Chapter Focus

- How large is the government sector, and what are the main activities undertaken by government?
- What are the differences and similarities between market and government actions?
- What insights can economics provide about the behavior of voters, politicians, and bureaucrats? How will their actions affect political outcomes?
- When is democratic representative government most likely to lead to economic efficiency?
- Why will there sometimes be a conflict between winning politics and economic efficiency?
- How does economic organization influence the efficiency of resource use?

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As we have previously discussed, the protection of property rights, evenhanded enforcement of contracts, and provision of a stable monetary environment are vital for the smooth and efficient operation of markets. Governments that perform these functions well will help their citizens prosper and achieve higher levels of income. Governments may also help allocate goods difficult for markets to handle. However, it is crucially important to recognize that government is simply an alternative form of economic organization. In most industrialized nations, the activities of governments are directed by the democratic political process. In this chapter, we will use the tools of economics to analyze how this process works.

THE SIZE AND GROWTH OF THE U.S. GOVERNMENT

What exactly does government do? Has its role in the economy shrunk or grown over time? Data on government spending sheds light on these questions. As Exhibit 1 illustrates, total government expenditures (federal, state, and local combined) were only 9.4 percent of the U.S. economy in 1930. (Note: GDP is generally how economists measure the size of the economy. The term will be explained more fully in a macroeconomics course.) In that year, federal government spending by itself was only 3 percent of the economy. At the time, this made the federal government about half the size of all state and local governments combined.

However, between 1930 and 1980, the size of government grew very rapidly. By 1980, government expenditures had risen to 32.8 percent of the economy, more than three times the level of 1930. Moreover, the federal government grew to about twice the size of all state and local governments combined—despite the fact that they were growing rapidly, too. Over the last two decades, total government spending as a share of the economy has been relatively constant at approximately one-third of GDP.

Exhibit 2 shows the major categories of government spending for both the federal government and state and local governments. The major categories of federal spending are health care, national defense, Social Security, and other income transfers. Education, administration, and public welfare and health constitute the largest areas of spending for state and local governments.

EXHIBIT 1
The Growth of Government Spending between 1930 and 2003

U.S. government expenditures as a share of the economy’s gross domestic product have risen dramatically over the past 70 years.

EXHIBIT 2

Government Spending by Category

The major categories of federal government spending are health care, Social Security, national defense, and income security (welfare programs). The major categories of state and local government spending are education, health care, and welfare programs.

EXHIBIT 3

The Growth of Government Transfer Payments

The government taxes approximately 13 percent of national income away from some people and transfers it to others. Means-tested income transfers—those directed toward the poor—account for only about one-sixth of all income transfers. Government income-transfer activities have grown substantially over the past 70 years.

Transfer payments

Payments to individuals or institutions that are not linked to the current supply of a good or service by the recipient.
1.1 percent of total income. By 1970, the figure had jumped to 7.7 percent, and by 2002 it had risen to 13.4 percent of national income. Obviously, the government has become much more involved in tax-transfer activities during the last several decades.

Given the size and growth of government, analyzing how the political process works and what impact it is likely to have on the economy is a vitally important topic. The remainder of this chapter will address this issue.

THE DIFFERENCES AND SIMILARITIES BETWEEN GOVERNMENTS AND MARKETS

When political decisions are made democratically, the choices of individuals will influence outcomes in the government sector—just as they do in the market sector. Therefore, when we analyze the political process, we focus on individuals and how incentives influence their choices, just as we do when we analyze markets. There are both differences and similarities between political and market decision-making. Let’s take a look at several of them.

1. Competitive behavior is present in both the market and public sectors. The nature of the competition and the criteria for success differ between the two sectors, but people compete in both. Politicians compete for elective office. Bureau chiefs and agency heads compete for taxpayer dollars and the authority to regulate others to meet their bureau or agency goals. Public-sector employees compete for promotions, higher incomes, and additional power, just as they do in the private sector. Lobbyists compete for program funding, for favorable bureaucratic rulings, and for legislation favorable to the interest groups they represent—including both private and government clients. The nature of the competition may differ between the two sectors, but it is present in both. (See Applications in Economics: Perspectives on the Cost of Political Competition.)

2. Public-sector organization can break the individual consumption-payment link. In the market sector, goods are allocated to those who are willing to pay the price: there is

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APPLICATIONS IN ECONOMICS

**Perspectives on the Cost of Political Competition: What Does It Cost to Get Elected?**

Competition for elective office is fierce and campaigns are expensive. For example, in recent years, candidates for U.S. House and Senate positions raised and spent more than $1 billion. This amounts to approximately $2 million per congressional seat! Highly contested seats are often far more expensive.

During and after an election, lobbying groups compete for the attention of elected officials. In fact, the greatest portion of campaign funds raised by incumbents is not raised at election time; rather, it accrues over their entire term in office. A large campaign contribution may not be able to “buy” a vote, but it certainly enhances the lobbyist’s chance to sit down with the elected official to explain the power and “beauty” of the contributor’s position. In the competitive world of politics, the politician who does not at least listen to helpful “friends of the campaign” is less likely to survive.

The U.S. Congress controls approximately $2 trillion in spending annually and imposes regulations that cost another $800 billion. That’s a huge amount of money. As long as Congress wields the power to spend these sums, huge expenditures designed to influence the policies representatives make will continue.1

a one-to-one relationship between a person’s payment and receipt of a good. This is often not the case when decisions are made politically. Sometimes people receive very large benefits from the government even though they do not pay much of the cost to cover them. In other cases, individuals are required to pay dearly for a government program even though they derive few, if any, benefits.

3. **Scarcity imposes the aggregate consumption-payment link in both sectors.** Although the government can break the link between a person’s payment for a good and the right to consume it, the reality of the aggregate consumption—aggregate payment link remains. Resources used by the government have alternative uses. Therefore, it is costly to provide goods and services through the government. This is true even if the good is provided “free of charge” to certain consumers.

4. **Private-sector action is based on mutual agreement; public-sector action is based on majority rule.** In the market sector, when two parties engage in trade, they do so voluntarily. Corporations like General Motors and Microsoft, no matter how large or powerful, cannot take income from you or force you to buy their products. On the other hand, when collective action occurs in a democratic setting, majority rule is the key, either through direct voting or through legislative procedures involving elected representatives. If a legislative majority decides on a particular policy, the minority must accept the policy and help pay for it, even if they strongly disagree. Similarly, if government regulators mandate that private parties must provide a wildlife habitat, wetlands, or housing at below-market prices, for example, both providers and potential buyers must comply. Although market action is based on mutual benefit, government action through the political process generates losers as well as winners.

5. **When collective decisions are made legislatively, voters must choose among candidates who represent a bundle of positions on issues.** On election day, the voter cannot choose the views of one politician on poverty and business welfare and simultaneously choose the views of a different politician on national defense and tariffs. This greatly limits the voter’s power to make his or her preferences count on specific issues. Since the average representative is asked to vote on roughly 2,000 different issues during a two-year term, the size of the problem is obvious. The situation in markets, however, is quite different. A buyer can purchase some groceries or clothing from one store, while choosing related items from different suppliers. There is seldom a bundle-purchase problem in markets.

6. **Income and power are distributed differently in the two sectors.** People who supply more highly valued resources in the marketplace have larger incomes. The number of these dollar “votes” earned by a person in the marketplace will reflect his or her abilities, ambitions, skills, past savings, inheritance, good fortune, and willingness to produce for others, among other things. Bill Gates is a good example. Many people have “voted” for his products. Consequently, Gates has become quite wealthy. This process results in an unequal distribution of income and power in the market sector.

On the other hand, in a democratic government, one citizen, one vote is the rule. But there are ways other than voting to influence political outcomes. People can donate both their money and their time to help a campaign. They can also try to influence friends and neighbors, write letters to legislators, and speak in public on behalf of a candidate or cause. The greatest rewards of the political process go to those best able and most willing to use their time, persuasive skills, organizational abilities, and financial contributions to help politicians get votes. People who have more money and skills of this sort—and are willing to spend them in the political arena—can expect to benefit more handsomely for themselves and their favorite causes. Thus, while the sources of success and influence differ, there is an unequal distribution of influence and power in both sectors.
Public-choice analysis is a branch of economics that applies the principles and methodology of economics to the operation of the political process. Public-choice analysis links the theory of individual behavior to political action, analyzes the implications of the theory, and tests them against events in the real world. Over the past 50 years, research in this area has greatly enhanced our understanding of political decision-making. Just as economists have used the idea of self-interest to analyze markets, public-choice economists use it to analyze political choices and the operation of government. After all, the same people make decisions in both sectors. If self-interest and the structure of incentives influence market choices, there is good reason to expect that they will also influence choices in a political setting.

The collective decision-making process can be thought of as a complex interaction among voters, legislators, and bureaucrats. Voters elect a legislature, which levies taxes and allocates budgets to various government agencies and bureaus. The bureaucrats in charge of these agencies utilize the funds to supply government services and income transfers. In a representative democracy, voter support determines who is elected to the legislature. A majority vote of the legislature is generally required for the passage of taxes, budget allocations, and regulatory activities. Let’s take a closer look at the incentive structure confronting the three primary political players—voters, legislators, and bureaucrats—and consider how they affect the operation of the political process.

The contributions of Kenneth Arrow, James Buchanan, Duncan Black, Anthony Downs, Mancur Olson, Robert Tollison, and Gordon Tullock have been particularly important. Public choice is something of a cross between economics and political science. Thus, advanced courses are generally offered in both departments.
Incentives Confronted by the Voter

How do voters decide whom to support? Self-interest dictates that voters, like market consumers, will ask, “What can you do for me and my goals, and how much will it cost me?” The greater the voter’s perceived net personal gain from a particular candidate’s election, the more likely it is that the voter will favor that candidate. In contrast, the greater the perceived net economic cost imposed on the voter by the positions of a candidate, the less inclined the voter will be to support the candidate. Other things equal, voters will tend to support those candidates whom they believe will provide them the most government services and transfer benefits, net of personal costs.

How well will voters be informed about political issues and candidates? When decisions are made collectively, the choices of a single person will not be decisive. The probability that an individual vote will decide a city, state, or national election is virtually zero. Realizing that their votes will not affect the outcome, individual voters have little incentive to spend much effort seeking the information needed to cast an informed ballot. Economists refer to this lack of incentive as the rational ignorance effect.

As the result of the rational ignorance effect, most voters simply rely on information supplied to them freely by candidates (via political advertising) and the mass media, as well as conversations with friends and coworkers. Surveys, in fact, indicate that huge numbers of voters are unable to even identify their own congressional representatives, much less know where they stand on issues like Social Security reform, tariffs, and agricultural price supports. Given that voters gain little from casting a more informed vote, their meager knowledge of political candidates and issues is not surprising.

On the other hand, when people can put information to good use, they will put forth the effort to acquire it. Consider the incentive of an automobile purchaser to make a well-informed choice. The model, the dealer, and the financial terms are a matter of personal preference. If a bad choice is made, the individual consumer will bear the consequences. As a result, auto consumers have a strong incentive to make informed decisions. Thus, they often take different models for test drives, review consumer publications, and consult with various car experts about them. On the other hand, the voter gains little or nothing in terms of a changed result from a more informed political choice. Because the person is not in a position to decide the outcome of an election, if he or she makes a mistake by casting an uninformed ballot, it won’t make much difference. Thus, it is actually reasonable to expect people to be far better informed when choosing a car than a senate, congressional, or other political candidate.

The fact that citizens realize their individual votes will not sway the outcome of an election also explains why so many of them don’t vote. Even in a presidential election,

James Buchanan is a key figure in the development of public-choice theory. Buchanan’s most famous work, *The Calculus of Consent* (1962), coauthored with Gordon Tullock, argues that unless constitutional rules are structured in a manner that will bring the self-interests of the political players into harmony with the wise use of resources, government action will often be counterproductive. This related contributions won him the 1986 Nobel Prize in economics. Buchanan is the founder of the Center for the Study of Public Choice and a longtime professor of economics at George Mason University.

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only about half of all voting-age Americans take the time to register and vote. The turnout for state and local elections is generally still lower. Given the low probability that one’s vote will be decisive, low voter turn-out is an expected result.

**Incentives Confronted by the Politician**

What motivates political candidates and officeholders? Economics indicates that the pursuit of votes will primarily shape politicians’ actions and political positions. No doubt, many of them genuinely care about the “public interest” and the quality of government, but they need to get elected to achieve their objectives, whatever they might be. To be successful, a candidate’s positive attributes must be brought to the attention of rationally ignorant voters focused on their families, jobs, various civic activities, and local sports teams (which are probably more entertaining). The successful candidate needs an expert staff, sophisticated polling techniques to uncover popular issues and positions, and high-quality advertising to favorably shape his or her image. This, of course, will be costly. It is not unusual for an incumbent candidate to the U.S. Senate to spend more than $15 million or more to get reelected. In other words, votes are the ultimate objective of politicians, but money helps them get those votes. Predictably, the pursuit of campaign contributions therefore shapes the actions of politicians, too.

Are we implying that politicians are selfish, caring only for their pocketbooks and re-election chances? The answer is “No.” Factors other than personal political gain, narrowly defined, may well influence their actions. Sometimes an elected official may feel so strongly about an issue that he or she will knowingly take a position that is politically unpopular and damaging to his or her future electoral prospects. None of this is inconsistent with the economic view of the political process we just described. Over time, however, the politicians most likely to remain in office are the ones who focus on how their actions will influence their reelection prospects. Just as profits are the lifeblood of the market entrepreneur, votes are the lifeblood of the politician.

Politicians face competition for elected office from other candidates. Just like market suppliers, political suppliers have an incentive to find ways to gain an advantage over their competitors. Catering to the views of voters and contributors is one way of doing that. Enacting rules that put potential challengers at a disadvantage is another. When geographic political districts are redrawn, for example, politicians frequently manipulate the process to increase their chances of reelection—a process known as “gerrymandering.” Incumbents can also attempt to use government resources for their reelection campaigns, an advantage challengers do not have. Campaign finance “reforms” that make it more difficult for a challenger to raise funds may also provide incumbents with an additional advantage.

**Incentives Confronted by the Government Bureaucrat**

Like other people, bureaucrats who staff government agencies have narrowly focused interests. They usually want to see their own agency’s goals furthered. Many bureaucrats believe strongly in what they are trying to do. Furthering these goals, however, usually requires larger budgets. In turn, larger budgets lead to more prestige and career opportunities for the bureaucrats. *Economic analysis suggests there is a strong tendency for government bureaucrats and employees to want to expand their budgets to sizes well beyond what is economically efficient.*

Legislative bodies are in charge of overseeing these bureaus, but the individual legislators themselves are generally not very knowledgeable about the true costs of running these agencies. This makes it even more likely that bureaucrats will be able to get funding beyond what’s economically efficient.

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4The economic analysis of bureaucracy was pioneered by William Niskanen. Reprints of some of his classic articles along with recent updated material can be found in William A. Niskanen, Jr., *Bureaucracy and Public Economics* (Aldershot, U.K.: Edward Elgar Publishing, 1994).
The political process, which begins with voter-driven elections and proceeds to legislative decisions and bureaucratic actions, brings about results that please some voters and displease others. The goals of the three major categories of participants—voters, politicians, and bureaucrats—frequently conflict with one another. Each group wants more of the government’s limited supply of resources. Coalitions form and the members of each coalition hope to enhance their ability to get the government to do what they want. Sometimes this results in productive activities on the part of the government, and sometime it does not.

WHEN THE POLITICAL PROCESS WORKS WELL

Under what conditions are voting and representative government most likely to result in productive actions? People have a tendency to believe that support by a majority makes a political action productive. However, if a government project is truly productive, it will always be possible to find a way to allocate the cost so that all voters gain. This would mean that, even if voting rules required unanimity or near-unanimity, all truly productive government projects would pass if the costs were allocated in the right manner. Exhibit 4 helps illustrate this point. Column 1 presents hypothetical data on the distribution of benefits from a government road construction project. These benefits sum to $40, which exceeds the $25 cost of the road, so the project is productive. But if the project’s $25 cost were allocated equally among the voters (plan A), Adams and Chan gain substantially, but Green, Lee, and Diaz lose. If the fate of the project is decided by majority vote, the project will be defeated by the “no” votes of Green, Lee, and Diaz. The reason this productive government project fails to obtain a majority vote, however, is because of the way that the costs have been allocated.

<table>
<thead>
<tr>
<th>VOTER</th>
<th>BENEFITS RECEIVED</th>
<th>PLAN A</th>
<th>PLAN B</th>
</tr>
</thead>
<tbody>
<tr>
<td>Adams</td>
<td>$20</td>
<td>$5</td>
<td>$12.50</td>
</tr>
<tr>
<td>Chan</td>
<td>12</td>
<td>5</td>
<td>7.50</td>
</tr>
<tr>
<td>Green</td>
<td>4</td>
<td>5</td>
<td>2.50</td>
</tr>
<tr>
<td>Lee</td>
<td>2</td>
<td>5</td>
<td>1.25</td>
</tr>
<tr>
<td>Diaz</td>
<td>2</td>
<td>5</td>
<td>1.25</td>
</tr>
<tr>
<td>Total</td>
<td>$40</td>
<td>$25</td>
<td>$25.00</td>
</tr>
</tbody>
</table>

When taxes are levied in proportion to benefits received (tax plan B), any efficient project can pass unanimously (and any inefficient project will fail unanimously). When taxes are not levied in accordance with benefits received (tax plan A), efficient projects can fail to win a majority vote (or inefficient projects can pass in a majority vote).
Because the project is indeed productive, there is an alternate way to allocate its costs so that Adams, Chan, Green, Lee, and Diaz all benefit. This can be accomplished by allocating the cost of the project among voters in proportion to the benefits that they receive (plan B). Under this arrangement, Adams would pay half ($12.50) of the $25 cost, since he receives half ($20) of the total benefits ($40). The other voters would all pay in proportion to the benefits they receive. Under this plan, all voters would gain from the proposal. Even though the proposal could not secure a majority when the costs were allocated equally among voters, it will be favored by all five voters when they are taxed in proportion to the benefits they receive (plan B).

This simple illustration highlights an extremely important point about voting and the efficiency of government action. When voters pay in proportion to benefits received, all voters will gain if the government action is productive, and all will lose if it is unproductive. When the benefits and costs derived by individual voters are closely related, the voting process will enact efficient projects while rejecting inefficient ones. When voters pay in proportion to the benefits they receive, there will tend to be harmony between good politics and sound economics.

How might the cost of a government service be linked to the benefits received? User charges, which require people who use a service more to pay a larger share of the cost, provide one way. User charges are most likely to be levied at the local level. Local services such as electricity, water, and garbage collection are generally financed with user charges. Sometimes the intensity of the use of a service and the amount paid for it can be linked by specifying that the revenue from a specific tax be used for a designated purpose. For example, most states finance road construction and maintenance with the revenue collected from taxes on gasoline and other motor fuels. The more an individual drives, the more he or she benefits from the roads—and the more he or she pays.

Exhibit 5 provides a useful way to look at the possible linkage between the benefits and costs of government programs. The benefits from a government action may be either widespread among the general public or concentrated among a small subgroup (for example, farmers, students, business interests, senior citizens, or members of a labor union). Similarly, the costs may be either widespread or highly concentrated among voters. Thus, as the exhibit shows, there are four possible patterns of voter benefits and costs: (1) widespread benefits and widespread costs, (2) concentrated benefits and widespread costs, (3) concentrated benefits and concentrated costs, and (4) widespread benefits and concentrated costs.

When both the benefits and costs are widespread among voters (type 1 issue), essentially everyone benefits and everyone pays. Although the costs of type 1 measures may not be precisely proportional to the benefits individuals receive, there will be a rough relationship. When type 1 measures are productive, almost everyone gains more than they pay. There will be little opposition, and political representatives have a strong incentive to support such proposals. In contrast, when type 1 proposals generate costs in excess of benefits, almost everyone loses, and representatives will face pressure to oppose such issues. Thus, for type 1 projects, the political process works pretty well. Productive projects will tend to be accepted and unproductive ones rejected.

Similarly, there is reason to believe that the political process will work fairly well for type 3 measures—those for which both benefits and costs are concentrated on one or more small subgroups. In some cases, the concentrated beneficiaries may be the same group of people paying for the government to provide them a service. In other cases, the subgroup of beneficiaries may differ from the subgroup footing the bill. Even in this case, however, when the benefits exceed the costs, the concentrated group of beneficiaries will have an incentive to expend more resources lobbying for the measure than necessary to ensure its passage.

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User charges

Payments that users (consumers) are required to make if they want to receive certain services provided by the government.

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Note: The principle that productive projects generate the potential for political unanimity was initially articulated by Swedish economist Knut Wicksell in 1896. See Wicksell, “A New Principle of Just Taxation,” in Public Choice and Constitutional Economics, James Gwartney and Richard Wagner (Greenwich, Ct.: JAI Press, Inc., 1988). Nobel laureate James Buchanan has stated that Wicksell’s work provided him with the insights that led to his large role in the development of modern public-choice theory.
Those harmed by it will expend opposing it. Thus, when the benefits and costs are both concentrated, there will be a tendency for productive projects to be adopted and unproductive ones to be rejected.

**WHEN THE POLITICAL PROCESS WORKS POORLY**

Although the political process yields reasonable results when there is a close relationship between the receipt of benefits and the payment of costs (type 1 and type 3 projects), the harmony between good politics and sound economics breaks down when there is not (type 2 and type 4 projects). Inefficiency may also arise from other sources when governments undertake economic activities. In this section, we consider four major reasons why the political allocation of resources will often result in inefficiency.

**Special-Interest Effect**

Trade restrictions that limit the import of steel and lumber from abroad; subsidies for sports stadiums, the arts, and various agricultural products; federal spending on an indoor rain forest in Coralville, Iowa; a tattoo-removal program in San Luis Obispo County, California; the Rock and Roll Hall of Fame in Cleveland, Ohio; a golf awareness program in St. Augustine, Florida; and therapeutic horseback riding in Apple Valley, California. These seemingly diverse programs funded by the federal government have one thing in common: They reflect the attractiveness of special interests to vote-seeking politicians. A special-interest issue is one that generates substantial personal benefits for a small number of constituents while spreading the costs widely across the bulk of citizens (type 2 projects). Individually, a few people gain a great deal, but many others lose a small amount. In aggregate, the losses may exceed the benefits.
How will a vote-seeking politician respond to special-interest issues? Since their personal stake is large, members of the interest group (and lobbyists representing their interests) will feel strongly about such issues. Many of the special-interest voters will vote for or against candidates strictly on the basis of whether they are supportive of their positions. In addition, interest groups are generally an attractive source of campaign resources—including financial contributions. In contrast, most other rationally ignorant voters will either not know or will care little about special-interest issues. Even if voters know about some of these programs, it will be difficult for them to punish their legislators because each politician represents a bundle of positions on many different issues. While there is little to be gained from the support of the disorganized majority, organized interest groups provide politicians with vocal supporters, campaign workers, and, most important, financial contributions.

As a result, politicians have a strong incentive to support legislation giving concentrated benefits to special-interest groups at the expense of disorganized groups (like the bulk of taxpayers and consumers). Even if supporting such legislation is counterproductive, politicians will often still be able to gain by supporting programs favored by special interests. For a real-world illustration of how the special-interest effect works, see Applications in Economics, “Sweet Subsidies to Sugar Growers: A Case Study of the Special Interest Effect.”

APPLICATIONS IN ECONOMICS

Sweet Subsidies to Sugar Growers: A Case Study of the Special-Interest Effect

For many years, the price of sugar in the United States has been two or three times as high as the world price. For example, in February 2004, the domestic price of sugar was 20 cents per pound while the world price was less than 6 cents a pound. Why? Because the U.S. government severely restricts the quantity of sugar imported. This keeps the domestic price of sugar high. As a result, the roughly 60,000 sugar growers in the United States gain about $1.9 billion. That’s more than $30,000 per grower! Most of these benefits are reaped by large growers with incomes far above the national average. On the other hand, these subsidies cost the average American household about $20 in the form of higher prices for products containing sugar. Even more important, the resources of Americans are wasted producing a good we are ill-suited to produce and one that could be obtained at a substantially lower cost through trade. As a result, Americans are worse off.

Why does Congress support this program year after year? Given the sizable impact the restrictions have on the personal wealth of sugar growers, it is perfectly sensible for them, particularly the large ones, to use their wealth and political clout to help politicians who support their interests. This is precisely what they have done. During the 2000 election cycle, the sugar lobby contributed almost $13 million to candidates and political action committees. In contrast, it makes no sense for the average voter to investigate this issue or give it any significant weight when deciding for whom to vote. In fact, most voters are unaware that this program is costing them money. Here, as in several other areas, the incentive structure provides politicians with a strong incentive to support policies favored by special interests, solicit those parties for political contributions, and use the funds to attract the support of other voters, most of whom know nothing about the sugar program. Even though the sugar program is counterproductive, it is still a political winner.

The sugar growers are not the only ones benefiting from government programs that are economically inefficient. Taxpayers and consumers spend approximately $20 billion annually to support grain, cotton, tobacco, peanut, wool, and dairy programs, all of which have structural characteristics similar to those of the sugar program. The political power of special interests also explains the presence of tariffs and quotas on steel, textiles, lumber, and many other products. Federally funded irrigation projects, subsidized agricultural grazing rights, subsidized business loans, numerous pork-barrel spending projects (the list goes on and on) are all policies rooted in the special-interest effect rather than economic efficiency and net benefits to Americans. Although each such program individually imposes only a small drag on the economy, together they exert a sizeable negative impact on our income levels and living standards.
Logrolling
The exchange between politicians of political support on one issue for political support on another.

Pork-barrel legislation
A package of spending projects benefiting local areas financed through the federal government. The costs of the projects typically exceed the benefits in total, but the projects are intensely desired by the residents of a particular district who get the benefits without having to pay much of the costs.

The power of special interests is further strengthened by logrolling and pork-barrel legislation. Logrolling involves the practice of trading votes by a politician to get the necessary support to pass desired legislation. Pork-barrel legislation is the term used to describe the bundling of unrelated projects benefiting many interests into a single bill. Both logrolling and pork-barrel legislation will often make it possible for special-interest projects to gain legislative approval, even though these projects themselves are counterproductive and individually would be unable to muster legislative approval.

Exhibit 6 provides a numeric illustration of the forces underlying logrolling and pork-barrel legislation. Here we consider the operation of a five-member legislature considering three projects: construction of a post office in district A, dredging of a harbor in district B, and spending on a military base in district C. For each district, the net benefit or cost is shown—that is the benefit to the district minus the tax cost imposed on it. The total cost of each of the three projects exceeds the benefits (as shown by the negative number in the total row at the bottom of the table), and therefore each is counterproductive. If the projects were voted on separately, each would lose by a 4-to-1 vote because only one district would gain, and the other four would lose. However, when the projects are bundled together through either logrolling (representatives A, B, and C could agree to trade votes) or pork-barrel legislation (all three programs put on the same bill), they can all pass, despite the fact that all are inefficient. When the number of districts (or projects) is large, the cost imposed on voters harmed by the legislation will be small. Given the weak incentive for voters to acquire information, those harmed by pork barrel and other special-interest policies are unlikely to even be aware of them. Thus, the incentive to support projects like these is even stronger than is implied by the simple numeric example in Exhibit 6.

Why don’t representatives oppose measures that force their constituents to pay for projects that benefit others? There is some incentive to do so, but the constituents of any one elected representative can capture only a small portion of the benefits of tax savings from improved efficiency, since the savings would be spread nationwide among all taxpayers. We would not, for example, expect the president of a corporation to devote any of the firm’s resources to projects not primarily benefiting its stockholders. Neither should we expect an elected representative to devote political resources to projects like defeating pork-barrel programs when the benefits of spending reductions and tax savings will be derived mostly by constituents in other districts. Instead, each representative has a strong incentive to work for programs that concentrate benefits among his or her own constituents—especially organized interest groups that can help the representative be reelected. Heeding such incentives is a survival (reelection) tactic.

<table>
<thead>
<tr>
<th>VOTERS OF DISTRICT</th>
<th>CONSTRUCTION OF POST OFFICE IN A</th>
<th>DREDGING HARBOR IN B</th>
<th>CONSTRUCTION OF MILITARY BASE IN C</th>
<th>TOTAL</th>
</tr>
</thead>
<tbody>
<tr>
<td>A</td>
<td>+$10</td>
<td>−$ 3</td>
<td>−$ 3</td>
<td>+$4</td>
</tr>
<tr>
<td>B</td>
<td>−$ 3</td>
<td>+$10</td>
<td>−$ 3</td>
<td>+$4</td>
</tr>
<tr>
<td>C</td>
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<td>D</td>
<td>−$ 3</td>
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*We assume the districts are of equal size.

Logrolling and pork-barrel policies can sometimes lead to the adoption of productive measures. However, if a project is productive, there would always be a pattern of finance that would lead to its adoption even if logrolling and pork-barrel policies were absent. Thus, the tendency for logrolling and pork-barrel policies to result in the adoption of inefficient projects is the more significant point.
On the other hand, when the benefits of a government action are widespread and the costs are highly concentrated (type 4 of Exhibit 5), special-interest groups—those who stand to bear the cost—will strongly oppose and lobby against it. Most other voters will be largely uninformed and uninterested. Once again, politicians will have an incentive to respond to the views of the concentrated interests. A proposal to reduce or eliminate a tariff (tax) on an imported good would be an example of this type of legislation. Although many thousands of consumers would benefit from the lower prices that result, the domestic firms that compete with the imported good would devote substantial resources toward lobbying to keep the tariff in place. Projects of this type will tend to be rejected even when they are productive, that is, when they would generate larger benefits than costs.

The bottom line is clear: Public-choice analysis indicates that majority voting and representative democracy work poorly when concentrated interests benefit at the expense of the general public. In the case of special interest issues, there is a conflict between good politics—getting elected—and the efficient use of resources. The special-interest effect helps explain the presence of numerous government programs that increase the size of government and reduce the overall size of the economic pie. As we discuss diverse topics throughout this text, counterproductive political action that has its foundation in the special-interest effect will arise again and again.

**Shortsightedness Effect**

Because voters have a weak incentive to acquire information, current economic conditions will have a major impact on their choices at election time. Complex issues, like reforming Social Security or restructuring health care programs that involve future benefits and costs, will be difficult for voters to assess. Thus, incumbent politicians will want to make sure economic conditions look good on election day. To accomplish this, they will favor policies that provide current benefits voters can easily identify at the expense of future costs that are complicated and difficult to identify. Similarly, they will tend to oppose legislation that involves immediate and easily identifiable costs (and higher taxes) but yield future benefits that are complex and difficult to identify. Economists refer to this bias inherent in the political process as the *shortsightedness effect*.

As a result of the shortsightedness effect, politicians will tend to favor programs that generate highly visible current benefits, even when the true cost of these programs outweighs the benefits. In contrast, their incentive is weak to support efficient programs that generate future benefits but involve current costs.

The shortsightedness effect sheds light on why legislators find debt financing so attractive. Debt financing makes it possible for officeholders to provide visible benefits to their constituents without having to levy an equivalent amount of taxes. During the last 45 years, the federal budget has been in deficit 40 times; there have been only five surpluses (1969 and 1998–2001). The bias toward budget deficits is a predictable result; it reflects the shortsighted nature of the political process. Similarly, the shortsightedness effect indicates that vote-seeking politicians will find it attractive to promise future benefits without levying a sufficient amount of taxes to finance them. This has been the case with both the Social Security and Medicare programs. The unfunded liabilities of these two programs are nearly three times the size of the official outstanding federal debt. By the time the higher taxes (or benefit cuts) for these programs are confronted, the politicians who gained votes from the promised benefits will be long gone.

It is worth taking a moment to consider the differences between the public and private sectors in terms of how future benefits and costs are considered in current decisions. As we explained in Chapter 2, private property rights provide a means by which the value of future benefits can be immediately captured (or costs borne) by a property owner. Owners who do not invest now to properly maintain their homes or cars, for example, will bear the consequences of the reduced value of those assets. Correspondingly, the value of a firm’s stock will immediately rise (or fall), depending on the shareholders’ perception of the expected future benefits and costs of an action taken by the company’s executives today. In contrast, the public sector tends to place more weight on current benefits and costs and
less weight on the future. In areas where the primary benefits are in the future, and property rights can be well defined and enforced, there is good reason to believe that the private sector will do a better job than the government sector.

**Rent-Seeking**

There are two ways individuals can acquire wealth: production and plunder. When individuals produce goods or services and exchange them for income, they not only enrich themselves but they also enhance the wealth of the society. Sometimes the rules—or lack of rule enforcement—also allow people to get ahead by taking, or plundering, what others have produced. This method not only fails to generate additional income—the gain of one is a loss to another—but it also consumes resources and thereby reduces the wealth of the society.

Rent-seeking is the term economists use when they refer to actions taken by individuals and groups seeking to use the political process to take the wealth of others. Perhaps “favor-seeking” would be a more descriptive term for this type of activity, which generally involves “investing” resources in lobbying and other activities designed to gain favors from the government. The incentive for individuals to spend time and effort in rent-seeking will be determined by how rewarding it is. Rent-seeking will be unattractive when constitutional constraints prevent politicians from taking the property of some and transferring it to others (or forcing some to pay for things desired by others).

When a government fails to allocate the costs of public-sector projects to the primary beneficiaries (through user fees, for example), or when it becomes heavily involved in transfer activities, people will spend more time organizing and lobbying politicians and less time producing goods and services. Resources that would otherwise be used to create wealth and generate income are wasted as people fight over slices of the economic pie—a pie that is smaller than it could be if they were engaged in productive activities instead. When the government grants favors to some people at the expense of others (instead of simply acting as a neutral force protecting property rights and enforcing contracts), counterproductive activities will expand while productive activities will shrink. As a result, the overall income level will fall short of its potential.

There is ample evidence that rent-seeking consumes a substantial amount of resources. Washington D.C. is full of organizations seeking subsidies and other favors from the federal government. More than 3,000 trade associations have offices in Washington, and they employ nearly 100,000 people seeking to alter the actions of Congress. Of course, business and labor organizations are well represented, but so, too, are agricultural interests, health-care providers, trial lawyers, senior citizens, export industries, and many others.

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As we noted earlier, income transfers have grown substantially during the last several decades. The government now taxes approximately one out of every seven dollars citizens earn, and transfers it to someone else. Rent-seeking is the political “fuel” for most of these transfer activities. Interestingly, means-tested transfers, those directed toward the poor, constitute only about one-sixths of all transfers. No income test is applied to the other five-sixths of income transfers. These transfers are generally directed toward groups that are either well organized (like businesses and labor union interests) or easily identifiable (like the elderly and farmers). The people receiving these transfers often have incomes well above the average person.

Within the framework of public-choice analysis, the relatively small portion of income transfers directed toward the poor is not surprising. There is little reason to believe that transfers to the poor will be particularly attractive to vote-seeking politicians. After all, in the United States, the poor are less likely to vote than middle- and upper-income recipients. They are also less likely to be well informed on political issues and candidates. They are not an attractive source of political contributions. Politicians often argue that their proposed policies will help the poor, but there is little reason to believe that this will be a high priority for most of them.

There are three major reasons why government transfer activity will reduce the size of the economic pie. First, income redistribution weakens the link between productive activity and reward. When taxes take a larger share of a person’s income, the reward from hard work and productive activity is reduced. Second, as public policy redistributes a larger share of income, more resources will flow into wasteful rent-seeking activities. Resources used for lobbying and other rent-seeking activities will not be available to increase the size of the economic pie. Third, higher taxes to finance income redistribution and an expansion in rent-seeking will induce taxpayers to focus less on income-producing activities, and more on actions to protect their income. More accountants, lawyers, and tax-shelter experts will be retained as people seek to limit the amount of their income redistributed to others. Like the resources allocated to rent-seeking, resources allocated to protecting one’s wealth from the reach of government will also be unavailable for productive activity. Predictably, the incentives created by government redistribution policies will exert a negative impact on the level of economic activity.

Inefficiency of Government Operations

Will government goods and services be produced efficiently? The pride of a job well done is likely to motivate both public- and private-sector suppliers. However, the incentive to reduce costs and operate efficiently differs substantially between the two. In the private sector, there is a strong incentive to produce efficiently because lower costs mean higher profits, and high costs mean losses and going out of business. This index of performance (profit) is unavailable in the public sector. Missing also are signals from the capital market. When a corporation announces a strategy or a plan that vigilant personally committed investors believe to be faulty, the price of the corporation’s stock will drop. There is no mechanism similar to the stock market in the public sector. Furthermore, direct competition in the form of other firms trying to woo the customers of a government agency or enterprise is largely absent in the public sector. As a result, bureaucrats have more freedom to pursue their narrow goals and interests without a strong regard for the control of costs relative to the benefits the public derives.

Bankruptcy weeds out inefficiency in the private sector, but there is no parallel mechanism to eliminate inefficiency in the public sector. In fact, failure to achieve a targeted objective (for example, a lower crime rate or improvement in student achievement scores) is often used as an argument for increased public-sector funding. Furthermore, public-sector managers are seldom in a position to gain personally from measures that reduce costs. The opposite is often true, in fact. If an agency fails to spend its entire budget for a given year, not only does it have to return the extra money, but its budget for the next year is likely to be cut. Because of this, government agencies typically go on a spending spree near the end of a budget period, if they discover they have failed to spend all the current year’s funds appropriated to them.
It is important to note that the argument of internal inefficiency is not based on the assumption that employees of a bureaucratic government are lazy or less capable. Rather, the emphasis is on the incentives and opportunities that government managers and workers confront. Government firms do not have owners that have risked their wealth on the future success of the firm. There is no entity that will be able to reap substantial economic gain if the firm produces more efficiently or incorporates a new product or service highly valued relative to its costs. The operation of the firm and the appointment of high-level managers might be influenced by political rather than economic considerations. Because the profitability criteria are absent, performance is difficult to evaluate. There are no tests to define economic inefficiency or measure it accurately—much less eliminate it. These perverse incentives are bound to affect efficiency.

The empirical evidence is consistent with this view. Economies dominated by government control, like those of the former Soviet bloc, India, Syria, and Nigeria (and many other African countries) have performed poorly. The level of output per unit of resource input in countries with numerous government enterprises is low. Similarly, when private firms are compared with government agencies providing the same goods or services (like garbage collection, hospitals, electric and water utilities, weather forecasting, and public transportation), studies indicate that private firms generally provide the services more economically.

**ECONOMIC ORGANIZATION: WHO PRODUCES, WHO PAYS, AND WHY IT MATTERS**

The structure of production and consumption will influence economic outcomes. Goods and services can either be produced by private enterprises or supplied by the government. They can be paid for either by the consumer directly or by the taxpayer or some other third party. As Exhibit 7 shows, there are four possible combinations of production and consumption. Let’s take a closer look at each and consider its impact on the allocation of resources and the incentive to economize.

In quadrant 1, goods are produced by private firms and purchased by consumers with their own money. Clearly, consumers will have a strong incentive to economize in this case. They will compare value with cost, and will make purchases only when they value items more than their purchase price. Correspondingly, the owners of private enterprises have a strong incentive to both cater to the views of consumers and supply goods efficiently. Net revenues can be increased if the output can be produced at a lower cost. Producers will continue supplying goods only if consumers are willing to pay an amount sufficient to cover their production costs. Essentially, the supply and demand analysis of Chapter 3 focused on quadrant 1 cases.

Quadrant 2 represents the case in which goods are produced privately but are paid for by the taxpayer or some other third party. Providing health care to citizens financed primarily by government (Medicare and Medicaid) or insurance is an example. If someone...
Good is produced by:

- Consumer-Purchaser
- Taxpayer or other Third party

Good is paid for by:

- (1) Examples: apples, oranges, television sets, food, housing, most other goods
- (2) Examples: health-care, food purchased with food stamps
- (3) Examples: Post Office, water and electricity in many cities, toll roads, many hospitals
- (4) Examples: public schools, streets and roads, national defense, law enforcement

EXHIBIT 7
The Private and Government Sector Matrix of Production and Payment

The incentive to economize is influenced by who produces a good and who pays for it. Economizing behavior will be strongest when consumers purchase goods produced by private firms (quadrant 1). The incentive to economize is reduced when payment is made by a third party and when production is handled by the government.

else is paying the bill, consumers have little incentive to care much about the price of their health-care services. Instead of economizing, many consumers will simply purchase from suppliers they believe offer the highest quality, regardless of the price. The behavior of producers will also be affected. If consumers are largely insensitive to prices, producers have little reason to control costs and offer services at attractive prices. This can dramatically affect economic efficiency.

Quadrant 3 represents the situation in which consumers pay for a good or service, but production is handled by the government. First-class mail delivery via the U.S. Postal Service, water and electricity by municipal governments, and the operation of toll roads are examples that fall into this category. When consumers pay for a good or service directly, they will economize and seek the most value per dollar they spend. This will be true whether their purchases are from private or government enterprises. As we just discussed, however, there is reason to believe that government-operated firms will generally be less efficient than private enterprises. Cost consciousness is also likely to be reduced if the government firm is a monopolist—if it is protected from competition with potential private rivals. Competition, however, is difficult to maintain in some markets. When this is the case, government enterprises may offer a reasonable alternative. As we proceed, we will investigate this issue in more detail.

Quadrant 4 represents the case in which the government both provides the service and covers its costs through taxation. In this case, the political process determines what will be produced, how it will be produced, and how it will be allocated among the general public. Under these circumstances, consumers are in a very weak position to either discipline the suppliers or alter their production. The incentive to produce efficiently is weak, and there is likely to be a disconnect between the goods produced and the preferences of consumers. As we discussed in the previous chapter, the nature of public goods—items such as national defense—makes it difficult, if not impossible, to supply them through markets. In these cases, there may be little alternative to having the government provide them. In other instances, however, there are feasible alternatives. This is true for education.

Most goods and services in the United States are allocated under conditions approximating those of quadrant 1. Thus, most of our analysis focuses on this case. However, a sizable portion of economic activity takes place under conditions present in quadrants 2, 3, and 4, where the incentive structure often creates problems. As a result, our analysis also considers modifications that might improve the efficiency of activities currently undertaken in these quadrants.
THE ECONOMIC WAY OF THINKING ABOUT GOVERNMENT

Given its monopoly power over the legitimate use of force, people have a tendency to believe that the government, particularly a democratic representative government, can solve all types of problems. Further, if things do not go well, people tend to think that it is because the “wrong” people won the last election. Public-choice analysis suggests that the problem is more fundamental: there is sometimes a conflict between winning elections and following sound policies. For some types of activities, there is reason to believe that the political action that will help get one elected will, at the same time, reduce income levels and living standards.

Both the market and the political process have shortcomings. In Chapter 5, we focused on the shortcomings of the market and explained why markets sometimes result in the inefficient use of resources. This chapter provides a parallel analysis for the political process. The accompanying Thumbnail Sketch lists the major deficiencies of both sectors.

Understanding the strengths and weaknesses of both sectors is important if we are going to improve our current economic institutions. As we have stressed throughout this textbook, when the government protects property rights, enforces contracts, and provides a stable monetary environment, economic prosperity is more likely to ensue. The basic problem, however, is how a society can obtain the benefits of the protective functions of government and at the same time constrain it to those activities where it is a productive force. As the analysis of this chapter illustrates, this is not an easy task.

Could Constitutional Changes Help Promote Prosperity?

When we think about how to get the most out of our government, it is important to distinguish between ordinary politics and constitutional rules. Constitutions establish the procedures utilized to make political decisions. Constitutions can also limit the activities of government.

The framers of the U.S. Constitution were aware that even a democratic government might undertake counterproductive actions. Thus, they incorporated restraints on the economic role of government. They enumerated the permissible tax and spending powers of the central government (Article I, Section 8) and allocated all other powers to the states and the people (Tenth Amendment). They also prohibited states from adopting legislation “impairing the obligation of contracts” (Article I, Section 10). Furthermore, the Fifth Amendment specifies that private property shall not be “taken for public use without just compensation.” Over time, however, these restraints have been significantly eroded, due in part to Supreme Court decisions that have effectively reinterpreted the Constitution. Today, it is difficult to think of an economic activity that is beyond the reach of majority rule or normal legislative procedure.

Public-choice analysis highlights the importance of constitutional rules and procedures capable of restraining government activities to those areas in which it will promote

THUMBNAIL SKETCH

What Weakens the Case for Market-Sector Allocation versus Public-Sector Intervention, and Vice Versa?

These factors weaken the case for market-sector allocation:
1. Lack of competition
2. Externalities
3. Public goods
4. Poor information

These factors weaken the case for public-sector intervention:
1. The special-interest effect
2. The shortsightedness effect
3. Rent-seeking
4. Weak incentives for operational efficiency
prosperity. If left alone, even democratic governments will tend to cater to special-interest groups and draw significant resources into rent-seeking. If we can figure out how to constrain the activities of government to those areas in which it is most likely to be productive, higher income levels can be achieved. The challenge before us is to develop constitutional rules and political institutions more consistent with economic efficiency and prosperity. The theory of public choice and its applications can help us do that. Needless to say, this topic is one of the most exciting and potentially fruitful areas of research in economics.

Cases involving potential government intervention will be discussed repeatedly throughout this book. The tools presented in this chapter and the previous one will help us better understand both the potential and limitations of public policy as a source for economic progress.

In recent years, government spending has been about one-third the size of the U.S. economy.

There are both similarities and differences between markets and governments. Competition is present in both sectors. The government can use its taxing power to break the link between payment and receipt of a good for an individual, but not for the economy as a whole. In the public sector, voters face a “bundle” purchase problem; they are unable to vote for some policies favored by one candidate and other policies favored by the candidate’s opponent. Power and income are distributed differently in the public sector than in the private sector.

In a representative democracy, government is controlled by voters who elect politicians to set policy and hire bureaucrats to run government agencies. The incentives faced by all three classes of participants influence political outcomes.

Voters have a strong incentive to support the candidate who offers them the greatest gain relative to their personal costs. Because collective decisions break the link between the choice of the individual and the outcome of the issue, voters are likely to be poorly informed on political matters.

Politicians have a strong incentive to follow a strategy that will enhance their chances of getting elected (and reelected). Political competition more or less forces them to focus on how their actions influence their support among voters and potential contributors.

The distribution of the benefits and costs among voters influences how the political process works. When voters pay in proportion to the benefits they receive from a public-sector project, productive projects tend to be approved and counterproductive ones rejected. When the costs of a policy are distributed among voters differently than are the benefits, democratic decision-making will tend to be less efficient.

Government actions will often lead to economic inefficiency as the result of (1) the special-interest effect, (2) the shortsightedness effect, (3) rent-seeking, and (4) weak incentives to keep cost low within government enterprises and agencies. Thus, just as the market sometimes fails to allocate goods efficiently, so, too, will the government.

Economic organization influences efficiency. The incentive to economize is strong when consumers use their own money to purchase goods and services from private firms. Both the payment by a third party and production by the government weaken the incentive to economize.
1. Are voters likely to be well informed on issues and the positions of candidates? Why or why not?

*2. “The government can afford to take a long view when it needs to, while a private firm has a short-term outlook. Corporate officers, for example, typically care about the next three to six months, not the next 50 to 100 years. Government, not private firms, should own things like forests, that take decades to develop.” Evaluate this view.

3. “If there are problems with markets, government will generally be able to intervene and correct the situation.” Is this statement true or false? Explain your response.

*4. “The political process sometimes leads to economic inefficiency because we elect the wrong people to political office. If the right people were elected, a democracy governed by majority rule would allocate resources efficiently.” Evaluate this statement.

5. What is rent-seeking? When is it likely to be widespread? How does it influence economic efficiency? Explain.

*6. “The average person is more likely to make an informed choice when he or she purchases a personal computer than when he or she votes for a congressional candidate.” Evaluate this statement.

7. “Government action is based on majority rule, whereas market action is based on mutual consent. The market allows for proportional representation of minorities, but minorities must yield to the views of the majority when activities are undertaken through government.” In your own words, explain the meaning of this statement. Is the statement true? Why or why not?

*8. “Voters should simply ignore political candidates who play ball with special-interest groups and vote instead for candidates who will represent all the people when they are elected. Government will work far better when this happens.” Evaluate this view.

9. If a project is efficient (if its total benefits exceed its total costs), would it be possible to allocate the cost of the project in a manner that would provide net benefits to each voter? Why or why not? Explain. Will efficient projects necessarily be favored by a majority of voters? Explain.

*10. “When an economic function is turned over to the government, social cooperation replaces personal self-interest.” Is this statement true? Why or why not?

11. What is the shortsightedness effect? How does the shortsightedness effect influence the efficiency of public-sector action?

*12. What’s wrong with this way of thinking? “Public policy is necessary to protect the average citizen from the power of vested interest groups. In the absence of government intervention, regulated industries, like airlines, railroads, and trucking, will charge excessive prices, products will be unsafe, and the rich would oppress the poor. Government curbs the power of special-interest groups.”

13. “Since government-operated firms do not have to make a profit, they can usually produce at a lower cost and charge a lower price than privately owned enterprises.” Evaluate this view.

14. What percentage of government income transfer payments go to the poor? Do you think that the political process in general works to the advantage of the poor? Why or why not?

15. Why does representative democracy often tax some people in order to provide benefits to others? When governments become heavily involved in tax-transfer activities, how will this involvement affect economic efficiency?

*16. The United States imposes highly restrictive sugar import quotas that result in a domestic price that is generally about three times as high as the world price. The quotas benefit sugar growers at the expense of consumers. Given that there are far more sugar consumers than growers, why aren’t the quotas abolished? Has government action in this area improved the living standards of Americans? Why or why not?

17. “The United States is rich because it is a political democracy where the people decide what policies will be followed.” Is this statement true or false? Discuss.

18. If the power of special interests were reduced, for example through the adoption of a supra majority voting rule, would economic efficiency improve? How would contributions to political campaigns be affected? Do you think politicians are very interested in curtailing the power of special interests? Why or why not?

*Asterisk denotes questions for which answers are given in Appendix B.*