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978-0-521-82804-8 - States and Markets: A Primer in Political Economy

Adam Przeworski

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## States and Markets

Political economy is the study of decentralized and centralized mechanisms for allocating resources and distributing incomes: markets and states. Both markets and states can be organized and combined in a variety of ways and they jointly determine what the economy produces as well as who gets what.

The purpose of this book is to introduce the reader to the concepts and tools for studying relations between states and markets. The focus is methodological. Both the economy and the state are analyzed as networks of relations between principals and agents, occupying particular places in the institutional structure.

Having introduced the principal-agent framework, the book analyzes systematically the effect of the organization of the state on the functioning of the economy. The central question is under what conditions governments will do what they should be doing and not do what they should not.

Adam Przeworski is the Carroll and Milton Petrie Professor of Politics at New York University. His previous books include *Democracy and the Rule of Law*, coedited with José María Maravall (Cambridge, 2002); *Democracy and Development*, cowritten with Michael Alvarez, Jose Antonio Cheibub, and Fernando Limongi (Cambridge, 2000); and *Democracy, Accountability, and Representation*, coedited with Susan C. Stokes and Bernard Manin (Cambridge, 1999).

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A Primer in Political Economy

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*New York University*



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## Preface

“I would like to study, among all the moderate governments we know, what is the distribution of the three powers, and to calculate in this way the degrees of liberty which each of them can enjoy. But one should not always exhaust a subject to such an extent that nothing is left for the reader to do. The point is not to make read but make think.”

(Montesquieu, *De l'Esprit des Loix*, Livre XI)

These are, only slightly polished, notes for lectures I used to give at the University of Chicago and now offer at New York University. They are based on the belief that political scientists cannot study political economy without knowing some economics. This was certainly my problem. Many years ago, I taught a course on the Marxist Theory of the State, only to conclude that neither the writers we studied nor I knew enough economics to make sense of the role of the state in a market economy. Hence, I decided to bite the bullet and, with the guidance of a graduate student at the time, Michael Wallerstein, I plunged. One unexpected consequence was that “Marxist” was dropped from the course title: I discovered that there are other sensible theories of the state. But, as I continued to learn economics, by that time by reading Joseph E. Stiglitz, I also discovered that there are many theories of markets. Thus I came to the conclusion that both “the state” and “the market” must be deconstructed. This conclusion provides the motivation for the course as it now stands.

I give this course to graduate students who have taken a basic course in microeconomics, with calculus. A former student in this course, James Vreeland, offers it to upper-level undergraduates at Yale. My motivation in making these notes public, however, is mainly to make the material accessible

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to colleagues. I know that there are many political scientists who were not taught this kind of material in graduate school, who run in the publishing race, but in the back of their minds always plan that one day they will “retool.” Having gone through a retooling process more than once – indeed, having spent most of my life retooling – I know this is not an easy feat. But it can be done, and these notes are intended to help.

The emphasis of the course is on concepts and tools. Its purpose is to teach the reader how to analyze markets and states and how to evaluate their functioning. The course prepares you to read the substantive literature but it does not review it systematically. If you want to continue, the best places are the textbook by Jean-Jaques Laffont and Jean Tirole that, in spite of its foreboding title, *Theory of Incentives in Procurement and Regulation*, is in fact an excellent introduction to political economy, and Allan Drazen’s magisterial review of the literature in *Political Economy for Macroeconomics*. Avinash Dixit’s *The Making of Economic Policy* will then put everything in perspective before you start reading frontier research.

Some of the chapters offer general introductions to particular concepts or techniques, but some are no more than explanations of representative articles or book chapters. I engage in mathematics only to illustrate general techniques needed to understand the substantive findings. However, some chapters do nothing more than fill gaps in mathematical derivations that were skipped by authors writing to an economic audience.

Each of the chapters is preceded by a list of readings. You should at least skim the items indicated as “Read” before studying each chapter and you should reread them afterward.

A note about the necessary mathematical background: You will need elementary calculus and a lot of courage. I found that students who cheat, entering the class without any knowledge of calculus, make it successfully through. They do work harder, often consulting some calculus textbook. But there is a lot of repetition in the course, and in the end they learn by having done it over and over. Hence, even if at the beginning your understanding is only fuzzy, by the end you should find it easier than it seemed.

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