

The Incentive Problem of perks in public sector

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One thing that differentiates public sector from private sector is the incentive. While private sector thrives on profit maximization and competition, firms run by state or in collaboration with the state run short of it. According to normative economics, it is clear that for any economy to work efficiently, it is very important that there is perfect competition and that producers are profit maximizers while consumers are rational and utility maximizing. In absence of any of these, resources are not efficiently allocated.

The economies where major industries are controlled or run by state suffer from a huge incentive problem. For instance, when a firm is owned by an individual, he would try to increase his profits as much as he can and hence, would try to cut the costs; thereby leading to efficient use of limited and scarce of resources. However the situation becomes a lot different in case of public sector. The managers and administrative staff don't reap the benefits of increased profits of the firm hence they don't have any incentive to cut costs. This leads not only to reduced efficiency but also higher costs.

One way to tackle this problem is to give perks to the workers and staff whenever the firm does well. Again , this solution has drawbacks. Perks lead to increased costs which have to be accounted for when calculating the firm's profits. The idea behind giving perks is to encourage people to work hard and increase productivity. For example, Ford's 1 \$ bonus for assembly line workers in 1900s became a rage at that time and led to great improvements.

Perks are a good way of solving incentive problem in public sector despite the fact that they increase costs of production. Therefore while deciding whether to give perks to workers, it has to be analyzed that whether increase in profits outweigh the increase in costs. And most importantly, vigilance is required to see that they are not misused and perks are proportionate to person's performance.