

See discussions, stats, and author profiles for this publication at: <https://www.researchgate.net/publication/308530946>

Political Economy. An Introduction to the Theory of Economic Policy

Book · June 2016

CITATIONS

0

READS

51,580

1 author:



[Krzysztof Piech](#)

Lazarski University, Warsaw, Poland

154 PUBLICATIONS 183 CITATIONS

[SEE PROFILE](#)

Some of the authors of this publication are also working on these related projects:



Pozycja innowacyjna Mazowsza na tle innych regionów kraju i Europy [View project](#)



HUMAN CAPITAL
NATIONAL COHESION STRATEGY



EUROPEAN UNION
EUROPEAN
SOCIAL FUND



The publication co-financed by the European Union from the European Social Fund

Political Economy

An Introduction to the Theory of Economic Policy

Krzysztof Piech

Warsaw School of Economics
JUNE 2015

This publication is the result of the project Młodzi projektują zarządzanie co-financed by the European Social Fund within Human Capital Operational Programme, Priority IV "Higher education and science," Measure 4.1 "Strengthening and development of didactic potential of universities and increasing the number of graduates from faculties of key importance for knowledge-based economy," Sub-measure 4.1.1 "Strengthening and development of didactic potential of universities."

Publisher:

Szkoła Główna Handlowa w Warszawie
(SGH)

Reviewer:

Barbara Kryk

First Edition



© Copyright by Szkoła Główna Handlowa w Warszawie (SGH)
al. Niepodległości 162, 02-554 Warszawa, Polska

Free copy

ISBN: 978-83-65416-50-6

Circulation: 200 copies

Cover design:

Monika Trypuz

Typesetting, printing:

Agencja Reklamowa TOP

87-800 Włocławek, ul. Toruńska 148

tel. 54 423 20 40, fax 54 423 20 80

e-mail: agencja.top@agencjatop.pl

It is ideas, not vested interests, which are dangerous for good or evil.

John Maynard Keynes

Contents

Figures	7
Tables.	9
Boxes	10
Preface	11
Chapter 1. What is politics?	13
1.1. Why does politics exist? The origins of politics.	13
1.2. The rights of the state and the rights of individuals	15
1.3. Definitions of politics	19
Chapter 2. Basic concepts of politics and political science.	25
2.1. Development of political science.	25
2.2. Political science within social sciences.	27
2.3. Kinds of states, governments and political systems	31
2.4. Historical evolution of democratic processes	37
2.5. Measuring democracy.	41
Chapter 3. Characteristics of democratic systems	47
3.1. Presidential and parliamentary systems	47
3.2. Legislative assemblies	48
3.3. Electoral market in democracies	53
3.4. Kinds of political parties	55
3.5. Ways of financing the political parties.	57
3.6. Legislative elections	61
3.7. Term limits: populism or effective change?	65
Chapter 4. Politics and social needs	71
4.1. Human needs and economic development	71
4.2. Measurement of development	75
4.3. Public choice theory on beneficiaries of economic policy.	81
4.4. The behaviour of voters	87

Chapter 5. Normative elements of public and economic policy	91
5.1. What is public policy?	91
5.2. Endogenous context of public policymaking	94
5.3. Government, its goals and decisions on policy	97
5.4. Kinds of public policies and relations between them.	102
5.5. Economies and economic policy in social sciences	107
5.6. Relations between political economy, economic policy and economics	110
Chapter 6. Introduction to the positive theory of economic policy	115
6.1. Relations between elections and economic situation.	115
6.2. Economic impact of democracy and its elements	120
6.3. Introduction to the political business cycle	125
6.4. Kinds of political business cycles.	128
6.5. Empirical verification	132
6.6. Central bank independence and macroeconomic results	137
6.7. Partisan central bank hypothesis.	140
References.	143

Figures

Figure 1. 15 countries of the highest value of the Failed States Index, 2012	18
Figure 2. 15 countries of the lowest value of the Failed States Index, 2012.	18
Figure 3. Kinds of human behaviour and sciences describing them	28
Figure 4. Forms of government.	33
Figure 5. Proportion of countries that held legislative elections, 1800-2000.	37
Figure 6. Global trends in armed conflicts, 1946-2011.	38
Figure 7. States experiencing warfare, 1946-2011.	39
Figure 8. Global trends in governance, 1800-2010	40
Figure 9. Eligibility, turnout, and participation, 1815-2000	40
Figure 10. Fully democratic countries, 2014	42
Figure 11. 15 countries of the lowest value of the Democracy Index, 2014	42
Figure 12. Electoral Democracies, 1989-2014.	43
Figure 13. Freedom status, 1972-2014	44
Figure 14. Number of countries with improvements or declines in freedom, 2005-2014 .	44
Figure 15. 10 countries with the highest and the lowest number of parliamentar- ians in Europe, 2014	49
Figure 16. Number of members of upper and lower houses in Europe, 2014	50
Figure 17. Number of members of parliaments in Europe and explanatory variables, 2014. .	51
Figure 18. Population and parliamentary size in 135 countries, 1970	52
Figure 19. Market of electoral votes	53
Figure 20. Promises, accountability, and votes	54
Figure 21. Policy preferences and perception of policy differences between left- and right-wing parties	55
Figure 22. Number of countries where political parties receive direct/indirect public funding, 2014	60
Figure 23. Diagram of Maslow's hierarchy of needs	71
Figure 24. Progress to higher human development groups since 1990.	77
Figure 25. Life expectancy and its changes between 1980 and 2003 in selected countries .	78
Figure 26. Life expectancy and HDI values in 1980 and in 2003 in all the countries	80
Figure 27. The hump-shape hypothesis of Calmfors and Driffill	85
Figure 28. Corruption Perceptions Index 2014	86
Figure 29. Visualisation of framework of public policy analysis	93
Figure 30. Groups of endogenous conditions	94
Figure 31. Structure of governing context	98
Figure 32. Kinds of public policies	103
Figure 33. Branches of science—the place of economics.	107

Figure 34. Branches of economics—German view	108
Figure 35. The democratic policymaking process	113
Figure 36. Optimal size of an electoral budget	117
Figure 37. Unemployment and nationalism in Germany, 1923-1933.	119
Figure 38. From the Great Depression to WWII—sequence of economic and political relations	120
Figure 39. Diagram of possible connections between democracy, the initial con- ditions associated with its emergence, and the consequences of an existent democratic system	121
Figure 40. Proportion of democratic countries on different levels of development, 152 countries, 1951–1999	122
Figure 41. Kinds of political business cycles.	127
Figure 42. Inflation patterns in G7 countries, 1959–1993	133
Figure 43. Selected macroeconomic indicators for Hungary since 1995 with fore- casts up to 2020	135
Figure 44. General government deficit (% of GDP) in Hungary and elections, 1995–2010 .	136
Figure 45. Relation between central bank independence and average inflation, GNP growth and unemployment, 1955–1988	138

Tables

Table 1. Democracy index, 2011 and 2014, by regime type	41
Table 2. Freedom status, 2011 and 2014, by regime type.	43
Table 3. Institutional variation among western democracies	47
Table 4. Probability of fiscal policy run by right, center and left governments in OECD countries	57
Table 5. Top Interest Groups Giving to Members of Congress, 2012 Cycle	58
Table 6. Total general government revenue (% GDP), selected countries, 1995–2014 . . .	83
Table 7. Constitutions and economic policy: Questions and findings	124
Table 8. Influence of change in government to the Left on growth and unemploy- ment, 1966–1996	137

Boxes

Box 1. First articles of the Universal Declaration of Human Rights	16
Box 2. Case study—failed states	17
Box 3. Is the Republic of China a sovereign state?	32
Box 4. Meritocracy in Singapore	35
Box 5. Number of members of parliaments in Europe	51
Box 6. Is the social justice just?	56
Box 7. Groups of interests and public policy: questions for discussion.	59
Box 8. The case of Obama’s campaign	59
Box 9. Financing political parties and public policy—questions for discussion.	61
Box 10. Voting system in Chile	63
Box 11. Selected social and economic human rights	72
Box 12. The ‘Lee thesis’—the case of freedom in Singapore	75
Box 13. HDI formula and other HDI-related indices	76
Box 14. Bhutan—happiness as a public policy ultimate goal	79
Box 15. Unions’ coordination and labour market: Calmfors–Driffill hypothesis	85
Box 16. Penalties for absenters	88
Box 17. “Troll factory” in Putin’s Russia	89
Box 18. Policy goals—objective or partisan?	100
Box 19. Contradictory goals and policy inconsistency—the case of tobacco industry . . .	100
Box 20. Public policy lectures at Harvard	103
Box 21. Weak internal policy as a risk for independence—the case of Poland	104
Box 22. ‘Globalisation with a human face’.	106
Box 23. Theory of economic policy in Germany	108
Box 24. Michał Kalecki—an underappreciated genius of economics.	115
Box 25. Economic situation and election results: the case of unemployment- driven nationalism in Germany.	118
Box 26. Elections and deficits in Hungary.	135
Box 27. Thomas Becket and his change of position on the Church.	141
Box 28. Partisan central bank in Poland?	142

Preface

What is economic policy about? Is this about having influence and power? Or is this about being a servant to the sovereign and to use all the wisdom to bring people welfare? What are the economic and social policies about?

In this book, we will introduce the readers to the concepts of social and economic policies. However, first we have to clarify a few important issues. Economic and social policies should be regarded as a part of a broader policymaking process. Thus, the essential objective is to make the reader familiar with public policy and even with politics. Only then, we would be able to understand economic and social policies. That is why this book is so much focused on political economy, before it takes the reader to the issues of the theory of economic policy. The book fits within a reactivated in mid-1980s trend of political economy as a crucial prerequisite enabling explanation of economic policy.

There are also other novelties of this book compared to others. It combines authors' experience as an independent expert advising governmental agencies and sometimes the political parties; it also includes part of his teaching experience in delivering economic policy, development economics, and behavioural economics to international students. Moreover, it tries to link German contribution to the theory of economic policy with the dominating approach presented in English textbooks and papers, as well as include some of his Singaporean hands-on experience.

All your comments, dear readers of this first edition of the book, are very welcome. If you have any doubts or if you think, the book could be improved, please can contact the author via e-mail: kpiech@sgh.waw.pl.

Last, but not least, I would like to express my gratitude to my students, who were the first readers of this book and sometimes very critical commentators of it. Among several persons, I would especially like to thank Karolina Demiańczuk, Madlen Karanović, Jasmina Kasperkiewicz, Łukasz Michałowski, Jakub Rogowski, Agnieszka Tekieli, Dorota Wiśniewska, and Ewelina Wojtal.

Warsaw, June 2015

Chapter 1

What is politics?

This chapter introduces the reader to the basic concepts of politics: its justification, obligations towards people and definitions.

1.1. Why does politics exist? The origins of politics

Politics is usually associated with the state. Plato in ancient Greece was the first philosopher who first started to treat politics as a science. For him, the most important concepts were justice and the state. Everything that leads to the improvement of the condition of a state is desired. This point of view has later influenced other thinkers.

The state has its roots in small communities in ancient times. Let us quote:

When several villages are united in a single complete community, large enough to be nearly or quite self-sufficing, the state comes into existence (...). And therefore, if the earlier forms of society are natural, so is the state, for it is the end of them, and the nature of a thing is its end. For what each thing is when fully developed, we call its nature, whether we are speaking of a man, a horse, or a family. (...) Hence it is evident that the state is a creation of nature, and that man is by nature a political animal.

(Aristotle)

We see that the state is a “natural” form, and people have a nature of a “political animal”. Therefore, there is no doubt that some people may become politicians, which should also be regarded as a “natural” thing. Moreover, people’s interest in politics should be “natural”, as well, because it creates a civil society and preserves democracy. Thus, all of us are part-time politicians:

Politics ought to be the part-time profession of every citizen who would protect the rights and privileges of free people and who would preserve what is good and fruitful in our national heritage.

Dwight D. Eisenhower (1964)

Moreover, everyone should engage in politics:

One of the penalties for refusing to participate in politics is that you end up being governed by your inferiors.—Plato

As Aristotle further argues, **the state is superior to the individual:**

The proof that the state is a creation of nature and prior to the individual is that the individual, when isolated, is not self-sufficing; and therefore he is like a part in relation to the whole. But he who is unable to live in society, or who has no need because he is sufficient for himself, must be either a beast or a god: he is no part of a state.

(Aristotle)

That explains why the state has the power to limit rights of an individual. We see a very simple logic behind these words. We may even say that this is a “natural” trait.

For man, when perfected, is the best of animals, but, when separated from law and justice, he is the worst of all; since armed injustice is the more dangerous, and he is equipped at birth with arms, meant to be used by intelligence and virtue, which he may use for the worst ends. Wherefore, if he have not virtue, he is the most unholy and the most savage of animals, and the most full of lust and gluttony. But justice is the bond of men in states, for the administration of justice, which is the determination of what is just, is the principle of order in political society.

(Aristotle)

Through the legal system, the state institutions protect people against the improper conduct of certain individuals. Which is also a “natural” task for the state. From this point of view, politics is not something harmful, or wrong, as it is often seen by the public. **Politics is**—as Aristotle thought—a kind of **art**. It is not always easy to conduct; it is not always carried out by the right people. However, in its very essence, people need the state and its institutions to eliminate their inherent weaknesses. Therefore, there has to be a state. Thus, there is politics.

One can wonder why we start from Aristotle since there are so many ideas that are more recent and so many powerful thinkers who live in our times. However, it is not only about knowledge. Our predecessors created core values of what we think today. Here we talk about evolution of institutions influenced by ideas (and their advocacies). They may be very powerful and despite of the fact that freedom may be suppressed during many years, it eventually wins:

He who puts out his hand to stop the wheel of history will have his fingers crushed.

Lech Wałęsa

Unfortunately, some of the values, are forgotten, if they are contrary to the common convictions or are not expressed clearly enough. Even two millennia ago Aristotle wrote:

Others affirm that the rule of a master over slaves is contrary to nature, and that the distinction between slave and freeman exists by law only, and not by nature; and being an interference with nature is therefore unjust.

(Aristotle)

He expressed his doubts whether slavery was justified. He, however, did not point out exactly that it was unfair. It took humankind about two thousand years to finally admit that slavery is a mistake. The evolution of sciences shows us also many examples of such disappearing knowledge, when after decades it had to be reinvented. We may think that we have made such a big progress since ancient times and our civilisation has advanced. However, when we speak about core values, about “right” and “wrong”, we can see that we have not changed much. Some people are still breaching the legal and moral norms; they have not disappeared, and there are still wars in the world. This is another argument supporting the view that the state with all its institutions, if we like them or not, is crucial.

Aristotle influenced many thinkers in the next centuries. He showed sympathies for democracy that were recalled even hundreds years later (he also appreciated a kind of ‘enlightened’ monarchy). In addition, he could be enumerated among the “grandfathers” of political science.

1.2. The rights of the state and the rights of individuals

Many concepts show that the rights of the state are not more important than the “natural” rights of people. We can recall the concept of the so-called human rights¹, which take precedence over the rights of states.

¹ On 10 December 1948, the Universal Declaration of Human Rights was adopted by the United Nations.

Box 1. First articles of the Universal Declaration of Human Rights

Article 1. All human beings are born free and equal in dignity and rights. They are endowed with reason and conscience and should act towards one another in a spirit of brotherhood.

Article 2. Everyone is entitled to all the rights and freedoms set forth in this Declaration, without distinction of any kind, such as race, colour, sex, language, religion, political or other opinion, national or social origin, property, birth or other status. Furthermore, no distinction shall be made on the basis of the political, jurisdictional or international status of the country or territory to which a person belongs, whether it be independent, trust, non-self-governing or under any other limitation of sovereignty.

Article 3. Everyone has the right to life, liberty and security of person.

Article 4. No one shall be held in slavery or servitude; slavery and the slave trade shall be prohibited in all their forms.

Article 5. No one shall be subjected to torture or to cruel, inhuman or degrading treatment or punishment.

Article 6. Everyone has the right to recognition everywhere as a person before the law.

Article 7. All are equal before the law and are entitled without any discrimination to equal protection of the law...

(United Nations, 1948)

This concept has influenced the United Nations to adopt a stance that it is an obligation to other nations to provide “humanitarian intervention”, when human rights are violated. This was initiated by the Secretary-General of the UN Kofi Annan in 1999, who—after the genocide in Rwanda and ethnic cleansing in Bosnia—said during the General Assembly:

No government has the right to hide behind national sovereignty in order to violate human rights.

Kofi Annan

These words were rooted in earlier processes and civilizational changes. The first step towards the protection of civil citizens on occupied territories was the Geneva Convention signed in 1964. The World War II and the Holocaust showed the need for further steps towards the protection of people against the state. The UN Charter and the UN Declaration of Human Rights were the first solutions to these needs obliging the states to protect individual rights. However, the UN could not intervene, because the domestic jurisdiction was regarded as more important than human rights. This was the idea of “sovereignty”, a major

concept of politics during the “Peace of Westphalia”². The contemporary system of states is also called “The Westphalian System”. It is based on three following key principles:

- The **principle of sovereignty** of states and the fundamental right of political self-determination.
- The **principle of legal equality** between states.
- The **principle of non-intervention** of one state in the internal affairs of another state.

The rules mentioned above have significant impact on contemporary international relations.

The concept of ‘**Westphalian sovereignty**’ states that a country is sovereign on its territory from foreign influence and interfering. It means that no foreign government, king, or emperor (like the Habsburgs’ family in those times) has a right to influence other nations’ domestic affairs. Thanks to this assumption it was (and is) believed that there are fewer wars in Europe, because the rights of different countries were clarified and limited to their territories.

The situation has changed after the end of the “cold war”, when some countries lost their powerful protectors and the idea of the so-called “failed states” emerged.

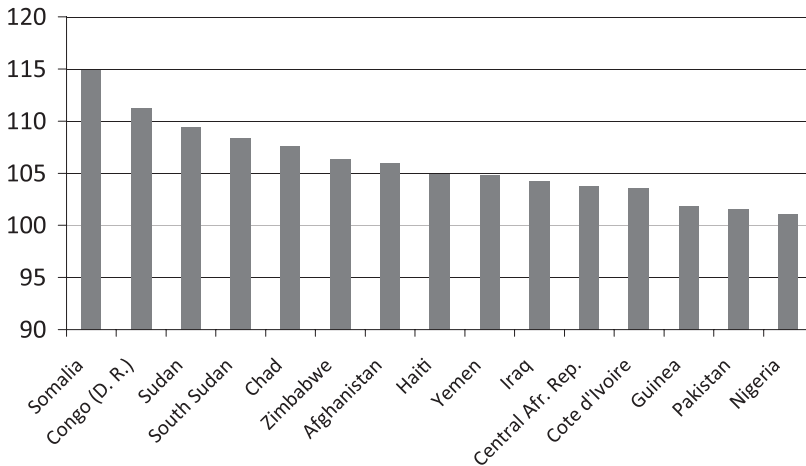
Box 2. Case study—failed states

The Fund for Peace and the “Foreign Policy” publish annually the ranking of the ‘Failed States Index’. Despite there is no formal definition of such a state, it is accepted that governments of such countries are so weak that they fail to deliver their basic responsibilities to citizens like public services, they have serious problems with corruption, criminality, refugees, economic growth. It is judged based on 12 social, economic, and political indicators. The examples of such countries are Somalia, Chad, Sudan, Democratic Republic of the Congo, Haiti, Zimbabwe, and Afghanistan. The ranking based on three groups of 12 indicators, namely:

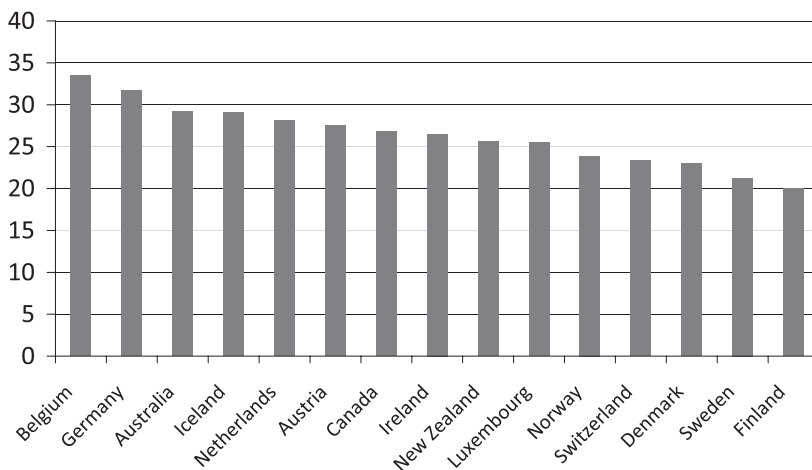
- Social indicators: demographic pressures, massive movement of refugees and internally displaced peoples, legacy of vengeance-seeking group grievance, chronic and sustained human flight;
- Economic indicators: uneven economic development along group lines, sharp and/or severe economic decline;
- Political indicators: criminalization and/or delegitimation of the state, progressive deterioration of public services, widespread violation of human rights, security apparatus as “state within a state”, rise of factionalised elites, intervention of other states or external factors.

Some of the results are presented below.

² Treaties signed in 1648 have ended the Thirty Years War (1618-1648) between Spain and the Dutch Republic. They are recognised as the basis for constitutional law of the Holy Roman Empire and further for general international law.

Figure 1. 15 countries of the highest value of the Failed States Index, 2012

Source: (Fund for Peace, 2012).

Figure 2. 15 countries of the lowest value of the Failed States Index, 2012

Source: (Fund for Peace, 2012).

The idea of humanitarian intervention was popularized in the late 1980s by Bernard Kouchner as a concept of *droit d'ingérence* (right of intervention). This idea was verified in practice in Kosovo and Haiti. The international pressure also convinced the Indonesian government in 1999 to accept the peacekeeping forces in East Timor (Timor-Leste) (Traub, 2009). Finally, during the UN General Assembly in 2005, the UN members have decided that:

Each individual State has the responsibility to protect its populations from genocide, war crimes, ethnic cleansing and crimes against humanity. (...) The international community, through the United Nations, also has the responsibility to use appropriate diplomatic, humanitarian and other peaceful means, (...) to help protect populations from genocide, war crimes, ethnic cleansing and crimes against humanity. In this context, we are prepared to take collective action, in a timely and decisive manner (...), should peaceful means be inadequate and national authorities manifestly fail to protect their populations....

(United Nations, 2005 p. 31)

This initiative is called the “**responsibility to protect**” (or R2P in brief). Sovereignty is not a right but a responsibility to protect its population from mass atrocities and ethnic cleansing. Moreover, the international community is responsible for helping to fulfil it. An example is the UN Security Council resolution in 2011 demanding ceasefire in Libya to protect civilians and the NATO military action following it.

If we consider legal grounds of these actions, we can take a closer look at the Chapter VII of the Charter of the United Nations. It allows the Security Council to take action in situations, where there is a “threat to the peace, breach of the peace, or act of aggression”. Opponents of this proposition however make use of another argument from this Charter:

nothing should authorize intervention in matters essentially within the domestic jurisdiction of any state.

As we can observe, it comes almost directly from the Westphalian sovereignty concept.

The R2P is not binding for every country. The U.S. has withdrawn from the International Criminal Court making sure that their actions will not be judged by any external court. The decisions of interventions are questionable in cases when the UN Security Council members’ interests are affected, such as the case of Chechnya.

Such **double standards** as well as domination of the West in international institutions (like IMF, World Bank, G7, and UN Security Council) may lead to “De-Westernisation”, by which e.g. India and China have disencumbered of Western influence. They create new institutions unknown in the West, and other Asian nations follow them (Mahbubani, 2008).

1.3. Definitions of politics

As many words in contemporary languages, the term “politics” stems from ancient Greek. This word has its origins in the word *politikos*, which means “of, for, or relating to citizens”. In Aristotle’s books, “politics” had the meaning of “affairs of the city”, as the city was commonly a state at those times.

Usually, when we want to define a notion that is relatively well-known, we can find many definitions, as this is the case with politics. We can distinguish between the following groups of meanings of the word “politics”:

- **the art (and science) of government** (Aristotelian meaning), i.e. politics is what the politicians (governments, kings etc.) do in terms of governance (management of a country and other political units); it is also a science of studying this practice (called political science);

Politics is war without bloodshed while war is politics with bloodshed.

Mao Tse-Tung

Politics, it is this: have a vision and act to realize it.

Françoise Giroud

- **acquisition of power** and keeping it, once it is gained;

Government is not reason; it is not eloquent; it is force. Like fire, it is a dangerous servant and a fearful master.

George Washington

The United States brags about its political system, but the President says one thing during the election, something else when he takes office, something else at midterm and something else when he leaves.

Deng Xiaoping

- **public affairs**, what means that politics is not only about governing itself, but is connected with many public matters (in contrast to the private ones, which are non-political),

Just because you do not take an interest in politics doesn't mean politics won't take an interest in you.

Pericles

- **compromise and consensus** among social groups; politics is a kind of the art of choice, of making decisions; there are many conflicts in public affairs and it is not possible to give everyone what he/she wants, especially when different social groups have different needs; hence, political skills are required;

All government, indeed every human benefit and enjoyment, every virtue, and every prudent act, is founded on compromise and barter.

Edmund Burke

No party has a monopoly on wisdom. No democracy works without compromise.

Barack Obama

- **the art of completing one's goals**, what is connected with power and distribution of resources. In this sense we can speak about politics, whenever we deal with influence of somebody over somebody else with some (limited) resources; then, the politics is the ability to achieve the desired goals with usually scarce resources (that implies the abilities of solution of conflicts within the society).

Pure politics is merely the calculus of combinations and of chances.

Napoleon Bonaparte

Congress, the press, and the bureaucracy too often focus on how much money or effort is spent, rather than whether the money or effort actually achieves the announced goal.

Donald Rumsfeld

The different meanings of politics, divided into specific groups, show that the notion of politics may be much more complicated in comparison to the general knowledge of many people. Sometimes they concentrate on the second meaning while thinking about politicians and their goals. However, some politicians do believe that they are servants to the society.

President means chief servant.

Mahatma Gandhi

In order to become the master, the politician poses as the servant.

Charles de Gaulle

I stand here before you not as a prophet, but as a humble servant of you, the people.

Nelson Mandela

One of the most frequently quoted definitions of politics is the following one:

Politics is who gets what, when, and how. (Lasswell, 1936)

In this sense, politics is about the influence and distribution.

In spite of the fact that there are many books on politics, it is difficult to find a single, universally accepted definition of politics. The one quoted above is sometimes regarded as a 'classic' one.

We may not attempt to elaborate such a single definition. However, in order to understand what the public policy is about, we need to have a clear vision of it. Moreover, as we can

see, politics is not only the notion that is commonly understood as politics. Having that in mind, we can say that **politics is a public decision-making process and execution of power concerning scarce resources in order to achieve the assumed goals in the world of conflicts of interests.**

We do not speak about politics as an unintended behaviour: the goals are extremely important (even if they are not officially expressed). Moreover, the goal can be, as Aristotle thought, a 'common good'. What also happens often is that politicians maximise their own utility. From this point of view, politics can aim at acquiring the power and holding it. However, we cannot speak of politics in every situation. If we had subordinates that always do what the boss tells them to do, we could not say that it is politics. To say so we need a condition that the entity undertaking politics is limited by others with the same goals, who are not subordinate to that individual:

Hence, we have two broad goals and meanings of politics:

- **altruistic**—when politicians aim at achieving 'common good',
- **selfish**—when they concentrate on their own interests.

These two meanings are also important when we speak about public policies.

Politics, when it is an art and a service, not an exploitation, is about acting for an ideal through realities.

Charles de Gaulle

We should also remember that politics is not limited to government, political parties, and the politicians only. It is universal and can be found in enterprises, trade unions, families, at universities etc. In many aspects of everyday life (even at academia and in the world of science), we can find the examples of the struggle for power and influence, we can find conflicts due to scarce resources, as well as trials of reconciliation, resolution and consensus. Politics can be found not only on the very high, (inter)national level.

Of course, there are critics that say that one does not have to be well-educated or have any special skills to become a politician. It is an exaggeration: you can be an excellent businessperson or just a petty money-maker; you can be a good politician with abilities to solve problems and make difficult decisions or you can be a ruler that wants to maximise only his or her own utility. Thus, in the interests of all of us is the situation, when we have really good politicians... They do not have to be university professors or influential intellectualists. Other skills are even more required to run good politics. However, it is not enough to win elections to prove that someone is a good politician:

In politics we presume that everyone who knows how to get votes knows how to administer a city or a state. When we are ill we do not ask for the handsomest physician, or the most eloquent one.

Plato

I have come to the conclusion that politics are too serious a matter to be left to the politicians.

Charles de Gaulle

That is also why studying public policy is important (and this discipline, if well-analysed, is not trivial) not only to be a good policymaker in e.g. economic and social spheres, but first of all to be able to judge:

- if the policies that are run are correct or not?
- if the politicians may succeed or rather not (and what to do then?),
- who will be the biggest winner of the policies and who will be a loser?

From this mixed perspective, we cannot say that politics is simple. Thus, its description by scholars is also complex. Political science nowadays covers areas such as:

- constitutional analysis,
- comparative politics,
- foreign affairs and international relations,
- political economy,
- public administration,
- public sector management,
- voting behaviour.

We see that there are quite many of them and that these disciplines may cover wide areas of problems.

Chapter 2

Basic concepts of politics and political science

Below the basic concepts of politics will be presented. They will be used in subsequent chapters.

2.1. Development of political science

Political theory is a science that deals with politics. Long time ago it was called political philosophy, because (similarly to economics) it was done by philosophers. It separated from other social sciences quite late (in comparison to others). Today, **political science divides into:**

- political philosophy (political theory),
- comparative politics and
- international relations.

Political science has a long history, which starts from **Plato** and his “Republic” and “Laws”. One of the members of the Plato’s Academy was Aristotle, who is called a “father of political science”. While Plato and **Aristotle** were generalising about the Greek world, **Polybius** used their ideas in the context of Rome, explaining its growth by political institutions. They consisted of a mixture of different kinds of governments: monarchy, aristocracy, democracy. Later, **Cicero** developed a doctrine of ‘universal natural law’ that results from divine order of the cosmos. It had an important impact on Roman law, on Christian doctrine, and ultimately on the Enlightenment movement.

There were many other thinkers and philosophers who contributed to political science. For instance:

- in the Middle Ages **Saint Thomas Aquinas** (the idea of power comes from God but states are the creation of people);
- during Renaissance **Niccolò Machiavelli** (“Politics has no relation to morals”);
- during Protestant Reformation **Jean Bodin** (he first used the term “political science” and contributed to the theory of sovereignty that was confirmed by the “Peace of Westphalia”);
- during the Enlightenment:

- » **Thomas Hobbes** (who created the theory of the social contract, according to which a strong central power was necessary to compromise the selfishness of individuals),
- » **John Locke** (who did not agree with Hobbes and Machiavelli and because all people are born with a mind as *tabula rasa*, it is natural that they seek not absolute rulers but peace and equality),
- » **Montesquieu** (who introduced the concept of separation of powers among a legislature, an executive, and a judiciary)³,
- » **David Hume** (who did not concentrate on a form of government but underlined a rule of law and its fairness);
- Founding Fathers of the United States, who were main authors of the Federalist Papers that promoted the ratification of the U.S. Constitution:
 - » **James Madison** (the fourth president of the United States, “Father of the Constitution” contributed the first ten amendments due to which he is called the “Father of the Bill of Rights” that were to protect the natural rights of liberty and property and to protect an individual from the tyranny of the majority);
 - » **Alexander Hamilton** (created the first national bank of the U.S., influenced Bismarck’s administration, Meiji reforms in Japan);
- in the 19th century Germany, within Leninism, which significantly influenced politics in the 20th century:
 - » **Karl Marx** (one of the architects of modern social science (with Émile Durkheim, and Max Weber), according to whom the class struggle will finally lead to the emergence of the new socioeconomic system called socialism, under which the power will be held not by bourgeoisie but by the proletariat, which will be replaced by communism, where there will not be any classes of society),
 - » and his co-author of “The Communist Manifesto” and co-father of Marxist theory Friedrich Engels.

In the 1960s, after the publication of a provocative paper entitled “Does Political Theory Still Exist?” (Berlin, 1962), where it was claimed that **there were no major books on political theory in the 20th century**, and that ‘political theory would never become a science’ (Grant, 2004 p. 174), some were not sure of its existence. There was a **decline** of Anglo-American literature on **political theory** (with some exceptions such as Hannah Arendt, Karl Popper, Friedrich Hayek, Isaiah Berlin), but it still developed in continental Europe (with e.g. Jean-Paul Sartre), being influenced by Marxism.

Several years later, the political theory ‘was **reborn**’ (Moon, 2004 p. 12). It was due to the influential book “A Theory of Justice” (Rawls, 1971), where the author **John Rawls** tried to reconcile liberty and equality. He established two principles of justice:

³ This system is widely adopted, e.g. in the U.S., in EU and so on. However, in its original form it is too simplistic nowadays, because we should include some groups of interests like e.g. trade unions, political parties, mass media, lobbyists, religious organisations, or whistle-blowers.

- **the liberty principle**, according to which citizens have basic liberties (to vote, run for office, liberty of speech and assembly, of conscience, of personal property, freedom from arbitrary arrest);
- **the difference principle**, when the benefits from social contracts should mostly be derived by the least-advantaged members of society.

The book was widely commented (and criticised, e.g. by Robert Nozick⁴). Since then, interests with theory of politics significantly increased.

Political theory, during the last two decades of the 20th century, developed in directions of:

- social justice and welfare rights theory (starting from the work of Rawles, 1971 including the studies by Sen, 1992);
- democratic theory;
- feminist political theory;
- postmodernism;
- new social movements and civil society; and
- the liberalism-communitarianism debate (Young, 1998 p. 481).

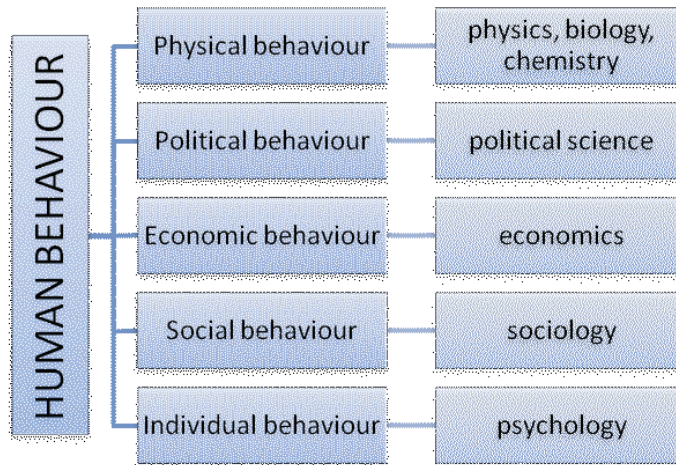
The Rawlsian issues of equality and freedom were also studied by Amartya Sen, who argued that because people have different needs and are in different situations, the notion of equal rights, liberties, or distribution of resources is too simplified. It is not true that “all men are born equal” because they differ in abilities and skills, gender, tastes and preferences, material and social status etc. The approach to giving everybody equal rights will sustain the inequalities and in order to achieve the equally desirable life prospects, one should apply unequal means. Therefore, people should concentrate on individual capabilities and freedom to achieve objectives (Sen, 1992).

We should also notice Jürgen **Habermas**, who pioneered the concepts of public sphere and communicative action. He was one of the contributors to the **theory of deliberative democracy**, which joins the consensus decision-making (like in a direct democracy) and the majority rule (traditional, representative democracy). It says that simple voting is not enough for democracy but authentic deliberation.

2.2. Political science within social sciences

Social sciences deal with human behaviour, and political behaviour is one of its aspects. From this perspective, science that describes political behaviour can be named as political science.

⁴ He challenged the Rawls's Second Principle of Justice asking, why well-off should be obliged to assist the worse-off and their property rights should be limited when their welfare was gathered without violating any others' rights, and why worse-off should not accept inequality and the benefit of the well-off.

Figure 3. Kinds of human behaviour and sciences describing them

Note: some of the disciplines enumerated above are interrelated (e.g., when psychology explains economic behaviour we speak about behavioural economics).

Political behaviour describes a process when people are engaged in the acts involving authority (and politics in particular). The examples range from disobedience to the teacher at school questioning his/her authority, to voting (decision of not participating in voting is also a political behaviour), demonstrating, striking, taking decisions in government, parliament etc.

2.2.1. Remarks on methodology of political theory

Development of political theory is reflected e.g. in existence of many university departments dealing with these issues. However:

The practical problem is that political theorists do humanistic research in a social science discipline.

(Grant, 2004 p. 174)

Public policy probably also conducts rather humanistic research, although when it applies to social and economic policy, the methods of social science are usually used. Contemporary political science is

too method driven and not sufficiently problem driven

(Shapiro, 2004 p. 194)

and one can see the

tendency for empirical political theory to become banal and method driven—detached from the great questions of the day and focused instead on what seems methodologically most tractable.

(Shapiro, 2004 p. 194)

As a result, the papers and books on political theory concentrate more on description of facts and on methodological correctness than on the real research problems. One could see a large difference while comparing the papers on e.g. economic policy with the ones on politics, when especially the contributions on monetary policy are frequently based on solid empirical research. If we look at economic policy, and further on social policy, they are more descriptive than problem focused. However, the papers on politics vary even more. It is more difficult to find the arguments in papers on politics than in papers on e.g. monetary policy. Moreover, it is both the matter of data and methods applied, but also of the attitude of scientists and their abilities (e.g. knowledge of the quantitative methods). Even willingness to focus the research on empirics has a significant meaning.

Political science has developed in many areas. Its main features are:

specialization, fragmentation and hybridization. Its frontiers are open and moving and need not be defined.

(Dogan, 1998 p. 97)

It hybridizes fragments of different sciences, borrowing from **neighbouring disciplines**, such as sociology, psychology, economics, philosophy, anthropology, theology, journalism, and politics (Dogan, 1998 p. 103).

2.2.2. Remarks on methodology of economics

However, economics has separated from other social disciplines in its quest for a mathematical precision that e.g. physics had, despite the view of Friedrich A. Hayek:

But nobody can be a great economist who is only an economist—and I am even tempted to add that the economist who is only an economist is likely to become a nuisance if not a positive danger.

(von Hayek, 1956 p. 463)

Together with Gunnar Myrdal, they began from contributions in pure economic theory...

But thereafter both Myrdal and Hayek greatly extended their range in order to deal with problems which cannot be studied only within a narrow economic framework.

(...) Thus, after their work in central economic theory, Professors Myrdal and Hayek have carried out important interdisciplinary research. The Royal Swedish Academy of Sciences has therefore decided to award the Prize in Economic Science in Memory of Alfred Nobel for 1974 (...) "for their penetrating analysis of the interdependence of economic, social and institutional phenomena".

(Lundberg, 1974)

This was rather an exception than a universal trend in economics. Many other authors still rely on formal theories using the methods borrowed from mathematics and physics rather than looking at other social sciences. In result:

the recent history of the social sciences shows that enormous areas of scientific knowledge have been abandoned by the science of economics. (...) it chose to remain unflinchingly pure, true to itself, thereby forfeiting vast territories. (...) Those abandoned lands now have their own flags: management, political economy, development science, the comparative study of Third World countries, economic and social history.

(Dogan, 1998 p. 115)

Indeed we can recognise between orthodox, mainstream economics and the rest—heterodox concepts that are rather on peripheries of interests of most of economics. Moreover:

- **over 50% of articles** published in one of the most prestigious journals of economics "American Economic Review" in 1972-1981 **were the models with no empirical data**,
- 15% contained nonmathematical theoretical analysis, and
- only 35% included empirical analysis (Leontieff, 1982).

As (Morgan, 1988) put it, the number of articles that did not use any data was greater than in journals of physics and chemistry.

However, the situation has started to change. **Development economics**, although separated from growth theories in the 1950s/1960s, have attracted more scientists trying to discover solutions to the Third World countries. Economic history, with the works of e.g. Kindleberger, Landes, Carmen and Rogoff, Rodrik, is now becoming a fundament of economics. However, there is still a long way to go to shift from formal models that are visible in textbooks to the real life ideas. Moreover, we should also appreciate the works of Olson, Alesina and many others, who bridged the gap between politics and economics. Contributions of North, Williamson, and Ostrom were important to the research of **influence of institutions** on economic behaviour. Finally, **behavioural economics** (with its borrowing from psychology, and very recently even from neuroscience), has a tremendous effect on rational expectation's-based economics.

As Mark Blaug has pointed out:

What after all is wrong with elegant economics practiced as an intellectual pastime? (...) economics throughout its long history has been intimately connected with

economic policy, with the desire to improve economic affairs, eradicate poverty, equalize the distribution of income and wealth, combat depressions, and so on, and never more so than in the recent postwar period. But if economists are going to take a stand on questions of economic policy, not to mention advising governments what to do, they must have knowledge of how the economic system functions. (...) All this is to say that economics must be first and foremost an empirical science or else it must abandon its age-old concern with »piecemeal social engineering«.

(Blaug, 1992 pp. xxii-xxiii)

Blaug calls for economics as an empirical science that is based on the purely theoretical concepts. Anyway, it took economics a few decades of trials and errors to develop in some other, non-mathematical, and more empirical areas and probably it will take much more time to change the ways we think about this discipline.

In the meantime, however, public policy developed independently of economics and disciplines related to it: political economy or economic policy. It became a part of political sciences. Both sciences could profit from the exchange of ideas: public policy could receive some more rigorous analyses and economics—a better understanding of policymaking processes. From this point of view, we should conclude that the right balance within social sciences should be established⁵.

Therefore, it would be naïve to think that economic policy is not a kind of public policy. It should not neglect the achievements of the theory of public policy, although it is a usual practice in this area. Moreover, even more importantly, social policy is usually delivered not by economists but sociologists, despite the fact that many economists claim to have the right to influence the public opinions with their views on pensions, maternity, health, housing etc. It all creates methodological mess. Thus, **this book tries to bridge the gaps between public policy, economic policy, and social policy.** And their starting (and common) points are e.g. politics, political science.

2.3. Kinds of states, governments and political systems

The most basic concept of politics is the state and its authorities.

2.3.1. What is the state?

We usually associate it with an independent entity (although there may also be *de jure* states that do not have control over their territory, like many European countries during

⁵ Such a trend is already visible in some world leading academic centres with strong public schools (like e.g. LKY School of Public Policy at the National University of Singapore). The public policy courses run there are accompanied with the modules on economics with its different extensions to e.g. psychology (behavioural economics), institutions (political economy of institutions) etc.

World War II with their governments-in-exile). We distinguish between two kinds of independence:

- based on **constitutive theory**, when a country is sovereign only if it is recognised by other countries; however there are problems with identification when some countries acknowledge the independence and some do not;
- based on **declarative theory**, a country is sovereign (basing on the Montevideo Convention on the Right and Duties of States) when it has:
 - » a defined territory,
 - » a permanent population,
 - » a government and
 - » a capacity to enter into relations with other states.

Box 3. Is the Republic of China a sovereign state?

After World War II and the Chinese Civil War between Chinese Nationalists (Kuomintang), led by Chiang Kai-shek and the forces loyal to the Communist Party of China, led by Mao Zedong, the government of the Republic of China (RoC) has lost the control over the mainland China and has left the continent. It went on exile to the Chinese island Taiwan. In total, about 2 million people emigrated there. The government of RoC did not accept the independence of the communist China and the division of the country. Similarly, the People's Republic of China (or in short China) does not allow for international recognition of the Republic of China (i.e. Taiwan) and considers it its 23rd province.

The Republic of China was a founding member of the United Nations and a member of this organization, representing China until 1971. Then, the UNO passed a resolution no. 2758 under which the People's Republic of China (PRC) became the sole representative of China, and Taiwan was removed from the United Nations.

With time, international recognition of independence of Taiwan is eroding. Currently, only 22 countries have full diplomatic relations with the Republic of China, including Europe's only Holy See (RoC's embassy located in premises rented in Rome, i.e. in a country, which does not have official relations with Taiwan). The island has its own constitution, democracy, civil liberties. It cannot participate in large international events under its name, and e.g. in the Olympic Games it represents "Chinese Taipei". It is a member of only those organisations only, where PRC is not a member of (e.g. Unrepresented Nations and Peoples Organization, World Organization of the Scout Movement).

The subject of interests of political science is not the state itself, but the decision-making process. It differs in various countries, but we can try to find common elements in countries that are similar from certain point of view. We can classify them according to:

- size: small countries, big countries,
- wealth (level of development): industrialised countries, catching-up, developing ones etc.,
- type of political system: democratic countries, authoritarian (totalitarian) ones.

The latter ones can be classified into some smaller groups, depending on the source of power or the role of the government (welfare state vs. minimalist state).

2.3.2. Kinds of governments and political systems

A political state is governed by a government. In the American literature, the latter notion has a broad meaning and consists of legislators, arbitrators and executors (administrators), following the division of power. In British English, it has a narrower meaning of administration. However, it includes not only a prime minister and ministries, but also e.g. the national bank. We will usually use the narrower meaning.

Below we are presented with a schema that classifies different forms of government according to the number of people executing power. Following ancient Greeks, there are “three alternatives in government:

- rule by one,
- rule by a few, and
- rule by many” (Parkinson, 1958 p. 12).

Figure 4. Forms of government



Source: own based on (Parkinson, 1958 p. 12) and other sources.

In an absolute monarchy, the ruler governs with the use of law. The same hold true for a constitutional monarchy, however within the limits given by the constitution (or other law). A despot is not bound with them and acts according to his will and caprice, even if he/she was 'enlightened' (and supported some personal liberties and rights). Monarchs usually receive their status:

- as members of a **ruling family (hereditary system)**, e.g. the United Kingdom of Great Britain and Northern Ireland or the Kingdom of Sweden or
- **through elections**, e.g. ancient Kingdom of Rome, the Holy Roman Empire, Anglo-Saxon England, medieval Scandinavia and Serbia, the Mongol Empire, Poland after the Piast dynasty; and nowadays Malaysia, Cambodia and the Holy See.

Rarely can they also be the heads of federation of other monarchs or states (e.g. the German Empire, the Union of South Africa; and nowadays the United Arab Emirates and Malaysia).

A dictator governs without people's consent. In a dictatorship, the power can be shared within a small group of people, which may control:

- some aspects of social and economic life (authoritarianism, e.g. Iran, Saudi Arabia, Zimbabwe), or
- all of them, trying to justify it with an official ideology (totalitarianism, e.g. fascism, Stalinism).

Similarly, the governing 'power of a few' is a characteristic of:

- **aristocracy**, where the privileged by birth or wealth (aristocratic) class of people holds the power. If this group was formed:
 - » On a basis of religion, then it is **theocracy** (e.g. Vatican City, some Islamic countries, Tibetan government in exile);
 - » On a basis of people's knowledge, abilities (merits) and contributions to society rather than on wealth or social position, then we speak about **meritocracy** (e.g. China during the Qin and Han dynasties, Napoleonic France, India under the British Empire, contemporary Singapore—see the case below).
- **oligarchy**, with even more limited group of people sharing power in comparison to aristocracy (e.g. until recently Ukraine). Here we can distinguish between:
- **plutocracy** (rule by the wealthy, e.g. some city-states in ancient Greece or in much later in Italy, the Roman Republic, some cities in Europe during the Middle Ages ruled by guilds, or the City of London),
- **bureaucracy** (rules of non-elected officials within government),
- **stratocracy** (people with military service have the rights to decide about public matters, e.g. late Roman Empire, partly contemporary Myanmar where ¼ of seats in parliament is reserved for military personnel);
- **military junta** (a country is governed by military leaders who took the power by force, e.g. Greece in 1967-1974, Portugal in 1974-1976, Chile in 1973-1990, Poland during the state of war 1981-1983, Egypt 2011-2012).

Box 4. Meritocracy in Singapore

The origins of meritocracy in Singapore can be traced to the ancient China, where it was introduced for the first time (started in 165 BC and introduced in full version in AD 605). In order to become an administrative official (mandarin), one had to pass an official imperial exam and in some periods, even people from the poorest parts of society could become a prominent politician.

Singaporean governments promote meritocracy and multiracialism as their founding principles:

People should be rewarded based on what they do, not who they are. The system of meritocracy in Singapore ensures that the best and brightest, regardless of race, religion and socio-economic background, are encouraged to develop to their fullest potential. Everyone has access to education, which equips them with skills and knowledge to earn a better living.
(Ministry of Education, Singapore)

About 75% of citizens in Singapore are of Chinese descent. In a society with such a large domination, it could be quite easy to discriminate the minorities (e.g. Malays 13%, Indians 9%).

- On the one hand, there are four official languages, and despite Chinese is a native language for 50% of Singaporeans, in this former British colony English is the language of politics, law, administration, business, public transport (or more precisely, its local Chinese version called ‘Singlish’).
- On the other hand, in late 1970s the “Speak Mandarin Campaign” was introduced to enhance knowledge of Chinese (or more precisely Mandarin Chinese) and Special Assistance Plan schools were created for the Chinese majority.

The government promotes the belief of the merit-based careers in public administration. This justifies keeping the salaries in the public sector on the levels comparable to the private one. In result, the best-paid head of government in the world is a prime minister of Singapore, and (after substantial cuts in 2011) earns US\$1.7 million annually (tax free; while the U.S. President earns US\$400,000). The ministers earn US\$850,000, and members of parliament—US\$150,000.

The myth that the regime operates on meritocratic principles (...) along with the capacity to deliver peace and prosperity, is one of the primary rationales by which Singaporeans reluctantly accept the many unpopular aspects of the regime, such as the lack of freedom and democracy, the intrusion of government into most aspects of private life (...) and the high cost of living. (Barr, 2006)

There are two major types of democratic systems (Munroe, 2002 pp. 47-49):

- **indirect democracy** (representative democracy), where people elect their representatives to rule on their behalf, being limited between the elections by constitution, laws etc.; this system can also use some participatory concepts and e.g. ask the sovereign for opinion on important matters (like joining in European Union), controversial or related to moral issues;
- **direct democracy** (participatory democracy), where people are engaged in the process of decision making e.g. through referenda (e.g. Switzerland), by submitting a law proposal to the parliament (if it was signed by significant number of citizens), or by the right to recall an elected official before his tenure ends.

2.3.3. Unitary states, federations, and unions

The great majority of countries are unitary states. There is one central government that rules them. Although there are administrative districts, their self-governing authority is limited and the centrally established laws must be obeyed. The other form, which gains more popularity and importance with the progress of regional integration, is federation. It can be formed as unification of independent countries that decide to form a common government, laws, unify borders, external policy etc. However, the legislative power is usually divided between the central legislative bodies and the regional/provincial ones.

The examples of federal states are:

- the United Kingdom of Great Britain and Northern Ireland,
- territories formerly owned by the UK, like the United States of America, Canada (with its famous French-speaking Quebec), the Commonwealth of Australia, Republic of India,
- some Latin American countries like: Argentine Republic, Federative Republic of Brazil, United Mexican States, Bolivarian Republic of Venezuela (there were also the United States of Colombia in part of the 19th century),
- some European countries, e.g. Federal Republic of Germany, Republic of Austria, Swiss Confederation, Kingdom of Belgium (in the past e.g. Austro-Hungarian Empire, Polish–Lithuanian Commonwealth),
- former socialist countries, like the Socialist Federal Republic of Yugoslavia (at present Bosnia and Herzegovina have created the federation), Czechoslovakia, or the Union of Soviet Socialist Republics (at present it is the Russian Federation),
- and other examples: Malaysia, Federal Republic of Somalia, Republic of the Sudan, United Arab Emirates and a few more.

Some of the federal countries have separated (sometimes using the warfare arguments) and some of the independent states—have unified (by force or freely).

The European Union can also be labelled as a federation, although such classifications are very sensitive to a public opinion. These are the following steps of deepening the integration in contemporary Europe:

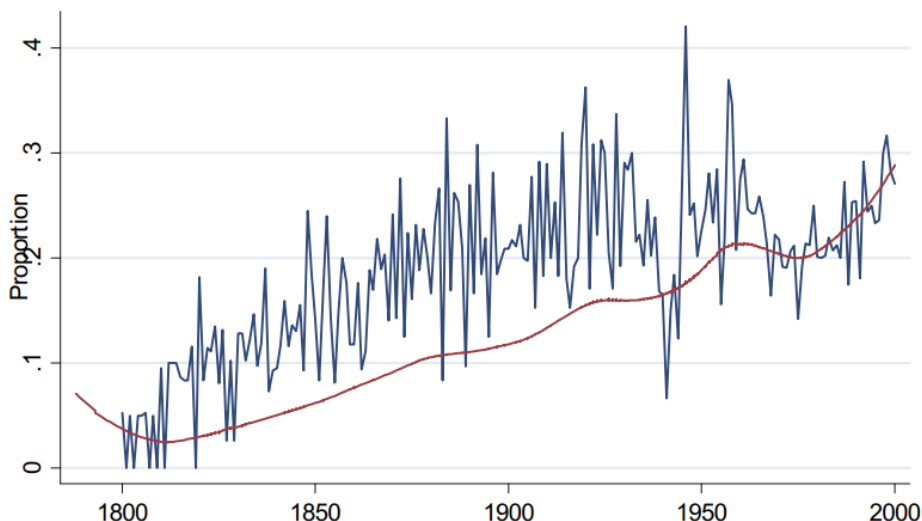
- a free trade area,
- a custom union,
- a single market,
- a monetary union,
- a fiscal union.

There are different policies engaged on different levels of integration. Of course, the co-ordination problems emerge very often—they may contribute to a larger crisis or, if the next step of integration is poorly prepared (or countries are not prepared for it), the integration may even step back (as it was at the beginning of the 1990s). There are some theoretical hints on how the unions should be created (e.g. a theory of optimum currency area (Mundell, 1961) or the theory of international unions (Alesina, et al., 2005)). However, political decisions may not always follow theoretical guidelines...

2.4. Historical evolution of democratic processes

The number of elections in the world before the 19th century was very small. Only Great Britain, the United States, France during revolution, and the Netherlands have established fully elective lower houses in short period of time. However, a quite visible trend started at the beginning of the 19th century, and lasted until the end of the Great Depression in 1930s. There was a significant increase in the share of countries (and dependent territories, which subsequently became independent) in the world that held legislative elections (see Figure 5).

Figure 5. Proportion of countries that held legislative elections, 1800-2000



Note: Lower bound assumes that no elections occurred in some cases with no information.

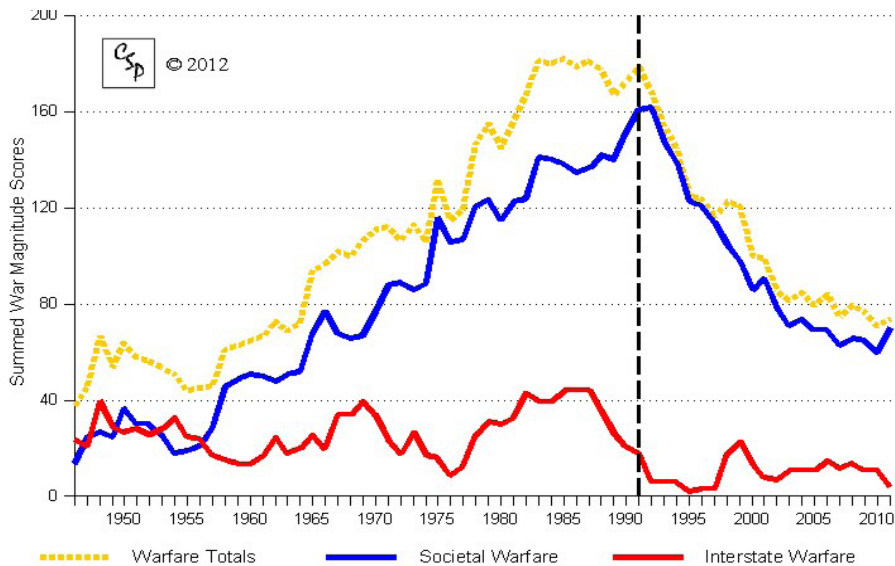
Source: (Przeworski, 2006 p. 7).

Looking at the rising number of democratic countries, compared to other political systems (esp. visible was the falling number of autocratic regimes; see Figure 8), we see that the period of 1990 brought victory of democracy in the world. These processes were called as the “third wave” of democratisation:

A wave of democratisation is a group of transitions from non-democratic regimes to democratic regimes that occur within a specified period of time and that significantly outnumber transitions in the opposite direction
(Huntington, 1993 p. 15).

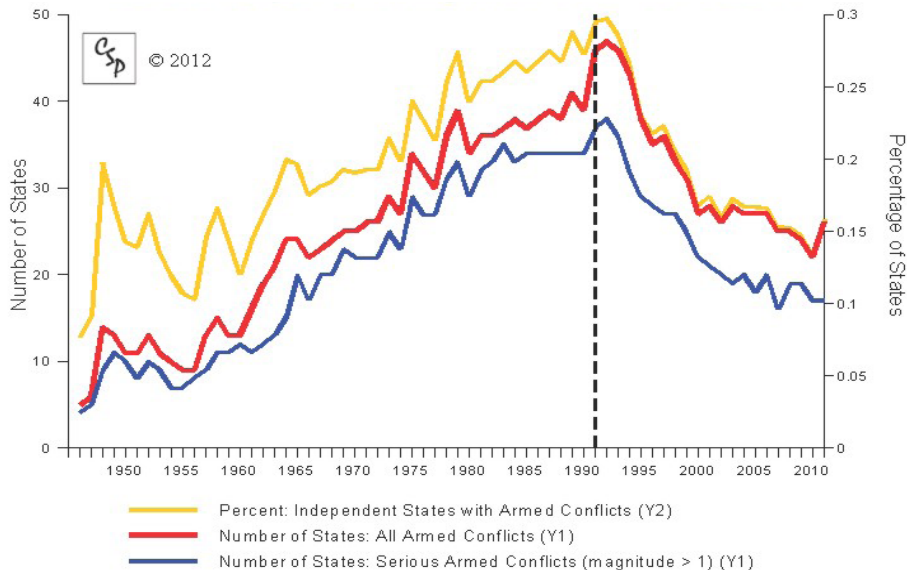
According to Huntington (1993), the first wave took place in 1828-1926 and it was a very slow process. It was reversed by Mussolini in Italy by fascism. World War II brought a new wave that was reversed soon after through the increase in the number of authoritarian regimes in postcolonial and developing countries. Huntington believed that the third wave would bring more international peace. Such process seemed to take place, especially when the number of civil (societal) conflicts decreased (see Figure 6).

Figure 6. Global trends in armed conflicts, 1946-2011



Source: (Marshall, et al., 2012).

Together with the number of armed conflicts, also the total number of wars between countries has decreased after its peak in 1992 from the level of 50 engaged countries (30% of analysed countries) to 24 in late 2011, with 13 of them that were protracted societal conflicts, e.g. in Myanmar, India, Israel, Philippines, Colombia, Afghanistan (Marshall, et al., 2012).

Figure 7. States experiencing warfare, 1946-2011

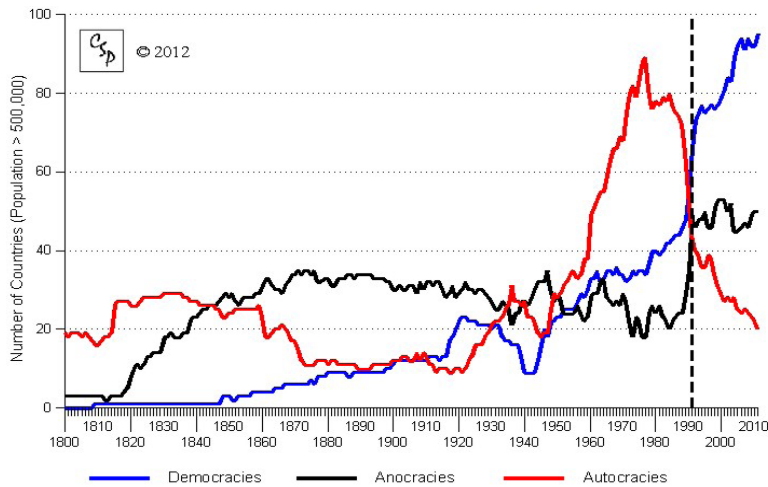
Source: (Marshall, et al., 2012).

It took the world almost half a century to transform from domination of autocratic regimes that became even more frequent after 1950s due to decolonisation processes and the problems with endurance of the new democratic regimes (they failed later on due to e.g. economic problems). That also happened to some post-socialist countries (some Asian countries, Belarus).

In order to prevent the fall of recently established democracies, governments may want to use fiscal policy with its growing spending to convince society that “democracy works”. As frequently underlined in literature, the new system may be endangered by some local anti-democratic elites (older citizens are also sceptical). Therefore, in order to protect the fragile democracy, **economic policy** could be used as an instrument to gain their support (Acemoglu, et al., 2005).

The election years can be especially risky, since the number of collapses of democracy in new democracies is three times higher in an election year than in other years. Empirical evidence suggests that although in new democracies spending is higher in election years, money was spent neither on health nor education, but on transfers and agriculture. It may suggest that not the elites but the masses were supported (Brender, et al., 2007 pp. 21-23)

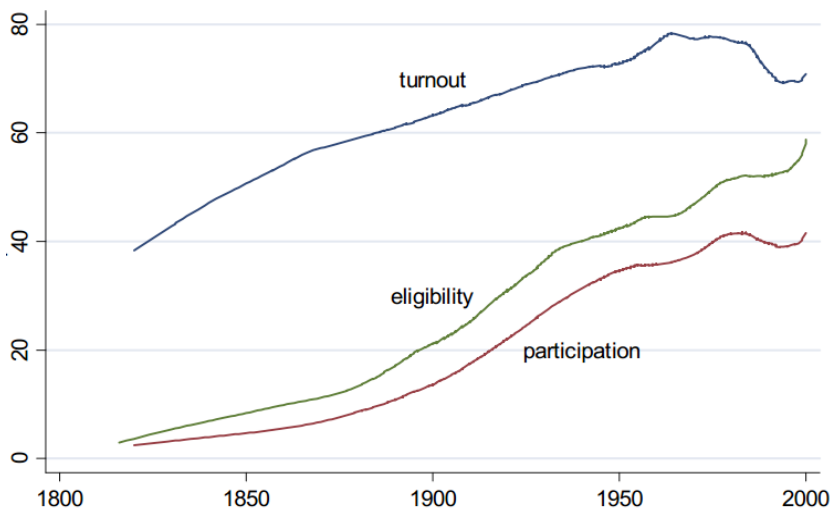
The proportion of people with the right to vote has also increased (see Figure 9). This number increased from about 1 million in 1820 to at least 21 million in 1900, and 730 million in 1996 (Przeworski, 2006).

Figure 8. Global trends in governance, 1800-2010

Note: anocracy is defined as a stage between full democracy and full autocracy.

Source: (Marshall, et al., 2012).

In the 1960s the share of countries that had legislative elections decreased and later increased. The share of eligible voters that actually voted decreased in the 1990s.

Figure 9. Eligibility, turnout, and participation, 1815-2000

Note: values expressed in percent; participation—share of population that actually voted, eligibility—share of population with the right to vote, turnout—share of eligible voters who actually cast votes.

Source: (Przeworski, 2006 p. 8).

2.5. Measuring democracy

Despite the usual problems with defining democracy, there are some indicators of it. The most important ones are published:

- by the US-based **Freedom House** organisation, and
- by the UK-based **Economist Intelligence Unit**.

Democracy is connected with freedom. There are a few international non-governmental organisations and information sources on its measurement, e.g.

- the Polity data series—a database that covers the period from 1800 (the Freedom House research covers the period from 1972 only),
- the Cato Institute and the Fraser Institute, which publish the “Economic Freedom of the World Reports”,
- the Wall Street Journal and the Heritage Foundation, which publish the “Index of Economic Freedom”,
- Reporters Without Borders (publish the “Worldwide Press Freedom Index”).

The Economist Intelligence Unit publishes reports in which it estimates the quality of democracy in over 160 countries. It uses 60 indicators on a 0 to 10 scale grouped in five categories:

- electoral process and pluralism,
- civil liberties,
- functioning of government,
- political participation, and
- political culture.

The countries are divided into four groups: full democracies, flawed democracies, hybrid regimes, and authoritarian regimes. For instance, Russia was downgraded to the last group in 2011 (and occupied 117th place among 167 countries), and the United States were not on the top, but on the 19th position (EIU, 2011).

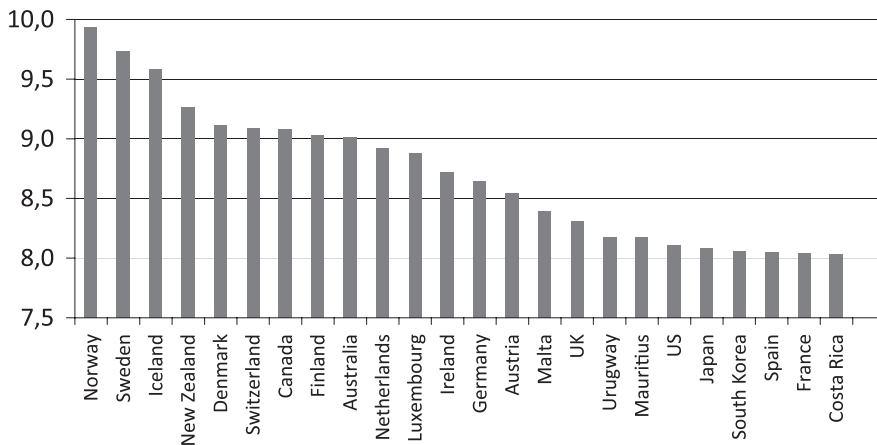
Table 1. Democracy index, 2011 and 2014, by regime type

	No. of countries		% of countries		% of world population	
	2011	2014	2011	2014	2011	2014
Full democracies	25	24	15.0	14.4	11.3	12.5
Flawed democracies	53	52	31.7	31.1	37.1	35.5
Hybrid regimes	37	39	22.2	23.4	14.0	14.4
Authoritarian regimes	52	52	31.1	31.1	37.6	37.6

Source: (EIU, 2011) (EIU, 2015 p. 2).

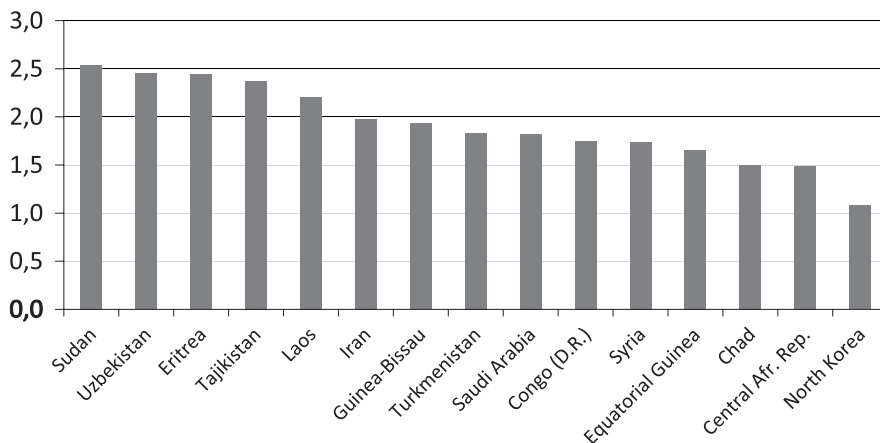
Below some data is presented comparing the countries of the highest and lowest values of the Democracy Index.

Figure 10. Fully democratic countries, 2014



Source: (EIU, 2015 pp. 3-4).

Figure 11. 15 countries of the lowest value of the Democracy Index, 2014



Source: (EIU, 2015 p. 8).

While measuring democracy, **the Freedom House** with its measures:

- of political freedom (based on 10 indicators) and
- of civil liberties (15 indicators) that may be treated as a proxy of the level of fulfilment of the Universal Declaration of Human Rights,

concentrates mostly on measurement of freedom, which is a necessary, but not sufficient element of democracy. It also measures the level of “electoral democracy”. Not all countries

with such a democracy were classified as “free” (87 countries were “free” while 117 were “electoral democracies”). A country is described as an electoral democracy when:

- there is a competitive, multiparty political system,
- there are universal voting rights,
- elections are conducted regularly and are free of manipulations,
- major political parties are able to communicate with electorate through media.

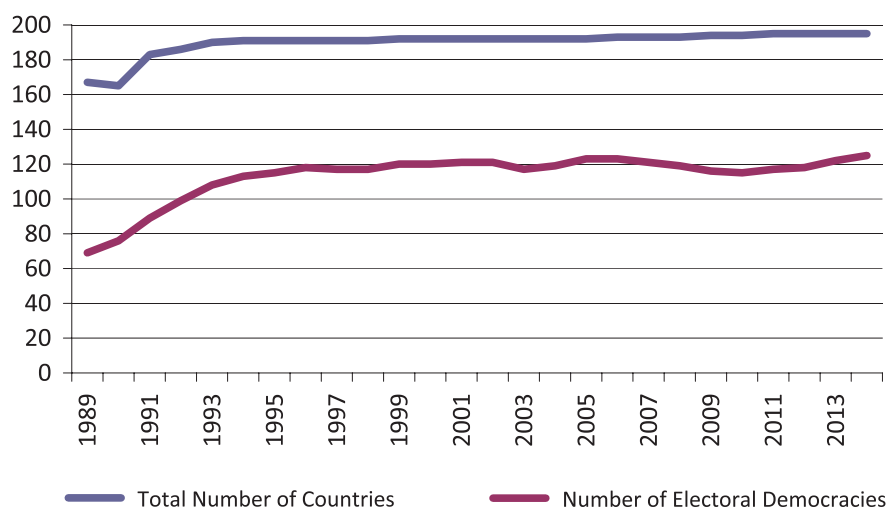
Table 2. Freedom status, 2011 and 2014, by regime type

	No. of countries		% of countries		% of world population	
	2011	2014	2011	2014	2011	2014
Free countries	87	89	45	46	43	40
Partly free countries	60	55	31	28	22	24
Not free countries	48	51	24	26	35	36

Source: (Freedom House, 2012 p. 24) (Freedom House, 2015 p. 8).

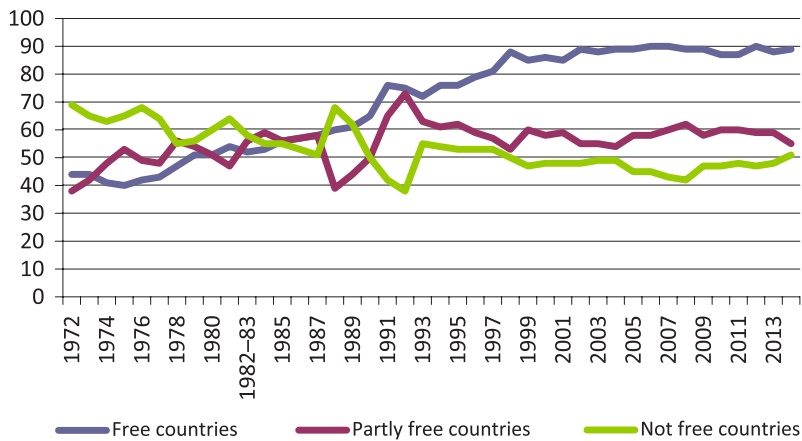
Below, some selected data is presented.⁶

Figure 12. Electoral Democracies, 1989-2014



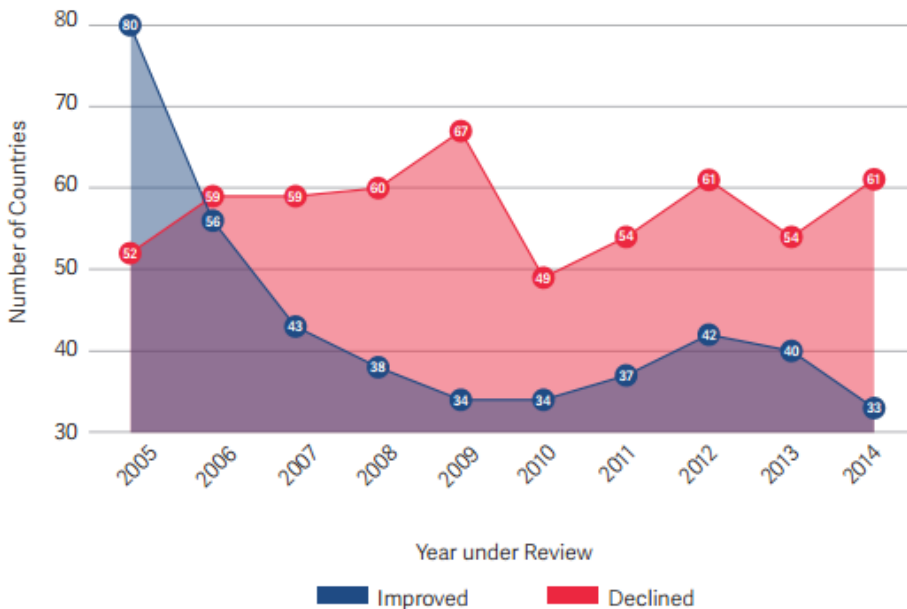
Source: (Freedom House, 2012 p. 29) (Freedom House, 2015 pp. 6-8).

⁶ The full dataset is available here: <https://freedomhouse.org/report-types/freedom-world>.

Figure 13. Freedom status, 1972-2014

Source: (Freedom House, 2012 p. 28) (Freedom House, 2015 pp. 7-8).

The situation since the beginning of economic transition processes has stabilised, however recent years brought the reverse of previous trends and since 2005 the freedom declines in more countries than it improves.

Figure 14. Number of countries with improvements or declines in freedom, 2005-2014

Source: (Freedom House, 2015 p. 4).

As the Freedom House worries:

acceptance of democracy as the world's dominant form of government—and of an international system built on democratic ideals—is under greater threat than at any point in the last 25 years.

(Freedom House, 2015 p. 1)

This warning has also gained an importance recently in Poland.

Chapter 3

Characteristics of democratic systems

Many other notions are associated with politics; some of them that are characteristics of democratic system are enlisted below.

Table 3. Institutional variation among western democracies

Party-system	Two-party vs. multi-party system
Electoral system	Proportional vs. majoritarian
Legislative assembly	Unicameral vs. bicameral
Government structure	Unitarian vs. federalist
Central authority	Parliamentarism vs. presidentialism
Court system	Judicial review vs. judicial preview
Local government	Weak vs. strong autonomy
Civil service	Spoils recruitment vs. merit recruitment
Armed forces	Professional vs. conscription
State–economy relation	Liberal vs. corporatist

Source: (Rothstein, 1998 p. 135).

These notions are quite well-known (or we do not need to know some others to understand economic policy) and do not require very detailed descriptions. Thus, we will present only selected information about them. A relatively new stream of economics called ‘the economic analysis of law’ deals with some of them in economic context.

3.1. Presidential and parliamentary systems

Depending on the political system particularities, we can distinguish between:

- **presidential system**—with the president who plays the role of the head of the government and is elected directly by the sovereign and not indirectly by its representatives in the parliament or any other legislative body (it is quite common in Latin America and of course it is in the U.S.);

- **parliamentary system**—where the executive power lays in the hands of the prime minister and his/her cabinet is appointed by and is accountable to the legislative body and the president (if exists) plays less significant role; there are two types of such systems:
 - » **the Westminster system** (or of the Commonwealth nations), in which the plenary debates in the parliament play a more crucial role than the work done in the parliamentary committees (plurality rule in single-member constituencies);
 - » **the Consensus (Western European) system**, where most of the legislation process is conducted during the debates within the commissions and uses a rather proportional representation (with proportional representation elections),
- **semi-presidential system**, with both prime-minister and the president sharing executive power, but the role of the president is larger (e.g. in France⁷).

Some countries are still debating on pros and cons of different electoral systems. This is especially important in countries which are still shaping their political system or wanting to change it in the future (like e.g. in some emerging or developing countries).

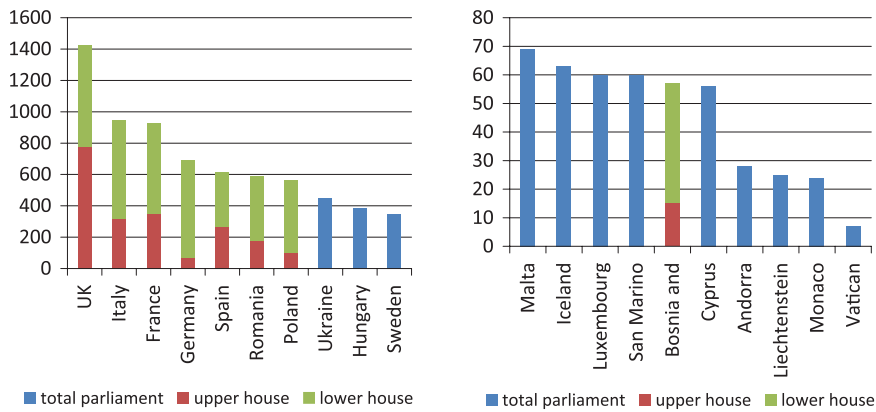
3.2. Legislative assemblies

Another important characteristics of political systems is the legislative assembly. In parliamentary democracies, there can be two kinds of systems that differ in the number of chambers:

- **unicameral**—with one chamber, often called the assembly or just the parliament,
- **bicameral**—with two chambers: the higher and lower one, although usually they have different names than the above, e.g.
 - » the House of Lords and the House of Commons in the United Kingdom,
 - » the Senate and the House of Representatives in the United States,
 - » the Senate and the National Assembly in France,
 - » the Senate of the Republic and the Chamber of Deputies in Italy,
 - » the Bundesrat and the Bundestag in Germany,
 - » the Federation Council and the State Duma in Russia.

Usually, if there are more members in parliament, it is divided between two chambers (China is the important exception of a large unicameral country, where the National People's Congress consists of 2987 representatives). Seven largest legislative bodies in Europe consist of two chambers, while the smallest legislatures are unicameral (with the exception of Bosnia and Herzegovina, see Figure 15).

⁷ In 1958, the parliamentary system was abandoned in France due to weakness of this system, e.g. problems with establishing stable parliamentary majority, inability of prime-ministers to introduce unpopular reforms.

Figure 15. 10 countries with the highest and the lowest number of parliamentarians in Europe, 2014

Source: own.

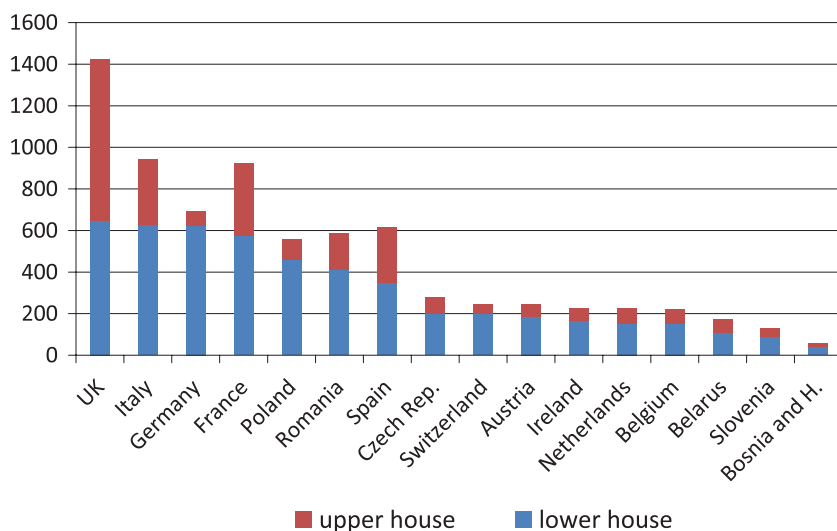
There are some characteristics of the upper house that distinguish it from the lower one, e.g.:

- The higher council frequently, contrary to its name, plays a **smaller role** than the other one (the exception is e.g. the Senate in Italy, which has almost the same role). It aims usually:
 - » to amend (revise) the legislation introduced by the lower chamber, or
 - » to advise, to express the opinions from a different point of view, enriching in this way the public discussion and decision-making process (like e.g. Bundesrat, which consists of the representatives of 16 federal states, *Länder*).
- Its members may be elected:
 - » with a different voting system than the lower chamber, e.g.
 - the House of Lords, where most new members are appointed by the Church of England (26 Lords Spiritual) or life peers who are appointed by the Monarch (Lords Temporal); there are also 92 hereditary peers;
 - members of the Bundesrat are delegated by the state governments under degressive proportionality system, while the Bundestag is appointed through elections;
 - in the parliament of Singapore, there are currently 87 members of parliament who are elected and 12 more who are nominated by the President or were the best performing losers in elections);
 - » partially (not the whole chamber at once):
 - in Chile, the Senators are elected for eight years, and half of them is replaced every fourth year;
 - » for a longer period (or even for a life time):
 - in the United States the Senators are elected for six years, while the representatives of the House serve for a two-year term;

- in Australia, the respective numbers are six and three years;
- in the Czech Republic, in Japan it is six and four years;
- in France, in Egypt, in India, the figures are six and five years, respectively;
- there are four life time senators in Italy (they include the former president and some former prime ministers).

Associated with the smaller role is the **lower number of members** in higher chambers (with exception of the UK and Russia). On average, in 16 European parliaments that were taken into account, the higher chambers had 42% of the number of members of the lower house (the UK was not considered in the above count due to its historical ‘overrepresentation’, see Figure 16).

Figure 16. Number of members of upper and lower houses in Europe, 2014



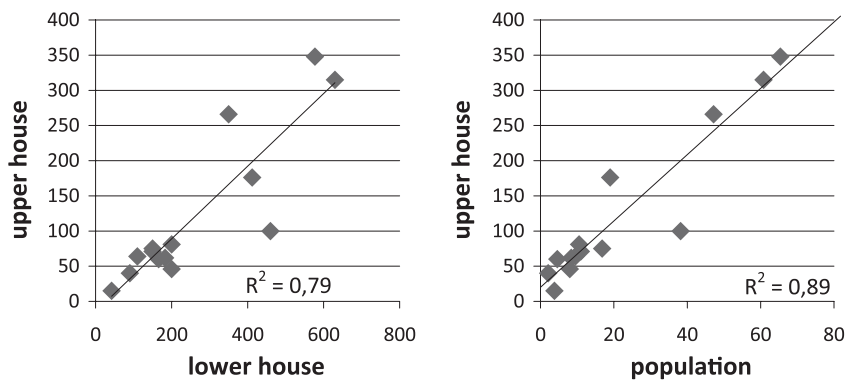
Source: own.

The number of members of both houses depends mostly on historical context. In contemporary Europe, the number of representatives in the upper chambers depends on the number of representatives in the lower chambers and on the size of the population in a country. In case of power chamber and consequently in total parliament, the number of parliamentarians depends mostly on the number of people in the population (see the case study below). This relation was true in case of most countries worldwide (see Figure 18).

Box 5. Number of members of parliaments in Europe

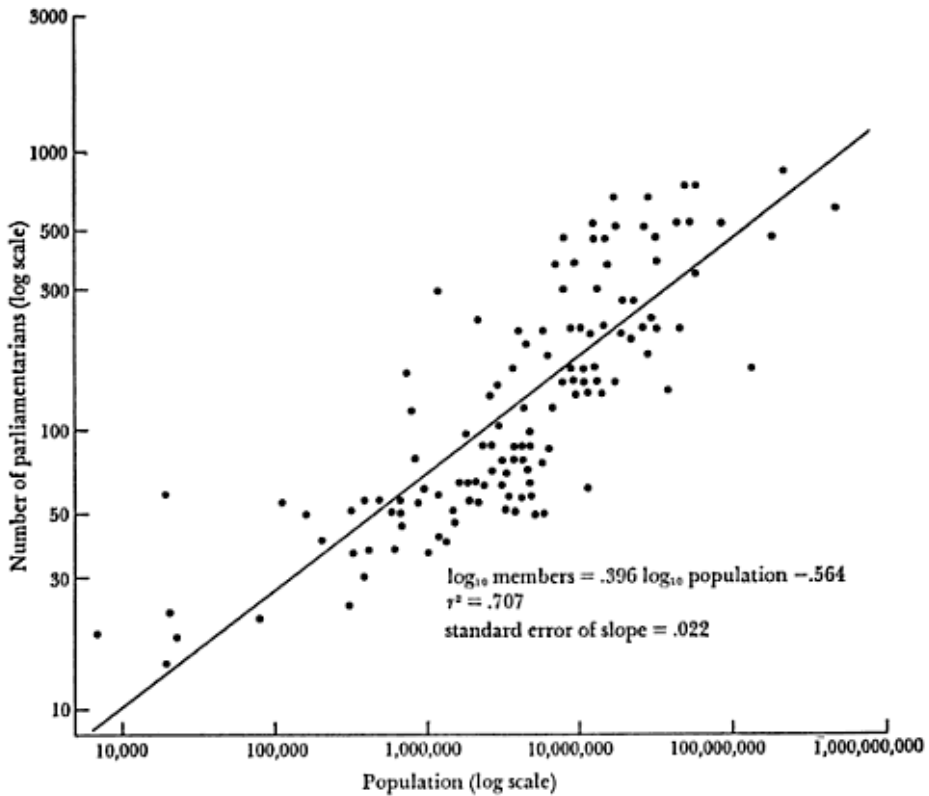
Some people (especially in transition countries that have recently rebuilt their political systems and are more eager to continue doing so in future), may wonder what number of members of parliaments would be ‘proper’ in case of their country. In order to check it we collected the information on 42 European countries (without Russia, the Vatican, Turkey, and the Caucasian countries). We have checked the relations between the number of parliamentarians in the total parliament, in both chambers, and the size of territory, population, density of population, nominal GDP, and GDP per capita. The regression analysis has shown that the most powerful explanation of the number of parliamentarians is the number of population (however, area and GDP were also significant in some cases).

Figure 17. Number of members of parliaments in Europe and explanatory variables, 2014



Note: without the UK and without Germany in case of lower house. Source: own counts.

Figure 18. Population and parliamentary size in 135 countries, 1970



Source: (Dahl, et al., 1973 p. 82)

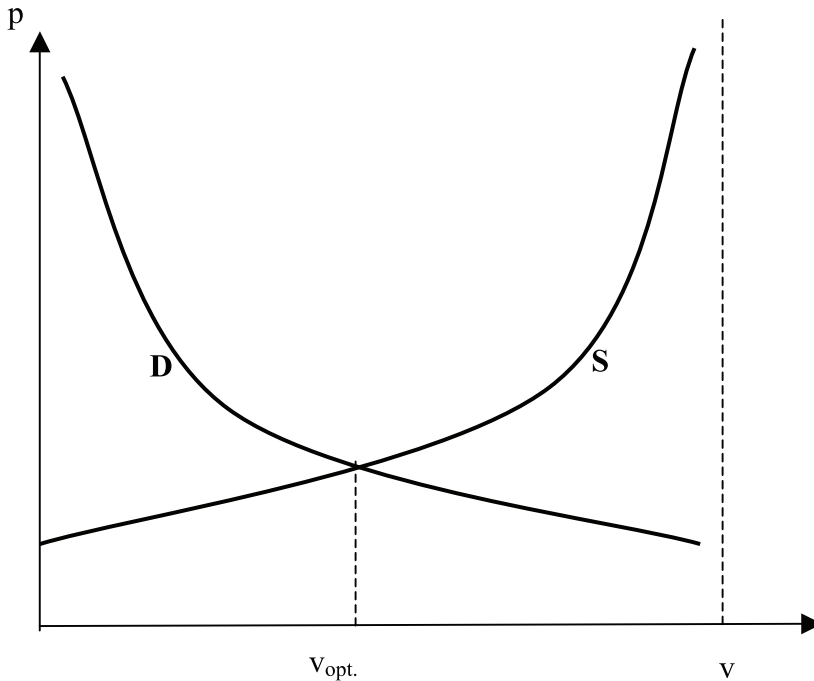
However, there can be a problem in a situation where both chambers end the cadencies at the same time. In case of the change of political majority in the parliament, we can **expect large shifts** in public policies. It is important from the point of view of the stability and the time perspective of some policies.

Short-term focused politicians have usually larger problems carrying long-term goals in comparison to the short-term ones. Thus, we could discuss the role of **one of the chambers as a kind of stabiliser of the public policies** and the body that cares more about strategic, long-term goals of the public policy.

3.3. Electoral market in democracies

Elections can be regarded as an example of a market, where the demand for votes meets their supply, limited by the number of eligible voters (and to some extent by the turnover).

Figure 19. Market of electoral votes



Notes: S—supply of votes, D—demand for votes, v —number of votes, p —price of votes (in practice: non-measurable), $V_{opt.}$ —number of votes when the price is optimal.

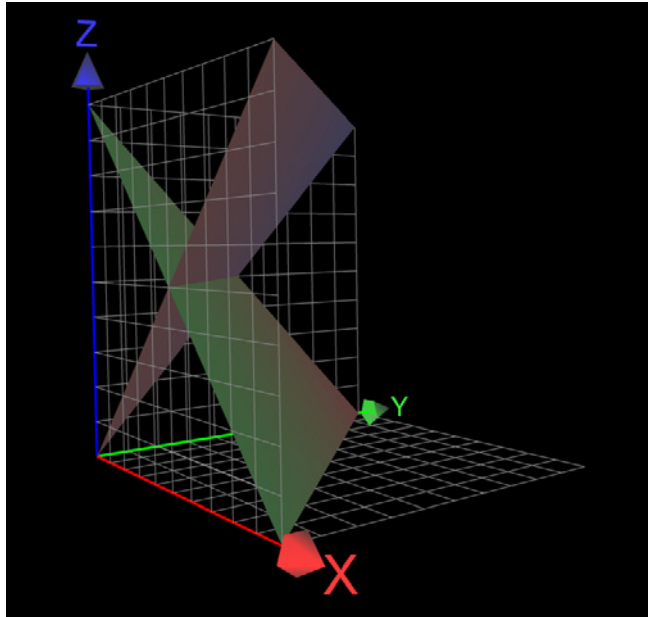
Although humans are political animals, politicians are economists from the point of view of optimisation of their spending. In this situation, we regard the price of the votes not only as a direct function of money that is spent on electoral campaign, but also the promises. However, there are some limits. Politicians cannot promise everything because they must take into account their **credibility**. On the other hand, if they promise too little, they risk being not elected. Thus, their job is to find a balance between credibility and promises.

Political language is designed to make lies sound truthful and murder respectable, and to give an appearance of solidity to pure wind.

George Orwell

The graphical solution to this problem is a line formed on crossing of the supply of the votes and the demand for the votes surfaces (Figure 20).

Figure 20. Promises, accountability, and votes



Note: x—promises, y—accountability, z—votes. Surface starting from the beginning of the coordinate system express supply, the second one—demand.

Source: own.

In order to be re-elected politicians should show their credibility through fulfilling their promises, sometimes even harming the economy, and as a consequence—the society. We could discuss the matters of the rationality of voters, the asymmetry of information about the economic situation and consequences of political steps etc.

The situation would change in a proportional system, where a voter may not necessarily vote for the party he/she prefers, but for another one, in order to increase the chances of winning of another party.

The matter of decision making while choosing the party or a candidate is often time consuming—one has to acquire information about the political programmes, stances of candidates etc. Reasoning voters, i.e. the ones that care about their levels of political knowledge (Popkin, 1991), may consider collecting information as expensive. Moreover, if we consider the **alternative costs** of participation in the elections and influence of the one vote given, we can speak about the **paradox of voting** (or Downs paradox), because the costs for rational voters outnumber the expected gains. In this situation, the task for politicians would be to

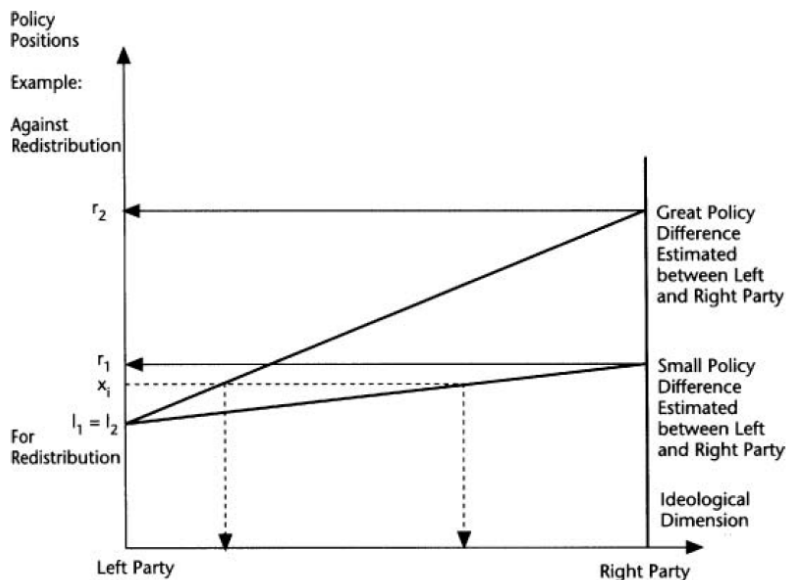
minimise the costs for citizens (e.g. by introduction of online voting) and to influence their utility function. In this way, they might persuade them to value the self-satisfaction of giving the vote (or threaten them with consequences of not voting, in some countries even by imposing penalties for those who did not vote).

3.4. Kinds of political parties

One of the ways to minimise the costs of acquiring the information about political parties in multi-party systems is to simplify the selection problem and divide the parties along the 'left-right' line. In some societies the distinction between 'Christian' (and conservative) parties and liberal (progressive) parties may also be important. Some ethically conservative parties may have more social or more pro-market economic orientation.

The situation becomes even more complicated if we consider the differences between the ideologies of the parties. Sometimes they can be small, or they can be recognised as small (or big). In particular, voters with the same preferences concerning any particular policy may choose a different party (a left-wing or a right-wing one), depending on their perception of the size of differences between the parties' view on this policy (e.g. redistribution one, see Figure 21).

Figure 21. Policy preferences and perception of policy differences between left- and right-wing parties



Note: i —voter (1 or 2), x_i —policy preference of voter, l_i - estimate of the policy position of left party, r_i - estimate of the policy position of right party.

Source: (Pappi, 1998 p. 267).

The division of parties to the left- and right-wing ones comes from France. During the French Revolution in the Estates-General, two blocks sat on the opposite sides:

- on the left those who supported the revolution, and
- on the right their opponents.

The country's motto was:

Liberté, égalité, fraternité

(Liberty, equality, fraternity).

Nowadays, the left-wing parties usually underline the second word only. They aim at introducing more of so-called '**social justice**', by which they mean more redistribution to make the incomes (or even assets possessed) equal. That may encompass the rights of minorities, disabled and other handicapped persons.

Box 6. Is the social justice just?

If the justice in the areas of the distribution of wealth, opportunities, and privileges within a society (these are usually the features of the social justice) was established, and if it really was fully fair, then one simple word would be enough to call it, i.e. 'justice'. If this is, however, the social justice, and not any 'normal' one, this means that it is not a simple, pure justice. Thus, social justice is not necessarily the normal, full justice.

What is more, the social justice can in particular serve the influential social groups (and the politicians representing them) as a justification for introduction of social injustice, arguing it with the desire to reach the social objectives. From here, it is very close to populism—to marginalize the position of less numerous social groups that—because of the size—could verily have smaller representation in a parliament. Thus, the "social justice" may restrict freedom and—if further developed—may lead to injustice. So, is the social justice simply just?

However, the right-wing parties usually assume that people are not equal and since 'natural' is, that they were not born equally (recall the A. Sen's views in the chapter 1.2); policymakers should not distort this natural order too much. Hence, conservatism and bias towards religious values is typical for right-wing parties.

- It is easy to have such a clear distinction in two-party system, like e.g. in the United States:
 - » the left-wing party is the Democratic Party, and
 - » the right-wing party—the Republican one,
- or in systems dominated by three parties, e.g. in the United Kingdom:
 - » the Labour Party is naturally the left-wing one (or precisely, centre-left), while

- » the Conservative and Unionist Party is the (centre) right one (Liberal Democrats are liberal, radical centrists).
- but more complicated in multi-party systems, e.g. in Germany
 - » the Christian Democratic Union (CDU), the Christian Social Union of Bavaria (CSU), and the Free Democratic Party are centre-right;
 - » the Social Democratic Party of Germany (SPD), the Alliance '90/The Greens are centre-left, and the Left Party is more on the left).

Contrary to a common belief, the left-wing parties are more likely to run tighter fiscal policies than the right-wing parties are, and their probability of success is higher as well. The centrist governments have the biggest problems in running a fiscal policy (Table 4), what can be explained by the observations that they are formed by coalition of right-and left-wing parties (Alesina, et al., 1995 p. 21).

Table 4. Probability of fiscal policy run by right, center and left governments in OECD countries

	Probability of very loose	Probability of very tight	Probability of success
Right	8.6%	10.9%	26.9%
Center	15.4%	10.8%	0.0%
Left	12.4%	17.8%	35.1%

Source: (Alesina, et al., 1995 p. 35).

Politicians have their own goals. Thus, they may engage in a rent seeking behaviour. For instance, they may be vulnerable to corruption.

3.5. Ways of financing the political parties

There are three major sources of incomes of political parties:

- public sources, in a form of
 - » direct subsidies or grants, or
 - » indirect, through the use of public services free of charge (e.g. broadcasting time in state-owned TV/radio stations);
- private sources, e.g.
 - » from physical persons (donations, membership dues),
 - » from legal persons (organisations, corporations),
 - » from interests groups,
- own business activity and rent from the assets possessed.

Another way of systemising financing of political parties is the division into:

- “Grassroots fundraising” coming from individuals (party members, individual supporters),
- “Plutocratic funding” that comes from wealthy people and / or the business.

Below the case of the United States is presented and all the major groups of interests are enumerated with the funds they have transferred to a certain candidate.

Table 5. Top interest groups giving to members of Congress, 2012 electoral cycle

Rank	Interest Group	Total	Dem Pct	GOP Pct	Top Recipient
1	Lawyers/Law Firms	\$48,664,854	70%	30%	Kirsten Gillibrand (D-NY)
2	Retired	\$42,020,708	38%	61%	Scott Brown (R-Mass)
3	Health Professionals	\$36,914,613	39%	61%	Ron Paul (R-Texas)
4	Securities/Invest	\$34,846,859	40%	60%	Scott Brown (R-Mass)
5	Real Estate	\$30,108,232	44%	55%	Scott Brown (R-Mass)
6	Insurance	\$25,960,449	37%	63%	Scott Brown (R-Mass)
7	Leadership PACs	\$23,652,557	39%	61%	Dean Heller (R-Nev)
8	Lobbyists	\$21,165,988	53%	47%	Jon Tester (D-Mont)
9	Oil & Gas	\$17,390,884	14%	86%	Rick Berg (R-ND)
10	Pharm/Health Prod	\$16,904,330	44%	56%	Orrin G. Hatch (R-Utah)
11	Commercial Banks	\$14,381,352	33%	67%	Bob Corker (R-Tenn)
12	Electric Utilities	\$13,700,253	39%	61%	John Boehner (R-Ohio)
13	TV/Movies/Music	\$13,673,201	56%	44%	Howard L. Berman (D-Calif)
14	Misc Finance	\$13,117,950	35%	65%	Scott Brown (R-Mass)
15	Misc Mfg/Distrib	\$12,325,519	31%	69%	John Boehner (R-Ohio)
16	Business Services	\$11,588,154	52%	48%	Scott Brown (R-Mass)
17	Computers/Internet	\$11,189,813	47%	53%	Ron Paul (R-Texas)
18	Hospitals/Nurs Homes	\$11,065,462	48%	52%	Mitch McConnell (R-Ky)
19	Crop Production	\$11,042,940	36%	64%	Frank D. Lucas (R-Okla)
20	Public Sector Unions	\$10,599,848	91%	8%	Christopher S. Murphy (D-Conn)
21	General Contractors	\$9,607,707	26%	74%	John Boehner (R-Ohio)
22	Health Services	\$9,533,907	43%	57%	Orrin G. Hatch (R-Utah)
23	Bldg Trade Unions	\$9,272,937	83%	16%	Kathleen Hochul (D-NY)
24	Retail Sales	\$8,906,129	37%	63%	John Boehner (R-Ohio)
25	Education	\$8,774,543	62%	38%	Ron Paul (R-Texas)
26	Accountants	\$8,447,615	38%	62%	Scott Brown (R-Mass)
27	Transport Unions	\$8,320,942	74%	26%	Nick Rahall (D-WVa)
28	Air Transport	\$8,292,920	36%	64%	John L. Mica (R-Fla)
29	Pro-Israel	\$8,005,683	67%	33%	Shelley Berkley (D-Nev)
30	Automotive	\$7,899,381	25%	75%	John Boehner (R-Ohio)
31	Defense Aerospace	\$7,628,902	40%	60%	Buck Mckee (R-Calif)
32	Beer, Wine & Liquor	\$7,313,212	43%	57%	Mike Thompson (D-Calif)
33	Food & Beverage	\$7,252,100	29%	71%	Scott Brown (R-Mass)
34	Misc Business	\$6,957,638	38%	62%	Ron Paul (R-Texas)
35	Repub/Conservative	\$6,686,882	0%	100%	Jeff Flake (R-Ariz)
36	Construction Svcs	\$6,611,596	45%	55%	Ron Paul (R-Texas)
37	Telephone Utilities	\$6,300,399	38%	62%	John Boehner (R-Ohio)
38	Agricultural Svcs	\$6,117,544	33%	67%	Deborah Ann Stabenow (D-Mich)

Rank	Interest Group	Total	Dem Pct	GOP Pct	Top Recipient
39	Industrial Unions	\$5,794,451	97%	3%	Kathleen Hochul (D-NY)
40	Candidate Cmtes	\$5,711,668	50%	49%	Thaddeus G. McCotter (R-Mich)
41	Mining	\$5,579,236	15%	85%	John Boehner (R-Ohio)
42	Railroads	\$5,487,688	36%	65%	Mitch McConnell (R-Ky)
43	Food Process/Sales	\$5,481,020	29%	71%	John Boehner (R-Ohio)
44	Chemicals	\$5,052,315	30%	70%	John Boehner (R-Ohio)
45	Finance/Credit	\$5,005,765	32%	68%	John Boehner (R-Ohio)
46	Defense Electronics	\$4,796,615	41%	59%	Scott Brown (R-Mass)
47	Misc Defense	\$4,745,381	39%	61%	Buck McKeon (R-Calif)
48	Building Materials	\$4,680,695	18%	82%	John Boehner (R-Ohio)
49	Casinos/Gambling	\$4,407,260	48%	52%	Shelley Berkley (D-Nev)
50	Women's Issues	\$4,184,876	98%	2%	Claire McCaskill (D-Mo)

Note: Based on data released by the FEC on Monday, November 12, 2012.

Source: (Centre for Responsive Politics, 2012).

Box 7. Groups of interests and public policy: questions for discussion

- Which groups of interests supported the democrats and which the republicans?
- Why?
- What is the influence of such support on the goals of economic and social policies in the U.S.?

The discussion indicated above Box 7 would probably lead the reader to the conclusion that these major streams of private funds, even if they are transparent, may influence the public policy run in a country. However, it does not mean that only powerful groups of interests matter to politicians (see the case below).

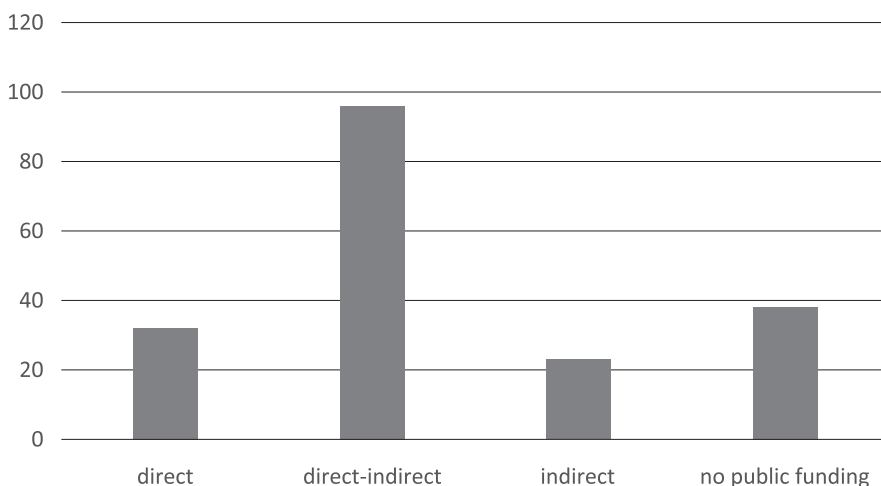
Box 8. The case of Obama's campaign

It may be assumed that it is easier to collect money from richer persons or from businesses to finance the campaign. The example of Barack Obama's campaign was exceptional from this point of view.

- In February 2007, 727,972 people sent money to the campaign of Senator Barack Obama, the presidential candidate of the Democratic Party.
- "The vast majority of the funds for as much as \$45 million was collected through the Internet. More than 90% of the revenue was less than \$100. More than half of these were payments not exceeding \$25." (CNN)

The end of the 1960s was the beginning of financing the political parties with public sources. The most common way nowadays is to provide political party both direct and indirect public funding (most of EU countries, the US). There are also countries, where there is no public funding granted to political parties; those are usually developing countries (e.g. Botswana, Egypt, Libya, Malaysia, Nepal, Pakistan, Singapore, Zambia, some Caribbean and Pacific islands). In 13 countries, only, it is forbidden to finance political parties from private sources (e.g. Austria, Belarus, Laos, Uzbekistan, and Zimbabwe).

Figure 22. Number of countries where political parties receive direct/indirect public funding, 2014



Source: (The Electoral Knowledge Network, 2015).

Despite the growth of popularity of public funding to political parties, the problems of political corruptions were not eliminated and can adopt forms such as e.g.:

- **embezzlement**, when somebody dishonestly withholds someone else's assets to keep them or to exchange them (e.g. for money);
- **extortion**, when someone is bringing another person (or company, institution) to transfer money, property or to provide some services through the use of violence against that person, e.g. by the threat of attack against life, health or property;
- **graft**, when public money is redirected to provide profits to politicians or their relatives / acquaintances etc.;
- **influence peddling**, when in return for some financial gratitude someone from the authorities favours somebody or gives him/her preferences;
- **kickbacks**, which are a mutually negotiated commission paid to the person that accepts the bribe for the services this person provides.

Box 9. Financing political parties and public policy—questions for discussion

- What are the pros and cons of different variants of financing? Reasons and consequences.
- Depending on the type of financing the political parties, what should be the rational strategy of preparing a political program to maximise inflow of funds to the given political party?
- Which political programs are supported by which groups of voters / groups of interests (e.g. pensioners, public servants, trade unions, entrepreneurs, enterprises)?
- What would be the goals of public policy while supported by different groups of interests?
- How the legal solutions concerning political fundraising may influence the economic and social policies run in a country?

3.6. Legislative elections

Among the most important characteristics of political systems are the ones connected with legislative elections. There are three groups of dimensions:

- **district magnitude**, which is the number of people elected in a given district (constituency) and has three forms:
 - » **single-member district** with one representative (e.g. U.S., Canada, UK, India),
 - » **multi-member district**, which functions usually in proportional systems (the exception is Singapore⁸),
 - » **hybrid system**, where there are two-three candidates nominated by a party/coalition to win two-three seats, in particular selected with plurality rule (used in Chile and in Mauritius);
- **electoral formula**, which recalculates votes to the seats and can be:
 - » **majoritarian (plurality rule)**, which is a single-winner voting system (used in 48 countries),
 - » **binomial representation system** to equalise the number of seats received by two parties/coalitions (used in Chile),
 - » **proportional representation (PR)**, where the seats are assigned proportionally to the number of votes (used in 90 countries in the world),

⁸ In Singapore, apart from the Single Member Constituencies there is the Group Representation Constituency. In GRCs the groups of people are voted and not individuals. The purpose of this solution was to ensure the minimal racial representation, because at least one of the candidates for a member of parliament had to represent the minority. Similar function plays the Best Loser System in Mauritius, where apart from directly elected members there are a few seats reserved for the best losers who represent minorities.

- » **“mixed” electoral system**, where a part of parliamentarians is elected with plurality rule, and a part with proportional representation or there are differences in case of a particular chamber (e.g. half of the Bundestag is elected through plurality in single-seat districts, and the other half through PR);
- **ballot structure** is about voting techniques and can be
 - » **ranked ballot** (“preference” system, e.g. Condorcet method, Borda count), where voters create a ranking of options that present their preferences,
 - » **range voting**, where different options are evaluated separately.

In majority of the developed countries the voting systems are based on the rule of **multiple-winner**, i.e. there can be many parties in the constituencies (usually selected proportionally) that can form ruling coalitions. This situation is described as a **multi-party system**. This system usually exists in countries with **proportional** electoral systems. In this system, the number of seats in the parliament taken by a party depends proportionally on the number of votes it has received during elections. In result, there are few parties in the parliament that can form a ruling coalition. In order to prevent having too many small parties (and problems with political stability), usually a minimum threshold for election is introduced. This is because too high fragmentation leads to poorer economic results, e.g. higher spending, or budget deficits etc.

Proportional rule is indeed associated with more fragmented party structures, which in turn lead to more frequent coalition governments, which spend more than single-party majority governments.

(Persson, et al., 2003 p. 45)

In a multi-party system, some parties may have similar views and they can be blocked and treated as similar from ideological point of view. This is the way to measure the ‘ideologically cognizable number of political parties / party groupings’ (e.g. in Canada a four bloc party system can be reduced to three bloc system, in Slovenia from five and in Spain from four to two) (Grofman, et al., 2012).

The exceptions in Western democratic countries are the U.S. and the UK. There is a **single-winner** rule and the system bases on ‘**first-past-the-post**’ principle (there are of course more countries with such a system; they are mostly the developing ones). In this system the seat is occupied by a person who won more votes than his/her competitors. Over time, such a system leads to creation of **two-party system** and gives a disproportionally large share of seats to largest parties, neglecting the rest of them. In this ‘**winner-takes-all**’ (or ‘simple plurality’) system in the U.S., if one candidate for a president’s office has a majority in a state, he takes all the electoral votes⁹. This system is typical for countries with the **majoritarian** electoral system.

⁹ In result there can be a situation that the candidate may receive more popular votes than the opponent at the country level, but may lose the elections, because of the smaller number of electoral votes received. It was e.g. in 2000, when Al Gore received about 0,5 million more popular votes than George W. Bush, but five less electoral votes.

Box 10. Voting system in Chile**Pinochet's regime**

An intriguing example of voting system can be found in Chile. This country experienced authoritarian rules under General Augusto Pinochet regime (1973-1990). In 1980, the military junta passed a new constitution (drafted by a professor of constitutional law Jaime Guzmán). According to it, the people should vote for a president in a plebiscite, and if they disagree for a military-appointed candidate, the power is to be granted to civilians and the democratic elections have to be called for. At that time it was believed, that the voters would support Pinochet.

In 1987, two important things happened. In April, the Pope John Paul II visited Chile and criticised the regime. Later that year, it allowed for a creation of opposition parties and for their advertising. In October 1988 the voters in referendum were to approve the 1980 constitution and decide about acceptance of a new eight-year term for the only candidate to the president's post—Pinochet. However, contrary to regime expectations, they did not agree.

Then, the military regime allowed free elections the next year and agreed with the opposition on the constitutional changes that were approved in a plebiscite in July 1989. The changes included e.g. election system matters. They were aimed at promoting two large right-wing parties, which supported Pinochet. In further elections, they (i.e. Concertación) received most votes in the lower chamber (Chil3). Later, the constitution was modified a few times. The present system is, however, a legacy of the old one.

Electoral system in Chile

In Chile, each of the 60 districts for the Chamber of Deputies and each of the 19 constituencies for the Senate has two seats. Deputies are elected for four years and senators—for eight years (half of them is changed every half-term). At the same time, parliamentary and presidential elections are conducted. The **binomial system** guarantees that the seats are divided quite equally between the two largest political blocks (even if the second coalition received much less votes). That was to protect the stability of the system (through smaller fragmentation), and to prevent one party from being able to change the constitution.

Each coalition elects two candidates for two seats in a district / constituency. One of the seats is won by a candidate who received most votes from one of two blocks that received most of the popular votes in total. In result, there are two blocks in the parliament (what is similar to the bipartisan system). For example in 1989 the largest block received 69 seats (51.5% of votes) and the second one 48 seats (34.2% of votes). In elections held 20 years later, they were 58 (43.4%) and 57 (44.4%) seats respectively (Álvarez-Rivera, 2010).

In December 1989 Patricio Aylwin was elected president in the first democratic elections since 1970 (until March 1998 Pinochet, however, remained the Commander-in-Chief of the Army; accused of e.g. human rights violations, was arrested in October that year in London; returned to Chile in March 2000 and died in 2006 during his trial). Despite criticism, lack of citizens' support and trials of reforms of the binomial system, it still functions.

Chile and Poland

The Chilean electoral system is claimed as being modelled on the Polish example, where the early 1980s were "the moments of greatest rise of labor and social movement" (Maira, 2001 p. 94). "To ensure that democracy would never become too liberal (...) Pinochet implemented the "binomial" electoral system, a method invented in late-Communist Poland in the 1980s, adapted to Chile, and today applied only in this Andean nation". (Benedikter, et al., 2015 p. 93)

After the Polish Round Table Talks (February-April 1989) the previous electoral system was changed (in April 1989), and the opposition was allowed to take up to 35% of seats in the lower chamber (and up to 100% in the Senate). If we group ruling coalition of the Polish United Workers' Party and its 'satellite' parties (United People's Party and others) and treat them as one block, and the Solidarity opposition as a second block, we could call this system as binomial. In the Senate, the magnitude of districts was two seats (apart from two largest districts of three representatives). After the semi-free elections in June 1989, Solidarność, however, took all of the possible 35% seats in Sejm and 99% of the seats in the Senate.

In the proportional electoral systems, we can expect:

- more voters participating in elections,
- conducting more left-oriented policies, that result in higher redistribution of welfare,
- forming coalitions,
- in result of coalition and higher leftism—higher public spending (esp. on transfers and welfare projects) and higher public debt that can produce higher income equality,
- lower ability to run fast policies (e.g. in case of threat of influence of external shock like financial crisis),

While in the 1960s-1980s there were almost no serious changes in electoral rules in the world, the 1990s brought many changes (Persson, et al., 2003 p. 88), among which the mixed system was the most popular. However, only a few countries use it today (52 countries had proportional elections, 33 majoritarian and nine had a mixed one¹⁰ (Persson, et al., 2003 p. 89)).

¹⁰ The examples are Bolivia, Germany, Hungary, Italy, Japan, Mexico, New Zealand, the Philippines, Russia, Venezuela, the Ukraine.

We can raise the question, which system better represent preferences of the voters. To do this we should consider if the political parties represent the differences of preferences of the electorate. The study of 12 Western European democracies (1976-1998) finds (Ezrow, 2007) that there is:

- the **Voter Distribution Effect Result**, which means that the changes in policy preferences of voters are associated with the changes in policy programmes of the political parties,
- the **Electoral Laws Result**, which states that in proportional electoral systems the variety of partisan ideologies is less linked with the voters' preferences than in non-proportional systems (esp. where the "winner-takes-all").

The study on over 80 countries has shown that "elections in developing countries have cyclical effects on policy", but their structural effect is positive and "frequent elections produce better policy" (Chauvet, et al., 2009 pp. 541-542).

3.7. Term limits: populism or effective change?

In most of the countries, the heads of states have limited possibilities to hold the office for a longer time. These ideas date back to ancient Athens, Sparta, and Rome. They were introduced among other things in order to prevent corruption. Such changes towards limiting the time spent occupying the same post became frequent and normal in many countries. In the United States, since its very beginning the tradition emerged that the president serves only two terms. It was broken by Franklin D. Roosevelt and when he died during his fourth term as a president, the presidential term limits were introduced in 1951 by the 22nd Amendment to the Constitution.

It is not a democracy limitation; quite the opposite—it is its extension. However, while term limits function on top level of politics (e.g. in the case of presidents), it is not so common in the parliaments or at local levels.

There are three countries, where limiting the number of parliamentarians' terms is functioning:

- **Costa Rica:** the rotation-style term limits were introduced in 1949. Parliamentarian can hold an office for unlimited number of terms; however, these terms cannot follow one after another.
- **Mexico:** the limitation to one term functioned in years 1994-2014. Recently, in the Lower House it was raised to 3 three-year terms, while in the Upper House to 2 six-year terms. The limit was increased because of the politicians learning their job too long, what affected their effectiveness. In addition, the increased rotation of parliamentarians caused that instead of voting for people, voters were persuaded by promises.
- **The United States:** term limits function in 15 states, including the most populated and the richest state of California. Total permitted time of holding the office is 8-16 years (depending on state). These solutions were introduced at the beginning of 1990s. Six

states resigned or did not implement state legislative term limits, because they were overturned or repealed.

The opposite solution may be to allow the legislators stay at the offices without any time limits.

- The institution of the **senator for life** functions in Italy, Congo, Paraguay, and Burundi.
- In a way, similar institution is the House of Lords in the UK. However, the Lords' essential function is a representative one, so their impact on the current policy is negligible.
- In Italy, senators for life are former presidents and up to five persons considered to be particularly deserved. Currently, there are six senators for life, of which two are former presidents. They have altogether 2% of votes; however, their actual position that has been built for the whole life (e.g. media conglomerate of Berlusconi) is stronger.

The introduction of the term limits was the most significant institutional change in the U.S. since 1970s. It was the largest 'natural experiment' in this field so far conducted anywhere in the world. The collected empirical experience allows already for some conclusions.

Theoretically, term limits could have many advantages, and some of them seem to be confirmed by observations. Arguments supporting introduction of term limits are as follows:

- They lead to the **development of democracy**, because e.g. thanks to them the age and parliamentarian's views better represent the society:
 - » The number of candidates to the office is increasing; society obtains more opportunities to cast a vote:
 - After imposing the term limits in California in 1990, the number of candidate fillings for the state Senate rose by 25% and for the state Assembly it grew up by more than 50%. (Armor, 1994)
 - In Nebraska in 2006, the number of candidates rose by 51%. (Bend, 2006)
 - » The competition between parties as well as the possibility of changing governing party is increasing.
 - » In a system based on term limits, it is easier for the debutants on the political scene to enter parliament, especially for the younger ones. Voters decide mainly based on candidates' recognition (and not due to their programmes). Persons holding the offices for a longer time have greater chances to show up in media.
 - » Young people receive more chances for carrying their ideas in the term-limited institutions. It is important, because usually they have almost no representation in the parliaments and often politicians, who are holding the office for many years, cannot understand the needs of younger generations.
- The **risk of corruption**, nepotism and self-interest motivated politicians decreases:
 - » Lobbyists and tenured bureaucrats have smaller chances to influence the politicians, because they have less time for creating eventual connections with them (thus lobbyists are less interested in creating them, as well).

- » Already at the early stages of their political careers such candidates drop out as those interested in becoming the professional parliamentarians only to receive long-term financial and social benefits.
- » Politicians would vote more frequently according to their beliefs, and not just to gain support before the next elections or to ingratiate them with party superiors.
- » Politicians are not exposed to the temptation of enforcing controversial, spectacular and nothing-giving projects, which are mainly aimed at drawing attention to get popularity rather than solving the real problems. "...a term-limited incumbent places less value on reputation-building than an incumbent eligible for re-election does" (Johnson, et al., 2004)
- The **functioning** of the authorities improves:
The case of California is often recalled: "Prior to term limits, California's state legislature was referred to as a political geriatric ward. Now, California has gone so far as to pass state budgets on time. (...) In many instances, the loss of institutional memory, legislative knowledge and political experience has fostered a more energetic and more effective deliberative body." (Basham, 2004)
 - » Generally, it is considered that during the second term a member of the parliament does little. However, it is not the case if he/she plans any public career in the future.
 - » There may be a relation between term limits and the rate of enactment of the bills (Basham, 2004) (i.e., the percentage of bills introduced that are enacted into law). The states with term limits: Michigan 69%, Ohio 52%, and California enacted 41% of introduced bills, while in the states of unlimited number of terms it ranged from 2.7% to 8.6% only (Illinois, Wisconsin, Pennsylvania, Massachusetts, New York, and New Jersey) (Creelan, et al., 2004 p. 38). This may suggest that the legislators whose number of terms is limited do not waste time so much and are more effective.
- The size of the state and **public spending** decreases:
 - » The longer a person stays in office, the more he/she supports the increase of public spending. (Payne, 1991) It is one of the most influential arguments for term-limits supporters. However, "...congressional tenure (number of term served) has a minor effect on spending decisions (...) Payne rejects the pork-barrel theory of congressional elections..." (Mann, 1994 p. 86)
 - » Introduction of term-limited provincial governors (and rotation of them) in China had positive impact on local economic growth. (Zhang, et al., 2008)
 - » In countries, where terms are limited to two consecutive terms, it has been found that government does not grow as quickly as in countries with single-term rule (Johnson, et al., 2004).

However, there are also many scientific **empirical research results** that do not support the introduction of term limits:

- Political idealism and the risk of corruption:

- » Especially against are obviously some politicians, but also interest groups (corporations) that can profit from politicians' involvement in economic activity.
- » However, the number of lobbyists increases and they work harder, because their ties have been broken and new legislators are suspicious. (Mooney, 2007)
- » Term limits can exacerbate the populist bias in policies (i.e. ideological shirking occurs). (Acemoglu, et al., 2011) "several studies find evidence of increased ideological shirking in the presence of term limits" (Yakovlev, et al., 2012 p. 4)
- » "Adoption of term limit measures has done little to reduce the influence on the political process of special interests and sophisticated political contributors." (Huefner, 2004 p. 427)
- Share of women:
 - » Establishing term limits for legislators is not as effective as it was hoped. Term limits have not increased the number of women legislators and some of the research shows a loss of seats for women (Stambough, et al., 2009)
 - » "Term limits alone are not enough to increase the number of female elected leaders". (Carroll, 2001)
- Organisational efficiency of intuitions:
 - » "By reducing legislative experience, changing legislative incentives, and weakening the control of legislative leaders, term limits have made legislators more hurried and aggressive." (Kurtz, et al., 2007 p. 8)
 - » The loss of institutional memory and the necessity of learning by new members are underlined, as well. Trainings for new legislators are an imperative in term-limited legislatures. (Kurtz, et al., 2007 p. 8)
 - » Term limits do not prevent careerism; transient career politicians may use the legislative office for further political advancement.
- The influence on public finance:
 - » "the short-term fiscal outlooks and loss of experienced legislators produced by term-limit turnover lead to poor fiscal conditions. Myopic legislators may avoid tough fiscal decisions, while inexperienced legislators may be ill-equipped to develop sound fiscal policy. (...) legislative turnover decreases budget balances", however only in the lower chamber, "perhaps because state senates have more experienced legislators than the lower chamber." (Cummins, 2013)
 - » Some research show that the adoption of term limits had the unintended, surprising consequence of increasing spending levels:
 - Usually democratic term-limited governors tax and spend more (Basley, et al., 1995). Others find that it is a pattern of all the governors who are term limited—they spend considerably more money, on average, than governors who are not. (Klepetar, 2011 p. 83)
 - The study based on 48 states from 1977 to 2001 finds that states with term limits have higher spending levels than states without term limits. (Erler, 2007)

- The study based on panel of 47 states from 1972 to 2005 shows that the pork-barrel money goes however not to welfare, education, transportation, or health, but to local governments, where the legislators came from. (Yakovlev, et al., 2012)
- However, the detailed results depend of the specific institution that has been analysed. “Legislative term limits do not significantly increase (or decrease) state expenditures on average, except when the concept is broken out and applied to each chamber of the state legislature independently.” (Klepetar, 2011 p. 84)
- » “Short-termism” in decision-making is visible while politicians whose time at office is limited favour short-term policy solutions. (Garri, 2010)

Some authors provide more neutral findings, like those that were collected in a comprehensive book edited by Kurtz:

- “...term limits have weakened legislatures institutionally, especially in states with strict limits that had more professionalized legislatures and low turnover in the membership. However, due to natural and planned adaptations, the consequences have not been as dire as they might have been.” (Kurtz, et al., 2007)
- „The impact of term limits on legislatures is greatly affected by two factors: the degree of professionalization of the legislature and the restrictiveness of the term limit.” (Kurtz, et al., 2007 p. 3)

Thus, the institutional reforms need to be carefully designed, taking into account different chambers of the legislature.

Summarising: there were high hopes that the term limits on lower policy levels like e.g. within state legislature will have a positive impact. Theoretically, it should have worked out well. However, the verification of the implemented solutions does not provide such optimistic results.

...term limits are not delivering all that was promised, especially in diversifying our elected representatives and reducing the influence of campaign financing on state legislative processes.

(Huefner, 2004 p. 492)

Moreover, the introduction of term limits sometimes gives results that are contrary to the expectations or—finally—may be partly harmful for the economy.

Ironically, it appears that term limits create outcomes that are often opposite of what their proponents hope to achieve.

(Yakovlev, et al., 2012 p. 5)

We should, however, remember that the vast majority of research conducted so far was based on U.S. examples (probably, there is only one study conducted so far on any other sample) and that the results are country-specific (while analysing particular states or chambers).

Chapter 4

Politics and social needs

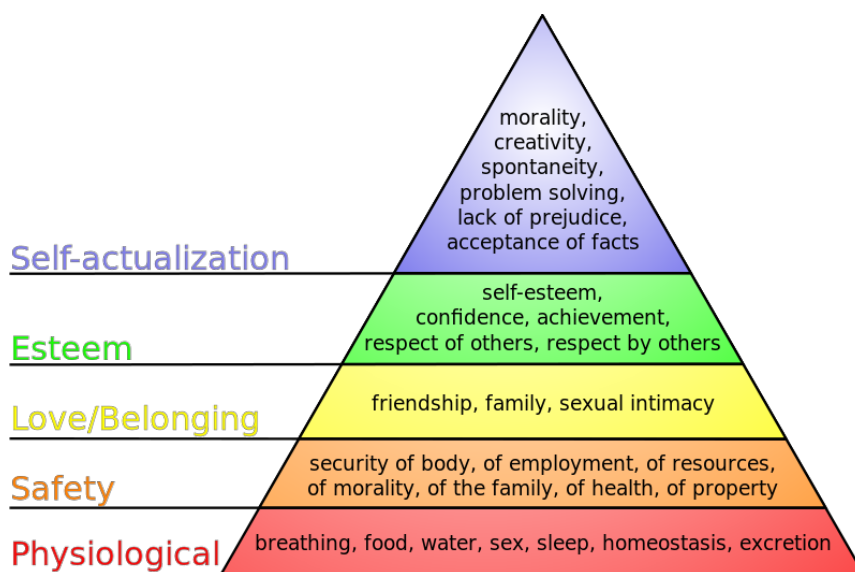
In this chapter, we will focus on needs in order to introduce the reader to the issues of answering them by politicians.

4.1. Human needs and economic development

One of the objectives of economic policy may be that politicians realize the objectives of the society. Below, we reflect on what could be their targets.

Let us start from the concept of the basic needs of people. They were described by Abraham Maslow, an American psychologist in his famous concept of the hierarchy of needs. According to this mode, low-level needs, fundamental for biological survival, must be satisfied before higher-level, non-material needs are pursued.

Figure 23. Diagram of Maslow's hierarchy of needs



Source: (Finkelstein, 2006).

Part of human needs was considered so basic that they have been included in The Universal Declaration of Human Rights. We can enumerate a few of them, e.g.:

- Rights to dignity, liberty, equality, and brotherhood.
- Right to life, freedom, justice.
- Rights to spiritual, public, and political freedoms (e.g. freedom of association, thought, conscience, and religion).
- There are also social, economic, and cultural rights (including the right to social security, the right to adequate a standard of living).

Box 11. Selected social and economic human rights

Article 22.

- Everyone, as a member of society, has the right to social security...

Article 23.

- (1) Everyone has the right to work, to free choice of employment, to just and favourable conditions of work and to protection against unemployment.
- (2) Everyone (...) has the right to equal pay for equal work.
- (3) Everyone who works has the right to just and favourable remuneration ensuring for himself and his family an existence worthy of human dignity, and supplemented, if necessary, by other means of social protection.

Article 24.

- Everyone has the right to rest and leisure, including reasonable limitation of working hours and periodic holidays with pay.

Article 25.

- (1) Everyone has the right to a standard of living adequate for the health and well-being of himself and of his family, including food, clothing, housing and medical care and necessary social services, and the right to security in the event of unemployment, sickness, disability, widowhood, old age or other lack of livelihood in circumstances beyond his control.

Article 26.

- (1) Everyone has the right to education. Education shall be free, at least in the elementary and fundamental stages. Elementary education shall be compulsory (...)
- (3) Parents have a prior right to choose the kind of education that shall be given to their children.

Source: (United Nations, 1948).

These human needs have certain objectives reflected in social and economic policies. The fields of economics, which takes into account the need to achieve these goals, include development economics. It focuses not so much on conventional macroeconomic indicators

(or more precisely: stabilization ones), but takes into account more social objectives, e.g. inequalities of income. In democratic societies, one of the objectives of economic and social policy is not only the enrichment of society as a whole, but such an enrichment, which would be considered by the majority of the population (which choose politicians as their representatives) as fair. Frequently, therefore, it is believed that excessive income inequalities are not fair, and in consequence, one of the objectives of social policy becomes their elimination, or at least their reduction.

It can be assumed that the objective of economic policy should be the development. However, the development of what? Development economics has shown that not of the economy itself, but the development should have an impact on the improvement of society's quality of life in various breakdowns, depending of its preferences. Hence, a few decades ago the **Three Basic components** (or core values) of development have been enumerated (Goulet, 1971):

- **life-sustenance:** provision of Basic Needs, such as housing, clothing, food and minimal education;
- **self-esteem:** feeling of self-respect and independence; to eradicate the feeling of dominance and dependence (from economic point of view);
- **freedom:** opportunities of choice of own destiny of people not limited by the lack of education or skills.

These ideas, as we have seen, had its origins in the concepts of Maslow. They were further developed in the coming years. For example, the **Vision of development of Amartya Sen**, the Nobel Prize winner in 1998, is that development is an expansion of:

- **entitlements**—‘the set of alternative commodity bundles that a person can command’; they generate the capability to do certain things, e.g. to sell their labour and to purchase goods,
- **capabilities**,
- **freedom**, e.g. from famine, undernourishment, poor health and lack of basic needs; lack of political liberty and basic civil rights, and economic insecurity.

Sen has developed the ‘capability approach’ notion and defined it as follows:

“capability approach” sees human life as a set of “doings and beings”—we may call them “functionings”—and it relates the evaluation of the quality of life to the assessment of the capability to function. (...) The roots of the approach go back at least to Adam Smith and Karl Marx, and indeed to Aristotle.

(Sen, 1989 p. 43)

Moreover, as Sen explains the meaning of “capabilities”:

The capability of a person is a derived notion. It reflects the various combinations of functionings (doings and beings) he or she can achieve. It takes a certain view of living as a combination of various “doings and beings”. Capability reflects a person’s freedom to choose between different ways of living.

(Sen, 1989 p. 44)

According to Sen, human development is

‘our capability to lead the kind of lives we have reason to value’

(Sen, 1999),

and not e.g. GDP per capita growth or other, typical macroeconomic indicators.

Sen emphasised “freedom” as both the primary end and the mean of development. According to him, there are five main dimensions of freedom:

- political freedoms,
- economic facilities,
- social opportunities,
- transparency guarantees, and
- protective security.

What Sen has introduced to economics is the break in the cause-effect relationship. Previously, the reasoning was simple: **first economic growth then social welfare** will come. This concept was introduced by W.W. Rostow in 1960 in his ‘stage’ theory of development. (Rostow, 1960)

However, the example of many developing countries shows that it is difficult in a contemporary world to focus only on economic growth leaving e.g. education, health, life expectancy behind, as not so much important goals of public policy. Moreover, empirical findings of dozens of countries show that **it is actually possible to have economic growth and social development at the same time**. Sen argues that the growth of GDP per capita does not have to lead to the increase of welfare of the society; it does not have to influence e.g. life expectancy. He also did not agree with the “Lee thesis”.

Sen’s approach can be criticized because:

- it bases on individualism, gives priority to individual preferences rather than favouring society, as a whole;
- it promotes liberalisation, despite in some cases the opposite economic policy occurred to be successful;
- it does not base on historical findings and is biased towards Western set of values, without appreciating some successful Asian examples. (O’Hearn, 2009)

Such broadly defined Sen’s terms meet problems with their operationalisation, e.g. measurement. For instance, how to measure entitlements? Thus, a challenge for development economics was to formulate economic theory, which can be adapted in practice in order to ensure development. The comprehensive practical theory of economic development based on freedom was not created (and implemented in public policies), however it influenced other scholars and ideas.

Box 12. The 'Lee thesis'—the case of freedom in Singapore

According to Lee Kuan Yew, the founding father of independent Singapore and its prime minister holding his office for more than three decades, it is justified to limit freedom if that can positively influence economic growth and development. Singapore is a very liberal country; for many it occupies the first positions in the “Doing business” annual reports.

For instance, the procedures of starting a business locates this country on the 10th position in the world: “starting a business there requires 3.00 procedures, takes 2.50 days, costs 0.60% of income per capita and requires paid-in minimum capital of 0.00% of income per capita” (The World Bank, 2015 p. 17). It is however not entirely true, because the company actually does not need a company seal to operate and it is not necessary at the beginning to sign up for Employee Compensation Insurance at an insurance agency. Thus, total time for registration takes only a couple of hours and may be performed fully online (what the author of this book has confirmed personally, while registering his company there).

However, the other kinds of freedom but economic ones are much limited compared to the most of developed countries. For instance, the country is recognised as:

- “partly free” only by the Freedom House (Freedom House, 2015) in terms of political rights and civil liberties, and
- is in “difficult situation” (or simply “not free”) occupying as far as the 148th position (together e.g. with Afghanistan) in the world measured by the Press Freedom Index (Freedom House, 2015a).

However, the society seems to agree with it and appreciates the fast economic development of this country. Thanks to it, the life expectancy in Singapore is the longest among all the countries of the world (recently, Singapore outpaced Japan, who was the world leader for many years). However, first the governments (of the same party—as it rules the country since its beginnings some 50 years ago) focused on economic situation, rather than on political freedoms or on social issues.

4.2. Measurement of development

The ideas of Goulet continued by Sen influenced the creation of the Human Development Index. It was developed by Pakistani economist Mahbub ul Haq in 1990 leading a group of internationally recognized development economists supported also by Amartya Sen. They tried to assess various dimensions of the ‘human’ development with one indicator only. The United Nations Development Programme (UNDP) publishes annual reports with the values of HDI.

HDI does not include only GDP per capita, but also two other issues, which were recognised as the most important in human's life: long life and education (see Box 13.).

Box 13. HDI formula and other HDI-related indices

The HDI is a geometric mean of three indices: life expectancy, education, and income and is calculated (since 2010) using the formula:

$$HDI = \sqrt[3]{\frac{LE - 20}{85 - 20} \cdot \frac{\frac{MYS}{15} + \frac{EYS}{18}}{2} \cdot \frac{\ln(GNIpc) - \ln(100)}{\ln(75000) - \ln(100)}}$$

where:

LE—life expectancy at birth,

MYS—mean years of schooling,

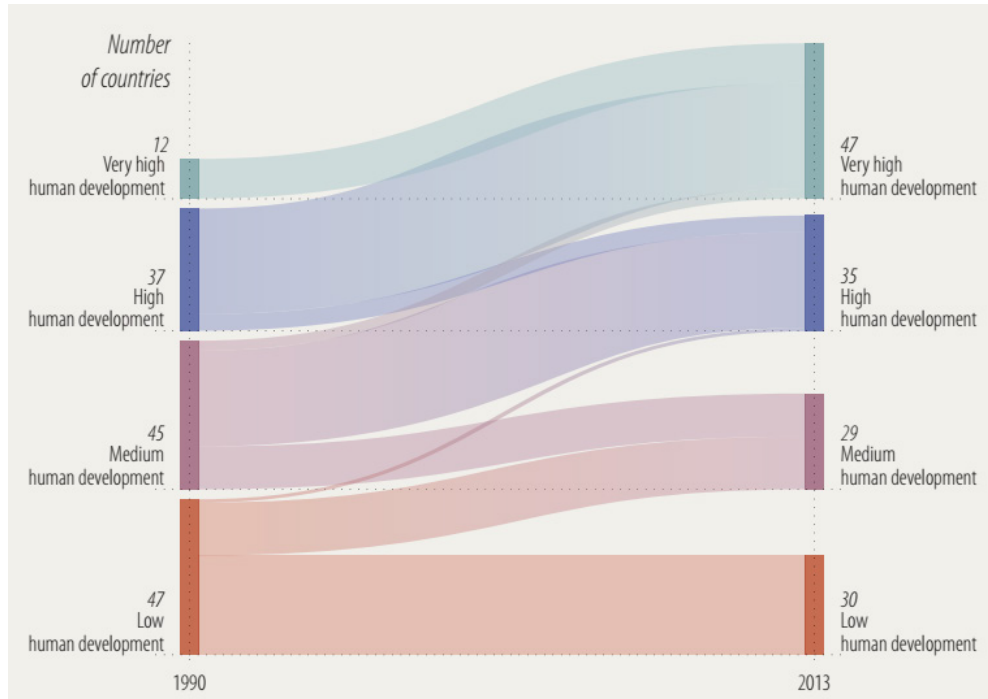
EYS—expected years of schooling,

GNIpc—Gross National Income at PPP per capita.

In 2010, the Inequality-adjusted Human Development Index (IHDI) was introduced. It takes into account also inequalities. For example, the United States are on the 3rd place in the world in HDI, but 13th position in IHDI in 2013. Two first countries in both rankings are Norway and Australia.

A “gender-sensitive extension of the HDI” is the Gender-related Development Index (GDI) introduced in 1995 together with the Gender Empowerment Measure (GEM). In 2010, UNDP introduced the Gender Inequality Index (GII), which replaced FDI and GEM. GII covers three dimensions: reproductive health, empowerment, and labour market participation. Top three countries are Norway, Australia, and Switzerland.

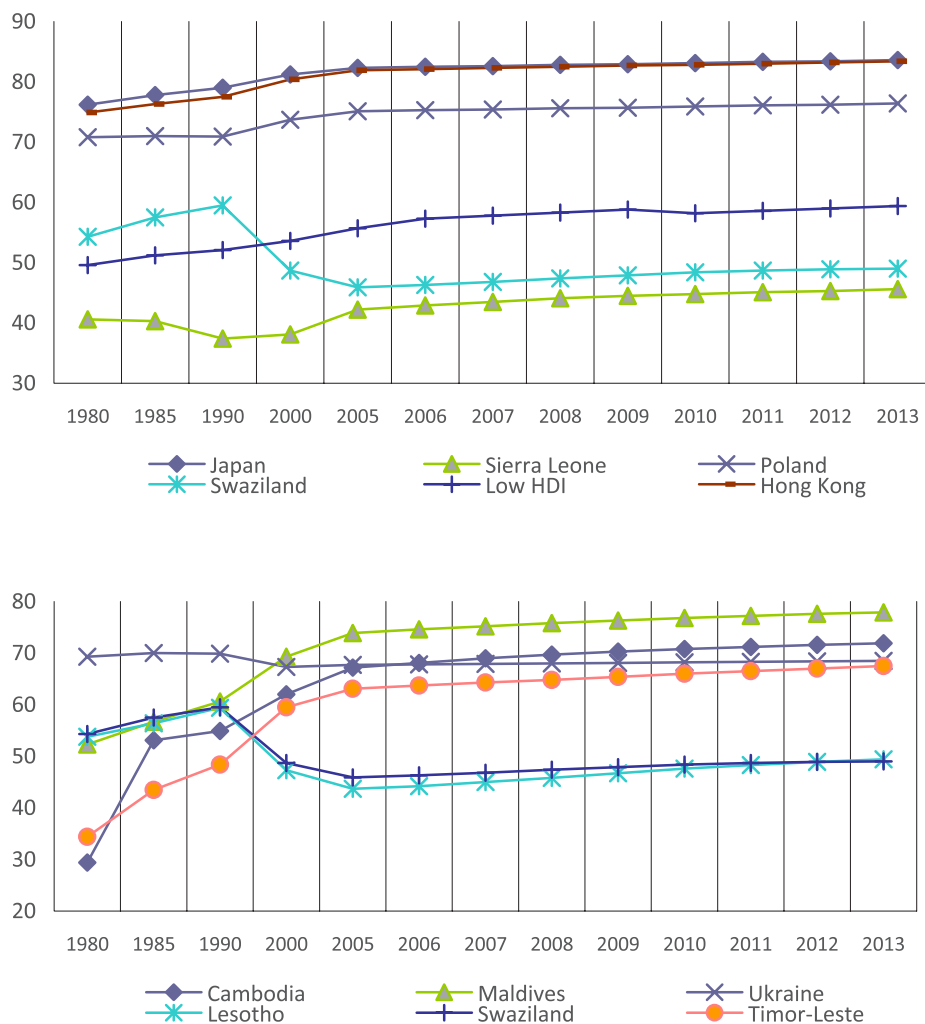
The world is constantly improving the average situation of people. There are however some differences: while for instance China has moved from low human development countries in 1990 to the group of high human development countries, 30 low-developed countries remained in that group. The situation has improved especially between East and Central Asia as well as in Europe, while huge problems are still in some Arab States and in Sub-Saharan Africa.

Figure 24. Progress to higher human development groups since 1990

Source: (United Nations Development Programme, 2014 p. 36)

The longest life expectancy in 2013 was in Japan (83.6 years) and in Hong Kong (83.4), while the shortest one is in Sierra Leone (45.6) and Swaziland (49). The largest progress within 33 years was done in Cambodia (expected life has increased by 42.5 years!), in East Timor (33.1), in Maldives (25.6), and in Bhutan (23.3), while in Swaziland it decreased by 5.3 years, in Lesotho by 4.4 years and at Ukraine by 0.8 years (the next country was Belarus).

Figure 25. Life expectancy and its changes between 1980 and 2003 in selected countries



Note: the upper graph shows two countries with the highest and the lowest life expectancy, Poland and low human developed countries. The lower graph shows three countries with the highest and the lowest progress in life expectancy since 1980. The scale on the vertical axes is slightly different.

Source: (United Nations Development Programme, 2013) and own counts based on it.

One of the goals of humans is to enjoy a happy life. For years it was mainly a subject of studies of psychologists, however later also economists have joined them. **The Easterlin Paradox** is an important starting point for research in the area of relations between welfare and happiness. It was discovered in mid-1970s by the economist Richard Easterlin and states that people's average life satisfaction did not seem to depend on their incomes. It is

not surprising however, for behavioural economists who easily explain it with the notion of the “framing effect”.

Since that time, more economists became interested in finding indicators of wellbeing better than e.g. GDP per capita only. Thus, the HDI was created, the Happy Planet Index, the World Database of Happiness, the General Social Survey in the US, the British Household Panel Survey, the Socio-oekonomisches Panel in Germany, Happiness Index in South Korea and in Dubai, to name a few. In addition, despite ‘**money cannot buy happiness**’, it provides better life quality, including health, education, clothing, housing, food etc. (Weimann, et al., 2015)

Box 14. Bhutan—happiness as a public policy ultimate goal

An interesting and intriguing departure from traditional macroeconomic indicators may be the Gross National Happiness Index (GNH) used in Bhutan. It consists of 33 indicators.

In GNH, material well-being is important but it is also important to enjoy sufficient well-being in things like community, culture, governance, knowledge and wisdom, health, spirituality and psychological welfare, a balanced use of time, and harmony with the environment.

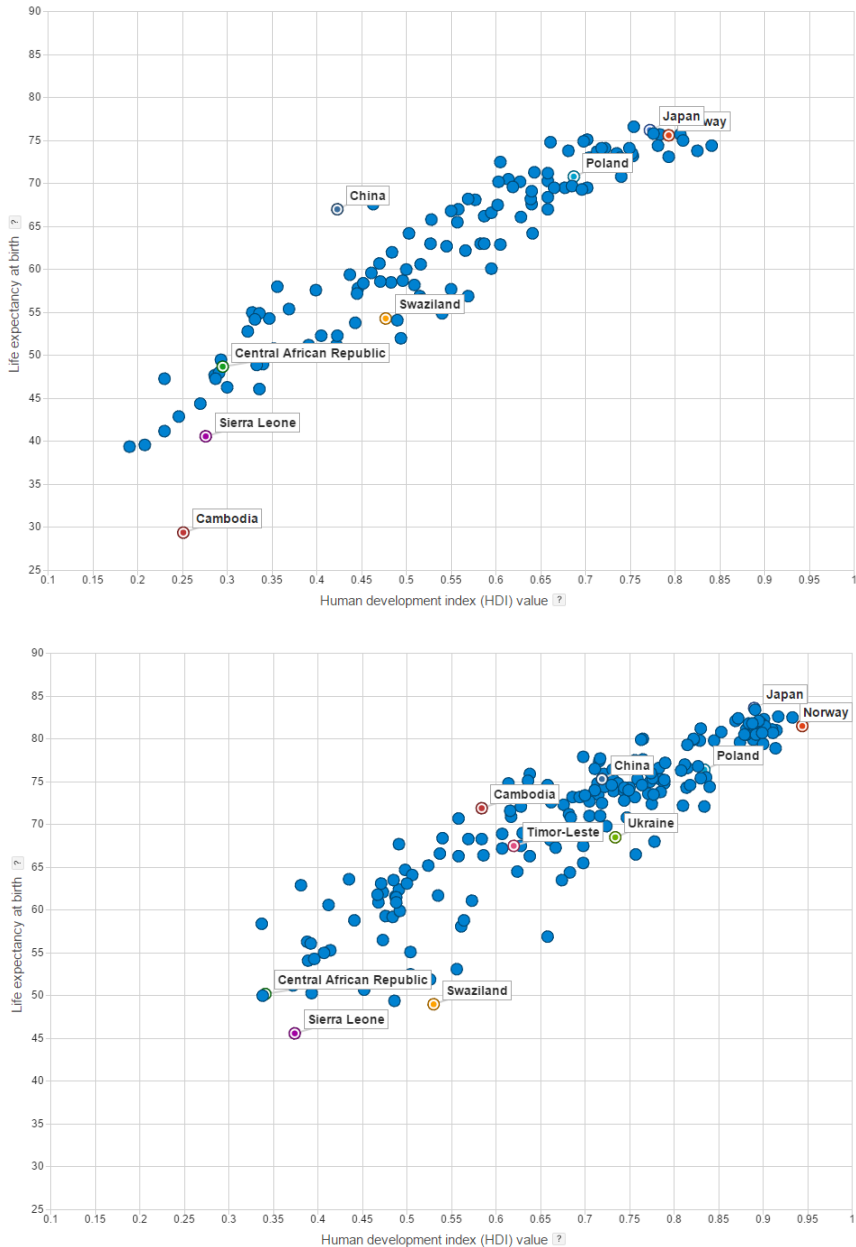
(The Centre for Bhutan Studies and GNH Research, 2015)

The values of indicators are obtained through a representative survey of the society conducted under the auspices of the GNH Commission—a governmental agency established in 2008 (and replaced the previous Planning Commission). The Commission is the central government body responsible for coordination and formulation public policy, including 20-year development strategy and five-year plans. The results show the progress in happiness and that society is generally happy (only c. 9% is unhappy).

The Index reflects more broader interests of first psychologists and then economists, as well, to study happiness-economic relations. This field is also analysed by behavioural economics.

Obviously, there is some causality between income and long life: it is easier to live longer in rich countries, thus the HDI does not include the independent variables only, as it is usually required in similar approaches based on composite indicators. Thus, however, it does not influence the overall conclusions that different components of HDI, like especially the life expectancy, and of course, the HDI itself have improved over the last three decades.

Figure 26. Life expectancy and HDI values in 1980 and in 2003 in all the countries



Note: Higher graph shows the data for the year 1980, and the lower one—2003. Data from Human Development Report 2014, United Nations Development Programme, Last updated: Jul 21, 2014.

Source: (Google, 2015).

4.3. Public choice theory on beneficiaries of economic policy

Once we know what the people's needs are and once we know how to measure some of them, we should say that policy is also an art of choosing the goals (and the means to fulfil them). Thus, running the economic and social policy is not an easy task. Especially, if we remember that policymakers can try to provide benefits to:

- the whole society (e.g. through regulatory policy, which the German calls *Ordnungspolitik*),
- the selected groups of citizens (voters) (see the concept of *Prozesspolitik*),
- politicians themselves.

We should however remember that although economic (or human) development is important, there is a threat of populism when politicians use such arguments that they promote development actually to fulfil their own interests. They can use economic policy tools to meet social goals, at least officially, but in practice, they can maximise their own, opportunistic goals. This is a threat for development and thus the opposition in a democratic system can play a huge role. Without it, another solution could be adopted like the one that functioned in Singapore, i.e. meritocracy.

The society is not consisted of indistinct members. There are various groups: of interests, lobbies, trade unions, supporters of certain political parties. There are people paid with public money (clerks, soldiers etc.), disabled and retired persons, entrepreneurs (and startups), employees of corporations, homeless etc. All of them may have different **social welfare functions**, thus in order to maximise their preferences different public policies should be adopted. It is sometimes impossible to do this at the same time, while some interests of groups of people are contradictory. Thus, **economic and social policies are not aimed at maximising the social welfare function** of the whole society (as e.g. Tinbergen has seen it), as it used to be usually assumed by conventional mainstream economics and by the normative theory of economic policy. Instead, policymakers have to choose the groups they would favour (recall here the definitions of politics).

Interest group theory sees government actions as a response to the interests shared by groups of individuals. It was formulated by the **public choice school** in 1950s. It examines the formation of institutions in the political arena. The theory of public choice includes, for example:

- The issues of voting (efficiency of the voting market).
- The choices made in democratic system (in direct and indirect democracies).
- The theories of social contract and constitutional order (constitutional economics, the economic effects of citizens' rights).
- Economic theory of power (including the theory of economic regulation, the theory of public finance, the role of ideology or party coalitions, and the economic behaviour of judges).
- The theory of interest groups and of distributive coalitions (the impact of interest groups on the efficiency of the economy, lobbying).

- The theory of rent-seeking (political rent and its impact on well-being).

The beginnings of this school are associated with:

- Duncan **Black**, who first in 1947 (and later in 1958) has formulated the first view on the **median voter theory** (Black, 1958). A median voter is a person with an equal number of votes on either of sides. He decides about the choice that is made and it does not have to give the best results for the whole society (but to himself). In result, a majority rule that is usually adopted in democratic systems will provide solutions that are preferred by the median voter. **Principle of the median voter** states that this voter determines the outcome of an elections governed by majority rule.
- Anthony **Downs**, who continued Black's earlier works for voting in committees and applied them in 1957 to electoral competition (Downs, 1957). He has shown that in two-party systems both parties try to make their views closer to each other while in multi-party systems they diversify their programmes and try to be as distinct from each other as possible.
- Kenneth J. **Arrow**, who in 1951 has formulated the "General Possibility Theorem". It is also called **Arrow's impossibility theorem**. It states that if voters have three or more alternatives, then it is impossible to meet three pre-specified criteria (all preferences of all voters are allowed, there is no 'dictator' that dominates voting, and there is Pareto efficiency) and to create a voting system that can convert individual preferences to a community-wide ranking. In result, the voting paradox appears due to which majority voting may not give expected outcome (Arrow, 1951).
- James M. **Buchanan** and Gordon **Tullock** in 1962 formulated the basic principles of public choice theory, using e.g. the Pareto optimality concept (Buchanan, et al., 1962). They concluded that the decisions where large external costs are involved should not be done with a single majority rule but at least with the supermajority one.
- Mancur **Olson**, whose book published in 1965, was one of the milestones of the public choice theory due to e.g. stressing the importance of **free-riders** in voting outcomes: in any community attempting to undertake collective actions to provide **public goods** there will be people who want to take advantage of the non-excludability of using of public goods. He also theorized that despite small social groups might share common views and interests; **larger organisations** do not care about the officially declared objectives unless its members are **motivated with their personal gains**. The book has changed the views on efficiency of democracy and minority-majority relations (Olson, 1965).

Other famous economists of this stream of economics are e.g. Becker, Niskanen, Peltzman, Stigler, Tollison. The theory was very appreciated by the Nobel Prize committee and the award was given to several scholars, including James M. Buchanan (1986), George Stigler (1982), Gary Becker (1992), Vernon Smith (2002) and Elinor Ostrom (2009).

The public choice theory contradicted the Keynesian theory, which focused on **market failures**. Public choice studied the issues of the **government failures**, including the eco-

conomic policy mistakes. **Contrary to the normative theory of economic policy, the positive approach emphasises that there are no universal goals in the practice of economic policy-making, because each time they depend on political choices.** Thus, the **goals of economic policy are established by the governments.** Moreover, if so, there can be among them **opportunistic goals** of politicians that want to be re-elected. In order to achieve this, they can use all available instruments of economic policy basing on their own preferences, without even trying to maximise “social welfare function”.

The development of public choice theory was justified also by the growth of public sector in many countries that has started exposing the economy to larger risks coming from the decisions of politicians and bureaucrats, and not of the markets themselves. When the share of budgetary revenues a century ago was typically circa 10% of GDP, nowadays it is on average more than 40% and in some countries over 50%.

Table 6. Total general government revenue (% GDP), selected countries, 1995–2014

	1995	2000	2005	2010	2014
Belgium	47,9	49,0	48,9	49,3	52,0
Bulgaria	34,0	40,6	37,8	33,4	36,3
Czech Republic	39,4	36,9	38,7	38,6	40,6
Denmark	54,9	54,6	56,2	54,3	58,4
Germany	45,2	45,6	42,8	43,0	44,6
Estonia	42,1	36,3	35,1	40,7	38,7
Ireland	38,7	35,8	34,7	33,3	34,4
Greece				41,3	46,4
Spain	37,3	38,1	39,5	36,2	38,6
France	49,1	49,8	49,7	49,6	53,6
Croatia			41,6	41,3	42,6
Italy	44,5	44,2	43,0	45,6	48,2
Cyprus	30,1	32,2	37,1	37,5	40,4
Latvia	34,2	34,5	33,8	36,2	35,6
Lithuania	33,0	36,2	33,7	35,4	34,1
Luxembourg	43,0	42,1	42,7	43,4	43,8
Hungary	46,7	44,2	41,7	45,0	47,4
Malta	35,7	34,7	39,6	37,9	41,9
Netherlands	45,1	43,6	42,1	43,2	43,9
Austria	49,3	48,3	48,5	48,3	50,0
Poland	43,5	39,0	40,5	38,1	38,8
Portugal	37,4	39,4	40,5	40,6	44,5
Romania	32,1	33,8	32,3	32,7	33,5
Slovenia	43,9	42,5	43,6	43,6	44,8
Slovakia	44,8	40,0	36,7	34,5	38,9
Finland	55,1	54,9	51,9	52,1	54,9
Sweden	56,5	56,8	54,5	51,1	50,1

United Kingdom	36,2	39,0	39,2	39,1	38,2
Iceland		42,6	45,9	39,6	45,6
Norway	53,4	57,1	56,9	56,0	54,7
Switzerland	32,0	33,7	32,8	33,3	33,5

Source: Eurostat.

Traditional economics tends to focus on the functioning of enterprises and households or markets, and not on the government. However, it is the government that has a decisive role in shaping the business activity, influence the economic conditions—even periodically, and therefore modifying the usual course of business cycles (see further: political business cycle).

The bureaucracy may not be interested in their contribution to maximizing the welfare functions of the society, but in maximizing their own budget and authority and that is its rational behaviour. This was William Arthur **Niskanen's** findings expressed by the **budget-maximizing model** (Niskanen, 1971). The governments' shares in economy increase and the following social efficiency of public expenditures decreases, because of the **activities of bureaucrats**. Heads of the departments of public administration are interested in **maximising the department's budgets**, the position and influence it brings. Thus, the bureaucracy is interested in providing as many services as possible to justify their existence and growing needs what would enable them to grow in power. The administration grows up until legislator (supervising it) would notice its (too large) size and the costs associated with it. From this point of view, departments of administration may be treated similarly to other interest groups in their attempts to maximise their needs.

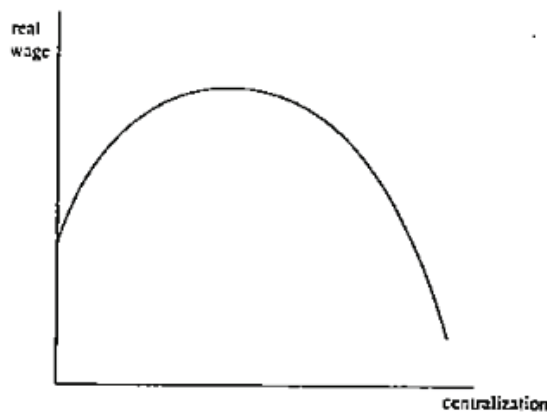
Olson has later analysed economic growth in various countries after World War II. He came to the conclusion that countries, which temporarily **decreased the activeness of interest groups** (cartels, lobbies (e.g. cotton-farmers, steel-producers), labour unions, professional associations, guilds, castes, social classes etc.) in public spheres and where important political changes took place (e.g. Germany or Japan), **developed faster** than the others (e.g. the UK). He has observed (Olson, 1982) a **negative correlation between the duration of political stability** (which is associated with an increased influence of interest groups on economic policy) **and growth**. The interest groups promote primarily their own welfare and can use to satisfy their needs e.g. oligopolies, favourable regulations, tariffs and restrictions on trade, subsidies etc., what hurts the economic growth (Behrman, 1983). Larger groups (e.g. a political party or confederation of industries of labour unions) are more interested in **general policy attitudes**, widespread government intervention, while smaller groups favour **selective interventions** (to individual companies or industries).

That can remind previous works of W. **Eucken**, according to whom the domination of any structures and organizations in the economy (companies, labour unions, or politicians) is dangerous for it as well as for the society. Thus, the policy of social order (*Ordnungspolitik*) should be designed and introduced.

Box 15. Unions' coordination and labour market: Calmfors–Driffill hypothesis

Olson's works influenced other economists and led e.g. to formulation of the **Calmfors–Driffill hypothesis** (Calmfors, et al., 1988). According to it, there is the non-monotonic relationship ('inverted U' shape) between a measure of unions' coordination and unemployment: highly coordinated or centralized bargaining would lead to wage restraint and low unemployment. If the position of labour unions start from zero unemployment increases and later it decreases when they start exercising their monopoly power.

Figure 27. The hump-shape hypothesis of Calmfors and Driffill



Source: (Calmfors, et al., 1988 p. 15)

The authors however have adopted a simple bivariate relationship and omitted other factors such as openness, and the effects of the macroeconomic policy context on wage setting. (Driffill, 2005)

Another Nobel Prize in economic laureate Gary **Becker** has coined “A Theory of Competition Among Pressure Groups for Political Influence” (Becker, 1983). His model was based on assumption that society is divided into two groups:

- those that want to lower taxes,
- those that want to preserve or increase transfers.

All actors maximize their utility based on their incomes. His conclusions are as follows:

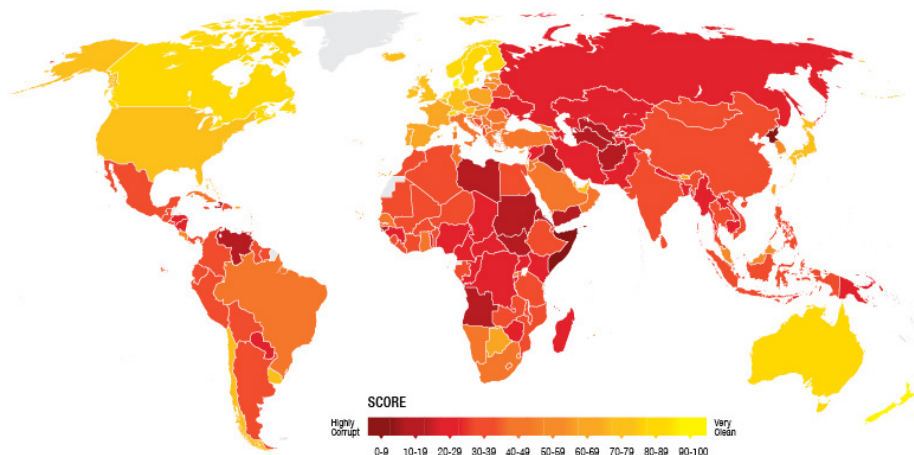
- The effectiveness of groups of interest in competing for higher subsidies (or smaller taxes) depends on the relative pressure mounted by the group on the government.
- The increase in unnecessary social losses (**deadweight loss**) diminishes the size of transfers in the equilibrium point. This is caused by the fact that the subsidised group

decreases pressure when transfers increase, while another group puts more pressure together with the increase of such losses.

- While the profits to the subsidised ('predatory') group increase linearly, the dead-weight losses to another ('victim') group are proportional to the square of the tax, what motivates it to intensification of their efforts to minimize the negative effects on their welfare.
- Thus, the competition between both interest groups increases the effectiveness of economic policy, what leads also to an increase in the effectiveness of taxation system.

Bureaucrats and political parties but also interest groups can try to satisfy their needs also through some illegal actions. They are **rent-seekers**. So far, we have studied the political corruption only. The interest groups may influence the government using voting, personal contacts, corruption, and promises to politicians and bureaucrats of their further careers after quitting the job at public sector (Grossman, et al., 1991). Usually it is believed that it is an obstacle to growth. Weak legal system leads to the asymmetry of information concerning the hidden price for incumbent's services what increases transaction costs, as well—to name just a few effects connected with **corruption**. Furthermore, corruption may degenerate the democracy. Wealthier countries are perceived to have lower corruption while it is higher in poorer countries (and they can be poor for a longer time because of corruption). Thus, it is a reason and a cause of poverty. However, corruption is not limited to the third world countries only.

Figure 28. Corruption Perceptions Index 2014



Source: (Transparency International).

One of the most well-known institutions assessing this problem is the **Transparency International**. As it writes:

Based on expert opinion from around the world, the Corruption Perceptions Index measures the perceived levels of public sector corruption worldwide...

(Transparency International)

For many years among the most transparent countries are the Scandinavian ones, New Zealand, Switzerland, Singapore, the Benelux countries. To the group of most corrupted countries belong some African ones, North Korea, Iraq, Afghanistan, Uzbekistan, and Turkmenistan.

4.4. The behaviour of voters

Some other effects connected with decision making that affects electoral outcome and furthermore the economic policy run thereafter are:

- swing voter and
- voter apathy.

A **swing voter**, called also a floating voter, is a person who can change its decision concerning a political party he/she votes for. Swing voters can be close to median voters and take the central position on the political market scene. Because their electoral decisions are not strongly ideologically motivated, they are especially vulnerable to pork barrelling because they are more motivated by self-interest. Some of the swing voters can be **first-time voters** or **low-information voters**. Swing voters are also within some commissions or committees. They are also called the **pivotal members** (e.g. of monetary policy councils).

A **voter apathy** occurs when a person is not motivated enough in participation in elections. They can compare the costs of participation in elections with their (marginal) influence in the outcome and can decide not to vote at all. This behaviour is then called a **rational abstention**. Especially younger generation shows the lack of interests in participation in elections. In the US, the turnout of people aged 18 to 24 was just 21% in America's mid-term election in 2010. In the UK, it was 44% (compared to 65% of people of all ages) in 2010 in the same age group. The Liberal Democrats candidate for Mayor of London in 2008 has commented:

Why do politicians tend to look after older people? Because young people don't vote.

Lord Brian Paddick

Politicians of some countries have considered these behaviours as serious enough to introduce a legislation forcing everybody to vote. There are several countries in the world that have introduced **compulsory voting**, including e.g. Argentina, Australia, Brazil, Cyprus, Luxembourg, North Korea, Peru, Singapore. There are also several other countries where compulsory voting is existing in the law, but it is not enforced (e.g. Greece, Egypt, Mexico, Thailand, Turkey).

Box 16. Penalties for absenters

Among 21 countries that introduced compulsory voting, some penalise the citizens who does not vote.

- Australia: the fines are small at the beginning (AU\$20) and rise with repeating absenteeism (up to \$AU50).
- Belgium has the oldest compulsory voting system (introduced in 1892): absenters may receive a moderate fine or, if they do not participate in at least four elections, they can lose the right to vote for 10 years and can have difficulties with getting a job in the public sector.
- Bolivia: those that would not present proofs that they have voted may be forbidden to pay their salary out from the bank.
- Greece: no penalties ever given, but it is more difficult to obtain a new passport or driver's licence.
- Luxembourg: the fine for repeated violations can even reach €1,000.
- Singapore: non-voters lose their electoral rights until they reapply and explain their absenteeism.

In some countries compulsory voting is limited by age (Brazil—70 years, Ecuador—65 years, Paraguay—75, Peru—70). Sometimes people with mental incompetence, illiterates or in military services are exempted.

The Netherlands and Venezuela abandoned compulsory voting:

The last election in which the Dutch were obliged to vote was in 1967. Turnout in the subsequent national poll decreased by around 20%. Venezuela saw a drop in attendance of 30% once compulsion removed, in effect, in 1993.

(Frankal, 2005)

Introduction (or abandonment) of compulsory voting modifies the electoral outcome and may change the partisan structure of the parliament.

Source: (Frankal, 2005), (CIA), (Birch, 2009).

However, the large number of voters does not necessarily mean that this was a good election. More important than simple participation (although it matters for developing a civil society) is reasonable voting, based on analyses of political programmes, with reasoning on the possible economic outcomes of the promises made.

Moreover, the research within the field of **behavioural economics** delivers many proofs that people are not fully rational. Instead, it says that they are “**predictably irrational**”. Behavioural economics study the effects of social factors (emotional, psychological) and their consequences for market prices, returns. It also includes how market decision is made and what drives the **public choice**.

This branch of economics questions one of the basic assumptions of economics concerning human behaviour. It says that people are not *homo economicus*. People are not always self-interested (or rational). They make decisions quickly, instead after long deliberations on the pros and cons of various decision options. People can be motivated with **altruism**, the fear of **rejection**, or **retaliation**, and may be motivated by **reciprocity**—and not only by self-interest, as for the decades the economists assumed in order to operate with simple, solvable optimisation problems.

Real life is not as individualistic, as (neo)classical economists used to thought. People are “**social animals**”, as states the title (i.e. “The Social Animal”) of one of the most famous books of modern psychology, which describes how human minds operate and interact with each other (Aronson, 2007). People make different decisions while being in different context, also the social one. Thus, their **rationality is bounded** and is not full, as it is conventionally assumed.

People are vulnerable to political marketing. Traditionally, politicians wanted to influence mass-media like TV stations, newspapers etc. Recently, the situation has hanged due to the growth of popularity of **social media**, especially among younger generation of voters. Thus, even if they do not know the details of political programmes of the parties, they may know the opinions of their friends and acquaintances and share them. This may help with creation of civil society, as well.

However, politicians have noted these changes and started to be active in social media, as well. Some of them e.g. establish the **Twitter** accounts just before the election time to show that they want to be closer to the people, that they are eager to communicate with the voters. In response, some bottom-up social initiatives (e.g. on **Facebook**) emerges to get people to be aware of such manipulations.

Another interesting change that influences electoral outcome are the “**haters**” and “**internet trolls**”. The freedom of expression of ideas on internet and easiness of doing that encourage some to show their negative feelings on political opponents and their supporters—they are called the “haters”. Some politicians may even higher companies to perform **negative political social media marketing**—hiring the “trolls”.

Box 17. “Troll factory” in Putin’s Russia

In Russia, the “troll factory” (called “trolls from Olgino” after the name of one of the districts of Saint-Petersburg, where it is located) employs about 300 professional social media manipulators having thousands of fake Facebook and Twitter accounts working 24/day in two shifts. It runs pro-Putin’s propaganda (e.g. against NATO, Ukrainian government, political opposition etc.) on different internet forums, in Russian but also in English, trying also to influence Western public opinion.

Internet is also a medium through which the “**Whistleblowers**” can transfer their findings, documents, and evidence to the public opinion. Traditionally, they used contacts with mass media. The most well-known example was the “**Deep Throat**”, who in 1972 gave the information to The Washington Post journalists about the president’s involvement in spying on political opposition. The **Watergate scandal** forced Richard Nixon to resign and almost 50 people were found guilty, some of them were the top administration officials.

A recent example of whistleblowing (or some say, like the U.S. administration—a betrayal) is **Edward Snowden**. He is a former CIA employee, who in 2013 revealed to “The Guardian” journalists (with whom he communicated using encrypted e-mail) the classified information about the activities of the National Security Agency of the U.S. They included checking millions of e-mails, instant messages, tracking mobile phones not only of the American citizens, but also spying on its allies and their world political leaders, most notably the German Chancellor Angela Merkel.

While it is difficult to be truly anonymous on the internet (this requires some advanced IT knowledge of e.g. using secure e-mail accounts, encrypted VoIP calls, VPNs, or the Tor network), it seems that **WikiLeaks** still guarantees it to its informers. Among its most important “leaks” were the documents on the war in Afghanistan, in Iraq or the release U.S. Department of State diplomatic “cables”.

Chapter 5

Normative elements of public and economic policy

5.1. What is public policy?

5.1.1. Definitions

In order to introduce the reader to some specific concepts of economic policy, we will come back to politics, again. Let us see some **definitions of policy**:

Purposive course of action that an individual or group consistently follows in dealing with a problem.

(Anderson, 2006)

Instruments through which societies regulate themselves and attempt to channel human behaviour in acceptable directions

(Schneider, et al., 1997)

Course of government action or inaction in response to public problems

(Kraft, et al., 2007 p. 5)

Public policy is a kind of politics concerning public matters. As we could see above, politics has also meanings other than relating to public affairs only. Thus, some further definitions could also be required. However, we would not simply add the word “public” to “politics” to receive them. Public policy is:

- the activity of public administration (the government, broadly speaking);
- regarding various issues considered by them as important enough to regulate or at least influence them;
- run within the existing law (constitution and subsequent regulations, as well as their interpretation) and institutional customs.

Public policy is also:

- Governing the public affairs, which may be conducted according to the policymakers’ own goals and preferences, including their will to keep the power (even at the cost of

inefficiency of public spheres). In particular, public policy may use the power to redistribute public (and private) resources.

- The purposive course of action of government, who acts in a certain context that influences its decision-making process of choosing the tools and means to achieve the goals set. In particular, public policy is the **art** of decision making (that includes e.g. compromise and consensus) over the ways of running different kinds of public policies and the art of achieving the public goals.
- A branch of social science that describes the public policies, which are run in practice.

5.1.2. Public policy as a science

Public policy has also become a new **scientific discipline**. As a social science, it is based on the principles of economics, sociology, and law. Usually, however, it is practiced not by economists, sociologists, or lawyers, but by political scientists or persons specialising in public administration.

Although it implemented some elements of the theory of economic or social policy, it seems still to be far from generalising their findings to create a coherent theory. Instead, it offers some own theoretically-based approaches (like analytical framework, policy cycle) accompanied by a mixture of different examples from the real life.

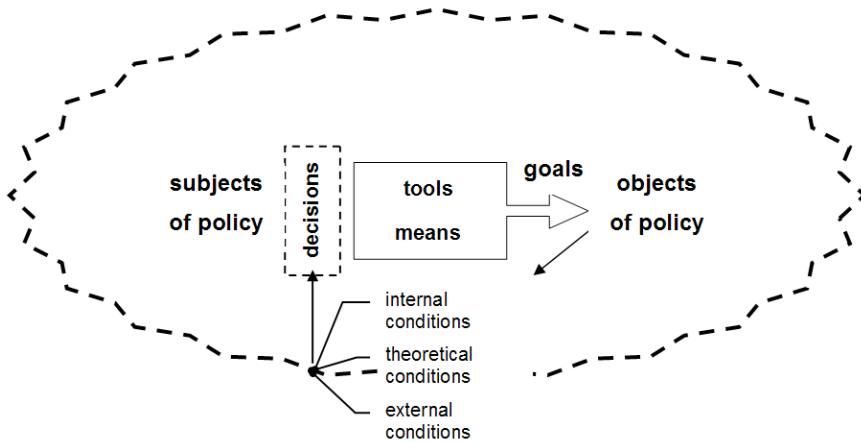
There are several public policy schools in the world. They offer degrees of the Master of Public Policy, the Master of Public Administration, PhD in Public Policy or the Doctor of Public Administration (as well as some courses, usually for graduate students, often with practical experience). Among the best such schools, the most important are the following ones:

- in Europe:
 - » Hertie School of Governance, Berlin
 - » Sciences Po Paris - Paris School of International Affairs
 - » University College London - School of Public Policy
 - » London School of Economics and Political Science - Institute of Public Affairs
 - » Maastricht University - Maastricht Graduate School of Governance
- in Asia and in Latin America:
 - » Peking University - School of Government
 - » National University of Singapore - Lee Kuan Yew School of Public Policy
 - » FGV-EAESP (São Paulo, Brazil)
 - » University of Tokyo - Graduate School of Public Policy
- in the U.S.:
 - » University of California, Berkeley—Goldman School of Public Policy
 - » Harvard University—John F. Kennedy School of Government
 - » University of Michigan, Ann Arbor—Gerald R. Ford School of Public Policy
 - » University of Chicago—Harris School of Public Policy Studies
 - » Princeton University—Woodrow Wilson School of Public & International Affairs
 - » Columbia University—School of International and Public Affairs

5.1.3. Theoretical framework of analysis

We can try to show the definition of public policy on a graph to help with understanding this process (public policy is a process, and not one-time act; and it is a repeating process).

Figure 29. Visualisation of framework of public policy analysis



Source: own.

Policymakers (subjects of policy) take the decisions often on the choice of tools and means to reach the goals they have previously set up, influencing the public sphere (object of policy).

Policymakers' decisions are determined by some context. It can be divided into three parts:

- endogenous conditions,
- scientific theories,
- exogenous conditions.

The endogenous (or domestic) context changes in a long-run together with the changes in the situation of public affairs. For instance, if we are to analyse economic policy we should understand that the present and past economic situation determines contemporary policy choices, and the influence of policymakers on economic situation will later on determine the future decisions of economic politicians. Thus, endogenous context can be influenced by domestic public policy.

Different situation is with exogenous context, which is hardly manipulative by domestic authorities. For instance, international crisis influences economic policy of many countries, however they may not have enough power to control it (it is difficult even to the United States, the largest economy in the world).

The third group of factors forming the context are the ideas, especially scientific theories and concepts that can be used to support or justify the decisions. Some countries may influence them promoting creation of such theories that would bring benefits to them. The rest of the countries can:

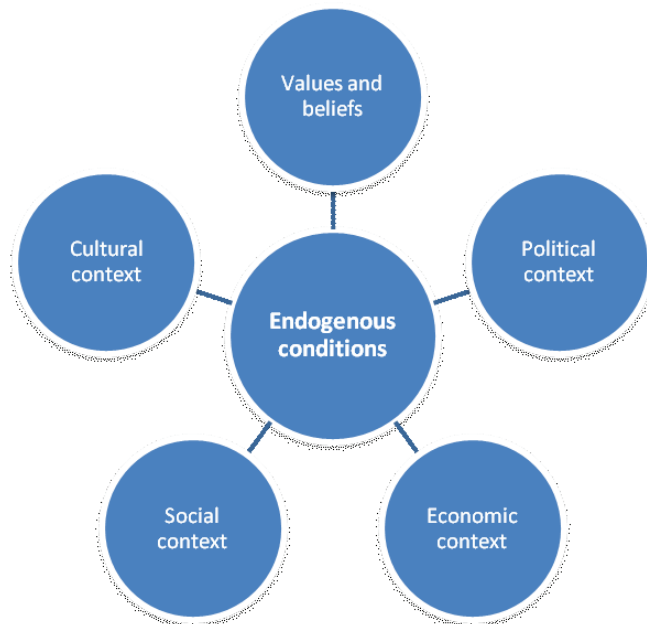
- try to develop their own scientifically-backed solutions (see e.g. development economics) or
- choose some of many economic concepts trying to adjust them to their preferences and needs, or
- can make decisions based on politicians' own experience, knowledge and intuition.

The last kind of decisions, theoretically, would have smaller chances for success compared to the first ones. They, however, sometimes require years of research, thus in practice a mixed solution is adopted and policymakers do not follow theory exactly, trying to find their own ways justifying it with the specifics of a country and particular context it is immersed in.

5.2. Endogenous context of public policymaking

Below we will concentrate on endogenous context, as it can be influenced by public policy. Therefore, we will enumerate a few groups of endogenous factors influencing public policies. The most important are usually political conditions, then—economic ones.

Figure 30. Groups of endogenous public policy making conditions



Source: own.

5.2.1. Values and beliefs

Values and beliefs are part of a broader institutional context (this, however, would include some political institutions, which are a part of political and economic context, thus the “institutional context” is not distinguished separately). They are often neglected in textbooks (or grouped in a cultural context), but are important in practice of public policy.

Some values and beliefs determine the choice of goals and shape of policies. We mention here the **pre-decision stage** of policymaking. However, there may be a problem, which needs policy intervention when there is a **conflict of values**. In such cases politicians sometimes may decide that their legitimacy is too small to give them the rights to judge, which values overwhelm the others (e.g. if abortion or euthanasia rights are discussed). In such cases, a referendum may be called upon.

There are the following, widely-shared values and beliefs:

- **value of life**, however with some exceptions:
 - » from an economic point of view it might be justified to kill less able individuals (see e.g. of ancient Sparta), however nowadays any such policy proposal would end up in a trash even before proceeding with it; it is unimaginable to introduce any such regulations;
 - » in some countries abortion is allowed (with differences in details), however it may contrast with personal freedom of women, thus there is often a conflict of values,
 - » in some countries (Netherlands, Belgium, Luxemburg, Japan) it is legal to remove somebody from artificial life support, however the individual freedom and the right to avoid suffering contradicts here with religious beliefs;
- **democracy**; while we can imagine that the government has a substantial majority and change a constitution to change a political system and decrease democracy, such situations are rather rare in present times; thus, a lot of other political decisions that may be associated with limitations to democracy are not taken, and even if so, when discovered, they may cause a big scandal (see e.g. the Watergate affair);
- **respect for minorities**, however it depends on other factors (level of unemployment, popularity of nationalism, dominant religion);
- **freedom**, e.g. of press, individual (human rights), however in some cases it may be limited, when universal good is in question.

Many of them and many others are enumerated in The Universal Declaration of Human Rights (discussed so far in previous parts of this book).

5.2.2. Political context

The political context may be complicated in some countries, as it consists of visible elements, but also of many tacit ones. They may include:

- visible elements:
 - » parliamentary majority,

- » particular offices taken (e.g. of president),
- » geographical distribution of support for political parties,

Constitutional rules appear to shape economic policy.

(Persson, et al., 2004 p. 94)

- tacit elements:
 - » informal influence on the prime minister / president,
 - » influence of religious leaders, global and national thinkers, lobbies,

Many of the above-mentioned issues have been discussed in the previous chapters.

5.2.3. Social context

The social context includes the issues such as:

- population, with e.g. migration, birth rates, aging,
- safety, e.g. crime rate,
- health,
- housing (e.g. social preferences: private houses vs. flats), density of population,
- education: quality of education, attendance rates.

It determines especially social policy, which, however, relates to economic policy, as well, thus cannot be neglected.

Should any political party attempt to abolish social security, unemployment insurance, and eliminate labor laws and farm programs, you would not hear of that party again in our political history. There is a tiny splinter group, of course, that believes that you can do these things. (...) Their number is negligible and they are stupid.

Dwight D. Eisenhower

For instance, the fringe benefits (e.g. unemployment / sickness payment) are elements of social policy, but because the financial matters are used, thus budget policy (expenditure policy) is involved, as well. In practice, it is difficult to run social and economic policy separately, however in academia they are usually studied and researched by separated groups of students and scientists. Thus, **the problem with public policy coordination emerges.**

5.2.4. Economic context

While social conditions largely determine the social policy, economic context is more important for economic policy (however, both areas overlap). Economic context may include the following groups of factors:

- dynamism of development, e.g. GDP growth rates;

- » with high expected growth rates it is easier for the policymakers to start long-term costly projects (like e.g. the infrastructural ones);
- stability of development, e.g. volatility of exchange rates, GDP, unemployment;
 - » with higher volatility it is more difficult to plan long-term goals and policymakers more often aim at short-term stabilisation programmes;
- level of development, e.g. GDP per capita;
 - » on higher levels of development policymakers can concentrate more on increasing the quality of life of the population;
- public finance conditions, e.g. deficit, incomes, expenditures (incl. fixed ones);
 - » it is one of the most important groups of determinants of public policies, esp. if they include larger expenditures (during recession government may want to cut some kinds of expenditures and favour others);
- and many more.

5.3. Government, its goals and decisions on policy

The structure of governments is usually quite complex. Thus, the decision-making process may be complicated and long. Moreover, the structure may be changed and some time is needed to adjust to a new institutional context.

Usually, we distinguish between three kinds of political institutions: legislative, judicial, governing. Their power is used to be separated, however often the same political party controls legislative and governing bodies. During recent years, the independence of central banks was widely introduced. Some of them have independent monetary policy councils, which are supposed to be less political than the governor of the central bank is (as he is usually politically-nominated). Similarly, within the judicial system, a supreme court or a constitutional tribunal e.g. decides if a law follows the constitution or may violate it. Moreover, a two-chamber system is also common. The policymakers are also bounded with international agreements; they can be modified, but in a short-run they may seriously influence the scope of policymaking.

The system, which prevents one branch (e.g. political party) from becoming supreme, where the power is distributed over many bodies, is called “checks and balances”.

The situation complicates when we try to distinguish between governing context and actors, i.e. policymaking institutions. The context directly determines the actors; however, actors take decisions, and not a context, of course.

Figure 31. Structure of governing context



Within that context, political institutions function and run their policies. Using the top-down approach, we can distinguish between the following levels of government:

- just a few global institutions, e.g.
 - » The Internet Corporation for Assigned Names and Numbers (ICANN), which is responsible for some part of internet policy of all the countries using the internet.
- some international bodies and institutions,
 - » For instance, within the Eurozone, the power of domestic central banks is very limited because it was transferred to the European Central Bank, which runs the monetary policy for the euro area, and therefore it makes decisions that are superior to domestic monetary institutions.
- national (federal) institutions,
 - » Traditionally, it is the government and its agencies specialised in selected public policies (e.g. supervision of the financial markets, of the competition etc.), parliament, and a president.
- regional (state) and local institutions,
 - » Depending on the political, governing context, they can have different dependence or autonomy from the central (federal) government.

There are also some rare forms of government entities, e.g.:

- foreign governments (e.g. in Iraq after the U.S. and allies' intervention),
- labour unions (e.g. in Poland at early 1990s the leaders of Solidarność union formed the government and had the majority in the parliament),
- companies (these can be multi-national companies or large domestic private or state-owned firms usually having a monopoly, which can be protected by the government, e.g. they can run part of telecommunication policy of a country),
- NGOs (e.g. ICANN runs parts of internet policy on global level),
- churches (Roman-Catholic Church which rules in Vatican), however usually it is included in a context.

Very many different areas are covered by many institutions. Their number seems to increase over time with the growth of governments and regulations imposed by them. Thus, the problem of overlapping competencies and responsibilities emerges that requires coordination.

For instance, in order to run successful **innovation policy**, which is one of the most difficult public (or more precisely: economic) policies, the **multi-level governance** should be introduced. It is a vertical coordination of activities focused—as in this example—on innovation within a specific geographical region (and similar areas like research, education, entrepreneurship etc.), which can be aimed e.g. at creation of so-called **clusters** (of companies, universities and public institutions supporting them forming regional and national innovation systems).

The decisions that are taken by policymakers can flow in different ways:

- bottom-up: the problems that were not solved at the local level are brought to the higher level at governance,
- top-down: a national government decides about actions that will be taken which will be binding and influencing situation on local levels,
- multi-level governance, basing on free flow of information in both directions.

Public policymakers also decide about **priority of goals** and the **sequence of achieving** them. They use their legal power to decide about them and their decisions are more important than the will of a society (frequently, governments may introduce decisions that are not supported by the majority of voters). They also **decide about the means** they would use to achieve the defined goals.

As we have mentioned many times so far, the policymaking process can largely be influenced by politics. In this sense, politicians may want to maximise their chances for re-election. Thus, they may run policies that

- would prefer their constituencies or
- the swing groups that may support them in the future (and they may profit even more than core constituencies).

Because of this, it is difficult to analyse public policy from e.g. an economic point of view, assuming e.g. that it aims at maximisation of welfare of all groups of society. Due to the political character of public policymaking process, real goals may differ much in comparison with official statements. Hence, we can distinguish between two kinds of goals:

- *de jure*—expressed in official policy programmes (agendas, laws, strategies),
- *de facto*—actual goals that are implemented.

Moreover, as it was noted, the goals that the policymakers fulfil, the intensity of their efforts to achieve them—they all depend on political decisions. Thus, the theoretical question emerges: can we speak about objective policy goals, when all of them depend on specific context that has a dynamic nature?

Box 18. Policy goals—objective or partisan?

One Polish leading scientist of the field of the theory of economic policy, prof. Jan Kaja (1954–2015), has questioned the notion of existence of objective policy goals. Even during socialism, he used to say that there is no such things, because the goals at that time depended on the decisions of the Party, and not even on the opinions of economists trying to support it. In a democratic system, citizens may have indirect influence on economic policy goals through their representatives. Even though, the final choice of the goals and of their priorities depends on specific context and political decisions. Thus, the objective goals of economic policy do not exist.

Usually, however, it is assumed that for instance the major goal of economic policy is the GDP growth. It is however not the entire truth, as economic reality is too complicated to be squeezed to one measure only.

Moreover, public policy consists of more than one policy only, thus the coordination of policies is needed to avoid conflicts of goals that are to be fulfilled by different ministers of the same government. For instance, one department of a government administration may want to increase industrial or agrarian production, while the other one would like to limit it due to too extensive negative external effects (e.g. pollution, smoking—see Box 19).

Box 19. Contradictory goals and policy inconsistency—the case of tobacco industry

Generally, we agree that smoking threatens health and life, thus public policy in many countries discourages people from smoking.

...smoking-related deaths still costs the nation [i.e. the U.S.] about \$92 billion a year in the form of lost productivity (...) during 1997–2001 an estimated 438,000 premature deaths occur each year as a result of smoking and exposure to second-hand smoke. In comparison, approximately 440,000 smoking-related deaths were estimated to have occurred annually from 1995–1999.

(Longley, 2005).

On the other hand, governments support tobacco industry, e.g. because it create jobs and brings revenues to the budget. Recent regulations of the European Commission concerning the Common Agricultural Policy for 2014-2020 brought larger coherence in this sphere, because the direct support to tobacco farmers was eliminated.

...White House expresses disappointment at the continuing subsidy by the European Union of tobacco cultivation to the tune of some £260 million each year despite the many more millions paid by the EU in anti-tobacco public information campaigns and billions of pounds worth of damage done to the EU's economy by the public health impact of smoking as well as the real damage on the health of individuals.

(United Kingdom Parliament, 2010)

In the United States, the Office of the Surgeon General and the Food and Drug Administration try to discourage smoking, while the Department of Agriculture still supports it with subsidies.

It is often claimed that the tobacco industry has a strong lobby. In 2010, the U.S. supported the tobacco industry with almost \$200 million in subsidies. Moreover, for decades it was allowed for the tobacco industry to influence the American public opinion deliberately. It was not an unintentional behaviour. In November 27, 2012 the U.S. federal judge...

...ordered tobacco companies to admit that they have deliberately deceived the American public and finally tell the truth about their deadly and addictive products and fraudulent marketing.

(Myers, 2012)

The Lobby is also well organised within the EU bureaucracy.

Lobbying efforts were well-organised and informed by a detailed analysis of the EU co-decision procedure, in which legislation must be agreed by the Council of Ministers (CoM, representing Member States) and the European Parliament (EP). (...) Lobbying encompassed both direct and indirect approaches. The direct efforts targeted those who could directly influence the text of the directive - Commission civil servants, Members of the European Parliament (MEPs) and national politicians including ministers. Attempts to table industry-authored or industry-favoured amendments were made through the CoM and, in the Parliament, via MEPs, especially those on influential committees.

(Mandal, et al., 2009 p. 7)

Such a situation, where government runs to contrary policies, is called the **policy inconsistency**.

Bureaucracies typically resist working with other bureaucracies for fear that their own power and budget might decline as a result. If high-ranking politicians wanted to, they could insist on coordinated policymaking. But they don't, because coordinating does not matter to them. The ultimate goal for a politician running for office is to get elected. From that vantage point, politicians tend to consistently push for policies that will bring them votes, funds or both. Anti-smoking gestures and agricultural subsidies are consistent with politicians' self interest.

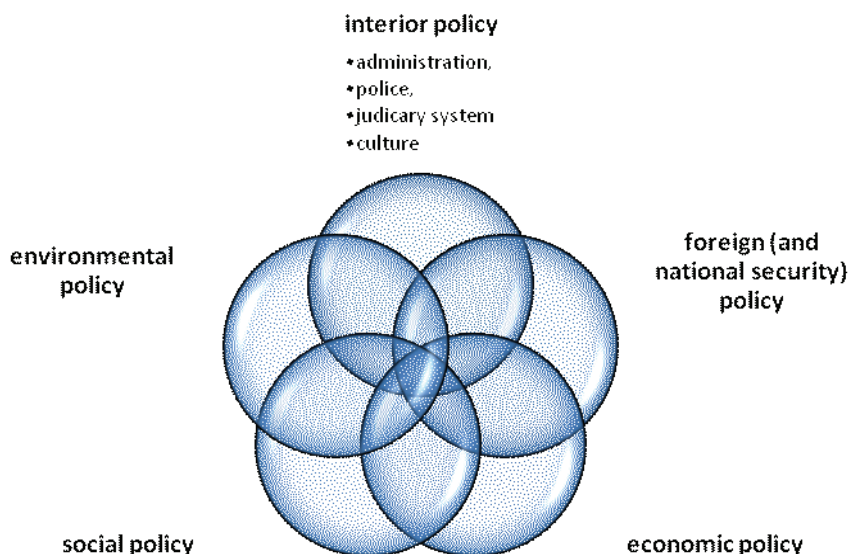
(Kurdas, 2012)

5.4. Kinds of public policies and relations between them

Public policy covers a wide spectrum of government actions. It deals with the following issues and respected policies:

- domestic, administrative issues—internal policy,
- relations with other countries—foreign policy,
- protection against foreign countries intervention in domestic matters—defence policy,
- social issues—social policy,
- economic issues—economic policy
- protection of natural environment—environmental policy.

From this perspective, public policy is a collection of specific policies. From the efficiency point of view, they should be coherent, coordinated, in order to avoid the policy inconsistency. Moreover, such specific policies overlap and sometimes it is difficult to run one without influencing the others. Hence, the role of the prime minister or the president (depending on specific political system of a country) is not only to represent a country, not only to be a supervisory of the ministers, but also to be a negotiator, conciliator, and coordinator of all the public affairs where the government is active. This, however, may sometimes be difficult and may require a visionary to be the leader of a country. If not, such a person may end up as a public affairs administrator only.

Figure 32. Kinds of public policies

Source: own.

Policies may have different names but can cover similar issues, e.g. national security policy can be a synonym of defence policy.

Box 20. Public policy lectures at Harvard

We can check what public policy is related to while looking on the set of lectures on it and on the disciplines related to it. At the Harvard University, thought to be the best one in the world, we can find the following lectures:

- Public policy area:
 - » Economic Analysis of Public Policy
 - » A Libertarian Perspective on Economic and Social Policy
 - » Public Economics: Designing Government Policy
 - » Environmental Science and Public Policy 10 - Environmental Policy
- Economic policy area:
 - » International Financial and Macroeconomic Policy
 - » The Monetary and Fiscal Policy Seminar
 - » Public Economics and Fiscal Policy
- Social policy area:
 - » Poverty and Social Policy
 - » Social Policy II

- » Housing and American Social Policy, 1930-Present
- » Seminar: Social and Urban Politics
- » Education Policy Analysis and Research in Comparative Perspective
- » Health policy
- » Global Health and Health Policy
- » Politics and Education Policy in the United States
- Policies of particular countries:
 - » American Economic Policy
 - » American Foreign Policy
 - » The Politics of Social Policy in Brazil
 - » Middle Eastern Politics and Policy
 - » Latin American Politics and Policy Making

Source: own search on www.harvard.edu.

Moreover, the role of different specific public policies changes over time. For instance, during last decades social policy grew on importance. Recent years have brought more focus on environmental issues, and less on defence. In some European countries, environmental policy starts dominating (at least in some aspects) the economic policy. However, there are still some countries that strive for independence of their neighbours and the defence policy may be the most important one there. Sometimes, however, the changes in military policy are subordinated to economic policy requirements. In consequence, it may cause conflicts due to competition for resources, e.g. crude oil, access to fresh water.

Internal policy, if it is too weak, may limit the chances for economic policy successes. For example, the corruption and low quality of judiciary system increase transaction costs and disturb economic growth. In most extreme cases, if the government is internally too weak, the neighbours may decide to divide its territory.

Box 21. Weak internal policy as a risk for independence—the case of Poland

Too intensive and developed internal policy may be costly, however, if it is too weak this may lead even to the loss of independence. This was the case of Poland at the end of the 18th century: the mighty and powerful in the past Polish–Lithuanian Commonwealth that have stopped the invasion of the Ottoman Empire to Europe in 1683 (the Battle of Vienna) was later partitioned by Austria, Prussia, and Russia. In result, Poland has disappeared from the maps for 123 years until 1918 (and just 21 years later, it was invaded and partitioned again: by Nazi Germany and the Soviet Union due to the Molotov–Ribbentrop Pact). The reasons of this regression are connected with the government inefficiency (as we may contemporarily call it):

- the loss of central control over country in favour of ‘oligarchs’ (that resulted e.g. with Lubomirski’s Rokosz against the king John II Casimir),
- mistakes in organisation of policymaking process (*liberum veto* was a right of every member of the parliament to block any of its decisions),
- corruption of MPs by neighbouring countries and powerful families.

In consequence, the Commonwealth deteriorated from a European power into a state of anarchy.

Economic policy is:

The discipline that studies public economic actions, inasmuch as it studies all three levels: the ‘current’ choices of the government, the choice of higher-level institutions (i.e. the definition of society’s ‘economic constitution’) and the identification of social preferences or objectives.

(Acocella, 2005 p. 2)

Apart from the issues on how economic policy actually fulfill the needs of society (and not of politicians or of interest groups) one often point to the conflict between economic policy and social policy. We may rise a question—what is more important: economic or social policy? Should the needs of society be fulfilled first, or maybe the ones of markets and enterprises? (recall A. sen’s view).

It’s the economy, stupid!

A slogan for the Bill Clinton’s successful election campaign in 1992.

Economists usually believe that economic goals are more important, because once economic growth comes it disseminates and more people become wealthier. Sociologists usually reply that the growth is not divided equally and it does not necessarily affect the most needy, the poorest ones. Moreover, development economics as well as the empirical evidence suggest that it is possible to reach both economic and social goals at the same time. While the developing countries significantly improved conditions of life, especially level of education, of health system and the life expectancy has increased substantially over last few decades, they still experienced economic growth, the pace of which was frequently higher than the one of the developed countries.

Although, there is a threat that too intensive focus on social issues may hamper economic growth. That risk was one of the fundamentals of the so-called **Washington Consensus** and the policy recommended by the International Monetary Fund. It is much easier to spend money than to earn it, both on micro and on macro levels. Some developing countries have suffered the painful consequences of populist policies.

Box 22. 'Globalisation with a human face'

The Washington Consensus and the IMF's policy recommendations were widely criticised, especially in the aftermath of the East Asian crises of 1997-1998. One of their most famous opponents was Joseph Stiglitz, the Nobel Prize winner (2001), former chairman of the Council of Economic Advisers under Bill Clinton and chief economist at the World Bank.

He argues that neoclassical-backed, Chicago-style free-market recommendations to economic policy for countries applying for the IMF's loans led to deterioration of the social situation of their citizens, and sometimes even undermined the democracy. He noted that the IMF is more interested in increasing the chances for loans repayment than in the situation of the poorest. Apart from that, he attacks the fundamentals of the IMF's recommendations saying:

Recent advances in economic theory—ironically occurring precisely during the period of the most relentless pursuit of the Washington Consensus policies—have shown that whenever information is imperfect and markets incomplete, which is to say always, and especially in developing countries, then the invisible hand works most imperfectly.

(Stiglitz, 2002 pp. 73-74)

If so, if the market left without a state intervention cannot work properly, then institutions should be established first and government interventions are allowed.

He gives the examples of countries that:

- have used the IMF's help and failed, e.g. East Asian countries suffering from the financial crisis, sub-Saharan Africa, Argentina or Russia and
- argues that those who resisted IMF conditions or refused to use its loans performed better, e.g. Malaysia, South Korea, and China.

Later on, Hungary joined the IMF's critique. In 2013, it has repaid the rest of the loans and the Orban's administration (actually, the chief of the central bank) has asked the IMF to close its offices in Budapest and to leave the country saying that it was "not necessary to maintain" any longer because it wants to end undue foreign influence over its economic policies.

However, without social spending investment outcomes in long-term growth may be limited. This encompasses e.g. education, health, which build up the human capital. Economic policymakers sometimes neglect such investment, while they—under the pressure of politicians elected for a defined term—may concentrate on short-term solutions giving effects in a short- or medium-run.

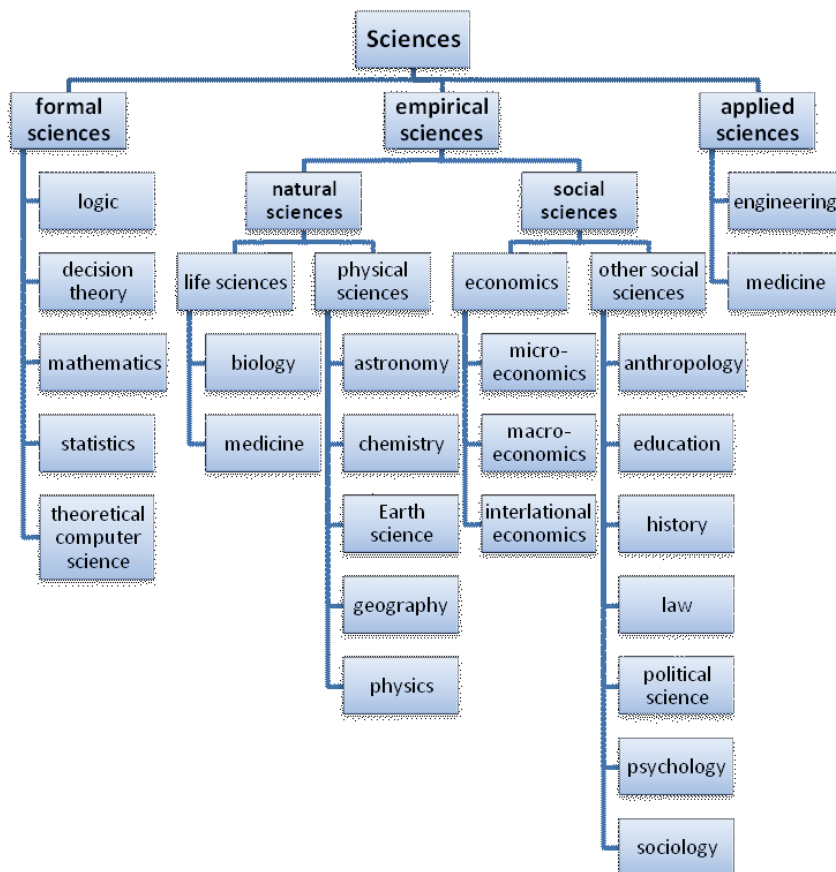
On the other hand, the lack of concentration on unemployment issues even during a financial crisis may lead to the erosion of human capital (it depreciates due to long-term unemployment). Its reconstruction or reinvestment in it is lengthy and costly.

Moreover, we should remember that economic policy does not have to be economic, at all. It means that the government does not have to take decisions that are economical, that will be profitable, or that are aimed at increasing overall welfare. They can intentionally be costly, misled, populist and aimed only at increasing the politicians' chances for re-election.

5.5. Economics and economic policy in social sciences

Before we will go to some detailed analyses, let us see where we are when we speak about economics and its subdisciplines or fields related to it.

Figure 33. Branches of science—the place of economics

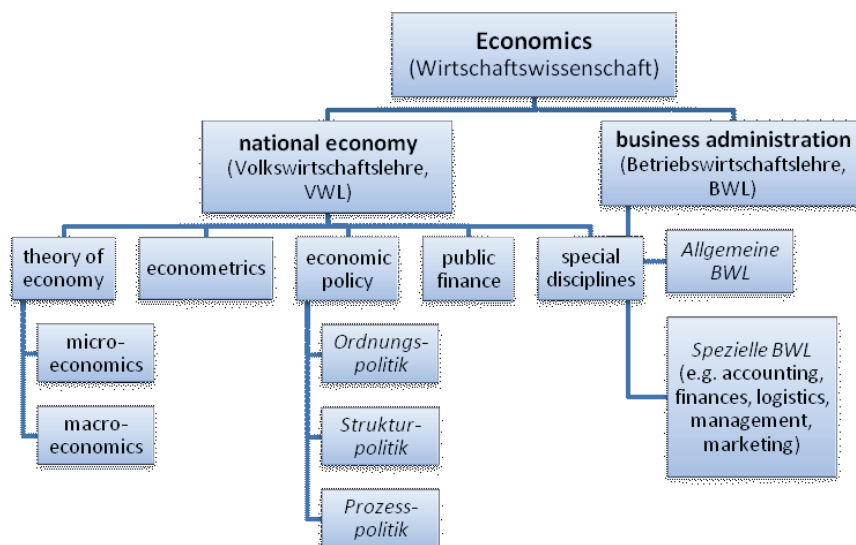


Source: own.

Economics is a social science. However, sometimes it looks rather like an example of formal sciences, if mathematic models are the basis of certain papers. Economics has many years ago separated from the rest of social sciences, what influences the theory of economic policy and makes it difficult to run social policy. It will be discussed further in this book.

In Germany, different division of economics is usually adopted.

Figure 34. Branches of economics—German view



Note: *Ordnungspolitik* may be translated as ‘regulatory policy’; *Strukturpolitik*—structural policy, *Prozesspolitik*—process policy.

Source: own.

Here we see that the division on micro- and macroeconomics is not the main within economics as econometrics, theory of economic policy, public finances and other disciplines describing national economy are distinguished. We can note here that public finance is closely linked to economic policy.

Box 23. Theory of economic policy in Germany

Context

After the end of World War II, there was an important discussion run in many European countries on the future social and economic system for those countries. Especially intensive disputes have been held in Germany. Its Eastern part was occupied by the Soviet Union, and socialist system was not recognised as an acceptable solution. The *laissez-faire* capitalist system, as it was before WWII, was not acceptable, as well. The **hyperinflation**, which occurred after the World War I, a **mass**

unemployment that grew during the Great Depression of 1930s that led to political radicalization in Germany, have transformed the democratic republic of 1919 to the national socialist dictatorship in 1933. Thus, the need to rebuild the economic system to avoid such problems in the future became of premier importance.

The theory of economics (and any other theory) did not provide any complex solutions. Keynesianism was already in use, but there were no clear answers, for how long it may be introduced, how strong interventionism should be, what should be the role of a government in the 'new' country, etc.

Social market economy

On the initiative of the Federal Minister for Economic Affairs and later Chancellor **Ludwig Erhard**, the system of the "Social Market Economy" was introduced in 1949. It was inspired by the German concept of Ordoliberalism (social liberalism) and among its most influential thinkers, there are Walter Eucken, Wilhelm Röpke, Franz Böhm, and Alfred Müller-Armack (who coined the term *Soziale Marktwirtschaft* in 1946). This system combines private ownership with state regulation (and even interventionism) in order to reach the defined set of social and economic goals without favouring any of them (e.g. economic growth only).

Kinds of economic policies in the social market economy

According to these views, there are two kinds of economic policies:

- **Ordnungspolitik** (policy towards creation of economic order) that designs the framework within which economic processes take place, and
- **Prozesspolitik** (policy towards influence on economic processes) of direct influence of a government on economic processes (to stabilize economy or to influence the economic growth) established by *Ordnungspolitik* with the use of e.g. such instruments as subsidies, minimum wages, redistribution, stimulus programs, bailouts, etc.

One of the kinds of the 'process policy' is the **Strukturpolitik** (structural policy), which is aimed at changing the structure of the economy to avoid or overcome structural problems that disrupt the macroeconomic balance:

- at a **regional level** (regionale Strukturpolitik), and
- at a **sectoral level** (sektorale Strukturpolitik).

All of these new forms of policies are not usually mentioned in the English literature on the subject. The social market economy concept has however tremendously influenced the shape of economic and social policies in the European Union, as it is still at present times. For instance, structural policy, regional policy, competition policy became one of the most important EU policies.

Before discussing further details, we should remember that there are some other subdisciplines within economics and many schools of economic thoughts. The overall division is to distinguish between:

- **mainstream** (or orthodox, conventional) **economics**, which is nowadays associated with neoclassical synthesis developed by John Hicks and popularised by Paul Samuelson, which combines neoclassical microeconomics with Keynesian macroeconomics;
- **heterodox economics**, which includes all other approaches, schools or traditions, e.g. Austrian, evolutionary, innovation, or institutional economics, or even such new ones as neuroeconomics.

In order to better explain the differences between the above using three words only, we can say (Davis, 2007 p. 58) that:

- mainstream economics combines such categories as **rationality-individualism-equilibrium**, while
- heterodox economics rejects concentration on them and introduces alternative **institutions-history-social** structure nexus.

Although mainstream economics is more coherent than the heterodox one, we can distinguish between two major groups of economists practicing it. They are gathered in:

- the **‘freshwater’ school** concentrated around the area of the Great Lakes: in the Carnegie Mellon University, the University of Chicago, the University of Minnesota, and the University of Rochester;
- the **‘saltwater’ school** on the east and the west coasts of the United States, including e.g. University of California-Berkeley, Harvard University, Princeton University, Columbia University, MIT and Yale University.

There are some differences between them and among them; the most important one may be associated with different approach to economic policy making:

- ‘saltwater’ economists put more pressure on creation of proper **rules and structure** of the economy to stabilise it.
- ‘freshwater’ economists favour a **discretionary approach** in order to fight with market failures that cause business cycles (and recessions within them) using e.g. public spending and the short-term interest rates,

In other words:

- freshwater economics—more **active economic policy**.
- saltwater economists prefer **passive economic policy**, while

5.6. Relations between political economy, economic policy and economics

Political economy is related to economic policy, but both terms have different meaning. The relations between economic ideas and political motivations are the subject of interest of political economy. Political economy also takes...

...political decisions as a topic for research and endeavour to identify and explore the determinants of economic policy decisions.

(Bénassy-Quéré, et al., 2010 p. 5)

Political economy has a very long tradition. It comes from the Greek words *oikos* (home) and *nomos* (government). It was used publicly for the first time in French as *économie politique*. This was in 1615 in the book ‘*Traité de l’économie politique*’ by Antoine de Montchretien. As a distinct field of study, it emerged from the works of Scottish philosophers Adam **Smith** and David **Hume**. The first comprehensive system of political economy and an example of political economic analysis was Smith’s work ‘*An Inquiry into the Nature and Causes of the Wealth of Nations*’ (1776). Such classical economists as e.g. John Stuart **Mill** and David **Ricardo** did also use this term. They all treat it as an equivalent of “general economics”. The first chair of political economy was established in 1763 at the University of Vienna. Thomas **Malthus** in 1805 became the first England’s professor of political economy¹¹.

First economists following **Smith’s** approach showed **individual-centered** analysis of political economy. This is shown by the notion of “invisible hand”, which assumes that self-interest is beneficial for the whole economy rather than state interventionism. Smith’s and Say’s “individual economics” or “cosmopolitan economics” was contrasted by Friedrich **List**, who noted that individual behaviour might harm the interests of a nation. Later, Karl **Marx** developed the class-based analysis of political economy.

Since 1890, when Alfred **Marshall** published his very influential textbook “*Principles of Economics*”, **political economy has started separating into a few disciplines**: economics, sociology, political science, and international relations. He reshaped the discipline following the physics example and hence wanted economics to be formal and precise. This was continued by Paul **Samuelson**, who in the “*Foundations of Economic Analysis*” published in 1947 introduced mathematical tools to economics (while e.g. John Maynard **Keynes** avoided any mathematics in his *magnum opus*, “*The General Theory of Employment, Interest and Money*” published in 1936). This approach is used until nowadays and economics (or economic science) usually has a narrower focus than originally.

Political economy is now a discipline of broader social sciences and deals with governing the state. It uses not only economics, but also takes into account political factors. Hence, it is more disciplinary, as it includes contributions from economics, political science, but also from sociology. Political economy studies the political motivations of economic policy decisions. Thus, political decisions are endogenous to the researcher.

The government is therefore no longer regarded as a Deus ex machina that monitors and steers the private economy in the name of the general interest but, instead, as a machine directed by politicians, i.e., by rational players whose behaviour follows specific objectives and faces specific constraints.

(Bénassy-Quéré, et al., 2010 pp. 8-9)

¹¹ The Department of Political Economy existed as early as in 1811 at the Imperial University of Warsaw. It lasts until nowadays at the University of Warsaw.

Within economics, similar approach is visible in public choice theory (which deals with the issues of voters, politicians, and bureaucrats behaviour related to economic problems). This theory, instead of assuming that politicians tend to maximise individual utilities from social welfare function, adopts the approach that they are rent-seekers, they are self-interest motivated and are to maximise their own utilities. Political economy is interested in rent-seeking, monopoly, corruption, influence of elections on economic policy, political business cycle, and central bank independence, among others.

Economic policy deals with the actions that governments take in the economic field. We can distinguish between:

- the **practice of economic policy**, and
- the **theory of economic policy**, which analyses the practice.

People implementing economic policy in real life can be called the practitioners of economic policy or—what is more frequently used—the **policymakers**, while the scientists describing their activities can be called the **theoreticians** of economic policy (the term “economic politician” is not as common as its German equivalent *Wirtschaftspolitiker*). Sometimes, the same person can play both roles or at first is a theoretician, then a practitioner, and finally comes back to the previous role. Then, there may be a problem of neutrality of descriptions of economic policy introduced in real life, if they were performed by a person, who was earlier an active practitioner.

Following (Acocella, 2005), the theory of economic policy can be divided into:

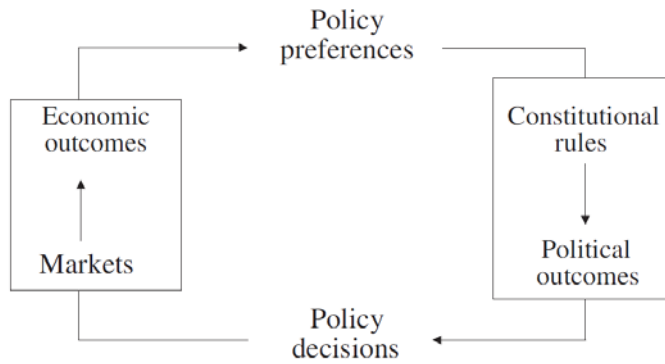
- **normative** (or ‘classical’) theory, called also the theory of public interest, seeks the answer to the questions “how something should be”; it assumes that anonymous politicians act to fill the interests of non-defined private agents; in this approach society reveals its preferences to the politicians who adopt them to the social welfare function, as (Tinbergen, 1956) has hoped;
- **positive** theory, which accepts that the society is not uniform and can be divided into some groups, which have their own differing interests and which make pressure on politicians (through lobbies, trade unions, political parties) to realise their demands.

Normative theory is closer to economics, while the positive one to political economy.

The schema (Figure 35) shows the links between political and economic activities. **Political scientists study the box on the right, while economists the one on the left.** Once we know political determinants of policymakers’ decisions, we can understand the economic policy better. Political economists...

...have asked how economic policy interact with markets to shape the policy preferences of specific individuals and groups and how the distribution of those preferences in turn induces economic policy outcomes and performance.

(Persson, et al., 2003 p. 3)

Figure 35. The democratic policymaking process

Source: (Persson, et al., 2003 p. 3).

Various aspects of political economics have already been described in this book. We will continue these considerations in the next chapter.

Chapter 6

Introduction to the positive theory of economic policy

6.1. Relations between elections and economic situation

Political economy studies the relations between economy and elections, too. The theory of public choice also deals with them. A specific and widely discussed in the literature aspects of such relations is called the political business cycle (PBC). The father of this theory was one of the most prominent Polish economists Michał Kalecki.

Box 24. Michał Kalecki—an underappreciated genius of economics

Polish economist Michał Kalecki (1899-1970) has published the Keynesian theory before J.M. Keynes has did it, however in Polish only.

Michał Kalecki's claim to priority of publication is indisputable. With proper scholarly dignity (which, however, is unfortunately rather rare among scholars) he never mentioned this fact.

(Robinson, 1964 p. 337)

He applied approach that is more mathematical, thus, his works were more concise and precise than original works by Keynes. Still as a student of engineering, he generalised Pascal's theorem, however later he became known as one of the first macroeconomists that applied mathematics and statistics to solve economic problems. Some say that he is one of the greatest economists of the 20th century.

In 1933, Kalecki has published the essay "Próba teorii koniunktury" (An Essay on the Theory of the Business Cycle) and in 1935 "Teoria cyklu koniunkturalnego" (Theory of the Business Cycle). In the first one, he indicated that investment is a key factor determining the aggregated demand and therefore economic growth. He has also explained there the reasons of high unemployment of the Great Depression of 1930s through introduction a theory of monopoly. Although the manuscript of Keynes' book published in 1936 was written in 1993 and was available to some readers, it was not accessible to Kalecki.

Kalecki has divided the society into two classes: capitalists and workers. The latter ones do not have savings, thus the investment may be determined by capitalists' consumption: when the latter falls, recession may come. According to Kalecki:

Investment finances itself

because it generate incomes, and therefore also savings. The increase of consumption (of capitalists; while workers cannot do so) does not lead to decrease of savings but it generates demand, and later also the incomes. His one of the famous quotes is:

Capitalists earn what they spend, and workers spend what they earn.

Michał Kalecki.

In other words, in the Kaleckian growth model a decrease in the propensity to save leads to the increase of rates of profit and to higher rates of output.

He explained that if public investment increases during the boom, then big business persuade the government to decrease public spending, what will lead to a recession. He called this pattern a political business cycle.

However, before we will describe the PBC-related issues in details, we will learn some other findings of introductory nature.

We should remember that there is a two-way causality while analysing elections-economy relations:

- the current state of the economy influences the outcome of elections;
- the results of elections have an effect on economy.

It is **more difficult to reduce budget in countries with multi-party coalition governments** because of the need to reach a consensus on budget cutting. Large deficits were also observed in politically weak countries, where weakness was characterised by governments with a **short tenure** in office. (Roubini, et al., 1989) The problems with budgetary discipline are especially true with minority governments rather than majority coalition governments (Edin, et al., 1991).

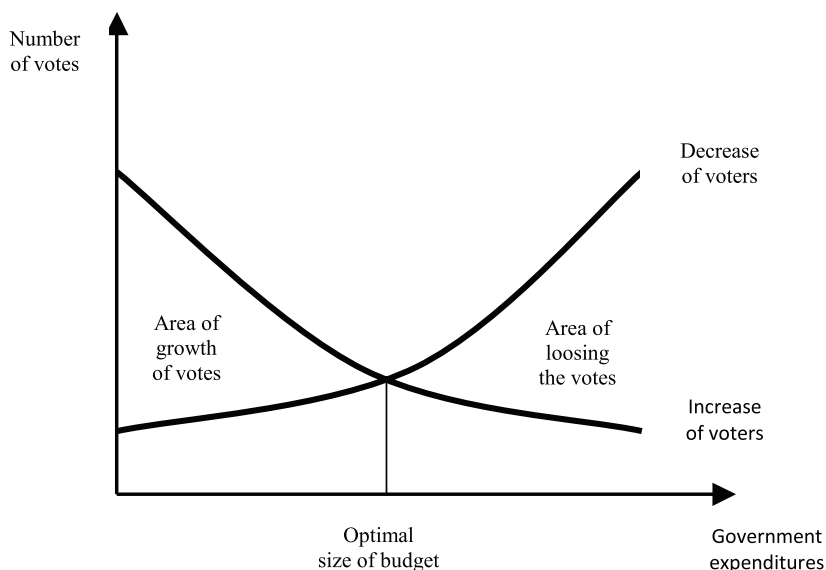
Other studies also show that when the **U.S. political power is divided between republicans and democrats** (i.e. in the situation when one party holds presidential office, while the other one has majority in the parliament), **the budget deficit grew up** (decisions have to be made with certain compromises).

One of the instruments of economic policy that can be used by politicians to manipulate the electoral outcome is government expenditures. It is often assumed that public expenditures may increase before the elections. However, the growth is not infinite, because it is restricted with another effect. Here we can simply divide a society into two groups:

- immediate beneficiaries of public expenditures,
- people afraid that with the increase of government size taxation will follow.

The more ruling party wants to spend from public budget, the higher is the number of disappointed voters that would understand that the increased debts would someday have to be repaid and the next governments may impose new taxes to compensate the pre-electoral increase of expenditures. Thus, there is an optimal point of public expenditures that will maximise the number of voters willing to support certain political parties. This mechanism is presented on the Figure 36.

Figure 36. Optimal size of an electoral budget



Source: (Teichmann, 1993 p. 14).

Thus, the relations between the number of voters willing to support a political party and public expenditure offered by it may be U-shaped curve, while the utility increases at a decreasing rate, and is not a simple, monotonically increasing line.

There are, however, some other considerations. The lower the approval ratings for the ruling party before the elections are, the bigger is the pressure to spend more public funds before the elections.

In practice, there are also two constraints, which limit the opportunistic policy in this simple electoral model presented above:

- internal limits—due to domestic institutions that may prohibit the use of federal budget to buy electoral votes; these are usually the central banks (they can, however, deepen or even create a political cycle following the preferences of central bankers);

- external limits caused by multilateral-agreements between countries (participation of a country in a system of fixed exchange rates) or a fear of reputation of a government and its policy affecting the bond yields.

Above we have analysed how rent-motivated politicians may influence economic policy. However, as we have already noted, there may be an opposite relation. The economic situation may influence the voters' behaviour and due to that reshape the political scene. That was the situation e.g. in the Weimar Republic of Germany (see Box 25).

Box 25. Economic situation and election results: the case of unemployment-driven nationalism in Germany

During the elections to Reichstag on 4 May 1924, after the year 1923 with large inflation and a currency reform, NSDAP accumulated 6.5% of votes and the conservative and nationalistic Deutschnationale grew from 15, 1% (1920) to 19.5%. (...) The economic situation leading up to the elections was characterized by growing unemployment (...). In December 1924 the next elections to Reichstag took place. By now the economic situation normalized. NSDAP again lost half of its votes in favour of DNVP, which obtained 20.5% of votes.

The next period up to 1928 is commonly referred to as the „Golden twenties“. Economic growth took place along with a real wage increase, but at the same time high unemployment was created especially in the winter months' period, which during the 1926-1927 years surpassed the level of 2 million people. This growth did not satisfy most workers and in the Reichstag elections of 20 May 1928 the Communist Party of Germany (KPD) achieved 2.6% more votes and got 10.6% overall, while the right wing NSDAP fell from 2.6% to a level which rendered the party obsolete, the DNVP again fell from 20.5% to 14.2%. (...)

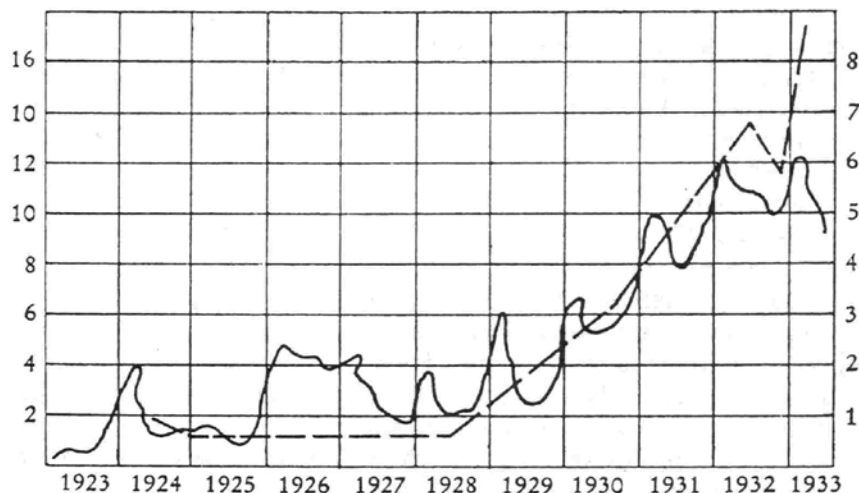
After 1928, the economic situation plunged. (...) So long as unemployment kept growing, namely from 1930 to mid-1932, NSDAP kept achieving meaningful victories in the Reichstag elections. On 14 September 1930 at an average yearly unemployment of 3,076 thousands (9,6%)—NSDAP's votes grew to 18.2% (compared to 2.6% in 1928). It became the second (after SPD) most powerful party in the Reichstag. At the beginning of 1932, NSDAP achieved its peak with unemployment above 6 million.

During the Reichstag elections on 31 July 1932 the party overtook SPD and became the strongest party with 37.3%. On 6 November of the same year elections had to be repeated (...). This time unemployment fell to 5 million. NSDAP lost 2 million votes in this election and fell from 37.3% to 22.1%. Only during the elections on 15 March 1933, when unemployment again rose back to 6 million, national socialists achieved 43.9%, in "somewhat" free elections. This was the largest share of votes.

Notes: DNVP (German Deutschnationale Volkspartei)—German National People's Party, right-wing political party in the Weimar Republic from 1919 to 1933. NSDAP (National-sozialistische Deutsche Arbeiterpartei)—National Socialist German Workers' Party, the Nazi Party ruling in Germany from 1933 until 1945.

Source: (Kaltfleiter, 1968 S. 37) quoted after (Hermann, 1995 p. 84).

Figure 37. Unemployment and nationalism in Germany, 1923-1933

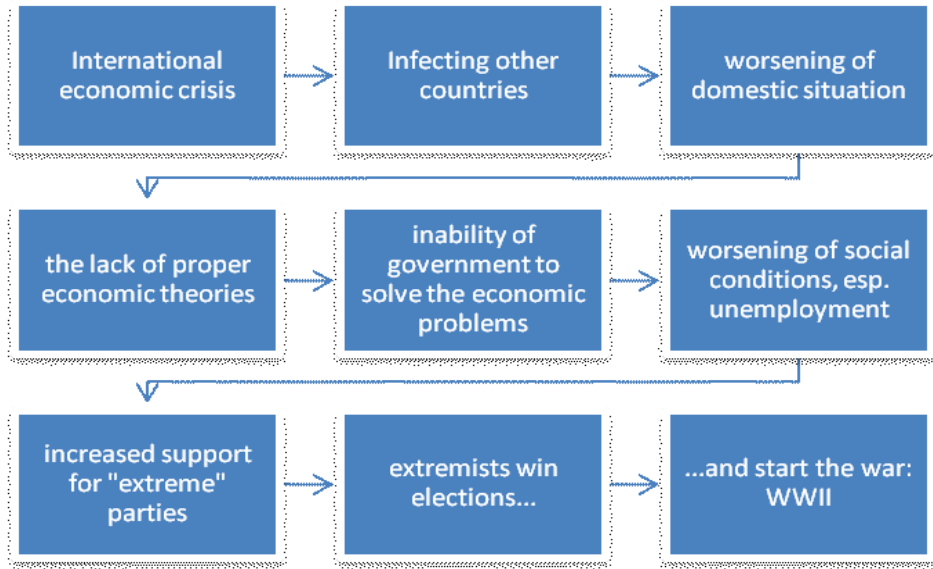


Note: Dashed line—votes for NSDAP (left scale) in millions, solid line—number of unemployed (right scale) in millions.

Source: (Kaltfleiter, 1968 S. 37) quoted after (Hermann, 1995 p. 84).

In most extreme situation, like in Germany in 1930s, the inability of policymakers to deal with economic problems that caused deterioration of situation of society (voters), may lead even to international conflicts. In consequence, millions may die.

Figure 38. From the Great Depression to WWII - sequence of economic and political relations



Source: own.

Thus, the recessions and anticyclical policy aimed at their elimination (or at least minimisation of their social consequences) are one of the most important goals of economic policy.

6.2. Economic impact of democracy and its elements

Below, we will present some empirical results on relations between different characteristics of democratic system and economy.

6.2.1. Democracy and economic performance

Having measures of democracy one can try to find linkages of it with economic growth. The results are twofold:

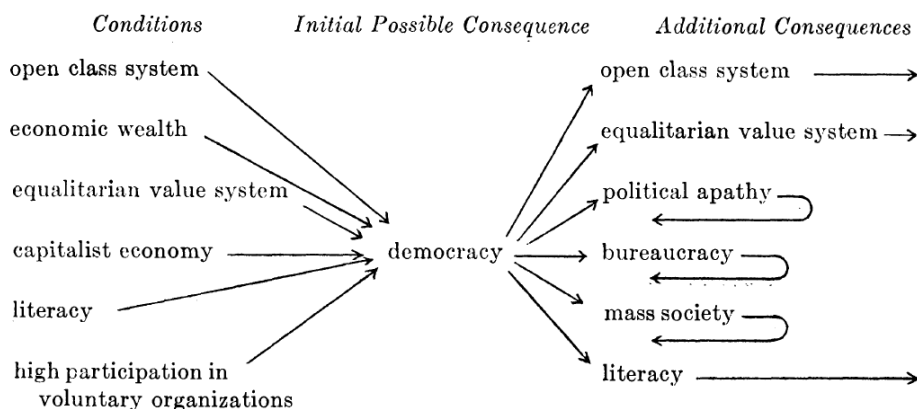
- On the one hand, some scholars find (non-linear) **correlation between growth and democracy** showing causation that democracy fosters development (e.g. (Barro, 1996) discovered that **democracy stimulates growth** on low levels of political freedom, but on higher ones it depresses growth). However, the **rule of law has stronger impact on income than democracy** and trade openness negatively influences democracy (Rigobon, et al., 2004).

- On the other hand, according to **Lipset's hypothesis** (Lipset, 1959), who derived his ideas from Aristotle (see the quote below), reaching higher levels of **development**¹² **stimulates** growth of probability of having **democracy** (Barro, 1996). This correlation is strong and most important for democratisation is primary school education; **democracy** is not related to the size of a country, but is **related to the share of middle-class** (Barro, 1999).

From Aristotle down to the present, men have argued that only in a wealthy society in which relatively few citizens lived in real poverty could a situation exist in which the mass of the population could intelligently participate in politics and could develop the self-restraint necessary to avoid succumbing to the appeals of irresponsible demagogues (Lipset, 1959 p. 75).

However, it must be remembered that economic wealth is not the only factor that influences democratisation processes (see Figure 39).

Figure 39. Diagram of possible connections between democracy, the initial conditions associated with its emergence, and the consequences of an existent democratic system



Source: (Lipset, 1959 p. 105).

Moreover, focus on growth policies, if they give too much delayed results, may lead to the increase of “**bureaucratic authoritarianism**” (O'Donnell, 1973), rather than to further development of democracy. There is an example of some Latin American countries (e.g. Argentina, Brazil) after the failure of their import-substitution industrialisation and expansion of domestic markets, which resulted first in emergence and second in failure of populist parties that targeted lower middle- and working-class groups (the “popular sector”). After that, they were replaced by:

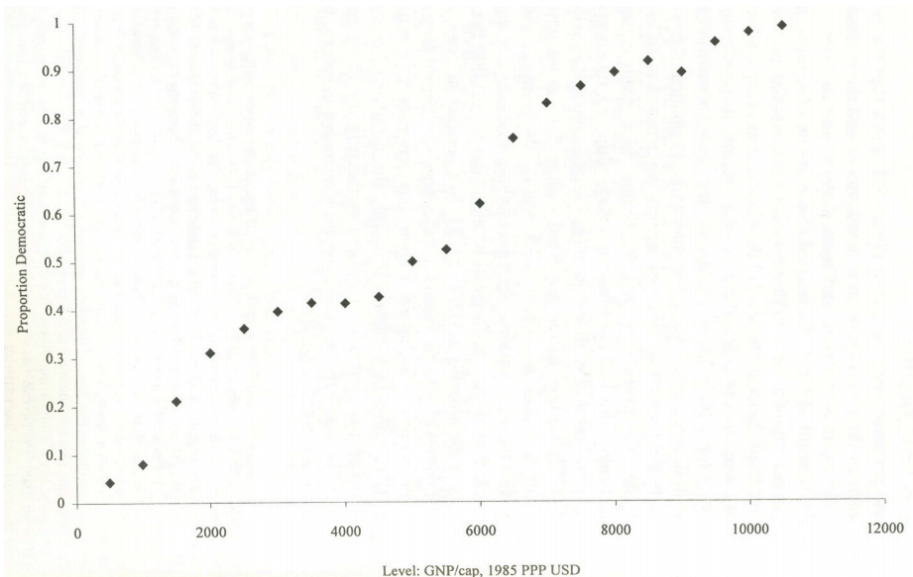
¹² It is approximated by per capita GDP, primary schooling and gap between male and female primary attainment.

- military regimes that tried to limit the influence of the popular sector, and
- technocrats, who focused on economic performance (O'Donnell, 1973) (Remmer, et al., 1982 pp. 3-4).

On the lower levels of development, it is possible to have the development both in democratic system and under a dictatorship (Przeworski, et al., 2000). During decolonisation processes in the 1960s some thought that in order to have a better economic performance, democracy should be sacrificed at least temporarily (Huntington, et al., 1976). This idea gained the support with the examples of Pinochet's Chile, contemporary China, Russia, or even Singapore. Such of thinking may give wrong policy recommendations and lead to poor results from the point of view of civil freedom or respecting human rights. The true casual relation is, however, not as simple: although **many "tigers" were dictatorships, not many dictatorship countries became "tigers"**. Moreover, there is new evidence from **post-socialist countries**, which usually have **higher rates of growth under democratic regime** than in the old system.

Democracy, once established, will almost certainly persist in countries with level of income over \$4,000 (Przeworski, et al., 2000 p. 273). Almost all the countries with an income over \$12000 are democratic.

Figure 40. Proportion of democratic countries on different levels of development, 152 countries, 1951–1999



Source: (Przeworski, et al., 2000 p. 80).

Despite the popular belief in the past, that authoritarian regime are necessary to stabilise and to foster growth (see example of Chile), the **development is much faster in democratic**

countries. Population in **democracies** grows slower, **labour productivity is higher**, **wages are higher**, and **technical progress is faster** (Przeworski p. 19).

6.2.2. Impact of electoral rules

*Coalition governments in parliamentary democracies produce **less efficient policies**, which end up with a bigger size of governments and higher budget deficits. They are more likely to happen in large district magnitude and proportional representation*

(Persson, et al., 2004 p. 96).

The proportional system favours voting for party lists rather than for individuals, as it is in the plurality system. Moreover, it is connected with more rent seeking and free-riding behaviour (in proportional systems the election is more related to the votes cast on the list than on individuals, and the re-election depends on the position on the list, which may depend on the will of the party leaders and not on the MP's performance).

In the presidential systems, there can be problems with sharing the power between the president and the congressional majority, if they are from different parties. Then, the problems with higher deficits may emerge.

Another interesting issue is the so-called **common-pool problem** of fiscal policy, which occurs in a situation when although the fiscal costs are paid by all taxpayers, only some of them are beneficiaries. In the U.S. such government money is often called the pork and such a policy—**pork-barrel politics**. There are many examples, including the EU structural funds that come from taxation of all of the countries, but benefit only some regions directly (indirectly all may eventually benefit). In such cases the beneficiaries are of course interested in pressing the government for increasing taxation what may lead to higher budget deficits and overspending, especially when there is a **coalition government** (Persson, et al., 2003 pp. 26-27). Such governments, although they have high propensity to engage in fiscal tightening, **are almost always unsuccessful in running fiscal adjustments** (only 9% of them among OECD countries succeed, while in case of single-party governments it was 36% and in minority governments 47%) (Alesina, et al., 1995 pp. 20-21). It is because such policies would require cuts in social expenditures and government employment, what in coalitions is difficult to agree. This confirms the general belief (and other empirical results) that **coalition governments run looser fiscal policies than single-party governments** (Roubini, et al., 1989), also because (in proportional voting systems) they are more vulnerable to government crises (Grilli, et al., 1991).

An interesting comparison of theory and empirical findings is presented in Table 7.

Table 7. Constitutions and economic policy: Questions and findings

<i>Policy outcome</i>	<i>Electoral rules</i> Majoritarian vs. proportional		<i>Form of government</i> Presidential vs. parliamentary	
	Theory	Data	Theory	Data
Overall size of government	–/?	–	–	–
Composition: Broad versus narrow programs	–	–	–	0/–
Rent extraction	+/?	+/?	–	0
Government deficits	–/?	–	?	0
Structural policy/Economic performance	?	+/?	?	–
Adjustment to shocks	?	0/–	?	–
Electoral cycles	+/?	+/?	?	+/?

Note: A plus (minus) sign in a column describing theory indicates that a constitutional reform, replacing the feature on the right at the top of the column with the feature on the left will induce a greater (smaller) degree or a higher (lower) level of the policy outcome for that row. A question mark indicates an unclear theoretical prior about the sign of the constitutional effect. The sign in the Data column indicates the direction of the empirically estimated effect of such a reform (a 0 indicates an inconclusive empirical result).

Source: (Persson, et al., 2004 p. 270).

The governments and welfare states are smaller in countries with a majoritarian system than in countries with proportional electoral systems. In particular, a change in regime from proportional to majoritarian results in a reduction of government spending by almost 5% of GDP, and lowering budget deficit by about 2% of GDP (Persson, et al., 2004 p. 270). Both theory and empirical findings show that **corruption is lower under plurality rule**, because individuals (and not the whole party, see free-riding behaviour) feel responsible for their own accountability which translates into voting results. One of the solutions to the common-pool problem is an introduction of a majoritarian system.

Empirical findings do not clearly decide which political system is better for the economic performance. It is quite widely accepted in political science on comparative politics and political economics literature, that the **choice of the electoral system** in practice is of **political nature** and bases on the **trade-off between the accountability and the representation** (Persson, et al., 2004 p. 272).

Interesting from the point of view of economic policy run in previous years in many countries is the fact that the **coalition governments** are more likely to be **less efficient** than the single-party governments in introducing reforms **responding to external shocks** (like e.g. financial crisis in the world). The reaction to the adverse shocks and economic downturns is also different:

- countries with a **majoritarian** regime (single-party governments) rather **cut taxes**,
- countries with **proportional** representation (coalition governments) rather **increase spending**, but later have difficulties in decreasing them during upturns (Persson, et al., 2004 p. 273).

Of course, this is a general historical rule and the data did not include the stabilisation policy during last few years (run e.g. in the US).

6.2.3. Impact of forms of government

Some scholars argue that there is no strong correlation between different kinds of political systems (parliamentary, presidential) and economic performance. However, a **parliamentary system provides better growth-promoting policies**, which in turn positively affect labour productivity (Persson, et al., 2004). It does not mean that the presidential system is inefficient, but in combination with a low quality of democracy, it gives poorer economic results, because a strong executive power may lead to its abuse (Persson, et al., 2004).

Others see the advantages of parliamentary democracies over presidential or semi-presidential regimes much clearer, and find evidence of negative influence of military regimes on economic growth (and even there, political pluralism in legislature influence growth positively), what underlines the important roles of institutions (Przeworski p. 20).

Similarly to the majoritarian system, **the government size is smaller by about 5% of GDP in a presidential system**. After the elections, the spending is cut by 1% of GDP. However, the overall **economic performance and on productivity is worse in less solid democracies**, mainly due to weaker structural policies in presidential systems (and smaller care about legal infrastructure and property rights) (Persson, et al., 2004 pp. 274-275).

6.3. Introduction to the political business cycle

Below we will assume that we only take into account such political systems, which are based on democracy, where the authority comes from the public choice. Thus, theory of the public choice may be applied. We also assume that the elections are won by a political program, which proposes the greatest probability of the realization of the social needs of particular groups of society.

In accordance with the concepts of the **political business cycle**, the rulers deliberately steer the economy in a direction that its assessment by society would maximize the number of votes. Then, **economic and social policies are treated instrumentally by politicians**. Politicians will tend to obtain such a state of the economy, the assessment of which by the public prior the forthcoming elections would increase the likelihood of their re-election. It does not have to be one-time behaviour; it can be repeated causing the political business cycles.

This simplistic view may, however, be more sophisticated in practice, because after the elections, some electoral campaign pledges should be fulfilled and longer-term relations

with social groups supporting a candidate or a party before elections should be kept (although it may result in corruption etc.). Even though, the political business cycle may repeat.

Moreover, society can identify this type of behaviour of politicians and make voting decisions keeping in mind such behaviour. Thus even when rational decisions are made, the political cycle can take place due to the fact that asymmetric information between government and society with regards to the state of the economy and scale of political decisions persists. In this case, the government's easiest move among different macroeconomic indices is to influence spending. This will of course affect other measures of economic conditions, including inflation. If we take the short term Philips curve into account, this behaviour will have its effect on unemployment, as well, with a certain time lag (so that the unemployment rate will not rise before elections).

Wherein there exists an important demarcation (although in practice it is very smooth):

- Politicians are opportunistic or ideological.
- Voters are naïve or rational.

Political parties opportunistically attempt to **influence voters** mainly through spending money on their **election campaigns** and make election **promises** that can be so huge that later on, the society may eventually realize they are impossible to introduce. Therefore, politicians function in a populist way, hoping that they will collect more votes by fulfilling the preferences (expectations) of a majority of voters.

After the elections, however, part of the promises remain unfulfilled, in hope that voters will forget them by the time the next elections come by and they will still vote for the same party.

Voters can also make decisions based on their long run interests and judge the program according to its probability of coming to life (rationally). They can support an **opportunistic party**, if they believe the program is **coherent**.

Ideological parties on the other hand target a certain group of voters, based on their political preferences that can be frequently expressed by either left-wing or right-wing in accordance to their political program. Again, they can treat voters as irrational or rational.

Rational voters are those who fulfil the following **criteria**:

- Take all available information in consideration when making decisions.
- Judge the actual program and functioning of a party, and not its past behaviour.

Their expectations are rational, what means that the voters can foreshadow the effects of their own decisions and adapt to them.

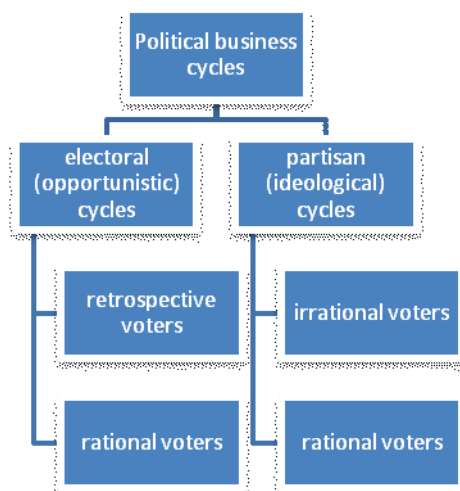
Irrational voters do not fulfil these criteria; they particularly consider future behaviour of a party instead of manipulative budgetary spending. If all the voters were rational, governments would not be able to influence changes in real economic indicators (such as production or unemployment). Politicians can, however, influence nominal values (inflation, transfers). Even in a highly educated population with access to information about the state of the economy and politicians, naïve voters still exist. The government is able to influence actual economic situation, and therefore the **political cycle will persist** both if we consider fully rational voters or only naïve ones and the mix of them.

In accordance with some research, a candidate party fighting for re-election after four years of taking the office is judged by its politics employed and introduced during these four years, and not on the basis of successes or failures of previous terms or of other previous political parties. The preferences of voters depend more on the state of the economy in the election period than what happened four years before (Mueller, 1989 p. 301).

There are two major groups of effects connected with the PBC:

- The shift in the state of economy described by the change of basic macroeconomic indicators influenced by the organization of state-wide elections is called the voting or **opportunistic cycle**.
- The second type of political cycle appear when the economic situation is affected not by the fact of elections taking place at any given moment, but by the change of the ruling party (coalition). This can occur for even a dozen or several dozen years. This is the political or **ideological cycle**.

Figure 41. Kinds of political business cycles



Source: own.

Without going into details regarding various types of business cycles, we should know that we could name several of them basing on the differences of their length. One of such probably most frequently identified cycles are the medium-run business cycles (which are also called the Juglar cycles), which last approximately 8-10 years. Another kind is the four year, short-term cycle (which we refer to as the Kitchin cycles). It is accepted that their occurrence can be caused not only by real changes, but also by the impact of politics. In the U.S., they are called the “**presidential cycles**”.

6.4. Kinds of political business cycles

Despite the fact that some consider the beginnings of the political cycle theory in the works of Joseph Schumpeter (1939), it is more commonly believed that it was derived from the article of **Michał Kalecki** published in 1943.

His view was based on class theory of business cycles.

...lasting full employment is not at all to their [business leaders—KP] liking. The workers would 'get out of hand' and the 'captains of industry' would be anxious to 'teach them a lesson'. (...) In this situation a powerful alliance is likely to be formed between big business and rentier interests, and they would probably find more than one economist to declare that the situation was manifestly unsound. The pressure of all these forces, and in particular of big business—as a rule influential in government departments—would most probably induce the government to return to the orthodox policy of cutting down the budget deficit. A slump would follow in which government spending policy would again come into its own.

This pattern of a political business cycle is not entirely conjectural; something very similar happened in the USA in 1937-8. The breakdown of the boom in the second half of 1937 was actually due to the drastic reduction of the budget deficit. On the other hand, in the acute slump that followed the government promptly reverted to a spending policy.

The regime of the political business cycle would be an artificial restoration of the position as it existed in nineteenth-century capitalism. Full employment would be reached only at the top of the boom, but slumps would be relatively mild and short-lived.

(Kalecki, 1943 p. 355)

According to (Kalecki, 1943), business cycles are the result of periodical changes of proportions or power between employers and employees. Whenever the strength of employees and unions was on the rise, salaries were rising as well, and employers were losing profits, they were resorting to countermeasures. These actions were meant to cause recession causing in turn unemployment and leading to victory over unions (Hermann, 1995 p. 80). In addition, although the governments are able to influence economic magnitudes, they will not tend to reach the full potential of economy (full employment), due to the 'power of vested interests'¹³. Such an approach was later adopted also by Nicholas **Kaldor**, who argued that

¹³ Later in his paper Kalecki has called for a reform of economic systems to create the "full employment capitalism" through development of new social and political institutions which will increase the power of the 'working class'. In his last paper (co-authored with T. Kowalik), published (in Italian) in 1971 after his death, he did not mention the creation of such institutions anymore. He observed that after WWII interventionism (including state purchases of military products) became the institution that has lowered unemployment rates to just a few percent only. Adding to that the growth of security systems, the position

such ‘interests’ were hostile towards the Keynesian economic policies adopted after WWII (Arestis, 1996 p. 27).

There are more advanced theories and descriptions of this phenomenon preached nowadays. Research on business cycles had been developed in the mid-1970s in the U.S. to reach its apogee in 1980s. As a result, research findings gained an established position in political economy and in textbooks on macroeconomics.

There are four groups of models of the political business cycles:

- Model with opportunistic parties and with irrational voters—Nordhaus’ opportunistic model;
- Model with opportunistic parties and with irrational voters—rational opportunistic model;
- Model with ideological parties and with irrational voters—ideological Hibbs’ model;
- Model with ideological parties and with rational voters—rational ideological model.

All of these models are based on the following assumptions:

- the economy is described by the Phillips curve,
- inflation is directly controlled by politicians,
- election date is known in advance and exogenously fixed.

1st PBC model

The first of political business cycle models was the **Nordhaus’ model** (Nordhaus, 1975). It was based on the following assumptions:

- inflation expectations are adaptive,
- politicians are opportunists (i.e. they only care about holding office),
- voters think “retrospectively”—they judge the authorities based on how they ruled so far and without anticipation of the future outcomes of their policy.

This theorem explains how measures leading to economy development are applied by the government in order to shape the economy before the elections and they are intended to increase chances of re-election. It was also based on an assumption of **adaptive expectations**, i.e. voter’s decisions are based on a **retrospective evaluation** of macroeconomic results, and inflation expectations will be fitted accordingly. In addition, Nordhaus assumed that **voters are short-sighted** and hence an opportunistic behaviour may appear repeatedly forming cycles. This was in turn based on assumptions that voters have an increased ability to forget the actions of manipulation before the next elections come.

The Nordhaus’ approach takes into consideration changes of business cycles caused with election date and not by ideology of political parties, among other possible factors of political nature that could influence business cycles. Nordhaus’ model predicts:

- pre-election economic growth, lower unemployment, inflation rise and
- a post-election economic slowdown.

of workers has improved, real wages have increased, and thus anticapitalistic mood has weaken (Kowalik, 2001).

Nordhaus implied that governments are responsible for both, fiscal and monetary policies. The government can influence both the nominal and real side of the economy. This pre-election policy is so expansive that post-election inflationary pressures are growing and the government is forced to eliminate them through policies that are more restrictive. After the elections, governments introduce a policy of preventing the side effects of their own actions conducted earlier with emphasis on fighting with the growth of inflation and unemployment.

Nordhaus' conclusions can be summed up in three statements:

- every government conducts the same policy,
- at the end of the term the government uses economic and social policy instruments to stimulate economic growth (and further to reduce unemployment), respecting the short-term Phillips curve, and
- as a result of the expansionary policy, after the elections restrictive policy must be introduced. PBC is therefore a regular succession of expansions and restrictions.

Nordhaus' research was soon abandoned because macroeconomists lost their interest due to the "revolution of rational expectations". Moreover, his model was lacking of empirical confirmations and outright McCallum in 1978 and Padam in 1979 presented negative results for the US and OECD economies (Alesina, et al., 1992 p. 663). The community of researchers returned to these issues only in the 1980s, with an exception of two influential papers published in 1970s.

2nd PBC model

Soon after Nordhaus' paper, another stream of research within the **opportunistic school** appeared. The second kind of PBC models introduced an element of classical thinking. It was initiated by (Kydland, et al., 1977) publicized in 1980s together with the critical approach of Keynes theories by (Barro, et al., 1983), and developed after 1986 by K. Rogoff, A. Sibert, T. Persson, and G. Tabellini. It was opposite to earlier macroeconomic ideas of Keynes, which were lacking empirical proof. This approach assumes that politicians and voters share the same preferences and require **rationality in inflation expectations** (Gartner 1999, p.705-706).

The assumptions are as follows:

- inflation expectations are rational,
- politicians are opportunists,
- voters choose a candidate from whom they rationally expect maximum benefits.

The retrospective point of view characterizes so-called "naïve voters", which are opposite to "rational voters", blessed with an "expected utility" point of view. The latter group understands and supports central role of rationality and coordination of monetary policy, which in turn constitutes the foundation of the European Monetary System (Gärtner, 1999 p. 706), which are the matters directly connected to the issues of the central bank's independence (see next subchapters).

This group of models can be divided into two subgroups:

- 1) In the first group, government cannot influence the real measures, thus there are only changes in inflation cycle. This is due to the long-term Phillips curve.
- 2) The second variant has yet additional assumption of asymmetric information between the government and voters—the first one know their powers, the second group is ignorant. Hence, the government can actually influence the real economy and the results are identical to the Nordhaus' model.

(Rogoff, et al., 1988), (Rogoff, 1990) and (Persson, et al., 1990) have changed the understanding of the Nordhaus theorem, which was abandoned prematurely, as they proved that business cycles may exist even assuming the rational expectations. This way of thinking was named the **rational opportunistic approach** or the theory of “rational political business cycle”. It assumes that voters lack information on competences of politicians. Several models of such thinking foresee apparent cycles of economic instruments usage as well as short, irregular cycles of economic variables, such as inflation rate or unemployment.

The models are based on the following assumptions:

- central bank and government cooperate;
- politicians enjoy autonomy in order to influence the economy.

However, there are two kinds of limitations to development of opportunistic policies:

- **internal limits**—if the central bank lacks in independence, it will likely put pressure on conducting monetary policy in line with fiscal policy. If such, the election cycle may be visible in monetary instruments, too. Hence, the introduction of central bank independence, which is intended to avoid opportunistic monetary policy, is crucial. In reality, central banks may be pushed into fulfilling the government's list of wishes as they are often threatened with a change of law on the central bank. If so or when the central bank is dependent, it may have to engage in a business cycle creation.
- **external limits** (international)—within the fixed exchange rates system, autonomy of economy is limited, hence the chances of a politically inclined business cycle are smaller (Leertouwer, et al., 2001 pp. 447-448).

3rd PBC model

The concept of the partisan cycle was initiated by (Hibbs, 1977). According to it, politicians are not opportunistic, but they run the economy in line with their ideological preferences, with the left-wing parties conducting policies that are more expansive and care more for unemployment than the right-wing ones, which are more focused on lowering inflation. Hibbs' model calls for systematic and stable changes in the relationship of inflation and unemployment. His research also focused on the independence of central banks.

Here are the assumptions:

- inflation expectations are adaptive,
- politicians are ideologised in the sense that different parties tend to reach for different goals,
- voters are aware of the ideological differences between the parties and choose the one that offers such policies that are attractive for them.

The fact that voters are irrational allows the government, as in the Nordhaus model, take advantage of the short-term Phillips curve. On this curve, the government chooses, in accordance with its political orientation and intentions, a point, which it wants to achieve and keep with their policies. Therefore, this model is sometimes called the ideological model with permanent effects.

4th PBC model

Rational ideological model was presented for the first time by (Alesina, 1987). It differs from the Hibbs' model with the assumption of rationality of voters. The assumptions are therefore as follows:

- inflation expectations are rational,
- politicians are ideologised in the sense that different parties tend to reach for different goals,
- voters are aware of the ideological differences between the parties and choose the one that offers them politics attractive for them.

Rationality of voters means that the Phillips curve is vertical, what changes the behaviour of the government completely compared to the situation of the previous model. It tries to fulfil its declared policy objectives related to unemployment rate and economic growth, as in the Hibbs' model. However, because of rational behaviour of voters, the real variables tend to return to their natural levels. Deviations in real measures can therefore only be temporal; the government can manipulate the economy in the short-run and only during its first term, because rationality of voters will not allow the re-induction of these deviations in subsequent periods.

6.5. Empirical verification

6.5.1. Electoral business cycle model

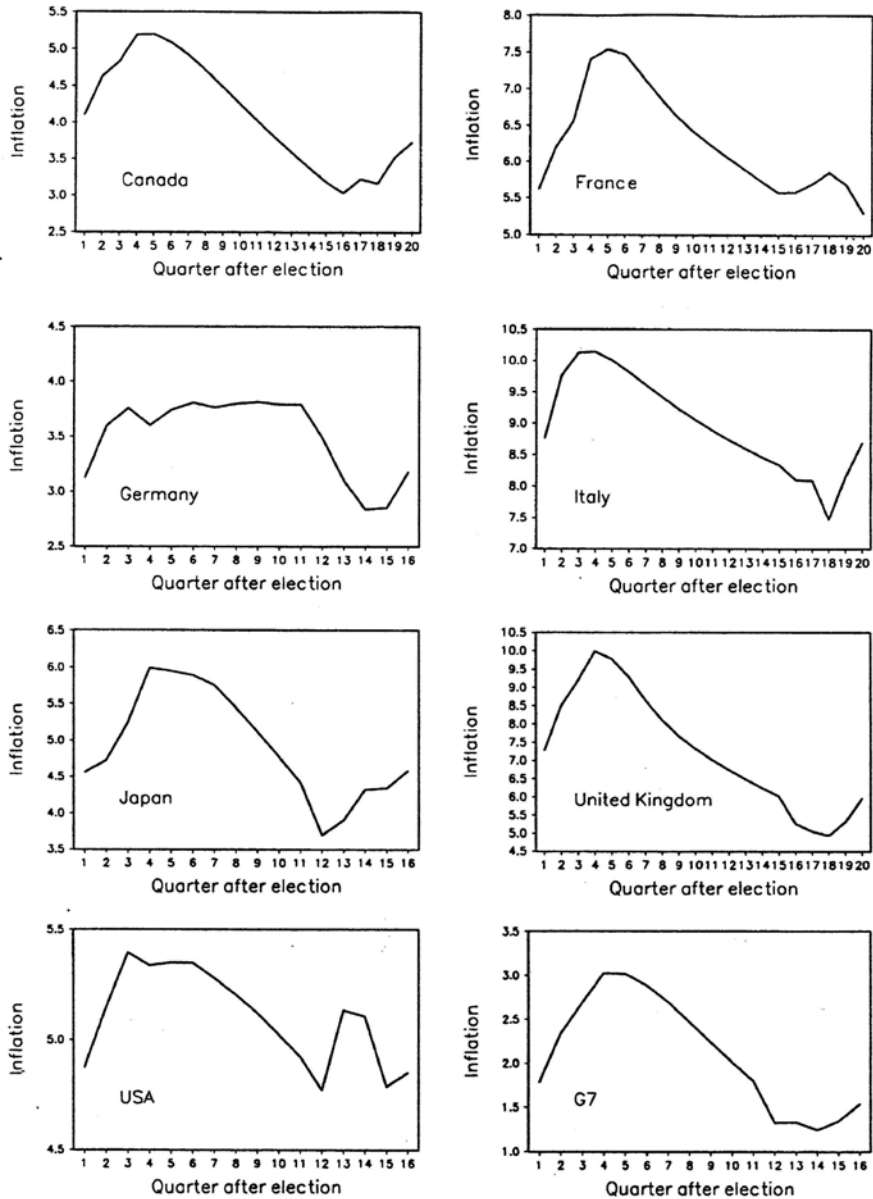
Both major concepts of the PBC: electoral and ideological cycles, were positively verified by empirical findings. Below we will present some examples of them.

According to (Gärtner, 1999), if the rational inflation expectation are assumed then inflation is determined by monetary policy only and does not reflect election cycles. However, when politicians maximize votes of retrospective voters, monetary policy determines inflation fluctuations as a function of elapsed time. Inflation rate decreases during parliament tenure, reflecting an election cycle.

It was empirically verified on a sample of G-7 countries in 1959-1993. The results have confirmed the existence of retrospective (naïve) voters. **Inflation rises for about four quarters after elections to start falling until next the elections.** This conclusion almost perfectly explained the overall trend of inflation processes in France and the United Kingdom, but fall short to clarify data from Canada, Italy and Japan. Germany and the United States

have differed the most but even there the inflation rates have risen for several quarters after elections to indicate a downward trend later on.

Figure 42. Inflation patterns in G7 countries, 1959–1993



Source: (Gärtner, 1999 p. 715).

Interesting but difficult to explain, was the rise of inflation one or two quarters before elections. It may be a side-effect expansionary economic policy introduced prior to the elections (the increase of budgetary expenditures or of money supply). It does not change the fact that in line with the concept of rational political business cycle, inflation rises and reaches its peak after elections. In the original Nordhaus' model inflation was also supposed to increase before the elections.

It is not just inflation, which shows fluctuations due to the existence of a political cycle. Alesina has analysed the period of 1972-1984 of the sample of OECD countries and noted: *In the majority (almost 65%) of the cases considered, the budget deteriorated in the election year relative to the preceding year (Alesina, 1989 p. 77)*. He, however, did not find support for the existence of PBC in changes of unemployment rates.

In technical analysis of stock markets, the term “**presidential cycle**” is known as one that supposedly exists in the US every four years. According to it, the prices of stocks plunge after elections, when the newly elected president makes unpopular decisions in order to heal the economy after the pre-electoral stimulation. In the medium run, the prices of stock market shares start to grow alongside the anticipation of the improvement of the condition of economy until the next elections.

One of many examples of the existence of election business cycles is the case of fiscal policy and currency rates analysed by a WTO employee (Schuknecht, 1999). The author elaborated a model based on data on 25 developing countries and conducted three different studies: In the first one, the budget equilibrium was calculated despite the exchange rate policy, the second one included the policy and the last one was conducted with a fixed currency and with adequate foreign exchange reserves.

Results prove that in countries with a floating exchange regime fiscal policy cycles tend to occur rarely. Independent of the current currency regime, the growth of budget deficit due to the elections was higher than average by 20%. Whereas in countries with a **fixed exchange rates** and adequate reserve levels the **fiscal deficit grows by nearly 1% of GDP during election period**. This translates into 25% of the average deficit.

Keeping an external financial balance of a country's balance of payments can be in danger in the case of falling investors' trust, which can lead to financial and currency crises. Attempts to increase the budget deficit before the election period, in an autonomous monetary policy, will lead to counter reactions of the central bankers. On the other hand, the government is endangered by a possible slowdown of economic growth (due to the increase of interest rates), which is contrary to its prior intentions of stimulating economic growth (in the short term). Thus, they will be forced follow much tighter budget policy contrary to its original intentions.

Brender and Drazen have analysed the period of 1960-2001. They found that increases in the government expenditures and deficits (relative to GDP) in election years take place predominantly in **new democracies**. The deficit increases by 0.8% of GDP after the transition to democracy (in 36 newly democratic countries they analysed) in the first elections (up to the first four) (Brender, et al., 2004).

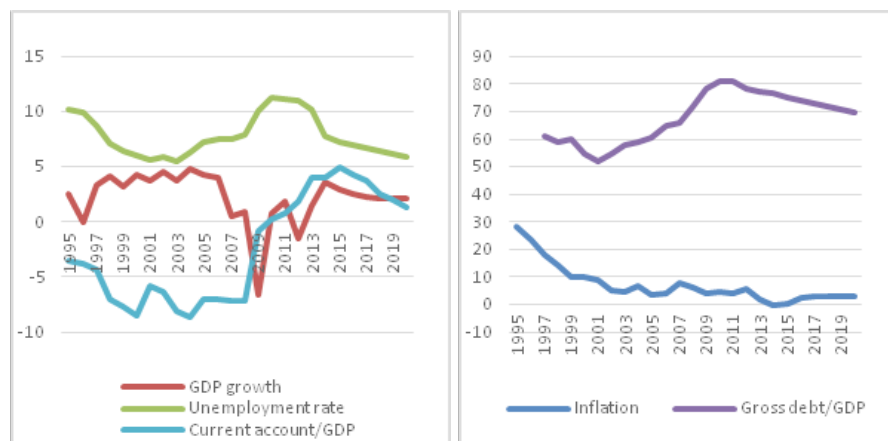
There are also many other studies proving that the PBC exists.

Box 26. Elections and deficits in Hungary

An interesting example is the case of Hungary. The PBC in this country can be studied there not with the use of some sophisticated econometric techniques, but it is visible with the unaided eye.

Hungary has started its transition quite impressively. However, after several years the current account deficits have increased, debt to GDP ratio has increased, to with the debts that followed it. The fiscal discipline was weak.

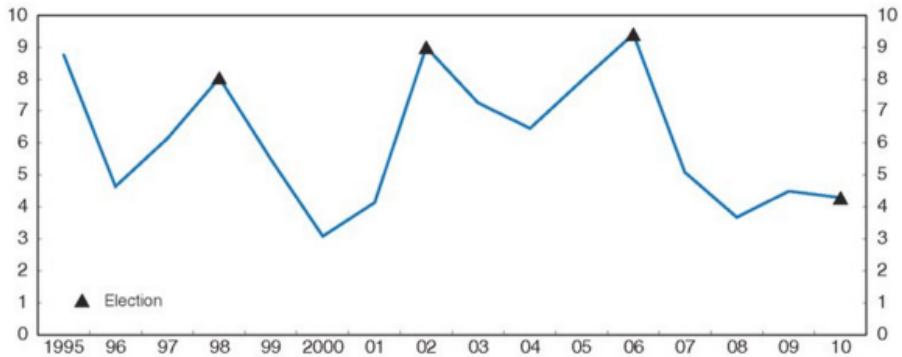
Figure 43. Selected macroeconomic indicators for Hungary since 1995 with forecasts up to 2020



Source: (International Monetary Fund, 2015).

There were also some social policy failures: in 2001-2002 the minimum wage has been increased by 100% (compared to 2000), what discouraged foreign investors, employment has declined (especially in SMEs, among elderly or less educated people and in areas with high unemployment), while the poverty has not decreased (since these are mainly unemployed people).

Since mid-1990s a clear electoral PBC in budget deficit is visible. Almost in every electoral year the budget deficit grew up. It peaked at almost 10% of GDP in the 2006 election year. This has changed during the 2010 elections due to adoption in 2008 of the Fiscal Responsibility Act (with fiscal rules) and due to introduction of independent Fiscal Policy Council in 2008 (later, it lost its independence).

Figure 44. General government deficit in Hungary and elections, 1995–2010

Note: values are expressed in percent of GDP. Dates of elections indicated with triangles.

Source: (OECD, 2012 p. 17).

Later, the deficits declined (from 5.5% in 2011 to 2.5% in 2014).

6.5.2. Ideological business cycles model

The phenomenon of partisan business cycles is particularly visible in countries with limited number of political parties including those having two-party systems. It can be observed in countries with a developed market economy and relatively old democratic traditions.

After studying several developed economies in 1945–1969 Hibbs noticed a correlation between the Left staying in power and unemployment, reaching -0.68 , as well as inflation: $+0.78$ (Hibbs, 1977).

His ideas were later developed by Alesina. The analyses of data of the period 1966–1986 confirm the existence of partisan business cycles. In almost all the cases, when the right-wing government was replaced with the left-wing ones, GDP growth followed and unemployment decreased (except for the Netherlands and Norway, for which the coefficients were statistically insignificant).

Table 8. Influence of change in government to the Left on growth and unemployment, 1966–1986

Countries	Output	Unemployment	Countries	Output	Unemployment
Australia	0.87	-0.29	Germany	0.39	-0.50
Austria	1.04	-0.24	Netherlands	0.67	0.36
Belgium	0.21	-0.53	Norway	1.04	0.01
Denmark	0.67	-0.42	Sweden	1.44	-0.16
Finland	2.32	-1.00	UK	1.51	-0.42
France	0.31	-0.67	US	2.51	-0.66

Note: output and unemployment for any country is measured as compared to the average of all other countries.

Source: (Alesina, 1989 p. 72).

The results presented above include only two out of many important macroeconomic goals of economic and social policy. A more representative picture should contain other data, like inflation rates, budget deficits or exchange rates and government debts. This phenomenon can be explained with political differences of both power systems and electorates, which are voting for them. This confirms that:

- with the Left in power, higher economic growth and lower unemployment can be observed, while
- during the right-wing governments lower budget deficits and a lower inflation rates may be seen.

The differences are caused by different weights attached by both kinds of political parties to certain economic policy goals:

Left wing government expand the economy when elected; for a while (about 2 years) they succeed, then inflation expectations adjust and the economy returns to its natural rate of growth. (...) When right wing governments are elected they fight inflation, causing a recession or a growth slowdown. Later in their term, the economy goes back at its natural rate of growth and inflation remains low.

(Alesina, et al., 1990 pp. 29-30)

6.6. Central bank independence and macroeconomic results

The issues of the central bank independence have been discussed in the framework of the new classical school since the mid-1980s. Rogoff in 1985 introduced a hypothesis stating that the positions of the central banks governors should be granted to risk-averse conservatives. This might prevent using monetary policy as an instrument of economy stabilizing, which could result in increase of inflation.

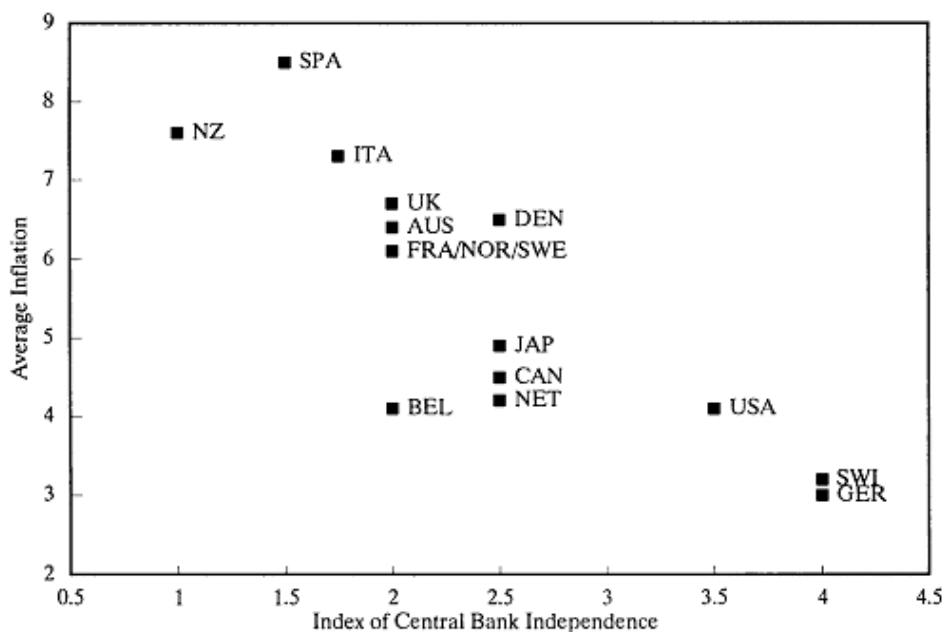
In order to analyse the above-mentioned issues, first quantitative indicators had to be elaborated. Alesina and Summers used the composite index presented by (Grilli, et al., 1991), who took into consideration the following issues:

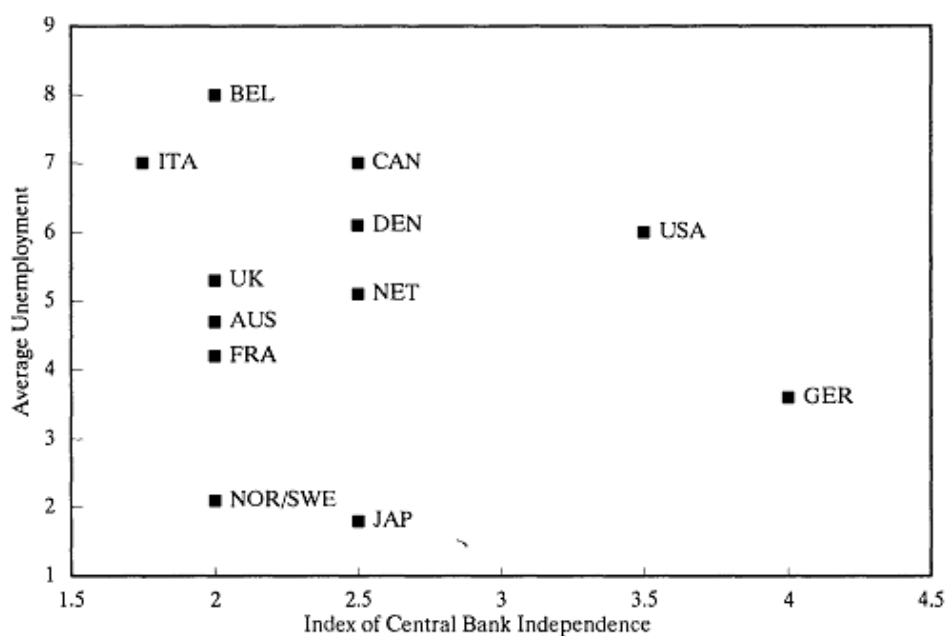
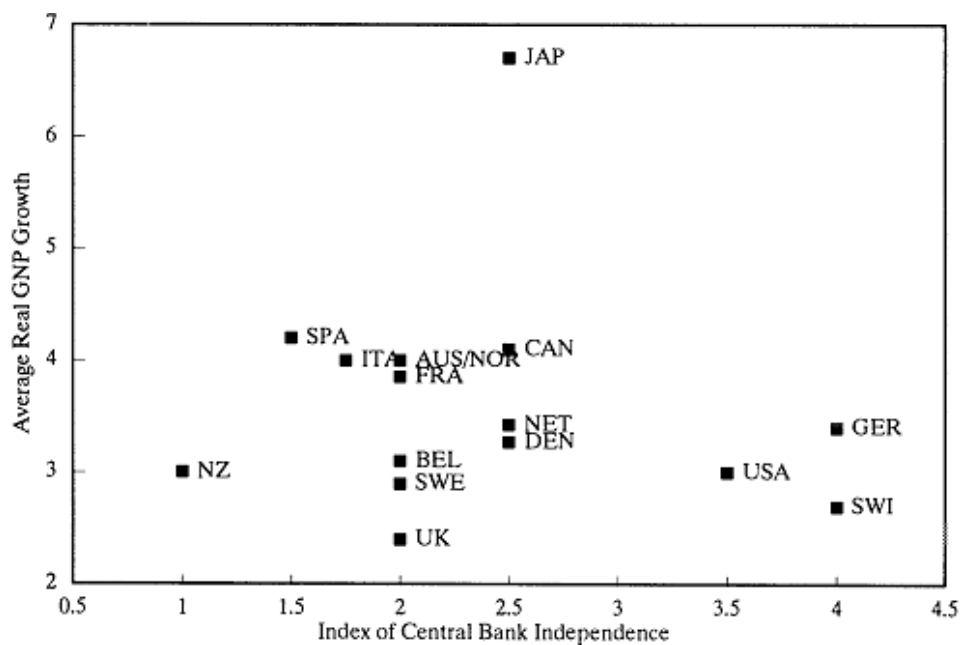
- the central bank's ability for an independent choice of monetary policy goals,
- procedure of central bank head election,
- ability to choose policy instruments with their scope and
- issue of budget deficit financing.

Their results show that the central bank's independence does not have any measureable impact on real economic performance, although it affects the inflation rate: its level and variability (Alesina, et al., 1993).

The correlation between inflation and central bank independence was clearly negative, while it did not exist in the case of e.g. GNP growth (and GNP per capita growth) and unemployment: both average level and its variance. As we have calculated based on the original data provided in (Alesina, et al., 1993), the linear correlation coefficient equalled to -0.84 and was statistically significant (at commonly accepted level of 5%), whereas the correlation coefficients between independence and average unemployment levels and average GBP growth rates were very low (0.06 and -0.12, respectively) and statistically insignificant.

Figure 45. Relation between central bank independence and average inflation, GNP growth and unemployment, 1955–1988





Source: (Alesina, et al., 1993 pp. 155-157).

Similar research was conducted for 14 Latin America countries for the period of 1999-2001. It also turned out that the central bank independence influences the inflation rate (although moderately). The decomposition of the index used has shown that a key factor influencing the above relation was the economic independence of a central bank (Jácome, 2001).

There are also many more studies confirming the relations analysed above. The overall conclusion is that the government should not expect that it will succeed in fighting e.g. with unemployment or economic growth through decrease of independence of central bank. The only result of such politics would be higher inflation rates. On the other hand, if politicians wants to treat the fight with inflation seriously, they should increase the independence of the central bank.

6.7. Partisan central bank hypothesis

The PBC literature traditionally assumed that only politicians are politically motivated. It does not have to be the whole truth. Central bankers may have political preferences, too.

The concept of politically motivated, partisan central banks was first presented by Roland Vaubel (Vaubel, 1993). Another German economist Gernot Sieg has modified it and expressed in the following way:

If incompetent government enjoying political majority and magnitude of party preferences in the central bank council during pre-election period, monetary expansion accelerates; while it slows down, when competent government has political minority in the council with heavy weight of party preferences during pre-election period
(Sieg, 1997 p. 505).

In result of his research, he concluded:

central bank's political independence does not prevent political business cycles occurrence but initiates it (...); if party politicians nominate central bankers, possibly party members, political business cycles will last
(Sieg, 1997 p. 514).

This means that the central bank's policy may have impact on government re-election chances, even in the case of fully rational voters. The manipulation may be visible through analyses of interest rates: if they are lowered prior to elections, it may imply central bank's influence on creation of political business cycle.

Some reject the views on partisan associated central banks. Linderlaub has criticised the Vaubel's hypothesis of partisan preferences of the members of the Bundesbank Council (the Bank is considered one of the most independent central banks in the world). He argued that with new members entering the Council, they change their views on inflation, making them

fit to the views of older members of the Council (Berger, et al., 1997 p. 809). The changes are caused by the organization of the Council (its members are changed twice during the term, each time half of members are replaced in order to maintain stability of the bank's monetary policy). This was called the **Thomas Becket effect**.

Box 27. Thomas Becket and his change of position on the Church

Thomas Becket (called also Saint Thomas of Canterbury, Thomas of London); born about 1118 and murdered in 1170, has been Henry's II of England Lord Chancellor since 1155. He became very effective in tax collection, including the revenues from churches and bishoprics.

Then, the King in 1162 has appointed his trusted counsellor to the position of priest, and the next day he was consecrated as the Archbishop of Canterbury (the leader of the Church of England). Once Becket took the new position, he resigned his chancellorship and became an orthodox clergyman opposing the King. The conflict between these two most powerful people of England intensified, especially because Becket did not want to sign the Constitutions of Clarendon, which were to give the King more independence, also from Rome. He also did not agree to crown the King's heir apparent by three other bishops, what was the privilege of archbishops of Canterbury. Finally, the conflict led to the assassination of Becket inside Canterbury cathedral by four King's knights. Two years after the death, he was canonised by the Pope Alexander III.

Berger and Woitek have analysed the monetary policy within the period of 1950-89. They concluded that the Bundesbank Council's decisions could not be explained by party associations of its members, although they noted that **council members elected by CDU/CSU government seemed to vote being politically biased** (Berger, et al., 1997 pp. 817-818).

The other research results were mixed. Some supported the Vaubel hypothesis, e.g.:

- Woll noted that the number of politically driven council choices has risen significantly during the tenure of social democrats (i.e. 1969-1982) (Woll, 1988).
- It was confirmed also in the case of the U.S. Federal Open Market Committee "both partisan ideologies and partisan loyalties appear to play an important role in the Governors' voting calculus" (McGregor, 1996).

and some did not:

- Dutch economists Leertouwer and Maier tested the possibility of a political business cycle creation by central banks of 14 OECD countries. They concluded that the hypothesis of the PBC based on short-term fluctuations has almost no foundation. There are two countries only, for which this might hold true: Austria and Japan (Leertouwer, et al., 2001 pp. 447-448).

Box 28. Partisan central bank in Poland?

The central bank in Poland has a constitutionally guaranteed independence. It was strengthened prior to the EU accession (it was a prerequisite for the entry into the European Union).

In July 2013 in a restaurant in Warsaw, a conversation between the governor of the National Bank of Poland Marek Belka (previously Deputy Prime Minister and Minister of Finance in 1997 and from 2001 to 2002, as well as the Prime Minister from 2004 to 2005) and the Interior Minister Bartłomiej Sienkiewicz was conducted. It was secretly recorded and later revealed in June 2014. It suggests that the central bankers could have had some opportunities to manipulate electoral outcome once e.g. some pivotal members of the Monetary Policy Council are persuaded to support the governor, who leads the Council (but does not have a majority there, as he has one vote only, out of ten in total). In exchange, the governor could eventually demand the removal of the minister of finance and his replacement by a “technical and apolitical” minister. This has actually happened in November 2013. Another Belka’s condition to support for the government was to allow the central bank to buy government debt on secondary markets. This law was introduced, as well.

Despite declarations of professor Belka that this talk was only a kind of “academic lecture”, together with other recorded meetings of politicians with businessmen and others, their publication substantially contributed to defect the ruling coalition in the 2015 elections.

Central banks may also influence economy (and modify the normal course of a business cycle) being politically motivated without any opportunistic intentions. They may take a high (political) responsibility on their shoulders trying to limit the consequences of financial crises and prevent longer economic recession. However, taking over by economists the role for which are usually responsible politicians can bring disastrous results.

References

- Acemoglu, Daron and Robinson, James A. 2005.** *Economic Origins of Dictatorship and Democracy*. Cambridge (UK) : Cambridge University Press, 2005.
- Acemoglu, Daron, Egorov, Georgy and Sonin, Konstantin. 2011.** A Political Theory of Populism. *NBER Working Paper*. 2011, 17306.
- Acocella, Nicola. 2005.** *Economic Policy in the Age of Globalisation*. Cambridge : Cambridge University Press, 2005.
- Alesina, Alberto and Perotti, Roberto. 1995.** Fiscal expansions and fiscal adjustments in OECD countries. *NBER Working Paper*. August 1995, 5214.
- Alesina, Alberto and Roubini, Nouriel. 1992.** Political cycles in OECD economies. *Review of Economic Studies*. 1992, Vol. 59, 4, pp. 663-688.
- . 1990. Political cycles in OECD economies. *NBER Working Papers Series*. October 1990, 3478.
- Alesina, Alberto and Summers, Lawrence H. 1993.** Central Bank Independence and Macroeconomic Performance: Some Comparative Evidence. *Journal of Money, Credit and Banking*. May 1993, Vol. 25, 2, pp. 151-162.
- Alesina, Alberto. 1987.** Macroeconomic Policy in Two-Party System as a Repeated Game. *Quarterly Journal of Economics*. 1987, Vol. 102, 3, pp. 651-678.
- . 1989. Politics and Business Cycles in Industrial Democracies. *Economic Policy*. April 1989, Vol. 4, 8, pp. 57-87.
- Alesina, Alberto, Angeloni, Ignazio and Etro, Federico. 2005.** International Unions. *American Economic Review*. 2005, Vol. 95, pp. 602-615.
- Álvarez-Rivera, Manuel. 2010.** Presidential and Legislative Elections in Chile, Parts I and II. *Election Resources on the Internet*. [Online] 28 January 2010. [Cited: 5 January 2013.] http://www.electionresources.org/cl/index_en.html.
- Anderson, James E. 2006.** *Public Policymaking: An Introduction*. 6. Boston : Houghton Mifflin, 2006.
- Arestis, Philip. 1996.** Kalecki's Role in Post Keynesian Economics: an Overview. [book auth.] John E. King. *An Alternative Macroeconomic Theory: The Kaleckian Model and Post-Keynesian Economics*. Boston/Dordrecht/London : Kluwer Academic Publishers, 1996, pp. 11-34.
- Aristotle. Politics**. [trans.] Benjamin Jowett. s.l. : The Internet Classics Archive. p. Part III. Vol. Book One, <http://classics.mit.edu/Aristotle/politics.html>.
- Armor, John C. 1994.** Foreshadowing Effects of Term Limits: California's Example for Congress. *Term Limits Outlook*. 1 June 1994, Vol. 3, 3.
- Aronson, Elliot. 2007.** *The Social Animal*. 10th edition. Basingstoke : Palgrave Macmillan, 2007.

- Arrow, Kenneth J. 1951.** *Social Choice and Individual Values*. New York : Wiley, 1951.
- Barr, Michael D. 2006.** The Charade of Meritocracy. *Far Eastern Economic Review*. October 2006.
- Barro, Robert J. and Gordon, David B. 1983.** Rules, discretion, and reputation in a model of monetary policy. *Journal of Monetary Economics*. July 1983, Vol. 12, 1, pp. 101-121.
- Barro, Robert J. 1996.** Democracy and Growth. *Journal of Economic Growth*. March 1996, Vol. 1, 1, pp. 1-27.
- . **1999.** Determinants of democracy. *Journal of Political Economy*. 1999, Vol. 107, 6, pp. 158-183.
- Basham Patrick. 2004.** Bring Back the Gov's Idea - Term Limits. *New York Daily News*. 5 October 2004.
- Basley, Timothy and Case, Anne. 1995.** Does Electoral Accountability Affect Economic Policy Choices? Evidence from Gubernatorial Term Limits. *The Quarterly Journal of Economics*. 1995, Vol. 110, 3, pp. 769-798.
- Becker, Gary S. 1983.** A Theory of Competition Among Pressure Groups for Political Influence. *The Quarterly Journal of Economics*. August 1983, Vol. 98, 3, pp. 371-400.
- Behrman, Jere R. 1983.** Review. *Population and Development Review*. Population Council, June 1983, Vol. 9, 2, pp. 377-379.
- Bénassy-Quéré, Agnès, et al. 2010.** *Economic Policy. Theory and Practice*. Oxford : Oxford University Press, 2010.
- Bend Doug. 2006.** Term Limits for Nebraska State Senators: A Challenge to the Future Effectiveness of the Nebraska State Legislature. *Creighton Law Review*. 2006, 40, strongy 3-39.
- Benedikter, Roland, Siepmann, Katja and Zlosilo, Miguel. 2015.** The Political Dimension: Chile After the Presidential and General Elections of 2013-What Future? [ed.] Roland Benedikter and Katja Siepmann. *Chile in Transition. Prospects and Challenges for Latin America's Forerunner of Development*. Cham : Springer International Publishing Switzerland, 2015, pp. 79-102.
- Berger, Helge and Woitek, Ulrich. 1997.** How opportunistic are partisan German central bankers: Evidence on the Vaubel hypothesis. *European Journal of Political Economy*. 1997, Vol. 13, 4, pp. 807-821.
- Berlin, Isaiah. 1962.** Does Political Theory Still Exist? [ed.] Peter Laslett and Walter G. Runciman. *Philosophy, Politics and Society*. Oxford : Basil Blackwell, 1962.
- Birch, Sarah. 2009.** *Full Participation: A Comparative Study of Compulsory Voting*. Manchester : Manchester University Press, 2009.
- Black, Duncan. 1958.** *The Theory of Committees and Elections*. Cambridge : Cambridge University Press, 1958.
- Blaug, Mark. 1992.** *The methodology of economics. Or how economists explain*. Cambridge : Cambridge University Press, 1992.
- Brender, Adi and Drazen, Allan. 2004.** Political Budget Cycles in New versus Established Democracies. *NBER Working Paper*. June 2004, 10539.

- . 2007. Why is Economic Policy Different in New Democracies? Affecting Attitudes About Democracy. *NBER Working Paper*. October 2007, 13457.
- Buchanan, James M. and Tullock, Gordon. 1962. *The Calculus of Consent: Logical Foundations of Constitutional Democracy*. Ann Arbor : University of Michigan Press, 1962.
- Calmfors, Lars and Driffill, John. 1988. Bargaining structure, corporatism and macroeconomic performance. *Economic Policy*. April 1988, Vol. 3, 6, pp. 14-47.
- Carroll, Susan J. 2001. The Impact of Term Limits on Women. *Spectrum: The Journal of State Government*. 2001, Fall, pp. 19-21.
- Centre for Responsive Politics. 2012. Top Interest Groups Giving to Members of Congress, 2012 Cycle. *Centre for Responsive Politics*. [Online] 12 November 2012. [Cited: 9 January 2013.] <http://www.opensecrets.org/industries/mems.php>.
- Chauvet, Lisa and Collier, Paul. 2009. Elections and economic policy in developing countries. *Economic policy*. July 2009, Vol. 24, 59, pp. 509-550.
- Chile: A System Frozen by Elite Interests. *The Electoral Knowledge Network*. [Online] [Cited: 4 January 2013.] http://aceproject.org/ace-en/topics/es/esy/esy_cl.
- CIA. Suffrage. *The World Factbook*. [Online] Central Intelligence Agency.[Cited: 10 November 2015.] <https://www.cia.gov/library/publications/the-world-factbook/fields/2123.html>.
- Creelan, Jeremy M. and Moulton, Laura M. 2004. *The New York State Legislative Process: An Evaluation and Blueprint for Reform*. New York : Brennan Center For Justice - New York University School of Law, 2004.
- Cummins, Jeff. 2013. The Effects of Legislative Term Limits on State Fiscal Conditions. *American Politics Research*. May 2013, Vol. 41, 3, pp. 417-442.
- Dahl, Robert Alan and Tufte, Edward Rolf. 1973. *Size & Democracy*. Stanford : Stanford University Press, 1973.
- Davis, John B. 2007. Heterodox Economics, the Fragmentation of the Mainstream, and Embedded Individual Analysis. [ed.] John T. Harvey and Jr., Robert F. Garnett. *Future Directions for Heterodox Economics*. Ann Arbor : University of Michigan Press, 2007, pp. 53-72.
- Dogan, Mattei. 1998. Political Science and the Other Social Sciences. [ed.] Robert E. Goodin and Hans-Dieter Klingemann. *A New Handbook of Political Science*. Oxford : Oxford University Press, 1998, pp. 97-132.
- Downs, Anthony. 1957. *An Economic Theory of Democracy*. New York : Harper and Brothers, 1957.
- Driffill, John. 2005. The Centralization of Wage Bargaining Revisited. What have we learned? *Birkbeck College*. [Online] November 2005. http://www.bbk.ac.uk/ems/faculty/driffill/research/corp_paper_b.pdf.
- Edin, Per-Anders and Ohlsson, Henry. 1991. Political determinants of budget deficits: Coalition effects versus minority effects. *European Economic Review*. December 1991, Vol. 35, 8, pp. 1597-1603.

- EIU. 2011. *Democracy index 2011. Democracy under stress*. s.l. : Economist Intelligence Unit, 2011.
- . 2015. *Democracy Index 2014. Democracy and its discontents*. s.l. : Economist Intelligence Unit, 2015.
- Erler, H. Abbie. 2007. Legislative term limits and state spending. *Public Choice*. December 2007, Vol. 133, 3, pp. 479-494.
- Eulau, Heinz and Prewitt, Kenneth. 1973. *Labyrinths of Democracy*. Indianapolis : Bobbs-Merrill, 1973.
- Ezrow, Lawrence. 2007. The Variance Matters: How Party Systems Represent the Preferences of Voters. *The Journal of Politics*. February 2007, Vol. 69, 1, pp. 182-192.
- Finkelstein, J. 2006. Maslow's hierarchy of needs. *Wikipedia*. [Online] 27 October 2006. https://commons.wikimedia.org/wiki/File:Maslow%27s_hierarchy_of_needs.png.
- Frankal, Elliot. 2005. Compulsory voting around the world. *Voter apathy*. [Online] The Guardian, 4 July 2005. <http://www.theguardian.com/politics/2005/jul/04/voterapathy.uk>.
- Freedom House. 2012. *Freedom in the World 2012: The Arab Uprisings and Their Global Repercussions*. Washington : Freedom House, 2012.
- . 2015. *Freedom in the World 2015. Discarding Democracy: A Return to the Iron Fist*. Washington : Freedom House, 2015.
- . 2015a. *Freedom of the Press 2015. Harsh Laws and Violence Drive Global Decline*. Washington : Freedom House, 2015a.
- Fund for Peace. 2012. Failed States Index. *The Fund for Peace*. [Online] 2012. [Cited: 5 January 2013.] <http://www.fundforpeace.org/global/?q=fsi-grid2012>.
- Garri, Iconio. 2010. Political short-termism: a possible explanation. *Public Choice*. October 2010, Vol. 145, 1/2, pp. 197-211.
- Gärtner, Manfred. 1999. The election cycle in the inflation bias: evidence from the G-7 countries. *European Journal of Political Economy*. 1999, Vol. 15, pp. 705-725.
- . 1999. The election cycle in the inflation bias: evidence from the G-7 countries. *European Journal of Political Economy*. November 1999, Vol. 15, 4, pp. 705-725.
- Google. 2015. Public Data. [Online] 8 November 2015. http://www.google.com/public-data/explore?ds=bqed7l430i2r6_&ctype=b&strail=false&bcs=d&nselm=s&met_x=indicator_137506&scale_x=lin&ind_x=false&met_y=indicator_103606&scale_y=lin&ind_y=false&idim=country:15503:10303:2403:3803&ifdim=country&tunit=Y&pit=333777.
- Goulet, Denis. 1971. *The cruel choice: A new concept in the theory of development*. New York : Atheneum, 1971.
- Grant, Ruth W. 2004. Political Theory, Political Science, and Politics. [ed.] Stephen K. White and J. Donald Moon. *What is political theory?* London : Sage Publications, 2004.
- Grilli, Vittorio, Masciandaro, Donato and Tabellini, Guido. 1991. Political and Monetary Institutions and Public Financial Policies in the Industrial Countries. *Economic Policy*. October 1991, Vol. 6, 13, pp. 341-392.

- . 1991. Political Monetary Institutions and Public Finance Policies in the Industrial Democracies. *Economic Policy*. 1991, Vol. 6, 13, pp. 342-392.
- Grofman, Bernard and Kline, Reuben. 2012. How many political parties are there, really? A new measure of the ideologically cognizable number of parties/party groupings. *Party Politics*. June 2012, Vol. 18, 4, pp. 523-544.
- Grossman, Gene M. and Helpman, Elhanan. 1991. *Special Interest Politics*. Cambridge, MA : MIT Press, 1991.
- Hermann, Adam. 1995. *Wirtschaftspolitik und Regierungssystem der Bundesrepublik Deutschland. Eine Einführung*. 3. Bonn : Bundeszentrale für politische Bildung, 1995.
- . 1995. *Wirtschaftspolitik und Regierungssystem der Bundesrepublik Deutschland. Eine Einführung*. 3. Bonn : Bundeszentrale für politische Bildung, 1995.
- Hibbs, Douglas A. 1977. Political Parties and Macroeconomic Policy. *American Political Science Review*. December 1977, Vol. 71, pp. 1467-1487.
- Huefner, Steven. 2004. Term Limits in State Legislative Elections: Less Value for More Money? *Indiana Law Journal*. 2004, Vol. 79, 427, pp. 427-492.
- Huntington, Samuel P. and Nelson, Joan M. 1976. *No Easy Choice: Political Participation in Developing Countries*. Cambridge : Harvard University Press, 1976.
- Huntington, Samuel P. 1993. *The Third Wave: Democratisation in the Late Twentieth Century*. Oklahoma : University of Oklahoma Press, 1993.
- International Monetary Fund. 2015. *World Economic Outlook Database*. October 2015.
- Jácome, Luis Ignacio. 2001. Legal Central Bank Independence and Inflation in Latin Amerika During the 1990s. *IMF Working Paper*. December 2001, 01/212.
- Johnson, Joseph M. and Crain, W. Mark. 2004. Effects of Term Limits on Fiscal Performance: Evidence from Democratic Nations. *Public Choice*. April 2004, Vol. 119, 1/2, pp. 73-90.
- Kalecki, Michał. 1943. Political aspects of full employment. *Political Quarterly*. 1943, Vol. 14, 4, pp. 322-331.
- Kaltefleiter, Werner. 1968. *Wirtschaft und Politik in Deutschland. Konjunktur als Bestimmungsfaktor des Parteiensystems*. 2. Köln und Opladen : s.n., 1968.
- Klepetar, Dillon T. 2011. Fiscal Implications of Legislative and Executive Term Limits at the State Level. *The Public Purpose*. Spring 2011.
- Kowalik Tadeusz. 2001. Michał Kalecki, kim był, jakim go znałem i podziwiałem. *Człowiek i Świat*. Warszawa : Fundacja Innowacja, 2001.
- Kraft, Michael E. and Furlong, Scott R. 2007. *Public policy. Politics, Analysis, and Alternatives*. 2. Washington : CQ Press, 2007.
- Kurdas, Chidem. 2012. Why Public Policy Is Inconsistent. *ThinkMarkets—A blog of the NYU Colloquium on Market Institutions and Economic Processes*. [Online] 19 January 2012. [Cited: 1 November 2012.] <http://thinkmarkets.wordpress.com/2012/01/19/why-public-policy-is-inconsistent/>.

- Kurtz, Karl T., Niemi, Richard G. and Cain, Bruce. 2007.** Introduction. *Institutional Change in American Politics: The Case of Term Limits*. Ann Arbor : The University of Michigan Press, 2007, pp. 1-9.
- Kydland, Finn E. and Prescott, Edward C. 1977.** Rules rather than discretion: the inconsistency of optimal plans. *Journal of Political Economy*. 1977, Vol. 85, pp. 473-491.
- Lasswell, Harold Dwight. 1936.** *Politics: Who Gets What, When and How*. New York : McGraw-Hill, 1936.
- Leertouwer, Erik and Maier, Philipp. 2001.** Who creates political business cycles: should central banks be blamed? *European Journal of Political Economy*. 2001, Vol. 17, 3, pp. 445-463.
- Leontieff Wassily. 1982.** Academic economics. *Science*. 1982, Tom 217, 4555, strony 104-107.
- Lipset, Seymour Martin. 1959.** Some Social Requisites of Democracy: Economic Development and Political Legitimacy. *American Political Science Review*. March 1959, Vol. 53, 1, pp. 69-105.
- Longley, Robert. 2005.** Smoking Deaths Cost U.S. \$92 Billion a Year. Total costs, including health care, more than \$167 billion yearly. *About.com—US Government Info*. [Online] July 2005. [Cited: 24 November 2012.] <http://usgovinfo.about.com/od/medicalnews/a/smokingcosts.htm>.
- Lundberg, Erik. 1974.** The Prize in Economics 1974 - Presentation Speech. *Nobelprize.org*. [Online] 1974. http://www.nobelprize.org/nobel_prizes/economics/laureates/1974/presentation-speech.html.
- Mahbubani, Kishore. 2008.** *The New Asian Hemisphere: The Irresistible Shift of Global Power to the East*. New York : PublicAffairs, 2008.
- Maira, Luis. 2001.** El amarre institucional del general Pinochet y las restricciones de la transición chilena. [ed.] Julio Labasida Martin del Campo and Antonio Camou. *Globalización, identidad y democracia: México y América Latina*. s.l. : Siglo xxi editores, 2001, pp. 82-110.
- Mandal, Sema, et al. 2009.** *Block, amend, delay: tobacco industry efforts to influence the European Union's Tobacco Products Directive (2001/37/EC)*. s.l. : Smoke Free Partnership, 2009.
- Mann, Thomas E. 1994.** Congressional Term Limits: A Bad Idea Whose Time Should Never Come. [ed.] Edward H. Crane and Roger Pilon. *The Politics and Law of Term Limits*. Washington D.C. : Cato Institute, 1994.
- Marshall, Monty G. and Cole, Benjamin R. 2011.** *Global Report 2011: Conflict, Governance, and State Fragility*. Vienna (VA USA) : Center for Systemic Peace, 2011.
- Marshall, Monty G. and Jagers, Keith. 2012.** Measuring Systemic Peace. *Center for Systemic Peace*. [Online] 31 October 2012. [Cited: 6 January 2013.] <http://www.systemicpeace.org/conflict.htm>.
- . 2012. Polity IV Project: Political Regime Characteristics and Transitions, 1800-2010. *Polity IV Project*. [Online] 2012. [Cited: 5 January 2013.] <http://www.systemicpeace.org/polity/polity1.htm>.

- McGregor, Rob Roy. 1996.** FOMC voting behavior and electoral cycles: Partisan ideology and partisan loyalty. *Economics and Politics*. March 1996, Vol. 8, 1, pp. 17-32.
- Ministry of Education, Singapore.** Principles of governance. *National Education*. [Online] [Cited: 24 12 2012.] http://www.ne.edu.sg/principles_of_governance.htm.
- Moon, J. Donald. 2004.** The Current State of Political Theory. Pluralism and Reconciliation. [ed.] Stephen K. White and J. Donald Moon. *What is political theory?* London : Sage Publications, 2004.
- Mooney, Christopher Z. 2007.** Lobbyists and Interest Groups. [ed.] Karl T. Kurtz, Richard G. Niemi and Bruce Cain. *Institutional Change in American Politics: The Case of Term Limits*. Ann Arbor : The University of Michigan Press, 2007.
- Morgan Theodore. 1988.** Theory versus empiricism in academic economics: update and comparison. *Journal of Economic Perspectives*. 1988, Tom 2, 4, strony 159-164.
- Mueller, Dennis C. 1989.** *Public choice II*. Cambridge : Cambridge University Press, 1989.
- Mundell, Robert Alexander. 1961.** A Theory of Optimum Currency Areas. *American Economic Review*. September 1961, pp. 657-665.
- Munroe, Trevor. 2002.** *An Introduction to Politics. Lectures for First-Year Students*. 3. Kingston : Canoe Press, 2002.
- Myers, Matthew L. 2012.** U.S. Judge Orders Tobacco Companies to Admit Deception and Tell the Truth to the American People. *Campaign for Tobacco-Free Kids*. [Online] 27 November 2012. [Cited: 2 December 2012.] http://www.tobaccofreekids.org/press_releases/post/2012_11_27_ruling.
- Nelson, Barbara J. 1998.** Public Policy and Administration: An Overview. [ed.] Robert E. Goodin and Hans-Dieter Klingemann. *A New Handbook of Political Science*. New York : Oxford University Press, 1998, pp. 551-592.
- Niskanen, William A. 1971.** *Bureaucracy and Representative Government*. Chicago : Aldine Press, 1971.
- Nordhaus, William D. 1975.** The political business cycle. *Review of Economic Studies*. 1975, Vol. 42, 2, pp. 169-190.
- O'Donnell, Guillermo A. 1973.** *Modernization and Bureaucratic-Authoritarianism: Studies in South American Politics*. Berkeley : Institute of International Studies, University of California, 1973.
- OECD. 2012.** *OECD Economic Surveys: Hungary 2012*. Paris : OECD, 2012.
- O'Hearn, Denis. 2009.** Amartya Sen's Development as Freedom: Ten Years Later. *Policy & Practice: A Development Education Review*. Spring 2009, Vol. 8, pp. 9-15.
- Olson, Mancur. 1982.** *Rise and Decline of Nations: Economic Growth, Stagflation, and Social Rigidities*. New Haven, CT : Yale University Press, 1982.
- . 1965. *The Logic of Collective Action: Public Goods and the Theory of Groups*. Cambridge, Mass. : Harvard University Press, 1965.
- Pappi, Franz Urban. 1998.** Political Behavior: Reasoning Voters and and Multi-party Systems. [ed.] Robert E. Goodin and Hans-Dieter Klingemann. *A New Handbook of Political Science*. Oxford : Oxford University Press, 1998.

- Parkinson, Cyril Northcote. 1958.** *The Evolution of Political Thought*. Boston : Houghton Mifflin, 1958.
- Payne, James L. 1991.** *The Culture of Spending: Why Congress Lives Beyond Our Means*. San Francisco : Institute for Contemporary Studies, 1991.
- Persson, Torsten and Tabellini, Guido. 2004.** Constitutions and Economic Policy. *The Journal of Economic Perspectives*. 2004, Vol. 18, 1, pp. 75-98.
- . 1990. *Macroeconomic policy, creditability and politics*. Chur Switzerland : Harwood Academia Publishers, 1990.
- . 2003. *The Economic Effects of Constitutions*. Cambridge : The MIT Press, 2003.
- Persson, Torsten, Roland, Gerard and Tabellini, Guido. 2003.** How do electoral rules shape party structures, government coalitions, and economic policies. *NBER Working Paper*. December 2003, 10176.
- Popkin, Samuel L. 1991.** *The Reasoning Voter: Communication and Persuasion in Presidential Campaigns*. Chicago : University of Chicago Press, 1991.
- Przeworski, Adam. 2006.** Constraints and Choices: Electoral Participation in Historical Perspective. *Department of Politics, New York University*. [Online] 2006. <http://politics.as.nyu.edu/docs/IO/2800/alessandria.pdf>.
- . Political Institutions and Economic Performance, 1950-1999. *United Nations Public Administration Network*. [Online] <http://unpan1.un.org/intradoc/groups/public/documents/un/unpan006223.pdf>.
- Przeworski Adam, Michael E. Alvarez, José Antonio Cheibub, Fernando Limangi 2000.** *Democracy and Development: Political Institutions and Well-Being in the World, 1950-1990*. Cambridge : Cambridge University Press, 2000.
- Rawls, John. 1971.** *A Theory of Justice*. Cambridge : Harvard University Press, 1971.
- Remmer, Karen L. and Merx, Gilbert W. 1982.** Beaucratic-Authoritarianism Revisited. *Latin American Research Review*. 1982, Vol. 17, 2, pp. 3-40.
- Rigobon, Roberto and Rodrik, Dani. 2004.** Rule of Law, Democracy, Openness, and Income: Estimating the Interrelationships. *NBER Working Paper*. September 2004, 10750.
- Robinson, Joan. 1964.** Kalecki and Keynes. *Problems of economic dynamics and planning: essays in honour of Michal Kalecki*. Warszawa : PWN-Polish Scientific Publishers, 1964, pp. 335-341.
- Rogoff, Kenneth and Sibert, Anne. 1988.** Elections and macroeconomic policy cycle. *Review of Economic Studies*. 1988, Vol. 55, pp. 1-16.
- Rogoff, Kenneth. 1990.** Equilibrium political budget cycles. *The American Economic Review*. March 1990, Vol. 80, 1, pp. 21-36.
- Rostow, Walt Whitman. 1960.** *The Stages of Economic Growth: A Non-Communist Manifesto*. Cambridge University Press : Cambridge, 1960.
- Rothstein, Bo. 1998.** Political Institutions: An Overview. [ed.] Robert Goodin and Hans-Dieter Klingemann. *A New Handbook of Political Science*. Oxford : Oxford University Press, 1998, pp. 133-166.

- Roubini, Nouriel and Sachs, Jeffrey. 1989.** Government Spending and Budget Deficits in the Industrial Countries. *Economic policy*. April 1989, Vol. 8, pp. 100-132.
- . **1989.** Political and Economic Determinants of Budget Deficits in the Industrial Democracies. *European Economic Review*. May 1989, Vol. 33, pp. 903-933.
- Schneider, Anne Larason and Ingram, Helen. 1997.** *Policy Design for Democracy*. Lawrence : University Press of Kansas, 1997.
- Schuknecht, Ludger. 1999.** Fiscal policy cycles and the exchange rate regime in developing countries. *European Journal of Political Economy*. 1999, Vol. 15, 3, pp. 569-580.
- Sen, Amartya. 1989.** Development as Capability Expansion. *Journal of Development Planning*. 1989, Vol. 19, pp. 41-58.
- . **1999.** *Development as Freedom*. New York : Alfred A. Knopf, 1999.
- . **1992.** *Inequality Reexamined*. Cambridge : Harvard University Press, 1992.
- Shapiro, Ian. 2004.** Problems, Methods, and Theories: What's Wrong With Political Science and What To Do About It. [ed.] Stephen K. White and J. Donald Moon. *What is political theory?* London : Sage Publications, 2004.
- Sieg, Gernot. 1997.** A model of partisan central banks and opportunistic business cycles. *European Journal of Political Economy*. 1997, Vol. 13, 3, pp. 503-516.
- Stambough, J. Stephen and O'Regan, Valerie R. 2009.** *Are Term Limits a Woman Candidate's Friend?* Toronto : American Political Science Association 2009 Annual Meeting, 2009.
- Stiglitz, Joseph E. 2002.** *Globalization and Its Discontents*. New York : W.W. Norton, 2002.
- Teichmann, Ulrich. 1993.** *Wirtschaftspolitik*. München : Verlag Vahlen, 1993.
- The Centre for Bhutan Studies and GNH Research. 2015.** Bhutan's 2015 Gross National Happiness Index. *Gross National Happiness*. [Online] November 2015. <http://www.grossnationalhappiness.com/SurveyFindings/Summaryof2015GNHIndex.pdf>.
- The Electoral Knowledge Network. 2015.** Comparative Data. *Public funding of parties*. [Online] 30 10 2015. http://aceproject.org/epic-en/research/PC/spreadsheet_country.
- The World Bank. 2015.** *Doing Business 2016. Measuring Regulatory Quality and Efficiency. Economy Profile 2016. Singapore*. Washington : The International Bank for Reconstruction and Development / The World Bank, 2015.
- Tinbergen Jan. 1956.** *Economic Policies. Principles and Design*. Amsterdam : North-Holland, 1956.
- Transparency International.** Corruption Perception Index 2014: Results. *CPI 2014*. [Online] [Cited: 10 November 2015.] <http://www.transparency.org/cpi2014/results>.
- Traub, James. 2009.** Absolute Fiction: The Perversion of Sovereignty. *World Affairs*. winter 2009.
- Tully, James. 2004.** Political Philosophy as a Critical Activity. [ed.] Stephen K. White and J. Donald Moon. *What is political theory?* London : Sage Publications, 2004.
- United Kingdom Parliament. 2010.** EU Tobacco Subsidy. *Parliament*. [Online] 25 February 2010. [Cited: 12 November 2012.] <http://www.parliament.uk/edm/2009-10/948>.

- United Nations. 2005.** *2005 World Summit Outcome*. A/60/L.1. s.l. : United Nations General Assembly, 15 September 2005.
- United Nations Development Programme. 2014.** *Human Development Report 2014. Sustaining Human Progress: Reducing Vulnerabilities and Building Resilience*. New York : United Nations Development Programme, 2014.
- . **2013.** Life expectancy at birth (years). *Human Development Reports*. [Online] 15 November 2013. <http://hdr.undp.org/sites/default/files/69206.xlsx>.
- United Nations. 1948.** Universal Declaration of Human Rights. Paris : United Nations, 1948.
- Vaubel, Roland. 1993.** Eine Public-Choice Analyse der Deutschen Bundesbank und ihre Implikationen für die Europäische Währungsunion. [ed.] Dieter Duwendag and Jürgen Siebke. *Europa vor dem Eintritt in die Wirtschafts- und Währungsunion*. Berlin : Duncker and Humbolt, 1993, pp. 23-80.
- von Hayek, Friedrich August. 1956.** The Dilemma of Specialization. [ed.] Leonard White. *The State of the Social Sciences*. Chicago : University of Chicago Press, 1956, pp. 462-473.
- Weimann, Joachim, Knabe, Andreas and Schöb, Ronnie. 2015.** *Measuring Happiness. The Economics of Well-Being*. Cambridge, Massachusetts and London, England : The MIT Press, 2015.
- Wikipedia.** Binomial voting system. *Wikipedia*. [Online] [Cited: 31 October 2015.] https://en.wikipedia.org/wiki/Binomial_voting_system.
- Woll, Artur. 1988.** Die Unabhängigkeit der Deutschen Bundesbank muß gesichert werden. *Wirtschaftsdienst*. 1988, 3, pp. 122-124.
- Yakovlev, Pavel A., Tosun, Mehmet S. and Lewis, William P. 2012.** Legislative Term Limits and State Aid to Local Governments. *IZA Discussion Paper*. March 2012, 6456.
- Young, Iris Marion. 1998.** Political Theory: An Overview. [ed.] Robert E. Goodin and Hans-Dieter Klingemann. *A New Handbook of Political Science*. New York : Oxford University Press, 1998, pp. 479-502.
- Zhang, Jun and Gao, Yuan. 2008.** Term limits and rotation of Chinese governors: do they matter to economic growth? *Journal of the Asia Pacific Economy*. 2008, Vol. 13, 3, pp. 274-297.