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## THE SEARCH FOR A BETTER PUBLIC / PRIVATE MIX IN CONTEMPORARY MARKET ECONOMIES

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**Abstract.** Applying a conceptual approach, taking into account international experience, this article proposes four normative vectors in order to improve the public-private mix in contemporary market economies: 1) that the analysis go beyond the underlying macro approach to public spending/GDP ratios; 2) that an integral evaluative framework be adopted; 3) that the mutual implications between public policy ends and means be carefully considered; and 4) that strategic reviews and continuous learning, together with accountability and participative arrangements, be used to counteract incrementalism and uncontrollability.

**Keywords:** public / private mix, performance criteria, public value, privatization, incrementalism, uncontrollable spending.

In a society that views itself as “free” and “democratic”, establishing a permanent ideal distribution of economic activity between the public and private sectors is impossible. This is because optimal allocation of economic activity results from confronting a changing set of social values with an also changing set of achievable allocative alternatives (the so-called “budget constraint”, which depends on the relative productivities and factor prices of the different productive activities). Therefore, either liberal or statist dogmatic assumptions seem to provide no promising way to determine the optimum public / private mix in contemporary market economies. Pushing apriorisms aside, some normative vectors can be proposed on a pragmatic approach to improve the current mix by removing inertia and reinforcing rationality.

*Analytical level.* The distribution of economic activity between the public and private sectors is not a merely macro, quantitative issue. Although a growth-maximizing government has been theoretically identified as that in which the marginal impact of taxation equals the marginal productive gain of public expenditure, the empirical literature has so far provided inconclusive results on the relationship between government size and economic growth [8]. The expectation of an inversely U-shaped relationship between them, or even between government size and economic development [21], barely formalizes more than a plausible intuition: any government expansion has a limit beyond which it would become unfavorable for growth or development. However, such a limit or shift point may be contingent on several country-specific factors, and its specification in terms of the percentage of public spending compared to GDP may be problematic. Indeed, public expenditure / GDP ratios are intrinsically heterogeneous, as transfers are included in their numerator and excluded from their denominator. This makes a ratio higher than 100 % possible, as illustrated by the first case of the following table.

Table 1

**The arithmetic of public expenditure/GDP ratios\***

	Case 1		Case 2	
		£		£
Public expenditure on goods and services		30		110
Public expenditure on transfers		80*		0*
Private expenditure: privately financed	30		70	
publicly financed	40		0	
	----	70	----	70
		----		----
GDP		100		180
		----		----
Public expenditure / GDP		110		110
		100		180
Public expenditure / GDP ratio (x 100)		110 %		61 %
<i>Note:</i> * Excluded from GDP to avoid double counting of the transfers and of final expenditure. Although that public transfers exceeds private expenditure seems to be rare, it may occur if transfers are heavily taxed (at 50 % here).				

\*Source: Heald [16, p. 13].

On the other hand, maximizing economic growth is not necessarily the only purpose nor the first priority of a government and, therefore, a greater research effort is needed to test the relationship between government size and so-

cial welfare – see, for instance, Flavin, Pacek and Radcliff [14], who find robust evidence that human wellbeing increases as government is greater and its scope is wider. Most importantly, the macro approach of government-size literature cannot substitute for the more fruitful analyses to be done at *meso* and *micro* levels, following Bouckaert's [4, 5] distinction. These analyses have to go far beyond the conventional classification of public spending subaggregates into “productive or growth friendly” and “unproductive” categories, because “the assessment of expenditure quality cannot exclusively be based on the composition of spending but also has to look at whether those resources are translated as efficiently as possible into beneficial outputs to citizens” [12, p. 21]. Issues like in such cases and to the extent that a public intervention proves suitable, as well as through which instruments it must be done, are key issues to improving the public-private mix in contemporary market economies. Government-wide value for money probably depends much more on the roles that government assumes and the way it plays them than on its total size relative to GDP.

*Evaluative framework.* To judge when markets or governments fail or achieve success, either a synthetic criterion or a reference set of value criteria are needed. In welfare economics, the synthetic criterion has been that of Pareto optimality, a particularly narrow byproduct from the Utilitarian tradition. According to Sen's [31] masterful analysis, such traditions involve three questionable requirements: “welfarism”, “sum-ranking”, and “consequentialism”, which come to neglect, amongst other things, the “agency aspect” of a person and the intrinsic value of their freedom and rights<sup>1</sup>. Further, the Pareto efficiency criterion sets aside equity and fairness, thereby being able to lead to “efficient” but unfair decisions or to block redistributive programs as “inefficient”. It is no wonder, therefore, that a heterodox economist like Philip A. Klein [18] has proposed to go beyond this narrow efficiency towards a *higher efficiency*, understood as the extent to which the economy reflects all the relevant values of all its participants and facilitates the development and transmission of emergent values. As he writes, “the task of an economy is to play a role in transmogrifying individual values into social values – a task that must recognize that some values can be expressed *only* socially; that any given economic mechanism, whether prices, administrative fiat, or any other, is imperfect; and that in playing an interactive role in the dynamic process of transmitting and shaping values the public sector can aspire to no higher purpose than reducing imperfections.” [18, p. 62].

In the public management field, moreover, the narrow and abstract Paretian criterion tends to be substituted by the also narrow but more operative three “e” criteria of economy, efficiency, and effectiveness. However, a strong dominance of these results-oriented criteria, based on an aspect of Pareto optimality (production efficiency), may weaken commitment to democratic-constitutional values like representation, participation, transparency, and individual rights [27]. There may even be a risk of distorting the role of government, as the core issue in government is often fairness, both procedurally and in outcomes: “The private market is designed to be efficient but not to be fair. Democratic self-government is designed to at least try to be fair, and hope to be efficient. As American governments at all levels have embraced market logic, they have become less fair. Is this not an ethical issue?” [15, p. 317]. More than half a century ago, Herbert A. Simon [32] claimed that evaluating results of administrative activity requires one to take into account all the significant value elements of the alternatives considered, and that some of these value elements may not be found only in the result proper, but also in the administrative activity itself. These claims can fit well into the current Moore's [24, 25] view of governmental administrative activity as one aimed to create *public value*. However, this notion goes beyond the welfarist framework to embrace also deontological values like government fairness and justice or government promotion of a just and good society.

Table 2

Philosophical/normative frameworks for valuing the use of public assets\*

		Normative / Philosophical Framework	
		Utilitarian	Deontological
		Focusing on the good at individual and collective levels	Focusing on the right, the fair and the just at individual and collective levels
Public Assets Being Deployed	Money	Efficient and effective use of public money	Fair use of public money to help produce a just society
	State Authority	Efficient, effective and accepted use of state authority	Fair use of public authority to assure justice in individual transactions and in society as a whole

\*Source: Moore [25, p. 473].

*Ends and means.* In the middle third of the twentieth century, the economic theory of market failure appeared to provide, on a “scientific” basis, a catalogue of corrective ends and suitable means to address the market failures [22, p. 356-357]. On the other hand, when public provision of goods and services was indicated, public production often tended to be taken for granted. However, in the last third of the century, an emerging theory of “government failure” or “nonmarket failure” [38, 39] stood in opposition to the neoclassical theory of market failure. Then, the idea made its way that the unavoidable publicness of certain ends does not necessarily need to be translated into the means, thereby opening a door to pursue “public ends” by “private means” [11]. In the eighties, a growing wave of privatizations of public firms was extended throughout developed countries, but the public-interest component of these firms' activities compelled governments to play a regulatory role. Indeed, the firms' efficiency gains depended more on their pre-

privatization reforms, the introduction of competition, and the regulatory framework than it did on privatization per se [9, 34]. Additionally, contracting out was expanded to privately produce public services, despite the general and specific limitations found early on in implementing this strategy. Among the general limitations are the possible creation of bilateral monopolies, worsening of working conditions, and outsourcing more guided by the stakeholders' interests than by the public interest. Among the specific limitations are the high fixed costs or economies of scale that discourage competition in some industries, the substantial externalities difficult to control without public production, and the demand manipulation, cream skimming, and quality shaving in the production of *merit goods*.

In the last few decades, however, new forms of marketization like public-private partnerships have proliferated, and nonprofit private organizations and citizens have become progressively involved in pursuing and even co-defining public goals [6, 7, 10, 30]. Current welfare systems, for instance, appear as public-private mixes where four core institutions – the polity or state, the market or economy, families and households, and the not-for-profit or civil society organizations – are continuously interacting. According to Estes and Zhou [13, p. 361], “the genesis, nature, structure, and dynamics of contemporary social welfare can only be understood through an examination of the interactions that occur over time between and within the four core welfare institutions and their complex networks of interstitial organizations.” Some scholars even call for a general reconfiguration of the state, shifting from the technocratic delivery state to a *relational state* that acts as an enabler, steering an interconnected system and promoting deep relationships between the key actors [23, 26]. Others focus on governing through persuasion, and argue that it does not exclude the pivotal role of the states “because they retain a responsibility for the metagovernance of such relationships and because they alone can combine efforts at persuasion with the imposition of hierarchical authority.” [3, p. 866].

In any case, both marketization and non-governmental prominence are being revealed as considerably problematic. Nowadays, there is widespread criticism of privatization and an emerging tendency to bring services back under public control, especially through re-municipalisations conducive to noticeable efficiency gains [35, 28]. Additionally, evidence exists that the intended efficiency gains from public-private partnership are only within reach of those governments with very strong management capacity [1]. Public value may be undermined by the private sector involvement and, therefore, the mutual implications between public policy ends and means have to be carefully considered. Moreover, Kettl [17] underlines that the increased interweaving of the public, private, and nonprofit sectors not only complicates the tasks of separating public from private spheres, ensuring the accountability of public programs and pursuing high performance in such programs, it also transforms the debate over the role of government and its programs. “It is hard to cut government because government is so deeply part of nongovernmental institutions – and because the non-governmental world has become so dependent on these interwoven relationships that it has become increasingly impossible to make any decision about cutting government without simultaneously affecting the deep patterns of public-private-nonprofit interdependence.” [17, p. 220]

*Controllability.* From the seminal contributions of Lindblom [19] and Wildavsky [37] to the more recent literature based on punctuated equilibrium theory [2], a huge amount of research has tested incrementalism in public policy and budgeting. Incremental behavior may perpetuate policies or expenditures arising from a given conjuncture, even when their *raison d'être* has disappeared. This phenomenon tends to be especially acute in government budgeting, given some particularities of the budgetary process. Added to this is the fact that budgeting often consists of previous decisions costing more than taking new ones. Indeed, a high percentage of budget appropriations usually correspond to “committed expenses” or “uncontrollable expenditures”, the amount of which cannot be significantly affected within the annual budgetary process. “From the viewpoint of appropriations review, there are thus numerous exogenous forces and factors which they [the President and the Congress] must take account of and cannot effectively control: the number of eligible veterans who apply for pensions or compensation, the amount of public assistance payments made by the states and for which they must be partially reimbursed according to prescribed matching formulas, and so forth. The relatively controllable portion of the budget, from this viewpoint, consists of those government spending programs where the determining factors are endogenous to the appropriation process, which may modify them, at least to a considerable extent.” [36, p. 417].

To counteract incrementalism and uncontrollability, several reform efforts may be required. Strategic review of public policies and public spending [29, 33, 40] potentially enables eliminating or transforming those policies or expenditure programs that have become obsolete or the justification of which has declined, removing the inertia underlying many of the committed expenses. Continuous learning and improvement, resulting from either those reviews or diverse participatory and accountability devices, may also play a key role to this respect. “Public services need to include structures which ensure that the public objectives are constantly reinforced and monitored by democratic mechanisms of accountability and involvement of the public. Such mechanisms include formal accountability to elected public bodies, such as municipalities or governments; structures for public participation in decision-making, including full transparency of information; and active involvement of representative organizations, such as community associations.” [28, p. 24]. A parallel effort may be required to counteract the regulatory incrementalism that imposes increasing costs on the private sector, being these costs still largely hidden and exempted from any accountability comparable to that of fiscal activities. Without aspiring to a full and short-term implementation of the extremely ambitious *regulatory budgeting*, some governments have begun to deal with this issue by assuming the duty of identifying offsetting reductions in regulatory burden wherever new regulations were proposed [20].

### Note

<sup>1</sup> Different than the “wellbeing aspect” of a person, their “agency aspect” supposes that they can be geared to considerations (goals, commitments, values...) beyond their own wellbeing. The intrinsic value of their freedom and rights is opposed to their merely instrumental consideration, i.e., their valuation by only the wellbeing they achieve in exercising their freedom.

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## ПОИСК ЛУЧШЕГО СОЧЕТАНИЯ ГОСУДАРСТВЕННЫХ И ЧАСТНЫХ ИНТЕРЕСОВ В СОВРЕМЕННОЙ РЫНОЧНОЙ ЭКОНОМИКЕ

**Хосе Кааманьо-Алегре**, доктор юридических наук, доцент кафедры политической экономии и государственных финансов на факультете права, отделение прикладной экономики  
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***Аннотация.** Принимая концептуальный подход с учетом международного опыта, в данной статье предлагается четыре нормативных вектора в целях улучшения сочетания государственных и частных интересов в современных рыночных экономиках: 1) анализ выходит за рамки основного макроподхода к соотношениям государственных расходов / ВВП; 2) будет принята интегральная оценочная структура; 3) будут тщательно продуманы взаимные последствия между целями и средствами государственной политики; и 4) стратегические обзоры и непрерывное обучение вместе с подотчетностью и механизмами, основанными на вовлечении, можно использовать для противодействия инкрементализму и неуправляемости.*

***Ключевые слова:** сочетание государственных / частных интересов, критерии эффективности, общественная стоимость, приватизация, инкрементализм, неконтролируемые расходы.*