

# **The Political Economy of the Political Economy of Reforms**

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# Question

“What are the main political economy reasons for **insufficient reform progress**?”

- The obvious answer is because governments do not think they are going to benefit from them.
- Thus, the real question is why they do not think so. Possible answers:
  1. Ignorance/bounded rationality
  2. short-termism
  3. reforms are not really beneficial
  4. reforms are overall beneficial but politically influential groups lose, while the majority benefits

“**Which European rules and policies** have supported incentives for national governments to do beneficial reforms and which have more likely been counterproductive?”

# Positive or Normative Approach?

## Public finance:

Positive: what happens when I tax sugar?

Normative: how to design a tax on sugar so to maximize a given social welfare function

## Political economy:

Positive: how rational, self-interested politicians and voters make decisions (e.g., to introduce a tax on sugar)

- If the question is “how to design rules that maximizes the speed of adoption of a tax on sugar” am I doing positive or normative PE?
- If normative, who decides the preferences?

# What Are the Limits?

- If voters reject a tax on sugar, should we try to find ways to approve a tax on sugar against voters' will?
- Justifications:
  - Voters are uninformed
  - Information is purposefully distorted by vested interests (soda pops lobby)
  - Even if informed, voters are myopic/bounded rational
  - Even if not myopic, they are addicted
- What are the limits?
  - Should we decide that forcing people to exercise every morning is good for them and find ways to impose it to people?
- May be voters are wiser (Sapienza and Zingales, 2013)

# Jonathan Gruber on ACA

“This bill was written in a tortured way to make sure [the Congressional Budget Office] did not score the mandate as taxes. If CBO scored the mandate as taxes, the bill dies. OK? So it’s written to do that. In terms of risk-rated subsidies, if you had a law which said healthy people are going to pay in — you made explicit that healthy people pay in and sick people get money — it would not have passed. OK? **Lack of transparency is a huge political advantage.** And basically, call it the stupidity of the American voter or whatever, but basically that was really, really critical to get the thing to pass. Look, **I wish ... we could make it all transparent, but I’d rather have this law than not.**”

Jonathan Gruber at the 24th Annual Health Economics Conference at the University of Pennsylvania in October 2013

<http://www.snopes.com/politics/medical/gruber.asp>

# From Sugar To Catalonia

- From an economic point of view, Catalonia will lose from becoming independent
- Assume that the majority of Catalan people wants independence in spite of the economic losses
- Should we design institutions trying to make it difficult for this to happen, because they do not know what they are doing?
- Who are we?
- Are we playing the benevolent dictator (God)?

# Back to the Original Question

“What are the main political economy reasons for **insufficient reform progress**?”

“Why can governments sometimes get away for so long without addressing crucial challenges with **structural reforms and better policies**?”

- Just a positive analysis or is there a hidden normative agenda?
- If the first, who decides on what are the “better policies”?
- A political economy of political economy?

# Mandate of the Conference

“We would appreciate, if in your presentation you could address reforms and economic policies that ...

(i) are important for long-term (inclusive) growth, resilience and/or social fairness in the EU and in particular euro area countries”

- What is the most important reform to guarantee **long-term (inclusive) growth, resilience and/or social fairness in the EU?**

# Risk Sharing at the Eurozone Level

- All economists agree that a common currency area with asymmetric shocks requires a substantial amount of fiscal redistribution to amortize those shocks
- Why 20 years after the creation of the euro and after an enormous asymmetric shock in great part caused by the imperfect design of the common currency we still do not have any serious reform on this front?

# Political Constraints

- “Ex ante” vs “ad interim”
- Even if risk sharing does not mean subsidizing, rich countries fear they might have to pay for poorer ones
- Exactly like richer Americans in the healthcare debate
- We know why in the USA was so difficult to pass a comprehensive healthcare package
- Why is it so difficult in Europe to pass a risk-sharing plan?

# What To Do?

- I am not a political scientist
- But I dare to advance the hypothesis that the current intergovernmental approach favors the largest/more powerful countries
- The solution is very simple, we need more democracy in the EU (and eurozone)
- As economist, it is above my pay grade to figure out how to achieve it