Chapter 1

Contemporary political economy: An overview

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Most of the chapters in this volume are revisions of papers presented at conferences on "Political–Economic Models and Cycles" held at the Center for Advanced Study in the Behavioral Sciences, Stanford, California, February 26–March 1, 1978 and Bonn University, West Germany, January 4–7, 1979.[1] The aim of the conferences was to bring together European and American political scientists and economists engaged in analytical and empirical research on the interdependence of politics and economics.

The general research paradigm underlying most of the work reported in this book is illustrated by fig. 1.1, which draws upon the research frameworks described elsewhere by Gordon (1975) and Frey and Schneider (1975). Macroeconomic performance, mass political support, and macroeconomic policy are viewed as a system of dynamic, interdependent political–economic relationships. Following Gordon's terminology, the system is conceived in terms of the "demand for" and "supply of" economic outcomes. Most empirical work has given special attention to inflation and unemployment outcomes.

As fig. 1.1 suggests, political support for incumbent chief executives, parties, or political blocs is influenced, among other things, by current and past macroeconomic performance. The response of mass political support to fluctuations in economic conditions implicitly reveals infor-

[1] The conferences were organized and chaired by Douglas A. Hibbs, Jr., Harvard University, and Heino Fassbender and Wilhelm Krelle, Bonn University. The hospitality of the Center for Advanced Study in the Behavioral Sciences and Bonn University and the financial support of the National Science Foundation and the Deutsche Forschungsgemeinschaft are gratefully acknowledged.

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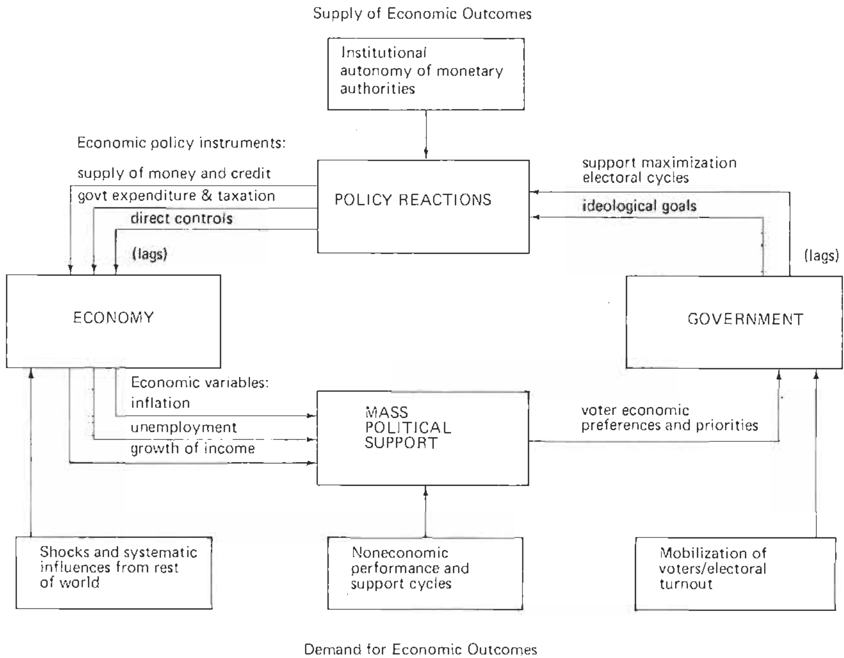

Figure 1.1. A simplified political–economic system.

mation about the public's relative economic priorities and preferences and comprises the voters' "demand" for economic outcomes.

The papers in Part II deal exclusively with such "demand" functions for the United States, Great Britain, Germany, and France. Chapter 3, by Douglas Hibbs and Nicholas Vasilatos ("Macroeconomic performance and mass political support"), is a comparative investigation of political support in the United States and Great Britain that attempts to evaluate rigorously a number of "retrospective comparison" models of the way in which voters judge a government's economic performance. Several of the models yield plausible estimates and, although it is difficult to settle on one specification from the results of regression experiments based on such highly aggregated observations, the empirical evidence in this paper does indicate that a government's contemporaneous support in the mass public depends upon its past as well as its current macroeconomic performance. This conclusion contrasts with the results of most of the earlier work on economic conditions and political behavior, which implied that

voters discount heavily prior performance in making contemporaneous political choices.[2]

The next chapter by Samuel Kernell and Douglas Hibbs ("A critical threshold model of presidential popularity") covers ground similar to the Hibbs and Vasilatos paper with respect to the U.S. case, but employs explicitly a threshold-response model of presidential approval. The threshold-response model captures well the micro process of individuals making binary choices and yields predictions consistent with the observed nonlinear marginal response of a president's approval rating within partisan subgroups to movements in the macro economy.

Morris Fiorina's paper, Chapter 5 ("Short- and long-term effects of economic conditions on individual voting decisions"), also deals with American political behavior, but focuses on the ways in which personal economic experiences as well as national economic outcomes influence long- and short-run electoral behavior. Fiorina's work is important, among other reasons, because it successfully integrates a rational choice model of political behavior with the affective, social-psychological approach associated with the Michigan school. Rather than viewing voters' party affiliations ("party identification") as exogenous, as for example Kernell and Rattinger implicitly do, Fiorina (correctly in my view) treats party identification as endogenous.

The remaining chapters in Part II report investigations of economic performance and political support in Germany and France. In Chapter 6 ("The effect of economic change on political parties in West Germany") Paul Peretz analyzes aggregate postwar German time-series data to determine if macroeconomic fluctuations have differential effects on popular support for incumbent political leaders as opposed to incumbent political parties or on governing parties as opposed to opposition parties. Peretz also tests the proposition that, in the short run at least, high inflation typically advantages the "right" party (CDU/CSU) and high unemployment typically advantages the "left" party (SPD), no matter which party is in power.

The latter hypothesis forms the major theme in Hans Rattinger's paper ("Unemployment and the 1976 election in Germany"), which appears in Chapter 7. Contrary to Peretz, who concludes that German voters do not necessarily turn to the SPD in periods of high unemployment, Rattinger argues from his cross-sectional analysis of district level data that rising cyclical unemployment did advantage the governing Social Democrats in 1976. However, the impact of structural unemployment on the 1976 district vote shares was more complicated and depended significantly on the

[2] See, for example, Fair (1978), Kernell (1978), and Kramer (1971). Several of the papers in this volume also implicitly make this assumption.

political ecology of the area. Perhaps this helps explain the differences between Rattinger's and Peretz's conclusions.

Jean-Dominique Lafay's chapter ("The impact of economic variables on political behavior in France") concludes this part of the volume. Although Lafay's analysis is admittedly preliminary and his specification is somewhat *ad hoc*, his paper represents the first empirical study of economic conditions and popular support for (satisfaction with) the Prime Minister in France. The most novel feature of Lafay's work is his simulation of the political consequences of various macroeconomic policy scenarios and his exploration of the relationship between the standing of the government in the opinion polls and actual electoral outcomes. These lines of analysis could be replicated productively elsewhere.

As fig. 1.1 indicates, governments are assumed to attempt to maximize political support and perhaps also to pursue ideological goals, which might best be conceived in terms of the distinctive economic priorities of their core political constituencies. The way in which government macroeconomic policy reacts to voters' preferences, subject of course to external constraints, defines the "supply" of economic outcomes. The papers in Part III of the volume focus largely on this question, that is to say they involve attempts to make government policy actions endogenous and to identify politically motivated business cycles.

Part III opens with Heino Fassbender's contribution in Chapter 9 ("From conventional IS–LM to political–economic models"). Building upon Blinder and Solow's (1974) conventional IS–LM model, Fassbender investigates analytically the implications for stability of a closed political–economic system in which macroeconomic policies are driven by movements in the government's political support.

In the following chapter ("On the political business cycle") Duncan MacRae extends empirically the earlier theoretical work of Frey and Lau (1968), Nordhaus (1975), and MacRae (1977) on the short-run political business cycle. MacRae applies discrete-time control theory in conjunction with a linear inflation–unemployment relation and a standard quadratic vote loss equation to compare the explanatory power of the assumption of a myopic electorate that evaluates economic performance only over the electoral period to the assumption of a rational electorate with an unlimited time horizon. Since voter myopia is a critical assumption of all short-run political business cycle models, MacRae's empirical results for five U.S. presidential election periods have important implications for the future development of this line of work.

The next three chapters report empirical analyses of the evidence in favor of politically driven policy cycles in Great Britain, West Germany, the United States, and Switzerland. In Chapter 11 ("Politico-economic models of British fiscal policy") James Alt and Alec Chrystal

propose a "permanent income" model of fiscal policy actions in Great Britain and argue that it better explains the fiscal data than the alternative explicitly political policy functions of Frey and Schneider (1978a, b). Reiner Dinkel's investigation of electorally motivated fiscal expansions in the U.S. and Germany in Chapter 12 ("Political business cycles in Germany and the United States") also does not favor the short-run political cycle hypothesis. Dinkel finds little evidence of electorally timed fiscal expansions in either Germany or the United States. However, Schneider, Pommerehne and Frey's paper in the following chapter ("Politico-economic interdependence in a direct democracy"), which applies the framework developed in Frey and Schneider's earlier pioneering studies of Great Britain, Germany, and the United States (Frey and Schneider, 1978a, 1978b, 1979) to the special circumstances of Switzerland, indicates that public expenditures do respond in a systematic way to popular political support.

Two studies of longer run, structural political influences on economic outcomes conclude the volume. The paper by Burton, Hawkins and Hughes in Chapter 14 ("Is liberal democracy especially prone to inflation?") employs a standard closed economy analytic framework in conjunction with a simplified political support function to analyze the common argument that policy officials in liberal-democratic, electorally competitive regimes are more prone to pursue inflationary policies than governing authorities in nonelectoral systems. Burton et al. point out and illustrate analytically that although officials in nondemocratic regimes do not have a "vote motive" for inflationary policies, they probably face "survival in office/prevention of coup" constraints and, therefore, it is not possible to derive unambiguous qualitative conclusions about the inflationary consequences of electoral competition. Tentative empirical evidence reported elsewhere appears to support their argument (Hughes et al., 1978).

In the final chapter of the book ("Partisanship and macroeconomic outcomes") Henrik Madsen evaluates for the Norwegian case an argument I made earlier (Hibbs, 1977) concerning partisan effects on macroeconomic policies and outcomes. Briefly, my argument was that governments pursue macroeconomic policies broadly consistent with the objective economic interests and subjective preferences of their core political constituencies. Social Democratic and Labor parties typically attach greater weight to the full employment goal than centrist and rightist parties, and these partisan differences in economic priorities have an observable impact on macroeconomic outcomes, particularly unemployment outcomes.

In the case of the small open Norwegian economy, Madsen finds that the equilibrium target rate of unemployment does not appear to differ

appreciably across Social Democratic and Bourgeois governments. Instead, he suggests that the political importance of the memory of the Great Depression of the 1930s constrained all governments to pursue high employment policies. He also introduces cross-national evidence to support the more general argument that actual control of the executive by Social Democratic or Labor parties is less important for employment policies and outcomes than the organizational strength of trade unions in the political system.

Considered as a whole, the empirical evidence presented in this volume and elsewhere indicates rather convincingly that public support for political authorities in a wide range of institutional settings responds quite systematically to macroeconomic conditions. Nonetheless, at this writing there is no consensus about the appropriate theoretical specification for the economy–political behavior linkage. Until empirical studies are integrated into a persuasive, sharply defined theoretical model it will not be possible to draw precise conclusions about the political consequences of macroeconomic developments.

The idea that macroeconomic policy-makers react in a predictable way to fluctuations in political support remains controversial. Empirical work on this topic has produced mixed results, but it is clear that macroeconomic policies and outcomes do not consistently exhibit easily identified short-run electoral cycles.[3] I suspect that the failure of many empirical studies to identify clearly political influences on macroeconomic policy reactions merely reflects the fact that such investigations often are considerably less sophisticated than even the most routine studies of economic influences on political behavior. Clearly we have much to learn about how to exploit the information embodied in studies of the "demand" for economic outcomes in analyses of the politics of the "supply" of economic policies.

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[3] In addition to the papers in part III see, for example, Eckstein (1978), Paldam (1978, 1979), and MacCallum (1978).

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