
41 Public choice economics

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Positive public choice – or the economics of politics – is a relatively new field of scientific endeavor, located at the interface between economics and politics. It was founded in 1948 by Duncan Black, whose paper on the rationale of group decision making (Black, 1948) showed that, at most, only one motion, before a committee or an electorate, can secure a simple majority over every other motion. Specifically, if voter preferences are single-peaked over policy issue space, a unique equilibrium exists in the motion most preferred by the median voter.

In 1957, Anthony Downs moved positive public choice from its initial preoccupation with committee voting and direct elections to its subsequent concern with democracy and representative government. In a far-reaching contribution (Downs, 1957), he skilfully moved the median voter theorem from the realm of committees to the more complex environment of representative government. In so doing, he laid the foundations for a major research program that applies rational choice theory to every aspect of the political market-place. Public choice, thus defined, is a positive science concerned with what is or what conditionally might be. Its practitioners seek to understand and to predict the behavior of political markets by utilizing the analytical techniques of economics, most notably the rational choice postulate, in modelling non-market decision-making behavior (Rowley, 1993a).

Normative public choice – or social choice – is concerned with the appropriate relationships between individuals and society, the extent to which individuals' preferences can and should be aggregated into some overall notion of social welfare, social judgement or social choice. This research program examines relationships between ethics, economics and the state, combining moral philosophy, economics and political science to explore the rationale and implications of a range of alternative and sometimes conflicting social goals.

Because of the pre-eminence of Virginia political economy in normative public choice, the dominant ethics are widely seen to be conservative (Buchanan and Tullock) or classical liberal (Rowley and Wagner). However, the socialist ethic is well represented (Arrow and Rawls), as is the social

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democrat ethic (Mueller and Olson). Normative public choice provides a much larger ethical tent than many of its practitioners and many of its critics are willing to concede (Rowley, 1993b). As public choice extends its influence beyond the North American sub-continent, ethical diversity, predictably, will increase even as scientific knowledge begins to converge.

Rational choice

The most distinctive single characteristic of positive public choice is its reliance on the rational choice model of neoclassical economics in modeling the behavior of all participants in political markets. Indeed, it is unlikely that public choice as it is now would survive the jettisoning of this principle as the protected core of its research program. Yet the resolute application of this principle has provoked strong scholarly criticism, not least from within the Austrian school (Rothbard, 1989). Rothbard's specific criticism of rational choice is his belief that public choicers carry economic determinism to the extreme of denying any motivation in human history except monetary gain. As he sees it, the only argument in the utility functions of those individuals who are modeled in public choice is expected wealth: 'Accumulate, accumulate: that is Moses and the prophets.' In this respect, Rothbard is misinformed. Public choicers, with but few exceptions, view individual utilities as multidimensional, albeit with expected wealth playing an important role. There is a considerable literature, for example, exploring the role of altruism and ideology in political market behavior (Rowley, 1993a).

What does appear to be incontrovertible is the remarkable empirical power of the expected wealth variable in models purporting to explain and to predict the demand and supply of public policies. Rothbard may wish that this were not so, may choose to stand in front of water that flows downhill and command it to reverse its flow, but he is about as likely as was Canute to be successful in a similar endeavour. Much of public choice analysis is directed at the margins and not the totality of individual behavior. If the expected cost of a course of behavior increases, the evidence indicates that supply, almost without exception, falls; if the expected return increases, the evidence indicates that supply, almost without exception, rises. Once the *ceteris paribus* conditions are acknowledged, Rothbard's criticism is seen to be misplaced.

An important presumption of the Austrian research program is the unknowability of the future and the problem of disseminating information, yet Rothbard (1989) is particularly shocked by one of the truly important paradoxes of public choice, namely the concept of the rationally ignorant voter. One of the earliest discoveries of positive public choice (Downs, 1957) was an explanation as to why many rational potential voters are ill-informed about political matters. Given the extremely low probability that an individual's vote will be decisive in an election (one in one million in a typical

presidential election in the USA), the expected benefit of well-informed voting is small to the point of invisibility and much less than the cost of search.

Since the cost of voting is relatively high, abstention is the rational policy for the investment-oriented potential voter. Those who vote for consumption reasons are rationally ignorant of the competing candidates' policy positions and may indeed pull the election levers randomly or on the basis of valence considerations. Such behavior in no sense implies a judgement that individual voters are unconcerned about acquiring knowledge as a basis for human betterment. It implies that knowledge will move, readily acquired, in areas over which individuals have some influence, to the neglect of areas which are largely beyond an individual's control. Such a notion is entirely consistent with Hayek's writings on the use of knowledge (Hayek, 1945).

Equilibrium

A great deal of positive public choice scholarship applies the equilibrium analysis of neoclassical economics to political markets, indeed is viewed by many political scientists as straightforward imperialism on the part of neoclassical economists. To the extent that this approach is influential, it runs counter to the broad thrust of Austrian economics which analyses markets as disequilibrium processes, which views individuals as subjective decision makers in environments characterized by radical uncertainty and which emphasizes alertness to as yet unperceived opportunities as the principal criterion of entrepreneurial success (Kirzner, 1987).

Without doubt, the most committed applications of neoclassical economics to public choice stem from the Chicago political economy program (CPE) which was launched in 1971 by George Stigler's article on economic regulation. The leading practitioners of CPE are Becker, Peltzman, Landes and Posner. CPE views government primarily as a mechanism exploited by rational, self-seeking individuals to redistribute wealth within a society. *Homo economicus* is modeled almost exclusively as a wealth maximizer. The thrust of the theory is towards instantaneous and durable equilibrium, with political markets clearing continuously. Politicians broker political markets without invading them as principals. They are driven by constraints and not by preferences. Their own ideologies are tightly suppressed (Rowley, 1993a).

The auxiliary hypotheses of CPE ensure that political market equilibrium is both tight and instantaneous. All individuals are assumed to be price takers, transacting at market-clearing prices consistent with optimizing behavior. All individuals are assumed to engage in optimal search and prices thus reflect all economically relevant information. All constraints on economic behavior are viewed as technically efficient, the outcome of wealth-maximizing behavior on the part of those who create or modify them. The equilibria predicted by

CPE are not based on perfect foresight and uncertainty conditions individuals' behavior in political markets. However, individuals respond to uncertainty stochastically as expected utility maximizers, and not as entrepreneurs groping towards profit opportunities in an environment characterized by Knightian uncertainty. For the most part, CPE views political markets as technically efficient, parlaying the preferences of the decisive actors into well tailored public policies.

CPE is a body of literature that analyses political markets from the perspective of price theory and positive economics. Its models are precisely formulated in the language of mathematics. The predictions of its models are rigorously evaluated through state-of-the-art statistical techniques. In all these respects, it is sharply at odds with the methods of Austrian economics, which to a significant extent eschews as inappropriate modern mathematical and econometric techniques (Kirzner, 1987). It is noteworthy that two scientific programs that are so mutually incompatible are advanced by scholars who share much the same anti-government ideology.

The scientific approach of the Virginia political economy program (VPE), though still emphasizing equilibrium analysis, is distinctly closer to that of Austrian economics. Government is analysed from the perspective of price theory as a vehicle exploited by rational, self-seeking individuals to redistribute wealth. In this respect, the protected core of the VPE research program closely resembles that of Chicago. Yet its central hypotheses – suggestive of universal government failure – could not be more different. In explaining such a divergence in predictions, important differences in the auxiliary statements of the two programs must be identified. Virginia, unlike Chicago, does not assume that individuals are always price takers in political markets. Significant discretionary power is anticipated. Virginia does not assume as generally as Chicago that political markets clear instantaneously and continuously. It does not as frequently assume that the future should be analysed in terms of risk rather than Knightian uncertainty. It does not generally perceive political equilibria to be durable, nor does it as easily excise human error from its theories of political markets. In general, its approach is that of diffuse rather than tight prior equilibrium. However, it does not regularly analyse political markets from the perspective of disequilibrium, nor does it regularly employ the radical subjectivism of the Austrian school in its analysis of public choice.

Although Virginian theories are formulated generally at a lower level of mathematical sophistication than those of Chicago and with more concern about institutional details, the methods of hypothesis testing are much the same. Once again, Virginian and Austrian scholars, who have much in common in the field of ideology, and whose understanding of political market failure is much closer than is the case with CPE, derive their results through radically different scientific methods.

Catallactics

The term 'catallactics' meaning the 'science of exchanges', was first proposed as a replacement for the term 'political economy' by the Reverend Richard Whately in his 1831 Drummond Lectures delivered at Oxford University. Whately denounced Adam Smith's definition of the scope of political economy as the science of wealth (Rothbard, 1987), instead defining man as 'an animal that makes exchanges'. This shift of emphasis led Whately in the direction of a subjective theory of value and to the judgement that differences in subjective value are the foundation of all exchanges. Catallactics made heavy weather in the powerful currents of neoclassical economics and all but died out after 1905 following the death of Arthur Latham Perry, the foremost proponent of the approach in the USA. It was resurrected as a central pillar of Austrian economics by Ludwig von Mises in his major treatise on economics (Mises, 1949). Mises embedded catallactics in the wider discipline of 'praxeology', the science of human action, thus setting out the core of the modern Austrian economics research program.

Only in the Virginian political economy program does catallactics play a significant role in public choice analysis, and then almost exclusively at the constitutional level. Under the intellectual leadership of James M. Buchanan and Gordon Tullock, catallactics has been renamed as the contractarian approach (Buchanan, 1987) and has drawn its intellectual inspiration more from the writings of Knut Wicksell than from Ludwig von Mises. It made its initial dramatic entry in 1962, arguably in the most important single contribution to public choice, *The Calculus of Consent* (Buchanan and Tullock, 1962). Remarkably enough, this text has become a focal point of hostile attack by one of Ludwig von Mises's most devoted pupils, Murray Rothbard, precisely because of its reliance upon the catallactic method (Rothbard, 1989). In *The Calculus of Consent*, Buchanan and Tullock attempted to delineate the logical foundations for constitutional democracy vested in universal consent, rather than in conflict, conquest and subjugation of some individuals by others. By assuming that individuals make constitutional decisions under conditions of generalized uncertainty, they claimed to derive, on the basis of strict methodological individualism, universal consent for constitutional rules designed to minimize the joint cost of external effects and of collective decision making. Simultaneously, such universal consent was seen as defining the range and extent of collective action, and as delineating the constitutional constraints within which the ordinary processes of politics must take place.

Rothbard's attack on this model claims that it is predicated on a fatally flawed attitude towards government, in that it fails to grasp the crucial distinction between a voluntary exchange, where both parties gain, and a coerced exchange, where one party gains at the expense of the other. Instead of

regarding the state as the organization of the political means – as the systematization of theft and coercion on a grand scale – the Virginian public choicers are viewed by Rothbard as regarding the state much more benignly, as merely one large firm, albeit a particularly inefficient firm. Rothbard is categorically incorrect in this reading of *The Calculus of Consent*. For Buchanan and Tullock, the state is the product of universal consent, offering gains from trade to those who otherwise must exist in the Hobbesian state of nature, suffering the privations brought on by the war of each against all. Its existence, as referee, as provider of public goods and as rectifier of market failure, is based entirely on rules that are endorsed universally in the constitutional settlement. There can be no coercion within this concept of government, as long as the parchment of the constitution is systematically upheld. Evidently, Rothbard confuses the logic of constitutional democracy with the malignancy that is *realpolitik*.

The relevant criticisms of Buchanan and Tullock's catallaxy of politics lie elsewhere. First, they require all individuals residing within prespecified geographical limits to participate in the constitutional settlement. No one is free to remain in the state of nature. In this sense, the constitutional settlement is a political and not a private act, in contravention to the Lockian tradition. Second, there is no right of secession in the contractarian constitution, no prospect for disaffected citizens either to return to the state of nature or to Balkanize into independent nation-states. Third, there is no recognition that real-world parchments are of a very different texture from that of any calculus of consent, the derivative at best of a transient supermajority, ultimately dependent for its survival upon the competing guns of often minority interests. All of these issues have been reviewed in detail by Virginian scholars (Rowley and Wagner, 1990; Rowley, 1993c; Wagner, 1993) from a perspective not too distant from Rothbard's own libertarian thrust. From such perspectives, real political markets behave in a manner much closer to Rothbard's Satan than to any calculus of consent, largely by dishonoring the constitutional calculus.

Political markets

In the public choice approach, politicians are modeled as providing a brokerage function in the political market for wealth transfers. Individual voters and special interest groups capable of effective political organization 'demand' such transfers evidencing willingness to pay in some combination of votes and campaign contributions. Other voters and interest groups, less capable of effective organization, 'supply' such transfers, albeit at some price in terms of displaced votes and campaign contributions. Politicians effect market equilibrium, balancing benefits against costs at the margin, in order to maximize their own utility functions, weighted variously in terms of expected wealth, expected votes and ideology.

The concepts of 'demand' and 'supply', in this stylized model, require a somewhat special interpretation. Demand is forthcoming only when the wealth transfers that are sought are perceived to carry a positive net present value to those concerned. Such positive returns represent rent, and not profit, insofar as overall wealth is not enhanced by political transfers. The existence of rent induces rent-seeking behavior which dissipates wealth by diverting scarce resources to non-productive ends (Tullock, 1967). The rent seekers who predictably represent demand are not limited to the ultimate beneficiaries of wealth transfers. Typically, they are joined by those departments of government and those government-dependent private contractors whose budgets and/or profits can be augmented by engaging in the political transfer program.

Supply consists of the unwillingness or inability of those from whom wealth transfers are sought, at the margin, to protect themselves with countervailing offers of money transfers or votes to the politicians who broker policies. The existence of supply is fully consistent with the existence of inframarginal rent protection outlays, since political market equilibrium is not necessarily equivalent to political market domination. It also has connotations of coercion that are absent in private markets, hence Rothbard's vigorous defense of anarchy.

When Duncan Black discovered the median voter theorem, he truly believed that he had identified a unique connection between the voting process and the actual outcomes of committees and direct elections. Unfortunately, this initial confidence was misplaced, as Black's subsequent work, consolidated by Kenneth Arrow, quickly established. Separately, they identified a set of mathematical problems sufficiently difficult to suggest that democracy is either an illusion or a fraud (Tullock, 1987), most notably because of the prevalence of vote cycles and the consequential path dependence of the vote mechanism. If cycles exist, in essence there are two possibilities when we observe such voting bodies as The House of Representatives in the USA or The House of Commons in the UK and review the outcome. The first is that the outcome is random and due to chance, since the order of the agenda dictates the outcome and no one realizes this within the chamber. The alternative is that the outcome is manipulated by some evil agenda setter who understands the situation and uses it to dictate solutions. Among public choice scholars, Gordon Tullock (1987) is almost a lone voice playing down the significance of this problem. No doubt Murray Rothbard would be sympathetic to the views of Arrow on this matter and would deploy the cycling problem as further evidence of the evils of democracy.

Even should single-peakedness conditions hold, the uniqueness of the median voter theorem is suspect once the ideal conditions posited by Anthony Downs (1957) are relaxed. If elections comprise three or more competing

parties, or if abstentions due to alienation are possible, or if policy issue space is multidimensional, or if political parties are immobile across policy issue space, or if voters are rationally ignorant, the median solution is much less dominant, even if an equilibrium should exist. Furthermore, there is no guarantee that a government elected on a median voter platform will honor its political pledges. As the 1992 Clinton presidential victory demonstrates, elected officials may cynically jettison *all* their electoral pledges immediately following an election and rely upon voters' failing memories to carry them forward to subsequent electoral success. As long as they recognize the logic of collective action (Olson, 1965) and concentrate political benefits on well organized special interest groups while dispersing the political costs across the electorate at large, such deviant politicians stand every chance of continuing success in the rent-seeking environment of democratic politics.

Conclusions

For Rowley and Wagner (1990) a knowledge of public choice, drawn largely although not exclusively from neoclassical economic analysis, confirms a dislike of big government that is shared, perhaps for different reasons, by most scholars of the Austrian school. For us, the principle of liberty, linked to the lessons of public choice, leads not to the parchment of even some widely endorsed *limited* transfer state, but rather to the classical liberal doctrine of the *minimal* state, in which government is small, heavily constrained and acts only as nightwatchman for an otherwise unconstrained market economy. Such a solution would not be enough for Murray Rothbard; but it is a long way further in his direction even than the position of contractarian public choicers like Buchanan and Tullock, who are not known for their love of non-market decision making.

See also:

Chapter 49: Interventionism; Chapter 42: The economic theory of regulation; Chapter 62: Political business cycles

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