

July 16, 2018

## **Reflections on Politics and Populism: Part I**

The rise of populism and the preference for unconventional leaders are upending the world order that the U.S. created after WWII. Accordingly, across the West, we are seeing a steady rejection of centrist, establishment parties. Here are some of the changes we have observed recently:

**France:** Emmanuel Macron was elected to the presidency last year without previous experience of holding an elected office. He started a new party which now holds the majority in the French National Assembly. His election and new party are clear rejections of the existing establishment parties.

**Germany:** Although Chancellor Merkel continues to hold power, her party, the CDU, had the weakest performance in last year's election since 1949. The SPD, the other party in the "grand coalition," had its worst showing since WWII. The Alternative for Germany (AfD), a populist right-wing party, was the first of its kind to win seats in the Bundestag in the postwar era and is the official opposition.

**Italy:** Voters rejected mainstream parties and elected a coalition consisting of the Five-Star Movement, a left-wing populist party, and the League, a right-wing populist party.

**Mexico:** Lopez Obrador, better known as AMLO, won the election held on July 1. He is the first Mexican president since 1929

who doesn't represent one of the mainstream parties.

**United States:** Donald Trump, who had never held elected office, won the presidency and has been mostly governing as a right-wing populist.

This list isn't exhaustive. Populists are currently governing in Hungary, the Czech Republic, Austria and Poland. It is quite possible that Brazil's October presidential election will give the office to Jair Bolsonaro, who seems to be running as a right-wing populist strongman. In addition, Brexit is a populist movement; if Theresa May's government, which is teetering toward a no-confidence vote, fails, there is a good possibility that a populist left-wing government led by Jeremy Corbyn will emerge.

In the media, there is much consternation about a number of developments, including non-establishment candidates on both the left and right defeating experienced political figures. This report is our attempt to put context around these developments.

In Part I of this report, we will define the terms that we use to describe the political landscape. These definitions will be used to characterize the four major political coalitions and their basic policy positions. Part II will begin with general observations about the effects of class and identity. From there, we will discuss actual historical developments that describe how these four coalitions interact. As always, we will conclude with market ramifications.

### **The Political Landscape**

These four political coalitions, while not perfectly homogenous, are the basic building blocks of the political landscape. In the U.S., and to some extent in the U.K., the major parties are created by forcing groups to cooperate. In multi-party systems, such as in continental Europe, these groups act independently but can establish formal governments. After describing these four coalitions and showing how they have formed in the past, we will use this insight to speculate on how future coalitions may form and how they would affect the economy and financial markets.

### **Definitions**

In this section, we will define our key political terms.

**Group:** A group is a set of like-minded people who tend to support similar political, economic and social positions. We break those down into four areas—identity, class, world openness and regulation outlook. A set of groups makes up the political coalitions we will discuss below.

**Identity:** This term describes the ethnic, racial, sexual orientation (which would include reproductive rights) and religious leanings of a group. Identity also includes age. People within a group will often have multiple “identities.” For example, they may be male, Christian, Hispanic, working age and heterosexual.

**Class:** This term describes the economic position of a group. It is mostly based on income and wealth. Using the previous example, this person may be upper middle class, working age, male, Christian, Hispanic and heterosexual.

**World openness:** There are two areas of openness to the world, people and goods. A

person can favor or oppose immigration. At the same time, a person can favor or oppose free trade. In other words, there is a continuum between being a nationalist or a globalist on trade and immigration.

**Regulation outlook:** Like world openness, views toward regulation exist on two continuums, class and identity. The first class continuum is economic, centering on deregulation to regulation. In terms of class, the distinction is economic freedom or constraint. For example, supporting anti-trust measures, high taxes or unions would favor economic regulation. This area also includes social spending (e.g., Social Security, welfare, disability, unemployment insurance, etc.) Favoring social spending means one favors regulation. The identity continuum is social regulation. Examples here would be positions on affirmative action, gender fluidity, religious freedom, etc.

**Traitor to one’s class:** Marxists believe that class is the key determining factor to political affiliation. Although they acknowledge that identity exists, they believe identity differences should be subsumed to class. A “traitor to one’s class” is someone who is of a given class (usually wealthy and thus establishment) but favors policies of the populists. However, it is possible for a perceived populist to govern as an establishment figure.<sup>1</sup>

### **The Coalitions**

**Right-Wing Establishment (RWE):** The RWE is one of our four political coalitions. Although this coalition has groups that can span all religious, ethnic, age and racial identities, the most likely identifiers would be Caucasian, older and Christian. In terms of class, this coalition tends to be wealthy.

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<sup>1</sup> Our contention is that President Obama was an example of this type of figure.

RWE members tend to be very open to trade and immigration. In terms of regulation, they tend to favor low levels of economic regulation including restrained social spending but would favor a restrictive social regulatory environment.

**Left-Wing Establishment (LWE):** The second of our four political coalitions also includes groups representing a variety of religious, ethnic, age and racial identities and would also be most represented by older Christian Caucasians. In terms of class, this coalition also tends to be wealthy as well as globally open to trade and immigration. In terms of regulation, they tend to favor moderate levels of economic regulation with greater support for social spending compared to the RWE and a less restrictive social regulatory environment, compared to the RWE.

**Right-Wing Populist (RWP):** The third of our four political coalitions can include groups of different religions, ethnicities, ages and racial identities but, in general, this coalition is older Christian Caucasians. In terms of class, this coalition is mostly middle to lower class. Members of this coalition tend to be closed to the world on both continuums, opposing trade and immigration. On regulation, they are skeptical of government but favor universal, as opposed to means-tested, social spending and regulation. They tend to support regulation that protects jobs, including private sector unions but oppose affirmative action, which they view as a means-tested benefit. This coalition favors a restrictive social regulatory environment.

**Left-Wing Populist (LWP):** The LWP is the last of the primary coalitions. This coalition includes groups of the broadest identities. It would not necessarily have any common racial, religious, age or sexual

orientation and tends to be the youngest of the coalitions. This coalition is mostly middle to lower class. In terms of world orientation, it is divided; it tends to oppose trade but favor immigration. It generally prefers all types of regulation on economic activity and supports both universal and means-tested governmental economic support. The LWP tends to support group and minority rights.

### Coalitions as Archetypes

It is important to remember that the four coalitions are archetypes. Very few individuals completely fit any one of the four. Libertarians, for example, would tend to fall into the RWE category based on their positions on regulation, social spending and trade but would be LWP on openness to immigration and social tolerance. A small businessman may fall most closely into the RWP coalition but, due to his business interests, favor free trade. Or, a Christian in a minority group may have an affinity for most LWP positions but support restrictions on reproductive rights. Thus, it's important to understand that if the definitions were a set of Cartesian coordinate planes, few of us would fit perfectly on the axis lines.

However, the votes we make and the positions we adopt become a sort of "revealed preference." In other words, we may say we support certain positions but who we vote for does tend to show what we most value in terms of the definitional spectrum, as described above. For example, a pro-life candidate who holds mostly LWP views may be attractive to an RWP. If they voted for this candidate, it would suggest that reproductive issues were more important than other issues relative to other available candidates.

**Part II**

Next week, we will conclude this report with observations on how the coalitions interact, discuss the “natural” pairings of the

coalitions and examine historical examples. We will conclude with market ramifications.

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