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ORIGINAL PAPER

The political economy of public debt

Geoffrey Brennan

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Abstract Public debt (as opposed to current taxation) alters the inter-temporal pattern of tax rates—it reduces current rates and increases future rates. Accordingly, whether the share of the cost of a given public expenditure is reduced or increased by debt for a given individual depends on the time profile of that individual's income (tax base) vis-à-vis others' incomes. Therefore, given the age-profile of income in virtually all Western countries, individuals will tend to be better off under current taxes the younger they are. If (as most standard models of political economy assume) individuals vote according to their economic interests, and if they are tolerably well-informed, then the pattern of support for public debt will track age. And increases in the median age of the population will lead to larger public debt. In other words, public debt policy collapses to a kind of demographic politics. This explanation may, however, be sensitive to assumptions about motives for bequest. Specifically, if bequestors seek to leave positive bequests and are motivated exclusively by the lifetime consumption of their heirs (as well as themselves) then the aged may, under plausible assumptions about the age of their heirs, prefer current taxes over debt.

Keywords Public debt · Age-income profile · Median voter theorem

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G. Brennan (✉)
Political Science, Duke University, Durham, NC, USA
e-mail: Geoffrey.Brennan@anu.edu.au

G. Brennan
Philosophy, UNC-Chapel Hill, Chapel Hill, NC, USA

G. Brennan
Philosophy, Australian National University, Acton, ACT, Australia