The Electoral Micro-Macroeconomic Cycle: Taking Tufte to the State Level

Introduction

Citizens of democratic governments wield a tool by which they can send a signal to their elected officials. Through voting these citizens can reward elected officials by reelecting them into office, or they may also signal discontent and vote them out of office. This accountability mechanism places emphasis on the performance their representatives. As a result, the politician should respond by attempting to enhance performance, or at least enhance perceived performance in order to win the election. A way to achieve this end is through the provision of public goods. One such public good includes favorable macroeconomic conditions. For example, the president of the United States has the available instruments, like transfer payments, public spending, and tax policies, to try to influence the economy in a positive direction. If he or she can successfully stimulate economic conditions, voters will likely reward the incumbent for their performance.

With that said, attempts to stimulate the economy to capture votes should increase in the months leading up to an election. Scholars and academics have explored this idea and have actually observed this trend of pre-election economic expansions (Tufte 1978; Nordhaus 1975), labeling it the political business cycle. Edward Tufte found a pronounced relationship between presidential election cycles and economic boosts. This is an interesting model that can be pushed further empirically.

In March 2006, Jennifer Granholm the governor of Michigan signed into law an increase in the minimum wage. This legislation was set to take effect October 2006, exactly a month before the gubernatorial election. It could have been altruistic, but the timing is suspect. It is my conjecture that other governors engage in the same sort of opportunistic behavior. Governors have the same incentives as presidents, and Tutfe's political business cycle model should extend empirically onto these sub-national elections.

Literature Review

First, it would be prudent to consider the academic literature on the political business cycle. Scholars have continuously revisited the topic since it was first posited in the 1970s. One of the early pioneers of this theory was Edward Tufte, as mentioned before. In his seminal work *Political Control of the Economy*, Tufte found that out of 27 democratic countries, 19 showed evidence for an electoral-economic cycle (1978). This meant that 19 of 27 countries showed economic acceleration in the months leading up to the election. The United States, in particular, exhibited increased short-run growth in the run up to elections as opposed to drop down in the non-election years for the majority of post-WWII presidencies (Tufte 1978).

As time went on, an alternative theory arose; some academics moved towards the "partisan" theory. Unlike the political business cycle, the partisan theory suggests that different parties will implement policies that appease to their base constituencies. Parties of the left often represent the working class. Thus, they will pursue policies that decrease unemployment since effects of unemployment fall disproportionately on lower income workers (Hibbs 1987). Parties on the right, on the other hand, tend to minimize inflation, because they typically represent the upper income populace.

More support for the political business cycle came in 1995. Improving on the model Kenneth Schultz (1995) observed a pronounced, and at times sizable, trend of expansionary policies in the pre-election months. His improvement included controlling for the political incentives to manipulate at election time, which previous works did not take into account. As a result previous studies displayed a higher level of variance in the data supporting this model; however, controlling this variable revealed robust evidence in favor of Tufte's theory (Schultz 1995).

Douglas Hibbs, a proponent of the partisan theory, even admits to empirical evidence in favor of the political business cycle. He stated that the Reagan administration was a "textbook illustration" of the political business cycle (Hibbs 1987). The two years preceding the election experienced an unprecedented growth in real disposable income and low unemployment. Hibbs conceded that the Nixonian heaping of social security checks just days preceding the election was also clear evidence in support of the political business cycle. Hibbs then goes on to say that none of the assumptions underlying the model is implausible.

These assumptions are consistent throughout the literature, and because of their importance, they are worth addressing. They also allow Tufte's political business cycle theory to map onto sub-national elections empirically. The first assumption is that politicians seek reelection, and an expanding economy prior to the election will increase votes (Tufte 1978). Assuming politicians seek reelection is a very plausible and reasonable assumption. The incumbent is presented with a choice between holding onto their job and losing it. If rational (meaning the benefits of keeping the job are greater than the costs), the incumbent would prefer to keep his or her job. If not, they would not be seeking reelection in the first place, unless the derived benefit from election process trumps the benefit from holding the office itself.

The second part of the first assumption reasons that favorable economic conditions prior to the election will increase ballots cast for the incumbent. This is realistic when evaluating previous literature and empirical studies on voting behavior. When people go to the polls to vote, a myriad of studies have shown them to be retrospective, instead of prospective (forward looking) (Tufte 1975; Fiorina 1981; Kinder and Kiewiet 1979; and Abramowitz et al. 1988). This suggests voters assess candidates based on economic prosperity before the election. If they feel as though they are better off, they reward the incumbent. To summarize, voters prefer candidates whom they expect, based on the incumbent's previous track record, will deliver them greater material well-being, perhaps through better aggregate economic performance. Thus, incumbents have powerful incentives to improve voters' economic fortunes. (Franzese 2002)

Now that the incumbent's motive (Tufte 1978) and the voter's preferences have been established as sound assumptions, it is appropriate to discuss the last assumption. This assumption relies on the government's, mainly the incumbent's, ability to affect macroeconomic outcomes given the institutional constraints of a democracy. The executive branch, the president's administration, has a lot of tools at its disposal to try to positively affect the macroeconomy.

One, the president gives the budget to Congress through executive communication. He or she can increase spending during the election year to help stimulate the desired effect. The president can also speed up the bureaucracy to distribute transfer payments right before the election (as in the case of Nixon). Increasing the amount of transfer payments to individuals is another tool the president can take advantage of with the approval of the legislature. Nixon increased social security benefits to stay in line with inflation prior to the election period. Lastly, the president may appoint the chairman of the federal reserve. The president cannot conduct monetary policy, but appointing a chairman with similar beliefs is beneficial to achieving the president's policy goals.

Empirical Application

Having stated the former, Tufte's political business cycle should be observed on the sub-federal level. Economic expansions should be evident on a state level preceding gubernatorial elections. Governors, like presidents, have the motive to expand their local economies.

One study reinforcing similar incentives for governors and presidents found that presidential voting and gubernatorial to be exclusive. Political Scientists Atkeson and Partin (1995) study showed that when evaluating a governor, the voter is retrospective in judging the governor's performance. The voters cast ballots based on their view of the state's economic condition, independent of the national economic condition. As the chief executive, the governor is seen as responsible for state economic fortune or woes. Their study furnished no evidence in support of the national referendum hypothesis (Atkeson and Partin 1995), or the idea that the gubernatorial election to be a referendum on the president's performance. These findings make it clear that the governor must present favorable macroeconomic conditions to get re-elected. They also discovered that this effect was not seen at the senatorial level. If the senators are of the president's party, depending on the national economic condition, voter's either reward or punish senators based on the president's performance.

A caveat, however, is that it would be hard to argue that the national economy and the state are completely separate. The state economy is inextricably linked to regional economies and the national economy. For example, an expanding national economy (assuming relatively cheap gas prices) could increase the demand for Cadillacs (assuming it is a normal good) from Michigan thereby improving economic conditions in Michigan. While the governor of Michigan had no direct impact on the state's expansion, this study suggests that they are held responsible. Therefore, regional and national economic conditions can without a doubt impact a state's gubernatorial elections, and this indirect effect would be difficult to parse out.

Another aspect allowing for empirical application is that the governors as the executive of their respective states share a similar role to that of the president. Most of the states give governors veto power, power of appointment, and often the governor plays an important role in the creation of the budget. Although the governors cannot engage in monetary policy, these features give the governor ample space and ability to try to effect macroeconomic outcomes. A survey of the state governments conducted by an American political scientist found that governors wield a considerable amount of power over their respective state's agenda (Wright 1967). In fact, this scholar's article found that the governor's office tended to be the dominant branch of state governments. As formerly stated the incumbent governor of Michigan was able to exert her executive power to get an increased minimum wage legislation passed despite a republican controlled legislature leading to the election. The Michigan election came, and she won with an overwhelming majority of the vote. Governors could also pursue policies that include, but are not limited to, increased public spending, expansion of state employment, manipulation of tax policies, increasing the minimum wage, etc.

Methodology and Results

To test this empirical application, it would be appropriate to look at pre- and post-gubernatorial election periods for all of the states (in the post-WWII/Keynesian period of demand management). The benefit of this experiment would be that there are 50 individual democratic states. More data points would give better picture on the existence of the political business cycle as compared to one national presidential race every four years. If the results do find evidence of electoral manipulation, it strengthens Tufte's argument, yet no results definitely weaken his claim.

Tufte posited that changes in real disposable income were a sound indicator of detecting pre-electoral manipulation. Tufte reasoned that positive changes in real disposable income were the desired outcome in pre-election periods for the incumbent. If a relationship existed, he thought there would be clear evidence for the political business cycle. Regressing this measure with pre- and post-elections periods should give the data needed to identify the presence of a trend. A sample equation is as follows:

Changes in Real Disposable Income = $\alpha + \beta$ *(Pre/Post-election period)* + ε

If the empirical application, lending support to Tufte's political business cycle, the *beta* coefficient should positive and the t-score yield a value greater than two for a robust statistical relationship between positive changes in real disposable income and pre-election periods. Conversely, the relationship between post-election periods and no changes (or negative changes) in disposable income should exhibit no relationship or (an inverse relationship); in other words, we should not see increases in real disposable income during non-election phases.

These relationships do not happen in a vacuum, however. There are instances in which the degree of the relationship should be magnified or mitigated depending on several factors. One dynamic to take into consideration is whether the gubernatorial election is synced with the presidential election or not, particularly a presidential election when the incumbent president is seeking re-election. In the states that are synced with the presidential election we would expect the pre-election economic expansion to be greater. The president's opportunistic behavior coupled with the similar behavior of the governor should amplify the short-run economic boost. States with different election years should display some sort of manipulation, but less pronounced since less is at stake on a national level with gubernatorial elections synced with congressional midterm elections; however, the effect should be positive.

Now that real disposable income has been examined, or the potential result of economic tampering, the means to achieve this end needs to be considered. Politicians may not be able to effect real disposable income as desired, but evidence of the attempting to increase disposable income should be present. Thus, policies like public spending and tax policies must be analyzed with election phases. There is an expectation to see a pattern of increasing public spending prior to elections. Increased public employment, social programs, increased public projects, etc would all be good examples. Changes in tax policy are another good way to discover an incumbent's attempt at manipulation. Tufte observed this idea on the national level. He found that increases in taxes did happen after the election and not before (Tufte 1979). State governors, if consistent with Tufte's model, should decrease taxes before the election and increase afterwards.

This effect, however, would vary depending on the composition of the state government. If the governor's office and the legislature are of the same party, the ability to manipulate is greater. Less veto players should increase the magnitude of the political business cycle. On the other hand, a governor and legislature of a different party stripe would minimize the effect. The governor ability to pass legislation slows when a gridlock exists; the legislature is less likely to agree with the opposing party's policies.

In addition, states that give more institutional power (i.e. less oversight by the legislature) should also exhibit a great effect of the political business cycle. For instance, some states allow governors to appoint the heads of agencies without the necessary approval of any other branch. States without these checks allow for governors to appoint officials in lock-step with their own policies. As a result of less institutional veto gates the more room the executive can more quickly and effectively alter policy outcomes that benefit his or her election bid.

Although no tests were conducted given the nature of the assignment, a study in Canada found that sub-national provincial elections did in fact show evidence of opportunistic behavior on behalf of the incumbent (Petry; Imbeau; Crête; Clavet 1999). Most of the provinces exhibit expansions in public spending before elections and spending reductions after the elections. They also found that in the non-election phase partisan differences between candidates surface, meaning that candidates will pursue policies that appeal to their party base. These partisan policies dissolve as the election approaches, and opportunistic policies are pursued. The cycle was found even amid overall government cutbacks in spending. This Canadian study of elections on the sub-national level could shed light on potential results for a future study on state gubernatorial elections and Tufte's model.

Another complement to this application comes from Political Scientist William Clark's book *Capitalism, Not Globalism* (2004). In his book Clark found that with fixed exchange rates, central bank independence, and capital mobility, countries in the European Union exhibit cycles of expansion pre-election. Since the United States is a conglomeration of the 50 independent economies brought together by an economic monetary union, the U.S. is analogous to the European Union. The individual states cannot manipulate monetary policy, making the central bank independent. Brought together under the one currency in the United States also brings a sort of fixed exchange rate among the states. Each state cannot alter the exchange rate regime. Lastly, capital is mobile. Assets can be moved from state to state with great ease. Thus, there similar behavior should be observed in the individual states in the U.S. as the countries of the European Union with regards to political business cycles.

Conclusion

So after the data is analyzed, there should be a clear attempt for governors to influence the economic conditions prior to elections. Governors and presidents share the same incentive, the same tools, and as long as the voters are retrospective, this sort of behavior should reward the incumbent. The assumptions are plausible, and such cycles have been observed on the provincial level in Canada as well as European nations under the constraints of the monetary union. Therefore, Tufte's idea of political business cycles should extend empirically to the American state governments.

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