APPLIED ECONOMICS

SER

Low Turnout: Reducing Demand for Income Redistribution and the Development of the Welfare State?

Doireann O'Brien

In this paper, Doireann examines the relationship between low voter turnout in elections and its impact on the demand for income redistribution policies, as well as the development of the welfare state. She outlines the existing literature, which draws on theories of political economy to explain this negative relationship between low turnout and income redistribution policies. She then critiques the main used, that of Meltzer-Richard, showing how the sample used means the findings can only be applied to developed countries, and finds assumptions regarding bureaucratic efficiency and governance quality are needed to apply their model to the developing world.

In this paper, I analyse the validity of the hypothesis that low voter turnout reduces the demand for income redistribution and the development of the welfare state as put forward by Meltzer and Richard (1981). I briefly trace the academic roots of this claim by seeing the Meltzer and Richard model as the culmination of a history of academic development from Hotelling (1929), through Black (1948) and Downs (1957) (and later adapted by scholars such as Lijphart (1997)). I analyse the validity of the Meltzer-Richard model against well-respected empirical evidence and find that, while econometric analyses offer support for the model, once overall government size is replaced with pure redistribution as the dependent variable, sampling issues render external validity questionable since developing countries are excluded from the literature. I develop two arguments, related to bureaucratic quality and governance strength, as to why the Meltzer-Richard hypothesis and the title proposition may be invalidated when applied to developing regions. I conclude that additional assumptions capturing the fact that the model s success is contingent on the level of development of the context would heighten its predictive power and promote understanding of these mechanisms more clearly in developing regions, where welfare state development could arguably be in most urgent need.

The Meltzer-Richard model was not generated in a vacuum and understanding its debt to Black and Downs, and their academic antecedents, is useful. Hotelling initiated spatial economic theorisation and rejected the representation of the market as a "…point, without length, breadth or thickness" (Hotelling, 1929, p.44). The characterisation of markets as populated by a single, homogenous good and the treatment of markets as lacking in a spatial dimension prohibits insight into economic phenomenon that ought to be understood. Firstly, in terms of physical space, he demonstrates that sellers will strategically converge geographically to capture the demand of the maximum number of consumers by, if we conceptualise the phenomenon as one-dimensional, capturing the entire consumer-base to one side of the already stationed seller (Hotelling, 1929). Similarly, in terms of product characteristics, he explains that new entrants to a market make marginal adjustments to existing products to capture the proportion of the established sellers demand whose preferences will be marginally better matched by the slightly differentiated product. Briefly noting that a similar interpretation of political competition among parties could help understand tendencies for party platforms to converge, he paved the way for Duncan Black to develop the median voter theorem. This theorem states that with a decision taken on any topic by means of voting (Black, 1948, p.34) the median voter is decisive in determining the outcome due to their crucial position on the spectrum of preferences.

It is demonstrated mathematically that if preferences were ordered, the median voter's preference will consistently be a Condorcet winner among the group, and thus this determines the outcome (Black, 1948; Mueller, 2003.). Importantly this model only holds under strict assumptions of voters having single-peaked preferences over the ordering of policy alternatives in a single dimension, with majority rule in operation (Mueller, 2003). Downs applies this theory to the political domain, with his spatial theory of democracy being a crucial turning point within political economy s conceptualisation of electoral politics. Downs states that under the conditions of a unidimensional policy space, perfect information, majoritarian voting, rational utility maximising voters with single-peaked preferences, two-party competition between purely office-seeking candidates, the median voter theorem can be used to explain why party platforms tend to converge towards the median voter preference (Downs, 1957).

Informed by Black, Downs and the contributions of De Toqueville (1835), Romer (1975), and Roberts (1977), Meltzer and Richard developed their model to apply the median voter theorem of party competition to the issue of redistribution. By setting the single issue on which voters base their party preferences to the level of redistribution, Meltzer and Richard illustrate the impact of income inequality on the size of government with the important theoretical step of balancing the budget. By dismissing the assumption that voters suffer from a fiscal illusion which would lead to myopic demand for total redistribution from lower income voters, the predictive ability of the model was heightened significantly (Meltzer and Richard, 1981). Their central thesis is as follows: […the size of government is determined by the welfare maximising choice of the decisive individual…With majority rule the voter with median income among the enfranchised citizens is decisive The decisive voter chooses the tax share.] (Meltzer and Richard, 1981, p.924). They recognise that the expansion of the franchise to lower income citizens in the nineteenth and twentieth centuries in industrialized states caused the decisive voter to be in favour of higher levels of redistribution which would maximise their utility as welfare recipients.

Applying this theory to increased turnout among the already franchised, Lijphart, informed by a rigorous review of the empirical data on the income distribution of voters and non-voters, argues that since low voter turnout means unequal and socioeconomically biased turnout (Lijphart, 1997, p.2) increased political participation by voting should induce increased redistributive spending and welfare state development, aligning with the Richard-Meltzer model s predictions (Lijphart, 1997). By increasing voter turnout, the median voter moves down along the income distribution and the decisive preference becomes in favour of increased redistribution, to which office-seeking and pre-committing politicians respond, giving rise to the title hypothesis.

The credibility of the Meltzer-Richard model and the proposition up for discussion hinges on how their predictions align with empirical findings. Lindert (1996) provided early indirect support for the model by finding unconvincing evidence for the hypothesis that the deadweight losses (such as the accelerating costs of bureaucracies as proposed by Niskanen (1971)) is a key explanatory variable determining the level of social welfare expenditure. Instead, the key determinants of the level of redistribution within OECD countries were the relative sizes of age groups, electoral conditions, the income level, and most relevant here, the income distribution, providing an indication that the Meltzer-Richard model was promising. Husted and Kenny (1997) acknowledge a general lack of empirical support for the model at that time (Pelzman, 1980; Inman, 1978; Murell, 1985) and address this by highlighting the importance of differentiating between policies of general public expenditure on government services and pure redistributive social policy. Those below the median income level are unambiguously predicted by the Richard-Meltzer hypothesis to demand increased pure redistribution. However, when it comes to government services, the expected preferences of those lower income voters are ambiguous, according to Husted and Kenny, due to conflicting income and price elasticities of demand for state services (Husted & Kenny, 1997).

By correcting for this and setting the model s dependent variable to a measure of redistribution, the results of an econometric analysis of the lifting of poll taxes and literacy tests in the US show strong support for the prediction that welfare spending rises as political power shifts from a state s richer citizens to its poorer citizens (Husted and Kenny, 1997, p.79), providing strong support for the title s proposition. Abrams and Settle use a quasi-experimental approach to analyse the effects of the enfranchisement of women in Switzerland in 1971 and validate the findings of Husted and Kenny (1997). Discovering that enfranchising women led to a surge of 28% in public social spending, they claim that the underlying mechanism was largely the median voter s income shifting down the distribution as women had, on average, lower incomes due to gender-specific obstacles within the labour market and the appropriation of their share of household wealth by their male counterparts (Abrams & Settle, 1999). Similarly, noting the importance of differentiating between total expenditure and redistributive expenditure, Borge and Rattso (2004) exploit variability across local government districts in Norway to test the impact of income inequality among voters on the relative levels of the poll tax (a non-redistributive compulsory tax on domestic services such as waste removal) and the property tax (a redistributive tax) set by local representatives. They find that increased income inequality, as predicted, shifts tax weighting away from non-redistributive taxes to more redistributive ones, joining the growing body of literature validating the Meltzer-Richard model convincingly.

This review of the empirical evidence is supportive of the theory that low turnout reduces the demand for income redistribution and the development of the welfare state, to the point that it seems almost conclusively proved. However, upon deeper analysis, I identify a key issue that causes doubt in relation to the validity of this hypothesis. The fact that each of these papers tested the predictions of the model against data from exclusively developed countries (OECD members, the US, Switzerland and Norway respectively) means questions of external validity become pressing. Among the available empirical evidence, Larcinese s (2007) cross-country analysis is particularly insightful as he uniquely includes a substantial number of developing democratic countries in his sample. While the key objective of the paper is to explain why poorer countries do not have higher social spending levels by reiterating the importance of the distinction between income distribution of the population as a whole and that of the subset who vote, given the widely accepted evidence that turnout and income are strongly positively correlated, the significance of his results stretch far beyond what he claims. Importantly, Larcinese explains that the strength of his work does not lie so much in an innovative theory or specification, but in the comprehensiveness of his sample which covers longitudinal data for 41 countries, both developing and industrialised, for the period 1972-98 (Larcinese, 2007). He finds that while political participation is an important determinant of social spending levels across countries, country-specific features play a significant role in partially determining the size of the government and are decisive when the explanatory variable is income inequality of the population in its entirety rather than voters (Larcinese, 2007). The fact that the results are less conclusive than the studies mentioned above based solely on developed economies, it is worth exploring how the inclusion of less developed countries could be affecting the results.

In light of the absence of empirical tests focusing solely on the applicability of the Meltzer-Richard model to developing regions, paired with the literature highlighting the exceptionalism of welfare state development in developing democratic countries (Gough & Wood, 2004; Segura-Ubiergo, 2007), questions are raised that I will attempt to answer here - should we expect the Meltzer-Richard model to retain its predictive power when applied to developing regions, and if not, why not? I put forward two arguments as to why the Meltzer-Richard model is theoretically less credible for developing regions. The first relates to bureaucratic inefficiency and the second to poor governance, both of which are variables unaccounted for by Meltzer and Richard.

My first argument states that the assumptions of the Meltzer-Richard model allow for variability of bureaucratic efficiency, yet this can be shown to undermine its predictions when applied to developing contexts. The assumption that voters are sufficiently informed means they are aware of the labour substitution effects determining the tax base, and refrain from unsustainably demanding a 100% tax rate (Meltzer & Richard, 1981). A question left unaddressed by the model is whether voters are informed on the efficiency of their state's bureaucracy and the indirect welfare effects of market distortions through high taxes on the upper half of the income distribution and how these are offset by the subset of tax revenue that will reach them as transfers or services. Inefficiency causes the quantity of tax revenue that reaches those lower-income groups in the form of welfare transfers to be much lower than the amount of tax collected.

A UN study on the income inequality and fiscal policies of developing countries provides evidence for this, finding that most developing countries do not have adequate redistributive programs to achieve a greater post-tax, post-transfer income equality comparative to those of industrial countries (Chu et al., 2000, p.31). For the sake of conceptualising my argument, it is helpful to imagine bureaucratic waste is 100%, meaning no tax revenue is effectively redistributed - government distortions to the market by way of high levels of tax extraction from those above the median income level, without that being offset by effective redistributive bureaucratic activity, causes lower-income voters to be made indirectly less well off. For example, prices are likely to be pushed up due to the enlargement of the tax wedge on the producer side and unemployment of low-skilled workers is likely to rise also (Varian, 2014).

Important to note is that bureaucratic waste levels lie largely outside the control of the electorate and representatives, since bureaucrats transcend electoral politics and so this factor arguably also lies outside of the domain of the assumptions of the Meltzer-Richard model. Candidates can follow through on their election platform exactly as they promised by implementing the redistributive policy; it is simply that the implementation can fail due to inefficiency. Thus, one of two additional assumptions would improve the rigour of the model - either the assumption of a perfectly efficient bureaucracy or the assumption that voters have perfect knowledge of the level of bureaucratic waste if non-zero.

The latter assumption intuitively seems too unrealistic to be useful given that inefficiency is, by definition, covert. Despite this, it could conceivably reverse the predictions of the Meltzer-Richard model, thus invalidating it, when applied to countries with sufficiently ineffective bureaucracies. The implication that low-income voters in countries with inefficient bureaucracies could demand less welfare spending might seem implausible, however its possibility is empirically supported. Segura-Ubiergo finds empirical evidence on Latin American democracies to suggest that a low-income voter may vote against social spending if the benefits to them are unclear: [If median income decreases but the median voters perceive that social spending does not benefit them sufficiently (in terms of the cost borne in the form of higher taxes), then support for social spending will decline.] (Segura-Ubiergo, 2007, p.108). Segura-Ubiergo uses this to invalidate the Meltzer-Richard model in terms of social spending failing to be effectively redistributive across all income levels, however it also provides empirical grounding to my claim that similar patterns could be observed in reaction to bureaucratic inefficiency.

For this reason, I propose that the addition of the assumption of insignificant bureaucratic waste would correct for this, however, this roughly restricts the domain of the model to developed democracies, since bureaucratic waste and degree of economic development are widely evidenced to be negatively correlated (for instance Kaufmann, 2003). Relating this back to the statement at hand - lower voter turnout, I argue, does not lower demand for redistributive policy universally. This relationship is contingent on the condition holding that an efficient bureaucracy can roll-out policy with minimal waste, and hence renders the hypothesised relationship between turnout and redistribution at best tenuous in developing regions.

My second argument extends my justification that the title hypothesis loses credibility in developing countries, now looking at the role of governance which is again unaddressed by the Meltzer-Richard model s assumptions. In the existing literature on the link between turnout and redistribution, it is taken for granted that the existence of a political will among representatives to roll out redistributive policy in accordance with the preference of the median voter is sufficient for and analogous to the realisation of those outcomes. A variety of factors can prevent the successful roll out of policies preferred by the median voter, even when satisfying all the assumptions of the Richard-Meltzer model such as pre-commitment to platforms and candidates being purely office-seeking. Illegal markets, and tax avoidance and evasion can have grave impacts on the dynamics predicted by the Meltzer-Richard model. An office-seeking political representative, according to the Meltzer-Richard model, will choose redistributive policy according to the demands of the median voter, but even when that policy is passed and legislated for as committed to by the representative, it may be the case that the forecasted rates of redistribution as demanded by the median voter will not be generated ex-post, thus invalidating the model even when satisfying each assumption.

This is particularly problematic in less developed countries where there is weaker enforcement of tax policy (Chu et al, 2000), lower rates of formalised/taxable enterprise (Schneider & Enste, 2002), and more prevalent tax avoidance and evasion (Bird et al., 2008). Prevalent non-compliance with tax policy can be explained by a variety of factors but can be countered generally with effective enforcement accruing from strong governance, in which developing countries are characteristically lacking. Extensive evidence unsurprisingly supports this criticism - for example in the Italian and Canadian economies it was found by

Fugazza and Jean-François that increasing detection rates significantly decreases illegal economic activity (Fugazza & Jean-François, 2004) and Richardson, based on data from 47 countries finds that the lower levels of legal enforcement cause higher levels of tax evasion, after controlling for economic development (Richardson, 2008).

Therefore, I propose that an additional assumption is added to the Meltzer-Richard model of perfect tax compliance thus making the model especially non-applicable to developing countries where this is not achieved due to poor governance. The alternative is to interpret the implications of the model in a way that is stricter and less informative - that the shifting of the median voter down along the income distribution as a result of increased turnout can only go as far as to generate a political will or policy design for increased redistribution. In developed countries it is relatively unproblematic to make the leap from the emergence of a political will/policy design to predicted policy outcomes given relatively stronger governance, which ensures lower levels of illegal or informal economic activity, tax avoidance and evasion (Schneider & Enste, 2002). In developing regions however, it is crucial to peer inside that black box containing the sequence of events between policy support and implementation by representatives and the actual policy outcomes that are achieved.

There seems to be a general problem in the current literature of conflating ex-ante redistributive policy design and corresponding ex-post redistributive policy outcomes - while voters demand and can vote on variations of the former, it is less clear that those votes are guaranteed to relate to expected values of the latter, especially in developing regions. Thus, this critique joins my earlier argument in dismissing the title hypothesis as a universal law and roughly restricts its validity to industrialised states.

I conclude that predictions about the response of welfare state development to the income distribution and political participation levels, modelled by Meltzer and Richard, is not universally true nor universally false. Its accuracy is contingent on the level of development of the context to which it is applied. Alternatively, if the hypothesis, corrected for turnout, is intended to be evaluated across contexts as a sort of universal law, I argue that the semantics of the Meltzer-Richard model are critical - under its assumptions, can only go as far as to predict demand for redistribution and the attempt by politicians to implement policy in accordance with this demand. I maintain that, due to a lack of accounting for bureaucratic quality and public compliance as a function of governance in the Meltzer-Richard model, the prediction of the real level of redistribution generated is beyond its scope. I acknowledge that my critiques are in no way comprehensive, but simply exploit a single issue in the literature - that of sampling - of which there are surely many, even related to its validity in developed regions. The arguments I have developed urgently call for empirical testing as the econometric analysis of the causal relationship between turnout and redistribution outside of industrialised states is essential if we are to vividly understand the complex mechanisms at play in developing regions, which all too often go overlooked.

Reference List:

1. Bird, R.M., Martinez-Vazquez, J. and Torgler, B., 2008. Tax effort in developing countries and high income countries: The impact of corruption, voice and accountability. Economic analysis and policy, 38 (1), pp.55-71.
2. Borge, L.E. and Rattsø, J., 2004. Income distribution and tax structure: Empirical test of the Meltzer–Richard hypothesis. European Economic Review, 48(4), pp.805-826.
3. Chu, M.K.Y., Davoodi, M.H.R. and Gupta, M.S., 2000. Income distribution and tax and government social spending policies in developing countries (No. 0-62). International Monetary Fund.
4. De Tocqueville, A., 2003. Democracy in America (Vol. 10). Regnery Publishing.
5. Downs, A., 1957. An Economic Theory of Democracy, pp.599-608.
6. Fugazza, Marco, and Jean-François Jacques. "Labor market institutions, taxation and the underground economy." Journal of Public Economics 88, no. 1 (2004): 395-418.
7. Gough, I. and Wood, G., 2004. Insecurity and welfare regimes in Asia, Africa and Latin America: Social policy in development contexts. Cambridge University Press.
8. Hotelling, H., 1929. Stability in competition. The economic journal, 39(153), pp.41-57.
9. Husted, T.A. and Kenny, L.W., 1997. The Effect of the Expansion of the Voting Franchise on the Size of Government. Journal of Political Economy, 105(1), pp.54-82.
10. Inman, R.P., 1978. Testing political economy's 'as if' proposition: is the median income voter really decisive?. Public Choice, 33(4), pp.45-65.
11. Kaufmann, D., 2003. Rethinking governance: empirical lessons challenge orthodoxy. The World Bank.
12. Larcinese, V., 2007. Voting over redistribution and the size of the welfare state: the role of turnout. Political Studies, 55(3), pp.568-585.
13. Lijphart, A., 1997. Unequal participation: Democracy's unresolved dilemma presidential address, American Political Science Association, 1996. American

political science review, 91(1), pp.1-14.
14. Lindert, P.H., 1996. What limits social spending?. Explorations in Economic History, 33(1), pp.1-34.
15. Meltzer, A.H. and Richard, S.F., 1981. A rational theory of the size of government. Journal of political Economy, 89(5), pp.914-927.
16. Murrell, P., 1985. The size of public employment: an empirical study. Journal of Comparative Economics, 9 (4), pp.424-437.
17. Niskanen, W.A., 1971. Bureaucracy and representative government. Transaction Publishers.
18. Peltzman, S., 1980. The growth of government. The Journal of Law and Economics, 23(2), pp.209-287.
19. Richardson, G., 2008. The relationship between culture and tax evasion across countries: Additional evidence and extensions. Journal of International Accounting, Auditing and Taxation, 17(2), pp.67-78
20. Roberts, K.W., 1977. Voting over income tax schedules. Journal of public Economics, 8(3), pp.329-340.
21. Romer, T., 1975. Individual welfare, majority voting, and the properties of a linear income tax. Journal of Public Economics, 4(2), pp.163-185.
22. Schneider, F. and Enste, D.H., 2002. The Shadow Economy: Theoretical Approaches, Empirical Studies, and Policy Implications. Cambridge University Press.
23. Segura-Ubiergo, A., 2007. The political economy of the welfare state in Latin America: globalization, democracy, and development. Cambridge University Press.
24. Varian, H.R., 2014. Intermediate Microeconomics: A Modern Approach: Ninth International Student Edition. WW Norton & Company.