Packet 1
This course is intended to increase the student’s analytical skills in evaluating public policies in terms of economic efficiency and equity. The first two weeks are devoted to the efficiency criteria of welfare economics. We will examine the conditions that lead to efficient markets and those that lead to market failure and suggest public policy responses. We will also discuss some of the efficiency problems in the delivery of public goods and services. The remainder of the course examines existing and proposed public policies in a number of areas, including education, health care, poverty, business and financial markets, and the environment, where public policy may be able to increase efficiency as well as equity.

Course Requirements and Grading

The text is: Gruber, Jonathan, Public Finance and Public Policy 5th edition, but fourth edition is OK
Worth Publishers, 2016 (More emphasis will be placed on the packet readings)

This text does not cover regulation of financial and operating businesses. For regulation of businesses we will use a few chapters in
Viscusi, Vernon and Harrington, Economics of Regulation and Antitrust, 5th edition. But this is an expensive book and the packet and class notes cover the needed areas
These books will be on reserve in the Woodrow Wilson Library.

There are two required packets, which you will need to purchase from Pequod, at the U-Store
The packets have problem sets and newspaper and academic journal articles and are different every year.

As a source of current events, you are asked to read some articles in the Economist. Several articles will be assigned from The Economist each week and you will be tested on the assigned articles. (The Economist is free online to all Princeton students.)

There will be several questions to prepare and/or problem sets due for each of the precepts during the semester. If you cannot attend a precept, then you are responsible to hand in the written problems and brief answers to all the discussion questions.

There will be a policy proposal (1,000 word maximum, which is about 4 pages with 1” margins, 12 pt Times New Roman font, plus relevant graphs + references page) in which you recommend a public policy toward education, health care, crime, income redistribution, regulation of business, financial regulation or the environment. State your proposed policy and the main efficiency theory behind it. Then briefly explain why your policy improves efficiency. This policy paper is a special exercise in applying economic efficiency theory. This policy proposal is due on Monday, Jan. 16, 2017, the day before Dean’s date. (Two or three people may do one policy paper together or you may do it individually.) You could suggest creating a new policy or eliminating an existing public policy.

There will also be a mid-term examination and a final examination.

The course requirements are weighted as follows in determining the final grade:

<table>
<thead>
<tr>
<th>Requirement</th>
<th>Weight</th>
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</thead>
<tbody>
<tr>
<td>Precept participation and problem sets</td>
<td>20%</td>
</tr>
<tr>
<td>Mid-term Exam</td>
<td>30%</td>
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<tr>
<td>Final Exam</td>
<td>40%</td>
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<tr>
<td>Policy Proposal</td>
<td>10%</td>
</tr>
</tbody>
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Teaching Assistant: Mauricio Matsumoto email: mmsm@princeton.edu
Thursday September 15 and full Week 1

Problem Set 1 (Packet pp. 16-18) due in first precept Wednesday, September 21 (Graded P/F)

Pareto optimality and efficiency criteria
Equity and efficiency - welfare economics: What makes people happy?
Individual and/or societal perspectives


{You may also need to read the Gruber text, 3rd or 4th edition, pp. 26-37 if you are weak on indifference curves}

IMF “Economic Issues #16” pp. 3 and 10 (Packet p. 28)

“Happiness is a Warm Vote,” The Economist, April 17, 1999, p. 82 (Packet p. 29)

“Chasing the Dream,” The Economist, August 9, 2003, p. 62 (Packet p. 30)


When markets fail to be efficient (externalities, information failures, monopoly, pure public goods, the problem of moral hazard)
Government responses: ownership, regulation, insurance

Text: Gruber, Jonathan, Chapter 5, Externalities, 3d and 4th editions pp 121-137, {The rest of the chapter relates environmental economics, which we study at the end of the course}; Chapter 7 Public Goods

Week 2 Problem Set 2 (Packet pp. 39-42) Due in precept, Wednesday, Sept. 28th

The Problem with Price Controls (Packet pp. 43-44)
Economic theory of public choice - efficiency failures of governmental allocation. (rent seeking, separation of costs and benefits, free riders, costs of litigation, special interest effects, weak demand articulation)

Text Gruber, Jonathan, Section 9.4 3rd edition pp. 249-258 4th edition pp. 251-259 (The rest of chapter 9 is optional, but interesting especially if you care about voting theory and the difficulty of demand articulation)

A quick look at the econometrics of policy analysis


Week 3 Problem Set 3 (Packet pp. 45-46) Due in precept Wednesday, October 5

Education and human capital
Education production functions

Text: Gruber Chapter 11 Education


“Tracking the Gifted Boosts High-Achieving Minorities,” www.nber.org/digest, August 9, 2016 (Packet p. 51)

“The Rise and Fall of the College Graduate Wage Premium,” NBER Digest, January 2008 (Packet p. 52)


“Schooling Spending Differences are not the Source of Income Inequality,” NBER Website, July 11, 2005 (Packet p. 68)

“The Underworked American,” The Economist, June 13, 2009 (Packet p. 69)


Monopoly Public Education with Teacher’s Unions versus Choice with Vouchers and Charter Schools

Hoxby, Caroline M, “Achievement in Charter Schools and Regular Public Schools in the United States” NBER, December 2004 (Packet pp. 71-80)


Optional:
Chubb, John and Terry Moe, Politics, Markets and America’s Schools, Chapter 6, pp. 185-229 and Appendix D, pp. 259-277. (WWS Library)

Bush’s Program: No Child Left Behind – Universal Testing


Early childhood education

“Canada’s Universal Childcare Hurt Children and Families,” NBER Digest, June 2006 (Packet p. 104)


Bassok, Daphna, Fitzpatrick, Maria and Loeb, Susanna, “The Impact of Universal Preschool on the Childcare Sector,” The NBER Digest, June 2013. (Packet p. 128)


Reference:

Race and Education


Gender and Education

“Girls are getting as good as boys in maths, and are better at reading,” economist.com, June 2, 2008 (Packet pp. 132-133)

Week 4 Problem Set 4 (Packet pp. 134-136) Due Wednesday, October 12

Health Care Economics
Problems in equity and efficiency

Text Gruber Chapter 12 Social Insurance: The New Function of Government
Text Gruber Chapter 15 Health Insurance I: Health Economics and Private Health Insurance

Medical Care is Only One Input to Health (others include: genetics, life style choices like drinking and smoking, diet, exercise, sleep, occupational and environmental hazards, relationships with family and friends, religion, etc.)


“Economics focus: Waist Banned,” Economist, August 1, 2009 (Packet p. 149)

“Is Obesity Rational?” NBER Bulletin on Aging and Health, 2010 No. 2 (Packet p. 150)

“Keeping Employees Healthy – Trim staff, fat profits,” The Economist, July 30, 2011 (Packet pp. 151-152)

Lordan and Quiggin, “Should We Put a Thin Subsidy on the Policy Table in the Fight against Obesity?,” NBER (Abstract) (Packet p. 153)

Health and Education


**Demand for Medical services:**
1. high income elasticity of demand
2. 3rd party payment

**New Drugs and their pricing**


Civan and Maloney, “The Effect of Price on Pharmaceutical R&D” (Packet p. 166)

**Productivity in Medical Care - Effects of Subsidizing Medical Care**


“Life Expectancy Drops for White Women, Increases for Black Men”
www.npr.org/sections/health-shots/2016/04/20 (Packet pp. 188-190)


Wright, Sara, “The Effect of WIC on Infant Health,” NBER Digest, April 2010 (Packet p. 194)


**Supply of Services:**

Managed Care and the Emergence of HMOs
The Integration of doctors, hospitals, and insurance; payment systems
Can the inefficiencies be reduced?


Wright, Sara, “Evidence on the Effects of Nurses’ Strikes,” The NBER Digest, July 2010, p. 3 (Packet p. 212)


Week 5 Problem Set 5 (Packet pp. 217-218) Due Wednesday, October 19

General Suggestions for changing government policy on health care and for improving efficiency

Text Gruber, Chapter 16, Health Insurance II: Medicare, Medicaid, and Health Care Reform

Cartel Pricing in Medicare


The Canadian System of National Insurance


Challenges for Health-Care Reform


Optional Readings of Interest if your research question is on healthcare:

Symposium: Constraining Healthcare Costs Journal of Economic Perspectives MAY 16 2011

The (Paper)Work of Medicine: Understanding International Medical Costs (#2)
David M. Cutler and Dan P. Ly

The Pragmatist's Guide to Comparative Effectiveness Research (#3)
Amitabh Chandra, Anupam B. Jena and Jonathan S. Skinner

Patient Cost-Sharing and Healthcare Spending Growth (#4)
Katherine Baicker and Dana Goldman

Reforming Payments to Healthcare Providers: The Key to Slowing Healthcare Cost Growth While Improving Quality? (#5) Mark McClellan

Evaluating the Medical Malpractice System and Options for Reform (#6)
Daniel P. Kessler

Problems with Efficiency in Medical Delivery


“The looming train wreck is driven predominantly by health care,” Diagram of Projected Health Care Costs in Federal Budget (Packet p. 251)

Week 6 –

Tuesday October 25 Lecture 1 – Crime (The first precept after fall break is on crime, but crime will not be covered on the midterm exam.)

“Smoking, Drinking, and Drug Use Respond to Price Changes,” NBER Website, May 9, 2005 (Packet pp. 252-253)


Gorman, Linda, “The Impact of Childhood Lead Exposure on Adult Crime,” NBER Digest (Packet p. 283)

“What Reduced Crime in New York City?” NBER Digest, January 2003 (Packet p. 284)


Kelling, George & Catherine Coles, “Disorder and the Court,” The Public Interest, Summer 1994 (Packet pp. 302-306)

“Abortion Legalization Reduces Adolescent Substance Abuse,” NBER Digest, March 2003 (Packet p. 307)


**Wednesday, October 26, No Precept**
The midterm is at 7:30 p.m. on Wednesday, October 26. If you have a Wednesday evening class, please schedule with Professor Bogan to take the exam at 7:30pm on Tuesday evening or a daytime exam on Wednesday or Thursday.

Midterm Exam – Wednesday evening 7:30 p.m.

Sample Midterm and Answers (Packet pp. 319-334)

**Week 6 - Lecture 2 Thursday, October 27 (Day after Midterm)**
Finish Crime and begin Income Distribution

Over fall break please read the material listed at the beginning of the next packet on income distribution and poverty as you are unlikely to have time to do it for this lecture.
Packet 2

If you are interested in becoming a corporate lawyer or in the regulation of business, you may wish to purchase

Viscusi, Vernon and Harrington, Economics of Regulation and Antitrust, 3rd or 4th edition. But it is a big, expensive book, so you may prefer to use it in WWS library or just follow lecture carefully.

There will be a policy proposal (1,000 word maximum, which is about 4 pages with 1” margins, 12 pt Times New Roman font, plus relevant graphs + references page) in which you recommend a public policy toward education, health care, crime, income redistribution, regulation of business, financial regulation or the environment. State your proposed policy and the main efficiency theory behind it. Then briefly explain why your policy improves efficiency. This policy proposal is a special exercise in applying economic efficiency theory. This policy proposal is due on Monday, Jan. 16, 2017, the day before Dean’s date. (Two or three people may do one policy paper together or you may do it individually.) You could suggest creating a new policy or eliminating an existing public policy.
Week 7 Problem Set 6 (Packet p. 11) Prepare for November 9
Nothing to be handed in assuming you attend precept

Facts and theories on income distribution in the U.S.
Lorenz curves
Long term trends

Text Gruber, Chapter 17 section 17.1, “Facts on Income Distribution in the United States”


“Income Inequality,” FRB Cleveland, June 2005 (Packet p. 14)

Figure 3: Ratio of Family Incomes at 95th and 80th Percentiles to Incomes at the 20th Percentile in the United States: 1947-2000 (Packet p. 15)


Corak, Miles, “Income Inequality, Equality of Opportunity, and Intergenerational Mobility,” Journal of Economic Perspectives, Vol. 27, Number 3, Summer 2013, pp. 97, 98 (Packet p. 18)


Picker, Les, “Abortion and Selection,” NBER Digest, December 2006 (Packet p. 34)

Reasons for the widening distribution of income.
Implications for the future


The Income Distribution and Federal Tax incidence

Text Gruber Section 19.4 “The Incidence of Taxation in the United States”


African Americans, Mexican Americans, Asian Americans & Income Distribution


Women and Income Distribution


Fitzgerald, Jay, “Do Women Avoid Salary Negotiations?” nber.org/digest/apr13/w18511 (Packet p. 87)


“Princeton Economics Seniors by Academic Year” (Packet p. 101)


**Week 8 Problem Set 7 (Packet p. 108) Due November 16**

**Age and the Distribution of Income**

Text Gruber Chapter 13 Social Security


**Wealth Distribution and a Symposium on the top 1% of the Income Distribution**


**Poverty and Redistribution**

Text Gruber Chapter 2 Section 2.2
Text Gruber Chapter 17 Sections 17.2, 17.3, and 17.5
Text Gruber, Chapter 21 Section 21.3
(If you are weak on income and substitution effects also read section 21.1)


Optional:
Welfare Reform

Outline: 1996 Welfare Reform (Packet p. 146)


Entitlements


“Disability” Speech by Edward Glaeser, Harvard (Packet pp. 160-161)

Optional:
Currie, Janet, “Cutting the Safety Net, One Strand at a Time,” The Economists’ Voice, Volume 2, Issue 2, Article 5, 2005

Optional:
The following is a volume of separate papers on all the major means tested programs in the US as of 2000. I list it as a reference because each chapter summarizes the research findings on a program.


Optional: Blank, Rebecca, “Fighting Poverty: Lessons from Recent U.S. History,”
Journal of Economic Perspectives, Spring 2000, pp. 3-19
Optional: Jencks, Christopher, Rethinking Social Policy: Race, Poverty and the Underclass, Harvard University Press, pp. 1-23, 204-235 (WWS library)

Week 9  Tuesday, November 22

(No Precept as Thanksgiving Break - Wednesday November 23)

The Role of Business in a Free Economy

“Profit and the Public Good,” Economist.com, Jan. 20, 2005 (Packet pp. 162-166)

“Public Policy and Management,” knowledge@wharton.upenn.edu (Packet pp. 167-168)

Theory of government regulation of business

Viscusi, Vernon and Harrington, Economics of Regulation and Antitrust, 4th edition, Chapter 1, pp. 1-10, Chapter 3–Introduction to Antitrust and Chapter 10–Introduction to Economic Regulation (This is background material if you need it.)

“Antitrust Case, United States District Court for the District of Columbia,” Case 1:16-cv-01493 (Packet pp. 171-175)

“Who Owns the Knowledge Economy?” The Economist, April 8, 2000, p. 17 (Packet p. 176)

Gorman, Linda, “University Innovation and the Professor’s Privilege,” NBER Digest (Packet pp. 177-178)


The Federal Drug Administration
Expected value and risk aversion
Type 1 and Type 2 errors and costs of banning drugs

Viscusi, Vernon and Harrington, Economics of Regulation and Antitrust, 4th edition, Chapter 22–Premanufacturing Screening: The Case of Pharmaceutical, pp. 793-804 on Type 1 and Type 2 errors.

Frances, David, “Orphan Drugs Cure Rare Diseases,” NBER Digest, May 2002 (Packet p. 197)

Price Control


The Interface of Corporate and Financial Regulation
Sarbanes-Oxley and Corporate Governance


Week 10   November 29

Problem Set 8 (Packet pp. 209-210)   Due Nov. 30 (Because of Thanksgiving break last week, this precept and problem set is on earlier material, i.e., poverty and redistribution.)

Banking and Financial Regulation

Notes on the Financial Industry by Professor. Bogan (Packet p. 211)


Jordon, Jerry, “Specialization in Risk Management,” Economic Commentary, October 15, 1994 (Packet pp. 224-228) (this is the argument that “won” until 2007)

Mian, Sufi, and Trebbi, “Pressure on the U.S. Government to expand subprime credit came from both mortgage lenders and subprime borrowers.” (Packet p. 229)


“The Dodd-Frank Act Too big not to fail Flaws in the confused bloated law passed in the aftermath of American’s financial crisis become even more apparent,” The Economist, February 18, 2012 (Packet pp. 245-249)


Bogan, Connor, and Bogan, “Can an ETF collapse?” September 2010, revised August 2011 (Packet pp. 254-256)


Week 11  Problem Set 9 (Packet p. 262-263)  Due December 7

Sustainability
Environmental Regulation
Internalizing externalities
Emissions, Bubbles, Tradable emission allowances

Text Gruber Chapter 5, section 5.4, Chapter 6 Externalities in Action, sections 6.1 and 6.2

Solow, Robert, “Sustainability: An Economist’s Perspective,” presented at Woods Hole Oceanographic Institution, June 14, 1991 (Packet pp. 264-268)  [This is a classic in economics.]


For your reference perhaps the best text on environmental economics is:
Tientenberg, Tom, Environmental and Natural Resource Economics, 8th Edition. (WWS Library) Chapter 2, Valuing the Environment: Concepts; Chapter 4, Property Rights, Externalities and Environmental Problems; Chapter 15, Economics of Pollution Control: An Overview; Chapter 19, Water Pollution; Chapter 21, Environmental Justice.


“Is Trade Good or Bad for the Environment?” NBER Digest, November 2002, pp. 2-3 (Packet pp. 274-275)

Davis, Matthew, “Does the U.S. Outsource Polluting Industries?” The NBER Digest, February 2005 (Packet pp. 276-277)

Optional:

Cost-benefit analysis with present value consideration
Wetlands and Endangered Species
What is private property?

Text Gruber Chapter 8 Cost-Benefit Analysis (optional)

Global Warming (Climate Change)
 Tradable Emission Allowances or Fees in Climate Change Policy


Problems with Environmental Regulation

Week 12  Problem Set 10 (Packet pp. 305-308)  Due December 14
(Some students may find this problem set takes longer than some of the earlier assignments.)

Finish Economics and the Environment
Public Policy and Economic Growth—A Broad Overview of the Issues

Emphasis on the efficiency of markets versus government correction of market failure with an explicit industrial policy

Optional:
Dertouzos, Lester and Solow, Made in America, MIT Commission on Industrial Policy, Chapters 1,2,10 and pp. 166-167.

Final Exam Sample (Packet pp. 309-320)