Markov Perfect Political Equilibrium with Social Security:
The Role of Education Cost

RYO ARAWATARI† AND TETSUO ONO‡

April 17, 2007

Abstract

This paper focuses on how education costs affect the political determination of public policy via individual decision-making. The paper extends the model in Hassler, Storesletten, and Zilibotti (2007, Journal of Economic Theory; henceforth HSZ) by generalizing the cost function of education and considers several cases, along with HSZ as a special case. In cases where education cost is high, the characterization of political equilibrium is similar to HSZ. In cases where education cost is low, the characterization is entirely different from HSZ: namely, a political equilibrium exists where (i) the rich are always politically decisive and (ii) the equilibrium outcome is unique.

Keywords: Markov perfect equilibrium; Dynamic political economy; Public policy; Education cost

JEL Classification: D72; D78; E62; H41; H53

†Graduate School of Economics, Osaka University, 1-7, Machikaneyama, Toyonaka, Osaka 560-0043, Japan. E-mail address: ege001ar@mail2.econ.osaka-u.ac.jp
‡Corresponding Author. Graduate School of Economics, Osaka University, 1-7, Machikaneyama, Toyonaka, Osaka 560-0043, Japan. E-mail address: tono@econ.osaka-u.ac.jp

We would like to thank Ryuichi Tanaka and participants at the Seminar on Economic Theory and Econometrics, Osaka Prefecture University, February 2007, and the Macroeconomics Conference for Young Professionals, Osaka, March 2007, for their useful comments and suggestions. Arawatari acknowledges financial support from JSPS Research Fellowships for Young Scientists. Ono acknowledges financial support from the Japan Society for the Promotion of Science (JSPS) through a Grant-in-Aid for Young Scientists (B) (No.17730131) and the 21st Century COE Program (Osaka University). All remaining errors are mine.