

Is it the Economy, Stupid?
Some Economics and Politics of the November 2006 Election

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The frequently cited admonition about the economy and elections (often attributed to former President Bill Clinton) . . . “It’s the economy, stupid!” . . . did not seem to have held true this election cycle. The U.S. economy has been performing quite well over the past few years. Though GDP growth seems to be slowing lately, it grew by over 3 percent in 2004 and 2005 and is likely to finish at over a 3 percent this year. Unemployment has fallen steadily and employment risen over this same time. The stock market is performing well. (See the accompanying chart of recent data on the economy.) Despite this, the Republican Party lost its majorities in both the U.S. House of Representatives and the Senate.

Though the economy matters a lot in elections, I think that *a fundamental reason for the electoral losses of the Republican Party was its inability to distinguish its domestic economic policies from that of the Democratic Party.* At least since the 1980s, the Republican Party has sold itself as the party of smaller government and lower taxes while the Democratic Party has, for the most part, continued to favor a larger government presence in the economy. Yet it has been very difficult to see this distinction in recent years. For example, domestic, non-defense spending has grown rapidly during the years of Republican control of government, filled with pork-barrel, earmarked spending. (For a partial list of the latter, see <http://www.heritage.org/Research/Budget/wm1256.cfm>.) The Republican Party sponsored new Medicare benefits that, if they continue as enacted, promise years of troublesome finances since projected benefits will soon outstrip projected Medicare payroll taxes. The likely outcome is more government involvement in medical markets. The President’s proposal to reform Social Security to save it from a similar fate was met with strong Democratic Party opposition and then was essentially deserted by Republican members of Congress.

This inability of Republicans to exert some control over spending seems quite odd to me. Trying to outdo the Democratic Party on spending is a losing proposition. After all, if the body politic wants bigger government, why not vote for the party that does big government best . . . the Democratic Party?

However, I think that the recent election was not an open-arms embrace of larger government and Democratic Party policies. Voting against the incumbent is an inexact piece of information. It can mean frustration with the incumbent or support for the challenger. I believe that the results of the November election reflect a lot of the former rather than much of the latter. Voting against the incumbent is the only way to signal one’s displeasure clearly, and voters were clearly frustrated with the Republican Congress. I don’t sense overriding voter support for more government in the economy.

Though I maintain that the economic issues raised above were most important in this election, I expect that the war in Iraq played a role, too. The war does not seem to be going well and it's not clear how it will be resolved. Nevertheless, I don't think there is widespread displeasure with the administration's policy of trying to nurture democracy in the Middle East and other parts of the world . . . I suspect it's a policy that most favor (and one that I applaud). However, the implementation of this policy regarding Iraq has been quite problematic.

Now that the Democratic Party has control of both houses of Congress, what are we likely to see and what does it portend for the economy? Two particular issues that have gained attention in the media in this regard are: (i) Democratic Party skepticism regarding open international trade and (ii) suggestions of a military draft by Charles Rangel, incoming chair of the House Ways and Means Committee. Both of these are examples of more government intervention . . . and both are bad for the economy.

Limiting free trade limits individual choice, limits competition, and means that we end up paying more for goods and services. Just like it's a bad idea to grow oranges in Kentucky rather than "import" them from Florida, it's evidently a bad idea to produce toys in the U.S. instead of importing them from China. Despite all the folks who might be employed maintaining greenhouses for orange trees if Kentucky grew oranges, it's simply too expensive and we are better off doing something else and trading with Florida for oranges. The same line of reasoning applies to trading with China for toys . . . they apparently do it at lower cost and we are better off specializing in something else and buying toys from China companies.

Regarding the military draft, it's much better to have those willing to serve rather than those conscripted. Though the budgetary cost of the military is higher under a voluntary force, the true cost to the economy is just as high (if not higher) under a draft. The true cost of the military is the private-sector goods that would have been produced if military personnel were employed as civilians. With a draft, those serving in the military bear most of this cost because they are paid less than their private sector earnings. With a voluntary force, military pay is higher (since pay must compete with the private sector) entailing a larger military budget and more taxes to pay for it. However, the burden is spread over all taxpayers and not just draftees. And, of course, a great benefit of an all-voluntary military is that we don't have to force anyone to join. That ought to matter a lot in a free society.

Frankly, I am somewhat surprised at the play that these issues are getting. I thought that there was a long-standing bipartisan consensus in favor of (mostly) free trade and a voluntary military. Deep down, I think opposing these goes against most people's grain . . . it certainly does mine. My prediction is that policy proposals to restrict trade and impose a draft will not be political winners. That will be good for us . . . and good for the economy.

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