

When is Rent-Seeking Wasteful? : A Critique of the Theory of Rent-Seeking*

Ha-Joon Chang
University of Cambridge

The paper examines the theory of rent-seeking (*TRS*) with an emphasis on the implications of different institutional settings for the efficiency consequences of rent-seeking, using Korea and Japan as examples. The first section summarizes the standard *TRS* argument. In the second section, some conceptual problems of *TRS* are discussed. The third section questions the validity of "competitive rent-seeking" models and discusses problems of collective action and of strategic behavior. The last section extends our discussion and deals with problems of unequal distribution of rent-seeking opportunities and, more importantly, of "dynamic" benefits of rent.

I. The Theory of Rent-Seeking: The Argument

One of the fastest growing body of recent economic literature is theory of rent-seeking (henceforth *TRS*). This theory may not be very sophisticated, but the very simplicity of the argument adds to its power as a tool for public policy analysis. With reasonably simple analytical manipulations, it can help us to analyze a wide array of issues ranging from 16th century Mercantilism (e.g., Tullock 1984) to trade policy in contemporary Turkey (e.g., Krueger 1974).

The starting point of *TRS* is that state intervention, by restricting entry, will create artificial scarcity and the consequent rent (the receipt in excess of opportunity cost). This will encourage, the argument goes, activities which are rational on individual level but are wasteful on social level.

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According to *TRS*, *rent-seeking in itself* may be socially productive in a competitive setting. After all, as Schumpeter (1961), following Marx (1981, pp. 373-4), forcefully argued, entrepreneurs innovate to capture the rent from being a monopolist, and this process of seeking rent (or "surplus profit" of Marx, and "entrepreneurial profit" of Schumpeter) is the essence of dynamism of capitalist economies (more on this in subsection IV. B.). In a competitive setting, once rent is created in an industry, other entrepreneurs will move into this industry and eventually erode the rent (driving the profit down to "zero," or less misleadingly, to the "normal profit" level, or to the reservation utility level of the entrepreneurs). However, in a non-competitive setting, people will "waste" resources by seeking rent, since "[r]esources devoted to efforts to curry [the authority's] favor *might be used to produce valued goods and services elsewhere* in the economy, whereas *nothing of net value is produced by rent seeking* [*italics added*]." (Buchanan 1980, p. 8)¹ That is, the central theme of *TRS* is that the existence of contrived (or artificial) rent leads to a "wasteful rent dissipation," where the whole rent is spent in people's attempts to seek rent without producing any socially useful by-product.

II. Some Conceptual Problems; Is "Waste" Wasteful?

Of course, *TRS* assumes away any benefit from the state's creation of monopoly rights (and hence rents). And given the existence of market failures and hence the benefits from correcting them, this is certainly a misleading assumption. It is clear that when market failure justifies the creation of monopoly (e.g., natural monopoly due to increasing returns to scale), the "waste" from rent-seeking can be, at least partially, offset by the benefits from the correction of market failure. Although this is an important point, our criticism of *TRS* starts from something more fundamental, that is, the concept of "waste."

The most fundamental weakness of *TRS* is the ill-defined concept of "waste." The standard argument is that an individual rent-seeker will spend up to the expected value of his/her rent (his/her chance

¹Here, it is interesting to note the similarity between this argument and the Classical/Marxian notion of productive-unproductive labor. This is a very interesting issue, but we do not have the space to pursue this issue further. For a brief but interesting discussion of this issue, see Boss (1990, pp. 223-6).

of getting the rent multiplied by the value of rent), and then these spendings will, definitionally, add up to the amount equivalent to the whole rent, which are purely "wasted." However, as Samuels and Mercurio (1984) have pointed out, changes in the distribution of rights (which precisely is the aim of rent-seeking behaviors) bring about changes in cost structure, and with a changing cost structure, it is not easy to determine which part of a revenue is a rent element which are "wasted" and which is not.

Even when ignoring the thorny problem of changing cost structure, it is unclear why these resources are "wasted." Can we say that something is "wasted" when it is "spent" for an unproductive purpose? We do not think so. Let us illustrate this point with an example.

Let us suppose that an Industrialist seeking a monopoly right in an industry can achieve his aim in two different ways. He can either bribe the Minister of Industry by buying him a car or ask his lawyer to make a case for a monopoly right in the court. Let us suppose that the cost to the Industrialist is same in each case. Although the costs to the Industrialist are the same in both cases, the two cases have different social outcomes. The first case, bribery, is one of redistribution of income (or what Varian (1989) calls "direct transfer") from the Industrialist to the Minister. The car is not "wasted" because, presumably, the Minister did not need to devote his labor in deciding whether to grant monopoly right to the Industrialist. If he had to expend extra labor to get this decision through, the car is not a "bribery" in a strictly analytical sense, but is a form of informal wage for him (equivalent to the fee to the lawyer).² In this case, only the amount of resources equivalent to the Minister's disutility from the work (which may be measured by the hour spent multiplied by his hourly wage) is a real expenditure (as against transfer) and is "wasted." The central message of *TRS* is that creating allocative inefficiency requires resources (which are "wasted"), but in this case, it did not require resources. In the second case, "production" of a legal service, the resource has clearly produced no value (or what Varian (1989) calls "transaction costs"). The particular legal service diverted the labor of the lawyer from other presumably useful activities (unless he/she was unemployed beforehand) and there is no valued transfer of resources to the Minister (unless he has a perverse preference of enjoying a lobbyist pleading to him).

²Clearly, with pure bribery, we have other problem like income distribution, illegality, morality and so on, but these are not related with "waste."

The essence of the problem is that the sum of individual costs in seeking rent and the social cost or rent-seeking are not necessarily the same. For example, if there were 10 contenders for £50,000 rent, each will spend £5,000 for seeking rent (of course, on the rather unrealistic assumption that they all correctly estimate the amount of rent and their chances of getting it; for a similar point, see Fisher 1985). But if 5 of them use £5,000 each to bribe the official concerned and the rest use £5,000 to hire lobbyists, the social "waste" will only be £25,000, and not £50,000, as the standard *TRS* argues. From the individual point of view, say, the £5,000 spent for bribery and the £5,000 spent for the lobbyist are equally costly, but from the social point of view, they are not.

Therefore, the above quotation from Buchanan is very misleading because he dumps all "[r]esources devoted to effort to curry [the authority's] favor" as having been "wasted." If we are to remain faithful to the concept of opportunity cost (which is usually employed by *TRS*, especially given their Austrian flavor) the "waste" should be defined as the difference between the "rent" and valuation of the transferred resources by the transferee (in our example, valuation of the car by the Minister). The legal service case in our example has no valued transfer, because the lawyer got his wage but had to work for it, whereas our Minister did not have to work in order to get the car.

III. Non-competitive Rent-Seeking

As Tullock clearly states, the basic assumption of *TRS* is "simply that getting a monopoly whether by influencing the government or by getting it privately is essentially a competitive industry" (Tullock 1984, p. 228). The crucial assumption for a competitive equilibrium to exist is that the decisions of the agents are not interactive. If decisions are made interactively, the competitive equilibrium collapses. Certainly, in the real world, everything depends on everything else, however tenuous the correlation might be. Nevertheless, there are good reasons in the competitive model why one agent can act *as if* the decisions were not interactive.

One reason to adopt the "as if" approximation is that, in the competitive equilibrium model, there is no public good. With private goods, one gets as much as one pays and the cost and benefit fall on the decision-maker alone. There is no need to care about others. Introduction of public goods in the model creates complexity be-

cause then we have the problem of collective action or the free rider problem (on the problem of collective action, see Olson 1965; Hardin 1982; Elster 1989). Here my decision depends on what others do, and vice versa. I cannot act as if there is no interaction between my and others' decisions. Another reason to adopt the "as if" approximation is that, in the competitive equilibrium model, there are infinitely numerous and identical agents. Certainly, in real life where the agents are not infinitely numerous, decisions are interactive. Nevertheless, one can act as if there is no such interaction in a large number setting, because given the number of agents in the system, the impact of my decision on others is negligible.

The "as if" approximation, then, can break down in basically two ways. There may be only a small number of agents in a system. Or there may be numerous agents but they are not identically positioned that some of the agents' actions leave visible impacts on the system. In such cases, strategic behavior becomes possible.³ And in the following, we probe what happens when the two crucial assumptions of the competitive equilibrium model (i.e., no public good and large number) are violated.

A. Collective Action

The possibility that rent-seeking might suffer from the collective action problem (since it usually involves organizing an interest group) has already been pointed out by Tullock (1984). Tullock, however, does not clearly specify that the problem of collective action exists only for some kinds of rent, that is, the one generated from a "public" source of rent (named after public good). Let us explain this further.

Irrespective of the group size, there are some rents which cannot be shared with others. Rents from industrial licensing, import quotas, and patents are cases in point.⁴ The sources of these rents are "private" goods in the sense that the sharing of them with others reduces one's benefit. In this case, the problem of collective action simply does not exist, and, therefore, Tullock's argument does not hold. The problem of collective action does exist when the

³We follow Schelling in defining strategic behavior (or strategic move) as "one that influences the other person's choice, in a manner favorable to one's self, by affecting the other person's expectations on how one's self will behave" (Schelling 1960, p. 160).

⁴Terence Moll suggested me that this may be the reason why the protectionist lobby prefer quota to tariff, although I did not have the opportunity to probe this possibility further in an empirical context.

rent is generated from a "public good." Tariff protection will be a case in point, since the fact that others are getting tariff protection does not reduce one's benefit from the protection. When the source of the rent is a "public" good (although the rent itself is a private good; an analogy is that a fishery might be a public good but that the fishes caught from the fishery are private goods) and when the potential rent-seekers fail to organize themselves, the rent will not be dissipated, as Tullock (1984) argues.⁵

A policy implication of the argument is that there are certain types of government policies which are more prone to rent-seeking than others. For example, tariff protection (a "public" source of rent) will result in less dissipation of the rent than import quotas (a "private" source of rent), even if the resulting amount of rents in the two cases are the same (in the short-run when the demand schedule remains the same), simply because dissipation will occur less frequently in the former case.⁶

B. Strategic Behavior

Another important point against standard *TRS* is the rent-seeking does not always, and not even predominantly, involve large number of equally-positioned competitors. When there are not many competitors in a particular rent market, strategic behavior becomes possible where one cannot take the environment as given (for example, as firms' price-taking behavior in a competitive market). In the below, we probe the implications of strategic behavior in a small number setting for *TRS*.

A) Monopolistic Rent-Seeking

Before we deal with the possibility of strategic behavior in rent-seeking, let us look at, as a limiting case of the small number setting, monopolistic rent-seeking, or the "sole contender" case where there is only one contender for rent.

It is possible that there is only one contender for the rent for various reasons. For example, an incumbent firm in, say, the petrochemical industry may become the sole contender of tariff protec-

⁵The problem of collective action does not exist, definitionally, where there is only one contender for the rent, a case not considered by the standard *TRS* arguments (more on this later).

⁶In her seminal work on rent-seeking, Krueger (1974) assumes that there is no rent-seeking in the case of tariff protection. However, it is possible that people may spend resources to acquire tariff (e.g., costs of overcoming free rider problem).

tion because it happens to have a monopoly position due to the state's industrial licensing policy. Or Mr. Brown may be the sole contender in getting the license for the new automobile industry because every other potential seekers of this particular rent knows that he is a brother-in-law of the Prime Minister and therefore is certain to get the license. In other words, rent-seeking can be a monopolistic industry.⁷ In a case where there is a sole contender for a rent, the "dissipation" argument will not necessarily hold, and the outcome becomes indeterminate.

For example, the state may grant a (property) right over the rent at no price to this sole contender on an arbitrary ground (say, because this is a "strategic" industry, or because this corporation is run by a friend of a minister). In this case, the resources devoted to the creation of rent can be minimal. Of course, there is the possibility, as argued by Buchanan (1980, pp. 13-4), that the state will extort all the rent, which in turn is reflected in bureaucratic pay and therefore leads to the "second tier" rent-seeking, where people invest "excessive" resources in education and so on to become bureaucrats, although in this case, the positive externalities generated by more education should be offset against the "waste" due to such educational expenditure.

B) Oligopolistic Rent-Seeking

As soon as we recognize that not all the potential rent-seekers may be equally positioned to join the "rent market" (for reasons analogous to the sole-contender case), there arise many interesting possibilities which go against the dissipation argument.

Small number, of course, does not necessarily guarantee less rent-seeking. There can be cutthroat competition even with a very small number of participants, like the Bertrand price competition. In this case, the competitors will have to compete with each other as fiercely as in the large number case, and the "dissipation" argument holds. Nevertheless, the small number setting is inherently different from the large number setting, where one can act as if one's action

⁷Of course, there is a possibility that there are derivative rent-seekings where people try to secure incumbency in a prospective rent market, and therefore that more resources are "wasted." Nevertheless, this involves an infinite regress (seeking monopoly to seek monopoly to seek monopoly...), which may not be an analytically useful way of envisaging the situation. Of course, this does not exclude the possibility that a monopolistic or oligopolistic incumbency in a "rent market" helps one to build up ability to enter into another such market. Our argument in section IV. A. of this paper is that, rather than multiplying rent-seeking costs, this possibility works to decrease such costs.

		A	
		Bid	Stay Out
B	Bid	(0, 0)	(0, 100)
	Stay Out	(100, 0)	(0, 0)
Payoffs to (A, B)			

FIGURE 1.

does not affect the others', for in the former setting, an individual's best response is affected by those of all others (and the common knowledge about this fact). In a small number setting, one cannot take the "environment" as given. He/she is a part of the "environment." Here, there exists "strategic uncertainty", which results from the fact that one cannot take the environment as given, in addition to "parametric uncertainty."⁸ And strategic uncertainty is a crucial element in a Game-like situation. After all, the use of randomized (or mixed) strategies is a way to prevent other players from capitalizing on the certainty of one's future action.

Certainly, when communication is possible, players in the game may be able to overcome the strategic uncertainty problem by devising a proper binding contracts between them. Here arises the possibility of collusion. The competitors for a particular rent might agree, and make a binding contract between them, that only one will bid for the rent at a price which is far less than the rent, and that they will split the spoil (rent minus the price), rather than compete the rent away. Let us elaborate this point with a simple example.

If there happen to be two firms contending for a monopoly position (say, via acquiring an industrial licensing), which will yield a rent of 100 and if they have an even chance of getting the position, we can suppose a payoff matrix as the following.

In Figure 1, if both bid for the rent, each has an expected payoff of 0, because they run the risk of spending the money but not

⁸The existence of parametric uncertainty also affects the "dissipation" argument. If there is uncertainty about the size of the rent, for example, in the case of a monopoly right to a new industry promoted by the government, the outcome of rent-seeking is not clear (see Fisher 1985), though we may suppose a strong bias against all the rent being competed away (see Rogerson 1982).

getting the rent, one out of two cases ($0.5 \times [100 - 50] + 0.5 \times [0 - 50]$). However, if the two of them reach a binding agreement that one of them stays out, they can acquire the rent without spending any resource. The strategy sets (Bid, Stay Out) and (Stay Out, Bid) are pure strategy Nash equilibria. Which of the two equilibria will obtain is determined by factors like the possibility of credible commitment by one side, the possibility of side payments, and other conditions related to bargaining (for these conditions, see Schelling 1960).

C) *Role of the State in Determining Strategic Behavior*

In considering the role of strategic behavior, we have dealt with the rent-seeking situation as that of a Game between the rent-seekers only. Ideally, we could have introduced the state as another player in the Game, acting strategically to further its own interest. This is not a simple matter and probably requires another paper. Here we discuss the role of the state as an entity which establishes the "rules of the game," in determining strategic behavior.

As Congleton (1980) argues, "artificial scarcity" alone does not create rent-seeking. There should be some means for the rent-seekers to influence the outcome of the contest. If the state is invulnerable to influences, there will be no rent-seeking however big the rent may be. The state can be invulnerable to influences for many reasons.

One possibility is that the state is invulnerable because it is not dependent on any democratic support. "Bureaucratic" regimes *à la* Gaullian France, Japan or Korea, where most of the decision-making power concerning economic policies are in the hands of the bureaucrats, who are less vulnerable to influences because of their job security (no need to be reelected), can be "invulnerable" states in this sense. This may be one of the reasons why these countries could reconcile high degree of intervention with good economic performance, if, as the TRS argues, rent-seeking acts as the major drain on valuable resources from other "socially useful" activities.

Another possibility is that the state is invulnerable because it has abdicated its power to make decision (for this reasoning, see Schelling 1960, Ch. 1). If the state legislates that the methods of "picking the winner" will be genuine lottery, total arbitrariness, equal sharing or rotation (although it is unlikely that these methods will be used in any extensive degree), people will not seek rent for they have no chance of affecting the outcome. In addition, the state can

employ other methods which can significantly reduce the state's vulnerability and hence "waste." Some, though not all, forms of queuing will be one of such methods. Unless queuing requires physically waiting in the line (for example, the queue can be formed by submitting some application), forgoing opportunities for other productive activities, the amount of resources "wasted" in queuing will not be very big.⁹

The third possibility is that the state might be vulnerable to pressure but it decides on the method of "picking the winner" as to generate some beneficial by-products. A method like picking the winner by observing past contribution or future prospect for contribution will make, to borrow from Congleton, some beneficial "by-stander effect," like the case where the contestants are required to use the wealth effectively to generate more wealth or to demonstrate benevolence or altruism" (Congleton 1980, pp.172-3). The fact that those ultra-interventionist countries like Japan and South Korea manage high growth might be also explained in terms of their methods of "picking the winner". To get bureaucratic favors in these countries, say, in the forms of trade protection or of monopoly right in some industry, a rent-seeker should demonstrate his ability to run a large enterprise (or a group of them) efficiently, at least partially offsetting the "waste" from rent-seeking in one industry by improvements in production and managerial capabilities in other industries.¹⁰

IV. Rent-Seeking at the Economy-wide Level

A. Unequal Distribution of Rent-Seeking Opportunities

In section III, we have seriously taken up the possibility of unequal access to the rent "market," which can lead to monopolistic or

⁹Some qualifications, which are due to the discussion with Terence Moll, may be needed here. First, it may be necessary to invest resources to get the qualification to be in the queue (you do not get a license to run a petrochemical plant just because you applied earlier). In this case, the resource is "wasted", although it is possible that they create "socially beneficial" by-products, for example in the form of managerial skills (to prove that you are able to run a modern plant). Second, it may be possible to jump the queue by paying the administrator of the queue, although, as we have argued, the payment to the administrator should not be counted as a rent-seeking cost if the payment does not affect the administrator to expend extra labor to do so.

¹⁰Especially, when the rent involves a new industry, the only viable means to choose the beneficiary may well be looking at its performance in other production activities.

oligopolistic rent-seeking. Now we extend this reasoning to the case where there is an unequal distribution of rent-seeking opportunities. That is, what if there is a small group which has an exclusive access to most of the "rent markets" in the economy?

Tullock argues that in 16th century England and Colonial America, rent-seeking was a major activity on the part of a very small minority of people, and that therefore the total cost was trivial over the economy as a whole (Tullock 1984, pp. 226-7). That is, when a small group has an exclusive access to rent-seeking opportunities, the consequent damage to the economy is relatively small. Tullock's logic is that if we define the total "waste" from rent-seeking (T) as the number of "rent" markets (N) multiplied by the average "waste" from individual rent "market" (W), that is, if $T = NW$, we may have a small total of "waste" (T) where the number of rent "markets" (N) is small, even if the average "waste" (W) is big (that is, even if it is a blatantly corrupt society).

This gives us a clue in explaining the fact that some of the most dynamic economies in the world, Japan and Korea, are precisely those countries where, according to the standard *TRS* argument, there will be the most amount of "waste," given their pervasiveness of state interventions, as we have repeatedly pointed out in the above. In Japan and Korea, however, large conglomerates as a group have an exclusive access to most rent "markets". And, related to our point in the previous section, joining the rank of privileged rent-seekers in these countries is very difficult, if not impossible, except through the demonstration of productive capabilities. Japan and Korea often have very large scale "corruptions" or "financial scandals," but given that the number of rent "markets" are small, the total amount of "waste" does not seem so big compared to the whole economy.¹¹

Having a small group with exclusive accesses to most of the rent "markets," although detestable in many other respects, can further cut down the "waste" for other reasons than are suggested by Tullock's argument (for an application of the following reasonings in a concrete context, see Chang 1990, subsection 5.3.).

First, the members of the small privileged group (be they Japanese and Korean conglomerates or 16th century English MPs)

¹¹With the same logic, we can explain that the apparently least "corrupt" countries like the US and the UK may have a bigger amount of "waste" because, although the average "waste" per market is small, the "rent markets," given the litigiousness of these societies, are so numerous that the total "waste" sums up to a high amount.

usually are *recurrently* engaged in rent-seeking contests between themselves. Because of the recurrence, the set-up costs involved in individual bargaining situations are reduced. First of all, the informational costs of the nature of the opponent (his preferences, his strategy set, his belief about my preferences and strategy set, and his belief about my belief about him, and so on) can be drastically reduced with recurrent bargaining. Moreover, recurrence can lead to more cooperation in the contest than in an one-shot situation. Strategies like temporary unilateral cooperation and retaliation for non-cooperation (the so-called tit-for-tat strategy; see Axelrod 1984, for an extensive discussion of this strategy) become available as inducements to solicit cooperation from the other party, which are not available in the one-shot games. Even if individual rent-seeking games are of Prisoner's Dilemma types, the recurrence can increase the possibility of cooperation, because there is no clear terminal date for the "supergame" (on the issue of cooperation in a "supergame" context, see Taylor 1987; also see Dawkins 1989, Ch. 12).

Moreover, the small privileged group is often engaged in bargainings in many different but related markets at the same time. If different bargainings can be brought together, there may be more possibilities of devising workable side payments, leading to more frequent agreements (see Schelling 1960, pp. 32-3). Industrial restructuring processes in Japan and Korea are examples of this. The majority of firms involved in industrial restructuring in those countries are owned by a small group of conglomerates. Consequently, the conglomerates often can avoid stalemates by forging an agreement that each conglomerate secures monopoly in some markets while exiting from all others, allowing other conglomerates to be monopolists in those markets. This is a contrast to some OECD countries where the fact that staying in or exiting from an industry is a matter of life and death for the firm concerned has made many firms reluctant to reach an agreement for restructuring, resulting in protracted and costly bargaining.

B. Dynamic Benefits of Rent

One important economy-wide implication of *TRS* is that rent-seeking saps resources away from production activities that it hampers growth. This argument has been employed by the proponents of *TRS* to explain the mediocre growth performances of countries like India and Turkey (see Krueger 1974). However, when we compare

the list of interventionist measures, which the sources of rents, in India cited in an article in the *TRS* tradition by Mohammad and Whalley (1984) with the list of such measures in "star-performer" countries like Japan and Korea (see Jones and SaKong 1980, and Chang 1990 for Korea; Johnson 1982 for Japan), there hardly is a big difference between the measures employed in the Indian case, on the one hand, and in the Korean and the Japanese case, on the other hand. But, then, why does one country grow so fast and the other doesn't? Can we reconcile this fact with *TRS* at all?

I think we can, but not in the manner usually employed by the proponents of *TRS*. Obviously, one clue in solving this enigma is to look at the institutional structure of the powerful interest groups (or the ruling class, if you like) of these countries. As we have argued in section III, Japan and Korea have oligopolistic "rent markets," and as we have argued in the previous subsection, recurrence of rent-seeking "Games" among a small group reduces the "transaction cost" involved in rent-seeking "Games." However, a much more fundamental and interesting way of solving this enigma is to bring the dynamic benefits of rent into the picture.

Attainment of high productivity is the *raison d'être* of rents in a capitalist economy, as was argued by Marx's theory of "surplus profit" and Schumpeter's theory of "entrepreneurial profit" (see section I). Rents in a capitalist society lure (in the case of positive rents) and force (in the case of negative rents) firms into more productive technologies, making the economy more productive. To be sure, this beneficial role of rents impinge on the fact that no rent accruing to the innovator is permanent, as was emphasized by Marx and Schumpeter. And it is true that state-created rents can become semi-permanent, allowing their benefits to be swamped by their costs after a certain amount of time (but not immediately, as implied by *TRS*, which assumes away any benefit from state-created rent).

Now, the question is "why do we need state-created rent to persuade investors to invest," as it will be questioned by the proponents of *TRS*, and, I suspect, by Marx himself. Are they not supposed to seek for their own self-interest and invest in whatever lucrative industries? We can answer this question by thinking about patent system for a while. Patent clearly is a system where an artificial rent is created. Of course, it exists because, if others can benefit from my R & D activities, one would not be bothered about investing resources for these activities.¹² Investing in modern industries with

¹²To be sure, even without patents, there is a certain amount of time required for the

large sunk costs and long gestation period, especially in a developing country context where such industries do not exist, is very much analogous to investing in R & D activities. These industries often create externalities that cannot be fully reaped by the investors themselves (e.g., creation of modern industrial labor, creation of modern managerial skills, creation of investment opportunities through linkages). Since investment as a whole cannot be protected by patent, the necessary incentive, the rent, need to be created in other ways (protection, industrial licensing, etc.).

What seems to have happened in Korea and in Japan is that the state has constantly been creating new and often bigger rents in more productive industries, preventing the existing rents to become semi-permanent (see Chang 1990, sections 4 and 5 for a more detailed documentation of the Korean case and a detailed argument of this point in the Korean context). In the Korean case, the dynamic benefits of (state-created) rents in the form of high productivity seem to have more than offset the costs of having such rents (in the forms of the deadweight welfare loss and of rent-seeking "wastes"), as far as they have been important in their magnitudes (we have provided some reasons why they may not be significant in Korea and Japan).

As we have discussed using Korea and Japan as examples, dynamic benefits of rent (especially as an incentive device for investments with positive externalities) do exist and can be very important. With proper institutional arrangements, it can far outstrip the (static, transaction) costs of rent-seeking. Of course, it would be unfair to say that TRS has not recognized dynamic role of rent (it says that seeking rent in a competitive setting is socially productive, as we have seen in section I), but it would not be unfair to say that it has seriously underestimated the possibility that, *even in a non-competitive setting*, the dynamic benefits of rent *can* exceed the costs from rent-seeking.

V. Concluding Remarks

In this paper, we have first summarized the standard TRS arguments to catch up with the innovator. And as is the case with invention and innovation, catching-up is an inherently uncertain matter. Others can catch up instantaneously or they may never be able to do so. Patent is a system which encourages investments in these projects by guaranteeing rent for a certain period of time, and thus freeing the innovator from the fear of being caught up by latecomers.

ment and then tried to examine the problems with its central concept, "waste." And then we tried to explore some institutional factors which can change, in some cases quite seriously, the standard prediction of "rent dissipation." This was done by relaxing assumptions which enable the agents in a competitive system to act as if there is no interdependence of decision-making (and action) in the system. In the single industry context, first, problems of collective action were examined, by making a distinction between "rents from *private* sources" and "rents from *public* sources." Second, we examined monopolistic and oligopolistic rent-seekings, allowing strategic behaviors. Third, role of the state in determining the strategic behaviors of the agents was examined, though we were not able to introduce the state as a player in the "Game." At the economy-wide level, first, the effects of unequal opportunities of rent-seeking among different agents were examined. And, second, the role of dynamic benefits of rent (as against its cost from rent-seeking) was examined.

Our argument was that even when we ignore the conceptual weaknesses of *TRS*, the conclusion of full rent dissipation without proper considerations of institutional settings is far too sweeping. Factors like "publicness" of the source of rent, number of the potential rent-seekers, uncertainty, "vulnerability" of the state, methods of "picking the winner," differential accessibilities to rent markets, and so on, affect the outcome of rent-seeking.

TRS, if used cautiously, can provide interesting insights into issues concerning state intervention, and even growth performances of the economies (as we have tried in a very simple manner), with relatively simple analytical manipulations. Nevertheless, the overly simplifying assumptions about behavior and institutions employed in many, if not all, of the works in the *TRS* tradition make this potentially very interesting theory a confused ideological muddle.

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