

The Role of the State

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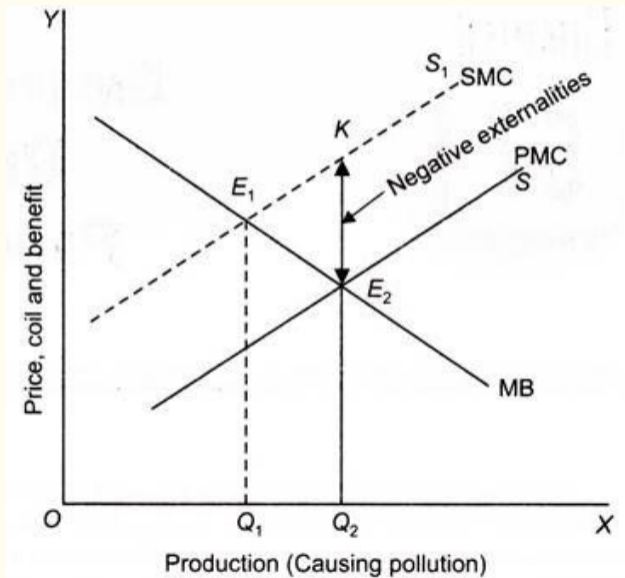
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Is there a dichotomy?

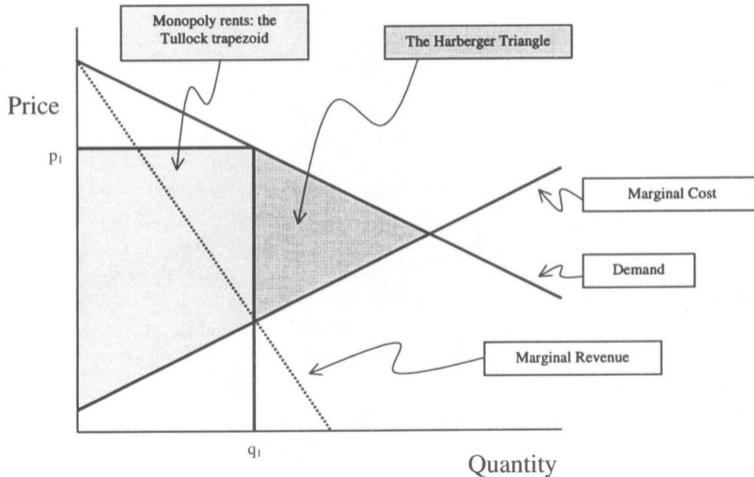


State as benevolent planner



State having its own incentive problems?

The Harberger triangle and the Tullock trapezoid with a monopoly



State, market, and welfare losses



(a) Arthur Pigou



(b) Ronald Coase



(c) Gordon Tullock



(d) Anne Krueger

Political philosophy

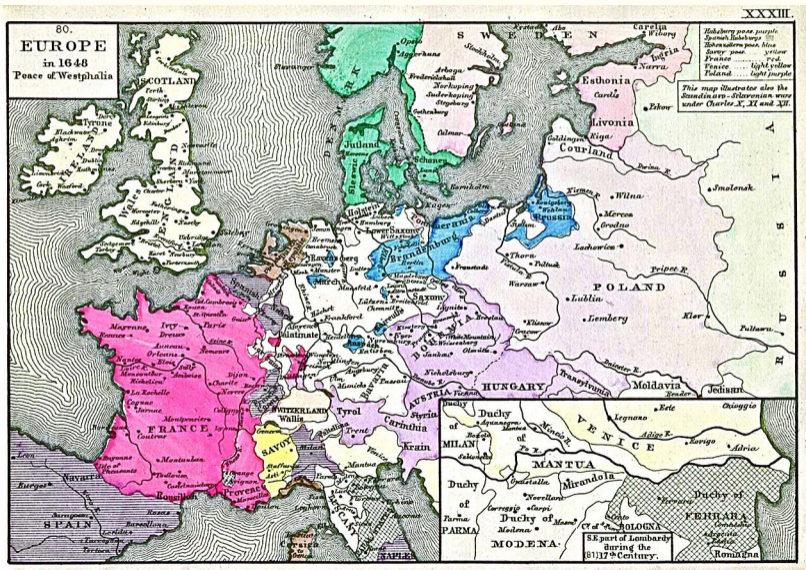
What is a state?



Key questions

- What is a State? What is its role?
- How/why did it arise, how/why it persists, and how/why it fails?
- Is there a positive correlation between the advancement of human civilization and the degree of its organization through a State?

Origin of the idea of Nation-State



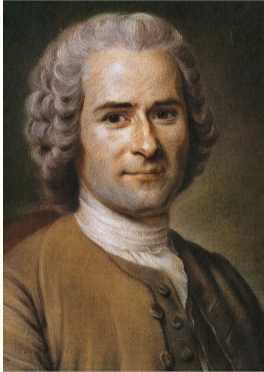


(a) Samuel Pufendorf

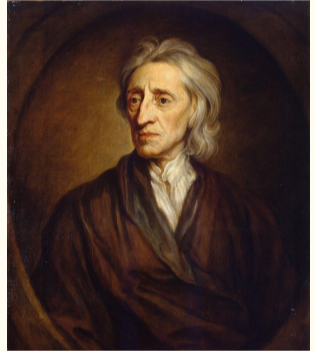
Political philosophy: Social contract



(a) Thomas Hobbes

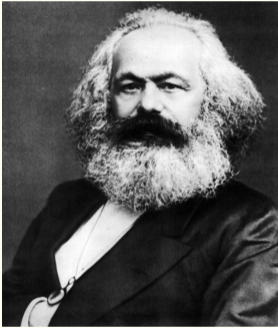


(b) Jean-Jacques Rousseau



(c) John Locke

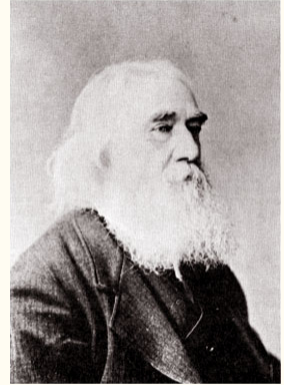
Political Philosophy: Socialism and anarchism



(a) Karl Marx



(b) Mikhail Bakunin



(c) Lysander Spooner

Theories of the origins and development of the state

What is a State?

Max Weber, 1919

“human community that (successfully) claims the monopoly of the legitimate use of violence within a given territory.”

- Depends on the definition of territory.
 - At a world stage, there is no State. At a local stage, States may exist everywhere.
- Coercion/compulsion distinctiveness?
 - Difference between private clubs and States

Weber provides a theoretical definition for a historical category.

- What do States do?
 - War and provision of public goods.
- How do States finance themselves?
 - Domain and taxing States.

What do States do?

Charles Tilly, 1975

"War made the State, and the State made war."

Expenditure on Warfare

MILITARY EXPENSES AS A PERCENT OF ANNUAL GOVERNMENT SPENDING: ENGLAND, FRANCE, PRUSSIA (1688–1790)

Country and Period	Minimum	Median	Maximum
England 1688–1790	25	48	84
France 1600–1688	19	73	94
Prussia 1688–1789	68	90	98

Note: Military expenses include subsidies for allies, but not debt service, even though the sole purpose of borrowing was to pay for wars. Debt repayments are also excluded to avoid double counting. Figures for England concern net public expenditures.

Source: Mitchell and Deane 1962, pp. 389–391 (England); <http://esfdb.websites.bta.com> (data on seventeenth-century French expenditure supplied Richard Bonney); <http://esfdb.websites.bta.com/table.aspx?resourceid=11768> (data for Prussia gathered by Martin Körner).

Role of the State according to Tilly

- Warring: Eliminate external threats and rivals to their power.
- Consolidation: Eliminate internal threats and rivals to their power.
- Protection: Eliminate threats to the general population.
- Extraction: Secure resources from the general population.

A subtle division among social classes emerges: The elites who wield influence over the State, contrasted with the remainder who contribute to its maintenance.

Joseph Schumpeter, 1918

“the fiscal history of a people is above all an essential part of its general history. An enormous influence on the fate of nations emanates from the economic bleeding which the needs of the state necessitates, and from the use to which the results are put.”

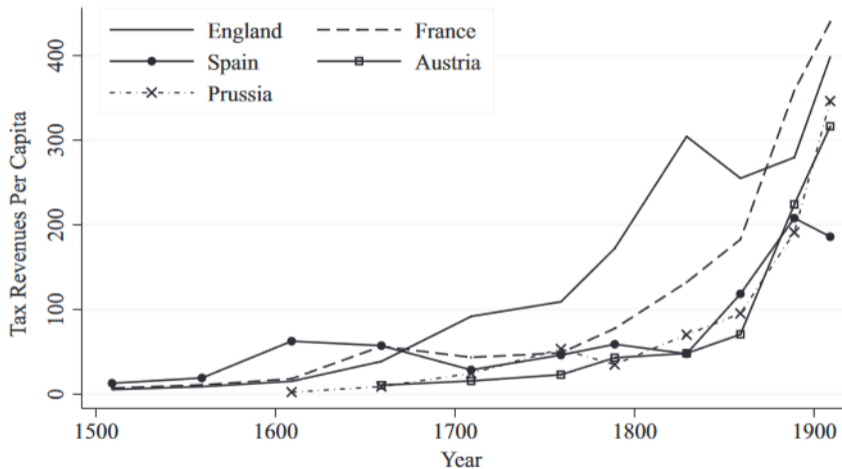


Fig. 1. Log Tax revenues per capita for five European powers. Source: [Karaman and Pamuk \(2013\)](#).

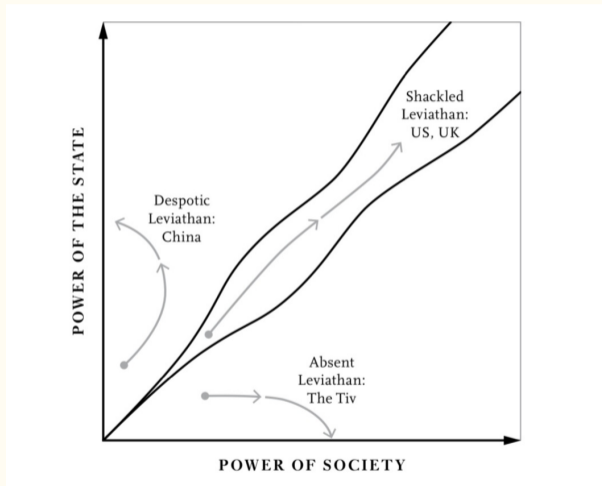
St Augustine, City of God (5th Century)

“Indeed, that was an apt and true reply which was given to Alexander the Great by a pirate who had been seized. For when that king had asked the man what he meant by keeping hostile possession of the sea, he answered with bold pride, What you mean by seizing the whole earth; but because I do it with a petty ship, I am called a robber, while you who does it with a great fleet are styled emperor.”

Mancur Olson's framework to understand origins of the State:

- Roving bandits predate and keep on the move.
- Stationary bandits predate and stay in place.
- Stationary bandits are incentivized to allow their prey to amass wealth, thus initiating a gradual alignment of incentives between both parties. These dynamics sow the seeds of transition from warlords to governors.

Acemoglu-Robinson's narrow corridor



Madisonian paradox

James Madison, The Federalist No. 51

“If men were angels, no government would be necessary. If angels were to govern men, neither external nor internal controls on government would be necessary. In forming a government which is to be administered by men over men, the great difficulty lies in this: you must first enable government to control the governed; and in the next place oblige it to control itself ”

Juvenal, Satires(2nd Century AC)

“Quis custodiet ipsos custodes?”

The basic problem of managing violence is to achieve cooperation.

- Natural state \Rightarrow Violence trap.
- Limited access orders \Rightarrow Coalition rules at the expense of others.
- Open access orders \Rightarrow Clear rule of law.

Table 1. Supply and demand for public-order CEIs

		<i>Organic, private-order CEIs (technological factors) as determinants of demand for public-order CEIs:</i>		
<i>Coercion-constraining institutions as determinants of ability to effectively supply public-order CEIs:</i>		<i>Low</i>	<i>High</i>	
	CCIs based on administrative structure	CCIs based on balancing coercive powers.	Communalism/ Segregation (Lower demand if small, static economies and low gains from impersonal exchange.)	Individualism/ Integration (Higher demand if large, dynamic economies and higher gains from impersonal exchange.)
<i>Low</i>	Absent state: Thin administration controlled by the state.	Mutual deterrence: No ruler. Asset holders coercive power mutually deters abuse.	Low demand, low ability to effectively supply. <i>E.g., China under the Qian and the First Muslim Empire. Communalism and an absent state.</i>	High demand, low ability to effectively supply.
<i>Medium</i>	Delegation: The state's administration is controlled by the asset holders.	A ruler with independent coercive power: Balanced by the asset holders coercive power.	Low demand, medium ability to effectively supply.	High demand, medium ability to effectively supply.
<i>High</i>	Self-governance: Administration provided by autonomous units controlled by the asset holders.	A ruler with conditional coercive power: Asset holders provide the ruler with coercive power.	Low demand, high ability to effectively supply.	High demand, high ability to effectively supply. <i>E.g., England: individualism. Autonomy with economic and coercive powers. A ruler with conditional coercive power.</i>

State capacity and social liberalism

The scope of the state

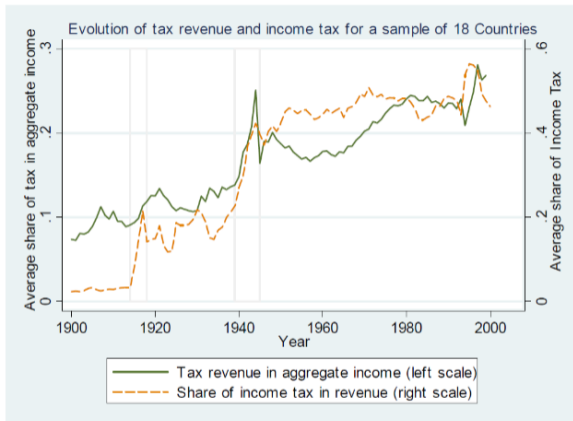
Once we see the State as a desirable way of organizing human societies, we still need to discuss its proper scope and its potential for transforming itself and the society from which it arose.

- Is the State an exogenous agent or endogenous agent?
 - Public Finance, Edgeworth's take: State as an entity that intervenes in the economy to maximize a social welfare function.
 - Public Choice, Wicksellian take: State as an institutional framework that governs human relationships.

Knut Wicksell, 1896

“taxation in the modern state has come more and more to depend upon the legislative assembly, which is nothing if it be not the representative of the interests of the taxpayers. It would be strange indeed if taxation by interested parties should not result in taxation according to interest.”

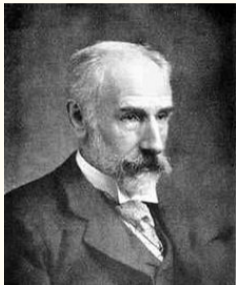
Increase of taxing capacity



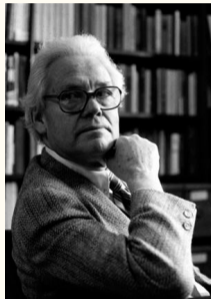
Taxes and share of income tax over time

Countries in time series are: Argentina, Australia, Brazil, Canada, Chile, Colombia, Denmark, Finland, Ireland, Japan, Mexico, Netherlands, New Zealand, Norway, Sweden, Switzerland, United Kingdom, and the United States.

Public finance and public choice frameworks



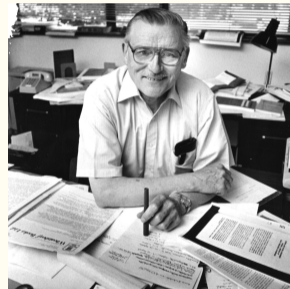
(a) Francis Edgeworth



(b) Richard Musgrave



(c) Knut Wicksell



(d) James Buchanan

How we perceive the State has changed?

Process of legitimization:

- Is it an illegitimate organization extracting wealth for self-enrichment or an organization levying taxes to fund public goods?
- Are we paying tributes to a lord out of fear, or are we paying taxes to the IRS because of a social agreement?
- Both an economic and cultural transformation needs to occur:
 - Recognition of the advantages of organization through state legislation, which aims to minimize transaction costs.
 - An increasing identification of the government with cultural traits associated with the people that support said government (Nation-state).

From illegitimacy to legitimacy

St. Augustine, City of God (5th Century)

“Justice being taken away, then, what are kingdoms but great robberies? For what are robberies themselves, but little kingdoms? The band itself is made up of men; it is ruled by the authority of a prince, it is knit together by the pact of the confederacy; the booty is divided by the law agreed on. If, by the admittance of abandoned men, this evil increases to such a degree that it holds places, fixes abodes, takes possession of cities, and subdues peoples, it assumes the more plainly the name of a kingdom, because the reality is now manifestly conferred on it, not by the removal of covetousness, but by the addition of impunity.”

Taxes and legitimacy

Panel B. International comparison of per capita tax revenue (grams of silver)

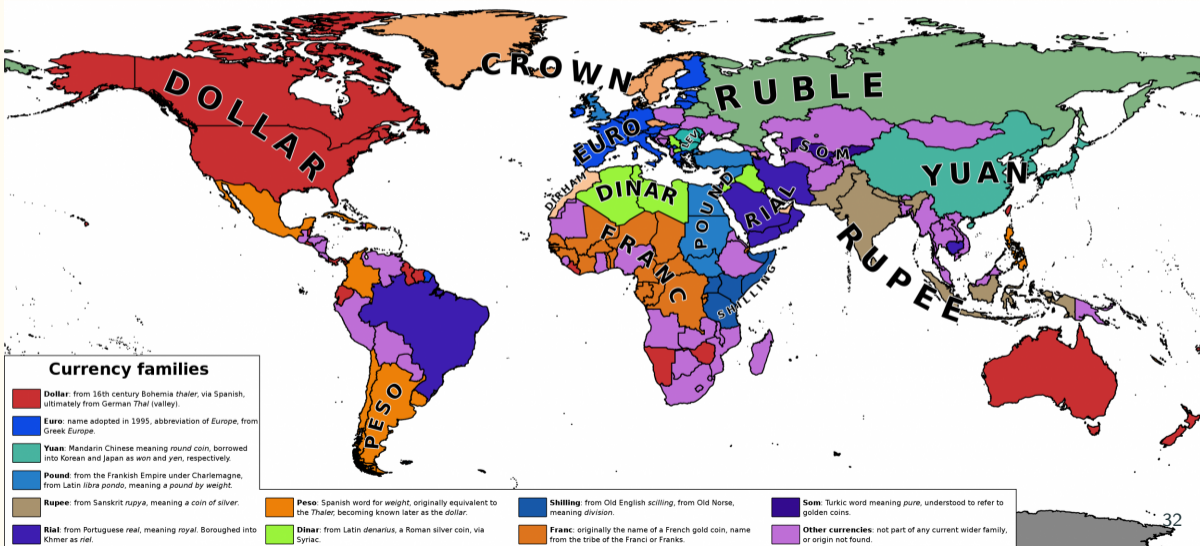
	<u>Absolutist Regimes</u>					<u>Constrained Regimes</u>	
	China	Ottoman	Russia	France	Spain	England	Dutch Rep.
1650-99	7.0	11.8		46.0	35.8	45.1	
1700-49	7.2	15.5	6.4	46.6	41.6	93.5	161.1
1750-99	4.2	12.9	21.0	66.4	63.1	158.4	170.7
1800-49	3.4					303.8	
1850-99	7.0					344.1	

Panel C. Per capita revenue expressed in days' wages for unskilled workers

	<u>Absolutist Regimes</u>					<u>Constrained Regimes</u>	
	China	Ottoman	Russia	France	Spain	England	Dutch Rep.
1650-99		1.7		8.0	7.7	4.2	13.6
1700-49	2.3	2.6	6.4	6.7	4.6	8.9	24.1
1750-99	1.3	2.0	8.3	11.4	10.0	12.6	22.8
1800-49	1.2					17.2	
1850-99	2.0					19.4	

Sources: Brandt et al. (2014); Dincecco (2009) for absolutist/constrained distinction

Culture and legitimacy



Building cultural identity

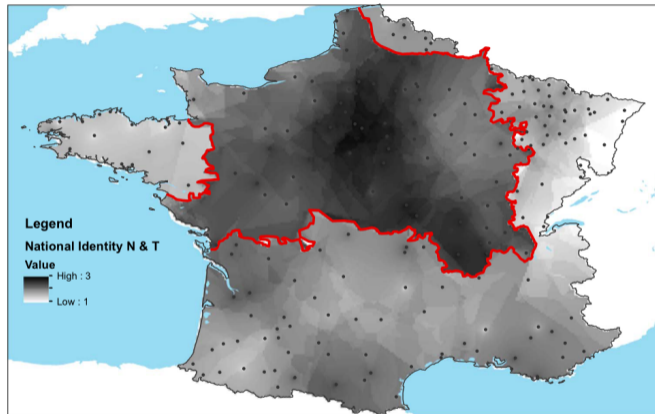


Fig. 2. *National Identity* in the 1789 General Cahiers. Darker color represents greater identification in the Cahiers by the Nobility and Third Estate with either the 'King' or 'France' according to Hyslop (1934). Each grid point in the map is assigned a value based on the inverse-weighted distance of surrounding 12 cities that sent in Cahiers (exponent of distance used is the default of 2). The Cinq Grosses Fermes region is delineated in red and treated as a barrier.

Can the State change the rules of the game?

Aristotle, *Nicomachean Ethics* (4th Century BC)

“lawgivers make the citizens good by training them in habits of right action—this is the aim of all legislation, and if it fails to do this it is a failure; this is what distinguishes a good form of constitution from a bad one”

Adam Smith, *Theory of Moral Sentiments* (1759)

“The man of system... is apt to be very wise in his own conceit; and is often so enamored with the supposed beauty of his own ideal plan of government, that he cannot suffer the smallest deviation from any part of it... He seems to imagine that he can arrange the different members of a great society with as much ease as the hand arranges the different pieces upon a chess-board. He does not consider that in the great chessboard of human society, every single piece has a principle of motion of its own, altogether different from that which the legislature might choose to impress upon it.”

Justification for increasing taxes: Wicksell's unanimity rule

Knut Wicksell, 1896

"Whenever this or that type of public service is expanded, the individual will reap a certain utility, be it of a selfish or altruistic kind; and this utility may appropriately be described as the marginal utility of the public service for our individual. Now it is correct that efficiency requires approximate equality between this marginal utility and the price (or tax) paid therefore. Otherwise the individual would desire a restriction or further expansion of the public service and related expenditure. However, the actual scope of the public service is not determined by the evaluation of the single individual, but by that of all (or at least all voting) members of the group. Equality between the marginal utility of public goods and their price cannot, therefore, be established single individual, but must be secured by consultation between him and all other individuals or their delegates. How is such consultation to be arranged such that the goal may be realized."