



# Introduction to Public Sector and Public Economics

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## WHAT ARE WE TALKING ABOUT TODAY

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### SOME DEFINITIONS

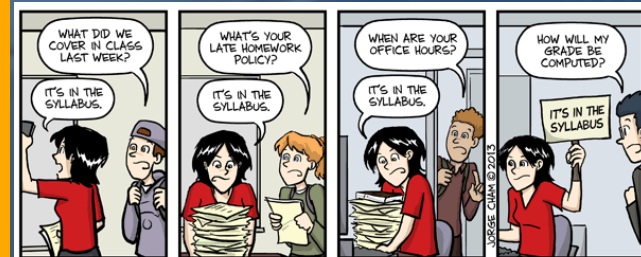
WHAT DO WE MEAN BY  
PUBLIC SECTOR?

WHICH ARE THE MAIN  
FUNCTIONS OF THE PUBLIC  
SECTOR?

WHICH ARE THE MAIN  
THEMES OF PUBLIC  
ECONOMICS?



**Don't forget!**



**IT'S IN THE SYLLABUS**

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# Public Economics

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Definitions and more

## Political Economy

**Political economy:** Branch of social science that studies the relationships between individuals and society and between markets and the state, using a diverse set of tools and methods drawn largely from economics, political science, and sociology. (Brittanica)

The term political economy is derived from the Greek *polis*, meaning “city” or “state,” and *oikonomos*, meaning “one who manages a household or estate.”

Political economy thus can be understood as the study of how a country—the public’s household—is managed or governed, taking into account both political and economic factors.

## The Economic Problem

The **economic problem** asserts that an economy's finite resources are insufficient to satisfy all human wants and needs. It assumes that human wants are unlimited, but the means to satisfy human wants are scarce.

Four questions emerge:

- ☐ What to produce?
- ☐ How to produce?
- ☐ For whom to produce?
- ☐ How are these decisions made?

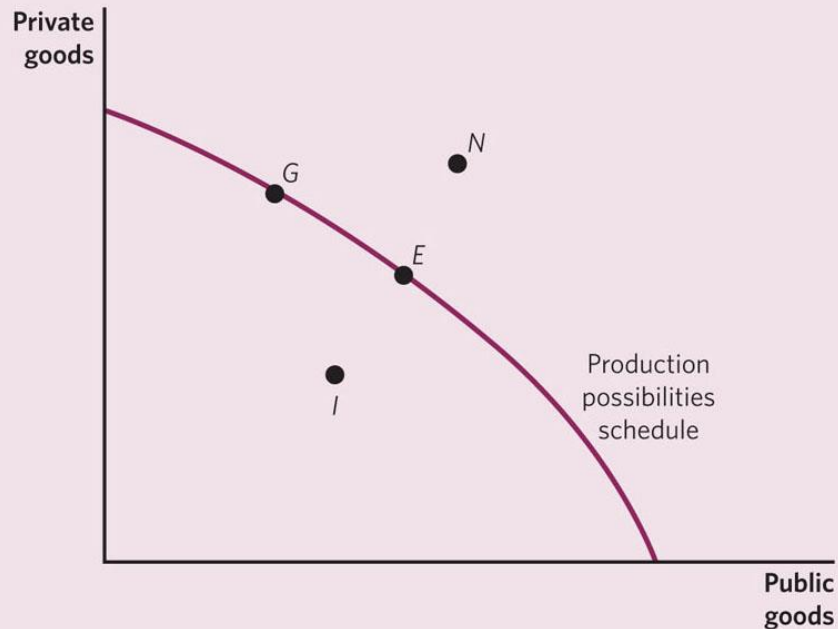
**Economics** deal with these questions

**Public economics** study the role of government in the economy. In other words, the role of government in answering these questions.

## What to produce?

How much of our resources should we devote to the production of public goods such as defence and highways and how much to the production of private goods such as cars, TV sets and video games?

FIGURE 1.1



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G → E: Public goods are increased but private goods decreased.

I: Inefficient – More private and public goods can be produced

N: Infeasible – Not possible, given the current resources and technology

## How to produce?

- Private vs Public Production
- Capital vs Labour intensive production
- Shall we use energy-efficient technologies?



## For whom to produce?

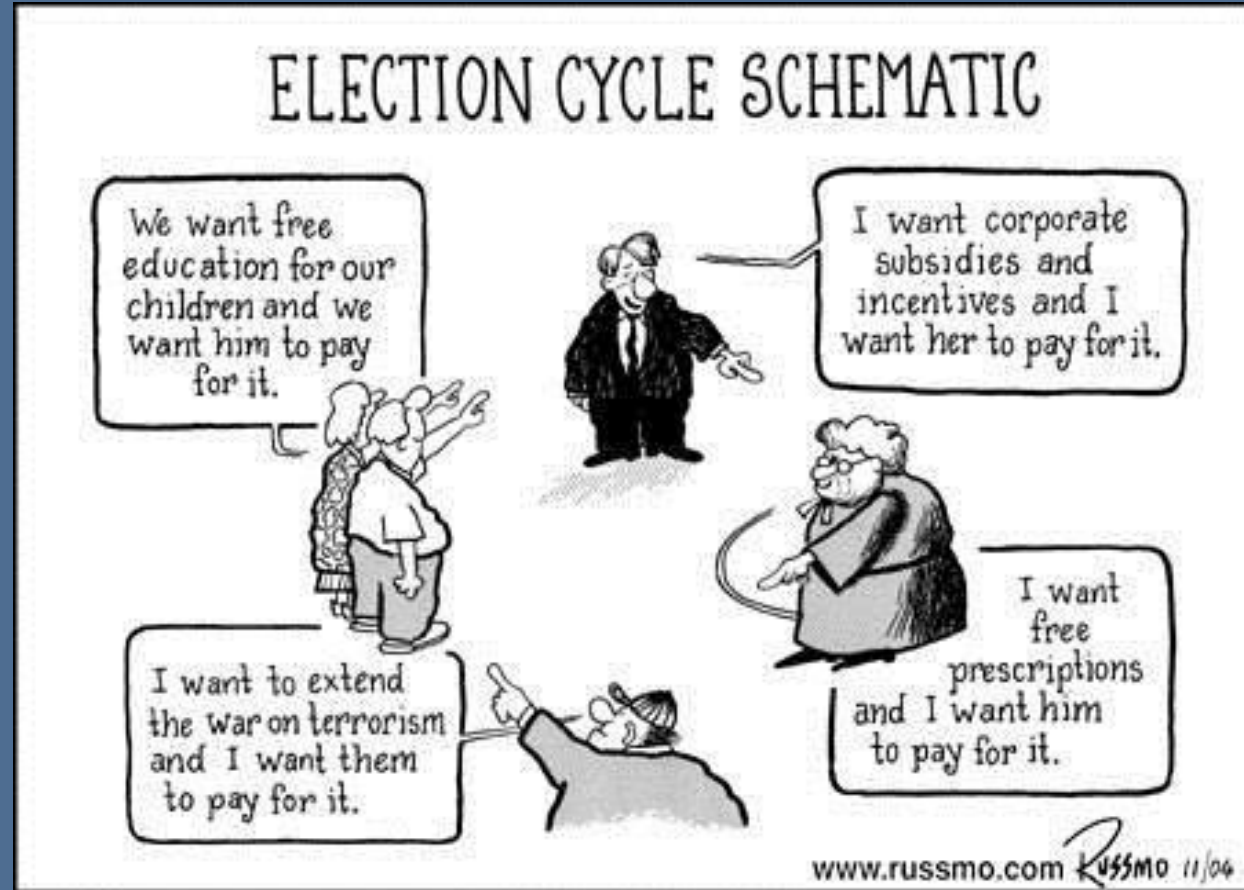
- The question of distribution.
- Taxation and welfare programs affect the disposable income of different individuals.
- Different groups benefit from the production of different public goods.





## How are these decisions made?

- Public Choice
- In the public sector, choices are made collectively
- Collective decision making is far more complicated



# Normative vs Positive

**Normative Public Economics:** Analysis of How Things Should be (e.g., should the government intervene in health insurance market? how high should taxes be?, etc.)

**Positive Public Economics:** Analysis of How Things Really Are (e.g., Does government provided health care crowd out private health care insurance? Do higher taxes reduce labor supply?)

→ Positive Public Economics is a required 1st step before we can complete Normative Public Economics

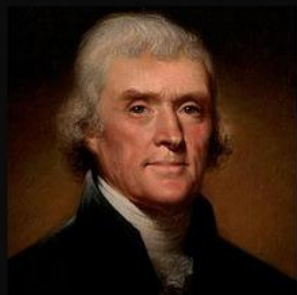
→ Positive analysis is primarily empirical and Normative analysis is primarily theoretical

# The Government

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And its role in the economy

Thomas Jefferson



The purpose of government is to enable the people of a nation to live in safety and happiness. Government exists for the interests of the governed, not for the governors.

AZ QUOTES

The government solution to a problem is usually as bad as the problem.

— Milton Friedman —

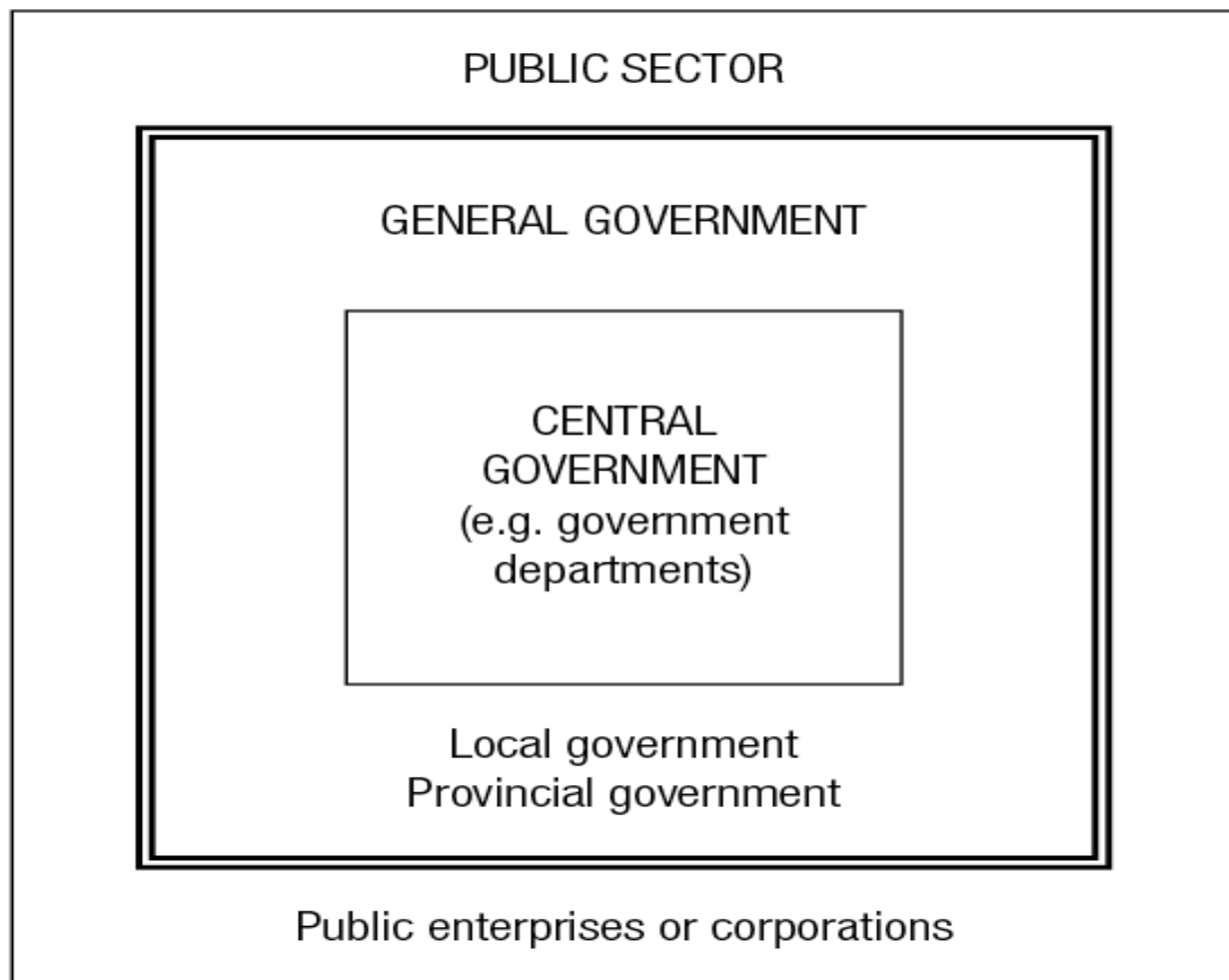
AZ QUOTES

## What is Government?

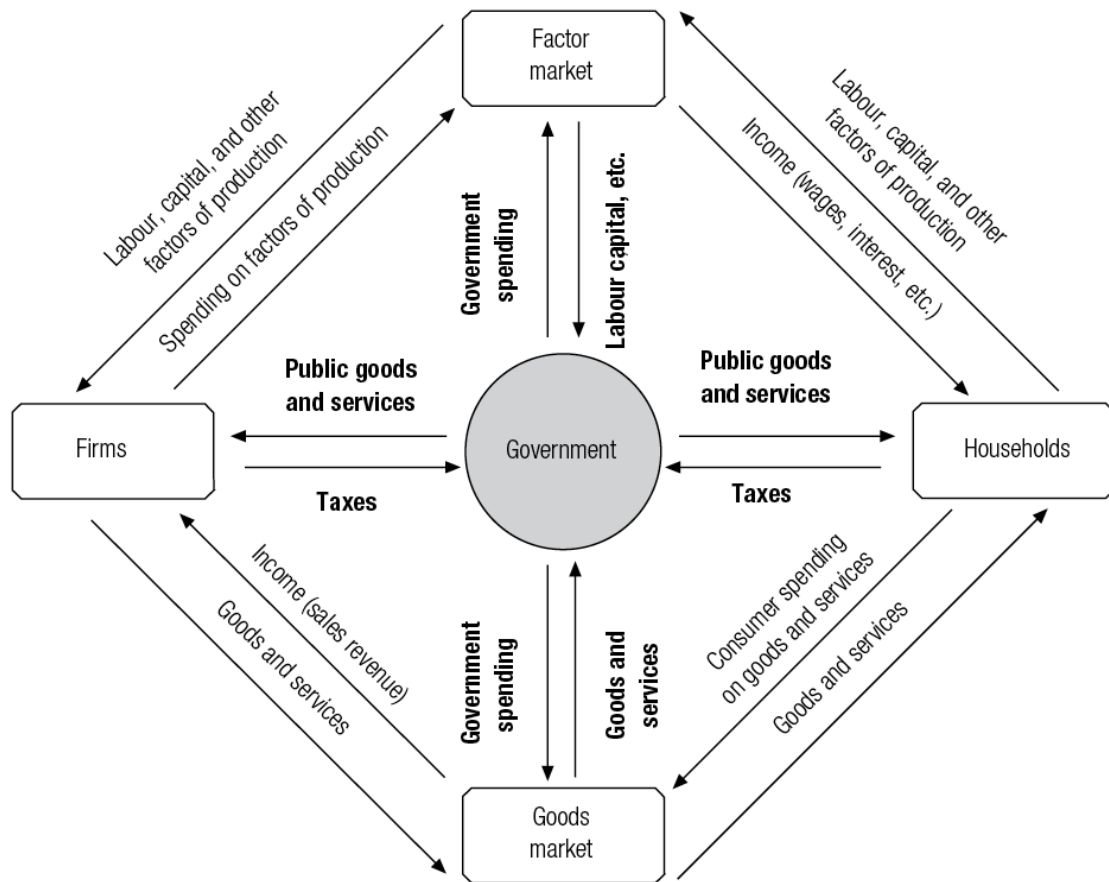
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### Three branches

- ❑ Stabilization
- ❑ Allocation
- ❑ Distribution



## Government in the economic system





# Government provides the legal framework

In other words, sets the rules of the game... and enforces them!

## Four categories of economic activity for the government

**Production of goods and services**



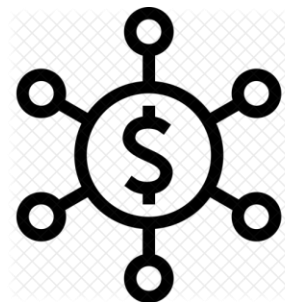
**Regulation and subsidization or taxation of private production**



**Purchase of goods and services**



**Redistribution of income**





## Production of goods and services

- Governments undertake certain types of production directly
- Differs from country to country
- **Privatization vs Nationalization**
- New models: GLC, PPP, PSP
- Best metric: employment



## Regulation and subsidization or taxation of private production

- Three main ways to subsidize:
  - Direct payments to producers
  - Indirect payments through taxation
  - Other hidden Expenditures
- Government Credit: Special form of subsidy when below market interest rates
- Regulation e.g. Environmental Protection Agency

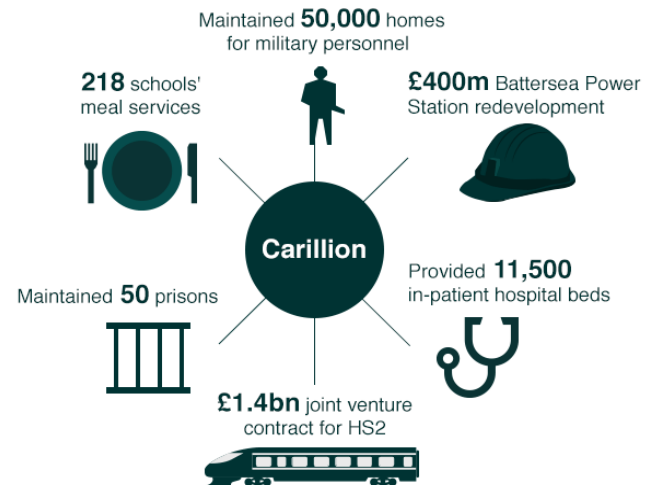


## Purchase of goods and services

- Governments spend millions in purchases of goods and services



### What did Carillion do?





## Redistribution of income

- Public Assistance Programs (cash or in-kind benefits)
- Social Insurance Programs
- Redistribution through the tax system



## Direct and indirect government intervention

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- **Direct government intervention** refers to the actual participation of government in the economy.
- **Indirect government intervention** refers to the regulatory function of government.

A person with long blonde hair is sitting at a desk, writing in a spiral notebook with a pen. On the desk, there is a white coffee cup on a saucer, a calculator, and other papers. The entire image is overlaid with a semi-transparent orange filter.

Have you chosen country for your individual report?

Yes, it's time to  
choose country for  
your individual  
report...

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- No more than two students working on the same country
- First comes, first served
- Assign your self in myCourses:

People → Groups →  
→ A1 - Individual Report



# Done it?

Great! You are ready to start work! Now you must be excited and start thinking about your group...





**Thanks!**

Any questions?