

Qvortrup, Matt

Article

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Intereconomics

Suggested Citation: Qvortrup, Matt (2016) : Brexit as an Inelastic Good: A Microeconomic Theory of Direct Democracy, Intereconomics, ISSN 1613-964X, Springer, Heidelberg, Vol. 51, Iss. 5, pp. 260-264,
<https://doi.org/10.1007/s10272-016-0615-x>

This Version is available at:

<https://hdl.handle.net/10419/191171>

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Matt Qvortrup*

Brexit as an Inelastic Good: A Microeconomic Theory of Direct Democracy

On 23 June 2016 a slight majority of 52% of UK voters opted to leave the European Union after 44 years of membership. Many were surprised by the result. Why did a majority vote Leave? Why were the majority of the voters not susceptible to the economic arguments advanced by major economic institutions such as the Bank of England, OECD, IMF, HM Treasury and virtually all major investment banks? Why did (now former) Prime Minister David Cameron, who campaigned for Remain, lose the vote only a year after his party had won a surprise victory in the 2015 general election?

This article advances the hypothesis that economic theory contributes to an understanding of the outcome. Ana-

lysed through the prism of microeconomics, in particular the well-known concept of elastic and inelastic demand curves, it is suggested that “Brexit” was an inelastic political good, and that a change in the price did not affect the desire to “purchase” this good.

Using economics to understand political phenomena

While political science has made advances in understanding voting intentions and rational choices in referendums,¹ most of the models have been based on either statistical models identifying common denominators for voting

Matt Qvortrup, Coventry University, UK.

* The author is grateful for comments from Erik Qvirin Hansen, Brendan O’Leary, Ece Atikcan, and to Lord Andrew Cooper and Gerry Gunster for taking time to talk about the referendum. The usual caveat applies.

¹ For an overview see M. Qvortrup (ed.): *Referendums around the World: The continued growth of direct democracy*, Basingstoke 2013, Palgrave.

decisions or on description-heavy,² empirical analysis of individual referendums.³ While some scholars have attempted to use formal modelling,⁴ the majority of studies have been case-specific and have not been based on economic models.

Could public choice theory and microeconomics provide insights into why voters voted the way they did? There is a large body of research that answers this in the affirmative. Mueller defines public choice as “the economic study of nonmarket decision making, or simply the application of economics to political science”.⁵ This article is an attempt to do exactly this; to analyse the nonmarket referendum through the prism of economics and economic theory, and the first steps are made towards establishing a microeconomic theory of referendum choice. In this article, qualitative evidence (such as reports from the campaign and interviews with leading representatives from each of the two sides) will be used to support the hypothesis. Thus, the study seeks to render plausible the hypothesis that microeconomic theory – especially the concepts of elastic and inelastic goods – can be used to illustrate voting behaviour in referendums. Once this theory has been corroborated, it can then serve as the basis of a more quantitative study analysing referendums more generally using economic modelling. For the present purposes, this article provides a first attempt at developing a scientific research programme within which future referendums can be analysed.

Referendums as goods

Economists since the 1950s have sought to use the basic logic and the basic concepts of economics to analyse such political phenomena as majority voting and party strategies in two-party and multiparty systems.⁶ As this pioneering research shows, situations when voters, parties and other political agents are dealing with decisions and trade-offs between two or more competing products are particularly suited for economic analysis, i.e. for applying economic reasoning to non-economic choices.

Fundamentally, the Brexit referendum could be seen as a choice between economic stability and political sovereignty. Each of these two options had – as in economic theory – different demand curves. The price of each had implications for the voter’s decision.

Elasticity and inelasticity in economic theory

So what do we mean by elastic and inelastic demand? Marshall’s classic definition of elasticity states that

the elasticity (or responsiveness) of demand in a market is great or small according as the amount demanded increases much or little for a given fall in price, and diminishes much or little for a given rise in price....⁷

Or, in the words of a contemporary textbook in economics:

The price elasticity of demand measures how much the quantity demanded responds to a change in price. Demand for a good is said to be elastic if the quantity demanded responds substantially to changes in price. Demand is said to be inelastic if the quantity demanded responds only slightly to changes in price.⁸

The contention (or hypothesis) here, then, is that the two options, Leave and Remain, were, respectively, inelastic and elastic goods. Leave, popularised as Brexit, with the rallying cry of “taking back control”, was a political good that many voters were willing to purchase even if the price for this was high – hence it was an inelastic good. Conversely, the demand for Remain dropped as the price for this was seen to increase. As Figure 1 shows, a change in the price for Brexit only marginally changed the demand – hence the steepness of the curve. Conversely, the demand curve for Remain is less steep, as a change in price *ex hypothesi* will lead to a fall in demand.

In the following, we will test this hypothesis using qualitative evidence from the campaign, including interview data.

The political economy of Brexit: demand for an inelastic good?

The main argument proposed by those who wanted to leave the EU was that a vote for Brexit was a vote for sovereignty. To support the hypothesis that Brexit was an in-

2 M. Qvortrup: Referendums on Membership and European Integration 1972-2015, in: The Political Quarterly, Vol. 87, No. 1, 2016, pp. 61-69.

3 M. Mendelsohn, F. Cutler: The effect of referendums on democratic citizens: Information, politicization, efficacy and tolerance, in: British Journal of Political Science, Vol. 30, No. 4, 2000, pp. 669-698.

4 S. Hug: Voices of Europe: citizens, referendums, and European integration, New York 2003, Rowman & Littlefield.

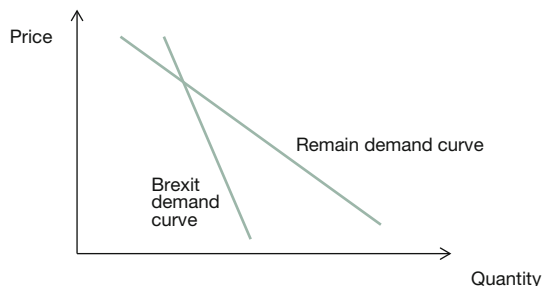
5 D.C. Mueller: Public Choice III, Cambridge 2003, Cambridge University Press, p. 1.

6 G. Tullock: Problems of majority voting, in: The Journal of Political Economy, Vol. 67, No. 6, 1959, pp. 571-579; A. Downs: An Economic Theory of Democracy, New York 1957, Harper and Row.

7 A. Marshall: Principles of Economics, Vol. 1, London 1890, Macmillan, p. 166.

8 N.G. Mankiw, M.P. Taylor: Economics, London 2011, South-Western, p. 95.

Figure 1
The elasticity of Brexit and Remain



Source: Author's illustration.

elastic good, we need to provide evidence that voters did not respond to price changes. In other words, it must be shown that voters' demands for Brexit remained relatively unchanged as the price of Brexit increased.

This contention can be corroborated in qualitative evidence, such as interviews. According to Gerry Gunster, an American political consultant who ran the campaign for the organisation Leave.eu:

It was clear from the start that we wanted a people's campaign. We wanted to focus on sovereignty. "Take back control", "I want my country back", that [*sic*] sort of slogans. They are priceless. Who does not want to get his [or her] country back?⁹

His argument – though, naturally he did not put it in the jargon of economic theory – was that some voters are willing to accept virtually any increased cost as long as they can "take back control". In his own words, sovereignty is "priceless". In economic terms, sovereignty can thus be seen as an inelastic good.

This puts the campaign into perspective and perhaps explains why those political "consumers" who were inclined to vote for Brexit did not heed some of the warnings by economic experts, financial institutions and the government. For these voters, even an increase in the price – as predicted by countless reports by the IMF, HM Treasury (the British Ministry of Finance) and others – would only lead to a negligible change in the demand for "taking back control". Related to this was the fact that sovereignty is a political product for which it is difficult to name a substitution good.

Of course, we cannot prove this in the strictest sense of the word. But the logic was certainly not lost on Nigel Farage. The stockbroker-turned-politician told the Eurosceptic Daily Express, "The wellbeing of those living

and working in our country matters to me more than GDP figures."¹⁰ Again, Mr Farage may not have considered his predictions in the jargon of economic theory, but the logic once again is clear; an increase in the cost of living – or, as voters saw it, a change in abstract macroeconomic figures – would be a small price to pay for "freedom" (Farage's term for leaving the EU).

That the voters were willing to pay almost any price for Brexit – that this political good followed an inelastic demand curve – is also evident from the qualitative evidence from one of the leading Remain campaigners, Lord Andrew Cooper, the Prime Minister's pollster:

We considered what we could do, if we could somehow come up with a pledge but we knew that it was pointless; there was nothing we could do that could even remotely satisfy the voters' views [regarding immigration and sovereignty].¹¹

Thus, it was all but impossible to lower the cost of Remain to a point where it was acceptable to those who wanted to vote for Brexit. Conversely, it was impossible for the Remain campaign to portray the price of Brexit as being so high that swing voters were willing to vote Remain.

The political economy of Remain

Yet, to render plausible the hypothesis that the Brexit referendum – and perhaps all referendums – can be analysed using microeconomics, we also need to consider the demand curve for Remain. The contention in this article is that Remain was an elastic good, and as such a small change in price led to a drastic change in demand. Can this hypothesis be corroborated by the empirical evidence?

It was clear that the campaign to stay in the EU wanted to push the economic argument. They had good reasons for doing so, as opinion polls suggested that many voters – indeed, a majority – believed that Britain would benefit economically from remaining a member of the European Union.¹²

The problem for the Remain side was, economically speaking, that their welfare argument was a classic example of an elastic good. A small change in the price of Remain would cause the demand for staying in Europe to drop.

9 G. Gunster, interview with the author, 6 July 2016.

10 N. Farage: Why we must vote LEAVE in the EU referendum, Express, 21 June 2016.

11 A. Cooper, interview with the author, 8 July 2016.

12 See survey in Financial Times, 3 May 2016, p. A3.

The government published a document in which it was claimed that each voter – according to econometric estimates – would be £4,000 pounds worse off in 2030 if Britain voted to leave the EU.¹³ Furthermore, it asserted that a “vote to leave would cause a profound economic shock creating instability and uncertainty, which would be compounded by the complex and interdependent negotiations that would follow”.¹⁴ To a degree, this argument had some impact.

As Figure 2 shows, there was a slight boost to the Remain side when the document was published at the beginning of May, and at this point “demand” for Remain – using referendum poll data as a proxy – reached a high of 55%. However, this demand soon evaporated and was neutralised by the counter-claim that EU membership was costly to the UK taxpayer.

One figure in particular was much discussed during the campaign, namely the contention that the UK paid £350 million every week to the EU. Those wanting to leave the EU had been behind until the beginning of May, but they began to close the gap in April when the “£350 million a week” soundbyte first surfaced. To be sure, the assertion was dismissed by the UK Statistics Authority, whose chair, Sir Andrew Dilnot, said, “UK Statistics Authority is disappointed to note that there continues to be suggestions that the UK contributes £350 million to the EU each week, and that this full amount could be spent elsewhere.”¹⁵

But this clarification did not convince voters and seems to have been largely ignored. The problem for the Remain side was that many voters accepted the £350 million a week figure or at least the gist of the argument. According to Cooper, “Voters totally internalised the argument when we used it in focus groups. When they were told that the figure was inaccurate, they would say, ‘Yes, but it is still a substantial amount’, and we would get nowhere.”¹⁶

The Remain campaign had done rather well in late February after David Cameron announced that the referendum would be held 23 June (see Figure 2). At this stage, the Remain side was still able to control the agenda and had argued that the price of leaving the EU was high. However, once the Treasury’s claim had been disputed by Leave campaigners such as Boris Johnson, Michael Gove and Nigel Farage, support for Leave increased, and demand for continued membership dropped significantly.

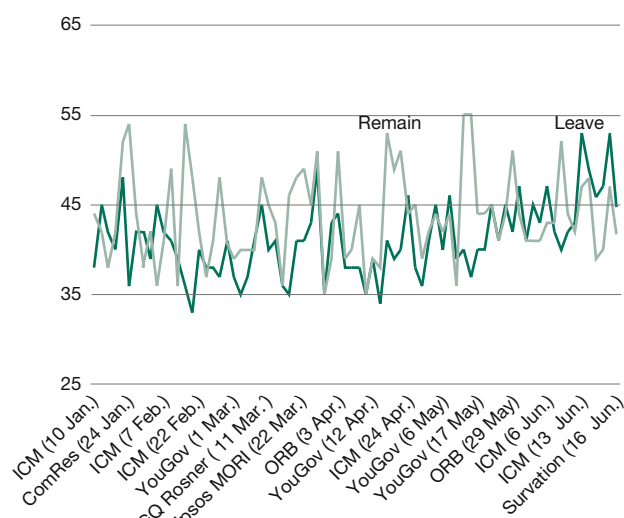
13 G. Osborne: HM Treasury analysis: The immediate economic impact of leaving the EU, London 2016.

14 Ibid., p. 5.

15 A. Dilnot: UK Statistics Authority statement on the use of official statistics on contributions to the European Union, 27 May 2016, available at <https://www.statisticsauthority.gov.uk>.

16 A. Cooper, op. cit.

Figure 2
Opinion polls during the Brexit referendum campaign
in %



Source: Business Insider 2016.

To come back to the microeconomic argument, the circumstantial evidence suggests that Remain was an elastic good. To wit, the perceived change in price had an immediate impact on the demand. When the price of EU membership was claimed to be £350 million a week, demand for EU membership responded substantially to the changes in the perceived price. This was evident in the last week of May, when the Brexit side again repeated the £350 million a week claim, and support for Remain subsequently dropped substantially (see Figure 2).

All this brings us to another aspect of the campaign – communication. The competing claims regarding Leave or Remain were not taking place in a vacuum. As in financial markets, the marketplace of politics is driven as much by perceptions as it is by quantity and price.

The key to a successful referendum campaign is in framing the debate. Commercials and advertising may not be able to tell people what to think, but at the same time they are tools that can influence which aspects of the debate people concentrate on. It is well-known from economic and business research that advertising is effective in “tip-[ping] the balance when alternative brands are otherwise equal”.¹⁷ Similar research has been carried out in political science. According to this research, an effective campaign can be successful in telling people what to focus on.

17 M. Sutherland, A.K. Sylvester: Advertising and the Mind of the Consumer, quoted in: N.G. Mankiw, M.P. Taylor, op. cit., p. 346.

Politicians attempt to mobilize voters behind their policies by encouraging them to think along particular lines, emphasizing certain features of these policies. These frames organize everyday reality by providing meaning to events and [by] promoting particular definitions and interpretations of political issues. The influences these frames have on the voter is the framing effect.¹⁸

The Leave campaign was a textbook example of this. According to Gunster, the framing of the debate effectively won the campaign. Unlike the Remain campaign, both the official and the unofficial Leave campaigns had a simple message. “We can’t remember the slogan for Remain. That says it all. But months after this campaign people will remember ‘I want my country back’.”¹⁹

This leads us back to the microeconomic argument. In terms of choice and economic theory, the utility of having control over one’s life is almost unbeatable, or indeed, “priceless”, to use Gunster’s word.

Once again, the Brexit argument followed an inelastic demand curve; even the barrage of statistics from HM Treasury and other institutions showing the rising cost of leaving the EU did not persuade voters. “Taking back control” was a prize that made tolerable a rise in the cost of living, not least since many voters, perhaps a majority, believed in the £350 million a week claim.

Despite the increased Brexit price, the voters (or at least the 52% who opted for Leave) were not convinced; if an inelastic good is one for which the demanded quantity is negligibly affected by changes in price, then the Brexit option – “to take back control” – certainly qualifies as such.

Needless to say, this economic theory of the referendum does not explain everything. While many voters were convinced by the £350 million a week argument, there were also other explanations. Demographic factors played a key role in the referendum.

What is interesting is that all the demographic groups that opted for Leave are also likely to be the ones who would be hit by the predicted economic malaise in the wake of a Brexit. That these groups were willing to pay the price of the impending doom foretold by Chancellor of the Exchequer George Osborne in return for “taking back con-

trol” shows the degree to which the perceived independence from the EU was an inelastic good.

By the end of May, immigration and sovereignty had emerged as the big issues in the campaign. Many of the “elites” believed this would hurt the Leave campaign. It did not; a majority of the voters were unconvinced by the economic warnings and were willing to pay a high price for “freedom” if necessary. The focus on immigration reinforced the perception that Brexit was a virtually priceless commodity for which there was no credible substitution good.

Conclusion

Based on qualitative evidence and interviews with leading representatives from the Leave and Remain campaigns, this article argues that economic theory provides a framework for analysing the 2016 Brexit referendum. According to the well-known model of price elasticity, the demand for an elastic good falls rapidly if the price increases. Conversely, the demand for inelastic goods does not change significantly as a result of price changes. According to the qualitative evidence presented in this article, it is possible to interpret leaving the EU as an inelastic good. Although the price for this option was predicted to be high, demand for Brexit remained relatively strong. Indeed, once it was believed that the cost of leaving the EU was negligible (due to the much debated £350 million a week claim), demand for Leave even increased.

Similarly, the political good of “Remain” can be seen as an elastic good. Until other factors came into play – such as the £350 million a week claim – a majority of voters were willing to vote for Remain, but once the perceived cost of membership went up, the demand for this political commodity went down.

Needless to say, there were other factors, such as the framing of the debate and demographic factors like voters’ class and income. Yet, this does not alter the conclusion that demand elasticity and demand inelasticity were factors that were overlooked when the Leave and Remain campaigns attempted to sell their goods. While empirical evidence is needed – in particular quantitative and statistical data – the qualitative evidence here corroborates the proposed hypothesis.

This is of interest to those who want to understand the determinants of referendum voting. But the conclusion is also of interest to those who are concerned with theoretical research, and it suggests that analysing non-market decisions using the tools of microeconomics is still a promising and fruitful endeavour 60 years after the path-breaking work by Downs and Tullock.

18 E.Ö. Atıkcı: Framing the European Union: The Power of Political Arguments in Shaping European Integration, Cambridge 2015, Cambridge University Press, p. 18.

19 G. Gunster, op. cit.