

ECON-A4000 - Economics of Global Challenges

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Return method: through mycourses by the deadline

Problem Set 3: Question 6

This question motivated by our discussions during lecture 11. We discussed the dictatorship model on pages 15-19 of the slide set.

Suppose the elite can borrow financial resources for providing public services. Assume in this discussion that the dictator plans to pay back the loan.

1. How would you introduce this possibility to the dictatorship model? If borrowing is an attractive option, it should lower the cost of providing the services. Can you elaborate the conditions for this to happen?
2. If borrowing indeed lowers the cost of services, some curves in the diagram will change when borrowing is introduced. Draw a figure depicting this new situation. Note: The (absolute value of the) slope of the isorent curves is $\frac{T-C}{D}$.
3. Can you say if the elite will levy the same level of taxes, higher taxes, or lower taxes after having the option to borrow?

This discussion helps in seeing if financial markets allow dictators to stay in power for longer periods. Of course, it is only model.