PUBLIC FINANCE (EC270)

Course duration: 54 hours lecture and class time (Over three weeks)

Summer School Programme Area: Economics

LSE Teaching Department: Department of Economics

Lead Faculty: Dr Daniel Reck and Professor Camille Landais (Dept. of Economics)

Pre-requisites: Introductory microeconomics.

Aims:
- To give students an appreciation of the analytical methods in economics for the study of the public sector and the role of the state in principle and in practice.
- To provide a thorough grounding in the principles underlying the role of the state, the design of social insurance and the welfare state and the design of the tax system.
- To enable students to understand the practical problems involved in implementing these principles.

Objectives:
By the end of the course students should be able to:
- Discuss critically key issues in public economics, informed by recent research.
- Present a coherent argument orally and in writing on topics in public economics.
- Demonstrate a familiarity with a range of policy issues and relevant analytical and empirical tools.

Content:
This course provides an introduction to the economic analysis of public policy issues. The focus of the course is on the development of up-to-date analytical tools, drawn from recent research, and their application to key policy issues relating to the spending, taxing and financing activities of government.

The first part of the course presents the foundations of public economics. We start by laying down the general problem and methods of welfare and distributional analysis, and review the traditional rational for government intervention (externalities, public goods, etc.). We also present empirical tools needed to evaluate public policies and conduct welfare analysis. We then look at problems of public choice and political economics, and go on to consider the implications of recent research in behavioural economics for welfare analysis.

The second part studies in much more detail two of the most important domains of public intervention: education policies, and social insurance programs.
The third part is devoted to taxation, behavioural responses and the design of tax policy. We begin by examining the effects of taxes and transfers on labour supply and migration, and then go on to consider incomes and behavioural responses at the top of the income distribution. We look at the implications of taxation for economic efficiency and explore the optimal taxation of commodities and income. The final lecture is devoted to the question of development and public finance.

Assessment

Formative

Students will receive formative feedback on a written assignment. This will be due on Thursday of week one, with feedback given on Monday of week two (in advance of the first summative assessment).

Summative

There are two two-hour examinations, each worth 50% of the final overall grade. The first exam will take place on Wednesday of week two, with results reported by Monday of week three. The final exam will take place on Friday of week three, and final grades will be reported to students within a week of this exam.

Precise time and locations of the exams will be circulated during the programme.

Reading:

The recommended textbook for the course is Jonathan Gruber (2011) Public Finance and Public Policy, 3rd edition, Worth Publishers. Students are encouraged to purchase the text for ease of reference. Copies will also be available in the Library Course Collection. The second edition of the text (Gruber, 2007) is less up to date but has similar coverage (note that the chapter and section references for the 2nd edition are identical to those in the 3rd edition).

Almost all of the journal articles in the reading list can be accessed via the LSE Library electronic journals collection. Hyperlinks are given for working and discussion papers. CC refers to Course Collection.

General:

- N Barr (2012), The Economics of the Welfare State, 5th ed., OUP
Review:


Please note:

The starred items are compulsory. But you should make no attempt to read everything on the reading list; the supplementary readings are provided for students interested in pursuing a particular topic in more depth or for those seeking an alternative approach to that in the starred readings. *It is not important to read a huge amount, but vastly important really to understand what you do read.*

PART I - Foundations of public economics

Introduction to public economics and public policy analysis

Background reading: Gruber (2011), chapters 2, 3

1. Introduction: what is public economics?

Motivation of the course. The 4 questions of public economics. Overview of the course topics. Outline of the course.

- *Barr (2012), chapters 2, 3, 5.
- *Gruber (2011), chapters 2 (especially 2.3), 17 (section 17.1)

Foundations of public economics

2. Foundations of welfare and distributional analysis


- *Gruber (2011), chapter 2
- *Barr (2012), chapters 3, 4.
3. Externalities


- *Gruber (2011), chapters 5, 6 (especially sections 6.1 and 6.2)
- HM Treasury, *The Stern Review: The Economics of Climate Change*, October 2006 (see especially part IV: “Policy responses for mitigation”)
- The Economist, various articles and online debates – including: “Getting Warmer: A special report on climate change and the carbon economy” (5 December 2009):

4. Public goods

Sources of market failure and the role for government intervention: competition failure, public goods, externalities, incomplete markets, information failures. The theory of public goods: non-rivalness and non-excludability; efficiency conditions.

- *Gruber (2011), chapters 2 (especially section 2.3), 7

**Empirical methods for public economics: treatment evaluation**

5. The evaluation problem (1/2)


6. The evaluation problem (2/2)
Instrumental variables: principles, examples. Regression discontinuity design: principles, examples.


**Social choice and the scope of government**

7. Public choice & political economy

- *Gruber (2011), chapter 9.*

**PART II –Public Interventions in the Education and Insurance Markets**

**Education**

8. Public intervention in the education market


Social insurance

9. Social insurance

(i) Why do people value insurance? (ii) Why have social insurance? Asymmetric information and adverse selection. (iii) What are the problems with social insurance? Crowd-out and moral hazard. (iv) Applications to Unemployment Insurance and Disability Insurance.


10. Retirement Pensions


Course content is subject to change. Last updated: January 2018
11. Health


- * Gruber (2011), chapters 15, 16.

12. Behavioural Public Economics

(i) Empirical evidence of mistakes. (ii) New policy tools from behavioural economics. (iii) Rethinking old policy tools in light of mistakes. (iv) Optimal policy and irrational behaviour: is welfare economics doomed?

PART III – Taxation

Taxation and transfer programs

13. Tax incidence


14. Poverty alleviation

15. Taxes, transfers, and labour supply

(i) The theory of tax and labour supply: income vs substitution effects, hours worked vs labour force participation. (ii) Evidence on tax and labour supply. (iii) In-work benefit programs: theory and evidence.


16. Taxes, transfers and migration


17. Income and Wealth Inequality


18. Incomes and behavioural responses at the top of the distribution

(i) The long-run evolution of top income shares and top marginal tax rates. (ii) The elasticity of taxable income: concept, policy relevance, and estimates. (iii) The high-income Laffer curve.


19. Tax inefficiencies and optimal commodity taxation


20. Optimal income taxation


21. Taxation and savings


22. Public Finance and Development

(i) Lessons from optimal tax theory. (ii) Actual tax systems across countries and over the course of development. (iii) Explaining the divergence between optimal and actual tax systems in under-developed economies. (iv) Tax evasion and tax enforcement: theory and evidence.


**Credit Transfer:** If you are hoping to earn credit by taking this course, it is advisable that you confirm it is eligible for credit transfer well in advance of the start date. Please discuss this directly with your home institution or Study Abroad Advisor.

As a guide, our LSE Summer School courses are typically eligible for three or four credits within the US system and 7.5 ECTS in Europe. Different institutions and countries can, and will, vary. You will receive a digital transcript and a printed certificate following your successful completion of the course in order to make arrangements for transfer of credit.

If you have any queries, please direct them to summer.school@lse.ac.uk

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