The size of the state, economic growth and the efficient utilization of national resources

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1. Introduction

The size of the state, measured conventionally as government expenditures as a fraction of national output, has grown enormously in modern times. During this century, among developed nations, government spending has risen from under a tenth to more than a third of a share of GNP. The rise of government control over national resources is ubiquitous. Is this substitution of public choice for private choice beneficial or harmful to society based on some objective criterion? Obviously, an array of criteria must be specified and their interrelationships modeled before a definitive, overall judgment can be made. The objective in this paper is more limited. Evidence is offered on the effect of the size of the fiscal sector, net of resource growth, on economic growth and on the efficiency of resource allocation for 115 market economies for the period 1960 to 1980. The overall conclusion is that for these criteria at least the growth in the size of the state has been harmful.

2. Increases in the size of government: Beneficial or harmful?

Several caricatures of the state are found in the literature. In the English-speaking public finance tradition the democratic state is characterized as benevolent. The agents (politicians and bureaucrats) benignly serve the polity in performing the Musgravian (1959: Ch. 1) fiscal functions. From a public choice perspective, the bureaucratic state in majoritarian, representative democracies is fiscally expansionist, redistributive, and self-serving, with public resources being allocated in a political market (Downs, 1957; Buchanan and Tullock, 1962; Tullock, 1965; Olsen, 1965; and Niskanen, 1971). In the Italian public finance tradition (Buchanan, 1960) and in Buchanan (1975) and Brennan and Buchanan (1980) the state is characterized as malevolent. Unshackled

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of constitutional rules, revenue maximizing Leviathan drives the polity to penury (Brennan and Buchanan, 1980: 40).

While malevolence for its own sake cannot be ruled out, political self-seeking with guile naturally is linked with rent-seeking (Tollison, 1982). In majoritarian, representative democracies logrolling politicians redistribute public income by concentrating net benefits (benefits minus taxes) among the majority coalitions electing them. This tends to lead to a growth of the public sector (Buchanan and Tullock, 1962) and toward a redistribution of public resources toward the middle class (Stigler, 1970; Tullock, 1983, 1986). In non-representative governments the public sector is a source of rents to the ruling class and a source of much mischief. Tullock's (1967) important theoretical insight on rent-seeking identifies tariff induced rents as a prize up for grabs (also, see Krueger, 1974). In a laissez-faire, free trade, market economy, competition erodes rents. State command of resources through its fiscal function and government rules, regulations, licensing, etc. give rise to political markets for rents. Resources flow into the pursuit of those rents. Buchanan (1980: 9) argues that the level of rent-seeking and the resources devoted to this socially unproductive pursuit are directly related to the relative size of the public sector in the economy. Therefore, the increased size of government is harmful. Resources are reallocated from productive activities into directly unproductive, rent-seeking pursuits. A consequence of the rent-induced distortions in resource allocation is a decline in economic growth and in efficiency.

Traditional arguments also plausibly link the size of the government sector with a reduction in national economic performance. Value added in the government sector is lower than in the private sector. Resources are not allocated to highest valued use but on political (bureaucratic) criterion. High taxes, tax progressivity, and the substitution in consumption of politically priced public goods for market priced private goods reduces the incentives of economic actors.

The secular rise in the size of the state and the near universal appeal of the relatively large government sector suggests that large segments of these societies find this result desirable. Arguments that the increased size of the public sector is beneficial and may promote growth and efficiency briefly would be of the following sort. (1) The larger the government sector the greater the macroeconomic stability, since government expenditures exhibit less variance than private sector expenditures. Ceteris paribus, economies with low variance in GNP grow at a higher rate than those with a high variance in GNP. (2) The larger the size of the government, the greater is the scope for income redistribution. Too much income inequality may create incentives for the low income types to seek another social order. Redistributions may reduce work incentives, but may be an inexpensive (efficient) means of preserving the social order. Satisfying the demand for income redistribution promotes political and social