Partisan views on the economy*

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Abstract. In this paper it is argued that political parties may have incentives to adopt a partisan view on the working of the economic system. Our approach is based on a dynamical spatial voting model in which political parties are policy oriented. This model revolves around two interrelated issues x and y. The policy maker sets x directly. There exist two views on the relationship between x and y. Model uncertainty confronts policy makers with the problem of the selection of a model to base their actions on. We show that if voters have imperfect information about the working of the economic system that model selection contains a strategic element. Policy makers are inclined to adopt a view on the working of the economic system which fits in with their preferences.

There is no inherent logic that places monetarists to the right of New Economists. They have different models of economic mechanism, but they need not have different political values. A conservative can be a Keynesian and a liberal a monetarist. These combinations are in fact surprisingly rare.

1. Introduction

The economic literature offers a large variety of models of the economy. These models often differ in the predictions of the effects of policy variables on target variables. So far, statistical analyses have not been able to show convincingly the superiority of one of the existing models. One could argue that reality is too complex to be captured by a single model. Alternatively, one could argue that a correct model exists, but has not been discovered yet. In any case, at present decision makers are confronted with model uncertainty.

As to economic policy, the presence of model uncertainty raises basically two questions. First, how should policy makers take account of model uncertainty when forming optimal policy? This question has received much attention in the literature. Brainard (1967) shows that uncertainty about the effects of instruments on targets should lead to a conservative use of instruments. Christo-

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doulakis and Van der Ploeg (1987) demonstrate how conflicting views on the same system can be pooled into a compromise model. Once the compromise model has been derived, the policy problem can be formulated as a standard optimisation problem. An alternative treatment of model uncertainty is to assign probabilities to each model being correct. The policy problem then amounts to maximizing a weighted utility function, with the probabilities serving as weights (Frankel and Rockett, 1988; Ghosh and Masson, 1991; and Holtham and Hughes Hallet, 1992).

The second question is how do policy makers actually deal with model uncertainty? This question has hitherto received little attention. There is some consensus that policy makers differ in their views on the economy and that these views are connected with their political preferences (Christodoulakis and Van der Ploeg, 1987). In the U.S., Republicans seem to have more faith in the invisible hand than Democrats and less faith in government intervention (Harris, 1962 and Tufte, 1978). An explanation for this phenomenon is lacking, however, as is expressed by the following quotation:

There is no inherent logic that places monetarists to the right of New Economists. They have different models of economic mechanism, but they need not have different political values. A conservative can be a Keynesian and a liberal a monetarist. These combinations are in fact surprisingly rare (Tobin, 1974:62).

This paper provides a possible explanation for the existence of partisan views on the economy that is based on the need of political parties for selling partisan policies to imperfectly informed voters. We present a model consistent with the notion that political parties differ in their views on the economy. The key elements of the model are adopted from two strands in the economic literature.

First, this paper is related to the rapidly growing literature on partisan models of economic policy. In partisan models, political parties have different preferences over economic goals, because they represent different constituencies (Hibbs, 1977). Wittman (1977, 1983) shows that when election outcomes are uncertain and political parties have different preferences, their policies diverge. The implications of partisan models of economic policy conflict with those of traditional Downsian models which are based on the assumption that political parties solely aim at winning elections. Traditional models predict that the policies of political parties converge. Considerable evidence exists indicating that economic outcomes do differ under different political parties. For the U.S., Beck (1982), Chappell and Keech (1988) and Hibbs (1986) find that unemployment tends to decline under Democratic administrations and that inflation tends to fall when a Republican is in the White House. These findings clearly