

NEW ZEALAND ASSOCIATION OF ECONOMISTS (INC.)
P.O. BOX 568, WELLINGTON, NEW ZEALAND

Issue no. 23

July 2005

ASymmetric information

**A newsletter to promote the exchange of information,
news and ideas among members of the
New Zealand Association of Economists (Inc).**

CONTENTS

Editorial	2	Popper and Smith	15
Albert Rex Bergstrom	3	The 2005 Conference Reports	16
The 2005 Budget	5	Conference Photos	20
The Philpott Dataset	6	Social Capital a Misnomer?	22
From the 2BRED file	7	The Scourge of Deflation	23
Bureaucrats and Incentives	8	Lord of the Regions	23
Paradigm-based Reasoning	9	Schopenhauer	24
Government - MPs	10	Research in Progress	25
Government – public servants	11	Boys Disadvantaged in Education	27
Generations and Perspectives	12	NZEP	28
The Electrical Age	14	NZAE Information and New Members	28

REMINDER: NEXT NZAE ANNUAL CONFERENCE
28TH - 30TH JUNE 2006
WELLINGTON

THIS CONFERENCE IS A MUST FOR ALL ECONOMISTS!!!

Past Issues of Asymmetric Information...

All past issues are now available for downloading (or for citing in scholarly publications)

FREE OF CHARGE From: <http://www.nzae.org.nz/newsletters/>

Is economics efficient?

EDITORIAL

After a stimulating conference, there are several themes running through this *AI*. Are we looking at issues in the best way? Are our approaches overly restrictive? Are we aware of inherent distortions in our perspectives? What are the matters which merit greatest attention, or for which our efforts might promise the greatest rewards?

Central to these questions is the acknowledgement of the limitations to our understanding, and the danger from failing to appreciate these limitations. On several occasions at the conference, mention was made of the benefits of tool building to assist in research. Less was said about the value of different types of tools. Should we be trying to develop more sophisticated tools (development at the “top end”), or more robust, basic tools, transparent and easy to apply, that might limit errors at the “bottom end”? Can we determine ideal outcomes, or are we simply trying to reduce the number of serious blunders that are made?

In his keynote address, John McMillan mentioned Karl Popper’s *The Open Society and Its Enemies*, so I looked it up. Popper talked about Utopian engineering and piecemeal engineering (Vol.1 chapter 9). The Utopian requires that the Ideal State be determined before policies can be put in place to achieve it. By contrast, “the piecemeal engineer will...adopt the method of searching for, and fighting against, the greatest and most urgent evils of society, rather than searching for, and fighting for, its greatest ultimate good” (p.158).

Popper also wrote, “...it is helpful to formulate the task of scientific method as the elimination of false theories (from the various theories tentatively proffered) rather than the attainment of established truths” (Vol.2, p.285). It may be that much can be gained simply by correcting for false perceptions. These take little effort to identify, but can be very hard to modify. Research is only a small part of this process. The diffusion of research findings is also a key component.

In Popper’s preface is written, “...if our civilization is to survive, we must break with the habit of deference to great men”. This seems like a good idea. There is also a play about Gramsci where, in a speech, he says, “Beware rhetoric, even mine”, an equally appealing thought. It is a mark of respect to take someone’s views seriously and subject them to serious questioning.

At the conference, it was suggested that economics should be thoroughly mathematical. I recently had a pleasant sojourn in the pages of Adam Smith’s *Wealth of Nations*, but found it hard to see what all the fuss is about. I found no equations there. Presumably Smith would not get far under today’s peer review processes. On the other hand, perhaps it is clear thinking that is required for good economics, and mathematics can assist with this. However, we can sometimes be constrained to think only within the limits of the mathematics being applied, regardless of the validity of the economic assumptions that this requires.

by Stuart Birks, Massey University

Lags in Policy Implementation

The Commerce Commission’s *Communique* Issue 9, March 2005, referred to the Credit Contracts and Consumer Finance Act 2003, which came into full force on 1 April, Commission Chair Paula Rebstock: ...says the Commission has been working hard to ensure credit providers are aware of the law change and the need to comply. Promotion of the new Act has included seminars and the production of a guide for industry participants, along with extensive staff training. The industry has also had 18 months to prepare for the changes. (p.1)

We invite members to submit a brief article on any issue of interest to NZAE members, and/or comments and suggestions. Enquiries and contributed articles should be sent to Stuart Birks and Gary Buurman [K.S.Birks@massey.ac.nz]. Views and opinions expressed in these articles are those of the authors, and do not represent the views of the New Zealand Association of Economists.



Albert Rex Bergstrom

Pioneer of Continuous Time Economic Models

Rex Bergstrom, former Professor of Econometrics in the Department of Economics at the University of Auckland, died on Sunday morning May 1 in the Royal Free Hospital in Hampstead, London. He was aged 79 and passed away in his sleep. He was admitted a week earlier following a fall in his apartment in London. His funeral was held in London on Friday May 6 at Golders Green. Several of his former Ph.D students at the University of Essex attended and the flag flew at half mast at the University of Essex on this day. A eulogy of Rex was delivered to the Senate at the University of Auckland on May 9.

Rex was New Zealand's first econometrician and a Fellow of the Econometric Society. At the time of his death, he had just completed a new book (co-authored with one of his former students from the University of Essex, Ben Nowman), which develops and estimates the latest version of his econometric model of the UK economy, allowing for stochastic trends. He was planning to stay in London to see the book in print at the LSE bookshop before returning permanently to New Zealand to be with his family.

Following the publication of a path-breaking article in *Econometrica* in 1966, Rex Bergstrom became the world's leading exponent of continuous time econometric modeling. The subject now has an extensive audience of theorists, econometricians and practitioners. Ongoing work is particularly active in financial econometrics. Rex's main interest was in economy-wide models of economic activity. Since aggregate economic activity continues without interruption between the discrete observations we make of it, Rex was convinced that the best way to model modern industrialized economies was in terms of stochastic differential equations. His contributions cover the entire field of research on this approach, encompassing the development of cyclical growth models, econometric methods of estimation, and major empirical implementations of the methodology. Most of his career was devoted to the task of building these models and developing tools of estimation. Following a prototype model that he designed for the UK economy (the so-called Bergstrom-Wymer model), economy-wide models of this type have been constructed for many of the world's leading industrialized nations, including the USA, Italy, Germany, Sweden and the Netherlands.

Rex's pioneering work and accomplishments in this field are an extraordinary testament of academic devotion. The work may not have had the impact he would have wished for it in macroeconomics. But his conviction of the importance of the continuous time approach has been truly vindicated in the world of finance, where ultra-high frequency, second-by-second transactions data are now widely available and used to price options and other financial derivatives, to measure market volatility, and to fit nonlinear stochastic differential equations.

It is an especially sad moment for New Zealand econometrics. One half of Rex's working academic life was spent in New Zealand and his impact on quantitative economics in this country has been enormous. Over the period 1950-1970, he trained successive generations of New Zealand economists. Hugh Fletcher, the Chancellor of the University of Auckland, Alastair MacCormick, the founding Head of the School of Business and Economics and former acting Vice Chancellor of the University of Auckland, and Viv Hall, the McCarthy

Professor of Economics and former Head of the School of Economics at Victoria University were among Rex's students at the University of Auckland during the 1960s.

When Rex joined the Department of Economics at the University of Auckland, the department had a complement of only 4 people, led by Colin Simkin. During his time at Auckland, Rex taught virtually all the courses in the department, including money and banking, public finance, and all the economic theory courses as well as econometrics. In the 1960s he developed an econometrics sequence that was the equal of the best Ph.D courses offered in North America and Europe. Rex supervised many dissertations at Auckland during the 1960s, encouraging his students to do empirical research on various aspects of the New Zealand economy. His students subsequently went on to become academics in economics, accounting, marketing, and econometrics, and to work in industry or government.

In addition to the two decades he spent at Auckland, Rex also played a key role in developing econometrics in the UK, starting at the LSE over 1962-1964, and later at the University of Essex. The 1960s was a period when the LSE took over from Cambridge as the leading centre in econometrics in the UK. During his time at LSE, Rex published in *Economica* a model of cyclical growth, extending earlier trade cycle models by introducing production, and earlier growth models by including cyclical behavior. This work provided the first disequilibrium model of neoclassical economic growth, building on earlier research by Bill Phillips, who was then a colleague at LSE. In 1967, Rex published his influential monograph on *The Construction and Use of Economic Models*, which elegantly expounded these models of growth and cycles, synthesized developments in the area, and laid out an econometric framework for fitting these models with observed data. In 1970, Rex moved from the University of Auckland to the University of Essex, where in addition to his academic work and to supervising several Ph.D dissertations in econometrics, he served as Chairman of the Department of Economics, Dean of the School of Social Sciences, and Pro-Vice Chancellor.

All of Rex's work bears the hallmark of exemplary scholarship. He held a deep concern for fundamental issues in economics, was a lucid thinker and a fine expositor. His lectures in microeconomics and in econometrics were models of clarity. His research was ambitious and original. In addition to his work on continuous time modeling, he initiated studies on the exact distribution of econometric estimators, providing for the first time (concurrently with independent work by Robert Basmann in the US) the finite sample distribution of the maximum likelihood and least squares regression estimates in a simple Keynesian model of simultaneous equations. After the publication of Rex's paper in *Econometrica* 1962, Trygve Haavelmo a later Nobel Laureate in economics, came rushing up to Rex at a conference telling him how excited he was about Rex's results and how he had himself tried to obtain these formulae for over a decade. Rex told me the problem yielded to a concentrated mathematical effort that he made in three weeks over a New Zealand summer. One of Rex's greatest loves was the subject of mathematics. The economy and precision of his own mathematics shine through in all his work, but especially so in this particular article in *Econometrica*.

Rex's passing is a great loss for the profession of economics and this loss will be dearly felt by a wide community of scholars throughout the academic world. Many economists, accountants and other professionals, both in New Zealand and in the UK, hold with pride a Bergstrom pedigree. We have much to remember of the times when Rex guided our work, taught the classes we attended, and influenced us through his writings and research. These wonderful memories of Rex we will carry forward throughout our own lives.

Peter C. B. Phillips
May 2005

The 2005 Budget and Children¹ by Dr Susan St John, s.stjohn@auckland.ac.nz

If you listened carefully to the budget there were some nuggets for children- \$47m more spending on sure start targeted services for families in need, more for after school hours care for working parents, and a welcome extra 300 new houses a year for South Auckland. But the clear message from budget 2005 is that the Working for Families package announced last year is all that will be done for the incomes of poor families for the next 3 years.

The centrepiece of this budget is the savings scheme. To its credit, the government has tried desperately hard to design a savings sweetener that does not give the most to the rich. But the kiwisaver is not going to help the immediate problems of low income families. The \$1000 tossed in by the state is only if you contribute at least 4%- regardless of your family obligations and family size. It is another classic example of a policy that has had no child impact analysis attached to it at all.

The kiwisaver can be used for a first home deposit after at least three years of contribution and after five years it attracts a subsidy of \$5000. No-one will get \$5000 until 2012 and it will be income tested. The devil is in the detail, but only 3000 households per year are likely to qualify. Worthy as it may be, this will do nothing for child poverty. Poor children born today into poor housing will have already had the seven most formative years of their life by 2012.

On international measures, we have 14.7% of children in 2005 living in households under 50% median income. NZ is one of the very worst in the OECD. But 50% is an impossibly low level of income-and lower than the poverty line that MSD uses. For a 2 parent, 2 child family it means \$23,300 to support four people. Even after some help from the accommodation supplement, rents are likely to absorb a large portion of that income - it is no wonder that families have been queuing up at our food banks.

Last year, CPAG cautiously welcomed the Working for Families package acknowledging the very real shift in political climate that at last placed the focus on family incomes. It undeniably gives a significant real income boost to many families who are in work, but many aspects of the package are disturbing.

It was a long time arriving. It was cold hearted to identify child poverty and then make children wait for any extra family support for a full year, after already waiting since 1996. But worse than that, the very poorest children did not get much at all this April. For example a couple on a sickness benefit with one child gains \$7.50 a week and gets nothing more for two years.

Under the cover of WFF, the core benefits were cut for those with children and this year, hardship provisions are also attacked, saving in total a massive \$230m per annum. In this period real per capita incomes have been growing, so in relative terms beneficiaries with children have fallen even further behind.

Growing inequality demands that the emphasis on work as the way out of poverty has to be balanced by deliberate sustained and generous redistribution to low income people both in and out of work, especially where there are children.

The Child Tax Credit remains until 2006 when it is replaced by an equally divisive and discriminatory 'In Work Payment'. Families getting the 'In Work Payment' in 2006 will be significantly better off with an extra \$60 a week or more than others not in work. But what happens when the next recession strikes, as it will? In good economic times or bad, if a sole parent cannot sustain 20 hours in employment a week, a big ask for a mother with young children, she will lose the \$60+per week In-Work-Payment. Her children have the same needs as they had before, but now will have to drop out of activities that their mother can no longer support.

In Budget 2005 there is no rhetoric around the plight of the low paid or even a doffing of the cap to the existence of child poverty. This is in sharp contrast to the concerns about growing inequality and child poverty expressed openly in other OECD countries and in the OECD itself (OECD Observer March 2005).

George Bernard Shaw said in 1907 'The greatest of evils and the worst of crimes is poverty' This month's Observer remarks "more than 100 years later this observation is truer than ever, for it is against the backdrop of today's wealthy OECD countries that the costs of poverty seem so large and reprehensible."

¹ From an address for the Child Poverty Action Group Budget Breakfast

Just found this:

“...increasing wages paid to workers in vocation-intensive sectors (such as nursing and teaching) may be more costly than just the payroll cost. Other things being equal, a lowly paid nurse is more likely to have a vocation, and so over-perform in his role, than a highly paid one. This accords with our intuition that a higher wage may attract the ‘wrong sort’ of person.”

[P.568 of Heyes A (2005) “The economics of vocation or ‘why is a badly paid nurse a good nurse?’” *Journal of Health Economics*, 24(3), May, pp.561-569]

...which explains why New Zealand universities attract a better type of person J

Efficiency in Research

“Forty years of empirical experience in macroeconomic forecasting suggests that there are limits to our capacity to make predictions about economic activity. In fact, the performance of aggregate predictions has improved little over this time in spite of much early optimism, enormous bodies of research in macroeconomic theory and modelling, improvements in econometric methods, and larger datasets of better quality.”

[P.C26 of Phillips P C B (2003) “Laws and Limits of Econometrics”, *Economic Journal*, 113 (March), pp.C26-C52]

So what is the value added of these advances, and are they cost-effective? Should we be concerned about efficiency in research? Is this distinct from meeting PBRF criteria?

Some Recent Updating of the Philpott Data Set

During the year I have been working on updating the Nominal Gross Output and the Nominal Intermediate Consumption industry sets in the Philpott collection. The main issue is to convert the Statistics New Zealand industrial classification from ANZSIC to NZSIC - the one Philpott employed. I have used the concordances for GDP in 1987-88 derived in my 2004 paper to the NZAE Conference (“Making ANZSIC Work for Economists”) for aligning nominal Gross Output and Intermediate Consumption. In addition I have employed the PPI-Inputs set to derive the Intermediate Consumption series in real terms by industry. This is a change in methodology from that Philpott used for this category. The Gross Output and the Intermediate Consumption sets covered 1959-60 to 1990-91 and the additions bring them up to 2001-02.

Previous work updated the following sets:

- a.Nominal GDP by NZSIC industry in current prices to 2001-02.
- b.Real GDP by NZSIC industry in 1995-96 prices to 2001-02.
- c.Real GDP by NZSIC industry in 1982-83 prices to 2001-02.
- d.Labour Employed in Full-Time Equivalents (FTE's) to 2001-02.
- e.Nominal Gross Capital Formation by NZSIC industry at current prices to 2001-02.
- f.Real Gross Capital Formation by NZSIC industry at 1982-83 prices to 2001-02.
- g.Real Gross Stocks of Capital by NZSIC industry at 1982-83 prices to 2001-02.
- h.Real Net Stocks of Capital by NZSIC industry at 1982-83 prices to 2001-02.

Please contact me for details of the methodology and the respective tables.

Robin Johnson (johnsonr1@paradise.net.nz)

From the 2BRED File

by Grant M. Scobie (grant.scobie@treasury.govt.nz)

I start this time with a review by a "guest reviewer". Bob Buckle has kindly allowed me to reprint a note he has written on a new book by Brian Snowdon and Howard R. Vane entitled *Modern Macroeconomics: Its origins, development and current state* (Cheltenham: Edward Elgar, 2005).

Bob writes:

Improved economic growth and a stable and sustainable macroeconomic environment are two key objectives for economic policy. The way economists think about these issues and the role that government policy can take in achieving better macroeconomic outcomes has changed markedly over time and continues to evolve. It is important that economists working as policy advisors keep abreast of these developments, but doing so is a significant challenge.

Brian Snowdon and Howard Vane have skillfully written a non-technical guide to the development and current state of macroeconomic and growth thinking from an historical perspective. The book opens with a review of the development of macroeconomic thinking and key international debates of the past century, including a fascinating snapshot of the Great Depression. Subsequent chapters provide more in-depth explanations of the various schools of thought ranging from the early "Keynesian" macroeconomics, the "new-classical" and "real business cycle" challenges through to the "new-Keynesian" macroeconomics.

Also included is an explanation of the "Austrian School's" view of macroeconomic fluctuations, a perspective that books often overlook. A feature of the book is interviews with the world's leading theorists (typically Nobel prize winners) in these respective areas of macroeconomics.

A significant improvement over their 1994 book "A Modern Guide to Macroeconomics", is the inclusion of two chapters that significantly enhance the book's value to New Zealand economic policy advisors. Chapter 10 surveys the burgeoning literature on the nexus between politics and macroeconomic outcomes (the "new political macroeconomics") and traces through explanations of political business cycles, the significance of time inconsistency, the political barriers to economic growth and the more recent literature on the size of nations. An interview with Alberto Alesina concludes this chapter.

Chapter 11 covers the history and renaissance of theories of economic growth. This is the place to go for an introduction to the neoclassical and endogenous growth theories, for an understanding of the significance for growth of convergence, the economics of ideas, and the importance to growth of institutions and political structures. Interviews with the growth gurus Robert Solow and Paul Romer round off this chapter.

If like Blaug you "have never been able to grasp how one can understand any idea without knowing where it came from, how it evolved out of previous ideas..." this is the macroeconomics primer for you. If you wish to test your own knowledge of the key issues in economic growth and macroeconomic stability, this is also for you. If you wish to read Nobel prize winners views on these topics, this book is for you.

Ron Chernow has produced a magnificent biography of *Alexander Hamilton* (New York: The Penguin Press, 2004). There is a host of reviews which can be found at http://www.reviewsofbooks.com/alexander_hamilton/. I have taken the following from this website as it is as good a short synthesis as I could produce. But let me warn you... this is a very large book. It took me weeks to read but was certainly rewarding. It is a fascinating tale of boy from a totally chaotic and dysfunctional background who rose to powerful positions and shaped the USA as a nation – to his demise as Secretary of the Treasury in a duel with the Vice President. As an employee of the Treasury I hasten to add that in no way does this imply that I condone or encourage differences between today's Secretaries of the New Zealand Treasury and their political masters being settled by duels.

Ron Chernow's biography of Alexander Hamilton brings to life a man who was central to the formation of the United States, but is most often remembered, if at all, for being killed in a duel with Aaron Burr in 1804. He traces the arc of Hamilton's life from his birth in poverty on

an obscure Caribbean island, to his days as a pamphleteer in New York, his roles as aide-de-camp to General Washington and hero during the Revolutionary War, his authorship of most of the Federalist Papers, and his role as the first Secretary of the Treasury of the new United States government. Hamilton was a fiery writer and debater who believed in a strong central government, often quarreling with Jefferson, Madison, and other founding fathers. This intense behavior also led to an affair with a married woman whose husband blackmailed him, and his ultimate undoing in his feud with Aaron Burr. *Alexander Hamilton* has received mostly positive reviews. The Rocky Mountain News calls it "a book that does such a fine job, not only of bringing Alexander Hamilton to full and varied life but of providing the reader, as well, with a richly textured picture of the America that was emerging from the blood and turmoil of the Revolutionary War."

On the young George Washington:

...what set George apart from other tall and robust Virginians was the intensity of his determination to better himself. He copied rules into a notebook that would guide him in making his way in the world. When speaking to men of quality, for example, he was not to look them full in the face. At meals, he shouldn't clean his teeth on the tablecloth.

[P.291 of Langguth A J (1988) *Patriots: The Men Who Started the American Revolution*, New York: Simon and Schuster]

Bureaucrats and Incentives [SB]

William Niskanen has discussed the incentives faced by bureaucrats¹:

The rationality of budget maximisation by bureaucrats may best be illustrated by considering the consequences of contrary behaviour. Consider the probable consequences for a subordinate manager who proves without question that the same output could be produced at, say, one-half the present expenditures. In a profit-seeking firm this manager would probably receive a bonus, a promotion, and an opportunity to find another such economy; if such rewards are not forthcoming in a specific firm, the manager usually has the opportunity to market his skills in another firm. In a bureau, at best, this manager might receive a citation and a savings bond, a lateral transfer, the enmity of his former colleagues, and the suspicion of his new colleagues. Those bureaucrats who doubt this proposition and who have good private employment alternatives should test it...once.

However, a bureaucrat could only test half of the proposition, that relating to the situation of the bureaucrat. Is it really different in profit-seeking firms? There was a Feltex share float last year at \$1.70 a share. The share price subsequently collapsed to 39c following very poor profit announcements.² This raised some issues. In particular, why weren't people warned?

Macquarie Equities research director Arthur Lim agreed it was difficult for brokers to publish research which went against information from a subject company.

"Analysts do their own work independent of what the company says," he said. "But there is a sense in which you are damned if you do, and damned if you don't."

"You could do work and come up with your own forecasts, but if companies come up with their own guidance, they will be the ones that the market – institutions as well as retail investors – will listen to. Because who is really in a better position to give a view of how things are going than the company?"

"Those who stick their necks out had better be right, because there are no prizes for being right and there is every punishment for being wrong. The company stops talking to you and the fund managers and investors think you are an absolute wally."

In other words, the brokerage company would be taking a big risk, and so is unlikely to reward its broker for behaving in this way.

¹ Footnote 1 on p.23 of Niskanen W A (1973) *Bureaucracy: Servant or Master*, London: IEA.

² Ninness G and Sheeran G (2005) "Broker: We blew it on Feltex", *Sunday Star-Times*, 26 June, <http://www.stuff.co.nz/stuff/0,2106,3325898a13,00.html>

Paradigm-based Reasoning [SB]

In the first chapter of his textbook, Eugene Silberberg attempted to show “the powerful nature of the economic paradigm”¹ (p.9). He took as an example the rise in women’s labour force participation in the past generation (i.e. up to 1990), seeking an economic explanation. He referred to constancy of tastes as a simplifying assumption in the neoclassical economic paradigm. Moreover, “to accept (changed tastes) as an explanation of observed events is to abandon the search for an explanation based on systematic, and therefore testable, behavior” (p.7). Hence, “We reject out-of-hand any explanation based on changes in tastes” (p.7).²

He identified, as a “wide ranging constraint that changed during the 1960s”, the ratio of young women to men a few years older. The post-WWII baby boom meant that there was a shortage of marriageable men for these women due to lower birth rates in the war years. Marriage was not an option for many young women, and so they pursued careers.

This is plausible, assuming low rates of divorce and no change in the relative ages of marriage partners. Silberberg goes further, predicting a return to more traditional lifestyles during the 1990s as the gender imbalance disappears. The economic paradigm may be powerful, but events in the 1990s did not support his prediction. There was a leveling off of female labour force participation, but no sharp drop in the 1990s, and there was increased participation by mothers.³

We could ask why he finds it so objectionable to consider the possibility of changes in tastes. They may not be unobservable, and even if they are difficult to identify, it could be wrong to disregard them simply because there is an alternative plausible explanation. The existence of one possible explanation does not exclude the possibility of others. If each generation has its own perceptions (possibly distorted, see p.12), why shouldn’t tastes change?

Silberberg illustrates what could be called “paradigm-based reasoning”, whereby it is important to explain events within a particular paradigm. The result is then considered to be sufficient, even though there may be alternative explanations. This is similar to the idea of “consistent” results. For example, someone could present a hypothesis and find it supported by the data. The data could also be consistent with a wide range of alternative hypotheses, but these are not explored. In terms of reasoning, this allows people to cling to a paradigm until it fails so badly that it has to be rejected. Even that might not be enough. There has to also be “a better approach on offer” (Phillips, 2003, p.C27, quoting Hoover). This may hinder, rather than assist, understanding. Perhaps more dangerously, it could lead us to have an inflated view of our level of understanding.

We can pursue this avenue further. In the context of paradigm-based reasoning, the text book theory of the firm could be called a Claytons theory of the firm, the firm to look at when you are not looking at a firm. If there is an actual firm to consider, presumably we should try to model the production and cost structures as observed for that firm, rather than attempting to squeeze the firm to fit a text book model.

Differentiable production functions with continuous, smoothly curved isoquants suggest an available technology for each of a wide range of capital/labour ratios. It is more likely that there is a limited number of viable technologies that have been developed for the production of each good. If so, a linear programming approach might be more realistic than one based on marginal analysis. That could still give problems, the assumption of constant returns to scale for example. Importantly, though, it raises the possibility of a very different set of solutions, whereby changes in circumstances may result in either no change or a large change in the optimal position. The standard paradigm could be highly misleading. As with any issue, a greater understanding can be obtained when it is viewed from a range of perspectives.

¹ P.9 of Silberberg E (1990) *The Structure of Economics: A Mathematical Analysis*, New York: McGraw Hill

² Note, however, Bowles, S (1998) ‘Endogenous preferences: The culture consequences of markets and other economic institutions’, *Journal of Economic Literature*, 36(1), pp75-111.

³ See Davis C, “Female Participation in the Labor Force”

<http://fubini.swarthmore.edu/~WS30/CDfinal.html>

Government – MPs by Stuart Birks

With an election due, and MPs playing a major part in determining policy, it may be worth asking what we can expect from these people. Some indication is given by Labour MP Tim Barnett, who has a document on his web page giving advice on lobbying.⁴

Under “Identifying and analyzing lobby targets” he describes MPs as: driven by media coverage; expert on a few things; averaging 6 years in parliament and fearful of losing their jobs; spending their days hopping from one issue/place to another; overwhelmed by an endless stream of faxes, etc.; having many decisions made for them (party agreements, policies and manifestos); and less powerful than they think they are.

He suggests, if meeting with an MP, not that you should know about your subject, but, “Only admit to ignorance if comprehensively cornered. If they ask a question, try and avoid saying that you don’t know”. If making an oral submission to a panel, “Use anecdote, especially personal experiences, to get panel members on your side. Telling a story about an issue, and/or talking about yourself, is a good way of getting a message over.” Would these MPs really want to hear from economists reporting on their analyses?

Another insight was given by ACT MP Deborah Coddington. As reported in *The Dominion Post*⁵, she said, “I’m so happy to be married to Colin that I find it difficult coming into the House and attacking people. I’m not angry any more. And I don’t see things in black and white.” While we should not generalize from case studies and anecdotes, it does provide a hypothesis that MPs may be angrier and more judgmental than the average individual.

There may be broader problems in the way parliament operates. Keith Jackson wrote⁶:

...unlike many other countries, parliament provides little real training for elected candidates. The future representatives of the nation are expected to learn their role on the job...new MPs are not imbued with the principle of what parliament is supposed to be about...The traditions of such a parliament quickly become the memory of the oldest member and the conditions prevailing when any particular member is socialised into the process.”

Once in government, there are additional problems. Marilyn Waring wrote that, in 1975, Prime Minister Muldoon had to fill 27 positions (a Cabinet of 20, two whips, a speaker, chairman of committees, and three under-secretaries) from only 30 MPs with previous parliamentary experience⁷:

“He was then stuck with his colleagues until death, sickness, or other political shocks removed them, reflecting the reality that there are only a few able people in any party and a cabinet of twenty exhausts the available supply...An important consideration in portfolio allocation is how to place some ministers in portfolios where they could do the least damage. (pp.46-7)

It is interesting to note that 13 of the 30 MPs were farmers. Also, by way of comparison, Waring states that, in 1979, Margaret Thatcher was able to select a cabinet of 22 from 339 MPs. This was in fact the total number of MPs, following a swing giving a gain of 62, so it does not represent the number of MPs with experience. The 1975 National government had 55 MPs.

Back to Keith Jackson, “...select committee places have to be distributed among a limited number of MPs, with the incidence of service falling more heavily upon government party members who have to maintain a majority in every committee without using members of the cabinet.” (p.118)

This, together with the problem of selecting cabinet members, suggests that there are a large proportion of first time MPs representing the government on select committees, of which there are now 20.

⁴ Barnett T (2002) *Lobby Pack*, <http://www.timbarnett.org.nz/documents/lobby%20pack%20model.doc>

⁵ “ACT MP gives up politics”, *The Dominion Post*, 16 April 2005, <http://stuff.co.nz/stuff/0.2106.3250262a10.00.html>

⁶ P.74 of Jackson K (1987) *The Dilemma of Parliament*, Wellington: Allen and Unwin and Port Nicholson Press

⁷ Waring M, “Revitalisation of Cabinet, Parliament and Parties”, in Hoadley J S (1979) *Improving New Zealand’s Democracy* Auckland: NZ Institute for Peace Studies

This does raise the question, whenever there is a change of government, how many of the new government's MPs will have previous parliamentary experience? Of these, how many will have previous cabinet and ministerial experience? More generally, how much power can we comfortably and safely place in such people's hands?

Government – public servants by Stuart Birks

It would appear that New Zealand is supposed to be following the Westminster system of a politically neutral public service. The following is an extract from Greaves H R G (1947) *The Civil Servant in the Changing State*, London: Harrap (pp.48-9). It refers to a commission that reported in 1931:

Sir Warren Fisher, in a paper handed in to the Tomlin Commission, defined the duties of the civil servant authoritatively. He wrote: "... it is the traditional duty of civil servants, while decisions are being formulated, to make available to their political chiefs all the information and experience at their disposal, and to do this without fear or favour, irrespective of whether the advice thus tendered may accord or not with the minister's initial view...The preservation of integrity, fearlessness, and independence of thought and utterance in their private communion with ministers of the experienced officials selected to fill the top posts in the service is an essential principle in enlightened government...it enables [ministers] to be assured that their decisions are reached only after the relevant facts and the various considerations have, so far as the machinery of government can secure, been definitely brought before their minds..."

The State Services Commission has a fact sheet on the subject, including the following on "free and frank advice"¹:

Public servants are required to provide free and frank advice to their Ministers, ie advice that is honest, impartial and comprehensive...Free and frank advice is not always advice that Ministers want to hear. While public servants need to be well-informed about the government's stated policies, and sensitive and responsive to Ministers' policy objectives, they must also take into account the broader public interest and be seen to be politically neutral...Therefore:

- *public servants need to alert Ministers to the possible consequences of following particular policies, whether or not such advice accords with Ministers' views (or the views of the individual public servant);*
- *the advice provided needs to be free of personal or agency/sectoral interests, it must be transparent, and it should not contain unclear or hidden agendas; ...*
- *similarly, important known facts should not be withheld.*

Parliamentary Question for Written Answer no.7396 (2005) asked, "Has the Ministry of Women's Affairs provided any advice or reports on family violence perpetrated by women; if so, what was the dates and titles of the advice or reports provided?" The answer focused on intimate partner violence, thus omitting child maltreatment, and asserted, "Given that intimate partner violence is carried out predominantly by men against women the Ministry of Women's Affairs is currently primarily focused on women as victims of violence." There were no reports on the magnitude or implications of women's violence. As for just one known fact that appears not to have been mentioned, the Dunedin longitudinal study found higher rates of partner violence by women.² We could ask to what extent Ministries with responsibility for specific sections of the community are fulfilling their duties in a neutral manner.

Another matter of concern, and raised in the first bullet point above, is the extent to which policy advice includes solid assessments of the possible consequences of proposed policies. Previous issues of *AI* have indicated deficiencies with Regulatory Impact Statements. A broader consideration is people's changed behaviour as a result of the changed policies.

¹ State Services Commission, *Political Neutrality: Fact Sheet 3 - The Relationship Between the Public Service and Ministers*, Last updated 25/9/2003,

http://www.ssc.govt.nz/display/document.asp?navid=183&docid=3995&pageno=2#P51_5389

² See exhibit 2 on p.4 of <http://www.ncjrs.org/pdffiles1/170018.pdf>

Generations and Perspectives by Stuart Birks

If behaviour is based on perceptions, and perceptions are influenced by experience, it could be argued that each generation may have its own impression(s) of events, and may therefore have its own unique concerns and behaviours.¹ Perceptions are also shaped by the information being presented, and this is often inaccurate. We see many signs of both changing concerns and distorted perceptions.

Popper wrote of Marx²:

For Marx lived, especially in his younger years, in a period of the most shameless and cruel exploitation. And this shameless exploitation was cynically defended by hypocritical apologists who appealed to the principle of human freedom, to the right of man to determine his own fate, and to enter freely into any contract he considers favourable to his interests... In view of such experiences, we need not wonder that Marx did not think very highly of liberalism, and that he saw in parliamentary democracy nothing but a veiled dictatorship of the bourgeoisie.

We should also note that Popper was writing *Open Society and Its Enemies* during the Second World War, so it is also not surprising that his focus was on tyranny and democracy.

Snowdon and Vane³ write, "The lessons from the history of economic thought teach us that one of the main driving forces behind the evolution of new ideas is the march of events" (p.9). Discussing the Christina Romer's work, "the Great Depression was not the norm for capitalism but a truly unique event" (p.17). Nevertheless, it shaped people's perceptions of the world and the workings of the economy as if it could be a recurring phenomenon.

It is only recently, sixty years after the end of WWII, that the relative magnitudes of the conflicts in eastern and western Europe have been acknowledged. For example, "In all the western campaigns of the war against French, British, Americans, and troops of many other lands, some 200,000 German soldiers died. Four million Germans died on the Eastern Front".⁴ This is not what was told to a generation of Britons which grew up with tales of Dunkirk, the Battle of Britain, and the Normandy landings.

Perhaps of even greater relevance today is the story of the vote and participation in politics. There was very little time between the granting of universal suffrage to men and its being granted to women. In Britain, which has a longer history than New Zealand, there were major changes over less than 100 years.⁵ Hence in 1832 the vote was extended to cover 14 percent of the adult male population. In 1867 this was extended to 34 percent, and in 1885 56 percent of males over 21 had the vote. As in New Zealand, the view was that the vote was linked to ownership of property.⁶ Probably half of the British men over 21 serving in the First World

¹ Note, when analysing data over time, the problem of time, age and cohort effects. At a given time, are differences in behaviour due to differences in age or differences in cohort? Similarly for a fixed time or cohort. (Here cohort = birth cohort.)

² P.122 of Popper K R (1966) *The Open Society and Its Enemies: Volume II*, London: Routledge and Kegan Paul

³ Snowdon B and Vane H R (2005) *Modern Macroeconomics: Its Origins, Development and Current State*, Cheltenham: Edward Elgar

⁴ Wheatcroft G (2005) "How good was the good war?", *The Boston Globe*, 8 May, http://www.boston.com/news/globe/ideas/articles/2005/05/08/how_good_was_the_good_war?pg=full

⁵ http://en.wikipedia.org/wiki/Elections_in_the_United_Kingdom#Expansion_of_the_franchise

⁶ The New Zealand situation is described at: <http://www.elections.org.nz/study/history/right-to-vote.html>. Universal male suffrage was introduced in 1879, and universal female suffrage in 1893. It is interesting that an influx of miners led to them being given the vote in 1860, so as to avoid the unrest experienced in Australia. This may have tipped the focus away from a property-based system, opening the door to universal suffrage, including women. Plural voting for those with property in more than one constituency was abolished in 1889. In the UK it was only in the Representation of the People Act 1949 that the property dimension finally disappeared, as until then owners of business premises had an additional vote (http://www.thepotteries.org/dates/votes_justice.htm). This was also when the UK saw the end of the university constituencies, whereby graduates of certain universities had an additional vote. In Northern Ireland Queen's University, Belfast, did not lose its representation until 1968 (http://en.wikipedia.org/wiki/University_constituencies).

War did not have the vote. In 1918 universal suffrage was granted to men over 21 and women over 30 (reduced to 21 in 1928).

We also hear about votes for British women being granted, against strong opposition, due to vigorous efforts by suffragettes. In 1869, unmarried and widowed women were given the right to elect members of municipal councils in certain towns.⁷ In 1888, women, if unmarried and otherwise eligible, were given the right to vote for county and county borough councilors. It is worth matching these dates with the following information about Emily Pankhurst⁸:

PANKHURST, Emmeline, nee Goulden (1857-1928) English suffragette, born in Manchester. In 1879 she married Richard Marsden Pankhurst (d.1898), a radical Manchester barrister who had been the author of the first women's suffrage bill in Britain and of the Married Women's Property Acts of 1870 and 1882. In 1889 Mrs Pankhurst founded the Women's Franchise League, and in 1903, with her daughter Christabel Harriette (1880-1958), the Women's Social and Political Union, which fought for women's suffrage with extreme militancy...

She was probably 12 years old when some voting rights were given to women, and 13 when her future husband succeeded in getting extended property rights for women. At the same time voting rights had only just been extended to one in three adult men.

What of the British experience of the First World War? Men served in the trenches, and women worked in the munitions factories. Haig described Passchendaele in an official dispatch⁹:

The valleys of the choked and overflowing streams were speedily transformed into long stretches of bog, impassable except by a few well-defined tracks, which became marks for the enemy's artillery. To leave these tracks was to risk death by drowning, and in the subsequent fighting on several occasions men and pack animals were lost in this way... (p.272)

Meanwhile women were also affected by the war: "Levelling was inevitable in a period when a duke's son served under his gardener's boy; or a duke's daughter hoed turnips while her 'social inferiors' were buying themselves fur coats out of their earnings in the munitions factories."¹⁰

The Order of the White Feather was responsible for men out of uniform being given white feathers by women as a sign of cowardice.¹¹ Christabel Pankhurst wrote of her mother, Emily, and giving an interesting connotation to equity, "She called for wartime military conscription for men, believing that this was democratic and equitable".¹²

There is now an extensive literature on cases where societies have accepted highly questionable ideas and beliefs, with a classic text being Mackay's *Extraordinary Popular Delusions and the Madness of Crowds*.¹³ The issue is not whether we now accept dubious ideas, but rather, what dubious ideas do we currently take to be true?

⁷ http://www.thepotteries.org/dates/votes_justice.htm.

⁸ P.1122 of Magnusson M (ed) (1990) *Chambers Biographical Dictionary*, Edinburgh: Chambers

⁹ From pp. 270-2 of Briggs A (compiled by) (1960) *The Saw It Happen: An Anthology of Eye-witnesses' Accounts of Events in British History*, Oxford: Basil Blackwell

¹⁰ From Hirst F W (1934) *The Consequences of the War to Great Britain*, OUP, pp.74-6, this extract reprinted on p.348 of Briggs A (compiled by) (1960) *The Saw It Happen: An Anthology of Eye-witnesses' Accounts of Events in British History*, Oxford: Basil Blackwell. Note the concern for class. I wonder when the focus switched from class to gender and ethnicity, and why these countries did not have a Ministry of Working Class Affairs.

¹¹ <http://www.spartacus.schoolnet.co.uk/FWWfeather.htm>

¹² <http://www.spartacus.schoolnet.co.uk/Wfirst.htm>

¹³ Mackay C (1995) *Extraordinary Popular Delusions and the Madness of Crowds*, Wordsworth, (originally published in 1841). It is also at: <http://www.litrix.com/madraven/madne001.htm>.

Interesting Statistic no.3288 [SB]

We hear a lot about “diversity of family types”, with an emphasis on same sex couples. Here are some data derived from the 2001 Census.¹ Same sex couples comprised approximately one percent of all couples without children. Of couples with children, less than a third of one percent were same sex couples. There were approximately 2,200 dependent children in these households. Not all of these children would have been born into an existing same-sex relationship, and so for these at least there will be a parent somewhere else.

There were approximately 667,000 dependent children in opposite-sex couple households. Family types that include couples with children do not distinguish between parents and step-parents or other new partners of a parent. Some of these children had a parent living in a different household. These children may have spent time living in two households.

In 2001 there were approximately 250,000 dependent children in sole parent households. Most of them had another parent somewhere else, and they could have spent much of their time with that parent.

If there is real concern for the broad diversity of family types, and concern for the interests and perspectives of children, why is there not even a term for the family type of children whose parents live apart?

¹ Statistics New Zealand (2002) *2001 Census: Families and Households*, <http://www.stats.govt.nz/NR/rdonlyres/ED8AF5A8-9FA8-4865-BD82-8ADA357DE7E3/0/FamiliesandHouseholds.pdf>

The Electrical Age

Wonders of electricity to be realized before many years

(Robert Luce in Van Nostrand’s Magazine.)

The possible applications of the principle of the electrical transmission of power are almost numberless. We shall, I believe, at no distant date, have great central stations, possibly situated at the bottom of coalpits, where numerous steam-engines will drive many electrical machines. We shall have wires laid along on every street, the electricity tapped into every house, and the quantity of electricity in each house registered as gas is at present. The storage battery will fill a place corresponding to the gasometer in the gas system, making the current steady, rendering the consumer independent of the irregular action or stoppages of the dynamos of the central station, and enabling the use of dynamos of the highest tension – i.e., those which produce the currents of the greatest intensity. The electricity will be passed through little electric machines to drive machinery to produce ventilation, to replace stoves and to work all sorts of apparatus, as well as to give everybody an electric light. Solar heat will be used to run the dynamos in the cloudless regions. Everywhere the power of the tides, and such waterfalls as Niagara, are to be utilized. Is not a millennium to be anticipated when the water power of a country will be available at every door?

Steam, which in the last century has conferred so many benefits on the world, will give way before electricity. The dynamo will replace the steam engine. This prediction seems wild and visionary; yet when steam was first thought of as an available force its advocates were considered, just as the advocates of dynamical electricity to-day are considered, mere enthusiasts. But public opinion never stops the march of intellect. After it had proved the powers of steam to be enormous, genius never halted, but straightway went on anticipating still more wonderful discoveries in the realms of electricity.

The prophetic ken of science was happily exhibited by Dr Lardner, in his treatise on the steam engine. ‘Philosophy,’ said he half a century ago, ‘already directs her fingers at sources of inexhaustible power in the phenomena of electricity and magnetism, and many causes combine to justify the expectation that we are on the eve of mechanical discoveries still greater than any which have yet appeared; and that the steam-engine itself, with the gigantic powers conferred upon it by the immortal Watt, will dwindle into insignificance in comparison with the hidden powers of Nature still to be revealed, and that the day will come when the machine which is now extending the blessings of civilization to the most remote skirts of the globe will cease to have existence except in the page of history.’

To-day we are beginning to appreciate the truth of this prophecy. To-day we see dynamical electricity in the forefront of the physical sciences. The principle of the transmission of power by electricity fast approaches its realization. We are, in truth, just entering upon a wonderful age.

[From *The Clutha Leader*, 29 May 1885, p.3, via <http://paperspast.natlib.govt.nz/>]

Some Thoughts by Karl Popper and Adam Smith

Popper on Utilitarianism

I believe there is, from the ethical point of view, no symmetry between suffering and happiness, or between pain and pleasure...In my opinion, human suffering makes a direct moral appeal, namely the appeal for help, while there is no similar call to increase the happiness of a man who is doing well anyway. (A further criticism of the Utilitarian formula 'Maximise pleasure' is that it assumes, in principle, a continuous pleasure-pain scale which allows us to treat degrees of pain as negative degrees of pleasure. But from the moral point of view, pain cannot be outweighed by pleasure, and especially not one man's pain by another man's pleasure. Instead of the greatest happiness for the greatest number, one should demand, more modestly, the least amount of avoidable suffering for all; and further, that unavoidable suffering – such as hunger in times of an unavoidable shortage of food – should be distributed as equally as possible.)

(Popper K R (1966) *The Open Society and its Enemies*, 5th edition, London: Routledge and Kegan Paul, Vol.1, pp.284-5)

Note that his argument relies on the use of “pleasure” and “pain” in place of the more common “higher and lower utility”, or “utility” and “disutility”. Schopenhauer's stratagem no.12 is to “choose a metaphor that is favourable to your proposition”. Of course, economists might have done the same thing to justify their proposition, and perhaps Popper is anticipating Rawles.

...and on Democracy

...the theory of democracy is not based upon the principle that the majority should rule; rather, the various equalitarian methods of democratic control, such as general elections and representative government, are to be considered as no more than well-trying and, in the presence of a widespread tradition of distrust of tyranny, reasonably effective institutional safeguards against tyranny, always open to improvement, and even providing methods for their own improvement. (Vol.1, p.125)

Note the stress on institutional safeguards, or checks and balances.

Adam Smith on a Related Theme

In the progress of the division of labour, the employment of the far greater part of those who live by labour, that is, of the great body of the people, comes to be confined to a few very simple operations, frequently to one or two...He... generally becomes as stupid and ignorant as it is possible for a human creature to become...Of the great and extensive interests of his country he is altogether incapable of judging...

By comparison:

In those barbarous societies, as they are called, every man, it has already been observed, is a warrior. Every man, too, is in some measure a statesman, and can form a tolerable judgment concerning the interest of the society and the conduct of those who govern it.

[From Smith A (1776) *The Wealth of Nations*, Book 5 chapter 1,

<http://www.bibliomania.com/2/1/65/112/frameset.html>]

...on the evolution of checks and balances

The separation of the judicial from the executive power seems originally to have arisen from the increasing business of the society, in consequence of its increasing improvement. The administration of justice became so laborious and so complicated a duty as to require the undivided attention of the persons to whom it was entrusted. The person entrusted with the executive power not having leisure to attend to the decision of private causes himself, a deputy was appointed to decide them in his stead.

[book 5 chapter 1]

...and on law and economics

"Thus, upon equal or nearly equal profits, every wholesale merchant naturally prefers the home trade to the foreign trade...He can know better the character and situation of the persons whom he trusts, and if he should happen to be deceived, he knows better the laws of the country from which he must seek redress."

[Book 4, Chapter 2]

The 2005 Conference [SB]

It was encouraging for the Council of the Association to see that Christchurch continues to be not only a welcoming, but also a financially viable conference venue. The numbers attending were encouraging, and paper offerings were varied and of a high quality. While lower in number than the surprise peak of last year's conference in Wellington, this was essentially a return to levels of previous years. Nevertheless, Wellington does seem to be the best venue overall. In response to increasing pressure on venues and requirements for keynote speakers, the Association is now planning further ahead than in the past, and is already committed to a Wellington conference next year on 28-30 June.

The keynote speakers made a major contribution to this year's conference, for which we are most grateful. They demonstrated the vast amount of work being done overseas. Some of this could well be useful to us. This writer also found their subject matter highly stimulating, as reflected in pieces below arising from the presentations of **Peter Phillips** and **John McMillan**.

An important aspect of the conference was the presentation of 2004 **Distinguished Fellows** awards to **Peter Phillips** and (by video) **Roderick Deane**, and 2005 awards to **Brian Easton**, **Lew Evans**, **Gary Hawke** and **John McMillan**. Also **Life Membership** was awarded to **Len Bayliss**. Further details will be posted on the NZAE web site. The Association also recognised **NZAE Education Trust Scholars**, **Amy Cruickshank**, **Kelly Lock**, **Hala Rohurua**, **Clayton Weatherston**, **Bill Kaye-Blake** and **Mohammed Shaahnawacz**.

Keynote speaker **Stephen Cecchetti** is a successful academic who also regularly contributes to the *Financial Times*. He has a collection of these articles on his web page at: <http://people.brandeis.edu/~cecchett/>. It is always interesting to hear those who can reach a wide audience. He began his presentation at the NZAE conference by pointing out that econometrics gives information on normal situations, near the mean of the data. This is not much use for catastrophic events or understanding outliers. This gives us grounds for justifiable caution when considering forecasts. For a more extreme position, an article by Nassim Taleb argues that the future is determined by such catastrophic events, and they cannot be forecast.¹ He suggests that we should consider whether our supposed understanding of events is distorted by hindsight bias.²

Keynote **Caroline Hoxby**'s talk on education included the appealing term, "internal dynasty financing", referring to families saving to fund their children's education. The subject matter was well received, and was a useful insight into the issue of policies affecting school choice and the quality of education. Two recent Education Forum publications on similar matters are Harrison M (2004) *Education matters: Government, Markets and New Zealand Schools*, Wellington: Education Forum, and Merrifield J (2005) *Parental Choice as an Education Reform Catalyst: Global Lessons*, Wellington: Education Forum. Adam Smith commented on education provision also. See "Boys disadvantaged in education" on p.27.

The papers from the conference are available from: <http://www.nzae.org.nz/conferences/>

Observations on the conference by Robin Johnson (johnsonr1@paradise.net.nz)

The Editor presses me for a comment on the Christchurch Conference. In general, I liked the facilities and the accommodation in the same venue in the winter season. I liked the overseas speakers (I missed Phillips due to transport delays) and I hope the sponsors can see their way to continue to give their support. Though their subject matter may not be relevant to one's daily tasks they are a breath of fresh air in terms of the outside level of expertise in the profession. There were two special sessions – one on the history of economics in New Zealand and the other on the economics of globalisation.

¹ Taleb N N (2004) "Learning to Expect the Unexpected", http://www.edge.org/3rd_culture/taleb04/taleb_indexx.html

² "Hindsight bias, sometimes called the *I-knew-it-all-along effect*, is the inclination to see past events as being predictable and reasonable to expect, perhaps because they are more available than possible outcomes which did not occur." http://en.wikipedia.org/wiki/Hindsight_bias

The history project is being led by Ralph Lattimore and Gary Hawke. With the 50th anniversary of the establishment of the association coming up in 2009, Council is supporting this project to identify the highlights of the past and the main actors in the cast. A publication is envisaged at the time of the anniversary. Gary spoke about some of the leading figures in the early days of the colony and development of the profession in the period between the wars. Brian Easton spoke about the Canterbury school of economics and the establishment of the Canterbury tradition. John Yeabsley spoke about the leadership shown by the Canterbury school and Ralph drew on some notes from Conrad Blyth about the life and times of Horace Belshaw. I enjoyed this session myself and I think the project as a whole is a most promising development for the association.

The globalisation project is being led by Brian Easton supported by the Marsden Fund. Brian outlined the chapter headings for a comprehensive publication he intends to complete for the study. Globalisation is a continuation of a process started in the expansionism of the 18th century, where international specialisation developed aided by access to new resources and also by economies of scale. Changes in transport and technology, as evidenced by the refrigeration example in New Zealand, overcame the tyranny of distance from markets which first stymied all the new colonies. Today messages and data can be transferred internationally almost instantaneously and in some respects, distance is no longer a restraint as evidenced by the transfer of call centres to Bangalore. It will be interesting as Brian moves into the international movement of labour and capital and their part in the globalisation debate. I see this project as very ambitious but potentially useful as an exposition of economic trends the public is scarcely aware of.

Among the contributed paper sessions I enjoyed Julia Hall on capital shallowness, the MED team on social and economic indicators, Des O’Dea on the work-rich and the work-poor, and Rosemary Goodyear on urban-rural comparisons. I was sorry to miss some of these sessions due to my late arrival. There appeared to be fewer contributed papers this year compared to last year in Wellington. I hope this is not a trend developing as I believe the association’s meetings are an extremely valuable forum for exchanging information and for raising standards in the economics profession and particularly in the civil service.

The Conference – Peter Phillips [SB]

Peter Phillips’ keynote address was based on a paper published in *The Economic Journal* in 2003.¹ The paper is there for people to read, so I’ll focus on the thoughts that his discussion of the issues brought to mind.

Early in the paper he introduces six “laws of econometrics”, which are really cautionary points, and “it is useful to present them in a way that does not overstate our scientific contributions given the complexity of the real economic world”.

Before presenting his laws, he describes four laws of sociology, credited to Lazarsfeld, but apparently not previously available in print. The second law is, “It’s Different in the South”, and is treated as a serious suggestion of regional heterogeneity. Potter, on the other hand, writing in 1953, presented something very similar as a technique for the uninformed to make a winning interjection against an expert by stopping the flow of conversation.² By a strange coincidence, given the location of the conference in Christchurch, Potter called it the “Canterbury block”, after the person who is (fictitiously) claimed to have first used it:

Expert (who has just come back from a fortnight in Florence): And I was glad to see with my own eyes that this Left-wing Catholicism is definitely on the increase in Tuscany.

The Canterbury: Yes, but not in the South.

"Yes, but not in the South," with slight adjustments, will do for any argument about any place, if not about any person. It is an impossible comment to answer. And for maximum irritation, remember, the tone of voice must be "plonking." (...i.e. roundly, but hollowly and dogmatically)

¹ Phillips P C B (2003) “Laws and Limits of Econometrics”, *The Economic Journal*, 113 (March), pp.C26-C52

² Potter S (1953) *Stephen Potter on Lifemanship*, London: Rupert Hart-Davis, p.43

This curiosity aside, I found Phillips presentation and paper highly thought provoking. He quotes Hoover, “even accumulated falsifications or anomalies do not cause scientists to abandon an approach unless there is the prospect of a better approach on offer”. If true, I can safely assume that, whatever criticisms might be raised against econometrics, it will continue to be used for the foreseeable future. Nevertheless, I will state some here for the record.

Phillips’ six laws describe areas of difficulty and steps that are being taken with respect to them. Lipsey and Lancaster presented a general theorem of second best, along with a negative corollary.³ The former “states that if there is introduced into a general equilibrium system a constraint which prevents the attainment of one of the Paretian conditions, the other Paretian conditions, although still attainable, are, in general, no longer desirable” (p.11). The negative corollary, in its specific form, reads, “it is not true that a situation in which more, but not all, of the optimum conditions are fulfilled is necessarily, or is even likely to be, superior to a situation in which fewer are fulfilled” (p.12). A key implication is that, where there are many constraints, the removal of one may improve or worsen the situation, or leave it unchanged.⁴

Given that the Theory of Second Best arises from the nature of solutions to constrained optimization problems, it is as relevant to econometrics as it is to economics. Solutions to one dilemma will not necessarily improve our results if other problems remain unresolved. (The same issue arises with Karl Popper’s piecemeal social engineering as compared to his utopian engineering.)

The problems and associated advances described in the paper by Phillips are essentially statistical. There are other concerns which could also be relevant (and may be mentioned in a plonking tone to great effect). Lazarsfeld had four laws, Phillips presented six, so, predictably, my concerns will be eight:

1. All econometrics does is find patterns within and between strings of numbers. We have to take a leap of faith to then interpret the results as descriptions of meaningful relationships between the variables that the numbers are said to represent.

2. All data points are assumed to be observations of the same underlying structure that is being estimated. This applies despite changes over time, adjustments to new equilibria, and lead and lag patterns that may not match the discrete data periods (so impact on the current and other periods depends on the timing within the period).

3. Geographical distance may have implications similar to those of time, as suggested in Phillips’ fourth law. However we don’t have an isotropic surface, and distance is two dimensional (at least).

4. “Output waves” may differ greatly from “input waves”. In other words, a change in one variable may have a complex pattern of impact on another variable.

5. Econometric models cover a limited range of functional forms.⁵

6. Data are not generally gathered specifically for economists, and commonly fail to measure the specific variables of interest. This is immediately apparent when we think of unemployment, profits, or capital, and there are difficulties even defining income.

7. Responses in economics are the result of people’s decisions based on their perceptions of the environment. These perceptions result from both what people see (information), and how this is interpreted (knowledge). The same information observed twice could be perceived differently, if only because people may learn from the first occasion. Even if variables are accurately measured, the resulting values may not coincide with people’s perceptions. The National Bank’s *Business Outlook* consistently shows inflation expectations higher than measured inflation, but by varying degrees.

³ Lipsey R G and Lancaster K (1956) “The General Theory of Second Best”, *Review of Economic Studies*, Vol.24, pp.11-32

⁴ See also the Theory of Third Best, as described in chapter 9 of Ng Y-K (1983) *Welfare Economics*, London: Macmillan

⁵ Also our criteria of best fit may be challenged. Hence, “The elementary point that there may exist nonlinear, or for that matter – biased, estimators superior to least squares for the non-Gaussian linear model is a well kept secret in most of the econometrics literature.” (p.35 of Koenker R and Bassett G, 1978, “Regression quantiles”, *Econometrica*, Vol.46(1), January, pp.33-50)

8. Model selection and the interpretation of results are primarily based on statistical criteria. Statistical significance can at best be only a partial test of economic or policy significance (see 1).

There may well be scope for improvement of our tools of analysis in many directions, quantitative and qualitative, and in the quality of reasoning applied to the evidence obtained. More generally, though, there is scope for recognition of the limitations of our understanding, and hence the degree of caution that should be applied when deliberating about policy.

The Conference - John McMillan [SB]

John McMillan gave a thought provoking keynote address. His PowerPoint presentation is on the NZAE web site. He discussed the role of narrative economics and, in particular, case studies, as a supplement to mathematical and econometric analyses. Here are five of the thoughts that came to mind for me.

1. His classification has a parallel in the distinction between qualitative and quantitative research methods. Qualitative studies can be useful for identifying relevant issues, variables, and hypotheses. These may then lead on to for further, quantitative analysis. In other words, it can be useful for specifying relevant quantitative analyses.

2. He rightly pointed out that tool building is important, and presented the view that tools (maths and econometrics) can expand to address more problems. What sort of tools would be most useful, given the possible applications? Are maths and econometrics the only areas for tool building, or are we just looking under the lamp post?

3. There was a telling example of a regression result where the finding only applied to half of the cases. Regression gives results in relation to averages, but many cases are not average. Similarly, studies on returns to education commonly give average returns to a qualification, when there can be wide variation. As has been said in relation to indicative planning, broad findings may be of little use to individual decision makers. As another example, the results of regressions in relation to unemployment in a collection of small towns could be of limited policy value when the major changes arise due to the closure of a major employer in a town, and a second one-off decision of a new employer to locate there. Econometric model building may be of limited use where individual decisions can have a large impact.

4. I liked the point, hopefully correctly quoted, “synthesizing research can add as much value as the original research”. Research does not necessarily involve starting from scratch, gathering data and estimating a model. There is value in critical comment, meta-analyses and even juxtaposition of findings and perspectives. It is common in research for people to overstate what they have found, and then to understate its relevance. It is worth being cautious in interpretation of results, and then devoting more time to placing the findings in a wider context. As an aside, are students generally told the importance of careful specification of the counterfactual?

5. In the discussion following the presentation, it was suggested that case studies could be useful for presenting otherwise obscure analysis to non-economists, or case study as exposition. This might be an example of eristic (see Schopenhauer). Diffusion of economic ideas is important, and they have to be presented in an intelligible way. At the same time, a danger is highlighted in the New Zealand media’s obsession with the personal angle on issues, at the expense of consideration of broad principles. It is important to stress the principle that is being illustrated by the example.

6. Many years ago, in an introductory lecture, a statistics professor stressed that statistics can only be applied in conjunction with knowledge of the area of application. The same could be said of economics or econometrics. We should not be only be trying to explain our findings to non-economists. We may well need the input of such people so as to understand the area of application, whether it is a particular industry, or a sector such as education or health, or related to social issues. Similarly, we need to understand the processes of application of policy, not least of these being the use of law, and the expertise of the people responsible for that implementation.

Conference Photographs

Peter Phillips:



Gary Hawke



Ralph Lattimore and
Frank Tay

John McMillan and Lew Evans



Brian Easton and
Elizabeth Caffin



Roderick Deane
(who attended
via a video
recording)

Mary Hedges and
Stephen Cecchetti

Caroline Hoxby and
Veronica Jacobson



Bill Kaye-Blake and
Mohammed Shaahnawacz



Amy Cruickshank Kelly Lock

Hala Rohurua

Clayton Weatherston

Social Capital a Misnomer? By Stuart Birks

Stephen Knowles presented a paper at the conference on “the future of social capital in development economics research”. He argued against use of the term, “social capital”, suggesting that it might be more helpful to talk in terms of “informal institutions”. One reason is that people might be overly influenced by the use of the term “capital”.

The Ministry of Social Development web page describes what it calls the Social Development Approach.¹ It refers to social investments, as if such investments can increase the stock of social capital, which may be true. It then goes on to extend the capital analogy further, suggesting a portfolio approach to social investments, treating them as if they were financial investments, “To manage its investments, the Ministry has to: have a diverse range of social investments to offset risks...”.

This ties in to an issue in health economics:

*Most analysts argue that health benefits should be discounted at the same rate as costs in the baseline analysis, even if they are expressed in non-monetary units, such as life years or quality adjusted life years. A zero discount rate--or one lower than that used for costs--can be introduced in the sensitivity analysis. A lower rate is advocated so as not to penalise preventive programmes and also because the results of some studies seem to suggest it.*²

In both these cases, thought should be given as to whether standard approaches in relation to financial matters can be applied in other areas. The second case then raises the additional issue of whether, if the approaches are valid, different (or zero) discount rates are justified.

Offsetting risks suggests that good returns in one area can balance poor returns in another. Financially, there is little problem with this because financial returns are all denominated in units of money, and hence are comparable. However, social, or health, returns are quite distinct. Whereas money from different sources can be used to buy the same goods, social and health returns cannot be readily converted from one form to another. It is therefore wrong to treat the various returns as comparable.

This is perhaps seen most clearly when considering discounting. One claimed reason for discounting is that a dollar today can be worth more than a dollar tomorrow simply because it can earn a day's interest in the meantime. Another explanation for comparisons of discounted present values is that, if it is possible to borrow or lend at the chosen discount rate, then it is possible to convert one net income flow to any flow that has the same net present value. We cannot generally defer consumption of health or social capital. Even if we could, they cannot be loaned to someone else, even though some of our decisions may affect others.

Looked at another way, what would discounted future years of life mean? Can we sensibly consider living not our allotted three score years and ten, but only three score “present years”? Given the limited opportunities to transfer these things over time, there is little opportunity to reveal our preferences in this regard, so what discount rate should we apply? Would we value a year in the future much less than a year now? Would nobody, given the choice, be willing to give up a year now in exchange for a year in thirty years time?

Given the interest that can be earned by deferred consumption, a materialistic individual may well prefer to defer life and benefit from accumulated interest. What of social capital? Would deferred use of social capital now result in more social capital in the future, or is it something that grows through increased current use? In both these cases, the analogy with financial assets is misleading.

As for the zero discount rate suggestion, this has also been proposed in relation to environmental issues on the grounds that desired projects would not otherwise meet the criterion for approval. Surely this reasoning is one of suggesting that criteria should be selected on the basis of their support for our desired position, when their purpose is to guide our choices. A “wrong” result should presumably mean that the benefits have been undervalued, not that they should be discounted differently. At least in the context of project evaluation, benefits are valued before being discounted, so the units in the calculation do lend themselves to such treatment. Discounting units rather than values is meaningless, as can be

¹ <http://www.msd.govt.nz/publications/statement-of-intent-2003/social-development-approach.html>

² Parsonage M, Neuburger H. “Discounting and health benefits.” *Health Economics* 1992;1:71-6

seen if we consider what this is really saying. Is a new car in 2010 the same as say 0.8 “present cars”? Its value might be, but in itself it is not now a car, or even part of a car. Schopenhauer’s stratagem no.2 is use of the homonymy – to extend a proposition to something which has little or nothing in common with the matter in question. It can then give a false argument, which can be refuted. Perhaps economists have done this unintentionally when extending the concept of capital to social capital or life. The point can be refuted if the analogy with capital breaks down.

In my opinion, Stephen Knowles was right to be cautious about the use of the term social capital.

The scourge of deflation [SB]

Conference keynote speaker Stephen G. Cecchetti is currently serving as a consultant to the European Central Banks Inflation Persistence Project. This suggests a different concern to one about the Japanese economy, which has experienced six years of deflation.¹ From an official Japanese web site²: “The general index of average consumer prices in 2004 for Japan stood at 98.1% (2000=100), [the] same level as the preceding year.” A graph showed a fall each year from a peak in 1998, until it stayed level in 2004. Another report on the same site, dated 25 March 2005, says, “The consumer price index for Japan in February 2005 was 97.4(2000=100), down 0.2% from the previous month, and down 0.3% from the previous year.”³ *The Financial Times*, in a report also on 25 March, indicated that deflation was still occurring, plus the following sentence: “Three years of growth, albeit sporadic, have brought the goal of eradicating deflation within tantalising reach.”⁴

So it seems that annual falls in the price index of less than half a percent are a problem.

¹ Reuters (2005) “Japan deflation persists - except for beef bowls”, 26 March, <http://www.stuff.co.nz/stuff/0,2106,3228146a6026,00.html>

² <http://www.stat.go.jp/english/data/cpi/158c.htm>, on the site of the Statistics Bureau of the Ministry of Internal Affairs and communications (the wording has since changed slightly)

³ <http://www.stat.go.jp/english/data/cpi/1581.htm>

⁴ Pilling D (2005) “Japan prices post fastest fall in two years”, *The Financial Times*, 25 March, <http://news.ft.com/cms/s/c47e227c-9cf1-11d9-a227-00000e2511c8.html>

LORD OF THE REGIONS: THE MYTHS, MAGIC AND MIX FOR REGIONAL INNOVATION

A JOINT CONFERENCE

**29th Annual Conference of
Australia and New Zealand Regional Science Association International**

**The September Conference of the
Economic Development Association of New Zealand**

**Manukau, Auckland New Zealand
27 – 30 September 2005**

ANZRSAI and EDANZ have come together to organise a joint conference in September 2005. The conference will bring together practitioners and academics from both sides of the Tasman (and further away) to focus on regional innovation. It is expected to attract between 350 and 400 participants.

Main topics addressed:

- Regional innovation
- Regional capability building in a global context
- Sustainable economic development in action
- Maori, Pacific and Aboriginal economic development
- Innovative solutions

For more details, go to: <http://www.lordoftheregions.org.nz/welcome.html>

Misc.

Schopenhauer - The Art of Controversy

This is the title of an essay by Arthur Schopenhauer, published posthumously and translated into English in 1896. (<http://etext.library.adelaide.edu.au/s/schopenhauer/arthur/controversy/>) He gives 38 stratagems for winning an argument, in large part so that people can see when they are being used against them. They could be particularly relevant when considering politicians, the media, or lawyers, but they may also be used by economists, if inadvertently. There are also some terminological issues that he covers which merit repetition.

In chapter 1, footnote 1, the following categories from Aristotle are described: (1) *Logic*, or Analytic, as the theory or method of arriving at true or apodeictic conclusions; (2) *Dialectic* as the method of arriving at conclusions that are accepted or pass current as true; (3) *Eristic* is the method by which the form of the conclusion is correct, but the premisses, the materials from which it is drawn, are not true, but only appear to be true; and (4) *Sophistic* is the method in which the form of the conclusion is false, although it seems correct.

He suggests, in relation to debate and the distinction between logic and dialectic, "The discovery of objective truth must be separated from the art of winning acceptance for propositions; for objective truth is an entirely different matter...". Also, still in chapter 1:

...even when a man has the right on his side, he needs Dialectic in order to defend and maintain it; he must know what the dishonest tricks are, in order to meet them; nay, he must often make use of them himself, so as to beat the enemy with his own weapons.

Accordingly, in a dialectical contest we must put objective truth aside, or, rather, we must regard it as an accidental circumstance, and look only to the defence of our own position and the refutation of our opponent's.

When detailing stratagem 38, he refers to *ad hominem*, highlighting a common misuse of the term, which actually refers to a valuable aspect of discussion, especially given Socrates' view on wisdom. Hence he identifies: *ad rem* - objective discussion of the subject pure and simple; *ad hominem* - discussing the statements or admissions which your opponent has made on the subject; and *ad personam* - attacking the person, by remarks of an offensive and spiteful character.

Socrates' Apology

Socrates' "Apology" can be found at: <http://www.saliu.com/socrates.html> He makes a very significant point when he argues that wisdom is in large part a matter of knowing how little you know. This is spelled out clearly in the three paragraphs starting with the one beginning, "Why do I mention this?" He demonstrates the point through *ad hominem* questioning of supposedly wise people (see Schopenhauer). It is also relevant to economists in that much that is said and done in the policy area is based on an inflated belief in the degree of understanding of the issues.

Who Needs Forecasts Anyway?

The following is the start of a Reuters report on American foreign policy in the Middle East¹:

CAIRO: US Secretary of State Condoleezza Rice has alarmed many reformist Arabs with comments suggesting a new US approach that promotes rapid political change without regard for internal stability.

Rice said in an interview with the Washington Post last week the Middle East status quo was not stable and she doubted it would be stable soon. Washington would speak out for "freedom" without offering a model or knowing what the outcome would be.

¹ Reuters (2005) "Rice alarms with comments on Middle East reform", 30 March, <http://www.stuff.co.nz/stuff/0,2106,3232282a12,00.html>

research in progress...

Continuing our series on the research projects currently underway in Economics Departments and Economics Research Units throughout New Zealand, in this issue we profile the research currently being undertaken by economists at Victoria University. The objective of this section is to share information about research interests and ideas **before** publication or dissemination - each person was invited to provide details only of research that is **new** or **in progress**.

... economic research at Victoria University as at July 2005.

Compiled by Stephen Burnell [Stephen.Burnell@vuw.ac.nz]

Contact details for staff of the School of Economics and Finance are listed at: <http://www.sef.vuw.ac.nz/vuw/content/popup.cfm?type=staff&school=sef>

Geoff Bertram is currently working in the following areas:

- 1) The incorporation of international aid flows into the standard infinite-horizon neoclassical growth model (With **Peter Chang**).
- 2) Editing the papers from the 2004 MIRAB conference to appear as a special issue of *Asia Pacific Viewpoint*. He is contributing an introductory paper.
- 3) He has joined the international editorial board of the new *Island Studies Journal*, ISSN 1715-2593, the first issue of which is to appear in May 2006. He has been invited to contribute a theoretical paper for the inaugural issue, and in the next few months will be working on that, in parallel with some joint work with **Bernard Poirine** (University of French Polynesia) on the economics of small islands, to appear in a forthcoming book "A World of Islands", edited by **Godfrey Baldacchino**.
- 4) There is a chapter to appear in a forthcoming book on electricity sector restructuring around the world, edited by Professor **W. Pfaffenberger** (Bremen U.) and **Perry Sioshansi**, to be published by Elsevier next year; some of the material for this will be presented at the IAEE conference in Taipei.
- 5) Light-handed regulation of electricity lines companies (in the latest issue of *Journal of Regulatory Economics*). Writing-up the issue of evaluating rates of return on gas pipelines and port companies, drawing on material provided over the past four years to the Ministers of Energy and Transport, and the Commerce Commission.
- 6) A paper on the rapidly rising importance of international migration and remittances in the globalisation process, accepted for presentation at the Oxford Roundtable in July.
- 7) Writing a chapter for the forthcoming *New Oxford History of New Zealand*.

Roger Bowden is working on: 1. Formulating and estimating dynamic regime models, with applications to FX forecasting and risk management (with **Jennifer Zhu** and **Jin Seo Cho**); 2. Hedging the corporate terms of trade, with special reference to NZ dairy farmer risk management (with **Jennifer Zhu**); 3. Macroeconomics and risk management of foreign exchange exposures; 4. The valuation and economic dynamics of scarcity premiums; 5. Ordered mean difference portfolio technology; and 6. Debt.

Glenn Boyle is currently researching: 1. Reputation effects in the sport of kings (with **Graeme Guthrie**); 2. Valuation of employee stock options; 3. Regulation of OTC stock markets; 4. Executive compensation in NZ since 1997; 5. Discipline in the market for NZ term deposits; and 6. The price of aggregate market risk.

Chia-Ying Chang is currently interested in the fields of monetary and macroeconomic theory, endogenous growth theory, and applied Industrial organization theories. More specifically, she is researching the effects of search frictions on economic activities, and most

macroeconomic issues related to economic fluctuations, banking, growth, as well as fiscal and monetary policies.

Peter Chang is currently researching: 1. Development aid and fungible investment under the neo-classical growth framework; and 2. Non-linear formulation of a prototype computational general equilibrium model of New Zealand.

Jin Seo Cho's current research is focused on examining the asymptotic behaviours of the standard test statistics under non-standard econometric conditions. These include the log-likelihood ratio statistic testing for regime switching in hidden Markov models, and unobserved heterogeneity in duration models. Another research topic is in developing non-standard and distribution free test statistics to identify economic data properties. It includes identifying the identical and independent distribution condition for the transformed economic data sets involving parameter estimates.

Viv Hall has research in progress, jointly with **C John McDermott**, into various aspects of New Zealand's business cycles, including draft papers involving: "The evolution of the New Zealand business cycle"; "The co-movement of New Zealand regional and Australian state business cycles"; "The roles and characteristics of regional house prices in New Zealand's regional activity cycles"; and "Regional business cycles in New Zealand". He also continues research into the issue of whether New Zealand should consider an Australasian currency, adopt the US dollar, or retain its independent monetary policy.

Chirok Han's main research interests cover econometrics, generalised method of moments, panel data models, and limited dependent variables. His research currently in progress includes: 1) "Bias-free estimation of dynamic panel data models", aiming to propose an estimation method available in case the autoregressive coefficient is unity. Existing estimation methods with dynamic panel data are biased when the dynamics is near unit-root. This project proposes a new and simple method that yields a consistent and asymptotically normal estimator for all cases including unit-root. "Panel GMM with fixed effects", which aims to explore the possibility of consistent estimation for nonlinear panel data models. There exists no known method generally available for nonlinear panel data models with fixed effects. This project considers a new approach to the identification and estimation of parameters for them.

Jacek Krawczyk is working on 1. Viability/Macro "A Viability Theory Analysis of a Simple Macroeconomic Model.", and 2. Financial Engineering "Dependence of Left-Skewed Payoff Distributions on Risky-Asset Price Uncertainty."

Martin Lally is interested in 1. Estimation of the Cost of Capital, Implications of regulation for the Cost of Capital, and 2. Implications of internationalisation for the cost of capital.

John Owens' work continues to be primarily concerned with market microstructure finance. He is currently considering how market microstructure models can improve realized volatility measurements. He has also recently become interested in insurance economics. This is with a special interest in pricing in incomplete markets, alternative risk transfer, and the relationship between panel data models and traditional actuarial credibility methods. He expects this line of research to make up an expanding portion of his output during the next few years.

John Randal's primary research area is financial econometrics. His current focus is on volatility estimation, particularly in the New Zealand context, where we must account for non-standard properties of New Zealand prices, including rounding. He also (further afield) has an interest in: robust scale estimation in finite samples; practical application of option pricing models, including the constant elasticity of variance model, and the compound option pricing model; the economics of voluntary contribution to public goods; and modelling New Zealand visitor arrivals.

Jack Robles is currently studying: 1. Fee arrangements in repeated relationships between lawyer and client. The majority of current research suggests that contingent fees are superior to hourly wages. However, it is quite common for lawyers to charge hourly wages. Our theory is that this discrepancy arises because the literature has focused entirely on one shot relationships even though there are a large number of repeated relationships between lawyers and clients. 2. Conditional dominance, which is a method for understanding the implication of rationality in certain types of games. He has written one paper regarding methods for the application of conditional dominance, and is currently investigating the application of

conditional dominance to a new class of games. 3. The economics of in group bias, investigating the economic consequences of the formation of cliques or (informal) clubs. 4. A theoretical model of workaholism.

John Singleton is completing a history of the RBNZ (with **Arthur Grimes**, **Gary Hawke** and **Frank Holmes**), and working on the history of public sector auditing in New Zealand (with **David Green**) and the development of central banking in Commonwealth countries since the 1920s.

Malathi Velamuri is currently undertaking research on: 1) Taxes, Health Insurance and Women's Self-Employment - whether the availability of health coverage through the spouse's health plan influences a married woman's decision to become self-employed. 2) Promotion Expectations, Job Turnover and Promotion Realizations (with **Richard Prisinzano**) - The National Longitudinal Survey of Youth (NLSY) asks a series of questions relating to an individual's job satisfaction. One of these questions elicits respondents' expectations for promotion on their current job. Using information from the 1996 through 2000 surveys, they analyze cross-sectional variations in expectations by gender, levels of education and labor market experience. They study the relationship between expectations and promotion realizations. 3) Marital Disruptions and Housing Transitions in Australia: Evidence from the HILDA Panel (with **Aydogan Ulker**) - Most public policies aim to maintain and improve living standards of individuals. In a world of no frictions or unexpected shocks it would be much easier to design and implement policies to insure the consumption streams of individuals over the life cycle. However, in reality many disruptions occur at both the micro and macro levels, which might hinder individuals' ability to sustain their well-being. Marital disruptions are some of the most common examples of those events that generally affect all members of a household both economically and socially.

Boys Disadvantaged in Education

There are no public institutions for the education of women, and there is accordingly nothing useless, absurd, or fantastical in the common course of their education. They are taught what their parents or guardians judge it necessary or useful for them to learn, and they are taught nothing else. Every part of their education tends evidently to some useful purpose; either to improve the natural attractions of their person, or to form their mind to reserve, to modesty, to chastity, and to economy; to render them both likely to become the mistresses of a family, and to behave properly when they have become such. In every part of her life a woman feels some conveniency or advantage from every part of her education. It seldom happens that a man, in any part of his life, derives any conveniency or advantage from some of the most laborious and troublesome parts of his education.

[From Book 5, Chapter 1 of Smith A (1776) *The Wealth of Nations*, <http://www.bibliomania.com/2/1/65/112/frameset.html>]

Treasury Working Papers and Policy Perspective Papers

The latest working papers are listed at:

<http://www.treasury.govt.nz/workingpapers/2005/>

New Zealand Economic Papers

Ian King, the editor of New Zealand Economic Papers, invites members to submit their papers to the journal. In keeping with tradition, papers in all economic subject areas will be considered, and papers covering New Zealand topics are particularly encouraged.

Offers and ideas for symposia of papers on particular topics are also welcome.

Book reviews and books to review (or suggested titles) are also needed.

Write to: ip.king@auckland.ac.nz

...about NZAE

The New Zealand Association of Economists aims to promote research, collaboration and discussion among professional economists in New Zealand. Membership is open to those with a background or interest in economics or commerce or business or management, and who share the objectives of the Association. Members automatically receive copies of New Zealand Economic Papers, Association newsletters, as well as benefiting from discounted fees for Association events such as conferences.

Membership fees:

full member: \$90

graduate student: \$45 (first year only)

If you would like more information about the NZAE, or would like to apply for membership, please contact:

Val Browning

Secretary-Manager, NZAE

PO Box 568

Wellington

phone: (04) 801 7139

fax: (04) 801 7106

email: economists@nzae.org.nz

EMAIL DATA BASE

We now have an email database of members to keep up to date with technology, and we are working towards eventually e-mailing as many of our notices/publications as possible. *If you have not yet supplied the Secretary-Manager with your email address please email: economists@nzae.org.nz*

MEMBER PROFILES WANTED!!!

Is your profile on the NZAE website? If so, does it need updating? You may want to check...

If you would like your profile included on the website - please email your details to: economists@nzae.org.nz

Welcome! to the following people who have recently joined NZAE...

Malathi Velamuri (Victoria University of Wellington); **Jonathon Bannatyne** (Student); **Andrew Ransom** (Statistics NZ); **Jason Attewell** (Statistics NZ); **Rosemary Goodyear** (Statistics NZ); **Peter Mohan** (Statistics NZ); **Christian Galbraith** (Statistics NZ); **Ian Ewing** (Statistics NZ); **Wido Van Lijf** (Statistics NZ); **Matthew Haigh** (Statistics NZ); **Natasha Petrie** (Statistics NZ); **Michael Anderson** (Statistics NZ); **Sonia Collins** (Statistics NZ); **Bridget Hamilton-Seymour** (Statistics NZ); **Dragos Ifrim** (Statistics NZ); **Daniel Griffiths** (Statistics NZ); **Min Shrestha** (Nepal Rastra Bank); **Daisuke Sawauchi** (Hokkaido University, Japan); **Tony Gollin** (Auckland International Airport Ltd); **Scott Fargher** (Auckland University of Technology); **Clinton De Bruyn** (Ministry of Economic Development); **Peter Goss** (Ernst & Young Corporate Finance Ltd); **Angela Forbes** (Statistics NZ); **Shamim Shakur** (Massey University, Palmerston North); **Ian Ewing** ((Statistics NZ); **Mark Holmes** (Univeristy of Waikato); **Bronwyn Bayne** (The Treasury); **Hannah Kite** (Reserve Bank of NZ); **Michelle Poland** (Families Commission); **Alan Bentley** (Statistics NZ); **Sai Lealea** (Ministry of Pacific Island Affairs); **Susan Jayson** (Statistics NZ).

WEB-SITE - The NZAE web-site address is: <http://nzae.org.nz/>
(list your job vacancies for economists here)