

Academic Year: ( 2023 / 2024 )

Review date: 04-12-2023

Department assigned to the subject: Economics Department

Coordinating teacher: LOEPER , ANTOINE

Type: Electives ECTS Credits : 6.0

Year : Semester :

**REQUIREMENTS (SUBJECTS THAT ARE ASSUMED TO BE KNOWN)****PREREQUISITE**

Attendance to class is highly recommended. The announced dates for midterms and homeworks are final, and they cannot be rescheduled with any justification, unless the circumstances require a make-up exam ACCORDING TO THE UNIVERSITY RULES.

Most of the material that is taught in this class is theoretical, although only basic mathematical tools will be used. The students are expected to have some familiarity with microeconomics.

**THE TOOLS THAT THE STUDENTS NEED TO KNOW ARE THE FOLLOWING:**

- the concept of ordinal preferences (weak and strict preferences, transitive preferences, rational preferences)
- differential calculus (differentiation of a simple function of two variables)
- basic optimization theory (how to maximize a function of one variable or two variables without restriction)
- welfare economics (social welfare functions, externalities, public goods, free-riding)
- basic notions of game theory (Nash equilibrium in finite games, in pure and mixed strategy)

**OBJECTIVES**

Attendance to class is highly recommended. The announced dates for the midterms and final exams are definitive. There is no make-up exam unless the circumstances requires to organize a make-up exam ACCORDING TO THE UNIVERSITY RULES.

Standard economic models have shown that in some cases, markets are not perfect and can fail to achieve a socially optimal outcome. The question is then: how can we remedy these inefficiencies? A naïve public economic approach would state that, with appropriate tools (taxes, subsidies, public provisions, antitrust policies, regulations...), a public intervention can fix the market failure and restore the social optimum.

However, this approach is not satisfactory because it compares a realistic market system with all its imperfections to an ideal, benevolent, and omniscient government which always implements the right policy. As everyone knows, governments do not always implement socially optimal policies. Political representatives may be biased because of reelection concerns, lobbying, or outright corruption; voters can vote against their interest because they are poorly informed about the candidates and the policies they propose; even when voters are perfectly informed, the voting rules (including majority rule) do not always lead to the socially optimal decision. A realistic model of government or collective decision should take into account these political failures.

Taking into account the possibility of market failures and government failures, to assess whether public intervention is beneficial, one has to compare the potential failures of free markets, and economic freedom in general, with the potential failures of public interventions and collective action. Market failures are relatively well understood by economists. Therefore, to complete the picture, one has to understand how government and collective institutions function. This is precisely what political economy is about.

Political economy uses the modern tools of economic analysis (basic decision theory, welfare economics, incentive theory, and game theory) to analyze the functioning and failures of political institutions.

The questions that we will focus on in this class are the following:

- How should we make collective decisions for a group of individuals with heterogeneous needs

and preferences? What are the typical failures of different voting rule? Can we design a voting rule that makes rational decisions and that, at the same time, satisfies some minimal democratic requirement?

- How do governments function? Can we use parsimonious economic models to predict their decisions, and in particular the provision of public good (education, healthcare, defense...) and the degree of redistribution?
- How does electoral competition work? Why are economic competition and electoral competition so different in nature?
- What is the role and influence of interest groups in the political process?

## DESCRIPTION OF CONTENTS: PROGRAMME

The course is divided into four blocks. Each block will be evaluated in the continuous assessment tests throughout the course. The 4 blocks are the following:

### THEME 1: HOW TO TAKE A COLLECTIVE DECISION?

Preferences aggregation rules and voting rules: how to make collective decisions based on the preferences of the individual members of society?

Majority rule: we will see why majority rule can be viewed as the most democratic voting rule. We will compare it to alternative voting rules such as the unanimity rule, the plurality rule, the Borda rule, or the Condorcet rule.

Condorcet cycles and voting paradoxes: we will see why majority rule can lead to irrational decisions.

Arrow and Brown's impossibility theorems: why it is impossible to make collective decisions that are both democratic and rational?

### THEME 2: DOES MAJORITY RULE TAKE GOOD DECISIONS?

The median voter theorem: how to predict the outcome of a majoritarian decision process.

We will use this model to investigate whether majority rule can mitigate the problem of inequality in the distribution of income.

We will use this model to investigate whether majority rule can solve the free-riding problem in public good provision.

We will see that the degree of redistribution of the taxation system used to finance the public goods in democratic societies can distort the incentives of voters, and thus lead to an excessive level of public goods.

The chaos theorem: why voting over multiple issues at the same time can lead to unpredictable and chaotic decisions?

### THEME 3: ELECTORAL COMPETITION

We will analyze a simple model of electoral competition (Downs) that will allow us to:

- see how political competition can shape the incentives of politicians
- investigate whether political competition induces candidates to propose what the citizens wants
- investigate whether political competition induces candidates to differentiate themselves or to all propose similar policies
- discuss the impact of politicians, ideologies, and credibility.

### THEME 4: COLLECTIVE ACTION PROBLEMS AND APPLICATION TO LOBBYING

How does political action and the actions of interest groups differ from voting? Are larger interest groups always more influential than small groups? If not its size, what determines the influence of lobbies?

## LEARNING ACTIVITIES AND METHODOLOGY

### METHODOLOGY

During the first 11 weeks (approximately), the course will alternate between master classes and practical classes (in reduced groups). Each type of class has a different role:

1. During the master classes the fundamental material of the subject is taught. It is taught on the blackboard, so that the classes are more interactive and alive. To facilitate learning, students have access to course notes before each class and know before each class which part of the notes will be covered. The course notes, available in Aula Global, contain additional exercises to complete and deepen the topics explained in class. The 2 midterm exams also take place during the normal master class (week 8 and 14 of the semester, approximately).

2. In small classes, students can take a more active role in solving the proposed exercises. Students' participation in class allows them to analyze problems, interpret models, and communicate solutions, fostering the exchange of opinions. Sharing answers to practical class exercises and joint correction should serve to consolidate knowledge and develop the ability to analyze and communicate relevant information for problem solving. In addition, sharing will favor the exchange of critical opinions both between teacher and students and between students. In these sessions, student participation (including

at the blackboard) is essential. Preparation before class by the students is emphasized in order to encourage more discussion time in class and prioritize those elements that require more interaction with the teacher.

In the last 3 weeks (approximately) of the semester, the small classes will be devoted to students' presentations. These presentations are made in groups of up to 3 to 4 students. During these presentations, students must illustrate the concepts taught in class with concrete examples, or through the discussion of related research articles.

#### ASSESSMENT SYSTEM

The continuous evaluation will be based on 7 problem sets (homework), 2 midterm exams (in class, closed book), and student presentations (in group of up to 4, these presentations are optional). The midterm exam and the final exam will consist of theoretical exercises (multiple choice questions or numerical questions) and short qualitative questions.

The course grade will be the greater of the two following grades:

(A) Continuous Evaluation only: weighted average between (i) grades of 7 homework (21% in total), (ii) the first midterm (30%), and (iii) the second midterm (49%). Additionally, the students can do an optional presentation that may increase their continuous evaluation grade by up to 15 points out of 100.

(B) CONTINUOUS EVALUATION AND FINAL EXAM: A weighted average of the final exam grade ("convocatoria ordinaria, with weight 60%) and the continuous evaluation grade as described in (A) (weight 40%).

In particular, if a student passes the continuous evaluation, that is, if (s)he gets 50 points over 100 or more in the category (A), (s)he does not need to take the final exam (convocatoria ordinaria) to pass the course. If (s)he fails at the continuous evaluation, that is, if (s)he gets less than 50 points over 100 in the category (A), (s)he can still pass the course if (s)he gets a sufficiently good grade at the final exam.

In the "convocatoria extraordinaria" (retake exam), the course grade of the students will be based only on her/hise grade in the exam of the extraordinary exam. The grading criterion in the retake exams are meant to evaluate the capacity of the student to understand and use the most important concepts of the course, with a particular emphasis on those illustrated in the 7 homework.

<b>% end-of-term-examination:</b>	60
<b>% of continuous assessment (assignments, laboratory, practicals...):</b>	40

#### BASIC BIBLIOGRAPHY

- Shepsle, K. A. and M. S. Bonchek Analyzing politics : rationality, behavior, and institutions., New York, W.W. Norton., 1997
- Timothy Besley Principled Agents? : The Political Economy Of Good Government, The Lindahl Lectures. Oxford University Press, 2007