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## Political leaders' socioeconomic background and fiscal performance in Germany

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# **Political Leaders' Socioeconomic Background and Fiscal Performance in Germany\***

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# **Political Leaders' Socioeconomic Background and Fiscal Performance in Germany**

## **Abstract**

This paper investigates whether the socioeconomic status of the head of government helps explain fiscal performance. Applying sociological research that attributes differences in people's ways of thinking and acting to their relative standing within society, we test whether the social status of German prime ministers can help explain differences in fiscal performance among the German Laender. Our empirical findings show that the tenures of prime ministers from a poorer socioeconomic background are associated with higher levels of public spending and debt financing.

JEL: E61, E62, H11, H72

Keywords: Leadership, socioeconomic status, fiscal policy, public spending, public deficit.

## 1. Introduction

Explaining variations in government size and public debt accumulation is an important issue for political economists, and one in which the motives of relevant political actors are thought to play a decisive role. The literature typically assumes that political decision-making is driven by one of three motivations. First, politicians behave in a *purely opportunistic* manner. For instance, political budget cycle (PBC) theorists argue that public spending and debt financing are connected to the legislation cycle (e.g., Rogoff and Sibert, 1988; Alesina et al., 1992; Persson and Tabellini, 1997):<sup>1</sup> to enhance their re-election prospects, politicians are expected to raise the level of public expenditure and debt financing in pre-election and election years, while fiscal consolidation is expected to occur in the aftermath of an election.<sup>2</sup>

A second branch of the literature views politicians as *purely benevolent*. Political actors design fiscal policy to optimise some sort of social welfare function. A well-known example is Barro's (1979) tax-smoothing hypothesis, in which it is assumed that governments choose tax rates with the aim of minimising the excess burden of taxation. As a consequence, the accumulation of public debt is expected to be linked to the business cycle, since governments are assumed to incur deficits during recessions and surpluses during booms (Alesina and Perotti, 1994).

Finally, there are political economists who link political performance to *partisan ideology* (see, e.g., Hibbs, 1977; Buchanan and Wagner, 1977). A common assumption in this body of literature is that the tenures of left-wing governments are associated with higher levels of public spending and debt financing than are the tenures of right-wing governments (e.g., Blais et al., 1993; Cusack, 1997).

However, empirical analyses cast serious doubt on all three approaches, since findings from different studies are often contradictory and the explanatory power of the employed covariates is low. In the case of PBC theory, for example, Shi and Svensson (2006) find robust evidence for PBCs in fiscal deficits for developing countries, but not for developed countries. Brender and Drazen (2005) provide similar results based on a differentiation between new and established democracies: PBCs are found in the former only.

Results from the two other strands are, at best, mixed, too. With respect to the partisan hypothesis, there is some evidence from OECD countries that tenures of left-wing

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<sup>1</sup> Originally, the theory of political business cycles was formulated in a Phillips curve context. See Nordhaus (1975) and MacRae (1977).

<sup>2</sup> These implications depend on the assumption that voters are either myopic, i.e., they overestimate the benefit of current public spending and underestimate the costs of future taxes (Alesina and Perotti, 1994), or have imperfect information regarding the competence of the incumbent government and the costs of publicly provided goods (Rogoff and Sibert, 1988; Rogoff, 1990). See Alesina and Perotti (1994) and Eslava (2006) for a summary.

governments are indeed associated with a rise in public expenditures (e.g., de Haan and Sturm, 1994, 1997; Cusack, 1997), but the conclusion that leftist incumbents accumulate higher public debt is made less than solid by the experience of many Western European countries between 1960–1990.

Finally, the tax-smoothing approach is not in line with observations on the development of public budgets in many OECD countries during the 1970s and 1980s (Roubini and Sachs, 1989; Alesina and Perotti, 1994). In particular, the absence of fiscal adjustments in some OECD countries after the recession of 1973–1974 and differences in the accumulation of public debt in the following decades cannot be convincingly explained by a tax-smoothing motive.

So, what *is* driving the fiscal decisions of political actors? In this paper, we argue that a broader social science perspective may provide some important insights. Sociologists emphasise the strong connection between an individual’s socioeconomic background—especially factors that determine an individual’s relative position within a society, called *status*—and preferences, attitudes, and habits.<sup>3</sup> There is a considerable amount of political economics literature suggesting that factors related to individuals’ status—such as occupation, income, and education—help explain differences in policy preferences and decision behaviour, but typically these variables are employed in a more or less *ad hoc* fashion. To the best of our knowledge, there is no empirical work that links theoretical research on status to the fiscal behaviour of leaders. We fill this gap by investigating the impact that a political actor’s family status has on his or her fiscal preferences. To this end, we utilise observations on the leaders, the *prime ministers* (Ministerpräsidenten), of the fiscally partially autonomous states making up the Federal Republic of Germany, the *Laender* (Bundesländer). We concentrate on the social status of the German Laenders’ prime ministers and study its influence on the level of public expenditures as well as debt financing.

Choosing the German Laender as the object of analysis has two advantages: first, they are highly homogeneous regarding politics, culture, demography, and institutional as well as constitutional frameworks, which limits the number of control variables required and minimises potential biases due to endogeneity problems. Second, the Laender are constitutionally endowed with a high degree of fiscal authority regarding budgetary matters.

These advantages have made the German Laender a popular venue for research into the motivations of incumbent governments. However, neither the PBC theorem (Berger and Holler, 2007; Schneider, 2010), the tax-smoothing approach (Seitz, 2000), nor the partisan

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<sup>3</sup> In fact, this belief is the motivation of a huge body of sociological research analysing the social structure of society.

hypothesis (Seitz, 2000; Galli and Rossi, 2002; Jochimsen and Nuscheler, 2010; Schneider, 2010) are supported by empirical findings from this work. In contrast to these studies, we find robust empirical support for our social-science-based approach to explaining political decision making.

In the next section of this paper, we discuss related literature. In Section 3, we take a brief look at the German system of fiscal federalism and its political landscape. Then, in Section 4, we introduce the concept of status, provide empirical measures for it, and identify transmission channels that link a person's status to his or her preferences public expenditure and debt financing. In Section 5, we conduct some preliminary analyses proving the accuracy of our conclusions drawn in Section 4. Section 6 presents the results of our main analysis, in which we investigate the influence of German prime ministers' socioeconomic backgrounds on the fiscal performances of the German Laender. Section 7 concludes.

## **2. Related Literature**

By focussing on how the head of government influences economic outcomes, this paper contributes to an expanding branch of the literature. Starting with the work of Jones and Olken (2005), researchers have become increasingly concerned with the question of whether political leaders exert an impact on economic performance. Jones and Olken (2005) provide evidence that leaders do influence the rate of economic growth in their country. They compare GDP growth rates before and after exogenous leader changes (i.e., leader transitions caused by natural death of the incumbent) and find significant differences. Brender and Drazen (2009) use the same approach to test whether political leaders affect the composition of government expenditures, finding significant effects in the long run. A major drawback of both studies is that they assume the relevant competences to be randomly distributed across political leaders and it is thus unclear in what specific characteristics leaders differ.

Other researchers attempt to overcome this shortcoming by focussing on the sociodemographics of leaders, e.g., age, tenure, education, and professional background, but with limited success.<sup>4</sup> For instance, Hayo and Voigt (2011) study determinants of constitutional change, particularly movements from the status quo toward more parliamentarism or presidentialism, in a large sample of countries. They find that these changes are influenced by specific characteristics of political leaders.

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<sup>4</sup> Individual characteristics are also used as explanatory variables for committee decisions. For instance, focussing on members of monetary policy committees rather than heads of government, Göhlmann and Vaubel (2007) investigate the impact of education and occupation histories of 391 central bankers from 10 European countries on inflation outcomes.

Besley et al. (2009) identify leaders' educational attainment and experience as relevant to differences in GDP growth. More precisely, they find that the more educated the leader (differentiating between non-graduate education, graduate education, and college education) and the longer the stay in office, the higher the country's economic growth.

Dreher et al. (2009) focus on the effect of different *fields* of education and occupation on economic reforms, measured as changes in the Economic Freedom Index. They are primarily interested in the effect of leaders' economic and entrepreneurial backgrounds and expect that economists, as well as entrepreneurs, should be more likely to liberalise the economy. The authors account for different educational and occupational backgrounds by including dummy variables and find evidence that supports their hypothesis. However, among the occupation dummies, there are three additional effects (for scientists other than economists, military personnel, and life-long politicians) that have a positive sign, but the authors conduct no further tests to compare these groups. Moreover, Dreher et al.'s (2009) findings are not robust to varying specifications, especially to the inclusion of a lagged dependent variable and additional controls.

Mikosch (2009) employs the same dataset in an attempt to explain differences in public deficits. According to his results, tenures of former economists, white-collar workers, and blue-collar workers are associated with significantly higher deficits than tenures of leaders who have been politicians most of their working life. However, this finding is counterintuitive and actually contradicts the author's hypothesis that economists should reduce public debts.

A problem with these studies is that the theoretical link between, say, certain educational and occupational backgrounds and economic performance remains vague. The authors refer to some sort of socialisation or, rather, 'professional indoctrination', which economists in particular are presumed to experience. However, experimental studies show that the differences between economists and other people with respect to ways of thinking and acting can at least partially be ascribed to a selection effect (for a recent summary on experimental findings, see Goossens and Méon, 2010). Moreover, sociological research reveals that educational and occupational choices themselves depend on the social environment, in particular family status (e.g., Bourdieu, 1984). Hence, instead of focussing on specific fields of education and work, we look at leaders' family status, i.e., parental status and the status of positions prime ministers held before entering office. Our novel approach to the analysis of leaders' influence is motivated by manifold empirical findings linking individual status to motives and patterns of behaviour. Thus, our measures of status are those frequently employed in the social sciences. In our empirical analysis, we find strong evidence that a

prime minister's socioeconomic background matters in terms of the incumbent government's fiscal performance: the higher a prime minister's status, the lower the public expenditures and debt financing.

### 3. Fiscal Federalism and Political Landscape in Germany

The German federal system consists of three parliamentary governmental levels, each with its own fiscal competences and responsibilities as specified by the German Constitution, the Grundgesetz: federal level, state level, and local level.<sup>5</sup> At the state level, there were 11 Laender before German Unification in 1990; 16 afterward.<sup>6</sup> Three out of the 16 are so-called city-states (Berlin, Bremen, and Hamburg), which combine competences assigned to the state and the local level.

The competences assigned to the German Laender are extensive and mainly defined in Articles 71–74 of the Grundgesetz. As Schneider (2010) states, these policy areas are potentially attractive for political manipulation as they include—among others—social security, public safety, education, cultural affairs, administration, and health.

There are currently five major political parties in Germany: the conservative Christian Democratic Party (CDU) and its sister party the Christian Socialist Party (CSU), the Social Democratic Party (SPD), the Green Party (Bündnis 90/Die Grünen), the Liberal Democratic Party (FDP), and the Left-Wing Party (Die Linke).<sup>7</sup> Governments at the state level are led by either CDU/CSU or SPD. During the period we study, some of the states in our sample have one-party governments, others are governed by some form of coalition government (mainly made up of two parties), majority governments, or minority governments.

Since the political system of the German Laender is parliamentary, the question may arise as to whether German prime ministers even can exert an influence on fiscal policy. *De jure* they can, for at least two reasons. First, the prime minister appoints the cabinet ministers and therefore can to some extent ensure that the members of government back his or her preferred policy. Second, the prime minister has guideline competences (Richtlinienkompetenz), meaning that he or she has the authority to issue directives to the ministers.

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<sup>5</sup> For a more detailed overview of the German fiscal federalism, see, e.g., Seitz (2000) and Jochimsen and Nuscheler (2010).

<sup>6</sup> The 11 Laender making up the former Federal Republic of Germany are Baden-Wuerttemberg, Bavaria, West Berlin, Bremen, Hamburg, Hesse, Lower Saxony, North Rhine Westphalia, Rhineland-Palatinate, Saarland, and Schleswig-Holstein. The additional five states are Brandenburg, Mecklenburg-Vorpomerania, Thuringia, Saxony, and Saxony-Anhalt. Before unification, Berlin was divided into West and East Berlin. They merged into the new state Berlin in 1990.

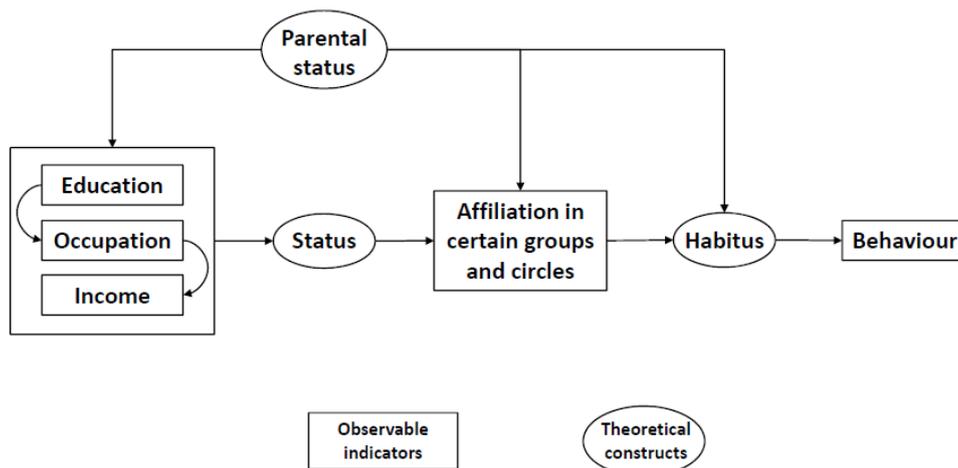
<sup>7</sup> The latter was founded in 2007 as a fusion of two parties: the Employment and Social Justice Party (WASG, founded in 2004) and the Party of Democratic Socialism (PDS, founded in 1989). Due to their substantive similarities, we do not differentiate between these three parties in our study.

Some hints of a *de facto* association between fiscal performance and prime minister transitions can be found in Figures A1 and A2 of the Appendix, which present movements in public spending and net public borrowing, respectively, within the Old German Laender between 1985–2009. To filter out symmetric business cycle effects, we calculated deviations from the contemporary means across the Laender. The marks along the single series indicate changes of prime minister. We observe a remarkable extent of cross-Laender variation with respect to fiscal performance. Moreover, leader transitions tend to be followed by changes in the (relative) level of public expenditures and debt financing. It is noteworthy that leader transitions do not necessarily coincide with changes in the governing party. In fact, only in 14 out of 38 cases did the incumbent prime minister have to leave office because he had not been re-elected. Hence, we need to carefully distinguish between leader and party effects.

#### 4. The Status Concept and its Measurement

In this section, we clarify the concept of *status*, discuss its implications for motives and patterns of behaviour, and show how it can be measured. Figure 1 provides a stylised account of how status is determined and how it translates into specific behaviour. First, we briefly describe this process and present empirical evidence linking attributes of status with economic behaviour and fiscal preferences. Second, we discuss quantitative measures of status widely used in many areas of sociology.

Figure 1: Stylised Status-Dependent Model of Action



#### About Status, Habitus, and Behaviour

Sociologists emphasise the importance of individual status in explaining patterns of and motives for behaviour. The term *status* refers to an individual's relative standing compared to

other members of society. It is determined by the individual's endowment with certain resources and attributes considered valuable by society, such as occupation, education, income, and prestige. Sociological research describes numerous examples of status-related behavioural patterns: the way people speak and dress, lifestyles, taste, consumption choices, leisure activities, political attitudes, and so on.<sup>8</sup>

The connection between status and behaviour is thought to be mediated by *habitus*. Habitus is defined as 'a system of lasting, transposable dispositions which, integrating past experiences, functions at every moment as a matrix of perceptions, appreciations, and actions' (Bourdieu and Wacquant, 1992: 18). In other words, the way people think and act is believed to be guided by a set of inclinations that individuals acquire over the life time, especially during adolescence (e.g., Crossley, 2001; Pickel, 2005).

Since nearly all personal experience occurs in structured social contexts (e.g., Berger and Luckmann, 1966; Bourdieu, 1984; Giddens, 1984; Bourdieu and Wacquant, 1992), the social environment plays a decisive role in the development of an individual's habitus. Of particular importance are so-called agents of socialisation, such as the family, peer groups, and educational institutions, as well as any other community or association with which an individual is affiliated. These agents filter the information an individual receives and provide him or her with—or, as some sociologists would say, condition the individual to<sup>9</sup>—predisposed interpretations, meanings, appraisals, and patterns of behaviour, manifested in (formal and informal) rules, codes of conduct, common ends, beliefs, ideals, etc. (Berger and Luckmann, 1966). Since the personal habitus is an individual representation of these social structures, it derives from a more general 'social habitus'. In status-conscious societies, there are at least two reasons why we should expect that social habitus appears to exhibit status-specific characteristics.

First, people of similar standing usually face similar life conditions, economic and cultural constraints, and pass through similar careers or trajectories, which is why they share certain perceptions and have similar experiences.<sup>10</sup>

Since the history of the individual is never anything other than a certain specification of the collective history of his class or group, *each individual system of dispositions* may be seen as a *structural variant* of all other group or class habitus, expressing the difference between trajectories and positions inside or outside the class. 'Personal style', the particular stamp marking all products of the

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<sup>8</sup> A particularly influential study in this field is Bourdieu (1984).

<sup>9</sup> This conditioning is done by the application of a complex system of social rewards and punishments, for example, approval/disapproval, esteem/contempt, or inclusion/exclusion. For a depiction in the context of a case study in an English township, see Elias and Scotson (1965).

<sup>10</sup> Analogue argumentations can be found, for instance, in Bourdieu (1984), Breen (1997), Sørensen (2000), and Goldthorpe (2002).

same habitus, whether practices or works, is never more than a deviation in relation to the style of a period or class [...]. (Bourdieu, 1977: 86; o.e.)

The second reason stresses the impact that personal status has on both the *quality* and *quantity* of social affiliation. On the one hand, high-status people are typically endowed with more prestige (Treiman, 1977), authority (Erikson and Goldthorpe, 1992), and power (Weber, 1946), inducing feelings of superiority (or inferiority, on the part of lower-status people), leading to resentment as well as social rivalry between ranks. On the other hand, a person's status defines the range of his or her social environment by increasing the intensity and likelihood of social interaction between people of similar standing. For instance, access to certain communities, associations, and institutions is usually limited to people sharing certain attributes related to status, e.g., to those in certain occupations or holding specific educational degrees, and even friendships and partnerships are primarily established between persons of equal rank (Blossfeld and Timm, 2003). Thus, status discrepancies within a society constitute a stratification system that sets boundaries between people of different standing, ties the formation as well as the reproduction of the habitus to these borders, and provides the basis for people's social identity (Goldthorpe, 2002).<sup>11</sup> As a consequence, we observe 'strong ties', emotional proximity, and solidarity between people of similar standing (Bourdieu, 1984).

Based on this line of reasoning, we expect that politicians' decisions will reflect the status-specific habitus of the social environment in which they were socialised. More specifically, according to the literature, there should be status-related differences regarding (i) time preferences and (ii) attitudes toward government size and welfare state.

- i. *Differing time preferences:* Empirical studies conducted at the household level show that lower levels of education and income are associated with a higher propensity to consume (e.g., Carroll and Kimball, 1996; Börsch-Supan and Essig, 2005) and lower debt aversion (Livingstone and Lunt, 1992; Lea et al., 1993, 1995), indicating a stronger preference for current consumption or even a greater than usual prevalence of myopic decision-making among individuals of low status (Angeletos et al., 2001).<sup>12</sup> In their model, Becker and Mulligan (1997) provide an explanation for this relationship

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<sup>11</sup> In this respect, a decisive aspect is that that the borders attributed to status discrepancies are hardly permeable. Studies such as the famous 'Programme for International Student Assessment' (PISA) conducted by the OECD, for example, reveal that the educational engagement of children is strongly influenced by the level of parental education (for Germany, see Prenzel et al., 2007). The same is true with respect to parental influence on the choice of occupation. Thus, we often observe little intergenerational mobility across different social strata (e.g., Breen and Goldthorpe, 2001; Büchner and Gerlitz, 2005).

<sup>12</sup> Further support for this conjecture is found in psychological and health studies showing that obesity, the use of tobacco and alcohol, drug addiction, etc.—which are commonly regarded as perfect examples of myopic decision-making—are much more prevalent among members of lower social classes. See Bradley and Corwyn (2002) for a review.

by determining individuals' time preferences endogenously. Both the level of education and the level of income enhance consumption patience by distracting people's attention from their present situation and promoting a greater consideration of future needs.<sup>13</sup> In this regard, Ainslie (1992: 57) states that 'living mostly for the present is our normal state of functioning, and that consistent behavior is sometimes acquired, to a greater or lesser extent, as a skill'.

- ii. *Differing attitudes toward the welfare state:* Survey data indicate that individual support of a large government sector and a high degree of redistribution is negatively correlated not only with personal income and education (Corneo and Grüner, 2002; Alesina and La Ferrara, 2005), but also with family income during childhood and father's education (Alesina and Giuliano, 2009). One interpretation of this finding is that the perceived value of publicly provided services depends on status: since persons with low status are more vulnerable to undesirable life events, such as unemployment and financial distress (McLeod and Kessler, 1990), they experience the benefits of public services more intensely and are more likely to be benefitted by them. In contrast, people of higher social status rarely need to rely on the social safety net. This conclusion is supported by Breen (1997), who argues that the modern welfare state is one of the most important institutions in reducing the high degree of uncertainty faced particularly by persons of low status.

Applying these arguments to the German Laender's prime ministers suggests that those with relatively lower status will be characterised by a lesser degree of consumption patience and a greater emphasis on the uncertainty reducing aspects of government activity and the welfare state. Thus, based on this reasoning, our research hypothesis is that due to a status-specific habitus, we expect prime ministers characterised by high status to bring about lower public expenditures and less reliance on debt financing.

An empirical indicator for status is derived in the next section.

### Measuring Status

Determinants of an individual's relative standing are studied in the sociological subdiscipline

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<sup>13</sup> In the case of education, they claim that 'schooling focuses students' attention on the future. Schooling can communicate images of the situations and difficulties of adult life, which are the future of childhood and adolescence. In addition, through repeated practice at problem solving, schooling helps children learn the art of scenario simulation. Thus educated people should be more productive at reducing the remoteness of future pleasures' (Becker and Mulligan, 1997: 735–736). With respect to income, they state that financial distress increases the desire for current income and, citing Irving Fisher, 'blinds a person to the needs of the future' (Becker and Mulligan, 1997: 732).

‘stratification research’. Here, status is regarded as an attribute of a social position, not of an individual *in persona*. Ranking of people is seen as a necessity of social life, since it provides individuals with an incentive to meet the requirements of a respective position.

As a functioning mechanism a society must somehow distribute its members in social positions and induce them to perform the duties of these positions. It must thus concern itself with motivation at two different levels: to instill in the proper individuals the desire to fill certain positions, and, once in these positions, the desire to perform the duties attached to them. (Davis and Moore, 1945: 242)

Accordingly, an individual’s status depends on the functional importance of the social position occupied. In modern societies, the position regarded as most relevant for an individual’s standing is occupation. Factors influencing the functional importance of a specific occupation are its endowment with certain resources and its association with valuable attributes. The most important indicators here are the required level of (formal) education, income, and prestige (Bourdieu, 1986; Bourdieu and Wacquant, 1992; Ganzeboom et al., 1992).

An important aspect of moving toward an empirical analysis is the operationalisation of status as a theoretical concept. There are, in general, two types of indicators measuring status: subjective and objective.

Based on survey data, indicators relying on subjective measures usually evaluate the prestige connected with different occupations. A widely used index is the Standard International Occupational Prestige Scale (SIOPS) by Treiman (1977). Objective indicators focus on the level of income and education associated with a certain occupation. A frequently applied index is the International Socio-Economic Index of Occupational Status (ISEI) introduced by Ganzeboom et al. (1992). This index is constructed by combining information on the average level of education and average income in different occupations.

Despite their differences, both indices provide a continuous measure of occupational status ranging from 0 to 100. However, in the subsequent analysis, we divide each index score by 100 to facilitate interpretation by avoiding very small coefficients. Both ISEI and SIOPS are based on the International Standard Classification of Occupations (ISCO-68) of the International Labour Organization (ILO, 1969), which makes them directly comparable. Although these indices are constructed based on international data, they are included in prominent nationwide surveys, such as the German Socio-Economic Panel (SOEP), the German General Social Survey (GGSS/ALLBUS), or the German version of the Programme for International Student Assessment (PISA) studies, and appear to perform well in empirical applications to Germany (Büchner and Gerlitz, 2005). Table 1 illustrates ISEI and SIOPS

scores for selected occupations.

Table 1: ISEI and SIOPS Scores for Selected Occupations

<b>Occupation</b>	<b>ISEI Score</b>	<b>SIOPS Score</b>
Architects and Engineers		
Architects, town planners	0.77	0.72
Electronics engineers	0.69	0.65
Mechanical engineers	0.68	0.66
Jurists		
Lawyers	0.85	0.73
Judges	0.90	0.76
Teachers		
University and higher education teachers	0.78	0.78
Secondary education teachers	0.71	0.60
Bookkeepers, Cashiers, and Related Occupations		
Bank teller	0.47	0.48
Bookkeeper	0.56	0.49
Cabinetmakers and Related Occupations		
Cabinetmakers	0.36	0.40
Bricklayers, Carpenters, Other Construction Workers		
Bricklayers	0.32	0.34
Carpenters	0.31	0.37

Note: Original ISEI and SIOPS scores are divided by 100.

To test the reliability of both indices in the case of Germany, Wolf (1995) calculates the correlation between ISEI and SIOPS based on data from the GGSS. A Pearson's correlation coefficient of 0.88 indicates that both indices are linearly connected and reliable. In the main part of our subsequent analysis we rely on the ISEI, since its construction is more transparent than that of a subjective indicator. However, we employ the SIOPS in robustness tests.

Our main variables of interest are the socioeconomic status of prime ministers' parents on the one hand and a prime minister's status advancement, understood as the distance between own socioeconomic status and parental status, on the other hand. Parental status is considered important, since the family is the most important agent of what sociologists call *primary socialisation*, which is understood as 'the first socialisation an individual undergoes in childhood' (Berger and Luckmann, 1966: 130). In contrast, a prime minister's own

occupational status defines his or her social environment after adolescence and hence affects *secondary socialisation*. However, since primary socialisation is regarded as ‘the most important one for an individual, and that the basic structure of all secondary socialization has to resemble that of primary socialization’ (Berger and Luckmann, 1966: 131), we expect own occupational status to be important only in case of a discrepancy with parental status.<sup>14</sup>

### **5. Preliminary analysis: Do time and fiscal preferences depend on status?**

Our research hypothesis is that German state governments led by prime ministers characterised by high family status spend less and accumulate fewer debts. This hypothesis relies on the assumption that an individual’s status determines his or her i) degree of consumption patience or myopia and ii) preferences for the size of the government sector.

The extant literature provides evidence that preferences for government size and patience are linked to single components of personal as well as parental status, i.e., education and income (cf. Section 4) but, to the best of our knowledge, there is no political economy study employing the status measures introduced above. Hence, in this section, we perform some preliminary analyses employing German survey data in order to demonstrate the accuracy of our core assumption. Our data source is the German General Social Survey (GGSS/ALLBUS), which has been conducted every two years since 1980. In every survey wave, about 2,800–3,500 representatively chosen respondents are interviewed.

We capture the degree of impatience or myopia, respectively, with answers to the following question, which was part of the GGSS questionnaire in 1984, 1994, 2000, and 2004:<sup>15</sup>

What about your personal pension provision or provision for incapacity or illness? Do you feel you are—

- (1) adequately provided for,
- (2) not adequately provided for,
- (3) or have you not thought about that yet?

We believe that a respondent who chooses either answer (2) or (3) can be regarded as impatient or myopic. Thus, we create a binary variable by assigning the value 1 to answer (1) and the value 0 to answers (2) and (3), pool the data from each single survey wave, and run a binary choice (probit) regression, employing respondents’ parental status (indicated by the

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<sup>14</sup> This point of view is quite different from the one employed by the few economic applications of the status concept. In those, only an individual’s contemporary or future *personal* status is supposed to influence decision-making. Status is seen as steering individual behaviour because it is viewed as a substitute for pecuniary incentives, i.e., status concerns are represented directly in an individual’s utility function. See Fershtman et al. (1996) for a summary.

<sup>15</sup> Descriptive statistics for this item can be found in Table A1 of the Appendix.

socioeconomic status of a respondent's father) and status advancement as defined in Section 4 as explanatory variables.<sup>16</sup> We control for the following factors:

- A time dummy for each survey wave (reference: first wave).
- Respondents' self-placement on a left/right scale capturing ideological affiliation. The scale ranges from 1 (left) to 10 (right).
- Dummies for respondents' employment status, differentiating between employees (including self-employed; reference group), students, retirees, unemployed, and other jobless persons.
- A dummy for members of employees' associations as membership may indicate identification with the working class.
- Respondents' age and a dummy for female respondents.
- A dummy for respondents living in East Germany, since the New Laender made up the former socialistic German Democratic Republic (GDR).

The GGSS reports ISEI (SIOPS) scores for each respondent, the respondent's father, and the respondent's spouse from 2000 (1980) onward. Hence, when utilising ISEI scores, we lose all observations from survey waves conducted before 2000. Therefore, we also employ SIOPS scores to test the robustness of our results.

Table 2 reports the results of the probit specification.<sup>17</sup> The first column shows the coefficients of the maximum likelihood estimation for the underlying continuous latent variable model. In our case, the latent variable may be interpreted as the individual degree of consumption patience. The second column shows the corresponding marginal effects, which are calculated based on the sample averages.

Focussing on our variables of main interest, we find that they are significantly different from zero at the 1% level. The prevalence of myopia is lower the higher both parental status and status advancement, which is well in line with our expectations. Both effects appear to be substantial: a hike in parental status (status advancement) by 0.5—which roughly corresponds to the distance between tradesmen and academic professions—increases the probability of being provided for by about 21 (18.5) percentage points (pp).

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<sup>16</sup> Here, the variable *status advancement* equals the difference between the parental status score and the status score of the head of the household the respondent lives in, whereas the latter score is calculated as follows: first, we consider the status score of the respondent and the respondent's spouse. Then, we assign the larger of the two numbers to the respondent.

<sup>17</sup> Alternatively, we employ an ordered probit model and a multinomial model. Our results remain robust and are available on request.

Table 2: Determinants of Consumption Patience

Variables	Coefficient	Marginal effect	Standard error
Constant	-1.023 **	–	0.156
2004	-0.294 **	-0.111	0.051
Left/right placement	0.049**	0.018	0.015
Student	-0.502	-0.197	0.275
Retiree	0.243**	0.089	0.091
Unemployed	-0.478 **	-0.187	0.105
Jobless for other reasons	-0.021	-0.008	0.087
Union member	0.128	0.047	0.073
Age	0.017**	0.006	0.002
Female	-0.147**	-0.055	0.053
East German	-0.177**	-0.067	0.055
Parental status	1.135**	0.427	0.194
Status advancement	0.989**	0.372	0.177
Pseudo-R <sup>2</sup>	0.091		
Observations	2798		
Parameters	13		

Notes: Results are based on a maximum likelihood probit estimation. White (1980) robust standard errors are reported. \* and \*\* indicate significance at the 5% and 1% level, respectively.

With respect to individual preferences for public sector size, we consider the following items, which were part of the GGSS waves in 1990, 1996, and 2006:<sup>18</sup>

On the whole, do you think it should or should not be the government's responsibility to ...

- a. ... provide a job for everyone who wants one
- b. ... provide health care for the sick
- c. ... provide a decent standard of living for the old
- d. ... provide a decent standard of living for the unemployed
- e. ... reduce income differences between the rich and the poor
- f. ... give financial help to university students from low-income families
- g. ... provide decent housing for those who can't afford it

The respondents could choose between four answers, which appear in a logical order, with higher numbers indicating less support for a large public sector: (1) definitely should be, (2) probably should be, (3) probably should not be, or (4) definitely should not be. Based on these seven items, we conduct a principal component analysis and employ the first principal component as an indicator capturing individual support for a large public sector.<sup>19</sup> Higher values of the indicator variable imply greater support for a large public sector.<sup>20</sup>

<sup>18</sup> Note that we again lose all observations collected before 2000 when employing ISEI scores. Descriptive statistics for these items can be found in Table A2 of the Appendix.

<sup>19</sup> The first principal component has an eigenvalue of 3.2 and explains 46% of the common variation. None of the other eigenvalues has a value greater than 1.

<sup>20</sup> The factor loadings of the seven items are sufficiently high: -0.40; -0.63; -0.65; -0.46; -0.42; -0.52; -0.51.

Table 3 shows the results of an OLS regression with the principal component as the endogenous variable, employing the same exogenous variables as before. The first column contains the coefficients calculated based on the original units of measurement. The second column reports standardised coefficients (beta coefficients), which facilitate interpretation of the effects and permit conclusions about the relative importance of the single covariates.

Concentrating yet again on our variables of interest, we find that both parental status and status advancement are significant at the 1% level and with signs in accordance with our prior. The poorer an individual's socioeconomic background, the greater his or her support for a large government sector. The beta coefficients reveal that the impact of our status measures is considerable as they have the largest standardised effects (in absolute terms): a hike in parental status or status advancement by one standard deviation decreases the fiscal preference indicator by about 0.17 standard deviations.

Table 3: Determinants of Preferences for Public Sector Size

Variables	Coefficient	Beta coefficient	Standard error
Constant	0.662	–	0.156
Left/right placement	-0.146**	-0.149	0.039
Student	0.216	0.011	0.770
Retiree	0.210	0.053	0.235
Unemployed	0.410	0.062	0.272
Jobless for other reasons	0.622*	0.099	0.260
Union member	0.363*	0.087	0.164
Age	0.011	0.097	0.006
Female	0.110	0.031	0.144
East German	0.573**	0.157	0.149
Parental status	-1.899**	-0.165	0.509
Status advancement	-1.518**	-0.171	0.392
R <sup>2</sup>	0.131		
Observations	597		
Parameters	12		

Notes: Results are based on an OLS estimation. \* and \*\* indicate significance at the 5% and 1% level, respectively.

To check the robustness of our results, we employ the SIOPS scores as status measures instead of the ISEI. This procedure has the advantage that SIOPS scores have been kept since the first wave of the GGSS, so the number of observations in each specification increases considerably. We find that our results are not only extremely robust, but even more significant, reflecting the larger sample size.<sup>21</sup>

<sup>21</sup> Results available on request.

## 6. Prime Ministers' socioeconomic background and fiscal policy

After these preliminary analyses, which support our hypothesis about the status dependence of consumption patience and fiscal preferences, we now turn to the investigation of the impact of German prime ministers' family status on fiscal policies in the German Laender. First, we will introduce the data and motivate our econometric setup. Then, we present the results of our main specifications and perform some checks for robustness.

### 6.1 Empirical approach

#### Model and Data<sup>22</sup>

We employ panel data from 1985–2009 for the West German non city-states and from 1992–2009 for the East German non city-states (unbalanced panel) and estimate the following model:<sup>23</sup>

$$(1) y_{i,t} = \alpha_i + \mu_t + \rho y_{i,t-1} + \beta' \text{economic variables}_{i,t} + \gamma' \text{political variables}_{i,t} + \delta' \text{leader variables}_{i,t} + \varepsilon_{i,t}$$

We use two dependent variables to measure the fiscal policy stance of a prime minister: (i) public expenditures and (ii) net public borrowing, both in percent of GDP. The *leader variables* contain characteristics describing the prime minister of state  $i$  at time  $t$ .  $\alpha_i$  is a state-specific intercept that is assumed to be time invariant and  $\mu_t$  a parameter that varies across time but not across states. We include the first lag of the dependent variable in our model to account for persistency and gradual budget adjustments.  $\varepsilon_{it}$  is an i.i.d. error term.

As economic control variables we consider the first lag of the debt-to-GDP ratio in order to capture the budgetary situation, the contemporary real GDP growth rate and the unemployment rate as business cycle indicators, and the share of net transfers received through the German fiscal equalisation system (Länderfinanzausgleich) to GDP.<sup>24</sup>

Our political control variables measure constraints on a prime minister's power, which could affect his or her impact on fiscal performance. We add a dummy variable indicating whether the government is led by the SPD or CDU in order to capture partisan ideology effects,

<sup>22</sup> Data sources are described in the Appendix.

<sup>23</sup> The time constraints are due to a lack of publicly available data on public expenditures and some of the economic controls from before 1985 for West German Laender and before 1992 for East German Laender. The three city-states are excluded from our analysis because they combine competences of the state and the local level and are therefore not comparable to the non city-states.

<sup>24</sup> The German fiscal equalisation system (Länderfinanzausgleich) harmonises revenues across states, i.e., revenues are transferred from financially strong to weaker states. This may affect the incentives to run a sound fiscal policy in states that are net recipients. See Seitz (2000) for a detailed description.

dummies for coalition governments and minority governments to account for effects of political dispersion or conflicts of interest,<sup>25</sup> and dummies for pre-election and election years to control for political budget cycles. Further, we control for the share of votes the prime minister's party received in the last election. This variable indicates the strength of the incumbent governing party. Finally, we include a dummy that indicates whether the minister of finance is from the same party as the prime minister, since the finance minister has significant authority regarding preparation of the public budget. We expect that a finance minister from the same party is more likely to back the prime minister's political course (Jochimsen and Nuscheler, 2010).

Our main variables of interest among the leader characteristics are the socioeconomic status of prime ministers' parents and change in their own status. Following the literature and adding additional controls, we include as further characteristics:

- A prime minister's age and number of years in office, thus capturing experience.
- A dummy for prime ministers who have been members in employees' associations, since membership may serve as an indicator of an individual's habitus, i.e., indicate that he or she is prone to implementing policies benefitting a certain group in society.
- A dummy for prime ministers of states in which they did not formerly reside. We believe this variable to be an indicator for how strongly a leader is attached to the state he or she governs.
- A dummy for years in which a new prime minister comes into power to capture transition effects.<sup>26</sup>

### Econometric Methodology

We estimate Equation (1) with a two-way fixed-effects model, allowing for the state- and time-specific effects to be correlated with the other covariates. A Hausman test reveals that the results of the fixed-effects approach differ significantly from those of a random-effects approach or a pooled OLS model, supporting our empirical specification. The lagged dependent variable correlates with the error term, which causes the least squares dummy variable (LSDV) estimator of the autoregressive coefficient  $\rho$  to be biased downward (Judson and Owen, 1997), while the bias in the coefficients of the exogenous regressors tends to be positive but much smaller (in absolute terms). Moreover, the bias becomes negligible for

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<sup>25</sup> As Edin and Ohlsson (1991) and de Haan and Sturm (1994, 1997) state, the measurement of political dispersion by a single ordinal variable, as employed by Roubini and Sachs (1989), is not recommended, since this imposes a strong restriction on its effect.

<sup>26</sup> Transition years imply coding problems, since we can only take into account one prime minister each year. In these cases, we decided to include the prime minister who held the office for the larger part of the year.

growing  $T$ .

An alternative to LSDV estimation is a GMM approach, as suggested by Arellano and Bond (1991). However, GMM estimators suffer from poor finite sample properties for small  $N$  and tend to underestimate the coefficients of the exogenous regressors (Kiviet, 1995).

Taking into consideration the advantages and disadvantages of both estimation techniques, we rely on the LSDV estimator in the main part of our analysis and apply GMM as part of our robustness tests. Other robustness checks investigate whether our results differ across the West and East German states, different government constellations, and when including additional control variables.

## 6.2 Results

### Main specifications

Results of the regressions explaining public spending in the German Laender are presented in Table 4. In a first step, we estimate a general model containing all the theory-relevant covariates described in Subsection 6.1. Then, we eliminate insignificant regressors by applying a consistent general-to-specific approach (Hendry, 2000) so as to enhance estimation efficiency.

We find that the coefficient of the lagged debt-to-GDP ratio is significantly negative at the 1% level. Hence, Laender with a poor budgetary situation reduce their expenditures. This suggests that the political process does react to the debt situation in a state, but not strongly. In the short run, a 1 percentage point (pp) increase in the previous period's debt-to-GDP ratio reduces government expenditures in relation to GDP by 0.06 pp. The long-run multiplier is 0.3, which is still quite modest.

The real GDP growth rate also exerts a significantly negative impact, indicating that state governments engage in counter-cyclical fiscal policy. However, given the short-term nature of stabilisation, the effect is small: a 1 pp reduction in GDP growth triggers an adjustment of 0.1 pp in the expenditure-to-GDP ratio; the long-run effect is about 0.5. Transfers received through the fiscal equalisation scheme in relation to GDP show a positive coefficient, but the individual effect is not significantly different from zero.<sup>27</sup>

Among the political covariates, three out of seven variables survive the model reduction. The dummies for minority governments and ministers of finance who are not from the same party as the prime minister have the expected positive signs, meaning that the greater the dispersion of power within a government, the higher the level of public spending. The former variable is

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<sup>27</sup> Note that we cannot exclude this variable from the model without violating the testing-down restriction.

individually insignificant; the latter has a substantial impact—a finance minister from a different party causes an increase in the expenditure-to-GDP ratio of over 0.45 pp in the short run. In the long run, this effect grows to over 2 pp. The vote share of the prime minister’s party also reveals a positive impact on expenditures, but the economic effect is almost negligible.

Table 4: Results for Public Expenditures Over GDP (in %)

Variables	General Model		Reduced Model	
	Coefficient	Stand. error	Coefficient	Stand. error
Publ. expend./GDP (-1)	0.750**	0.054	0.794**	0.046
<b>Economic variables</b>				
Debt-to-GDP-ratio (-1)	-0.061**	0.018	-0.059**	0.017
GDP growth	-0.083**	0.027	-0.094**	0.025
Unemployment rate	0.038	0.029		
Transfers/GDP	0.303	0.211	0.337	0.219
<b>Political variables</b>				
SPD-led government	-0.178	0.102		
Coalition	0.215	0.128		
Minority government	0.674*	0.318	0.427	0.234
Vote share gov. party	0.035*	0.014	0.018*	0.008
Pre-election year	0.070	0.065		
Election year	-0.002	0.058		
MoF from different party	0.411*	0.194	0.458*	0.189
<b>Leader variables</b>				
PM change	-0.018	0.077		
Outside PM	0.081	0.150		
Union member	-0.043	0.083		
Age	-0.002	0.006		
Years in office	-0.003	0.010		
Parental status	-1.448**	0.424	-1.021**	0.385
Status advancement	-1.481**	0.494	-1.116*	0.456
R <sup>2</sup> (without state and time fixed effects)	0.899		0.894	
Observations	277		277	
Parameters	55		45	
Testing-down restriction			Chi <sup>2</sup> (10) = 17.0562	

Notes: Results are based on a least squares dummy variable (LSDV) estimation. The models include cross-section and time fixed effects. Panel robust standard errors are reported. \* and \*\* indicate significance at the 5% and 1% level, respectively.

Regarding leader characteristics, we find that parental status and status advancement are the only variables remaining in the reduced model. They show the expected signs and are

significant at the 1% and 5% level, respectively. Tenures of prime ministers who worked in academic professions before taking up politics (average ISEI score about 0.85) are associated with a public expenditure quota that is on average 0.55 pp less than that during tenures of prime ministers who were formerly tradesmen (average ISEI score about 0.35), keeping parental status constant. The influence of parental status is only slightly smaller in magnitude: the difference between prime ministers whose parents hold academic professions compared to those whose parents are tradesmen is about 0.5 pp. Other leader characteristics exert no significant influence on public spending. In the long run, the expenditure-to-GDP ratio of Laender with prime ministers who formerly were tradesmen is 2.7pp lower than it is in Laender with prime ministers who previously held an academic post. The parental status effect multiplier is about 2.5, but the difference between the coefficients of the two status variables is not statistically significant.<sup>28</sup> Thus, the impact of status is not only statistically significant with theory-consistent signs but also economically substantial.

Table 5 presents the results for net public borrowing over GDP. The coefficients of the general model including all covariates are shown on the left-hand side; the results for the reduced model are shown on the right-hand side. With respect to the economic covariates, we observe a counter-cyclical movement of net borrowings, just like in the case of public expenditures, but whereas public spending responds to GDP growth, net borrowing reacts to the unemployment rate. This makes sense, since a rise in unemployment leads to a decrease in public revenues and, thus, raises the current deficit even if the level of expenditures is held constant. The economic impact of unemployment on the deficit-to-GDP ratio is small, though. After a 1 pp increase in the unemployment rate, the ratio decreases by only 0.07 pp in the short run and by about 0.15 pp in the long run. The coefficient of the lagged debt-to-GDP-ratio is negative also, which indicates that states tend to reduce deficits when they have a high level of debt. Yet, again, the adjustment effect is small, a decline of less than 0.1 (0.2) pp in the short (long) run. Unlike in the case of public spending, we find a negative effect of received transfers, which suggests that such transfers are a substitute for deficit spending. A 1 pp increase in transfers lowers the deficit-to-GDP ratio by 0.4 pp and the long-run multiplier is 0.8.

Regarding political controls, we find that the election year dummy has a positive sign, indicating evidence of a political budget cycle in public deficits, but it is not individually significant. The dummy for finance ministers from other parties is positive, which is in line

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<sup>28</sup> The p-value for a corresponding Chi<sup>2</sup>-test with the null hypothesis ‘coefficients are equal’ is 0.57.

with results reported in Jochimsen and Nuscheler (2010) and could be interpreted as evidence of a common pool problem with respect to the public budget (Roubini and Sachs, 1989).

Table 5: Results for Net Public Borrowing Over GDP (in %)

Variables	General Model		Reduced Model	
	Coefficient	Stand. error	Coefficient	Stand. error
Net borrow./GDP (-1)	0.549**	0.097	0.555**	0.080
<b>Economic variables</b>				
Debt-to-GDP-ratio (-1)	-0.086**	0.014	-0.086**	0.013
GDP growth	0.022	0.030		
Unemployment rate	0.073**	0.020	0.067**	0.024
Transfers/GDP	-0.258*	0.121	-0.367**	0.097
<b>Political variables</b>				
SPD-led government	-0.016	0.089		
Coalition	-0.019	0.081		
Minority government	-0.007	0.138		
Vote share gov. party	-0.004	0.008		
Pre-election year	0.039	0.055		
Election year	0.087	0.046	0.082	0.050
MoF from different party	0.303*	0.117	0.363**	0.118
<b>Leader variables</b>				
PM change	-0.179	0.103	-0.179	0.093
Outside PM	0.204*	0.086	0.270**	0.071
Union member	0.049	0.062		
Age	0.007	0.005		
Years in office	-0.023**	0.006	-0.018**	0.005
Parental status	-1.095**	0.343	-1.226**	0.309
Status advancement	-1.129**	0.360	-1.211**	0.299
R <sup>2</sup> (without state and time fixed effects)	0.765		0.763	
Observations	277		277	
Parameters	55		47	
Testing-down restriction			Chi <sup>2</sup> (8) = 6.99666	

Notes: Results are based on a least squares dummy variable (LSDV) estimation. The models include cross-section and time fixed effects. Panel robust standard errors are reported. \* and \*\* indicate significance at the 5% and 1% level, respectively.

Five out of seven leader characteristics remain in the reduced model. The dummy for years in which a new prime minister takes office has a negative sign but is individually insignificant. Tenures of prime ministers of states in which they did not formerly reside (dummy *Outside PM*) are connected with a rise in net borrowing. Arguably, prime ministers who come from outside the state they govern do not feel that closely connected to it and, thus, have fewer

incentives to conduct sustainable fiscal policy and are more prone to myopic decision-making. The deficit-to-GDP ratio is about 0.3 pp higher in the case of an outside prime minister, with a long-run multiplier of 0.6. We also find that the longer a prime minister stays in office, the smaller is net borrowing over GDP. We interpret this result as reflecting increasing competence during incumbency: the more experienced a prime minister, the easier it is for him or her to keep the budget in balance. In addition, staying in office for a long time may deepen attachment to the governed state. The effect is fairly modest, though. Staying in office for a second term lowers the deficit-to-GDP ratio by 0.07 pp.

As in the case of public spending, a prime minister's parental status and own status advancement play an important role in explaining variations in fiscal performance: the higher the parental status or own status advancement, the lower the inclination toward deficit spending. Both effects are significant at the 1% level and their coefficients are of a similar magnitude as in the case of public spending, which implies that, on average, every additional Euro of public expenditure by a prime minister of low status is deficit financed. Comparing again tradesman and academic profession parental background, prime ministers from the latter have a 0.6 pp lower deficit in the short run and a 1.4 pp lower deficit in the long run. Similar effects apply in the case of status advancement and the coefficients of the two status variables are not significantly different.<sup>29</sup>

### Checks for Robustness

To check the robustness of our results and glean further insight, we conduct several experiments. First, we test whether our results are affected by the estimation method. We re-estimate Equation (1) using a GMM approach to account for the fact that the lagged dependent variable is correlated with the error term. We apply one-step GMM estimation and use up to five valid lags of the dependent variable as instruments.<sup>30</sup> The results for public spending and debt financing are presented in the Appendix, Table A3. In line with findings from simulation studies, most coefficients and standard errors decrease in the GMM approach, but in our case the differences are typically rather small. The biggest difference can be found in the model for public spending and the coefficients for *parental status* and *status advancement*. However, both variables are now significant at the 1% level and the long-run

<sup>29</sup> The p-value for a corresponding Chi<sup>2</sup>-test with the null hypothesis 'coefficients are equal' is 0.92.

<sup>30</sup> The number of lags is restricted for two reasons. First, standard econometric software is not able to invert the matrix of instruments when using all valid lags to define moment conditions (as suggested by Arellano and Bond, 1991), as the computational requirements increase substantially. Second, simulation studies show that there is a tradeoff when increasing the number of lags: together with efficiency, the finite sample bias of the GMM estimates also increases (Judson and Owen, 1997). With respect to our variables of main interest, we find no significant changes when varying the number of lags used as instruments, employing from 1 up to 10 lags.

multipliers remain basically constant, so that even in this case our conclusions do not change notably.

Second, we check whether our results differ across the Old and New Laender. Since the New Laender made up the former socialist German Democratic Republic (GDR), there could be status-specific differences between them and the Old Laender. We address this problem by including two dummy variables:  $D_1$  takes the value 1 for West German Laender and 0 for East German Laender;  $D_2$  the other way around. Then, we let these dummies interact with the political controls and leader characteristics and estimate the following equation:<sup>31</sup>

$$(2) y_{i,t} = \alpha_i + \mu_t + \rho y_{i,t-1} + \beta' \text{economic variables}_{i,t} + \sum_k \gamma'_k D_k \text{political variables}_{i,t} + \sum_k \delta'_k D_k \text{leader variables}_{i,t} + \varepsilon_{i,t}$$

The results for both public expenditure and debt financing are presented in Table A4 of the Appendix. We find that our variables of main interest exert a statistically significant influence in both subpanels, and that this influence is greater in the East German states than it is in the West German ones.<sup>32</sup> The coefficient of *parental status* is more than two times larger in case of public spending and more than four times larger in case of net borrowing within the New Laender. The coefficient of *status advancement* is three times the magnitude in the case of public spending and seven times in the case of net borrowing.

An interesting result is that a prime minister's experience (measured as years in office) has a statistically significant effect only in the New Laender. The longer an East German prime minister stays in power, the lower the public spending and debt financing in his or her state, which supports our proposition that experience enhances competence. The five New Laender suffered a lack in infrastructure and continue to lag behind the Old Laender in per-capita GDP and income, making the economic conditions in those states far more challenging; hence, competence might be even more valuable in the New Laender.

There are several differences between East and West German states when it comes to the political controls. Within the New Laender, tenures of SPD-led governments are associated with a decline in public expenditure and net borrowing, whereas coalitions tend to increase

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<sup>31</sup> Alternatively, we could have estimated two balanced subpanels: one for the Old Laender and one for the New Laender. We decided to estimate a nested model for two reasons: (i) it increases the number of observations and hence enhances efficiency and (ii) it allows performing statistical tests across Old and New Laender.

<sup>32</sup> Note that a Chi-squared test reveals that *parental status* and *status advancement* are jointly significant within the East German Laender at the 1% level. Hence, the individual insignificance of both coefficients is due to collinearity.

public spending and debt financing. Minority governments exert a significantly positive influence only on public spending.

In a third robustness check, we examine the effect of including additional control variables. First, we control for different partisan compositions of the government, following Seitz (2000), Galli and Rossi (2002), Berger and Holler (2007), Schneider (2010), and Jochimsen and Nuscheler (2010). Dummies for each composition that occurred during our sample period replace the dummies for SPD-led governments and coalition governments. The output is presented in Table A5 of the Appendix and reveals that the results for the economic indicators and leader characteristics hardly change. We are also concerned about the problem of spurious causation due to omitted variables. It could be argued that our findings regarding the impact of a prime minister's socioeconomic background are driven by the socioeconomic conditions of the electorate. We examined this possibility by including real disposable income per head in our regressions. We also controlled for several demographic factors, i.e., population growth as well as the share of population aged less than 25 years and more than 65 years, since these groups typically benefit overproportionally from the public provision of goods. However, since none of these factors reveals a significant impact on the endogenous variables or changes our results, we do not report these estimates (they are available upon request).

Finally, we check whether choice of status index affects our findings. As mentioned in Section 4, there are essentially two ways of measuring an individual's status: objective indicators (e.g., ISEI) or subjective indicators (e.g., SIOPS). We replace the ISEI scores with the SIOPS scores and re-estimate Equation (1). As can be seen in Table A6 of the Appendix, use of the other index hardly changes the results: the coefficients of *parental status* and *status advancement* become a little larger and are still significant at the 1% level.

## 7. Conclusion

'Classical' theories in political economy that view politicians' motives as decisive in fiscal performance often reveal little explanatory power in empirical research. Neither opportunism, nor benevolence, nor partisan ideology satisfactorily explain politicians' decision-making. In light of this, some economics researchers have begun focussing on politicians' backgrounds instead, taking into account age, experience, or certain educational and occupational characteristics. However, yet again the results are ambiguous and not particularly robust.

In contrast, an important strand in sociological research argues that the way people think and act is steered by a set of socially constituted schemes that depend on an individual's status—

i.e., his or her relative standing within society. Evidence from household and survey data as well as our own empirical investigations employing the German General Social Survey indicate that individual status or factors related to it (such as educational attainment and income) might help explain differences in how leaders conduct fiscal policy.

In our novel empirical analysis, we test whether a head of government's family status has an impact on the incumbent government's fiscal performance. We focus on the German Laender, as they are characterised by a high degree of political and institutional homogeneity and their prime ministers' are empowered with extensive fiscal competences.

Our extremely robust and theory-consistent findings reveal that a prime minister's family status—operationalised by parental status and own status advancement—influences fiscal performance in a statistically significant and economically relevant way. The higher a prime minister's parental status and own status advancement, the lower are the incumbent government's public spending and debt financing in relation to GDP. For example, tenures of prime ministers who worked in academic professions before taking up politics are associated with a public expenditure quota that is on average 0.55 percentage points less than that of tenures of prime ministers who were formerly tradesmen. The influence of parental status is only slightly smaller in magnitude. In the long run, the expenditure-to-GDP ratio of Laender with prime ministers who formerly worked as tradesmen is 2.7 percentage points lower than that of Laender having prime ministers who formerly held an academic post. The parental status effect multiplier is about 2.5. In the case of net public borrowing over GDP, prime ministers with an academic history have a 0.6 percentage points lower deficit in the short run and a 1.4 percentage points lower deficit in the long run. Similar effects are found for the case of parental status.

In the theoretical part of our paper, we emphasise that individual preferences and patterns of behaviour reflect status-specific dispositions. However, it is not only aggregate public spending, but also preferences regarding the composition of the public budget, that might depend on individual status. In this regard, effects of social rivalry may be important, e.g., with respect to the share of public expenditure on policies such as social security or education. Therefore, an interesting task for future research would be an investigation of the influence of the head of government's status on single items of public expenditure.

## **Appendix:**

### **Data Sources**

#### Economic Controls

Data on public expenditures, real GDP growth, unemployment rate, per-capita income, and the demography of population for each German state are from the Federal Statistical Office (Statistisches Bundesamt). Data on public debts, net public borrowing, and transfers between the Laender within the fiscal equalisation system are from the Federal Ministry of Finance.

#### Political Controls

Data on election dates, vote shares, and government composition are taken from the homepages of the German Laender and the State Returning Officers (Landeswahlleiter), as is historical information on the party affiliation of the ministers of finance.

#### Leader Characteristics

Information on prime ministers is from various sources. Years in which a new prime minister took office are identified using the homepages of the German Laender and the State Returning Officers.

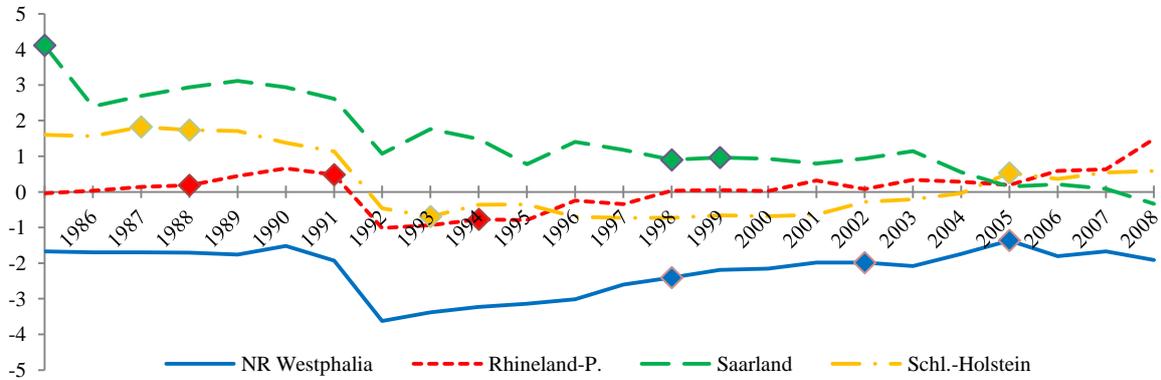
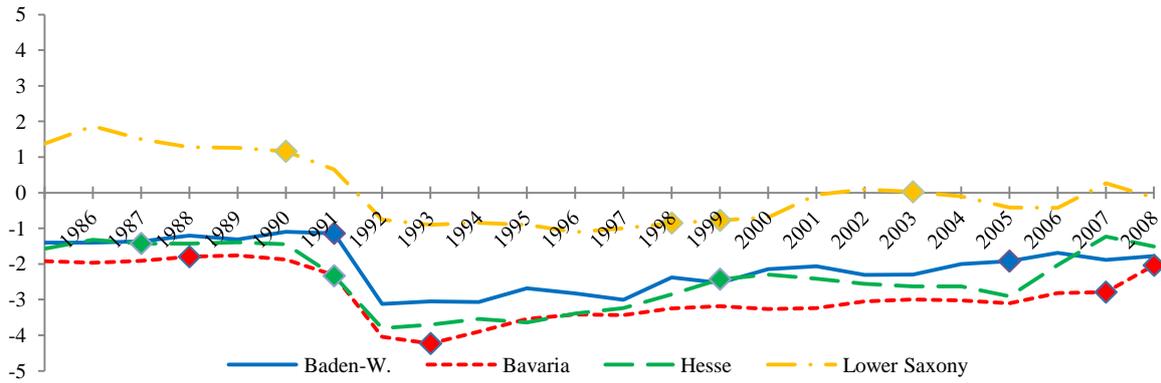
Information on prime ministers' dates of birth, places of residence, occupational histories, and whether they have been union members is from the Munzinger Online biography and the public record offices of the German Laender. Both provide brief biographies of public figures, especially politicians. In a few cases we also rely on information provided on personal homepages of (former) prime ministers. The variable *age* refers to a prime minister's age at the end of the year.

The variable *parental status* measures the occupational status score of prime ministers' parents. To construct this variable, we coded the occupations of prime ministers' parents according to the ISCO-68 and then applied the ISEI and SIOPS scores. When both parents were working or when a parent held more than one occupation during his or her career, we decided to employ the highest ISEI and SIOPS score. In cases where a prime minister was entirely raised by one parent only (due to divorce or death of the other parent), we decided to take only the status score of that parent into account. Further, we do not differentiate between biological and stepparents.

For the variable *status advancement* we focus on the positions prime ministers held before their political career, which we defined as first membership in a party executive committee or ministry. In cases where prime ministers engaged in more than one occupation during their career, we chose the occupation with the highest ISEI and SIOPS score.

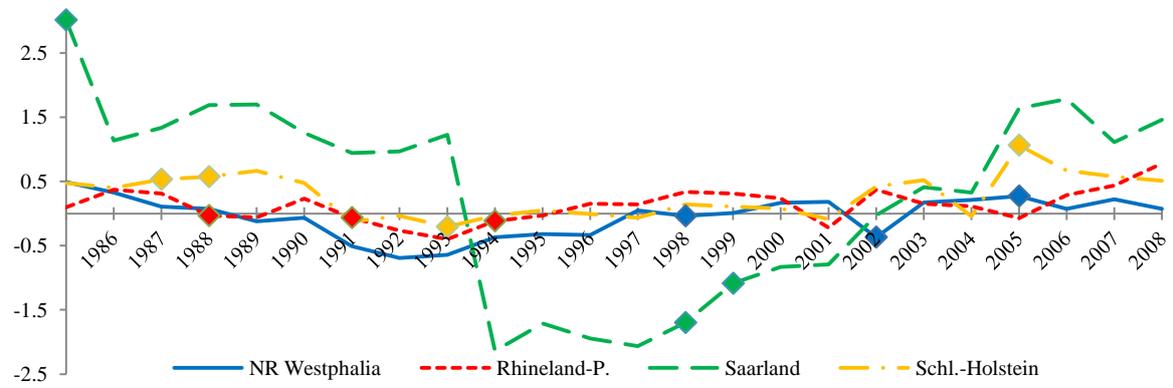
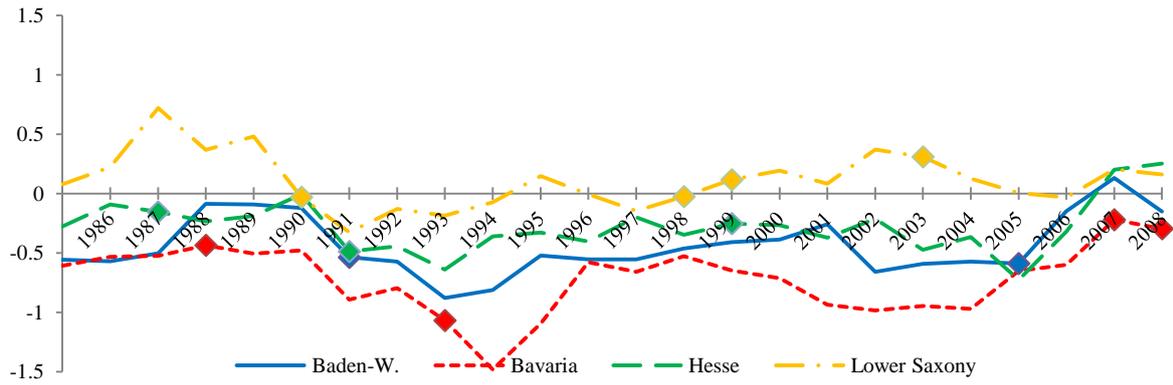
**Additional Figures, Descriptive Statistics, and Checks for Robustness**

Figures A1a and A1b: Public Expenditures Over GDP in the West German Laender (in %)



Notes: Public expenditures over GDP are calculated as deviations from the contemporary cross-sectional mean. Marks along the series indicate prime minister transitions.

Figures A2a and A2b: Net Public Borrowing Over GDP in the West German Laender (in %)



Notes: Net public borrowings over GDP are calculated as deviations from the contemporary cross-sectional mean. Marks along the series indicate prime minister transitions.

Table A1: Descriptive Statistics for the item ‘What about your personal pension provision or provision for incapacity or illness? Do you feel you are—

Year of survey	Obs.	Frequencies of different response options		
		(1) adequately provided for,	(2) not adequately provided for,	(3) or have you not thought about that yet?’
1984	2994	2133	491	370
1994	3446	2096	942	408
2000	3762	2379	996	387
2004	2925	1566	1107	252
Together	13127	8174	3536	1417

Table A2: Descriptive Statistics for the items ‘On the whole, do you think it should or should not be the government’s responsibility to ...

	Obs.	Frequencies of different response options				Mean	Standard deviation
		(1) definitely should be	(2) probably should be	(3) probably should not be	(4) definitely should not be		
a. ... provide a job for everyone who wants one	7584	2597	3136	1497	354	1.95	0.846
b. ... provide health care for the sick	7734	4318	3141	235	40	1.48	0.584
c. ... provide a decent standard of living for the old	7726	4050	3332	307	37	1.52	0.597
d. ... provide a decent standard of living for the unemployed	7469	1572	4354	1213	330	2.04	0.734
e. ... reduce income differences between the rich and the poor	7385	2140	2877	1802	566	2.11	0.906
f. ... give financial help to university students from low-income families	7564	2530	4184	694	156	1.80	0.681
g. ... provide decent housing for those who can’t afford it’	7476	1825	4186	1209	256	1.98	0.736

Table A3: GMM Estimation for Public Expenditures and Net Borrowing Over GDP (in %)

Variables	Public Expenditures/GDP		Net Borrowing/GDP	
	Coefficient	Stand. error	Coefficient	Stand. error
Y (-1)	0.813 **	0.060	0.594 **	0.110
<b>Economic variables</b>				
Debt-to-GDP-ratio (-1)	-0.048 **	0.018	-0.081 **	0.014
GDP growth	-0.109 **	0.027	0.016	0.031
Unemployment rate	0.014	0.033	0.076 **	0.020
Transfers/GDP	0.297	0.201	-0.267 *	0.123
<b>Political variables</b>				
SPD-led government	-0.137	0.092	-0.018	0.078
Coalition	0.198	0.123	-0.033	0.071
Minority government	0.511	0.326	-0.076	0.130
Vote share gov. party	0.029 *	0.013	-0.006	0.008
Pre-election year	0.067	0.064	0.040	0.055
Election year	-0.011	0.057	0.082	0.046
MoF from different party	0.301	0.169	0.251 *	0.108
<b>Leader variables</b>				
PM change	0.012	0.070	-0.158	0.094
Outside PM	-0.012	0.135	0.187 *	0.076
Union member	-0.039	0.071	0.060	0.054
Age	-0.003	0.006	0.006	0.005
Years in office	-0.001	0.009	-0.021 **	0.006
Parental status	-1.085 **	0.275	-0.998 **	0.332
Status advancement	-1.071 **	0.303	-1.032 **	0.365
R <sup>2</sup> (without state and time fixed effects)	0.897		0.764	
Observations	277		277	
Parameters	55		55	
Sargan test	Chi <sup>2</sup> (104) = 92.49		Chi <sup>2</sup> (119) = 106.3	

Notes: For GMM estimation, lags 2–6 of the dependent variable are used as instruments. Both models include cross-section and time fixed effects. Panel robust standard errors are reported. \* and \*\* indicate significance at the 5% and 1% level, respectively.

Table A4: Comparison Between West and East German Laender

Variables	Public Expenditures/GDP		Net Borrowing/GDP		
	Coefficient	Stand. error	Coefficient	Stand. error	
Y (-1)	0.701**	0.061	0.499**	0.106	
<b>Economic variables</b>					
Debt-to-GDP-ratio (-1)	-0.048**	0.024	-0.085**	0.015	
GDP growth	-0.080**	0.031	0.018	0.036	
Unemployment rate	0.055	0.037	0.088**	0.023	
Transfers/GDP	0.204	0.220	-0.250*	0.117	
<b>Political variables</b>					
SPD-led government	West	-0.167	0.085	0.023	0.116
	East	-1.992**	0.671	-1.325*	0.573
Coalition	West	0.070	0.119	-0.047	0.098
	East	1.023**	0.232	0.386**	0.117
Minority government	West	0.135	0.334	-0.391	0.221
	East	3.158**	0.443	1.076	0.603
Vote share gov. party	West	0.033	0.018	-0.023**	0.009
	East	0.075**	0.020	0.022	0.011
Pre-election year	West	0.103	0.052	0.062	0.065
	East	-0.097	0.187	-0.101	0.173
Election year	West	0.070	0.062	0.037	0.046
	East	-0.194	0.124	0.155	0.141
MoF from different party	West	---	---	---	---
	East	0.075	0.236	0.424	0.246
<b>Leader variables</b>					
PM change	West	-0.026	0.090	-0.084	0.058
	East	-0.136	0.188	-0.440	0.249
Outside PM	West	0.502**	0.160	0.369*	0.175
	East	0.242	0.340	0.449*	0.213
Union member	West	-0.094	0.085	0.050	0.072
	East	---	---	---	---
Age	West	0.001	0.006	-0.003	0.007
	East	0.051*	0.022	0.033	0.026
Years in office	West	-0.002	0.009	-0.011	0.006
	East	-0.105**	0.023	-0.087*	0.041
Parental status	West	-1.687**	0.511	-1.066**	0.341
	East	-3.709	2.287	-5.179*	2.039
Status advancement	West	-1.585**	0.555	-0.870*	0.376
	East	-4.931	2.654	-6.618**	2.368
R <sup>2</sup> (without state and time fixed effects)		0.909		0.778	
Observations		277		277	
Parameters		69		69	

Notes: Results are based on a least squares dummy variable (LSDV) estimation. The models include cross-section and time fixed effects. Panel robust standard errors are reported. \* and \*\* indicate significance at the 5% and 1% level, respectively.

Table A5: Controlling for Different Government Compositions

Variables	Public Expenditures/GDP		Net Borrowing/GDP	
	Coefficient	Stand. error	Coefficient	Stand. error
Y (-1)	0.723**	0.054	0.520**	0.117
<b>Economic variables</b>				
Debt-to-GDP-ratio (-1)	-0.056**	0.018	-0.081**	0.013
GDP growth	-0.074**	0.028	0.022	0.034
Unemployment rate	0.040	0.038	0.074**	0.027
Transfers/GDP	0.304	0.222	-0.193	0.116
<b>Political variables</b>				
CDU	Reference		Reference	
CDU/SPD	0.341	0.181	-0.091	0.135
CDU/FDP	0.313*	0.138	0.022	0.093
SPD	-0.090	0.112	-0.095	0.101
SPD/CDU	-0.166	0.337	-0.083	0.226
SPD/GREEN	0.089	0.157	-0.044	0.127
SPD/LEFT	0.053	0.234	-0.035	0.155
SPD/FDP	-0.107	0.155	-0.155	0.164
SPD/FDP/GREEN	0.526	0.408	0.766*	0.295
Minority government	0.723*	0.279	0.022	0.145
Vote share gov. party	0.034*	0.016	-0.001	0.010
Pre-election year	0.074	0.066	0.032	0.055
Election year	-0.008	0.059	0.078	0.049
MoF from different party	0.355	0.223	0.301*	0.136
<b>Leader variables</b>				
PM change	0.000	0.076	-0.160	0.106
Outside PM	0.187	0.125	0.330**	0.097
Union member	0.009	0.148	0.089	0.097
Age	-0.005	0.007	0.003	0.005
Years in office	-0.002	0.010	-0.021**	0.006
Parental status	-1.316*	0.505	-1.106**	0.327
Status advancement	-1.417*	0.551	-1.096**	0.355
R <sup>2</sup> (without state and time fixed effects)	0.901		0.770	
Observations	277		277	
Parameters	61		61	

Notes: Results are based on a least squares dummy variable (LSDV) estimation. The models include cross-section and time fixed effects. Panel robust standard errors are reported. \* and \*\* indicate significance at the 5% and 1% level, respectively.

Table A6: Measuring Status by SIOPS

Variables	Public Expenditures/GDP		Net Borrowing/GDP	
	Coefficient	Stand. error	Coefficient	Stand. error
Y (-1)	0.763**	0.049	0.553**	0.093
<b>Economic variables</b>				
Debt-to-GDP-ratio (-1)	-0.059**	0.015	-0.085**	0.014
GDP growth	-0.085**	0.026	0.024	0.030
Unemployment rate	0.038	0.028	0.074**	0.023
Transfers/GDP	0.341	0.220	-0.231*	0.117
<b>Political variables</b>				
SPD-led government	-0.171*	0.086	-0.014	0.088
Coalition	0.219	0.131	-0.006	0.086
Minority government	0.620	0.334	0.019	0.155
Vote share gov. party	0.039**	0.013	0.000	0.008
Pre-election year	0.072	0.065	0.038	0.054
Election year	0.001	0.057	0.088	0.047
MoF from different party	0.239	0.190	0.194	0.124
<b>Leader variables</b>				
PM change	-0.021	0.070	-0.186	0.101
Outside PM	0.144	0.165	0.285*	0.118
Union member	-0.040	0.085	0.036	0.055
Age	0.000	0.007	0.007	0.005
Years in office	-0.003	0.011	-0.022**	0.007
Parental status (SIOPS)	-1.691**	0.560	-1.359**	0.420
Status advancement (SIOPS)	-1.688**	0.562	-1.266**	0.430
R <sup>2</sup> (without state and time fixed effects)	0.898		0.764	
Observations	277		277	
Parameters	55		55	

Notes: Results are based on a least squares dummy variable (LSDV) estimation. The models include cross-section and time fixed effects. Panel robust standard errors are reported. \* and \*\* indicate significance at the 5% and 1% level, respectively.

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