Introduction to the Policy Forum: Economics and populism

Ian M McDonald

University of Melbourne

1. Introduction

The spectre of populism is haunting the Western world. Liberal economic policies, especially free-trade, are on the verge of suffering significant setbacks. Liberal political arrangements, especially a political union which respects individual rights, has already suffered a setback, that is Brexit, and may suffer further setbacks.

A characteristic of populism is the dismissal of the views of experts. Economists are perhaps the most prominent group of 'dismissed experts', partly because of the global financial crisis and partly because they expound a set of clearly defined policy proposals. Political scientists, sociologists and anthropologists are sheltered by the relative vagueness of their conclusions. For example, no question by the Queen has reached the public eye about the failure of experts to predict the civil war in Iraq that followed the intervention in 2003.

The three papers in this policy forum address various aspects of the links between economics and populism. The first paper, by Danielle Wood, John Daley and Carmela Chivers, investigates the causes of populism, in particular the relative importance of economic insecurity and cultural insecurity. The second paper by Max Corden and Ross Garnaut, analyses the economic consequences of the populist economic policies of President Trump. The third paper, by Sinclair Davidson, considers various ways in which political elites may manipulate the acceptance by voters of high tax rates.

This is the author manuscript accepted for publication and has undergone full peer review but has not been through the copyediting, typesetting, pagination and proofreading process, which may lead to differences between this version and the Version of Record. Please cite this article as doi: 10.1111/1467-8462.12293

2. The three papers in this Forum

2.1 Wood, Daley and Chivers assess the relative importance of economic insecurity and cultural insecurity in explaining the rise of populism in Australia. They identify populism with support for the “minor” parties at the expense of the established centre-right and centre-left political parties. They show that voter support for the minor parties has trended upward from something like 5% in 1949 to, in 2016, over 20% for the House of Representatives vote and over 30% for the Senate vote.

They find little correlation between the rise in the minor party vote and economic indicators of wages, income growth, economic optimism, income inequality and wealth inequality. There is some positive correlation with unemployment. However, in spite of the seeming unimportance of the economic indicators in general, they find that minor party voters are more likely to think that Australia has lost from globalisation and tend to be against free trade economic policies.

In keeping with studies in other countries, Wood et al. find that cultural insecurity appears to be a more important explanator of populism. Minor party voters are concerned about protecting the norms and historical narratives of traditional Australia. They take great pride in the Australian way of life. They feel left behind by cultural change. The rhetoric and policies of the minor parties tap into these concerns, such as “Australian made and Australian jobs”, “Australian sovereignty”, “putting Tasmania first” and even “make South Australia great again”.

Also consistent with trends around the developed world, Wood et al find that trust in institutions has been declining in Australia. Particularly worrying is an increase in those “not satisfied with democracy” from less than 20% in 2007 to 40% in 2016. (2007 was a trough-Wood et al wonder whether this trough was explained by a Kevin Rudd factor). Minor party voters are particularly disillusioned with political institutions.

2.2 Corden and Garnaut analyse the economic consequences of President Trump’s major economic initiatives: the cuts in corporate and personal income tax and the increase in barriers against imports. Their analysis is predicated on the assumption that the United States economy is at or close to full employment.

Corden and Garnaut explain how the tax cuts will lead to an increased government budget deficit, an increased trade deficit and increased capital inflow. The latter are associated with an appreciation of the exchange rate. Thus there will be a general tendency for employment in the export trades to decrease. Of course those workers lucky enough to benefit directly from a tariff increase, such as workers in the steel industry, may see some increase in their employment.

The appreciation of the real exchange rate will benefit US consumers in general, albeit tempered by the rise in prices of those goods directly affected by tariff increases. In any event Corden and Garnaut make the important point that these benefits are transitory; capital inflow in the immediate future will have to be offset later by capital outflow to service that inflow. The real exchange rate will depreciate, causing further pressure for structural change. They

suggest that the fall in living standards associated with this offsetting process may be disruptive.

The possibility of an international trade war caused by President Trump's increases in tariffs is particularly worrying. Corden and Garnaut point out that for other countries it is better for their well-being if they desist from retaliating through increasing their tariffs. Tariffs are bad for the well-being of a country's citizens independently what other countries do. It is best to avoid the "beggar thy neighbour" policies that countries resorted to in the 1930s.

2.3 Davidson focuses on the role of ignorance in populism. Because of the cost of acquiring and understanding information, it is rational to be less than fully informed on issues of public policy. Davidson calls this "rational voter ignorance". He goes on to make the important point that in a sea of ignorance there will be plenty of room for various interest groups to float false information and thereby deceive the rationally ignorant voters.

Davidson considers how rationally ignorant voters may be deceived into accepting higher tax rates than they otherwise would. This he argues is through the creation of "fiscal illusion". He *or was it Buchanan?* puts forward a six-fold categorisation of the sources of fiscal illusion: complexity in the tax system; taxing winners; taxing memorable or pleasant events; opportunistic taxation; taxation to avoid dread consequences; taxes with unknown or uncertain economic incidents.

By focusing on deception aimed at increasing tax rates, Davidson's application is unbalanced. Some interest groups create fiscal illusion in order to induce people to only accept lower taxes than they otherwise would. One thinks here of, for example, Tony Abbott labelling the carbon tax as a "great big new tax", having earlier labelled a proposed tax on mining companies as a "great big tax".

Davidson discusses some recent examples of what he considers were efforts to deceive the public.

Just how attempts to deceive work out is very unclear. As Davidson emphasizes, there is a marketplace of ideas in which ideas are contestable. This, I think, suggests that "truth will out". Will it? Perhaps there is no answer to this question? But perhaps the rise of populism describes a fear in people's minds that the public debate is getting less close to the truth than it used to. By dismissing the views of experts, which are presumably members of Davidson's elite, populism may reasonably be expected to contribute to this disturbing trend.

3. A paradox in populism?

The papers in this symposium reveal a paradox in populism. On the one hand, populism is driven more by cultural insecurity than by economic insecurity. But on the other hand, the feelings of populists spill over into economic policy, especially in their opposition to free trade. As Corden and Garnaut show, this opposition is antithetical to the well-being of domestic residents in general and to that of many supporters of populist political parties. In as far as populists are successful in creating barriers to trade, they are not putting 'their own people' first. However, it does not seem to me that rational voter ignorance can explain this confusion. Rather it is a dislike or fear of cultural change.

Minerva Access is the Institutional Repository of The University of Melbourne

Author/s:

McDonald, IM

Title:

Policy Forum: Economics and Populism Introduction

Date:

2018-09-01

Citation:

McDonald, I. M. (2018). Policy Forum: Economics and Populism Introduction. AUSTRALIAN ECONOMIC REVIEW, 51 (3), pp.396-398. <https://doi.org/10.1111/1467-8462.12293>.

Persistent Link:

<http://hdl.handle.net/11343/284432>