

Donici, Gabriel-Andrei; Incaltarau, Cristian

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PUBLIC GOODS AND THE PROBLEM OF ECONOMIC CALCULUS²

Gabriel-Andrei Donici

“Alexandru Ioan Cuza” University of Iași

Cristian Încălțărău

“Alexandru Ioan Cuza” University of Iași

Abstract: *Most papers regarding public goods have a certain predisposition to “classic aspects” like their characteristics of non-rivalry and non-excludability. In this paper we try to emphasize that in the area of public goods one of the major problems is, in fact, the one of economic calculus. The reality is that public finances exist in a limited quantity so the public authority is forced to choose between ways to spend them. According to the definition of public goods the expenditures should be for the production of essential assets that are neglected by private investors. The problem is how to choose between public possibilities of spending the money after the application of the first criteria.*

Key words: *public goods, E.U., economic calculus, public spending, public distribution*

JEL classification: D73, H40, H41

1. PRELIMINARY IDEAS

Generally, specialists consider that public goods are strictly necessary and that the state is their best provider (and often the only one assuming the production), because their production is not rentable for the private investors.

Starting from this, if we take into account the fact that funds for public spending are limited, some questions arise: In what extent can be achieved an efficient distribution of public money? How can money be directed to pressing needs? In what extent money spent for development are used more efficiently in the public sector than in the private sector?

Or, in other words: what provides the highest utility? Is the utility provided by public goods higher than the one of a smaller level of taxation³?

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³ A smaller level of taxation encourages the development of the private sector

Leading the discussion on, we could shift to another aspect: the problem of intermediate public goods. If the result of public investment consists of intermediate goods should they be available, for free, to manufacturers?

2. SOME CHARACTERISTICS OF PUBLIC GOODS

According to Ferroni (2002) three interrelated characteristics of public goods emerge:

- they generate a lot of externalities;
- they are to a considerable degree “non-rivalrous” and “non-excludable”;
- they create opportunities for the enhancement of welfare through collective action.

The major defining characteristic of a public good (Brownstein, 1980) is that the consumption of the good by one person does not reduce the amount available to any other person. The second major defining characteristic of a public good is that the costs of exclusion are high, so as to render pricing difficult. But he also states that there are no goods which are not non-rival in consumption.

And according to Holcombe (1997) a public good is:

- a good that can be consumed by an additional consumer at no additional cost, and
- consumers cannot be excluded from consuming it.

Holcombe (1997) also underlined that goods with these characteristics will be under produced in the private sector, or may not be produced at all, following the conventional wisdom, so economic efficiency requires that the government forces people to contribute to the production of public goods⁴, and then allow all citizens to consume them.

As a whole the category of public goods is comprehensive; it includes from “classic goods” like roads or railways to goods of which we are not usually aware of being public like governance.

Anyhow the classical theory of public goods has certain problems. Holcombe (1997) underlines two problems regarding the traditional theory of public goods:

- many public goods are successfully produced in the private sector, so government is not really necessary;
- many of the goods government actually does produce do not correspond to the economist’s definition of public goods, so the theory does not explain the government’s actual role in the economy.

3. THE PROBLEM OF ECONOMIC CALCULUS

⁴ Higher level of taxation

The problem of economic calculus (in socialist countries) was first underlined by Mises (2006) who clearly emphasized the fact that the prices can be formed only on the free market and that no central organism has a better alternative to establish them. Because the value of a good is relative and it is given by the quantity available for supply and by the demanded quantity. And if a public institution decides how to use a certain quantity of scarce resources it interferes with price formation and production on the free (real) market.

In a world of imperfect information, a central organism cannot possibly know the best alternative for using the scarce resources.

If we would let the private entrepreneurs to freely use the scarce resources the decision of allocating the resources will be one of the market.

Although the Austrian economists generally considered it⁵ a problem of the socialist societies, we believe that it could be assigned to democratic societies. Even if we could say that in democratic societies the prices are formed on the free market, we encounter the problem of preference in the distribution of scarce resources (in the public sector).

In the process regarding the production of a public good / service, the decision of allocating resources is taken in a “rude” way, by people, in key position, which “unfortunately” don’t have the ability to know everything about the market and it’s evolution on the long term.

Are the reasons behind providing public goods enough to decide the use of scarce resources?

Ideally, prices form on the free market. In the public goods case, although we don’t have a similar situation to one from a socialist system, there is a problem regarding the fact that decisions are “unilateral” and prices do not form naturally. The result is the following one: with no real prices⁶ we cannot choose properly and we cannot estimate the real costs (just in some measure through comparison with free market prices). So because the economic calculus is not really possible in the public goods sector it’s fairly improbable, for a public decider, to make the best election.

⁵ The problem of economic calculus

⁶ Prices are the expression of the calculus result

4. THE PROVISION OF PUBLIC GOODS IN EU

In EU we don't have only goods provided by member states to their citizens; we also have goods provided at a regional level by different states. Therefore we can speak about public goods at an international or regional level.

They differ of national assets because in this case we speak about citizens from more than one state, we speak of international finances and of a distribution realized at a higher scale.

According to Ferroni (2002) international public goods, and RPGs, include the knowledge, the regimes, and the standards and rules that are required to address cross-border problems or to engender desirable cross-border externalities; the institutions that monitor and enforce the rules and regimes; and the benefits that arise and are shared indiscriminately among countries.

This definition implies that international and regional public goods come into two forms: intermediate and final. Final goods are broad outcomes or manifestations of well-being such as peace, the absence of extreme poverty, a well-managed physical environment, and convergent international economic conditions capable of "lifting all boats".

Ferroni (2002) also states that regional goods arise when individual countries induce beneficial cross-border spillover. Regional "bads" arise in the case of undesirable spillovers.

Starting from the problem of public distribution an issue that concerns us is: how efficient are the criteria for distributing resources (for public goods) in the European Union? How appropriate is the convergence criteria? What is the basis for it? Can we really consider it a solution to reduce the discrepancies between the different regions of EU?

For the case of EU public goods become regional and the redistribution of money (for their production) is made in larger areas. That is way the probability that the tax payers enjoy the benefices of their contribution is smaller.

The situation is quite different because in a country tax payers have a larger chance to benefit of the roads, railways, schools built with their money. We could even say that the investments made in the public goods sector from a country contributes to the development of the private sector (e.g. infrastructure).

Instead through massive redistribution, in the European Union, large amounts of money are directed to poor areas. And although this flow has not a decisive impact on competitiveness within the Union, the competitiveness poles are affected at an international scale and thus EU's ability to compete with its tradition rivals China, Japan and US.

5. CONCLUSIONS

Public finances exist in a limited quantity so that public authority is forced to choose between ways to spend them. The impossibility to make economic calculus stops it to choose the best option.

Hoppe (1989) stated that all the questions regarding public goods must be answered somehow because as long as there is scarcity and we do not live in the Garden of Eden, the time and money spent on one thing cannot be spent on another. The state has to answer these questions, too, although it does it without being subject to the profit-and-loss criterion.

Clearly no public authority can take good decisions. Probably the best solution is the one provided by the liberal schools of economic thought, otherwise said, the provision of public goods should be made through private investments.

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