Electoral Studies 33 (2014) 137–143

Contents lists available at ScienceDirect

Electoral Studies

journal homepage: www.elsevier.com/locate/electstud

Do elections bring optimism?

Antonis Adam

University of Ioannina, Department of Economics, P.O. Box 1186, 45110 Ioannina, Greece

ARTICLE INFO

Article history:
Received 19 October 2012
Received in revised form 17 April 2013
Accepted 1 August 2013

Jel classification:
D72
H89

Keywords:
Economic sentiment
Elections

ABSTRACT

The purpose of this paper is to examine the effect of elections on economic sentiment. Using monthly data from 14 EU countries over the 1985–2011 period, we show that there is a significant improvement, statistically and economically, of sentiment of the month that elections take place, but this effect is rather short lived, lasting on average less than two months.

1. Introduction

The idea that shifts in expectations may result into changes in real economic conditions is a hardly a new concept in economics. For example, Pigou (1927) considers these waves of optimism and pessimism as main determinants of economic fluctuations. According to this view, optimism about future economic conditions may lead to economic booms by promoting private consumption and investment spending, even if the underlying fundamentals do not necessarily support this optimism. The question however of what drives the waves of optimism and pessimism has attracted little attention. The usual conjecture is that economic conditions affect the way economic sentiment is formed resulting in feedback from economic expectations to economic conditions and vice versa.

Upon this premise rests a large literature on Vote and Popularity functions as surveyed by Paldam (1981, 2003). On the other hand it has been argued that political evaluations may also be an important determinant of economic sentiment. De Boef and Kellstedt (2004) show that partisan considerations, extraordinary political events and media coverage of the economy are equally relevant when shaping economic expectations as real economic conditions. Similarly Suzuki (1992) has shown that, at least in the US, there appears to exist an electoral cycle in economic sentiment: the public tends to be more optimistic about the future of the economy before the presidential elections.

In this paper we show that favourable expectations about the economy exhibit a discreet improvement at the exact month that elections take place. Following De Boef and Kellstedt (2004) we call this effect the “honeymoon in economic approval ratings”.[1] However, as we show, this honeymoon is rather short lived: any positive effect dies out rather quickly-within the first quarter of the new administration. The evidence presented here rests on a panel dataset of 14 European Union countries over the 1985–2010 period, a period in which 86 elections took place, using monthly data.

The present analysis is related to three strands of literature. Firstly, it draws from the Vote-Popularity Functions literature. According to this view government support is a function of economic and political outcomes (Nannestad and Paldam, 1994). Here however, instead of using the share of votes that the party wins (as in Kramer, 1971; Peltzman, 1990; Fielding, 2000; Lewis-Beck and Nadeau,

E-mail address: aadam@cc.uoi.gr.

[1] De Boef and Kellstedt (2004), p. 647.

0261-3794/$ – see front matter © 2013 Elsevier Ltd. All rights reserved.
http://dx.doi.org/10.1016/j.electstud.2013.08.005

2012) or the popularity in pre-election polls (Hibbs, 1981) we use the general sentiment about the state of the economy as the dependent variable. If voters hold the government responsible for the macroeconomic performance of the country, as the Popularity Functions literature implicitly assumes, positive expectations about the future of the economy are directly translated to positive sentiment for the government.

The present analysis is also consistent with the opportunistic political business cycle literature (Nordhaus, 1975; Lewis-Beck, 1988; Alesina et al., 1997) which shows that before the elections the government manipulates the economy so as to deliver better macroeconomic outcomes and win more votes. For this reason there is a decline in the unemployment rate before the elections, whereas higher inflation and recession will set in afterwards. As long as economic expectations affect economic outcomes, our evidence is consistent with the empirical predictions of the opportunistic political business cycle literature. But in contrast to this view, the causation runs the opposite way: economic sentiment is exogenously improved at the month of the elections, which in turns creates a virtuous cycle in the economy.

Finally this paper is also related to the literature on the determinants of economic voting (MacKuen et al., 1992). The main results on this literature suggest that voters are influenced by politics or sentiments (Norpoth, 1996; De Boef and Kellstedt, 2004). Therefore their opinions can be considered as biased (Easaw, 2010). The most closely related paper to the present one is Suzuki (1992), which identifies a positive electoral effect on economic sentiment. Using economic expectations and quarterly data for the USA over the 1965–1988 period, he shows that there exists a cyclical movement to expectations. Here we extend this analysis by also considering the bias in economic sentiment at the exact timing of elections. We do so by using a more recent dataset (1985–2011) encompassing 14 EU countries. Our evidence suggests that there is no significant cycle in expectations but rather a discreet jump at the timing of elections. Thus the changes in economic sentiment do not coincide exactly with potential policy manipulations through the political cycle.

The main results of the paper can be summarized as follows: first, at the month that elections take place there exists a systematic increase in positive evaluation by economic agents about the future of the economy. This positive effect is quantitatively important as it has the same magnitude as a 1.2% decline in the unemployment rate. Secondly, we find that this effect is rather short lived, lasting less than 2 months, indicating that agents in a very short period of time revise their expectations about the performance of the government. Moreover our empirical results indicate that a potential explanation of this effect is the pre-electoral announcements of the contesting parties for “a fresh start” in the economy: the positive effect of elections on economic sentiment is present only when there is a change in government after the elections. Finally, for the period and countries under examination the evidence presented herein indicates that economic sentiment is affected only by changes in the unemployment rate and not in the inflation rate.

The rest of the paper is organized as follows. The first section describes the theoretical considerations upon which our main argument rests. Section 2 describes the data used and the empirical setup. Section 3, presents the main results, whereas Section 4 presents various sensitivity tests. Finally some conclusions and policy related remarks are in Section 5.

2. Theoretical considerations

Individuals form their expectations about the economy using the available information about the “state of the economy”. Following Fuhrer (1988) this information set will include current developments about the economy, forward looking information (not reflected yet in current economic variables) and “animal spirit” information, i.e. information not tied to economic fundamentals, but make individuals pessimistic or optimistic about the future.

Changes in unemployment and the inflation rate summarize in a general way the current state of the economy. At the same time these two variables appear to be the key indicators of macroeconomic performance in the minds of economic agents: the literature on vote and popularity function suggests that voters base their perceptions about the economy on them (see for example Mueller, 2003, chapter 19). As long as economic sentiment is affected by the current state of the economy it will be directly affected by changes in the unemployment rate and inflation.

Assuming however that individuals base the beliefs only on their current state of the economy and past realizations of economic variables implies that agents are only backward looking and do not try to make predictions about the future. MacKuen et al. (1992) and Erikson et al. (2000) show that agents' economic sentiment about the future respond more to forecasts about the economy rather to the current state of the economy. In their terminology voters behave more like “bankers” rather than “peasants” (MacKuen et al., 1992). Consequently forward looking, rational individuals form their expectations using all available information about the realization of economic variables in the future.

The aforementioned views consider economic sentiment to be determined exclusively by economic fundamentals, either in a backward or forward looking way. However there are instances where the economic literature has shown that economic agents more often than not behave irrationally. For example the finance literature has identified a number of so-called anomalies like the “weekend” effect, the “January” effect (Keim, 1983; Lakonishok and Smidt, 1988) or “electoral period” effects (Vuchelen, 2003; Siokis and Kapopoulos, 2007). The present paper hypothesizes a similar effect: the post-election effect. In the following section we show that economic fundamentals are not the sole determinants of economic sentiment. After elections take place, there is a post electoral optimism manifested in economic sentiment: agents believe the economy is going to perform better in the following months. This optimism however is not based on changes in economic fundamentals.

The post electoral optimism may be present for a variety of reasons. First of all, during electoral campaigns parties