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Hold on to Your Wallet: The Cost of Corporate Welfare and Rent-Seeking

By Veronique de Rugy
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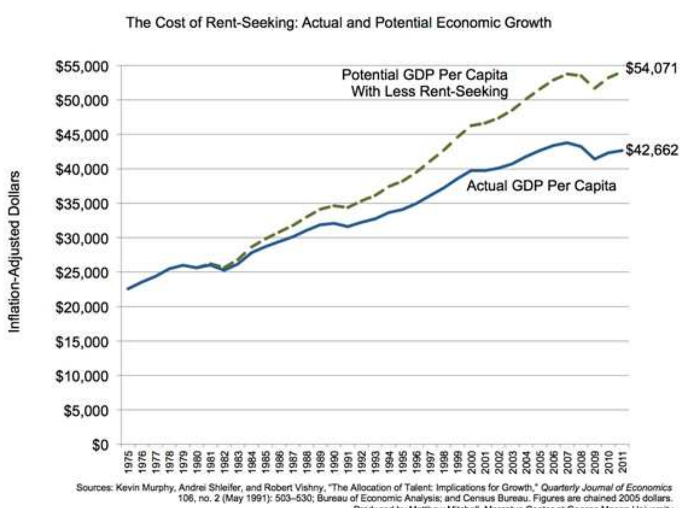
I have been talking a lot recently about the cost of cronyism – the practice by which government officials provide preferential treatment (such as loans, subsidies, or regulatory preferences) to handpicked firms or industries. Cronyism takes many forms: It is Solyndra, the farm bill, subsidies to oil-and-gas corporations, banks and automobile companies, but also the protections granted to the sugar industry and other industries, tax credits to private companies, and much more.

In a great new paper, Tad DeHaven of the Cato Institute looks at the cost of one aspect of cronyism: corporate welfare. Corporate welfare programs are "programs that provide payments or unique benefits and advantages to specific companies or industries." Putting a price on corporate welfare isn't a perfect science but, after going line by line in the budget and adding the programs up, DeHaven finds a total cost of $98 billion in spending in fiscal 2012.

That cost, however, doesn't include things like the higher price of goods and services that American consumers have to pay when the government grants special protection to special interests like it does with the sugar lobby.

Nor does it include the cost to our economy of the time, money, and energy that entrepreneurs and businesses spend asking politicians for those privileges, rent-seeking, as economists call it, instead of devising new ways to create value for customers. This chart by Mercatus Center's Matt Mitchell does:



That’s how it works:

Economists Kevin Murphy, Andrei Shleifer, and Robert Vishny studied this phenomenon using data from dozens of countries. They found that a 10 percentage point increase in the share of students concentrating in law was associated with 0.78 percentage point slower annual growth in per capita GDP. In other words, economic growth was slower in countries where there seemed to be more rent-seeking.

In this week’s chart, Mercatus senior research fellow Matthew Mitchell shows how this difference compounds over time. If, since 1980, per capita GDP had grown 0.78 percentage points faster than it actually did, then 2011 per capita production would have been $54,000 rather than $43,000. “When governments dispense privileges,” Mitchell says, “economic growth is diminished. This isn’t just an abstract idea. It means that real people earn less money than they otherwise could.”

The whole thing is here. This is serious and is just one added layer of evidence that we should end all special favors to private-sector companies.