ECON 5403 F – Topics in the Theory of Public Economics
(An Introduction to the Political Economy of Public Finance and Public Policy)

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Course Objectives: This term ECON 5403 will offer an introduction to the study of political economy, with emphasis on the political economy of public finance. In this course, microeconomics, public economics and analytical political theory are combined in the search for a more comprehensive vision of the economic and political forces underlying the structure and evolution of the public sector and the consequences of political institutions for the allocation and distribution of resources. Topics covered include selected aspects of public goods and externalities, the free-rider problem and collective action, the operation of collective choice mechanisms such as pure majority rule, the relationship between the institutions of representative democracy and economic welfare, the modelling of political competition, special interest politics, time consistency, electoral competitiveness, the efficiency of democracy, and other issues. Some attention is paid to the historical evolution of ideas. In addition to foundational issues and the methods used to study them, we will also look carefully at some recent research papers.

Course Requirements: There will be take-home questions to answer at two points over the term (worth 50% of your mark in total), and a project (worth 50%). Due date for the project will be after the last class. Sets of questions will be handed out periodically that review material considered in class. Questions from these sets to be answered and handed in will be assigned periodically (4 questions in total, in 2 sets of 2). The purpose of the project is to help you make the transition from consumers of research to producers of it, as applied to the topic of this course. This project may be completed by a team of 2 students, each of whom will receive the same mark. Please see the description of the project at the end of this outline.

Note: *= a book or reading on reserve.

Reference Textbook:

*Dennis Mueller. Public Choice III. Cambridge University Press. 2003. An excellent overview of the field that is partly a text and partly a reference book. We will not rely only on this book however, and it is not a course text because not enough of it is assigned as required reading. A copy of Mueller's book will be on reserve.

Additional References:

*Allan Drazen. Political Economy in Macroeconomics. Princeton University Press, 2000. (A recent textbook with many useful chapters surveying some of the topics we will cover. Emphasizes applications to macroeconomic policy issues).

Some interesting books:


* William Riker. *The Art of Political Manipulation*. Yale 1986. (Riker calls this the art of heresthetics - something all good politicians know a lot about).


**Some administrative matters:**

**(i) Academic Accommodation**

You may need special arrangements to meet your academic obligations during the term because of disability, pregnancy or religious obligations. Please review the course outline promptly and write to me with any requests for academic accommodation during the first two weeks of class, or as soon as possible after the need for accommodation is known to exist. Students with disabilities requiring academic accommodations in this course must register with the Paul Menton Centre for Students with Disabilities (PMC) for a formal evaluation of disability-related needs. Documented disabilities could include but are not limited to mobility/physical impairments, specific Learning Disabilities (LD), psychiatric/psychological disabilities, sensory disabilities, Attention Deficit Hyperactivity Disorder (ADHD), and chronic medical conditions. Registered PMC students are required to contact the PMC, 613-520-6608, every term to ensure that your Instructor receives your Letter of Accommodation, no later than two weeks before the first assignment is due or the first in-class test/midterm requiring accommodations. You can visit the Equity Services website to view the policies and to obtain more detailed information on academic accommodation at http://carleton.ca/equity/accommodation.

**(ii) University policy on plagiarism:** Please be aware that plagiarism is serious offence at Carleton and should be recognized and avoided. For the university policy, please see https://carleton.ca/registrar/academic-integrity/
Course Outline and Reading List:
Subject to revision. The timetable by week is tentative.

Required reading on Reserve in the library (when marked with a '*'), available online at the library on ARES, or at cuLearn, as indicated. Always check cuLearn first, then online journals and ARES. Some material is found on my website: https://carleton.ca/winer, as indicated

Please let me know right away if anything is missing from the reserve shelves or web sites listed.

NOTE: The reading list may be amended to incorporate recently published or other material. You will be advised well in advance of any changes in the outline, and reminded as to what reading is required.

Important notes on the outline: (i) While the whole outline is lengthy, I have kept the amount of required reading within reasonable bounds. (ii) Note also that we will study only a modest subset of the material listed here, especially in the applications sections. I will keep you well informed as to what material is relevant for the coming week.

Week 1
1. Background to The Political Economy of Public Finance: Economics vs. Politics
   What is 'politics' versus 'economics'. How should we approach the political economy of public finance? Basic issues concerning the direction of contemporary research.

   Lecture notes on economics vs. politics and the nature of political competition. See cuLearn.

   Supplemenatary: Some background reading
   Gary Miller (1997). The Impact of Economics on Political Science. Journal of Economic Literature 35(3), 1173- 1204. (A thoughtful review that touches on many of the ideas that the course covers.)

Week 2
2. From Public Goods to Political Economy
   From the Samuelson condition to the Wicksell-Lindahl solution. Why social planning is not adequate as a basis for understanding why governments do what they do.

   * Robin Boadway and David Wildasgin. Public Economics. 2nd edition. Little Brown 1984. Chapter 4 (the theory of public goods). For some or perhaps most of you, this is a review of standard normative theory.
   OR
Supplementary: the Wicksellian perspective


Weeks 3 and 4

3. The Free Rider Problem and the Evolution of Cooperation

Why people join, or do not join, with others in the pursuit of common goals. The essential free-rider problem in collective action. Introduction to basic non-cooperative game theory, and its use to study the evolution of cooperation in legislative institutions and other applications. The Folk Theorem.

Notes on non-cooperative game theory: backward induction and subgame perfection. To be supplied on cuLearn.

* T. Sandler, Collective Action. Chapter 2 "(Basic themes...". Overlaps with, but emphasizes different issues than Mueller, chp 2.


Applications


Supplementary


Robert Axelrod, The Evolution of Cooperation, Basic Books 1984. (Extension of the study of prisoner's dilemmas to dynamic or repeat play contexts. See especially chapter 4 on local truces in trench warfare of
Weeks 5 and 6


Mechanisms used by groups to allocate resources. The median voter theorem of Black. The instability of pure majority rule and the interaction of voting rules and preferences. Structure-induced equilibrium and the evolution of legislative institutions. Veto Players. Agenda control and other heresthetic manoeuvres. Cybersenate software and exercises

*D. Mueller, Public Choice III. Chapter 5. (A more technical introduction. Don’t focus on proofs unless instructed. Overlaps somewhat with Shepsle and Bonchek, but worth reading for its technical details and its different perspective).
Cybersenate software by J. Godfrey - Software to experiment with voting games. Provided on cuLearn.

Additional Applications:

Supplementary
*M. Hinich and M. Munger. Analytical Politics. Chapter 2: The Spatial Model of Downs and Black; and Chapter 3: Two Dimensions - Elusive Equilibrium. (An alternative to Shepsle and Bonchek.)

Weeks 7, 8 and 9
5. Modelling Representative Democracy When the Allocation of Economic Resources Matters

Models of political equilibria. Anthony Downs formalized as spatial, probabilistic voting. The Representation Theorem and the 'invisible hand' in a democracy. Special interest politics. The time-consistency problem as conflict of interests. Majoritarian (winner take all) and proportional electoral systems.


Additional Applications


Supplementary: Modelling democracy


**Supplementary: The role of governance from various perspectives**


A. Breton. Competitive Governments. 1996. Chapter 4 (On how budgetary processes in congressional and parliamentary systems evolve to control spending.)


W. Pommerehne, "The Empirical Relevance of Comparative Institutional Analysis", European Economic Review 34, 1990, 458-469. (Summarizes empirical work from Switzerland and elsewhere on the importance of direct vs. representative democracy.)

**Weeks 10 and 11**


A closer look at several interesting papers that combine theory and empirics to deal with (i) the consequences of political competitiveness; (ii) redistribution and inequality

(i) political competitiveness:


(ii) redistribution:


**Supplementary**

*A. Drazen. Political Economy in Macroeconomics, Princeton 2000. (Chapter 8 provides a nice survey regarding redistribution.)


Thomas Piketty, Capital in the Twenty-first Century. Harvard University Press, 2014. (Lecture notes briefly introducing his model to be provided. Many reviews and discussions online and in the JEL, etc.)


**Additional Supplementary: Special interest politics**


**Week 12 (If we dont run out of time)**

**10. Is Democracy Efficient?**

We turn briefly to the normative side of political economy, which we have already considered in the context of our study of electoral equilibrium. Interest groups: good or bad for economic efficiency? Is there an invisible hand in a competitive political system? Under what circumstances? What can go wrong? What is a failure in a policy process? How do we think about these matters? Alternative views about whether and how collective choice should be incorporated into the study of public policy, and in the formulation of policy advice


Regarding sources of efficiency: Don Wittman. Why Democracies Produce Efficient Results", Journal of Political Economy 97(6), December 1989, 1395-1424. A rosy picture of democracy. (See also Becker below)


**Applications (the debate in the context of tax policy):**


James Poterba. "Public Finance and Public Choice". *National Tax Journal* 51(2), 391-396. (A different defence of
the traditional approach to policy making).

**Supplementary:**

The following topics are included for your interest – we will not have time to cover them directly.

**Commitment and Contracting over Time in the Presence of Collective Choice**
Dynamic issues, mostly stemming from commitment problems that arise over time. The readings here just scratch the surface of these topics.


**Dictatorship**
Just a taste of recent work on this fascinating topic.

Due date: at the end of the exam period, to me by email or in person.

The research paper is designed to help you to go beyond being merely a consumer of research done by others. It allows you to start from the work of others, but then to propose your own research project that goes beyond what you have read. Combining this paper with an assignment for another course is fine provided you discuss this with me first. The project paper consists of two related parts:

Part I (approximately 6-8 pages double-spaced): This part represents a review of one or two research articles. One or both of the articles may be empirical in nature (review statistical or case study evidence concerning a main hypothesis), or, if you wish, you may deal with theory only. Articles chosen must deal with the same general topic or issue.

You are responsible for choosing the article(s). One of them may be a research article from the readings assigned for the course. The main topic treated in the articles must relate to some aspect of the course material. You may wish to seek my advice in choosing a specific topic and in locating relevant articles. I will suggest topics as we proceed through the term.

Your discussion in Part I should touch on the following:
- main thesis or hypothesis in each article
- analytic techniques used in each article
- type of data used and sources of the data
- main conclusions reached in each article
- how the articles complement and/or contradict each other, and why they do so

It is suggested that you use these or similar headings to organize the first part of your paper.

Copies of articles that are not part of the readings for the course must be attached to the paper when handing it in.

Part II (approximately 6-8 pages, double-spaced): In this part, you develop a research proposal on one aspect of the topic discussed in the two papers reviewed in Part I. You may start from the research design in one of the papers and amend it to make it your own. (This can be done, for example, by changing or extending the theoretical model in some manner; by changing the list of explanatory variables in an empirical analysis, or by changing the time period for which the statistical analysis is carried out.) You must explain why you are proposing these changes in the research design. Alternatively, you may propose your own research design that takes a different approach from the designs used in the two articles. Again, you must justify your design. Your proposal should have the following elements:

1. An hypothesis or clearly formulated economic question that can be investigated with either a theoretical model or empirical data, or both.

2. If you plan to do theory, a discussion of the model that you will use to examine your hypothesis or research question. This discussion should not be a general introduction to methodology. What is required is a discussion of the properties of the model in relation to the research question of interest, including:
   - what general features is it necessary for the model to have in order to deal with this question;
   - the critical aspects of the particular model you are proposing that will play key roles in determining the nature of conclusions. (You may wish to build on ideas from other papers here);
- how the treatment of the points above differ from that in the papers reviewed earlier;
- justification as to why this alternative model structure is well suited to answer your research question, including a discussion of why there is likely to be some interesting 'distance' between your assumptions and your conclusions;
- a time estimate for completing the project (assuming that would devote 15 hours a week to it);
- a brief discussion of how your research project will add to economic knowledge

(2') If you plan to do empirical work, you should discuss:
- the essential or critical aspects of the statistical model that will play key roles in determining the nature of conclusions about the question of interest;
- how your treatment in the points above differs from that in the papers reviewed earlier;
- justification as to why this alternative model structure is well suited to answer your research question;
- the data that will have to be collected for the research project and of the likely sources where they can be found;
- an example of such data (such as a relevant statistical table) and a discussion of how the numbers in the data set relate to the examination of your hypothesis or research question;
- a time estimate for completing the project (assuming that would devote 15 hours a week to it);
- a brief discussion of how your research project will add to knowledge.

It is suggested that you use above headings (or similar ones) in organizing your proposal that correspond to these points.

In designing your research proposal, it is important to be realistic. This means that you must be very clear about the question that you are investigating, the nature of the model used for theoretical work, and the data required for empirical work. It is generally better to choose a narrow topic than a broad one.

**Bibliography**: The paper must have a separate page with proper bibliographic citations of the two articles reviewed and any other articles cited. The bibliography should also include proper entries for the source of the data example in Part II and for the data sources that you plan to use in the proposed research.

**Team Research**: You may combine with another member of the class and turn in a joint paper. If you choose to do this, both authors will receive the same grade. Groups of more than two authors are not allowed.