

PUBLIC ECONOMICS AND FISCAL POLICY

University of The Witwatersrand - School of Economics and Finance

Lecturer: Michael Sachs
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Time: Monday, 10:00 - 13:00
Venue: NCB247

Overview

All modern societies are mixed economies. Capitalist development and the extension of markets has meant the secular growth of the public sector as a share of national income and a regulator of economic relations. This growth looks certain to continue as the demographic, social and economic challenges of the twenty-first century imply even greater reliance on non-market transactions to achieve growth, equity and development. Although pre-eminent, the public sector everywhere coexists with extensive market transactions. The relationship between public and private institutions remains a central issue of our times.

The course explores the economics of the fiscal state and considers the economic role of the public sector in redistribution, resource allocation and macroeconomic balance. It considers the challenges that arise with the expansion of public provision and state-mediated resource transfers, the tensions between equity, efficiency and other social objectives, the growing scope of public institutions in intergenerational transfers and the sustainability of these operations.

The course takes an ecumenical approach to theory. It is grounded in the social democratic stream in neoclassical economics (associated with Richard Musgrave, Amartya Sen, Tony Atkinson and Jo Stiglitz), but also considers critical and sociological perspectives. Macroeconomic topics are theoretically eclectic, and emphasis concrete analysis and applied policy work. The discussion is strongly located in South Africa's context, with broader implications for small, open, middle income economies.

The course is structured around three themes:

- First is the economics of fiscal redistribution and public provision and their implications for economic efficiency, equity, income distribution and welfare in a mixed economy. The criteria economics uses to evaluate these questions are considered together with applications to social policy, particularly health.
- Second is taxation. Theories of static tax incidence and optimality, which are particularly salient for developed economies are presented, as these define the language of global policy debate. The political economy of taxation in developing economies is also considered.
- Third is the macroeconomic role of public sector institutions. Topics include fiscal policy and stabilisation, public debt, net worth and fiscal sustainability, social pensions and intergenerational transfers.

Assessment

- Final exam: **45%**
- Topic commentaries: **45%**
- Class participation: **10%**

All students will prepare three short essays (maximum 2000 words each) critically engaging on topics selected from the course outline by the participant. Topic questions will be given at the end of each lecture. If a student selects a topic, they should submit the piece two weeks after the end of the lecture.

Readings

The course will draw extensively on the following textbooks

- Barr, N. A. 2012. *Economics of the Welfare State*. 5th ed. Oxford; New York: Oxford University Press.
- Hindriks, Jean, and Gareth D. Myles. 2013. *Intermediate Public Economics*. 2nd ed. Cambridge, MA: MIT Press.
- Black, P. A., Estian Calitz, Tjaart J. Steenekamp, and P. A. Black. 2015. *Public Economics*. Sixth edition. Cape Town, South Africa: Oxford University Press Southern Africa.

A indicative reading list for each topic is attached.

Topics

0. Course introduction
1. The rise (and rise) of the fiscal state

Redistribution and public provision in a mixed economy

2. Economic efficiency, redistributive justice and collective choice
3. Collective goods, private property and market failure
4. Redistribution, the budget and inequality
5. Public expenditure and fiscal institutions in South Africa
6. Economic theory of social insurance
7. Healthcare: market failure and government failure

Taxation

8. Taxation and development
9. Incidence, optimality and the distributional burden of taxation
10. The taxation of income and wealth in South Africa

Public institutions and the macroeconomy

11. Fiscal policy and macro stabilisation
12. Public debt and fiscal sustainability
13. Social security and intergenerational transfers

READINGS AND REFERENCES BY TOPIC

The following list is indicative and may change during the course. A shorter list of compulsory readings will be provided prior to the relevant lecture.

0: Course Introduction

Mazzucato, Mariana, and Robert Skidelsky. (2020) *Toward a New Fiscal Constitution* Project Syndicate, 10 July 2020.

Atkinson, A. B. and Stiglitz, J. E. (1980) *Lecture One: Introduction* in Lectures on Public Economics, London; New York, McGraw-Hill Book Co.

Calitz, Estian. 2015. *The Public Sector in the Economy* Chapter 1 in Black, P. A., Estian Calitz, Tjaart J. Steenekamp. 2015. Public Economics. Sixth edition.

1: The rise (and rise) of the fiscal state

Hindriks, Jean, and Gareth D. Myles (2013) Chapter 4: Public Sector Statistics and Chapter 5: *Theories of the Public Sector* in Intermediate Public Economics. 2nd ed. Cambridge, MA: MIT Press:

Lindert, Peter H. (2004) Chapter 1: *Patterns and Puzzles* and Chapter 2: *Findings* in Growing Public: Volume 1, the Story: Social Spending and Economic Growth since the Eighteenth Century. Cambridge University Press.

Black, P., Siebrits, K. and Van der Merwe, T. (2015) *Public Expenditure and Growth*. Chapter 7 in Black, P. A., Estian Calitz, Tjaart J. Steenekamp. 2015. Public Economics. Sixth edition.

2: Economic efficiency, redistributive justice and collective choice

Barr, N.A. (2012) Chapter 2 Political Theory: Social justice and the State and Section 3.1 and 3.2 of Chapter 3 Economic Theory 1: State Intervention in 'Economics of the Welfare State', 5th ed. ed. Oxford University Press, Oxford; New York.

Varian, Hal R. (2014) Chapter 32: *Exchange* in Intermediate Microeconomics: A Modern Approach, Ninth edition, 601–62. New York London: W.W. Norton & Company.

Hindriks, Jean, and Gareth D. Myles. (2013) Chapter 13: *Optimality and Comparability* Intermediate Public Economics. 2nd ed. Cambridge, MA: MIT Press.

Le Grand, Julian. (1991) Chapters 3: *Equity versus efficiency: the elusive trade-off* and Chapter 5 *Economic conceptions of equity* in Equity and Choice: An Essay in Economics and Applied Philosophy.

Atkinson, A.B., Stiglitz, J.E. (1980) *Lecture Eleven: Introduction to Part Two - Normative Analysis*' in Lectures on public economics. McGraw-Hill Book Co, London; New York.

3: Collective goods, private property and market failure

Barr, N.A. (2012) Chapter 3: *State Intervention* in 'Economics of the Welfare State', 5th ed. ed. Oxford University Press, Oxford; New York.

Varian, Hal R. (2014) Chapter 35: *Externalities* and Chapter 36: *Public Goods* in Intermediate Microeconomics: A Modern Approach, Ninth edition. New York London: W.W. Norton & Company.

Ostrom, Vincent, and Elinor Ostrom. 1977. *Public Goods and Public Choices* in Alternatives for Delivering Public Services: Toward Improved Performance, edited by Emanuel S. Savas. Westview Press.

Buchanan, James M. 1965. *An Economic Theory of Clubs* *Economica* 32(125):1–14.

Foley, D. K. (1978) *State Expenditure from a Marxist Perspective*, *Journal of Public Economics*, 9, 221–238.

Stiglitz, Joseph E., and Jay K. Rosengard. (2015) *Public Goods and Publicly Provided Private Goods* in *Economics of the Public Sector*. Fourth edition

4: Redistribution, the budget and inequality

Lambert, Peter J. (2001) Chapter 11: *The Net Fiscal System* in *The Distribution and Redistribution of Income*. 3rd ed. Manchester ; New York: New York: Manchester University Press.

Inchauste, Gabriela; Nora Lustig; Mashekwa Mabushe; Catriona Purfield and Ingrid Woolard. (2015) *The Distributional Impact of Fiscal Policy in South Africa*. World Bank Policy Research Working Paper, 7194.

Okun, Arthur M. (1977) *Equality and Efficiency: The Big Trade-off*. Brookings Institution Press (Especially Chapters 1 and 4)

Burger, Ronelle, Anja Smith, Nic Spaull, and Servaas Van der Berg. 2015. 'Poverty, Fiscal Incidence and Service Delivery in South Africa'. In *Public Economics*, edited by P. A. Black, EstianCalitz, and TjaartJ. Steenekamp, Sixth edition, 138–67. Cape Town, South Africa: Oxford University Press Southern Africa.

Bowles, Samuel, and Herbert M. Gintis. 1995. *Escaping the Efficiency-Equity Trade-Off: Productivity Enhancing Asset Redistributions* in *Macroeconomic Policy after the Conservative Era: Studies in Investment, Saving, and Finance*, Epstein and Gintis (eds)

5: Public expenditure and fiscal institutions in South Africa

Musgrave, Richard A. (1959) Chapter 1: *A Multiple Theory of the Public Household* in *The Theory of Public Finance: A Study in Public Economy*. McGraw-Hill.

National Treasury (2021) Budget Review Chapter 5 and Chapter 6

Schick, Allen. 1998. *A Contemporary Approach to Public Expenditure Management*. World Bank Institute.

6: Economic theory and social insurance

Barr, N. A. 2012. Chapter 4: Insurance and Chapter 6: Insurance: Unemployment, sickness and disability in *Economics of the Welfare State*. 5th ed. Oxford; New York: Oxford University Press.

Hindriks, Jean, and Gareth D. Myles. 2013. *Intermediate Public Economics*. 2nd ed. Cambridge, MA: MIT Press: Chapter 10 Asymmetric information (especially 10.1 –10.5)

Social Security Administration. 2019 'Social Security Programs Throughout the World: Africa, 2019'. (Guide to Reading the Country Summaries and South Africa Country Summary)

Velasco, Andres. 2020. 'Are We All Keynesians Again'. Project Syndicate, 25 August 2020

7: Healthcare: market failure and government failure

Arrow, Kenneth J. (1963) *Uncertainty and the Welfare Economics of Medical Care* *The American Economic Review*, LIII(5).

Barr, N.A. (2012) Chapter 10: *Health and Healthcare* in 'Economics of the Welfare State', 5th ed. ed. Oxford University Press, Oxford; New York.

Cutler, David M. (2002) Equality, Efficiency, and Market Fundamentals: The Dynamics of International Medical-Care Reform. *Journal of Economic Literature* 40 (3): 881–906.

Deaton, Angus. (2013) *The Great Escape: Health, Wealth and the Origins of Inequality*. Princeton University Press. (Introduction and Chapter 1)

James, Chris; Michael Gmeinder; Ana Maria Ruiz Rivadeneira and Camila Vammalle. (2018) *Health Financing and Budgeting Practices for Health in South Africa*. *OECD Journal on Budgeting*, 17(3), 1-33.

8: Taxation and development

Besley, T. and Persson, T. (2014) 'Why Do Developing Countries Tax So Little?', *Journal of Economic Perspectives*, 28, 99–120.

Braütigam, D (2008) 'Introduction' in Braütigam, D., Fjeldstad, O.-H. and Moore, M. (eds) *Taxation and State-Building in Developing Countries: Capacity and Consent*, Cambridge University Press.

Lieberman, Evan S. 2003. *Race and Regionalism in the Politics of Taxation in Brazil and South Africa*. Cambridge ; New York: Cambridge University Press.

Kaldor, Nicholas. 1963. 'Taxation for Economic Development'. *The Journal of Modern African Studies* 1(1):7–23.

9: Incidence, optimality and the distributional burden of taxation

Institute for Fiscal Studies. 2011. "The Economic Approach to Tax Design" in *Tax by Design: The Mirrlees Review*. Oxford University Press. Chapter 2:

Atkinson, Anthony and Joseph Stiglitz. 1980. "Household Decisions, Income Taxation and Labour Supply". In *Lectures on Public Economics*. McGraw-Hill, 160-199

Hindriks, Jean, and Gareth D. Myles. 2013. *Intermediate Public Economics*. 2nd ed. Cambridge, MA: MIT Press: Chapter 15 Commodity taxation and Chapter 16 and Chapter 17 Income Taxation.

Saez, Emmanuel, and Gabriel Zucman. 2020. 'Clarifying Distributional Tax Incidence: Who Pays Current Taxes vs Tax Reform Analysis'.

Mankiw, N. Gregory, Matthew Weinzierl, and Danny Yagan. 2009. 'Optimal Taxation in Theory and Practice'. *Journal of Economic Perspectives* 23(4):147–74.

10: The taxation of income and wealth in South Africa

Kemp, Johannes Hermanus. 2019. 'The Elasticity of Taxable Income: The Case of South Africa'. *South African Journal of Economics*

Wier, Ludvig and Hayley Reynolds. 2018. "Big and 'Unprofitable': How 10% of Multinational Firms Do 98% of Profit-Shifting." *SA-TIED Working Paper*, 24.

Chatterjee, Aroop, Léo Czajka, and Amory Gethin. 2021. 'A Wealth Tax for South Africa'. *World Inequality Lab Working Paper* 2021/02:31.

Davis Tax Committee (2015) *Final Report on Macro Analysis of the Tax System and Inclusive Growth in South Africa*.

National Treasury. 2021. *Budget Review*. Chapter 4 – Tax policy and Annexure B – Tax expenditures

11: Fiscal policy and macro stabilisation

Carlin, Wendy, and David W. Soskice. 2015. *Macroeconomics: Institutions, Instability, and the Financial System*. Oxford: Oxford University Press. Chapter 14: *Fiscal Policy*

Black, P.A., Calitz, E. and Steenkamp, TJ (2015) *Public Economics*. Chapter 1 *The Public Sector and the Economy* and Chapter 16: *Fiscal Policy*

Walsh. 2010. *Monetary Theory and Policy*. Chapter 4 *Money and Public Finance*

National Treasury. 2021. *Budget Review*. Chapter 3: *Fiscal Policy*

Sachs, Michael (2021) *Fiscal Dimensions of South Africa's Crisis*. Public Economy Project, Working Paper 1. Southern Centre for Inequality Studies

Sachs, Michael (2021) *The Devil and the Deep Blue Sea: South Africa's Fiscal Dilemma*. Public Economy Project Working Paper 2. Southern Centre for Inequality Studies

12: Public debt and fiscal sustainability

Wyplosz, Charles. (2011) *Debt Sustainability Assessment: Mission Impossible*. Review of Economics and Institutions 2(3):37.

Eichengreen, B., El-Ganainy, A., Esteves, RP. And KJ Mitchener (2020) *Public Debt through the Ages*. Chapter 1 in Abbas, S. A., Alex Pienkowski, and Kenneth S. Rogoff, eds. 2020. *Sovereign Debt: A Guide for Economists and Practitioners*. Oxford University Press.

Debrun, X. Ostry, JD., Willems, T and Wyplosz, C. (2020) *Debt Sustainability* Chapter 3 in Abbas, S. A., Alex Pienkowski, and Kenneth S. Rogoff, eds. 2020. *Sovereign Debt: A Guide for Economists and Practitioners*. Oxford University Press.

Blanchard, Olivier. (2019) *Public Debt and Low Interest Rates*. American Economic Review 109(4):1197–1229.

Blanchard, Olivier, Alvaro Leandro, and Jeromin Zettelmeyer. (2020) *Redesigning the EU Fiscal Rules: From Rules to Standards*. 72nd Economic Policy Panel Meeting Supported by the Federal Ministry of Finance, Germany 22-23 October 2020.

Eichengreen, Barry. (1990) *The Capital Levy in Theory and Practice* in Public debt management: theory and history, pp.191-220.

Black, P.A., Calitz, E. and Steenkamp, TJ (2015) *Public Economics*. Chapter 17 *Public Debt and Debt Management*

13: Social security and intergenerational transfers

Hindriks, Jean, and Gareth D. Myles. (2013) *Intermediate Public Economics*. 2nd ed. Cambridge, MA: MIT Press: Chapter 22: *Intertemporal efficiency* and Chapter 23: *Social Security*

Barr, Nicholas and Peter Diamond. (2010) *The Economics of Pensions* Oxford Review of Economic Policy, 22(1).

Barr, Nicholas. (2012) *Economics of the Welfare State* Oxford University Press. Chapter 7: *Consumption Smoothing: Old Age Pensions*

Richard Kohl and Paul O'Brien. (1998) *The Macroeconomics of Ageing, Pensions and Savings: A Survey*. OECD Economics Department Working Papers. 200.

Lindert, P.H. (2004) Chapter 8 *The Public Pension Crisis* in *Growing public: Volume 1, the story: Social spending and economic growth since the eighteenth century*. Cambridge University Press.

Oosthuizen, Morné. (2019) *Inequality and the Generational Economy in Race-Disaggregated National Transfer Accounts for South Africa*. WIDER Working Paper (2019/24):54.