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As far as midterms go, turns out it is not ‘the economy, stupid’, after all

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The US election results were clear evidence that for midterm American polls, Bill Clinton’s mantra is wrong. It’s not “the economy, stupid” that determines outcomes. Polling prior to the vote showed 65pc of Americans rated the economy “good” or “excellent” – the most optimistic since 2001. Yet Tuesday’s polls showed a large swing in the popular vote to the opposition Democrats, and that party regaining control of the House of Representatives.

Midterm elections are always tough for parties with incumbent presidents. These results were by no means a disaster for Republicans – a wipeout, or the so-called “blue wave” Democrats hoped for. The Grand Old Party (GOP) strengthened its grip on the Senate although it ceded its majority in the House. But given the excellent economic backdrop, this was surely a missed opportunity for sustained control of both houses. That they neither managed nor expected it shows how the president’s behaviour, and huge national divisions on healthcare, immigration and much else, makes it difficult for the party of Trump to build out from its base.

However much those who detest Trump’s tweeting, public pronouncements and explicit embrace of nationalism would wish otherwise, the American economy has performed extraordinarily well under his tenure. In the last six quarters of president Obama’s presidency, annualised growth averaged just 1.5pc. It has been 2.8pc in the Trump era. Real GDP growth for 2018 is now forecast to come in at above 3pc; a large increase on the pre-election forecast of 1.8pc from congressional bodies, and a world away from the raft of warnings that a Trump victory could trigger a recession. Whether one attributes this pick-up to Republican policies or not, the party in power could not have asked for more favourable conditions.

And business clearly felt a Republican presidential victory a factor. Sentiment inflected on Trump’s election. The proportion of businesses surveyed by the National Federation of Independent Businesses who say now is a good time to expand shot up and now stands at 33pc, against just the 11pc seen in late 2016. Small business optimism hit record highs, while consumer confidence peaked earlier this year at its highest level since 2004. No wonder now-former Republican House majority leader Paul Ryan implored the president to campaign harder on the booming economy, and less on culture war issues and illegal immigration.

Politically, of course, Democrats sought to diminish Trump’s economic record by crediting positive trends to the legacy of president Obama, before swiftly changing the subject. They

pointed out that while there have been just over 4m new jobs created under Trump's presidency, 4.5m were created in the equivalent 22 month period at the end of Obama's tenure.

But this compares apples with oranges. One would expect job growth to slow as the economy got closer to full employment. In fact, it is remarkable how robustly the labour market has performed. A year ago, economists still worried about Americans having permanently given up looking for work. Now the employment rate for 25 to 54-year-olds is higher than before the recession. Unemployment has fallen from 4.8pc to 3.7pc, with workless rates for women, African-Americans and Latinos all now at multi-decade lows. Even real wage growth has picked up somewhat in recent months.

Clearly, it would be a mistake to assume all these economic trends are within the gift of the president or Congress. But the large tax rate cuts the president and Republicans championed, coupled with a very significant slowdown in new regulatory activity, would be expected to enhance growth prospects, at least temporarily. The narrative that the GOP had taken active steps to increase prosperity should have been handy in an election year.

Yet there was little evidence that the economy was the central factor in these results. Yes, the seats up for grabs favoured Democrats in the House (and Republicans in the Senate). But results and polling suggest that non-economic issues – healthcare and immigration in particular, but also the fallout from the recent bitter dispute of the Supreme Court Justice Brett Kavanaugh – were all important factors in voters' thinking. Perhaps unsurprisingly then, this became more of a "base" election. That appears to be what Trump wanted, and probably helped shore up the Senate. The Democrats obliged too by focusing on wedge issues where voters in urban areas in particular fundamentally object to Trump's politics.

Losing the House though, and having divided government from here on, will likely paralyse a major economic policy agenda. Further tax cuts, and much-needed reform of the US's runaway old-age entitlement programmes, are now firmly off the agenda. But one area to watch is infrastructure spending. The president promised a "massive" spending package in his election campaign. Here his instincts are probably much closer to House Democrats than representatives in his own party. The former are chomping at the bit for major federal investment.

Unless an unforeseen economic recession occurs, the next two years will likely follow this election in being dominated by non-economic issues.

Of course, the Republicans would likely have fared far worse in bad economic conditions. But strong growth midway through a presidential term perhaps gave some voters the luxury of considering these other issues, where the Republicans and Trump are less trusted or liked. Whichever line of reasoning one prefers, it is clear the GOP underperformed relative to the economy.

US politics seems to be rapidly polarising towards a pro-Trump and anti-Trump camp, and the president pushed for these votes to be a referendum on him. This led to surprising strength in some rural regions. But it was also accompanied with the loss of a house despite an amazing economic backdrop. Yes, it could have been far worse for the GOP. But in time they will surely rue this missed chance to consolidate.

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