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The fragility of the partisan inflation gap: Evidence from the United Kingdom

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Abstract

Partisan theory predicts that left-leaning governments tolerate higher inflation, and UK data appear to confirm it. Before 1997, inflation averaged three percentage points higher under Labour than the Conservatives. I show this gap is not robust. It is the product of a single Labour government (1974-79) that coincided with the OPEC oil shocks; a randomisation test at the level of governments returns $p = 0.50$, and omitting any one of nine governments can swing the gap by up to four points. With so few in the sample, the data cannot sustain the partisan effect they appear to show.

JEL classification: C12; C22; E31; E58; D72

Keywords: Central bank independence; Inflation; Partisan politics; Small-sample inference; United Kingdom

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1. Introduction

A long tradition holds that the party in office shapes macroeconomic outcomes. Hibbs (1977) argued that left-leaning governments, weighting unemployment more heavily than inflation, run systematically more expansionary policy and therefore higher inflation; his evidence included Great Britain, where Labour governments drove unemployment down, with higher inflation the corresponding side of the trade-off. Alesina (1987) refined this argument into a rational-partisan account operating through inflation surprises early in a term, and a substantial empirical literature has since reported the predicted partisan effects on inflation, in OECD panels (Alesina and Roubini, 1992; Alesina et al., 1997; Potrafke, 2012, 2017) and in the United States (Verstyuk, 2004).

The question has recently regained prominence. The 2021-23 surge took British inflation to a 40-year high, renewing attention to an old assumption - that the left, as is commonly supposed, presides over higher inflation than the right. The belief is long-standing and frequently asserted, yet it has rarely been tested against the British record. This paper asks whether that record supports it.

Britain offers a clean test. Two parties have mainly alternated in single-party government over the past seven decades, the executive controls the legislature, and - until 1997 - the executive also controlled monetary policy, so any partisan tilt in policy preferences had a direct channel to inflation. The partisan growth question has already been settled for the UK, with no significant gap (Algarhi and Tziamalīs, 2021), which leaves inflation as the open case. At first glance, the data support the belief. Over 1948-1997, year-on-year retail price inflation averaged 8.6% under Labour governments and 5.6% under the Conservatives, a gap of three percentage points that is large relative to the sample mean and consistent with the sign that partisan theory predicts. The question is not merely historical. With the post-1997 independence settlement now under renewed political scrutiny, whether the party in office ever systematically shaped inflation bears directly on what is at stake in revisiting that arrangement.

This paper shows that the apparent gap is an artefact. The difficulty is one that Blinder and Watson (2016) emphasise but that much of the partisan literature sidesteps: the effective sample is not the number of quarters but the number of governments. Britain has had nine governments since 1948, not the 311 quarterly observations that a naïve regression appears to

exploit. Moreover, inflation is highly persistent, so adjacent quarters carry overlapping rather than independent information. Once inference is conducted at the level of governments, the partisan inflation gap dissolves. It fails a randomisation test ($p = 0.50$); it is driven entirely by the 1974-79 Wilson-Callaghan Labour government, which governed through the first oil shock, the secondary-banking crisis and the IMF intervention; and at the government level it is statistically indistinguishable from zero. An equivalence test shows that single-country data cannot even rule out a partisan gap of moderate size in either direction.

The contribution is twofold. First, I show that an apparent partisan inflation gap can be the imprint of a single government coinciding with a global shock, rather than evidence of a partisan mechanism. Second, the result is a cautionary one for the wider literature: where partisan macroeconomic comparisons rest on a handful of governments, conventional standard errors overstate precision, and panel estimates dominated by the inflationary 1970s may be capturing the same coincidental clustering of left governments with global shocks. The problem is not peculiar to the UK. Most countries have had only a dozen or so post-war governments, so a single inflationary episode - almost always the 1970s - can dominate the comparison. When that episode falls under a government of one colour, as under Labour in Britain or the Republicans in the United States, the apparent partisan gap reflects the timing of an external shock, not the preferences of a party. My central results rest on distribution-free procedures - a randomisation test and a leave-one-out check - so the conclusion does not depend on functional-form or distributional assumptions.

2. Data

The sample is quarterly and covers the UK from 1948:Q3 to 2026:Q1 (311 observations). The dependent variable is the year-on-year change in the all-items Retail Prices Index (RPI), computed on quarterly averages of the monthly index and obtained from the ONS.

To capture the partisan divide I construct a dummy variable equal to 1 when the Labour Party is in office and 0 when the Conservative Party is in office, assigning each quarter to the party that held office for its majority and treating each continuous single-party spell as one government. The Labour Party is conventionally regarded as centre-left and the Conservative Party as centre-right. This yields nine governments over the sample period: five Labour (Attlee; Wilson; Wilson-Callaghan; Blair-Brown; Starmer) and four Conservative (Churchill-

Douglas-Home; Heath; Thatcher-Major; Cameron-Sunak). The UK experienced one coalition government over the period, in 2010-2015, which I assign to its senior partner, the Conservative Party. A second dummy equals 1 from 1997:Q2 onward, when the Bank of England was granted operational independence, and 0 otherwise. Throughout, inference treats the number of governments, not the number of quarters, as the effective sample.

The robustness analysis uses two controls. The first is the sterling price of crude oil (Hamilton, 2003), constructed as the US-dollar crude price (World Bank) multiplied by the sterling-dollar exchange rate in pounds per dollar (FRED) and entered as a year-on-year change; the second is real GDP growth, measured as the four-quarter change in chained-volume GDP (ONS).

3. Results

3.1. *The apparent gap and its fragility*

Panel A of Table 1 reports the partisan inflation gap. Before 1997 it is +3.02 points; over the full sample it is a negligible +0.47 points, consistent with the absence of a partisan growth gap found for the UK by Algarhi and Tziamalis (2021). Importantly, even the pre-1997 gap is not significant once standard errors account for the data structure. Newey-West standard errors with eight lags give a t -ratio of 1.2; clustering by government raises the standard error further and gives $t = 0.8$. Neither approaches conventional significance.

Three further tests show the gap is not merely imprecise but fragile. First, a randomisation test reassigns the Labour and Conservative labels across the six pre-1997 governments (three Labour, three Conservative), and recomputes the quarter-weighted gap for each of the twenty relabellings that preserve this split. This traces out the exact finite-sample distribution of the gap under the null hypothesis that party and inflation are independent, and it requires no distributional assumptions and no asymptotics. The observed gap of 3.02 points is matched or exceeded in ten of the twenty relabellings, giving $p = 0.50$: the gap is no more extreme than a chance assignment of party to government would routinely produce.

Second, the leave-one-government-out exercise in Panel B traces the gap to a single government. Against the 3.02-point baseline, no other government changes the sign of the

gap; omitting the 1974-79 Wilson-Callaghan government flips it to -1.10 points. That government presided over the OPEC price shocks, when UK inflation peaked above 26%. The gap is not a partisan regularity - it is the 1970s, which happened to fall under Labour.

Third, treating each government as a single observation - the honest effective sample (Ibragimov and Müller, 2010) - the difference in mean inflation between the five Labour and four Conservative governments is 0.63 points, with a Welch t -ratio of 0.23 ($p = 0.82$).

This last result invites the obvious objection that the gap is insignificant only because nine observations cannot reject anything. A two-one-sided-tests (TOST) equivalence procedure (Lakens et al., 2018) addresses it directly by asking not whether the gap differs from zero but whether it can be bounded away from economically meaningful values. It cannot: the data fail to reject a partisan gap as large as ± 3 points ($p = 0.21$). The finding is therefore symmetric. Single-country inference can neither establish a partisan inflation gap nor rule out an economically large one, because the information in a national time series is governed by the few times the country has changed government, not by the frequency at which inflation is sampled. The appearance of precision in some single-country results comes from treating quarters as independent draws.

Table 1. The UK partisan inflation gap, 1948Q3-2026Q1

Panel A. Mean year-on-year RPI inflation by party (%)						
	Labour	Conservative	Gap (L-C)	HAC s.e.	Clu. s.e.	N
Pre-1997	8.62	5.60	3.02	(2.46)	[3.76]	195
Post-1997	2.79	4.10	-1.31	(1.01)	[0.22]	116
Full sample	5.63	5.16	0.47	(1.50)	[2.54]	311
Panel B. Pre-1997 gap, omitting one government at a time (%)						
Gov omitted	Attlee	Churchill-DH	Wilson	Heath	Wilson-Callaghan	Thatcher-Major
Gap (L-C)	4.20	1.83	5.98	3.40	-1.10	3.88

Notes: Year-on-year RPI inflation, quarterly. The gap is the difference in mean inflation between Labour and Conservative governments. HAC standard errors (parentheses) are Newey–West with eight lags; cluster standard errors (brackets) cluster by government. The post-1997 cluster standard error rests on three governments and is not informative. Randomisation test of the pre-1997 gap, permuting party labels across the six pre-1997 governments: $p = 0.50$. Government-level gap (effective $N = 9$ governments): 0.63 (Welch $t = 0.23$; $p = 0.82$). In Panel B, only omitting the 1974–79 government changes the sign of the gap (baseline 3.02, Panel A).

3.2. Robustness

The finding is robust across specifications: in each case the pre-1997 gap stays positive but insignificant. Point estimates are reported with Newey-West p -values in parentheses. Controlling for the sterling-oil price leaves the gap at 3.3 (0.24) while the oil term is strongly significant ($p < 0.001$), confirming that a linear oil control cannot absorb the 1974-79 regime even though oil clearly matters for inflation. Adding a real-GDP-growth cyclical control gives 3.6 (0.16), so the gap is not a by-product of differing cyclical conditions across parties. Charging the first quarter of each government to its predecessor, a one-quarter attribution lag, gives 3.1 (0.19); moving the break to 1998Q2 gives 2.7 (0.25); beginning the sample in 1955 to exclude the immediate post-war years of rationing and the 1949 devaluation gives 4.2 (0.16); and using annualised quarter-on-quarter rather than year-on-year inflation gives 2.9 (0.18). The randomisation and leave-one-government-out results are invariant to all of these choices: in every case the pre-1997 gap collapses once the 1974-79 government is removed.

3.3. Inflation by government

Figure 1 places the result in context. Before 1997, mean inflation across governments ranged from 3.6% to 16%, with wide within-government dispersion. After 1997 the three governments - Labour and Conservative alike - cluster between 2.7% and 4.1% with far smaller dispersion. The standard deviation of mean inflation across governments falls from 4.65 points before 1997 to 0.78 after, and the volatility of inflation within governments falls comparably. Whatever distinguished governments before independence, by party or by the global shocks they faced, the cross-government variation in inflation collapsed once monetary policy was delegated to an independent central bank. The partisan question became moot, in other words, not because the parties converged in their stated preferences but because the institution that determines inflation ceased to be the government of the day.

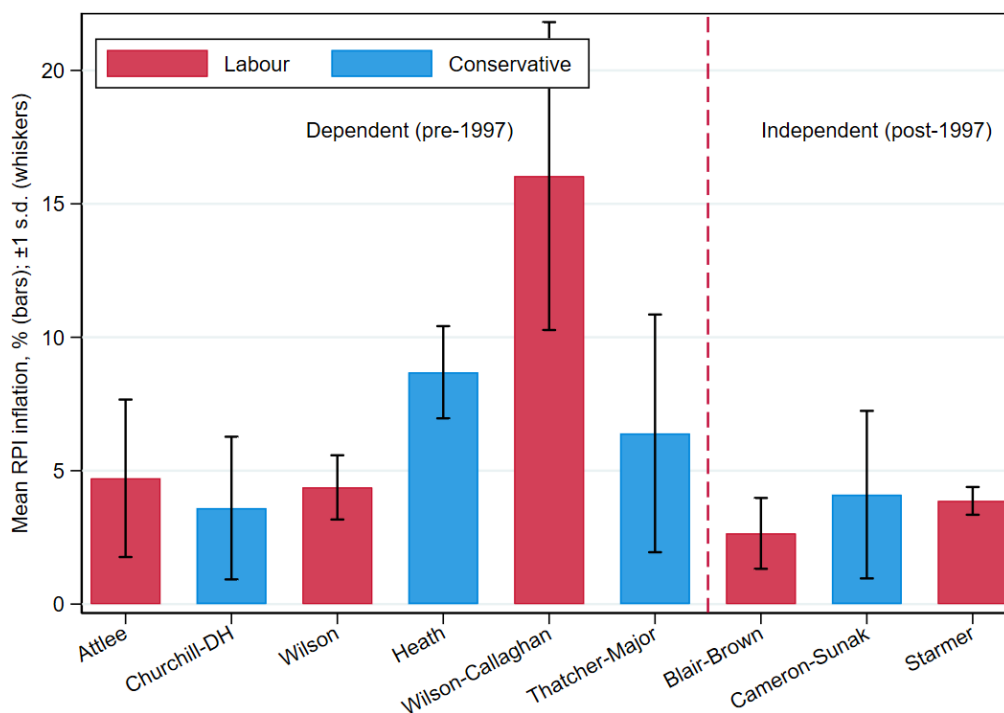


Fig. 1. Mean RPI inflation under each UK government, before and after central bank independence

4. Conclusion

The UK partisan inflation gap, large and correctly signed in the raw data, does not survive inference that reflects the small number of governments (cf. Campbell, 2012, for the US). It is the imprint of one government coinciding with a global oil shock, and conventional standard errors that treat quarters as independent create a spurious impression of a partisan effect. With a single country one can neither confirm nor exclude a partisan gap of moderate size; the apparent precision of some single-country results is an illusion of the effective sample. The same caution applies, more subtly, to the cross-country panels: if a common episode such as the 1970s supplies much of the identifying variation and that episode is unevenly distributed across parties, a pooled estimate can register a partisan effect that is really the shock in disguise.

The finding also clarifies why the question changes character after 1997. Once the Bank of England gained operational independence, inflation outcomes converged across governments of both parties, as Figure 1 shows. Whether this convergence reflects the institutional reform, as the delegation and time-inconsistency arguments of Kydland and Prescott (1977) and

Rogoff (1985) would suggest, or the worldwide anchoring of inflation expectations since the 1990s, cannot be settled within one country. Separating the two requires a cross-country panel in which country and time fixed effects absorb common global shocks while the staggered timing of central-bank-independence reforms identifies the partisan effect. That is the natural next step, and the design this paper motivates. What the UK evidence establishes here is narrower but firm: before drawing partisan conclusions from a country's macroeconomic history, one must count its governments, not its quarters.

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