

Public Economics (5 ESTC)

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Pre-requisites: Elementary Mathematics; Economics or Microeconomics (Introductory level) – not obligatory, but helpful

Course Type: compulsory

Abstract: This introductory course in Public Economics covers basic issues including a role of government in modern market economies, market failures and public goods, equity-efficiency trade-offs, public expenditure programmes, and taxation principles. It combines theoretical models with empirical evidence. Objectives and instruments of public policies are demonstrated with examples of health care, pensions, education, housing, crime control, and welfare programmes. General principles of cost-benefit analysis are introduced. The course ends in discussion of increasing government size, its underlying roots, and possible solutions for public spending reduction.

Methods of Instruction: lectures and seminars (including students' presentations and role-playing game)

Course Plan: the course lasts two modules and consists of 14 lectures, 10 seminars (48 academic hours), 1 intermediate test, and final exam.

Grading System: 20% for classes' attendance, 30% for activities at the seminars (presentations, discussions, role-playing game), 20% for intermediate test, and 30% for final exam

Examination Type: written exam with open questions.

Course Content:

1. Public sector in modern economies (1 lecture) *September 6*

Lecture: What is the public sector? Government in a narrow sense. Governmental budget, special funds, institutions and organizations. How to measure the government? Public spending as a share of GDP. Public employment. Government size and growth in modern economies: empirical evidence.

2. Market economy and arguments for governmental interventions (1 lecture and 1 seminar) *September 6, September 12*

Lecture: How markets work? Simple model of market equilibrium. Market efficiency and market failures. Competition failures, externalities, information failures. Incomplete markets. Unemployment and inflation. Public goods and merit goods. Types of state intervention. **Seminar:** group discussion

3. **Social objectives and social choice** (1 lecture) *September 12*

Lecture: Major goals of the modern welfare state. Equity and efficiency trade-offs. Social indifference curves and social welfare function. Various approaches to redistribution. Redistribution in practice: poverty line and inequality indices.

4. **Taxes and tax incidence; tax evasion and shadow economy** (2 lectures and 2 seminars) *September 20, September 25, October 4*

Lectures: Taxation aims and principles. Types of taxes. Direct and indirect taxes. Tax burden and tax incidence. Taxation and efficiency. Tax distortions. Optimal taxation. Tax avoidance and tax evasion. Tax evasion **Seminar:** students' presentations on taxation systems (5 groups). **Seminar:** students' presentations on shadow economy issues.

5. **Social insurance and pension programmes** (2 lectures and 1 seminar) *October 4, October 11, October 16*

Lectures: Private markets for insurance. Necessary conditions for private markets existence. Incomplete insurance markets and governmental interventions. Social vs. private insurance. Pension programmes: rationales for state intervention. Types of pension programmes: PAYG or fully-funded systems? Pro et contra. Ageing crisis and pension systems reforms. **Seminar:** students' presentations on pension system reforms.

6. **Social assistance and welfare programmes** (1 lecture) *October 16*

Lecture: Social assistance vs. social insurance. Rationale for state interventions in case of poverty or income inequality. Social benefits: horizontal and vertical efficiency. Types of social benefits: categorical or means-tested? Pro et contra. Motivation issues: what is wrong with a free lunch? Workfare vs. welfare.

Intermediate test (covers topics 1-6), 2 academic hours, multiple choice.

7. **Health care** (1 lecture and 2 seminars) *November 1, November 13*

Lecture: Health care: private or public good? Rationale for state interventions in health care. Incomplete information, agent's problem, supplier-induced demand. Cream-skimming on health insurance markets. Types of governmental interventions: public health care

system, or social health insurance? Mixed systems. **Seminar:** role-playing game “Adverse selection in medical insurance”. **Seminar:** students’ presentations on health care systems.

8. **Education** (1 lecture and 1 seminar) *November 8, November 20*

Lecture: Education: private or public good? Rationale for state interventions in education system. Education as human capital: direct and indirect costs and benefits. Externalities of education. Types of governmental interventions: public educational system, or state-financed private schools? Quasi-markets for education: voucher system. **Seminar:** students’ presentations on educational systems reforms.

9. **Housing** (1 lecture and 1 seminar) *November 15, November 27*

Lecture: Housing: rationale for state interventions. Housing and well-being. Externalities. House markets bubbles. Types of governmental interventions: regulation, financing, provision. Subsidized housing: who benefits? **Seminar:** students’ presentations on housing issues.

10. **Crime control and prevention** (1 lecture, 1 seminar) *November 22, November 29.*

Lecture: Private and social costs of crime. Market crime prevention: efficiency issues. Governmental crime prevention services: efficiency condition. Severity of punishment vs. probability of punishment. **Seminar:** students’ presentations on crime issues.

11. **Cost-benefit analysis for economic policies** (1 lecture and 1 seminar) *November 29, December 6*

Lecture: Private cost-benefit analysis and NPV concept. Social cost-benefit analysis. Non-monetary costs and benefits: valuing time and life. Market and shadow prices. Risk evaluation. Social discount rate. Cost-effectiveness comparisons. **Seminar:** students divided in small groups evaluate their leisure time, than comparing results.

12. **Government’s growth and policies reducing public spending** (1 lecture) *December 6*

Theoretical models and arguments explaining public expenditure growth. Wagner’s law, Peacock-Wiseman model, Baumol disease, Niskanen bureaucracy model, redistribution, political influence. Policies to reduce public spending: valuing public services, quasi-markets, privatization of public functions and institutions, outsourcing, better targeting of social benefits.

Final exam (covers the whole course content), 4 academic hours.

Reading List

Required

- Nicholas Barr (2012). *Economics of the Welfare State*. Oxford University Press; 5th edition.
- Nicholas Barr (2001). *Welfare State As Piggy Bank: Information, Risk, Uncertainty, and the Role of the State*. Oxford University Press.
<http://site.ebrary.com/lib/hselibrary/reader.action?docID=10273047>
- Julian Le Grand, Carol Propper, Sarah Smith (2009). *The Economics of Social Problems*. Palgrave Macmillan, 3rd edition. (*Also available in Russian, 2013, HSE Publishing House*).
- Joseph E. Stiglitz (2000). *Economics of the Public Sector*. W.W.Norton & Co. 3rd edition.

Optional

- Allingham M.G., Sandmo A. (1972). *Income Tax Evasion: A Theoretical Analysis*. // *Journal of Public Economics*, Vol.1, pp.323-338.
- Arrow, K. (1963). *Uncertainty and the welfare economics of medical care*. // *American Economic Review*. 53(5), pp. 941-973.
- Atkinson A.B. (1995). *Is the Welfare State Necessarily an Obstacle to Economic Growth?* // *European Economic Review*, Vol.39, №3-4, p. 723-730
- Barr N., Diamond P. (2006). *The economics of pensions*. // *Oxford review of economic policy*. Vol. 22 . №1.
- Becker G. (1968). *Crime and Punishment: An Economic Approach*. // *Journal of Political Economy* 76, pp. 169-217.
- Becker G. (1996). *Why a Draft Would Only Damage the Army?* In: G.S.Becker, G.N.Becker .*The Economics of Life*. McGraw-Hill. P.198-199.
- Besely T., Coate S. (1992). *Workfare versus Welfare: Incentive Arguments for Work Requirements in Poverty-Alleviation Programs*. // *The American Economic Review*, March, pp. 249-261.
- Blank R.M. (2000). *When Can Public Policy Makers Rely on Private Markets?* // *Economic Journal*, Vol. 110, No. 462, p. 34-49.
- Easterlin R. (2001). *Income and happiness: Towards a unified theory*. // *Economic Journal*, 111, 456-484.
- Fuchs, V.R. (1978). *The supply of surgeons and the demand for operations*. // *The Journal of Human Resources*. Vol.13. Supplement. P.35-56.
- Persson, T., Tabellini G. (1999). *The size and the scope of government: comparative politics with rational politicians* // *European Economic Review* 43, pp. 699-735.
- Poterba J.M. (1994), *Government Intervention in the Markets for Education and Health Care: How and Why?* / NBER Working Papers, No. 4916.
- White M.J., White L.J. (1977). *The tax subsidy to owner-occupied housing: who benefits?* // *Journal of Public Economics*, 3, 1977. p. 111-126.