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Econ 280—Bethany College

**Lecture 24: Rent Seeking and Government**

1. Rent Seeking
   1. The monopoly profits price setting firms get is called “rent.”
      1. This term is a relic from when the discipline treated land holders as monopolists. The payment they got for the use of their land, or rent, was seen as monopoly profits.
      2. Today, rent (now better known as economic rent), is a general turn for monopoly profits. Not all land owners collect economic rent and economic rent is collected by non-land owners.
   2. Rent is an excellent way to make money—you’re getting above average profits!—so it’s not surprising that firms pursue rent. This is called *rent seeking*.
      1. Specifically, rent seeking is the process of gaining by extracting value from the economy rather than adding value
      2. Rent seeking is at best, a *zero sum game* (the total losses must equal the total gains). It can also be a *negative sum game* (the total losses exceed the total gains).
   3. Here are some ways organizations seek rent. Note most of these require government action.
      1. Government contracts
      2. Patents and other monopolies
      3. Controlling specific inputs
      4. Licensing requirements
   4. Examples: taxi medallions, doctor licensing, diamond mines, pharmaceuticals
2. The Lobbyist and You
   1. Lobbying is a process of cultivating favor from powerful political agents (e.g. lawmakers and bureaucrats) to gain desirable political action from those agents. The lobbying is usually done by interest groups, or an organization of people and/or corporations with a common goal.
      1. In other words, you pay the government so the government will send you taxpayer dollars as a reimbursement.
      2. For example if the military’s interest in buying a new jet, Boeing might do everything from send key lawmakers money to take top Pentagon brass out to dinner to make sure the military buys it from them.
   2. Lobbying is often a particularly wasteful activity: instead of spending money to create something of value, you spend money so you can collect earnings taken from others.
   3. Lobbying gets particularly wasteful since there’s usually another interest group wanting the same thing you do.
      1. For example, Lockheed Martin also wants to build the jet for the government, so they lobby as well. Boeing and Lockheed Martin are now in an arms race.
   4. Lobbying resembles an all pay auction: everyone pays their bid regardless if they win the auction (the rent) or not.
      1. It is very easy to set this game up as a prisoner’s dilemma.
   5. Is lobbying always economically inefficient?
      1. Lobbying often manifests as legalized bribery, but that doesn’t mean lobbying is always undesirable.
      2. Interest groups exist because to make any sort of change, you need a lot of backers. And because there’s so much going on, it’s efficient to house all those interested in some common cause under one roof.
      3. Thus lobbying is a form of specialization. If a million people care about stopping animal cruelty, it makes sense that they appoint one person to represent them as a full time job. That way, you get the biggest bang (a favorable political result) for their collective buck (the cost of time and money).
      4. Lobbying can also counter lobbying. Steel makers lobby for steel tariffs. Car makers lobby against steel tariffs.
   6. Lobbying in the Long Run
      1. Lobbying tends to grow as people get better and better at manipulating the political system, and they manipulate it so they can get away with more and more.
      2. As an economy becomes increasingly dominated by interest groups, it becomes poorer and poorer, leading to its decline and eventual collapse. This was originally argued by economist Mancur Olson (1982).
3. Public Choice
   1. How do companies (and other interest groups) get away with all this rent seeking? Public choice.
      1. *Public choice* is the application of economics to political actors.
   2. Rational ignorance
      1. What can Google Trends teach you about public choice?
      2. 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*.
      3. However, it is expensive to learn such things. Just because someone is unaware of some things does not mean they are stupid. It is often rational to stay ignorant to that which doesn’t really impact your life.
      4. Thus we have *rational ignorance*: when the costs exceed the expected benefits of learning something, people don’t learn it.
      5. 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.
   3. Application: Why does the government pay farmers to not grow crops?
      1. One group to consider is the consumers who pay slightly more for food because there are fewer people producing.
      2. The other group to consider is the farmers who receive a tremendous boost in revenue because millions of people pay a little more.
   4. This is one of the key insights of public choice: *concentrated benefits and disperse costs.*
      1. Because the costs are disperse, 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 it to take to the streets for.
      2. 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.
   5. Politicians then have an incentive to impose laws that benefit the few at the cost of the many.