

Grinnell College
Economics 370
Spring 2020

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Office Hours: Tu/Th 2-5, & other times by arrangement

SEMINAR IN POLITICAL ECONOMY

Economic activity has its own political logic: many economic interactions are “political” in the sense that coalitions of participants, whose interest often differ, influence economic outcomes. Likewise, political activity faces resource constraints. Political economy follows because political interactions and institutions shape and constrain economic activity; and, simultaneously, economic conditions and outcomes shape political interactions and institutions. This course will explore these processes using the concept of collective-action problems as an analytical lens that illustrates common underlying principles. More specifically, we will analyze how incentives, information, shared understandings, and rules influence individual and group tendencies to compete, cooperate, and engage in conflict as they pursue various private and public economic and political activities that affect production, distribution, and power. The course will use relatively simple game-theoretic modeling as a tool for analytical inquiry. At a micro level, we will investigate the influence of material incentives, social incentives, and incomplete information on transactions costs—especially the costs of enforcing economic contracts and political agreements. Enforcement, in turn, generates a potential for exercising of power—even within exchange relationships. We will proceed to investigate various contours of social contexts within which such activity operates, including reciprocal relationships, social norms, and formal institutions. Turning to the macro-level, we will address relations among economic institutions, governance, development, growth, and distribution. Especially during the second half of the semester, students will conduct research projects on political economy topics of their choosing, utilizing theoretical and empirical tools to investigate contemporary or historical political economy problems.

Now at last we are setting ourselves seriously to inquire whether there should be any so-called “lower classes” at all: that is, whether there need be large numbers of people doomed from their birth to hard work in order to provide for others the requisites of a refined and cultured life; while they themselves are prevented by their poverty and toil from having any share or part in that life. . . The question cannot be fully answered by economic science. For the answer depends partly on the moral and political capabilities of human nature . . . But the answer depends in a great measure upon facts and inferences, which are within the province of economics; and this it is which gives to economic studies their chief and their highest interest. -- Alfred Marshall, Principles of Economics, 1890.

What is missing from the policy analyst’s tool kit – and from the set of accepted, well-developed theories of human organization – is an adequately specified theory of collective action whereby a group of principals can organize themselves voluntarily to retain the residuals of their own effort. – Elinor Ostrom (2009 Nobel Prize in Economics)

A good part of social organization—of what we call society—consists of institutional arrangements to overcome these divergences between perceived individual interest and some larger collective bargain. – Thomas Schelling (2005 Nobel Prize in Economics)

There is a large arbitrary element in the relative rates of remuneration, and the factors of production get what they do, not because in any strict sense they precisely earn it, but because past events have led to these rates being customary and usual. -- John Maynard Keynes

One of the great challenges in the social sciences is to understand how aggregate outcomes are often different from anyone’s intent, sometimes better as ...[in] Adam Smith but sometimes worse, as an American family seeking a multi-racial neighborhood might suspect. – Samuel Bowles

COURSE POLICIES

Class Meetings and Etiquette

MW 2:00 until 3:50. I expect students to attend class and show up on time. Please plan to stay in the room for the entire class except for the five minute break in the middle of class. Please TURN OFF your cell phones! I do not want you to know that you received a text message! Please do not use laptops without permission from the instructor. Laptops are distracting and studies show that handwritten notes improve memory.

Inclusivity and Accommodation for Disabilities

At Grinnell, we strive to create fully inclusive classrooms. The college offers reasonable accommodations for students who observe religious holy days. Please contact me in advance to discuss specific instances that apply to you. I welcome individual students to approach me about distinctive learning needs. Grinnell College makes reasonable accommodations for students with documented disabilities. I encourage students with documented disabilities, including invisible or non-apparent disabilities such as chronic illness, learning disabilities, and psychiatric disabilities, to discuss reasonable accommodations with me. You will also need to have a conversation about and provide documentation of your disability to the Coordinator for Student Disability Resources, John Hirschman, located on the 3rd floor of Goodnow Hall (x3089).

Assignments and Grading

I evaluate students on written work, formal oral presentations, attendance, and the quality and frequency of their participation in classroom discussion.

Written assignments: three problem sets; two short papers (5 pages); one initial research project thesis statement and outline (2-3 pages); one “long” research project thesis and outline (5+ pages); and a research paper (15-20 pages, not counting figures, tables, and references). Papers must be clearly written and concise. Draft them at least twice before turning in. Evaluation will involve both clarity and content.

I strongly encourage students to use the [Writing Lab](#) (HSSC N3129) for support on papers, projects, and presentations. In one-on-one sessions, students can get feedback as they brainstorm ideas, strengthen arguments, choose and analyze evidence, focus paragraphs, craft introductions and conclusions, rewrite sentences, organize and revise whole drafts, plan presentations, and more. Set up appointments in advance.

Late work: Work turned in late receives a grade deduction, which adds up quickly as time passes.

Formal oral assignments: panel presentations related to course readings, usually occur on Mondays extending into early April. All students participate each session—either presenters or discussants. At the end of the semester, students will present their research projects to the class.

Absence: Attendance is *required* for all classes. Notify me a week in advance for sports absences. For all absences, excused or unexcused, students should email me written answers to the discussion questions for the day(s) missed (usually before the next class is OK). These answers can raise the day’s participation score above zero (the score for not doing so), but they are not equivalent to attending class. It is YOUR responsibility remember to email me answers to discussion questions for any missed day.

READINGS:

To Purchase:

(Bookstore or Amazon; get them by the first day of class)

- Basu, Kaushik, *Prelude to Political Economy: A Study of the Social and Political Foundations of Economics*, Oxford U.K.: Oxford University Press, 2000.
- Ferguson, William D. *Collective Action and Exchange: A Game-Theoretic Approach to Contemporary Political Economy*, Stanford, CA: Stanford University Press 2013.
- Schelling, Thomas, *Micromotives and Macrobehavior*, New York, N.Y.: W.W. Norton, 2006.

On Library Reserve (* = e-reserve; the rest are books)

- Acemoglu, Daron, Simon Johnson and James Robinson (2004), *Institutions as the Fundamental Cause of Long-Run Growth*, National Bureau of Economic Research Working Paper 10481.*
- Bowles, Samuel, *Microeconomics: Behavior, Institutions, and Evolution*, Princeton University Press, 2004, selected pages*; chapters 2-4, 7 (the book is on physical reserve)
- Dixit, Avinash and Susan Skeath, *Games of Strategy*, Second Edition, New York, NY: W.W. Norton, 2004.

Available through JSTOR:

- Akerlof, George, “On Making Economics Realistic,” Interview, *Challenge*, Vol. 45, No. 6, Nov. – Dec. 2002, pp. 6-20.
- Akerlof, George and Rachel Kranton, “Economics and Identity,” *Quarterly Journal of Economics*, Aug. 2000, pp. 715-752.
- Akerlof, George and Rachel Kranton, “Identity and the Economics of Organization,” *Journal of Economic Perspectives*,” 19 (1), Winter 2005, pp. 9-32.
- Bowles, Samuel, “What Markets Can and Cannot Do,” *Challenge*, July/August 1991.
- Elster, Jon, “Social Norms and Economic Theory,” *Journal of Economic Perspectives*, 3(4), Fall 1989, pp. 99-117.
- Fehr and Fischbacher, “Why Social Preferences Matter – The Impact of Non-selfish Motives on Competition, Cooperation and Incentives,” *The Economic Journal* 112 (March), 2002.
- Ostrom, Elinor, “Collective Action and the Evolution of Social Norms,” *Journal of Economic Perspectives*, Vol. 14, No. 3, summer 2000, pp. 137-158.

I will post additional handouts on PWeb.

COURSE OUTLINE

(Please refer to lists above for full citations)

I. Social and Political Microfoundations of Political Economy

The main weakness of previous theories that stress the importance of distributive questions has been the lack of microfoundations, or the mechanisms by which institutions emerge and change. – Jack Knight

- A. Introduction – Political Economy, Institutional, and Neoclassical Economics (Jan. 22, 27)
- Akerlof, “On Making Economics Realistic,” Interview
 - Bowles, *Microeconomics*, Prologue, pp. 1-14
 - Bowles, “What markets can and cannot do”
 - Basu, Chapter 1; Schelling, Chapter 1; Ferguson, Chapter 1
 - Handout on Concepts and Definitions

B. Individuals, Strategic Behavior, and Collective-Action Problems (Jan. 29, Feb. 3)

1. Elementary game theory and collective action: 2-person games and relations to problems of public goods, common pool resources, and externalities
 - Basu, Chapter 2, “Games and Misdemeanors”
 - Bowles, *Microeconomics*, pp. 23-27, 31-32, 35-37; optional 27-31 and 40-47
 - Ferguson, Chapter 2, sections 1 and 2
 - Optional: Review Mankiw, *Principles of Economics*, Chapters 10 and 11 on externalities, public goods and common resources and an intermediate micro text on game theory
2. Second-order problems of enforcement; Multi-player Games
 - Ferguson, Chapter 2, section 3
 - Ferguson, Chapter 3 sections 1 and 2
3. Tipping Points, Critical Mass, and Punctuated Equilibria
 - Schelling, Chapter 3

Related Readings:

Dixit and Skeath, Chapter 11, “Collective-Action Games” (book on reserve at Burling)
Bowles, *Microeconomics*, remainder of Chapter 1, Chapters 2-4 (the book is on reserve)

C. Power and Redress in Political Economy (Feb. 5-12)

1. Principal-agent problems and contested exchange:
 - Ferguson, Chapter 3, section 3
 - Bowles, pp. 253-266
2. Power, coercion and influence
 - Basu, Chapter 6
 - Ferguson, Chapter 4
3. Mechanisms of redress: exit, voice, and loyalty
 - Ferguson, Chapter 7, section 2

D. Types of Preferences and Rationality Feb. 17, 19)

- Fehr and Fischbacher, “Why Social Preferences Matter – The Impact of Non-selfish Motives on Competition, Cooperation and Incentives,” *The Economic Journal* 112 (March), 2002
- Ostrom, Elinor, “Collective Action and the Evolution of Social Norms”
- Ferguson, Chapters 5 and 6, selections
- Basu, Chapter 3, section 3.1.

Related Readings:

Bowles and Gintis, “Power and Wealth in a Competitive Capitalist Economy”
Fehr, Ernst and Klaus M. Schmidt, “A Theory of Fairness, Competition, and Cooperation,”
Hirschman, Albert O. *Exit Voice and Loyalty* (book is on reserve)

****First Short Paper due Monday, Feb. 24****

E. Informal Institutions, Formal Institutions, and Governance (Oct. 7 – Nov. 6)

1. Overview of institutions
 - Ferguson, Chapter 7, “Institutions, Organizations, and Institutional Systems”

2. Informal institutions

- Young, “The Economics of Convention”
- Elster, Jon, “Social Norms and Economic Theory”
- Basu, Chapter 4, “Social Norms, Culture and Beliefs”
- Ferguson, Chapter 8, “Informal Institutions”

****Research Paper Topic Paragraphs due Wed., Mar. 4****

3. Norms and identity

- Akerlof & Kranton, “Economics and Identity”
- Akerlof & Kranton, “Identity and the Economics of Organization”

4. Self-governance and second-party enforcement

- Ferguson, Chapter 9, “Internal Resolution via Group Self-Organization”

**Initial Thesis Statement, Outline and Bibliography for Research Paper
Due Wed., Mar. 11****

5. Formal institutions and third-party enforcement

- Basu, Chapter 5, “Law and Economics”
- Ferguson, Chapter 10, “Formal Institutions, Third-Party Enforcement, and Interactions with Self-Governance”

Related Readings:

Elster, Jon, *The cement of society: A study of social order*, Cambridge University Press, 1989.
Ostrom, Elinor, *Governing the Commons*, Cambridge University Press, 1990.

****Long Outline, Thesis & Bibliography due Monday, April 6**
(Meet with me at least a week in advance of this date)**

II. The Political Economy of Growth and Distribution (April 8 - 20)

“... the inability of societies to develop effective, low-cost enforcement of contracts is the most important source of both historical stagnation and contemporary underdevelopment in the Third World.” – Douglass North

*“The efforts of men are utilized in two different ways: they are directed to the production or transformation of economic goods, or else to the appropriation of goods produced by others.”
--Vilfredo Pareto (1905)*

A. Distribution, Institutional Evolution and Economic Growth

- Acemoglu, Johnson and Robinson, “Institutions and the Fundamental Cause of Long-Run Growth,” NBER Working Paper 10481
- North et al., *In the Shadow of Violence*, Chapter 1
- Ferguson, Chapter 13, “Knowledge, Collective Action, Location, Institutions, and Growth”

****Second Short Paper due Monday, April 13****

Related Readings:

- Grossman, Gene M. and Elhanan Helpman, "Endogenous Innovation in the Theory of Growth," *Journal of Economic Perspectives*, 8 (1), Winter 1994, pp. 3 - 23.*
- Rodrik, Dani, "Democracies Pay Higher Wages," *Quarterly Journal of Economics*, CXIV (3), Aug. 1999, pp. 707-738.

VI. Student Presentations of Research Papers: April 20 – May 4.

*****Draft of Research Paper (optional) due April 20*****

Concluding Session, Wed. Dec. 11.

****** FINAL PAPER DUE at Noon, FRIDAY, May 8******

(You know this now and you know the end of the semester will be busy. This is true for everyone; I expect the papers on time.)

Closing thought:

The problem is the really big sums cannot be picked up through uncoordinated individual actions. They can only be obtained through the efficient cooperation of many millions of specialized workers and other inputs: . . . they can only be attained if a vast array of gains from specialization and trade are realized. Though the low-income societies obtain most of the gains from self-enforcing trades, they do not realize many of the largest gains from specialization and trade. They do not have institutions that enforce contracts impartially, and so they lose most of the gains from those transactions (like those in the capital market) that require impartial third-party enforcement. They do not have institutions that make property rights secure over the long run, so they lose most of the gains from capital-intensive production. Production and trade in these societies is further handicapped by misguided economic policies and by private and public predation. The intricate social cooperation that emerges when there is a sophisticated array of markets requires far better institutions and economic policies than most countries have. The effective correction of market failure is even more difficult. . . the bargains needed to make efficient societies are not, in fact, made . . . individual rationality is very far indeed from being sufficient for social rationality.

—Mancur Olson