
The Grants Economy and Collective Consumption

Edited by

R. C. O. MATTHEWS

and

G. B. STAFFORD

for the

INTERNATIONAL ECONOMIC ASSOCIATION

The Grants Economy and Collective Consumption

Proceedings of a Conference held by the
International Economic Association at
Cambridge, England

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R. C. O. MATTHEWS

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G. B. STAFFORD



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Most of economics is written on the implicit assumption that goods and services are produced by enterprises that sell them in a market and thus recover the costs of their production, expanding if demand requires it, contracting if demand is lacking, always under the guidance of the market. But in reality a large proportion of all goods and services are produced and consumed outside the market system. At least until very recently this proportion has constantly increased. Sometimes these goods and services are provided free. Sometimes a charge is made. Sometimes it is expected that charges will come near to covering costs and sometimes it is recognised that a service must be considerably subsidised. In addition a large number of educational and cultural activities depend wholly or very largely on grants from a variety of grant-giving institutions.

The International Economic Association Conference that is recorded in this book was in large measure breaking new ground. It aimed to establish, for a variety of countries, the extent to which collective consumption prevails, the criteria they use to determine what shall be in the market sector and what in the collective sector, how to hold the balance between collective and personal consumption and yet provide incentives, the principles that should determine whether in a particular case services should be provided free or a charge made, and more generally the defects and difficulties of operating a system of collective consumption.

The countries whose problems, experiences and thinking are analysed range from the USA and Switzerland as predominantly private enterprise countries with, nevertheless, a considerable grants economy, through West Germany, the United Kingdom, the Netherlands, Norway and Japan as mixed economies, to Yugoslavia, Poland, Hungary and the USSR, where in predominantly socialist economies many of the same problems of the financing and pricing of collective consumption and the division between collective and individual con-

sumption equally arise. And apart from these countries, some of the relevant experience of a number of others has been contributed by participants in the course of the discussions, recorded by G. B. Stafford, which as in all IEA volumes are almost as interesting as the papers.

The authors include K. Boulding (the first to explore this subject), M. A. H. Dempster, H. Leibenstein (USA), B. Frey (Switzerland), A. Boltho (FRG), L. Pliatsky (UK), A. J. Meys (Netherlands), A. Sandmo (Norway), H. Uzawa (Japan), E. I. Kapustin (USSR), M. Pohorille (Poland), R. Hoch (Hungary).

R. C. O. Matthews, who as chairman of the Programme Committee had planned the conference, contributes an overview of the issues, written beforehand and discussed in the final session of the Conference. He and G. B. Stafford, in the introduction to the book, sum up the work of the Conference in retrospect.

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The Conference was held in Sidney Sussex College, Cambridge. To the Master and Fellows of the College and to our other hosts in Cambridge University we owe the pleasure of meeting in a most congenial academic setting.

Programme Committee

R. C. O. Matthews (Chairman)

S. Tsuru (President of IEA)

K. Boulding

B. Csikós-Nagy

L. Johansen

P. Maillet

E. I. Kapustin

List of Participants

- Professor Tamacs Bacskai, National Bank of Hungary, Budapest, Hungary
- Mr Andrea Boltho, Magdalen College, Oxford, England
- Professor Dieter Bös, Institute für Gesellschafts und Wirtschaftswissenschaften der Universität Bonn, West Germany
- Professor Kenneth Boulding, Institute of Behavioural Science, University of Colorado at Boulder, USA
- Dr Michael Dempster, International Institute for Applied Systems Analysis, Laxenburg, Austria
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- Professor Bruno Frey, Institute for Empirical Economic Research, University of Zurich, Switzerland
- Professor Horst Hanusch, Lehrstuhl für Volkswirtschaftslehre V, Augsburg, FRG
- Dr Robert Hoch, MTA Közgazdasgtudományi Intézet, Budapest, Hungary
- Dr Zoran Jašić, Ekonomski Institut, Zagreb, Yugoslavia
- Dr Pero Jurković, Ekonomski Institut, Zagreb, Yugoslavia
- Professor E. I. Kapustin, Institute of Economy of the Academy of Science of the USSR, Moscow, USSR
- Mr Michael Kaser, St Antony's College, Oxford, England
- Professor T. S. Khachaturov, Association of Soviet Economic Scientific Institutions, Moscow, USSR
- Professor Rudolf Klein, University of Bath, Bath, England
- Professor Harvey Leibenstein, Harvard University, Cambridge, Massachusetts, USA
- Professor Pierre Maillet, Centre Interuniversitaire de Recherches en Science Humaines, Lille, France
- Professor Gunter Manz, Hochschule für Ökonomie Bruno Leuschner Berlin, GDR
- Mr Robin Matthews, Clare College, Cambridge, England

- Mr Th. A. J. Meys, Director General of the Budget, Ministry of Finance, The Hague, Netherlands
- Professor Franco Modigliani, Alfred P. Sloan School of Management, Massachusetts Institute of Technology, Cambridge, Massachusetts, USA
- Professor H. M. A. Onitiri, Nigerian Institute of Social and Economic Research, University of Ibadan, Nigeria
- Professor J. J. Paunio, Institute of Economics, University of Helsinki, Finland
- Sir Leo Pliatzky, Department of Trade, London, England
- Professor Maksymilian Pohorille, Central School of Planning and Statistics, Warsaw, Poland
- Professor Sir Austin Robinson, Cambridge University, England
- Professor Agnar Sandmo, The Norwegian School of Economics and Business Administration, Bergen, Norway
- Dr Bernard Stafford, University of York, England
- Professor Shigeto Tsuru, The Asahi Shimbun, Tokyo, Japan
- Professor Victor Urquidi, El Colegio de Mexico, Mexico
- Professor Hirofumi Uzawa, University of Tokyo, Japan
- Mr H. Verwayen, Commission for the Development of Policy Analysis, The Hague, Netherlands

List of Observers

- Professor Dong Fu Reng, Institute of the Chinese Social Science Academy
- Mr Peter Lengyel, UNESCO, Paris

Introduction

R. C. O. Matthews and G. B. Stafford

The economic analysis of collective consumption, whether in theoretical, empirical or practical terms, has not kept pace with the growth in collective consumption's importance in national economies. Public macroeconomics offers an analysis of the effects on the economy of public expenditure for collective consumption without any consideration of why collective consumption has grown as it has; whereas much of public microeconomics aims to identify optimal reallocations of resources devoted to collective consumption without asking whether existing political and bureaucratic procedures will result in outcomes consistent with prescribed plans.

With such discrepancies in mind the International Economic Association chose collective consumption as the topic for its 1979 Round-table Conference. Many, though not all, of the problems involved are common to capitalist economies and to socialist ones, and the topic thus seemed a particularly appropriate one for the International Economic Association, whose gatherings are among the chief forums for serious discussion between economists of East and West. The aim set out at the planning stage of the conference was to analyse the positive and normative aspects of the long-run development of collective consumption, taking into account the political and bureaucratic methods by which its amount and composition are determined. The committee was pleased to secure papers from two very senior civil servants, Director-General Meys and Sir Leo Pliatzky, thus following a precedent in some earlier IEA Round-table Conferences of bringing economists and practitioners together.

Collective consumption can be defined in various ways, each appropriate for different purposes. The central concept used in the conference was goods or services provided free of charge, or nearly free of charge, to the beneficiary (a much wider concept than public goods in the strict Samuelsonian sense). In most of the papers and discussion sessions reported in this volume, the measure of collective consumption turned out to be not much different from public authorities' current

expenditure on goods and services, although there were some divergences of view: thus some argued that public transfers on income maintenance should be regarded as collective consumption on the grounds that they provide the benefit of security, and Boltho argued that defence expenditures should be excluded.

However, as is shown in Boulding's concept of the grants economy and in Hoch's and Kapustin's references to personal collective consumption, the issue of definition is really a broader one. Supply without charge by the state is not the only alternative to a market arrangement for individual purchases and private consumption, nor is it the only way in which what might reasonably be called collective consumption is organised in real life. Charitable organisations and clubs are important in capitalist countries, and in one socialist country, Yugoslavia, the 'communities of interest' that are the chosen vehicle of collective consumption are actually seen as a way of moving towards the Marxian goal of the withering away of the state. Moreover, in capitalist countries, a considerable amount of provision that could be made by the state is made also or instead by employers to their employees, both in the form of provision in kind, such as canteen facilities and sports grounds, and in the form of income-maintenance, especially pensions. Provision by employers (enterprises) is a still more important feature of arrangements in socialist countries. The fact that enterprises in socialist countries are themselves organs of the state makes for difficulties in defining and measuring the extent of state provision there.

This raises some important questions about the positive and normative relationship between governmental and non-governmental collective consumption in capitalist and socialist economies. That relationship is touched on at various points in this book, but it is not a central theme and requires further exploration. It is not difficult to see a direction such an initiative might take, for there is an obvious relationship between the theory of clubs developed by western economists and the concept of personal collective consumption developed in the papers of Hoch and Kapustin.

It is, however, the great rise in governmental collective consumption that has brought the subject into prominence. This rise has been a long-run trend, apparent already before the Second World War, but more rapid in the post-war period than it had been before. Trends in western countries are well documented in Boltho's paper. The conference papers unfortunately do not include any equally comprehensive data on socialist countries, but relevant material is provided by Hoch and Kapustin and in the comment by Kaser on pp. 328–9. These data leave it

rather unclear whether socialist countries have experienced a trend rise in collective consumption's share in national income comparable to that in the West. The historical circumstances in the socialist countries were rather different from those in capitalist countries. The period of rationing and shortages lasted much longer after the Second World War than in capitalist countries, and the transition from that period provided one force making for some actual reduction in collective consumption's share.

A major theme in the conference discussions was the normative rationale of collective consumption. A difference of view emerged between eastern and western participants that had little to do with the difference between capitalist and socialist methods of *production*. Participants from capitalist countries all tended to see the rationale as the maximisation of the sum of individual utilities in circumstances where the market, for one reason or another (including income distribution), failed to bring that result about. The socialist economists were not in complete agreement among themselves on the question, but they were unanimous that the welfare of the people is inadequately represented by preferences revealed in the market. Some of them, moreover, while firmly disclaiming paternalism, were unwilling to agree that the welfare of the people is identical to the sum of the welfare of individuals. Thus eastern participants argued that individual preferences in capitalist economies are distorted by business interests and the media (p. 106) and more generally, and in any case, that individual preferences must be assessed in terms of their consistency with well-defined goals relating to the development of the whole society (pp. 72–3). As a consequence they insisted that a variety of political as well as economic channels are needed in order to make known what it is that welfare consists of. These differences reflect in part the differing philosophical origins of the two systems of thought. Western economics is deeply rooted in Benthamite individualism. Socialist economics goes back, through Marx, to Hegel.

The honours in this debate were not all on one side. Participants from western countries expressed suspicion of anything providing a pretext for despotism, however paternalistic. But they were conscious that utility-maximisation is a jejune psychological postulate. At one point a western participant said that he tended to adopt the axiom of utility-maximisation mainly out of deference to the wishes of American journal editors. His East European neighbour at the table was then heard to say 'Oh, so you have trouble with orthodoxy too'. Boulding came nearest to the concerns of the socialist economists when he remarked that one of

the reasons for struggling to avoid the manifest potential pathologies of the grants economy is that, if the grants economy itself becomes discredited, the legitimacy of the whole social system comes under threat. The issues here stretch far beyond the realm of collective consumption as normally defined, and an easy resolution is not to be expected.

The extent of common ground between eastern and western participants was much greater on the issue of the practical difficulties encountered in implementing programmes of collective consumption. Well-recognised in capitalist economies are the problems of the choice between grants in kind and grants in cash, of the effects of grants of all kinds on incentives, and of unequal access to and overprovision of services provided free. The papers by Hoch, Pohorille and Kapustin and the comments by Bacsikai (p. 136) gave valuable insights into how such problems manifest themselves in socialist economies, and show that agreed solutions are no more available in the East than in the West.

None of the western papers at the conference was primarily concerned with the effects of the growth of collective consumption, as opposed to its causes. Nor did the conference include any representatives of the extreme school of thought that sees collective consumption itself as a pathological phenomenon, rather than as a phenomenon susceptible of pathological disorders. Dempster and Wildavsky perhaps came nearest to that position, but not on ideological grounds – rather on the grounds that the collective organisation of consumption is not well adapted to respond to economic change.

Be that as it may, all sensible people must agree that collective consumption is a major constituent of national income and is likely to remain so. Hence theoretical analysis of how it is and ought to be determined is a major item on the agenda of economists. Two quite different approaches exist, both represented in this volume. One is optimisation theory, well represented by Sandmo's contribution. This approach is normative and is in the mainstream of welfare economics. The other is the theories of public choice (Frey, Dempster and Wildavsky) and of bureaucracy (Leibenstein), which in principle are positive. It is to be expected that positive and normative economics should be different. But in this case they appear to inhabit universes of discourse that differ to an excessive extent. Moreover both, in their different ways, have proved rather unsatisfactory for their stated purposes. Optimisation theory has had a disappointingly small impact on policy-making, except at the strictly OR level (the best way of shunting railway wagons). The theories of public choice and of

bureaucracy are interesting but they are short on specific testable propositions.

The question naturally arises whether these deficiencies are related to each other. Optimisation theory as a rule does not take account of the processes by which political and bureaucratic decisions are arrived at, by whom, and with what motives. It therefore runs the risk of posing questions, ostensibly about policy, in a form that is non-operational. Some interesting observations on this subject were made in the course of the discussion (pp. 263–4) of the paper by Meys, a paper which described the attempts made in the Netherlands to integrate formal analysis in the decision-making process. But while it is easy to criticise optimisation theory for neglecting the processes of non-market choice, theories of non-market behaviour have proved difficult to construct.

It was the original intention of the programme committee that a good deal of the attention of the conference should be given to decision-making processes affecting collective consumption. This intention was formed in the belief that economics needs to develop a way of analysing non-market economic phenomena to match its existing way of analysing market phenomena. It was felt that, in current public discussion about decision-making and the administrative and political aspects of collective consumption, preoccupation with the *control* of expenditure, however necessary, tended to produce a one-sided emphasis, such as might be produced if one thought of the price mechanism merely as a device for keeping *down* consumption. Valuable contributions in this area were made in the papers by Frey, Leibenstein, Pliatzky, Meys, and Dempster and Wildavsky. None the less, it was noticeable throughout the discussion sessions that participants, eastern and western alike, showed a reluctance to come to grips with these questions and tended to veer off into the philosopher-king assumption and talk about questions about optimisation more familiar to most economists.

Does this reflect an inherent difficulty of producing general propositions about non-market decision-making that do not depend over much on the institutions of a single country? Do the price-mechanism and central planning under full information constitute economic systems more susceptible to intellectual analysis than systems where the market does not operate and power is diffused? The theory certainly has a long way still to go. Public choice theory offers the apparently attractive prospect of a single model embracing the economic and political behaviour of the individual; but it is far from giving generally usable conclusions. Much the same can be said about the theory of bureaucracy, though it too has provided useful insights. Both seem to be

more successful in analysing the proximate factors bearing on programmes of collective consumption than in explaining major changes in direction within and between programmes; and neither of them is very successful in analysing the forces responsible for shifts in the frontier between collective and individual consumption. The conference pointed to the need for continuing efforts by economists in this area. This effort is needed both in order to understand how 'endogenous governments' behave and in order to bring the expertise of economics more effectively to bear on an area of decision-making where the scope for oscillating dogmas and wasteful fudges is so great.

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Part One

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