

LECTURE 22: PUBLIC CHOICE

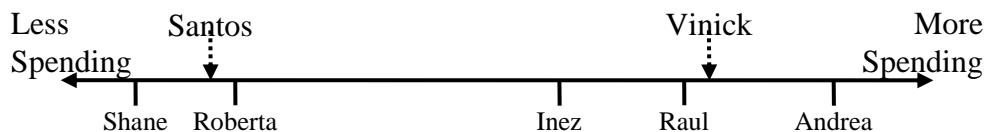
- I. What Is the Government?
 - a. A bunch of people with their own incentives. It is *not*, by definition, people who are out there to help you. While some people are motivated by helping others—and there might even be more of them on average working for the government than in other organizations—there is no reason to believe that is the ultimate motivating factor. Why should political actors be fundamentally different from everyone else?
 - b. Hence *public choice*—the application of economics to political actors (interest groups, politicians, bureaucrats, voters, etc).
- II. Rational ignorance
 - a. Let's begin with the Declaration of Independence and fireworks.
 - b. People often get upset when surveys reveal that a large number of Americans don't know common things (politics, geography, mathematics). See J.D. on *Scrubs*.
 - c. However, it is expensive to learn such things. Just because someone is unaware of some things does mean they are stupid. It is often rational to stay ignorant to that which doesn't really impact your life.
 - d. Thus we have *rational ignorance*: when the costs exceed the expected benefits of learning something, people don't learn it. It's a standard assumption of public choice.
 - e. Lesson: studies on what meaningless facts Americans don't know tells use little of the strength of the economy or intelligence of people. It would be much more illuminating to tailor questions to professions. If most political science professors couldn't find Europe on a map, I'd be much more concerned.
- III. Rational irrationality
 - a. Instead of focusing on voters being rationally ignorant, economist Bryan Caplan argues that people are *rationality irrational*—irrationality is a good that people indulge in when it is cheap to do so. They have emotional attachment to ideas such as economic isolation and since talk is cheap,¹ they gladly support tariffs and other poor economic ideas.

¹ If a protectionist withdrew her support, nothing would change as a single vote is too small to swing the election.

- i. This has the advantage of explaining why people who oppose free trade also buy the cheaper import. When actually shopping, indulging in the romanticism of economic nationalism is too expensive.

IV. Median Voter Theorem

- a. Now we turn to the incentives of politicians. While some politicians could sometimes be described as benevolent, all want to be reelected.
- b. To be elected, you need to appeal to the *median*—or middle—voter.
 - i. Note “median” is not the same as “average.” If one person has \$60 and two people have \$0, the average amount of money is \$20, but the median is \$0.
- c. The *median voter theorem* states when voters vote for the policy that is closest to their ideal point on a line, then the ideal point of the median voter will beat any other policy in a majority rule election
 - i. In other words, the median voter determines the election results.
- d. To see why, consider how much five voters and two politicians prefer to spend on military:



- i. Candidates Santos and Vinick prefer less and more spending, respectively. But what each really wants is to be elected.
- ii. Note how Santos gets more votes if he moves right and goes out for more spending. Note that Vinick can respond by going left and demands less spending. Eventually, they will meet at the median voter.
- e. MVT clearly plays out when politicians change their speeches when they are running in a primary election versus in a general election.
- f. MVT doesn't always apply. If Santos or Vinick moves too far to the middle, the extremes might not vote at all. At the same time, most voters are in the middle; losing a few fringe voters is worth gaining several mainstream voters.

V. Political formula for success

- a. Why does the government pay farmers to not grow crops?
 - i. One group to consider is the consumers who pay slightly more for food because there are fewer people producing.

- ii. The other group to consider is the farmers who receive a tremendous boost in revenue because millions of people pay a little more.
- b. This is one of the key insights of public choice: *concentrated benefits and dispersed costs*.
 - i. Because the costs are dispersed, people are rationally ignorant about these additional costs. A penny or two more for apples is hardly worth worrying about or even bother noticing. But even if they did know, it's not worth taking to the streets for.
 - ii. Because the benefits are concentrated, those that receive them have an interest to spend a great deal of money to lobby the government and secure such benefits. Their pressure will easily outweigh any token resistance consumers will bother with.
 - iii. Politicians then have an incentive to impose laws that benefit the few at the cost of the many.
- c. The ultimate result is *rent seeking*.
 - i. *Rent* is an increase in one's wealth that doesn't increase total wealth (and sometimes decreases it). Another way to put it is a payment for production beyond what's necessary to incentivize that production. While rent, as defined, isn't inherently bad, economists use the term "rent" to describe compensation that's inherently corrupt.
 - ii. *Rent seeking* is the act of pursuing rent. Remember when we discussed crony capitalism at the beginning of the semester? There are many examples of rent and rent seeking:
 - iii. Sugar tariffs protect the sugar and corn industries in the U.S. (it's why high fructose corn syrup is in so many things).
 - iv. Licensing requirements are often very strong making it hard for new firms to compete with existing ones. This lower level of competition allows companies to charge higher prices.
 - v. The Walt Disney corporation lobbied for copyright extension because Mickey Mouse and other works were about to enter the public domain. They succeed with the 1998 Copyright Extension Act, pushing the public domain date to 2023.²
 - vi. Technology firms of all stripes pursue similar efforts to extend their patents, making it more difficult to build and improve on the initial invention. The Wright Brothers were particularly

² <http://artlawjournal.com/mickey-mouse-keeps-changing-copyright-law/>

aggressive with their intellectual property, hamstringing early aviation development.³

- vii. New York City requires cab drivers to purchase the right to drive a taxi. Each taxi cab requires a license, called a medallion, to legally operate. These medallions are easily the most expensive part of running a taxi service. They can go for up to \$1 million each.

VI. The Worst Form of Government?

- a. This all seems to suggest democracy isn't all that great. Perhaps we should go back to a monarchy.
- b. But just because democracy is problematic doesn't mean other options aren't more problematic.
 - i. As Winston Churchill once said: "Democracy is the worst form of government, except for all the others."
- c. Remember: voters are rational. If things get really bad, you'd see people out in the streets demanding change (see Arab Spring). The fact that most voters don't care or pay attention to politics is actually a good sign.
 - i. Nothing brings out the vote better than famine.
- d. But don't forget there are alternatives to political based decision-making: market-based decision making! This of course comes with its costs and dangers (poor quality, high prices, fraud, etc.) which may occur at a higher rate than government services.
- e. So we must remember the ultimate takeaway: It is *never* a choice between a good thing and a bad thing. The choice is always either between two bad things or between two good things. The answer is never obvious.
 - i. If someone ever tells you the answer to a social problem is "really simple," immediately discount what they are about to say. They probably haven't thought about it carefully.

³ <http://knowledgenuts.com/2015/04/18/how-the-wright-brothers-set-back-aviation-history/>
<https://www.amazon.com/Unlocking-Sky-Hammond-Curtiss-Airplane/dp/0060956151>