures to private agents. The logical consequence of these contradictions would be an increase in uncertainty about the direction of economic policy where companies operate, with adverse effects on private investment. Therefore, achieving sustainable regional economic growth requires intergovernmental coordination.

### **3 Methodology**

This study assumes that we can approximate the coordination of economic policies across different levels of the executive branch – federal, state, and municipal – by the ideological bias of the executive leaders. Additionally, it argues that the political and discursive coordination provided by political party alignment has the potential to enhance optimistic conventions among private agents regarding the policies implemented by distinct government spheres and their effects on the hiring levels of individual companies. The following strategy was adopted, aiming to test these hypotheses: i) employment data from over 8.5 million Brazilian companies operating between 2000 and 2020 were assessed, and ii) an econometric estimation was conducted to evaluate whether there were statistically significant differences in the hiring patterns of companies operating in a more politically/economically homogeneous environment vis-à-vis companies operating in a less aligned political/economic environment, from the perspective of party affiliation.

#### **1.4 Data and empirical strategy**

The data used in this study come from the Annual Social Information Report (RAIS) and the Superior Electoral Court (TSE). Using RAIS data, we were able to track year-to-year formal employment relationships in 8,545,142 companies between 2000 and 2020, segmented by municipality and economic activity sections according to the National Classification of Economic Activities (CNAE)<sup>2</sup>. With TSE data, we identified elected representatives and their respective political parties at the three levels of the federalist system in Brazil: municipal,

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<sup>2</sup> CNAE is a classification used in Brazil to identify the economic activities of companies and other economic agents operating in the country. Brazilian tax administration bodies adopt this classification for registration purposes, and serves as a basis for the collection, analysis and dissemination of statistical data related to the production and distribution of goods and services

state, and federal. Thus, there is a nested structure in which company *i* operates in an economic environment influenced by the political guidelines defined by the respective mayors, governors, and presidents.

Under that assumption, we test the hypothesis that the political and discursive coordination provided by political party alignment enhances demand for hiring levels of private agents. If such a hypothesis is found to be plausible, it could imply that political coordination is enhancing optimistic conventions, as detailed in the previous section.

In this context, optimistic conventions, taken as shared beliefs resulting in collective rules and behavior adopted by economic agents over a certain period, tend to form when there is greater political alignment among the heads of the executive branches. Political, economic, and institutional stability are factors that reduce the level of economic uncertainty.

It is important to clarify how political alignment variables are treated in specific cases that occurred during the analyzed period. When a mayor changes political parties during their term, this change is not reflected in our data; instead, we maintain the party affiliation recorded at the time of election throughout the entire term. Similarly, for governors who change political parties during their mandate, we consider only the party of the elected governor at the time of election, maintaining this classification for the duration of their term. The only exception to this approach occurs in cases of impeachment, where the party affiliation of the executive leader is updated to reflect the successor. Specifically, this applies to the impeachment of President Dilma Rousseff in 2016, after which we consider the party affiliation of her successor, Michel Temer. This methodological approach represents a limitation of the present study, as it may not fully capture the dynamic nature of political alignments during electoral terms. This limitation could be addressed in future research through more sophisticated data processing approaches that account for intra-term political parties' changes.

Accordingly, this study aims to identify whether there are significant annual variations in the percentage change of employment relationships within firms, based on the political configuration of the executive power in their respective regional contexts. Thus, it is possible to empirically verify whether political alignment is an important factor in the variation of individual firm employment. The hypothesis is that in locations with political alignment, regionally embedded optimistic conventions may have persisted for a specific period, favoring employment growth. Furthermore, it is also possible to argue that, given party alignment, policies defined at the macroeconomic level can be intensified by party political confluence at the municipal level.

The estimation method employed is Ordinary Least Squares (OLS). The model to be estimated can be represented by Equation 1:

$$\Delta\% v_{n_{i,t}} = \beta_1 no\_conf + \beta_2 conf\_goma + \beta_3 conf\_prma + \beta_4 conf\_prgo + \beta_5 conf\_total + \epsilon_i \quad (1)$$

Where the dependent variable ( $\Delta\% v_{n_{i,t}}$ ) is the percentage variation in the number of employment relationships in the company  $i$ , year  $t$ , vis-à-vis the year  $t - 1$ . The variable *no\_conf* (no confluence) has a value of 1 when the mayor, the state governor and the president belong to different political parties and 0 otherwise. The variable *conf\_goma* assumes value 1 when the mayor and governor are from the same party, but the president is not. The variable *conf\_prma* equals 1 indicates that the president and the mayor are from the same party, but the governor is from another party. The variable *conf\_prgo*, when equal to 1, indicates the confluence between the president and governor, but not the mayor. Finally, *conf\_total* equal to 1 indicates that the mayor, the governor and the president are from the same political party, which possibly confers the maximum degree of alignment in the economic policies and, consequently, greater economic stability that allows the emergence of optimistic conventions.

It is important to acknowledge that including control variables in econometric models is a common practice aimed at minimizing omitted variable bias and ensuring the precision of estimators. Given that the model given by Equation 1 uses individual data from more than 8 million companies, potential omitted variables that could act as control variables include: i) financial condition of the company; ii) business management; iii) operational and input costs; iv) access to credit and financing; v) network of business relationships and partnerships, etc (Verbeek, 2021). However, such variables are challenging to observe, considering the number of companies and the time coverage, making it more practical to use a model that omits them without necessarily posing a problem (Angrist & Krueger, 1999; Moretti, 2010; Moretti & Thulin, 2013; Fleming & Measham, 2014).

In this case, there may be issues regarding the efficiency of the model. However, suppose a variable is not related to the predictor (political alignment) but is associated with the dependent variable (employment variation). In that case, the inclusion of this variable tends not to systematically alter the coefficient of the predictor (Wooldridge, 2009). Nevertheless, it may help absorb part of the residual variance in the model, leading to a more precise estimate (lower standard error) of the predictor's coefficient, although not the parameter value. On the other hand, including a variable that is related to the predictor but not to the dependent variable is generally not recommended (Battese & Coelli, 1995; Baltagi & Liu, 2020), as it does not improve the model and can result in less precise estimates of the predictor's coefficient (the added variable "steals" variance from the predictor itself, leading to biased parameters).

Regarding the consistency of the estimated parameters, the primary concern, in terms of endogeneity, arises if the political alignment variables are correlated with other unobserved variables that also affect

employment in individual firms (Moretti, 2010; Moretti & Thulin, 2013). However, given the political and institutional nature of these variables<sup>3</sup>, it is unlikely that they are directly correlated with specific variables that influence the dependent variable. That is, political alignment in the locality where the company operates depends on previous electoral choices, rather than on specific economic conditions that affect the hiring levels of companies.

Clearly, the pattern of hiring and layoffs among companies depends on the type of activity undertaken by the company, and that is why we separate the data across the 21 sections of the CNAE classification. Table 1 presents the number of employment links and the number of companies in the years 2001, 2010, and 2020 by CNAE section.

**Table 1** - Number of jobs and companies in 2001, 2010, and 2020 in Brazil by CNAE section

CNAE section	2001		2010		2020	
	N° jobs	N° companies	N° jobs	N° companies	N° jobs	N° companies
Agriculture, Livestock, Forestry, and Fishing	2,050,866	36,508	2,675,473	133,162	2,221,939	206,348
Extractive Industries	136,282	5,264	247,062	6,246	276,583	6,711
Manufacturing Industry	6,237,299	192,437	10,165,161	246,838	9,154,525	275,863
Electricity and gas	1,505	44	134,468	2,071	144,899	2,836
Water, sewage, waste management activities	225,189	3,752	212,216	4,500	415,561	9,178
Construction	1,761,051	40,022	4,147,914	67,948	3,498,031	119,185
Trade (retail and wholesale)	5,847,228	646,972	11,868,930	1,049,630	12,324,334	1,157,226
Transportation, storage and mail	1,491,145	53,214	2,716,277	102,040	3,075,654	137,217
Accommodation and food services	894,099	75,990	2,330,951	149,781	2,498,150	208,884
Information and communication	1,263,425	49,585	703,644	23,981	1,153,850	44,768
Financial activities	589,668	20,952	839,377	28,278	955,305	37,905
Real estate activities	72,165	9,537	118,527	13,075	204,173	28,589
Professional, scientific and technical activities	580,758	41,337	1,127,949	73,602	1,489,371	131,314
Adm. activities and complementary services	2,794,118	115,741	4,619,711	165,711	6,743,628	268,905

<sup>3</sup> The independent variables in the model are binary indicators of political alignment between different levels of executive power. Thus, these variables reflect the specific political configuration at a given time and location, which depends on previous electoral processes. In this sense, it is reasonable to assume that these variables are exogenous in relation to the variation in employment in companies in the short term, given that elections occur at different times and are not influenced by the specific employment conditions of each company.

Public adm., defense and social security	6, 227, 520	11, 786	9, 968, 298	14, 679	10, 107, 455	16, 793
Education	85, 595	5, 294	1, 824, 294	51, 145	2, 334, 380	74, 060
Human health and social services	1, 248, 219	49, 204	1, 892, 133	87, 777	3, 101, 800	159, 562
Arts, culture, sport and recreation	24, 148	2, 104	25, 204	2, 094	303, 751	28, 340
Other service activities	937, 268	74, 276	1, 448, 960	101, 018	1, 243, 037	120, 076
Domestic services	4, 947	1, 390	6, 294	2, 662	1, 930	605
International organizations	765	90	2, 616	162	1, 253	135

Source: Authors' own elaboration using RAIS data.

Considering the information presented in Table 1, upon initial analysis, we can observe a widespread expansion in both employment relationships and the number of companies across nearly all economic sectors. However, distinct nuances are evident in specific activities. For instance, in the Agriculture, Livestock, Forestry, and Fishing sector, despite the number of companies experiencing a remarkable growth of 465.21% between 2001 and 2020, averaging 9.05% annually, the number of employment relationships increased only by 8.34% during the same period. It declined by 16.95% from 2010 to 2020. This observation indicates either sectoral consolidation or a rising trend toward automation.

We find another notable example of a reduction in the number of employment relationships between 2010 and 2020 in the Manufacturing Industry, which witnessed a 62.97% increase between 2000 and 2010 but presented a decrease of 9.94% between 2010 and 2020. However, there was an 11.76% increase in the number of companies during the same period, suggesting a transition to less labor-intensive business models. In contrast, the Trade (retail and wholesale) sector showed continuous but more modest growth between 2010 and 2020. In the aggregate, Trade accounted for approximately 20% of employment relationships and around 40% of the total number of companies. To avoid erroneously capturing these sectoral effects, the analysis is conducted separately for each CNAE section. Consequently, the parameters of Equation 1 were estimated independently for each of the 21 sections. The results of these analyses are presented below.

## 4 Results

Table 2 presents the estimated results for the 21 CNAE sections under analysis. Twenty-one models were estimated to assess the influence of political alignment on different sectors of the economy. For example, it is expected that the effect of political alignment on the employment variation in companies operating in the Extractive Industries activity is less pronounced, as the external market primarily drives the dynamics of employment expansion in this sector. That is, Extractive Industries are activities focused on tradable goods, with

their central demand originating from the external sector, unlike activities such as Commerce, Construction, and Education, where local market dynamics are the primary determinant of employment variation; these are non-tradable goods sectors.

According to the specifications provided by Equation 1, the estimated values for the variable *no\_conf* represent the reference category. In other words, the average of the dependent variable when there is no political alignment between the mayor, governor, and president in year *t* and municipality *i*. Thus, the estimated values for the variables *conf\_goma*, *conf\_prgo*, *conf\_prma*, and *conf\_total* represent deviations from the observed values for the reference category.

As per Table 2, the vast majority of the estimated coefficients show statistical significance at least at the 10% level. The results of the estimated model for Agriculture, Livestock, Forestry, and Fishing indicate that holding everything else constant, the percentage variation in the formal employment rate for companies operating in a non-politically aligned environment was 16.46% per year, on average. For companies operating in a political environment where the president and governor were from the same party *conf\_prgo*, the percentage variation in the formal employment rate was 17.79%, an increase of 1.33% compared to the baseline scenario. In the case of companies operating where the mayor and president were from the same party *conf\_prma*, the variation compared to the baseline scenario was even higher, at 1.75%. Finally, for companies in this sector operating in municipalities where the mayor, governor, and president were from the same party, the percentage variation in the formal employment rate was 20.28%, an additional 3.82% compared to the baseline. Therefore, the results indicate that companies in this sector operating in a supposedly more politically and economically aligned environment tend to exhibit a higher expansion rate compared to companies operating in less aligned political environments.

Similar results can also be observed for (i) Manufacturing Industry, (ii) Construction, (iii) Transportation, Storage, and Mail, (iv) Accommodation and Food Service, (v) Public Administration, Defense, and Social Security, and (vi) Arts, Culture, Sports, and Recreation, with particular emphasis on Trade (retail and wholesale) and Education.

The estimated results for the Trade and Accommodation and Food Service activities, two of the economic sectors with the highest representation in the sample, showed similar values, in both the baseline scenario and in terms of results depending on the type of political alignment. When there was no alignment, the average percentage variation in employment relationships was 15.47% for Trade sector and 14.05% for the Accommodation and Food Services sector. The marginal increases in each type of alignment were all positive

and statistically significant, reaching values of 6.33% and 5.99% in the case of total political alignment for Trade and Accommodation and Food Service, respectively.

To a lesser extent, a similar trend was also observed for the Education section. In the baseline scenario, the employment variation for companies operating in periods of non-alignment was 13.09%. In the confluence scenarios, there were statistically significant marginal increases in all cases, with a particular highlight for the total confluence scenario, where the percentage variation in employment was approximately 4% higher than in the baseline scenario.

Sectors such as "Electricity and gas" and "Water, sewerage, waste management activities" did not show statistically significant differences in the number of employment relationships between different political scenarios. Similar to the extractive industries case, these results can be explained by the nature of the activities. Both are non-competitive sectors linked to infrastructure supply and require substantial investments to operate. In summary, these sectors are characterized as natural monopolies and, therefore, follow a distinct employment and investment dynamic compared to other sectors.

**Table 2 - Results: Annual percentage variation in the number of formal employment relationships**

Dependent variable:		Independent Variables					
<i>Δ% employment relationship</i>							
CNAE Section	no_conf	conf_goma	conf_prgo	conf_prma	conf_total	n obs	
Agriculture, Livestock, Forestry, and Fishing	16.4559*** (0.3062)	0.3589 (0.5722)	1.3338** (0.6671)	1.7539** (0.8896)	3.8220** (1.596)	2,579,121	
Extractive Industries	17.5537*** (3.0841)	0.8587 (6.4366)	15.7204** (7.249)	2.596 (8.7548)	-2.3516 (15.6171)	128,678	
Manufacturing Industry	18.3632*** (0.1865)	0.8036*** (0.2929)	1.0592*** (0.3393)	-0.0058 (0.3459)	6.4540*** (0.7899)	5130,441	
Electricity and gas	16.7450*** (2.1938)	2.8702 (3.5795)	6.4359 (4.4735)	3.8114 (5.3569)	3.5517 (11.9614)	39,588	
Water, sewage, waste management activities	33.9801*** (1.6737)	0.239 (3.0192)	1.4383 (3.7523)	2.7796 (3.7289)	12.3441 (8.8121)	157,044	
Construction	44.0483*** (0.5795)	0.5463 (1.0988)	-1.1439 (1.2789)	3.9167*** (1.3204)	11.5241*** (3.0036)	1,729,580	
Trade (retail and wholesale)	15.4672*** (0.0696)	0.7271*** (0.0913)	1.9704*** (0.1063)	1.9634*** (0.1125)	6.3315*** (0.2441)	20,445,311	
Transportation, storage and mail	21.4095*** (0.3014)	-0.1944 (0.5049)	0.0673 (0.599)	2.4176*** (0.6168)	4.5807*** (1.4373)	2,104,174	
Accommodation and food services	14.0481*** (0.1282)	0.4643** (0.2019)	0.9895*** (0.2436)	1.9647*** (0.2521)	5.9926*** (0.6281)	3,123,723	
Information and communication	31.5035*** (1.1829)	0.2026 (1.5624)	6.6062*** (1.9381)	0.1563 (1.818)	8.9195* (4.6495)	999,013	
Financial activities	18.5715*** (0.7684)	0.0581 (0.7666)	1.5999* (0.9011)	2.5015*** (0.9489)	2.9272 (2.2047)	587,227	
Real estate activities	19.4006*** (0.2842)	-0.1465 (0.4388)	0.3158 (0.5192)	0.419 (0.541)	4.1795*** (1.3958)	1,664,146	
Professional, scientific and technical activities	18.4362*** (0.4394)	-1.1487* (0.6311)	0.7159 (0.7718)	1.9837** (0.791)	7.7130*** (2.2959)	3,982,414	
Administrative activities and complementary services	26.4394*** (3.9557)	-1.3991 (6.9667)	-7.3148 (7.7388)	38.1286*** (10.2722)	26.6524 (17.1658)	294,789	
Public administration, defense and social security	16.3003*** (0.2716)	0.1647 (0.4658)	0.3593 (0.6004)	1.2280** (0.5588)	3.1504** (1.5538)	1,062,197	
Education	13.0938*** (0.3269)	1.5579*** (0.5034)	1.0985* (0.589)	1.4668** (0.6326)	4.0021*** (1.4714)	1,932,097	
Human health and social services	12.8659*** (0.3568)	0.1344 (0.6135)	-0.1407 (0.6825)	4.0734*** (0.8136)	5.7247*** (1.873)	284,065	
Arts, culture, sport and recreation	14.1386*** (0.4327)	-0.1309 (0.4124)	2.0315*** (0.4842)	2.2428*** (0.5144)	6.7118*** (1.2063)	2,123,093	
Other service activities	10.6180*** (0.3824)	-0.0624 (0.7787)	2.5249** (1.0504)	-0.2781 (0.9386)	1.8826 (2.1764)	54,053	
Domestic services	19.3316***	-1.0591	0.3342	0.9909	4.0128*	335,699	

	(0.4953)	(0.6697)	(0.7803)	(0.7976)	(2.2329)	
International organizations	13.7390***	-0.7368	-9.4529**	-0.2639	1.8222	2,979
	(2.445)	(2.7909)	(3.8511)	(3.3331)	(10.9154)	

Notes:

Levels of statistical significance: \* $p < 0.1$ ; \*\* $p < 0.05$ ; \*\*\* $p < 0.01$ ;  
Standard errors adjusted for heteroskedasticity in parentheses.

The results of the empirical analyses indicate that, in all CNAE sections, the presence of political alignments between different government spheres tends to positively influence the variation in the formal employment rate in each individual company. However, it is important to emphasize that the magnitudes of these effects vary significantly from one section to another, even if they are positive.

This type of analysis highlights the complex interplay between politics and economics, as well as how political decisions, particularly the alignment of executive leaders, can influence the business environment at the regional level. It underscores the strategic role of the government as an inducer of optimistic conventions, which can be observed and potentiated according to the degree of alignment among executive leaders.

## 5 Discussion

In an environment of uncertainty, the formation of optimistic conventions as shared beliefs can mitigate agents' negative perceptions of an uncertain future and enhance their confidence in the profitable return of investment. One of the primary factors contributing to increased uncertainty in Western republican economies, such as Brazil, the United States, and Argentina, is the political factor. Resende and Terra (2020) point out that during the economic cycle from 2004 to 2016 in Brazil, there were contradictions, political inconsistencies, and a lack of coordination between fiscal, exchange rate, and monetary policies. This made it impossible to maintain optimistic predictions about the economy's trajectory, and consequently, it constrained the country's investment rate.

The results of this study suggest that federative coordination, understood as the political alignment among mayors, governors, and presidents - leaders of the executive branch - from the same political party, can foster an economic environment with higher employment growth for companies immersed in such alignment vis-à-vis companies in the same industry that are not in a politically aligned environment.

Indeed, the findings indicate that companies operating in sectors associated with non-tradable goods and services, such as Construction, Trade, Accommodation and Food Services, Education, Human Health and Social Services, and Arts, Culture, Sports, and Recreation, which operated in municipalities where executive leaders were from the same political party, maintained a substantially higher level of job creation compared to companies operating in an environment with leaders from different parties. In this regard, regional optimistic

conventions are likely to form in these economies as the employment variation of individual firms expands considerably more in such scenarios.

While our results suggest a positive relationship between political alignment and employment growth in Brazilian companies, it is important to consider alternative explanations for this phenomenon beyond the formation of optimistic conventions among local economic agents. One alternative hypothesis is that the positive relationship found could simply result from increased government expenditure in municipalities with higher political alignment. Political alignment between different levels of government might facilitate larger budget transfers from federal and state governments to aligned municipalities, which could directly stimulate local economic activity and employment growth through increased public spending and investment.

However, empirical evidence from Sakurai and Theodoro (2020) provides important insights that help us evaluate this alternative explanation. These authors empirically tested how public budget transfers are affected by political alignment in Brazil, analyzing transfers from both federal and state governments to municipalities between 1999 and 2012. Their findings indicate that political alignment has a limited effect on most types of government transfers. Specifically, they found that only one type of transfer analyzed - capital transfers from the federal government to municipalities - is significantly impacted by political alignment, while other current transfers show little influence from political alignment.

The fact that only capital transfers (and not the broader category of current transfers) are significantly affected by political alignment suggests that the mechanism through which political alignment influences local economic activity is more nuanced than a simple increase in overall government expenditure. Capital transfers, while important, represent a smaller portion of total transfers compared to current transfers. This evidence indicates that it is unlikely that the positive relationship we found between political alignment and employment growth is merely a result of increased government expenditure in politically aligned municipalities.

Therefore, our interpretation that political alignment facilitates the formation of optimistic conventions among private economic agents, leading to increased confidence and investment in employment, remains a plausible explanation for the observed relationship. The coordination of political discourse and policy implementation across different levels of government may indeed create an environment of reduced uncertainty that encourages private sector employment expansion, independent of direct fiscal transfers.

## 6 Final Remarks

The conflicts existing in the economy are not merely of a technical nature but inherently political (Erber, 2011), as private agents rely on conventions to address the problem of uncertainty. Conventions, in the post-Keynesian tradition, refer to collective rules of behavior based on expectations formed through the interaction between economic agents. These conventions are shared beliefs that compose the uncertain calculation of the future made by agents. Conventions have high intersubjectivity and affect the confidence with which expectations are formed (Keynes, 1988). The formation of optimistic conventions about the future is a critical element in stimulating private investment and, consequently, promoting economic activity.

One of the primary functions of the State is to create an environment capable of generating optimistic beliefs, as it is the exclusive holder of various essential attributes, such as the formulation of economic policy. Although international organizations and the media play a relevant role in decoding and disseminating information, it is the government's responsibility to serve as a guide for expectations, aiming to stimulate job creation and income by the private sector (Erber, 2011; Resende et al., 2021).

The alignment of political discourse and action is, therefore, a determining factor in the level of economic activity. Based on this assumption, the empirical analysis proposed in this work used the concept of political-party alignment among the three levels of the executive branch in the Brazilian federation as a proxy for a guide of expectations for private agents, which consequently tends to create a favorable environment for the formation of optimistic conventions at the regional level.

The empirical results support this assertion. The results show significant differences in hiring patterns between Brazilian companies that operated in a presumably more politically homogeneous environment compared to those that operated in a less aligned environment. Some sectoral differences were observed and discussed. The findings, in general, support the hypothesis that party alignment among mayors, governors, and the President can stimulate local economic activity, possibly through the formation of optimistic conventions for society as a whole, generating more jobs. The concept of conventions is inherently latent and can hardly be directly measured. However, this research contributes to the post-Keynesian literature by proposing an indirect estimation of the impact of the formation of optimistic beliefs on labor demand in Brazilian companies.

From a methodological perspective, future research could benefit from employing municipality fixed effects models to better control for unobserved municipality-specific characteristics, provided there is sufficient within-municipality variation in both political alignment and company representation, thereby avoiding confounding between fixed effects and individual-level factors. The study is also limited by the lack of

operationalization of specific cases of party switching by mayors and governors during their terms, which could be addressed in future research.

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