For the first three or four weeks we will consider the theory of social choice, especially that part which most concerns ethics and objectives for economic policy. The rest of the course will consider welfare economics specifically, describing and taking account of the constraints on economic policy. In particular, we will see the effect of incentive constraints which arise because relevant characteristics of economic agents are private information, and because agents may make unofficial trades which escape taxation etc. Simplistic discussions of the efficiency of competitive markets, of the gains from free trade, and of the distortions created by income or commodity taxes, all lose their validity. Simple characterizations of optimal policies are generally impossible, and we conclude by discussing how to identify policy improvements — e.g., by cost–benefit analysis of projects, and analysis of tax reform.

1. Limits to majority rule (Condorcet paradoxes, single peaked preferences).
2. Strategic voting.
3. Arrow social welfare functions and independence conditions.
4. Sen social welfare functionals with interpersonal comparisons.
5. Economic environments.
6. Harsanyi’s utilitarianism with fundamental preferences.
7. Libertarianism.
8. Implementation: the revelation principle and incentive constraints.

Part II. Welfare Economics without Incentive Constraints
10. Efficiency with externalities and public goods.
11. Reform: the gains from trade, deadweight loss, etc.
12. Nonconvexities
Part III. Private Information and Incentive Constraints

13. Economies with a finite number of agents.

14. Continuum economies and markets as constraints:
   private goods decentralization and the need for linear pricing.

15. Second best taxation and public production.

Part IV. Policy Reform with Incentive Constraints


17. Improving directions of reform and the evaluation of small projects.

18. Discrete improvements and the evaluation of large projects.

READING LIST (with references to attached bibliography)

Background Readings (and alternative treatments of similar material)

**General**

Hammond (1985) (informal survey of developments that were recent in 1982);
Boadway and Bruce (1984) (advanced undergraduate textbook, more reliable than most);
Guesnerie (1995) (a careful exposition of the theory of incentives, etc.);
Atkinson and Stiglitz (1980) (public finance aspects);
Arrow and Scitovsky (eds.) (1969) (with most of the classic articles);
Bös (1987) (public enterprise); Campbell (1986); Starrett (1988); Laffont (1988);
Hammond (1990a); Myles (1995); and finally:
Hammond, P.J. (forthcoming) *Theoretical Principles of Economic Policy* (TPEP)
(some draft chapters to be made available).

**Social Choice**

Phelps (1973); and finally:
Hammond, P.J. (forthcoming) *Social Choice for Welfare Economics and Ethics* (a collection
of past papers — draft chapters to be made available).
Readings Specific to Each Topic
These will be supplemented with handouts and recent papers where appropriate.

Part I (Social Choice)

1. Condorcet paradoxes
Condorcet (1785); Bowen (1943); Black (1948); Plott (1967); Pattanaik (1971); Kramer (1973); Wagstaff (1975, 1976); Grandmont (1978); Greenberg (1979); Caplin and Nalebuff (1988, 1991*); McKelvey (1979); Cohen and Matthews (1980); Schofield (1978, 1983); Rubinstein (1979); McLean (1995); Craven (1996).

2. Strategic voting

3. Arrow social welfare functions and independence conditions

4. Sen social welfare functionals and interpersonal comparisons

5. Economic domains
6. Harsanyi’s utilitarianism

7. Libertarianism

8. Implementation

Part II (First Best)
9. Efficiency theorems
Hotelling (1938); Arrow (1951*); Debreu (1954); Koopmans (1957); McKenzie (1981); Drèze (1964); Hammond (1998).

10. Externalities and the public environment

11. Reform
Gale and Mas-Colell (1975); Grandmont and McFadden (1972*); Debreu (1982); Chipman and Moore (1980); Pazner and Sadka (1980); Boiteux (1951); Debreu (1951); Drèze and de la Vallée Poussin (1971); Malinvaud (1972); Hammond and Sempere (1995*).

12. Nonconvexities and Marginal Cost Pricing
Part III (Second Best)

13. Incentives with finitely many agents
TPEP, ch. 7; Maskin (1980); Laffont and Maskin (1983); Satterthwaite and Sonnenschein (1981); Postlewaite and Schmeidler (1983); Palfrey and Srivastava (1986), Hammond (1990b*); Piketty (1993); Barberà and Jackson (1995); Córdoba and Hammond (1998).

14. Incentives in continuum economies

15. Second best taxation and public production

Part IV (General Reform)

16. Measuring welfare

17. Improving directions
18. Discrete improvements

SELECTED BIBLIOGRAPHY:


