

The Political Effects of Inequality-Increasing Policy: Evidence from a Welfare and Tax Reform

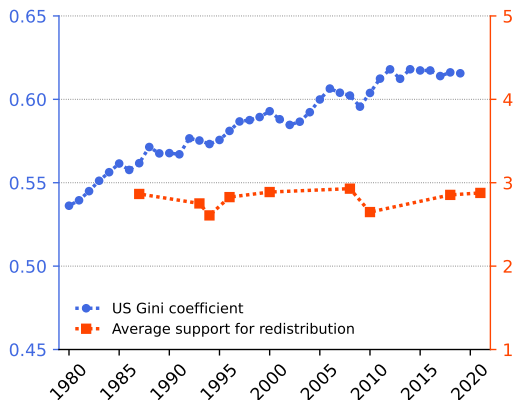
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Fifth Dondena Workshop on Public Policy, 19 December 2023

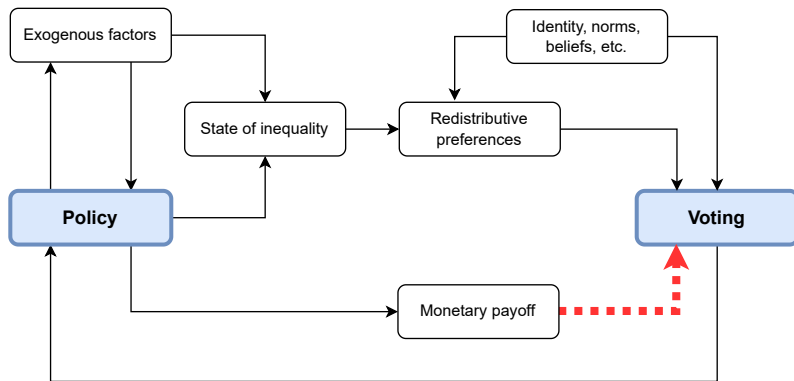
A big puzzle

- Despite rising inequalities and decreased tax progressivity in recent decades – only limited support for redistribution



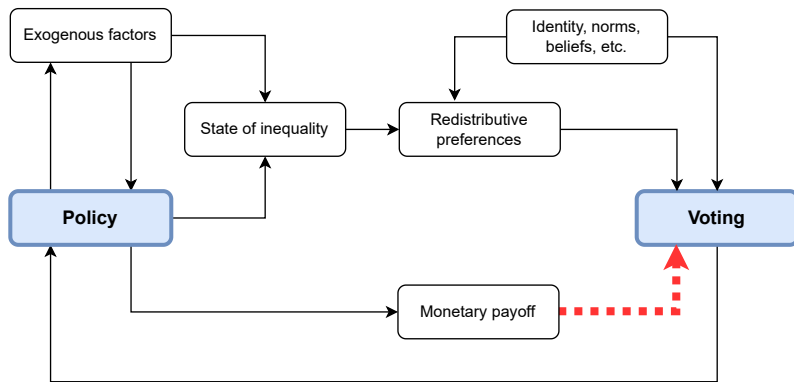
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A big puzzle

- Despite rising inequalities and decreased tax progressivity in recent decades – only limited support for redistribution



- Hard to estimate a direct link between policy changes and voting

This paper

- ▶ Exploit major reforms following Israel's 2003 elections
- ▶ Analyze changes in voting over time (in particular between 2003 and 2006)
- ▶ Primary question: How do voters respond electorally to inequality-increasing policies?
- ▶ Secondary question: Is electoral behavior really aligned with redistributive preferences?
- ▶ Related literature

Key results

- ▶ Significant electoral effect on affected individuals:

Asymmetry: Small negative effect on negatively affected poorer voters; Large positive effect on positively affected richer voters

- ▶ Identity-based voting may be the leading explanation for the weak effect on negatively treated voters – both instrumental and expressive

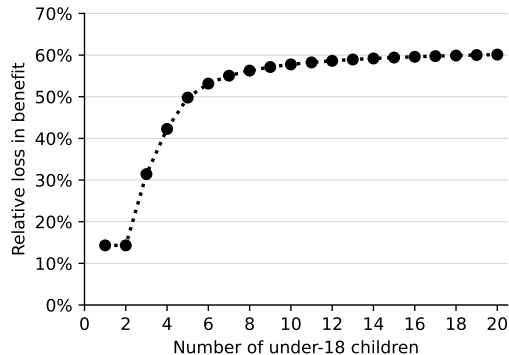
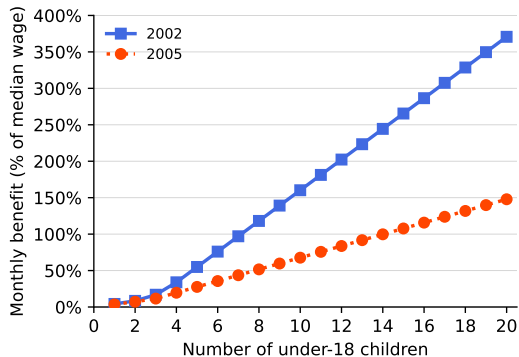
Background: Israeli political system

- ▶ Parliamentary system (single house)
- ▶ Closed party-list proportional representation (single constituency; vote is for a list, not candidates)
- ▶ Elections every four years (less, in practice)

Crisis, elections and reforms

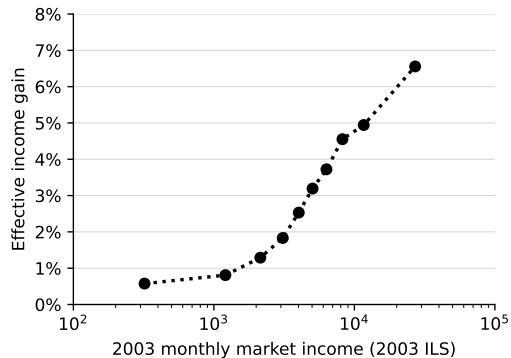
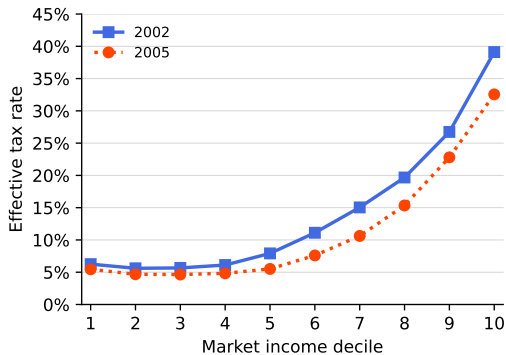
- ▶ 2001–2003 economic crisis:
 - ▶ Dot-com crash
 - ▶ Second Intifada (mainly from late 2000 to late 2003)
- ▶ 2003 elections:
 - ▶ Decisive win for the Likud (eqv. to Conservatives or CDU)
 - ▶ Enabled implementing major economic reforms
- ▶ 2003 reforms:
 - ▶ Sharp cut in child benefits
 - ▶ Tax cuts with decreased progressivity

Cut in child benefits

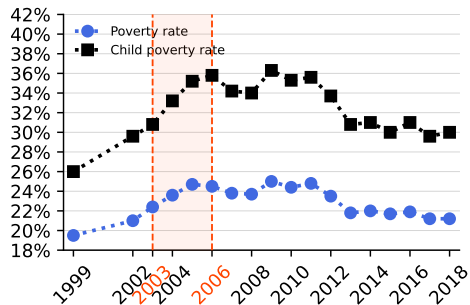
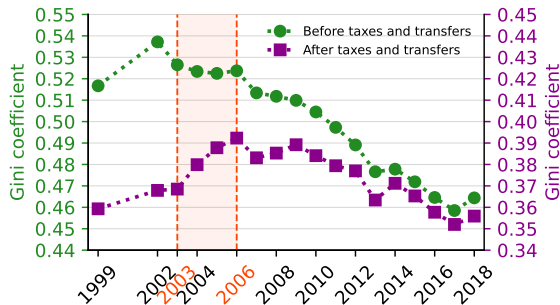


(17% of families with 4+ children; 4.5% with 6+)

Tax cuts



2003 reforms: Jump in inequality and poverty

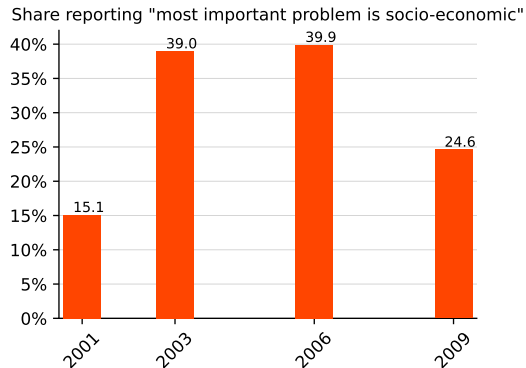
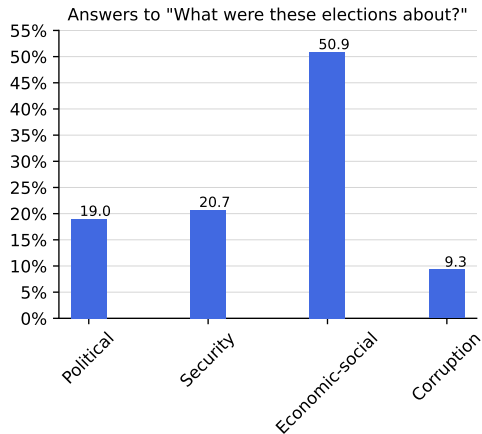


Analysis

- ▶ The reforms affected negatively families with many children
- ▶ They affected positively the top deciles of the income distribution
- ▶ **Did treated voters (negatively or positively) increased/decreased their support in the 2003 coalition parties in the subsequent elections?**

Analysis

Importantly: strong indication that socio-economic issues are cardinal in the 2006 elections



Data

Two key datasets:

- ▶ Pre- and post-election surveys
 - ▶ 1000-2000 respondents (representative of election results)
 - ▶ Individual voting (“For which party did you vote in ...”)
 - ▶ Socio-demographic variables including number of people in household
 - ▶ Attitudes towards policies and values

- ▶ Linked election results by local authority and socio-demographic administrative data
 - ▶ High accuracy of election results
 - ▶ Rich socio-economic data (including income)

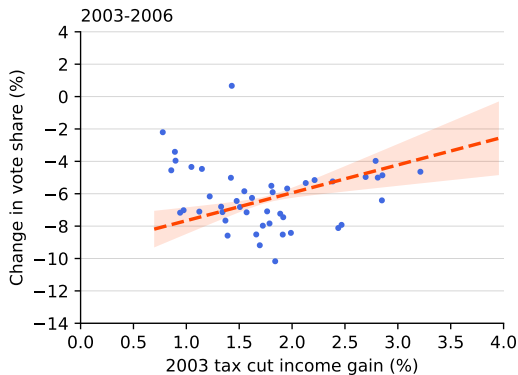
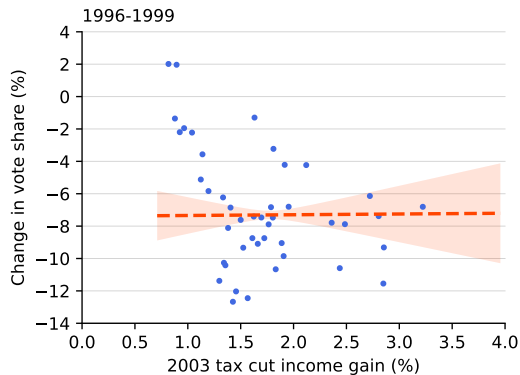
Research design

- ▶ Object of interest: Support for 2003 coalition parties in pre- and post-treatment elections (binary for individuals, vote share for local authorities)
- ▶ Difference in differences with continuous treatment:

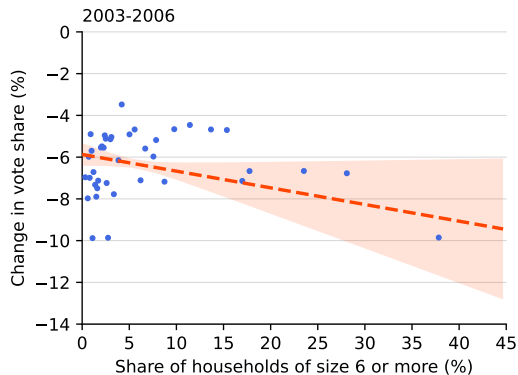
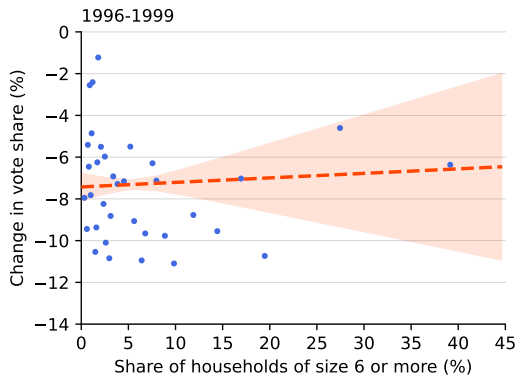
$$y_{i,r,t} = \alpha_i + \theta_{r,t} + \delta \times \mathbf{1}_{t>2003}(t) \times \text{Reform}_{i,j} + \epsilon_{i,r,t}$$

- ▶ Treatment 1: Tax cuts – treatment is defined as the income tax gain as a share of average income
 - ▶ Treatment 2: Cut in child benefits – treatment defined differently for individuals and municipalities
- ▶ Synthetic controls

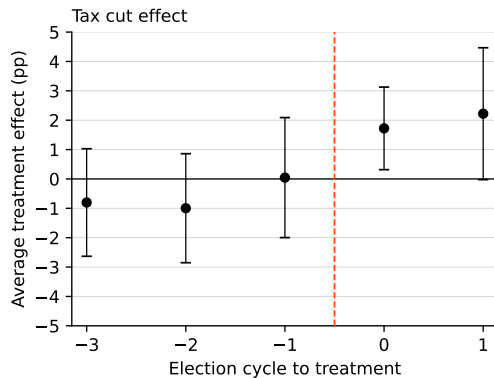
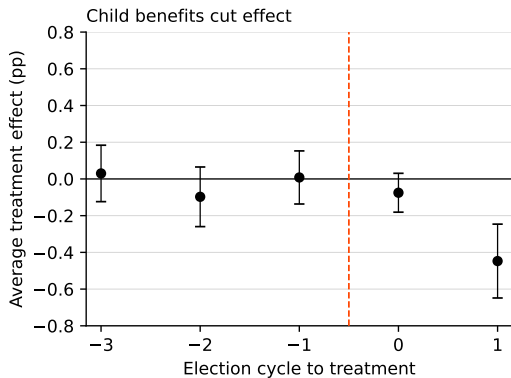
Municipality-level results: Tax cuts



Municipality-level results: Cut in child benefits



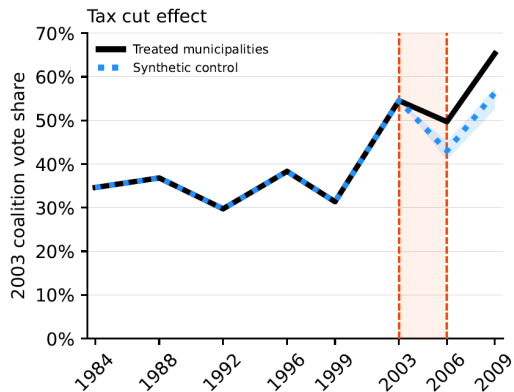
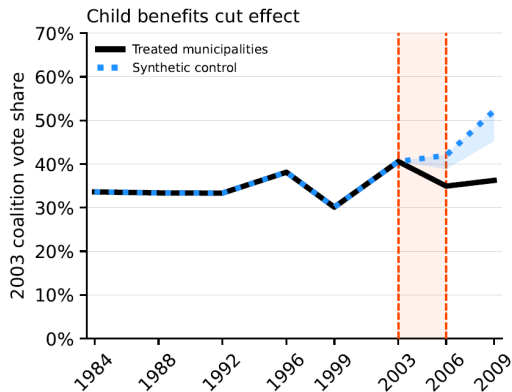
Municipality-level results



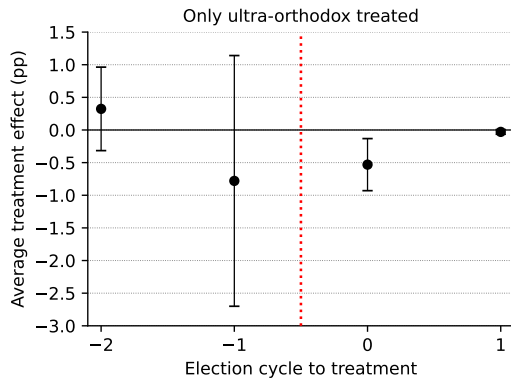
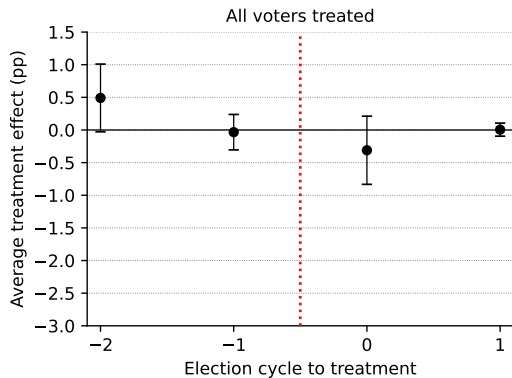
Municipality-level results

	Cut in child benefits <i>ShareOf6+</i>			Tax cuts <i>IncomeGain</i>		
	pop. weighted	unweighted	Small munis.	pop. weighted	unweighted	Small munis.
δ	0.112 (0.123)	-0.568*** (0.043)	-0.631*** (0.049)	8.074*** (0.654)	8.548*** (0.344)	10.419*** (1.427)
R^2	0.733	0.885	0.898	0.822	0.884	0.889
N	7342	7342	6009	7683	7683	6241

Municipality-level results: Synthetic controls



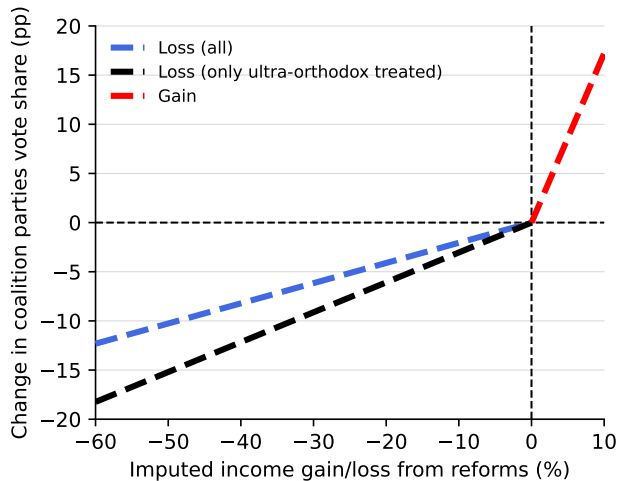
Individual-level results: Cut in child benefits



Individual-level results: Cut in child benefits – different specifications

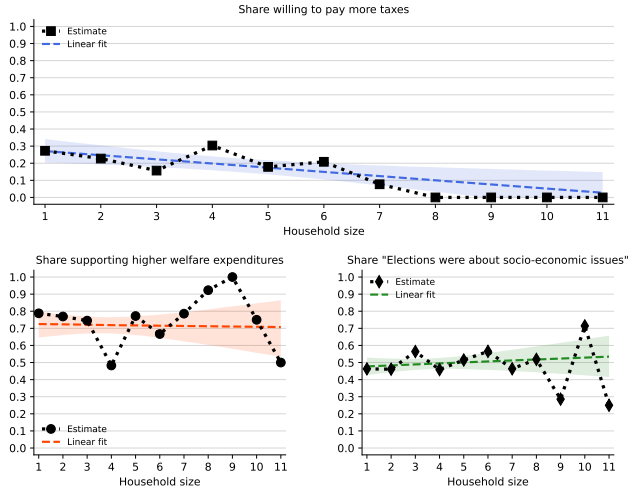
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Summary of results

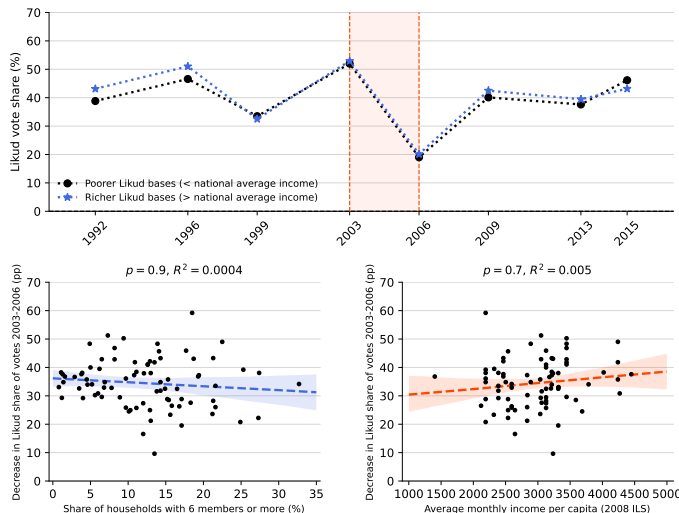


Mechanisms

- No clear relationship between treatment and redistributive preferences



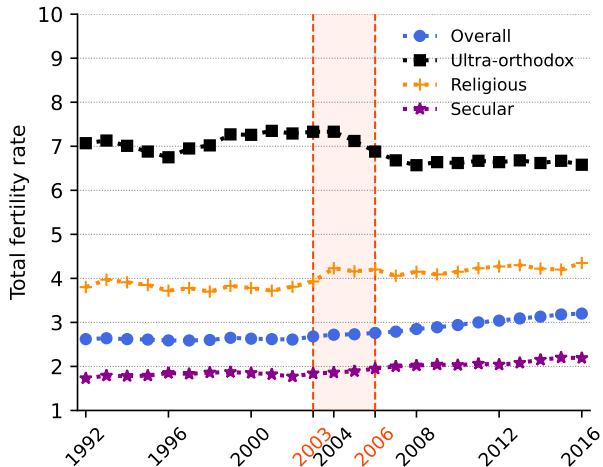
No differential effect in Likud strongholds – indication for identity politics



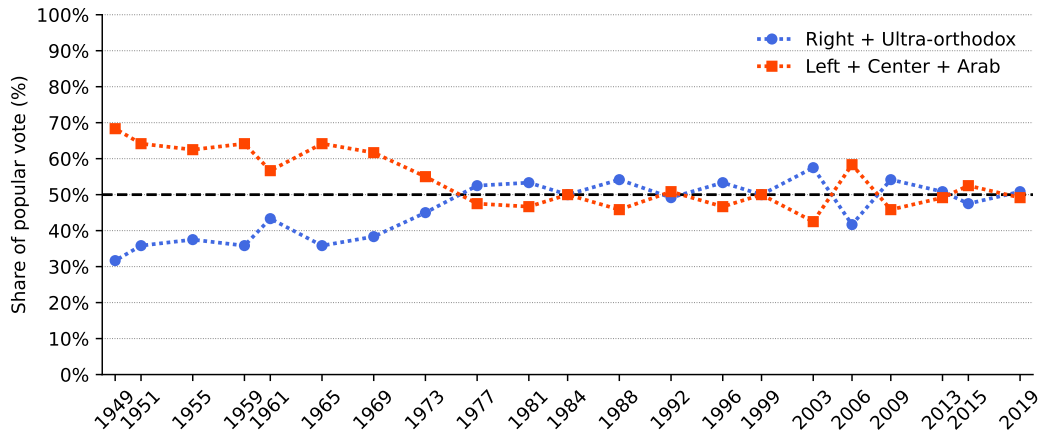
Conclusion

- ▶ Major welfare and tax reforms in Israel in 2003
- ▶ Asymmetry: Small negative electoral effect on negatively affected poorer voters; Large positive effect on positively affected richer voters
- ▶ Significant 'retaliation' occurred only among treated ultra-orthodox voters
- ▶ Identity-based voting may be a leading explanation
- ▶ Other possible explanations:
 - ▶ Lower salience of monetary treatments among poorer voters
 - ▶ Asymmetry between negative and positive treatments (reverse loss aversion)
 - ▶ Difference between taxes and transfers

Limited impact on fertility

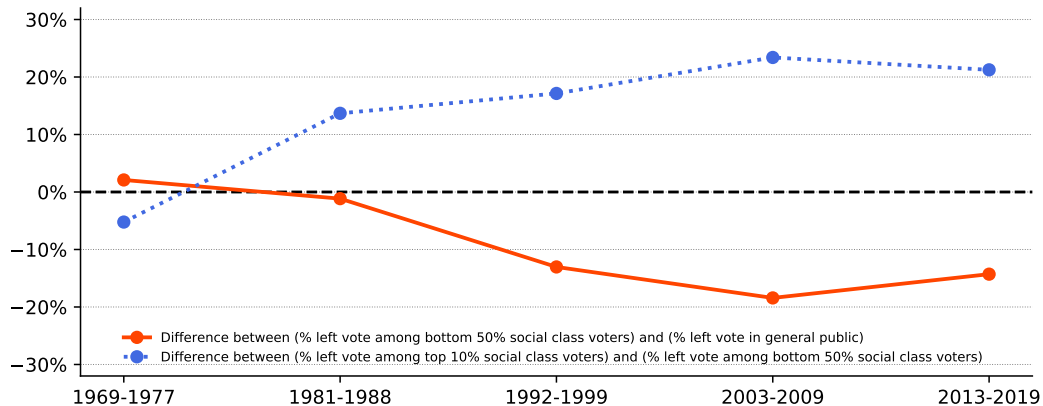


Background: Political blocs



Source: Berman (2020)

Background: Social class cleavage



Source: Berman (2020)