

Political Economy

Economic and Fiscal Policy

Last session



In It Together

Why Less Inequality Benefits All



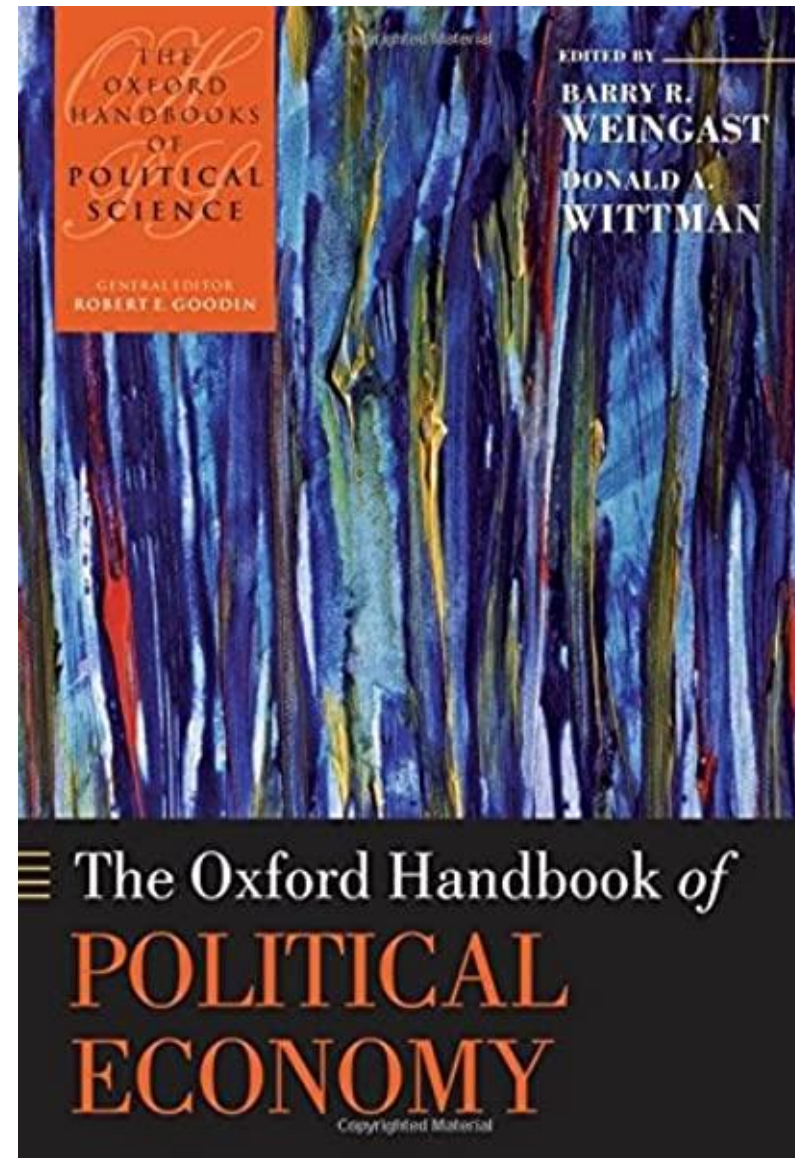
Who wins?

Majoritarian electoral
democracy

Elite theory

Majoritarian Pluralism

Biased Pluralism



Democratisation

- Warmup game
- Assume that
 - the government's role is redistribution
 - No deadweight costs to redistribution
 - the government collects flat tax from everybody and pays back as UBI
- Distribution today:
 - Total amount:
 - # of students:
- Your Task: Choose a flat tax rate between 0 and 100%
- Menti.com: 3487 2400,
<https://www.menti.com/1nv6ojseea>



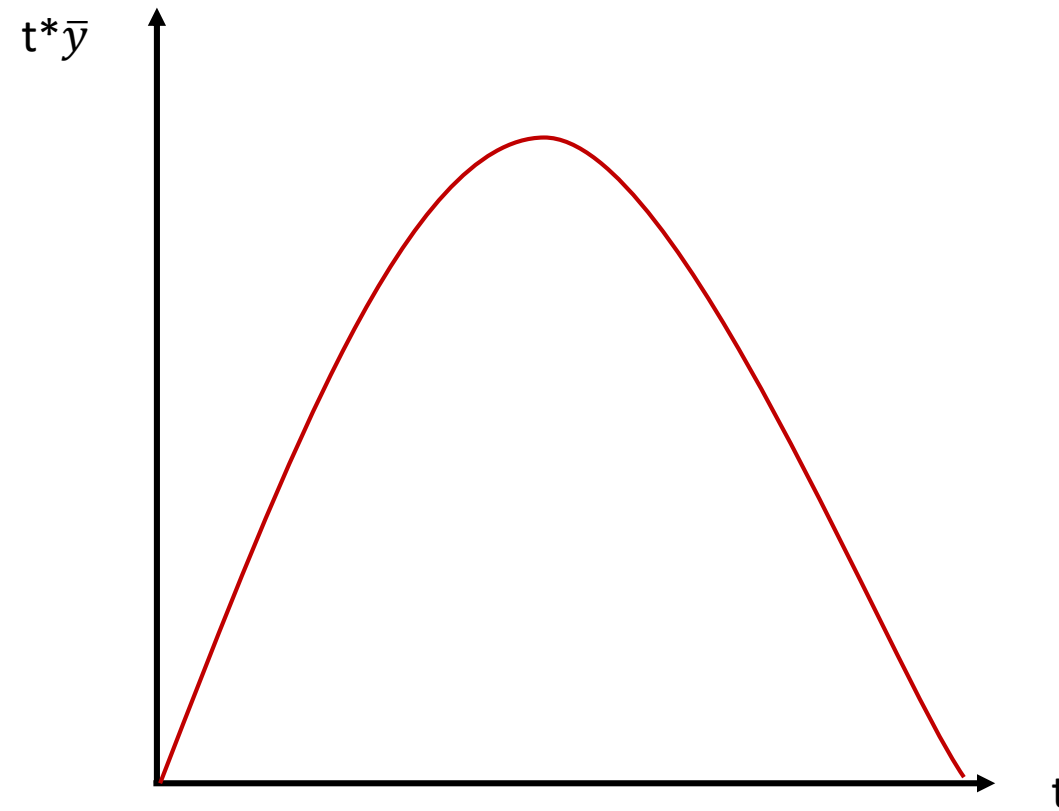
Democratisation

- What would a profit-maximising voter do?
- Prediction: relationship between property rights and democracy
 - “[pure] democracies...have ever been found incompatible with personal security or the rights of property.” (James Madison)
 - “Along with the constantly diminishing number of the magnates of capital [...] grows the mass of misery [...]; but with this too grows the revolt of the working class [...].” (Karl Marx)
- General intuition: As soon as more than half of voters can be made better off by a policy, they will rule over the minority

Democratisation

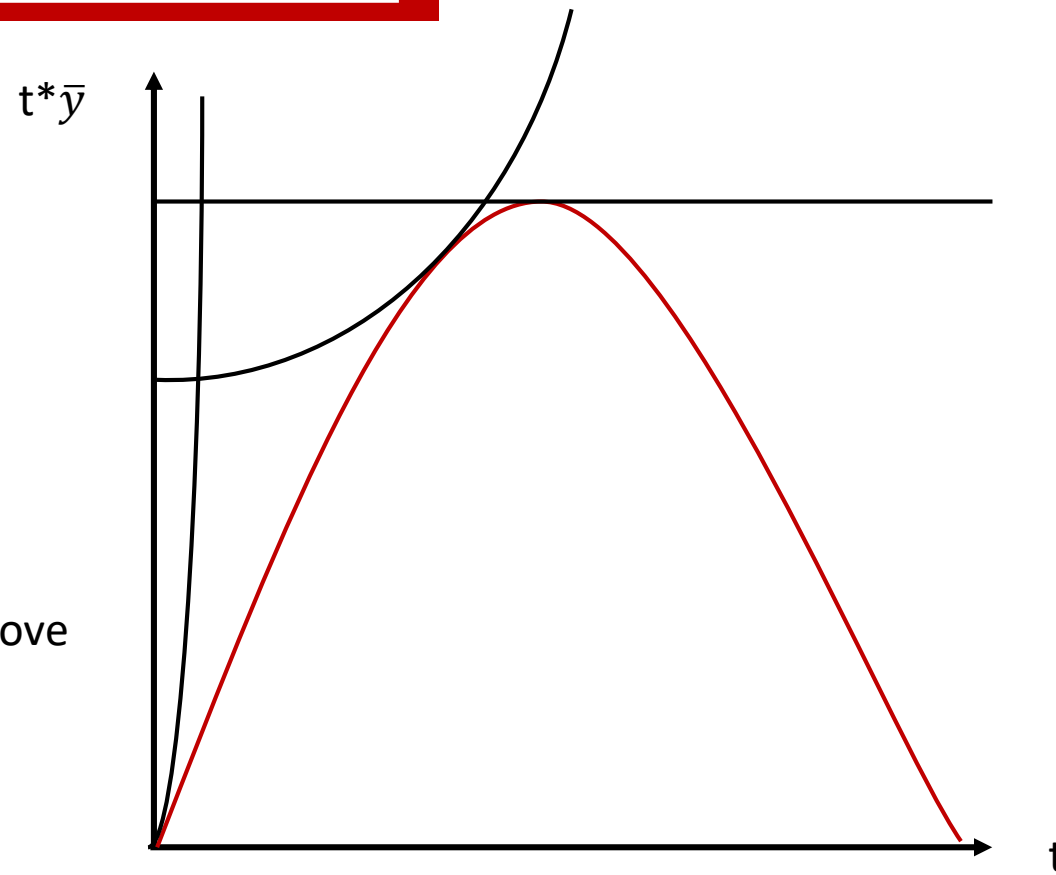
- Meltzer & Richards extend the idea by incorporating behavioural responses to taxation. The model suggests voters maximise their income. Work incentives: add leisure-labour tradeoff – pie shrinks
- $c = (1 - t)x * n + t * \bar{y}$
 - $t * \bar{y} \sim$ Basic income (paid to everybody)
 - Model assumption: $n \sim$ Laffer Curve (endogenous), n falls as t increases.

Democratisation



Democratisation

Somebody with lower income wants higher taxes



Person with lowest income will vote for the tax maximising the basic income

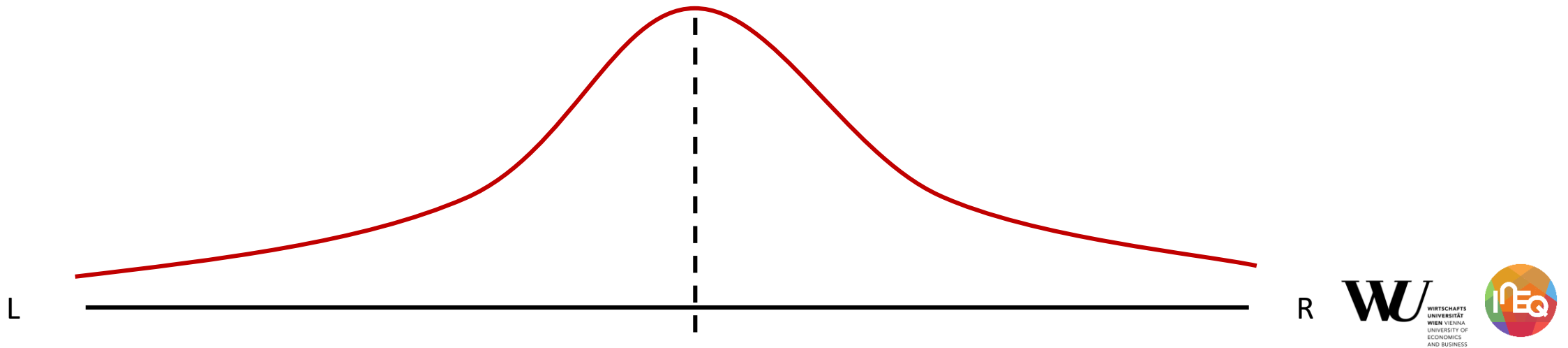
Somebody with income above mean income

Democratisation

- Why did you cast your vote like you did?

Democratisation

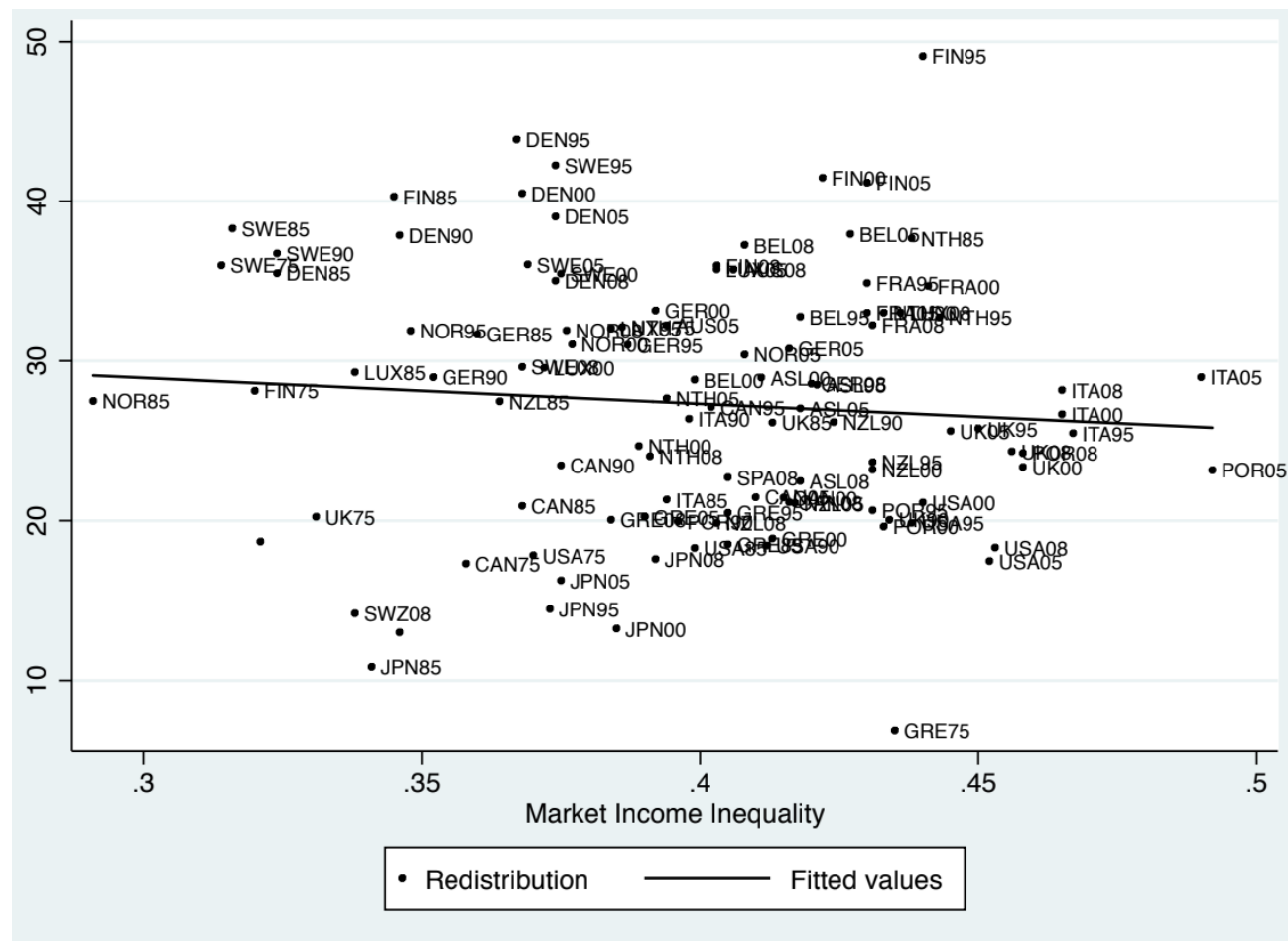
- What will a vote maximizing policy-maker do?
 - Policy makers will compete for the votes of one half of the population to achieve electoral success. They will aim to cater to the interests of the political center – Hotelling's Law
 - Frequently used in connection with left-right spectrum. One dimensional policy space
 - Of course, also tax rates work



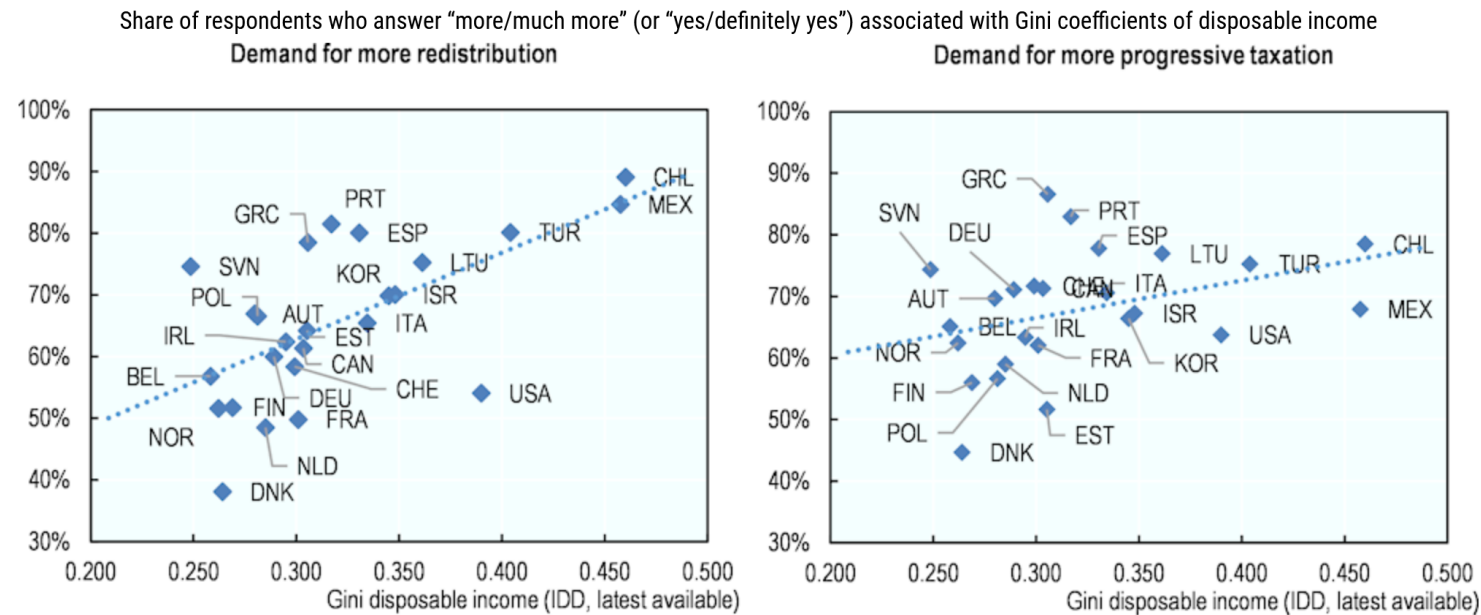
Democratisation

- If median worker does not work: they will set tax rate that maximises the amount of redistribution given the other voters responses to taxation
- If median voter earnings are below mean income: median voter maximises personal income (sum of work income and transfer income)
- If median voter earns average income or more: no tax
- Is this a good model?

Observable implications



Observable implications

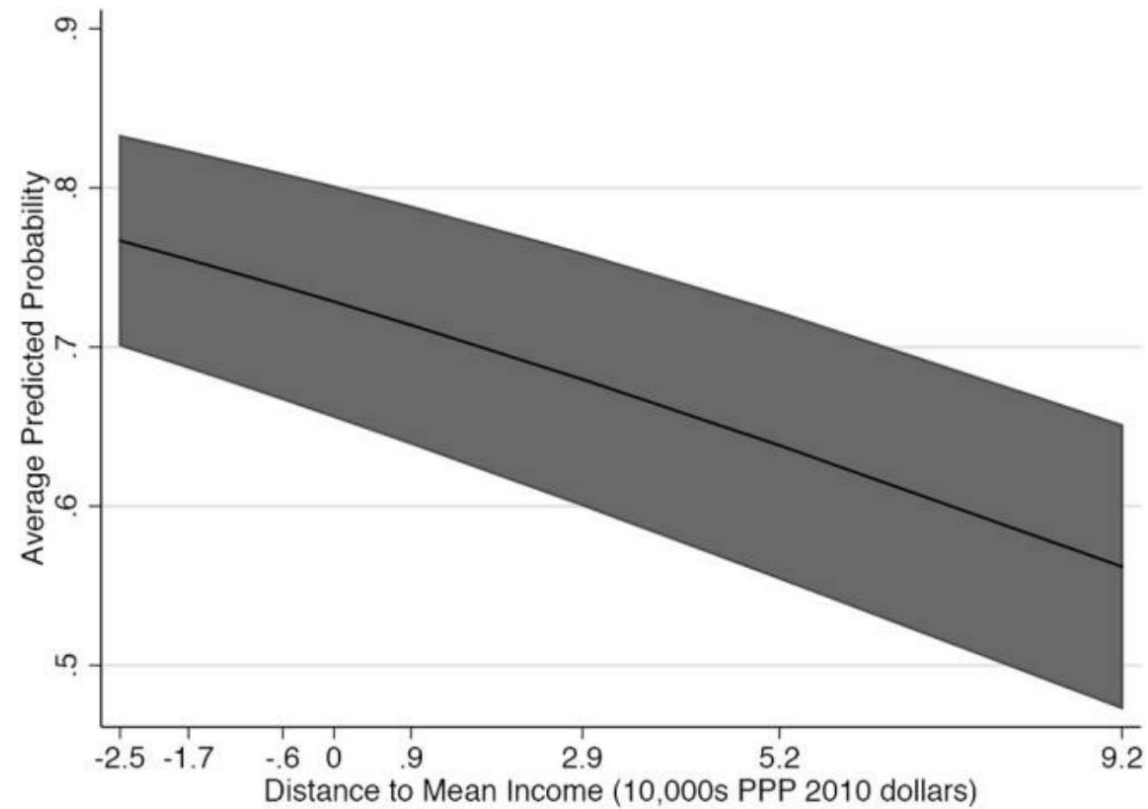


Note: The Gini coefficient for disposable income refers to 2018, apart from 2017 for Chile, Denmark, Germany, Ireland, Italy, Switzerland, the United States, 2016 for Mexico and the Netherlands, and 2015 for Turkey 2015.

Source: OECD calculations from the 2020 Risks that Matter Survey and *OECD Income Distribution Database* (<https://stats.oecd.org/Index.aspx?DataSetCode=IDD>).

StatLink <https://stat.link/lbj35u>

Observable implications



Individual voting other

- What are the most important drivers of tax policy preferences according to Stantcheva? How do they contrast with the median voter theorem?
- What is polarised reality and how does it affect voting?

Individual voting other

Growing up in a Recession

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First version received May 2010; final version accepted October 2013 (Eds.)

Does the historical macroeconomic environment affect preferences for redistribution? We find that individuals who experienced a recession when young believe that success in life depends more on luck than effort, support more government redistribution, and tend to vote for left-wing parties. The effect of recessions on beliefs is long-lasting. We support our findings with evidence from three different datasets. First, we identify the effect of recessions on beliefs exploiting time and regional variation in macroeconomic conditions using data from the 1972 to 2010 General Social Survey. Our specifications control for non-linear time-period, life-cycle, and cohort effects, as well as a host of background variables. Second, we rely on data from the National Longitudinal Survey of the High School Class of 1972 to corroborate the age-period-cohort specification and look at heterogeneous effects of experiencing a recession during early adulthood. Third, using data from the World Value Survey, we confirm our findings with a sample of 37 countries whose citizens experienced macroeconomic disasters at different points in history.

Key words: Preferences for redistribution, Beliefs, Recession.

JEL Codes: P16, E60, Z13

Majoritarian Pluralism

- PRT: Focus on political actors/Groups (in contrast to individualist theories such as median voter theorem)
 - Two arenas of political struggle. Parties/classes compete for influence on several realms. „Democratic class struggle“.
 - Politics
 - Parties represent certain voter groups (Workers, dependent on wage labour, agriculture (note: workers and farmers), SME, industry)
 - Political competition
 - Markets
 - Unions and trade associations
 - Industrial action – strike, sabotage, ...
 - In Austria: institutionalised
 - power resources of unions and left wing parties/business
 - “For those of modest means (workers), the only compensating power resource is their numbers, but this requires mass organization in unions and parties to be effective...” (Myles & Quadagno 2002)

Partisan Politics



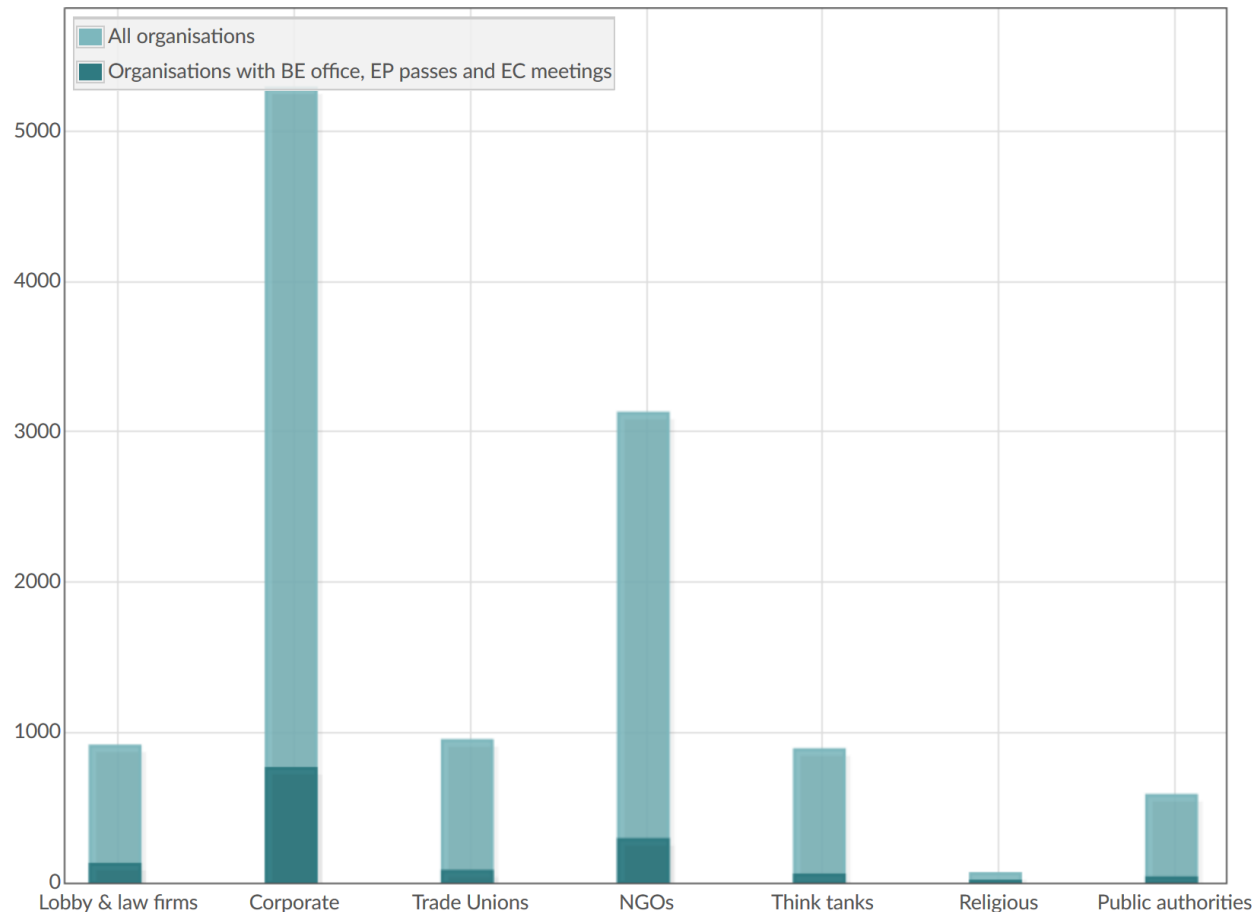
Biased pluralism

Organisation	Lobbying outlays in Mio Eur
European Chemical Industry Council	12
FTI Consulting Belgium	6,75-7
Fleishman-Hillard	6,75-7
Insurance Europe	6,5-6,75
Burson Cohn & Wolfe	6,25-6,5
EUROCITIES	6-6,25
Google	6-6,25
Europ. Federation of Pharmaceutical Industries and Associations	5,5
Interel European Affairs	5-5,25
Microsoft Corporation	5-5,25

- Lobbies, advocacy groups, firms, etc.

Katzemich, Nina, Timo Lange, und Max Bank. „EU-Lobbyreport 2019“. Köln: LobbyControl, 2019.
<https://www.lobbycontrol.de/wp-content/uploads/EU-Lobbyreport2019.pdf>.

Biased pluralism



„Charts & Graphs | LobbyFacts Database“. Accessed 5. März 2020.
<https://lobbyfacts.eu/charts-graphs>.

- Number of organisations by category
- For each organisation on employee interests, there are approximately 50 interest groups affiliated with employers

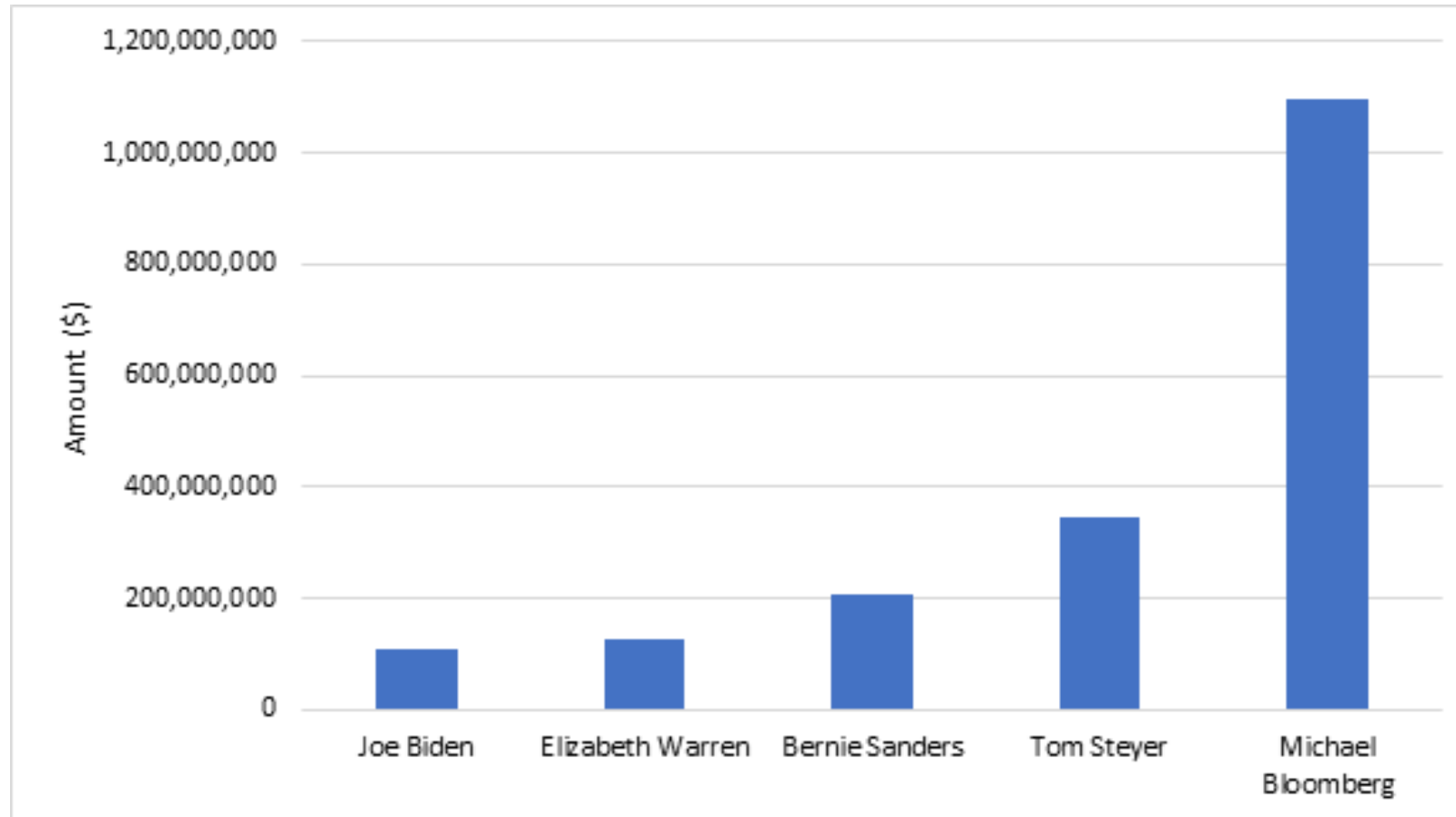
Elite theories

- Winner take all politics: Democracy does not balance capitalism, but supports economic system and sets rules such that it allows some „actos to win big and others to loose big“
- Elites
 - Who counts?
 - Scope of conflict and elite involvement
 - Does the elite speak with one voice?

Elite theories

- Campaign funding
- Evidence from the US (Kalla, Joshua L., und David E. Broockman. „Campaign Contributions Facilitate Access to Congressional Officials: A Randomized Field Experiment“. *American Journal of Political Science* 60, Nr. 3 (2016): 545–58.
<https://doi.org/10.1111/ajps.12180>.)
 - Most campaign funding from wealthy individuals
 - Campaign finance guarantees special access to politicians (though may not be sufficient)
 - Experimental evidence to distinguish correlation (such as shared beliefs) from causation
 - Scheduling meetings between organisation (advocacy) members and congressional offices with random revelation of donor status
 - „When informed prospective attendees were political donors, senior policy makers made themselves available between three and four times more often”

Elite theories



<https://blogs.lse.ac.uk/usappblog/2020/11/27/the-2020-election-was-the-most-expensive-in-history-but-campaign-spending-does-not-always-lead-to-success/#Author>

Elite theories

- Revolving door models
 - What happens?
 - Politicians can assume lucrative positions in organisations that they gave preferential treatments when in office. Also in the other direction: Organisations with political interests may place actors in decision-making positions
 - Reciprocal
 - Robertson u.a. (2019): More than one-third of people registered on the Australian Government Register of Lobbyists were previously government representatives
 - European union: Cool-down phase

Who wins?

- Gilens, Martin, und Benjamin I. Page. „Testing Theories of American Politics: Elites, Interest Groups, and Average Citizens“. *Perspectives on Politics* 12, Nr. 3 (September 2014): 564–81.
<https://doi.org/10.1017/S1537592714001595>
- Coincidental beneficiaries of policies in majoritarian democracy
- Differences between interest group influence (numerical dominance & heterogeneity)

Table 4
The separate policy impact of business-oriented and mass-based interest groups

Average citizens' preferences	.05 (.08)
Economic elites' preferences	.78 (.08)***
Mass-based interest groups	.24 (.07)***
Business interest groups	.43 (.08)***
R-sq	.07

***p<.001

Note: All predictors are scaled to range from 0 to 1. The dependent variable is the policy outcome, coded 1 if the proposed policy change took place within four years of the survey date and 0 if it did not. Predictors are the logits of the imputed percent of respondents at the fiftieth (“average citizens”) or ninetieth (“economic elites”) income percentile that favor the proposed policy change, and the Net Interest-Group Alignment Indices described in the text. Standard errors are asymptotically distribution-free, and all analyses reflect estimated measurement error in the predictors, as described in Appendix 2. N=1,779.