Economics and How Obama Could Have Lost the 2016 Election Too

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Abstract

During the 2016 U.S. election, many voters from democratic ('blue wall') states, which have voted consistently in the past elections for the democrats, suddenly moved back into the Republican fold. During this election, the primary economic issue was supposed to be NAFTA, both Bernie Sanders and Donald Trump claimed it has been responsible for U.S. manufacturing job losses. So, what is the effect of trade on personal income and in particular manufacturing income and employment? Still, manufacturing losses are unlikely to explain democratic losses in rural areas, such as Wisconsin, where farm voters switched parties. What is the relationship between farm income and election result? Finally, are farmers Republican, Democrat or Independent? Or just pragmatic?

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Introduction

Two things were noticeable in the 2016 U.S. election. A few days before the election, against the consensus polls favoring Clinton, one forecaster who has predicted correctly election results many times was doubling down on his forecast in favor of Trump. The first lesson one learns in business forecasting is you are remembered for going 'big' against consensus and quickly forgotten if you are wrong. Still, did he use data that we were unaware of? During the election night, several 'blue' states, including Wisconsin, were overwhelmingly voting for Trump. Sufficient to say, there is going to be a lot of explaining and blame to share for the Hillary Clinton loss. But the reality is most of the democrats, with maybe the exception of Bernie Sanders, forgot that elections are generally decided by economics, best represented by Bill Clinton's famous catch phrase, 'it's the economy, stupid!' Given a 50+% approval rate and the ability to run a third time, could Obama (or Bill Clinton) himself have lost the election this year? And, was Donald Trump just lucky?

Apparently, the main economics issue in 2016 election was the North American Free Trade Agreement (NAFTA), did President Clinton make one of the biggest blunders in his administration when he signed the NAFTA? Did it exacerbate the manufacturing jobs loss? Why was NAFTA discussion so important now? What really happened during the Obama Administration?

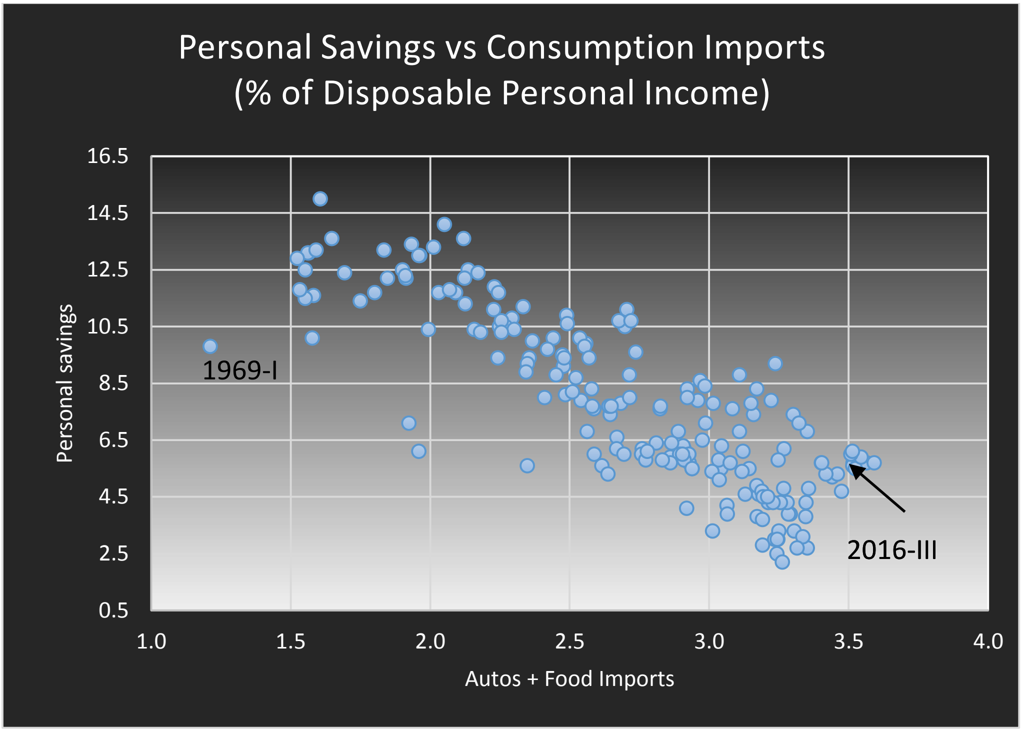
The idea that trade opens more markets to U.S. exports has been exposed due to the fact its trade partners have often neither the purchase power (China, Indonesia, Vietnam, India) nor a sizable consumer market (Germany, France, Korea, Japan, Singapore and Taiwan) to absorb American exports. In contrast, the U.S. has both purchase power and a large customer base for imports so it has run a large trade deficit with its trading partners for decades. This year, Trump has hammered with great effect the closing of small car plants by Ford in the U.S. and moving them to Mexico. Note that Clinton's counter argument that Trump was importing goods from Asia as well was no effective defense of NAFTA and Chinese imports. Also, Chinese steel and aluminum dumping became hot topic during the election. And to add insult to injury Obama proposed the Trans Pacific Partnership (TPP) agreement during an election year. Never mind the strategic reasons for the TPP. Clinton (and the democrats) flip-flop on TPP was fully exploited by both

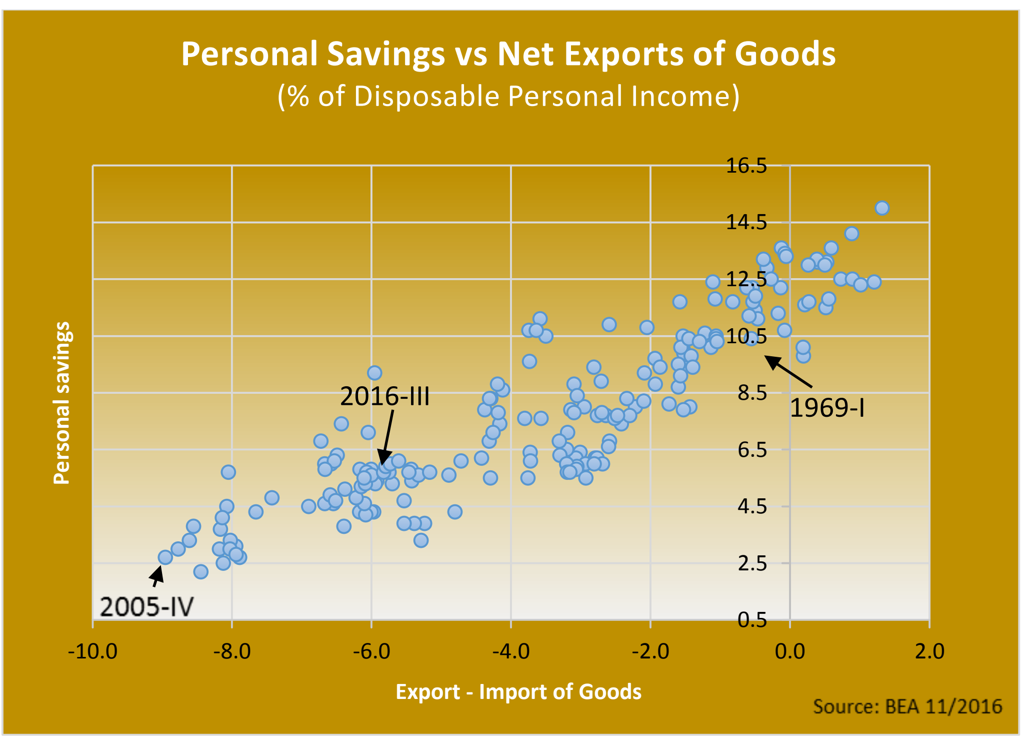
Bernie Sanders and Trump. Let's first examine the effect of trade on savings, on manufacturing income and jobs, and then to farm income.

Hall-Flavin's Consumption vs. Labor Income Growth and the Trade Evidence

For almost four decades, Hall (1978)-Flavin (1981) conclusion that expected consumption in t for period t+1 was equal to consumption in t, largely shifted the focus of consumption research from labor income and its growth to "deviations" to consumption martingale. When Obama's fiscal stimulus rescued the country from the 'great' recession, it was shown that Keynes' fiscal stimulus still hold its place in economics. Wu (2016) has questioned a critical assumption in Flavin's approach and has proved that change in savings is indeed a function of income growth. As a result, any factor affecting growth of income, e.g., fiscal stimulus, currency, and other factors, may affect change in savings. To understand the effect of trade on U.S. personal saving rate for almost half century, quarterly data from Commerce Department – BEA was used to compare consumption (automobile and food) imports and net exports of goods against personal savings.

The top chart shows the effect of consumption import on personal saving rate. The more imports the less the saving rate. The reasoning is that imports impact negatively jobs and less jobs generate less wage income (and state/federal income), which leads to lower savings. The bottom chart shows that net exports can increase or lower savings. Unusual factors, such currency, can stimulate or affect growth of income thru exports and imports and therefore savings. Basically, it is the same saving and dissaving mechanism described by Keynes and Clower's Dual Decision Hypothesis and combined with Friedman's Permanent Income Hypothesis. In other words, saving and dissaving occur because expected and actual income are usually different and consumers are constantly reevaluating their optimal consumption.

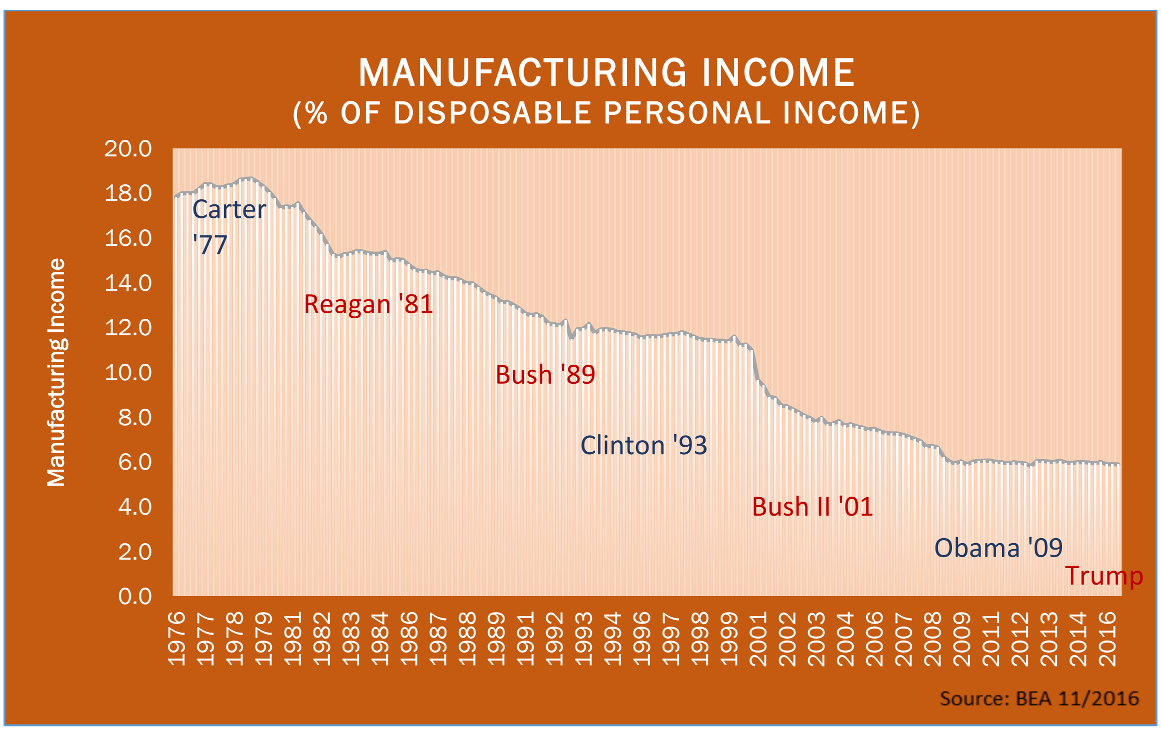

Personal Savings vs Consumption Imports
(% of Disposable Personal Income)
16.5
14.5
12.5
10.5
8.5
6.5
4.5
2.5
0.5
Personal savings
1969-I
2016-III
1.0
1.5
2.0
2.5
3.0
3.5
4.0
Autos + Food Imports

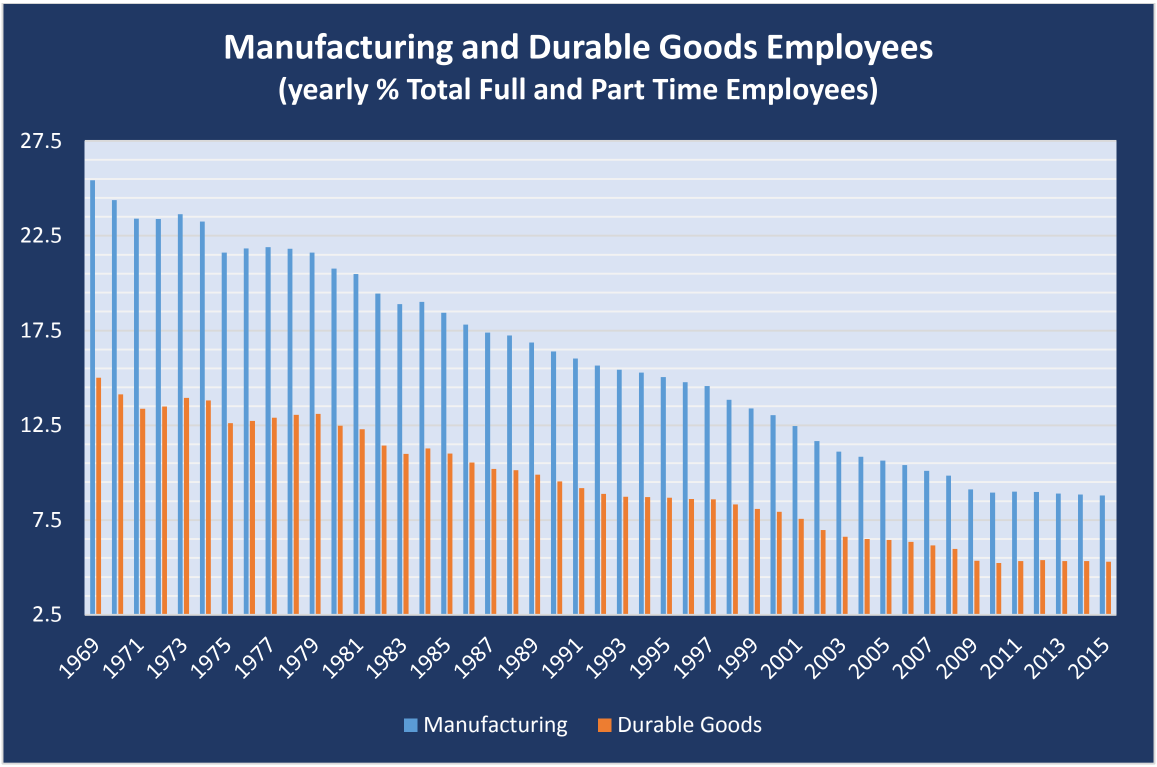

Personal Savings vs Net Exports of Goods
(% of Disposable Personal Income)
16.5
14.5
12.5
10.5
8.5
6.5
4.5
2.5
0.5
Personal savings
2016-III
1969-I
2005-IV
-10.0
-8.0
-6.0
-4.0
-2.0
0.0
2.0
Export - Import of Goods
Source: BEA 11/2016

Manufacturing and NAFTA

The yearly chart on manufacturing income shows a sharp drop at the end of Clinton II (2000) and the downward trend continued during GW Bush (2001- 2008), note the similar downward inclination from Reagan and GH Bush (1981-1992). Obama actually stabilized the downward trend of manufacturing income but it never went up in any significant way to offset earlier losses in employment from previous presidencies. It should be noted that some of the gains in Obama economy may be attributed to increased production and jobs in oil and gas extraction.

The yearly chart on manufacturing and Durable Goods employment shows that, from 1969 to 2015, employment has steadily fallen and has stabilized after 2009. It is not altogether clear that post-NAFTA industrial jobs lost during GW Bush (2001-2008) are trending worse than those under Reagan and GH Bush years (1981-1992). However, what is relevant to workers is that employment and income has been roughly one third of what it used to be in 1969 and has not recovered from historical lows. This may be the key to understand the resistance of manufacturing workers from throwing full support to the democrats in the 2016 elections.

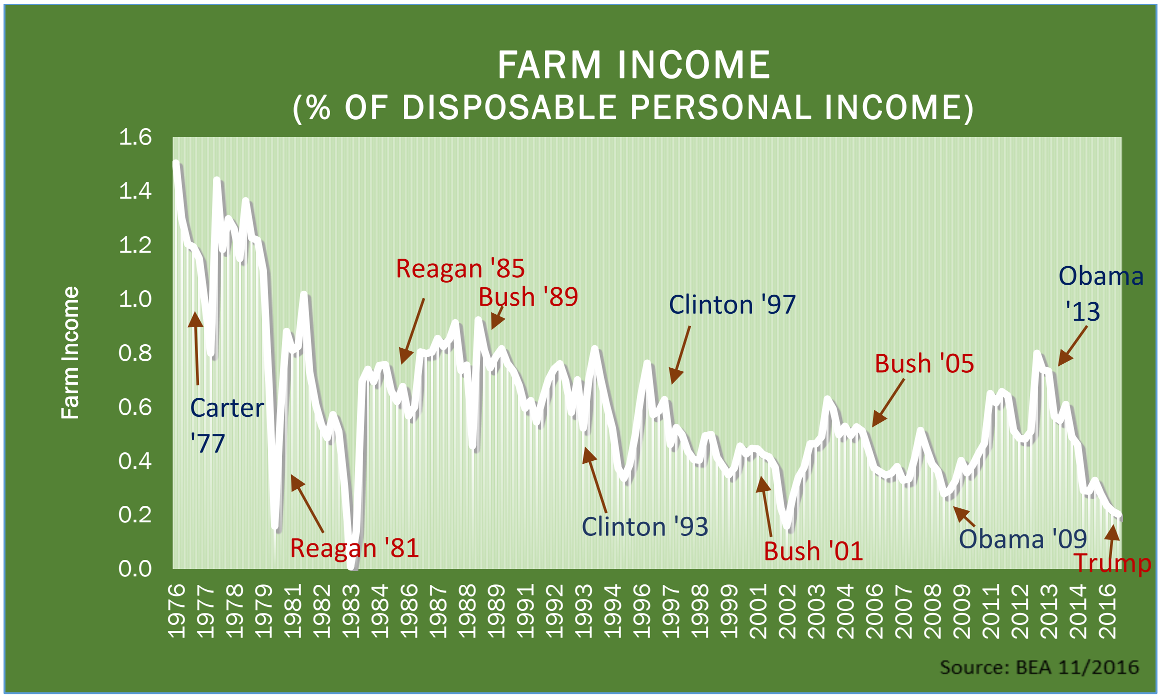




Rural Voters and Election Results

While, on the surface, the election was all about NAFTA, the greatest and often neglected issue during the past 40 years elections and during the 2016 election year has been the economics of the rural income. As post-election data shows, Wisconsin, Michigan, Iowa, Pennsylvania, Kansas and many other 'sun belt' states voted Republican. Should we be surprised most of rural areas voted for Trump and the Republicans?

Is it Obama's fault that oil and other commodity prices have collapsed and the Chinese economy has slowed down? For agriculture, there have been loss of subsidies and market share in key regions and countries, such as Europe, Russia and China, largely due to genetically modified organism or 'gmo,' and trade embargo/protectionism. Last few years, U.S. farm exports was also affected by a strong dollar. For instance, in the last couple of years, U.S. dollar has appreciated significantly against some of its main international competitors, including the Brazilian Real, appreciating from Real 1.8 per dollar to Real 3.8 per dollar. Thus, to what extent farmer anger has affected the outcome of the elections?



To show the effect of farmers in the elections, the quarterly chart of proprietor's farm income (as percentage of disposable personal income) shows their relative income from Carter election in 1976 to Trump in 2016. This chart shows that every time farm income drops sharply there is a high probability for reversal in presidential election, whether the candidate is republican or democrat. Carter in 1977 was the beneficiary of this drop. Reagan too in 1981 with help of Carter's Iran Hostage fiasco. But in the midterm election of 1982, Republican lost 27 seats in the House of Representatives. Farm business and first Bush did well in 1989. Clinton in 1993 was also aided partially because of his unique economic pitch and from coming from Arkansas. Note that Democrats suffered heavy losses in the 1994 midterm elections (Republicans gained 54 seats in the House and 8 in the Senate) when farm income was sharply down. Much of the effect of the extreme currency devaluation policy of Treasury Secretary Lloyd Bentsen in Clinton I was lost in Clinton II, after Robert Rubin and Larry Summers took over. The downward trend in farm income sealed Al Gore's fate in 2001, not surprisingly, losing even in his own home state of Tennessee. GW Bush was reelected after years of commodity inflation. Obama won handily in 2009 by a combination of factors, talk of reviewing the Canadian trade and a significant drop in farm income. Obama II had strong rural support in the reelection, partially due to rescuing the country from the recession and high farm income, largely from high commodity prices. In the elections of 2016, Trump exploited NAFTA and benefitted when farm income fell from 0.8% to less than 0.2% in the last four years.

Comments

What are some of the lessons from this election? a) the above farm chart helps explain how 'blue wall' states may collapse whenever farmer income is down; after all, some blue states have plenty of small farmers; b) a strong 'change' catch phrase, such as 'let's make America great again' or 'yes we can,' works best when farming income is declining. Farmers are unlikely to vote on an incumbent party when the rest of nation is doing well and they are not; c) NAFTA and farming are issues that political parties will use to control both houses and the presidency, of course; as the republicans have done for decades, democrats must woo 'sun belt' voters and convert them into blue states. After all, small states have the same number of senators as the big ones; d) are farmers democrat, republican or independent? The farm income chart suggests rural voters can be reasoned and persuaded by pragmatic policies favoring their income, which in a way has been obvious for all but the democrats; e) curiously, why did Trump call DC swamp so close to the elections? In the midst of all the insults, few probably paid attention to its meaning. Was it a subconscious rally call for farmers or a winner's lucky shot?

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