

Book Review:**“Government versus Markets: The Changing Economic Role of the State” by Vito Tanzi, Cambridge University Press***Reviewed by Richard W. Rahn*

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If one has an interest in political economy, yet only time enough to read one book, this is the book to read. Vito Tanzi is not only a first-rate scholar, but a man who spent much of his working life dealing with practical problems of political economy in very high-level positions. He is not an ideologue, but an empiricist. As a scholar, he is well-versed in economic theories of the state. For the last four decades, he has spent much of his time collecting and analysing the evidence of how different states have dealt with their economies.

Tanzi spent 27 years at the IMF and for many years was director of its fiscal affairs department. He was also a former undersecretary for economics and finance of the Italian government, has taught at a number of universities and is the author of 14 books.

Tanzi begins his book by noting that there is no more fundamental question in economics than in what role the state should play. Should government plan a country's economy, and, if so, how wide and how deep? In a market economy, what are the responsibilities of the state and how much should be left to the market and to the free economic decisions of individuals and groups of citizens? If a state intervenes in a market economy, how should it do it and what instruments should it use?

Tanzi documents the rise of government over the last hundred and thirty years. Before World War I, in 1913, the average government spent about 13 per cent of GDP; by the beginning of World War II, in 1937, it had risen to 24 per cent of GDP; as of 2007, spending had risen to 42 per cent of GDP. Even though in most countries government has slowly grown as a percentage of GDP, there are exceptions, notably the Swedes and the Canadians, which over the last 15 years have reduced the size and role of government in their economies.

Tanzi gets to the heart of the problem when he writes: “politicians learned they could get votes by providing government jobs for those who voted for them or by allocating public spending to particular groups, realising the benefits would go to the members of the groups while the costs would be shared by all, or most, citizens.

Public employment and public spending grew more than necessary while productive public spending was often reduced.”

Tanzi observes that as the productivity of public spending has declined, the struggle between trying to achieve both efficiency and distributional equity has undermined or begun to challenge the legitimacy of the implicit social contract between citizens and the state.

In a most interesting way, Tanzi has managed to weave in history and the philosophy of the various political thinkers, economists and others who have written about the role of the state and reasons for government.

Upon this foundation, Tanzi provides the documentation of the stated intentions of various government actors versus the outcomes of their actions and programmes. Tanzi is a realist, not a romantic, when it comes to government action. He looks at what higher levels of government spending by various governments have actually achieved – what has tended to succeed and what has not.

Tanzi is one of the world's leading tax experts. His evaluation of the pros and cons of the various systems and the effects of tax rates is first rate and very well written. He also documents the effect of tax rates and systems on economic growth – and clearly demonstrates that beyond some point – exceeded by most governments – taxation negatively affects growth.

Largely because of the growing complexity of government, Tanzi ends this fine book on a negative note. He argues that the increasing complexity of some new legislation, regulation, taxation (the US code alone contains more than 70,000 pages) and government programmes, which are often contradictory and counterproductive, diminish economic growth and liberty. He does not see a happy outcome to the growth of the bureaucratic state.

Despite the end of the book being a bit of a downer, it is well worth reading. Tanzi is a fine and interesting writer.

He presents his arguments and data in a clear, concise manner, often through the use of well constructed tables. Government versus Markets is both a good read and a fine reference book for those who like to debate the role of the state in the economy.

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