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New Zealand Association of Economists (Inc).**

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REMINDER: NZAE ANNUAL CONFERENCE
28TH, 29TH and 30TH JUNE 2006
Key dates are listed on p.2
For more details, visit the Website
<http://nzae.org.nz/conferences/>
THIS CONFERENCE IS A MUST FOR ALL ECONOMISTS!!!

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Questioning the Fundamentals?

EDITORIAL

In the last issue of *AI* it was suggested that economists know much less than might be commonly believed. In this issue questions are raised about the generality of some key economic assumptions and the possible contradictions between some of our approaches to preferences.

If contemplation or reflection is of value, and if, as some outside economics would suggest, such dimensions as a feeling of belonging and a sense of purpose are important, then the foundations of consumer behaviour could be overlooking some key concerns which are interlinked with economic activity. Similarly, if time is a scarce resource for people, then are we giving it enough attention under static analysis?

If economics overlooks some key elements, then the existence of these elements suggests additional constraints. Failure to consider them places us in a second-best situation, which makes economic conclusions suspect. It also means that we are constrained in terms of the policy dimensions that we are considering. The perspective shapes our view of the world, the problems that require attention, and the policy options available.

We would like to thank those who have contributed, directly or indirectly, to the content of this issue of *AI*. Economics tends to view the world in terms of incentives. One of the main incentives to contribute to *AI* is personal satisfaction. We can offer an outlet for the fruits of introspection and reflection, and also a feeling of belonging to a community of economists, as well as perhaps a sense that there is some broader purpose in the exchange of ideas. If, after reading this issue, any of you feel at all motivated to add to your wellbeing in any of these directions, we would be most grateful to receive your contributions.

by Stuart Birks, Massey University

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 [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.

NZAE Conference 2006 Key Dates

- 31st March 2006:** Submission of Paper Abstracts, including 'quality assured' entries.
Voluntary submission of 'Quality Assured' papers
- 28th April 2006:** Submission of Paper Abstracts for JAN WHITWELL entries.
Graduate Study Award Applications
- 5th May 2006:** Advice as to acceptance of Abstracts for presentation.
Advice as to acceptance of 'Quality Assured' papers.
- 12th May 2006:** Graduate Study Award Grant notifications to Applicants.
Early Bird (discounted) Rate Conference Registrations close
- 9th June 2006:** Close of Registrations (at standard rate) for all Presenters
Submission of all (non-QA) papers
- 16th June 2006:** All other Conference Rate Registrations close.
Poster Competition entries close

David Hume, Impressions and Ideas [SB]

Utility is very much a part of current economic thinking, but it is not so long ago that the concept was developed. Volume 1 of David Hume's work, *A Treatise on Human Nature*, was published in 1748, and could therefore potentially have had an influence on early deliberations about utility. Part I Section II¹ of the volume discusses what he calls impressions, and their role as the generators of ideas. He divides impressions into those of sensation and reflection, describing the latter as passions, desires, and emotions.

Had this perspective formed the basis of thinking on utility, economics would be very different today. We could speculate on this. Briefly, Hume suggested that people experience something, giving an impression on the senses. This is then stored in memory as an idea. Recollections of this memory serve as further experiences, even though they are just in the mind. This can go on through several iterations. Much of the pleasure gained arises through internal processing of experiences, in which case development of the ability to process effectively could be as significant for utility as the act of consumption itself. The utility of consumption is not dependent just on the characteristics of the goods and services consumed. It also depends on how individuals process the effects of consumption (reflection). In other words, both preferences and utility gained are endogenous, and we can become more efficient in generating utility.

According to this view, it is not just a matter of getting utility from consumption. The act of consumption can produce multiple impressions as the act is recalled. For example, we could think of holidays not as consumption, but as an investment in memories. The benefits of consumption are then as much a matter of how we retain and generate impressions as of the act of consumption itself. As another example, might a child get more pleasure from one treasured toy, about which impressions can accumulate, than from many toys which are quickly forgotten?²

There are additional implications. Preferences and utility are unlikely to be fixed as they are based on a collection of sensations and reflections that is ever-increasing (or ever changing, at least, as people may forget). It would hardly be surprising, were we to develop and sustain distorted perceptions, but this may, to a degree, be unimportant. At least, in the opinion of Samuel Johnson³:

Without asserting Stoicism, it may be said, that it is our business to exempt ourselves as much as we can from the power of external things. There is but one solid basis of happiness; and that is, the reasonable hope of a happy futurity. This may be had every where.

We may also wish to consider whether today's mass media is resulting in too much stimulus and too little reflection.⁴

¹ Available online at:

<http://ebooks.du.ac.in/etext.library.adelaide.edu.au/h/hume/david/h92t/chapter2.html>

² For a recent much publicised example, consider also Mireille Guiliano's book, *French Women Don't Get Fat: The Secret of Eating for Pleasure* (2005, London : Chatto & Windus), emphasises savouring small quantities rather than consuming large quantities.

³ P.105 of Wain J (ed) (1976) *Johnson on Johnson*, London: Dent

⁴ We could also question the realism of these vicarious impressions. Even if the representations are factually accurate, audiences are detached observers, and they tend to see events from far more angles or perspectives, and get far more information in a more condensed form, than an individual in a lived experience. See also "Whose Votes" in this issue of *AI* for comments on experience and perception.

Noise and Perceptions

"The amount of noise made over economic and social change is determined, not by the extent and importance of the changes that actually occur, but by the reaction of contemporary opinion to the problem."

From p.218 of Trevelyan G M (1948) *English Social History*, London: The Reprint Society

The Use of Economic Models

“These merger outcomes with high barriers to entry can be simulated quantitatively using economic models. Such models are at best imperfect representations both of actual markets and of the behaviour of participants. Judgements need to be made about the assumptions that are built into such models, and the strength of the results that they can produce. Nevertheless, the Commission considers that quantitative modelling may be a useful complement in some cases to qualitative analysis in assessing whether the price effects of a merger would be likely to be sufficient to amount to a substantial lessening of competition.”

P.32 of "Commerce Commission Mergers and Acquisitions Guidelines", Commerce Commission, <http://www.comcom.govt.nz/Publications/ContentFiles/Documents/MergersandAcquisitionsGuidelines.PDF> (accessed 9 February 2006)

If they don't speak your language, just talk louder...

On p.10 of last November's *AI*, there was an extract from a newspaper from 1895. It included the following: “That the Government repeat that which has been shown to be useless in the past is not a matter for commendation, but for condemnation”. If, despite heavy use of a policy, the objectives are not achieved, should the policy be applied even more vigorously, or should the relationship between policies and outcomes be reassessed?

Reported in the *Dominion Post* of 16 January 2006, “Police and transport officials will hold a crisis meeting today in a bid to stem the carnage on New Zealand roads”.¹ This was because, “Another horror weekend – in which five people were killed – has taken the road toll to 23 dead in the first two weeks of 2006, compared with 11 this time last year.” Of the three proposed initiatives mentioned, one was, “Toughening up speed enforcement by issuing more tickets”.

¹ Chalmers A (2006) “Crisis meeting over road carnage”, *The Dominion Post*, 16 January, <http://www.stuff.co.nz/stuff/0.2106.3541255a10.00.html>

Principles-based Policies? [SB]

Leanne Dalziel is considering altering competition law so that there would be different rules for different sectors or industries.¹ This is a move away from consistent principles. The treatment will depend on the industry, not the underlying circumstances that underpin the intervention. There will be costs in terms of transparency and consistency of policy. The National Party managed to challenge race-based policies, saying that they should be based on need. Is there a parallel here?

¹Allen S (2006) “Dalziel may alter competition law”, *The Dominion Post*, 4 March, <http://www.stuff.co.nz/stuff/0.2106.3592136a13.00.html>

Work-Life Balance Conference, Wellington, 21 April 2006

A work-life balance conference is to be held in Wellington on April 21 this year. This conference is jointly hosted by the Roy McKenzie Centre for the Study of Families and the Institute of Policy Studies, Victoria University.

The original idea for the conference grew from discussions generated at the Treasury, MSD, Ministry of Women's Affairs and Department of Labour sponsored Workshop on Labour Force Participation and Economic Growth held in April 2005. At that conference, much of the focus was on the employment of women with dependent children. This conference aims to continue and expand the conversations by exploring work/life issues for families with dependent children. In particular, more attention will be given in this conference to work-life balance issues for men with dependent children. More information can be found at <http://www.vuw.ac.nz/ips/current-activities/index.aspx>

From the 2BRED File

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

This is absolutely my top MUST READ. If you only read one book from the 2BRED file this year, make it this one! Steven D. Levitt and Stephen J. Dubner *Freakonomics: A Rogue Economist Explores the Hidden Side of Everything* (New York: Harper Collins, 2005).

Levitt teaches at the University of Chicago; he received the John Bates Clarke Medal for the best economist under 40. Dubner is a journalist who writes in a most readable style. They have combined to present a popular version of some of Levitt's work. Levitt, by his own admission (in an interview last year with Kim Hill on National Radio) is largely a-disciplinary. He fears that his fellow economists don't take him seriously as he brings no sophisticated theory to bear – in the words of Steven Landeur “Economics is about incentives – the rest is commentary”. This seems to be the only theory that Levitt needs. He asks interesting questions and then specialises in combing enormous data sets with considerable statistical skill and impeccable logic to come up with answers that don't always fit the widely held perceptions. Without spoiling the book for you let me tempt you with a few of his examples.

Why has the crime rate fallen? Levitt has canvassed all the standard arguments (eg, lower unemployment, tougher sentencing, better and more policing) and rejects them all. His answer: legalised abortion which eliminated a whole cohort of potential criminals (ie unwanted children). Why do drug dealers live with their Moms? This is a fascinating insight into the structure of the drug dealing underworld. Why is the Klu Klux Klan like real estate agents? Why are sumo wrestling matches rigged? Here he analyses data from 32,000 bouts. What effect does incentive bonuses paid to teachers have on test score of students? This time an analysis of the test scores of every 3rd to 7th grade pupils in the Chicago public School system from 1993 to 2000. ie 30,000 students per grade per year, 700,000 sets of answers and 100 million individual answers. The result: teachers offered a \$25,000 bonus have an incentive to cheat – and 5 % do. But how Levitt detects this is a story much better than a good whodunit. Get hold of this as soon as you can – a couple of evening's great reading. But beware – nothing should or does go unchallenged and I have already seen the abortion story challenged by reworking the data.

One advantage of a spatially diversified family is that one has an excuse to travel to see them. So I made a trip to Johannesburg to play with my 2 year old granddaughter. Her mother works for the World Bank, and insists that her father show up every so often. Well, in between the Moms and Tots afternoons and the Monkeynastics classes, I delved into daughter's book case. Let me tell you about a couple of volumes I managed to get through. The first I suppose is compulsory reading for Bank staff, but anyone with an interest in development issues, leadership, management and institutional change will find this of interest. Sebastian Mallaby *The World's Banker: a story of failed states, financial crisis and the wealth and poverty of nations* (New York: Penguin Press, 2004).

Sebastian Mallaby is an Englishman with a distinguished journalistic career with the Economist and since 1999 with the Washington Post. This is the story of the World Bank during the presidency of James Wolfensohn from 1995 to 2005. The book ends with his 70th birthday in 2003. Wolfensohn is an Australian. He was born in 1933 and raised in modest circumstances in the Sydney suburbs by English parents who migrated during the Depression. Wolfensohn turned out to be a larger-than-life figure - an Olympian, a cello player (he played at his own 70th birthday party at Carnegie Hall) financier and philanthropist. But these accomplishments came with an extraordinarily complex character, typified by violent mood swings.

At times Wolfensohn could range from noble to the manic, considerate to the egotistical, from harm to the thoughtful, to outbursts of violent temper and rage. Mallaby weaves a highly readable account, drawing together the character of Wolfensohn and the evolving role of the World Bank.

He arrived at the Bank with three goals: (1) determined to reshape the arrogant, pampered and highly paid staff (“the World Bank is eliminating global poverty one employee at a time” as the old saw goes); (2) to divert the Bank from its obsession with structural adjustment; and (3) to establish a dialogue with the Bank’s detractors, principally the NGO community

On the first the book paints a picture of failure. His attempts at private-sector management systems were often ill suited and implemented in a way that managed to alienate the majority of his senior staff. The number of outstanding people who left in sheer frustration after being publicly dressed down by a volatile boss reads like a Who’s Who of development economics. On the second he had more success though it was a struggle against the intransigence of the mini czars who ruled their internal fiefdoms. They constantly bemoaned that he gave short shrift to the role of sound macro policies (the clarion cry of the structural adjustment battalions), and his visions for community-based development were seen as fanciful and ill-conceived. However, he did succeed in introducing poverty focus throughout the bank

On the third he can claim his greatest success. He went to extraordinary lengths to listen to the Bank’s critics and bring them into the tent: “we share the same goals - let’s do this as a joint venture”. This approach seemed to defuse some of the antagonism, in part by acknowledging the Bank had made mistakes in the past.

The book is a marvellous blend of the economics and politics of aid and development, set against the talented, visionary, frenetic and maniacal character of Wolfensohn. Writing history as it just happens inevitably involves a risk that one’s perceptions will be altered as time passes and allows a different perspective to emerge. Future historians will have the luxury of a longer perspective; but it is unlikely that the main thrusts of this fascinating insight into a man at the helm of the world’s most powerful organisations would be significantly altered. And perhaps there are insights here that might have been lost had we waited for the story to mature with the passage of time.

Increasingly the international development community focuses on Africa. Why after nigh on 50 years of independence (well ok, the French haven’t quite left yet) is it so hard to find a good news story? Why would Zambia today have a per capita income over US\$20,000 had it invested the billions of aid it has received in even modest paying projects? Why is Kenya so poor when it had the same GDP per capita as Taiwan in 1950? Robert Guest tackles these and much more in *The shackled continent: Africa’s past present and future* (London: McMillan 2004). Guest is the Africa editor for the *Economist*. He uses his insights as an economist and his first hand experiences (3 days in a beer delivery truck in Cameroon) to weave a very readable piece indeed.

He is hopeful. After the sacking of Rome, most Europeans spent the next 1000 years cold, undernourished, illiterate, governed by cruel warlords and corrupt and imbecilic monarchs who stole from the peasants in endless forms. There are no quick fixes in Africa but transparent government, a rule of law and respect for property to attract investors, investment in basic health, education and infrastructure – nothing new and flashy here. But one is left wondering whether in a generation from now the real gains in human welfare in Africa will be due mostly to Bill and Nancy Gates rather than more of the failed states and ineffectual foreign do-gooding.

There has been some wringing of hands that New Zealand’s at times strained relations with the United States may have impeded progress toward a bilateral trade deal with Uncle Sam. After all – look at the Aussies – they have not thumbed their noses at the USA and their willingness to sign up against the axis of evil has, so the story runs, given them the jump start in getting a trade deal. Well there are two sides to every story and Linda Weiss, Elizabeth Thurbon and John Mathews presented a jaundiced view of the Australian –US Trade Agreement in *How to Kill a Country: Australia’s devastating trade deal with the United States* (Sydney: Allen & Unwin 2004).

There is nothing particularly scholarly or refined from the three Sydney academics who believe Australia sold out and is on the losing end of the deal. As the *Sydney Morning Herald* wrote in its review: “It is a pure joy when a group of academics, released by anger from the constraints of scholarly punctiliousness, launches a truly savage, no-holds-barred polemic. And, boy, is this savage: a hard-hitting, unremitting attack on both the Howard

government and the Latham opposition over Australia's recent Free Trade Agreement with America ... This is a book that should be read by every Australian". Well maybe not quite, but it raises some interesting pointers about which those negotiating on behalf of the Kiwis might want to at least be alert.

**Grant Scobie, John Gibson and Trinh Le (2005) *Household Wealth in New Zealand*,
Institute of Policy Studies, Victoria University of Wellington**

This book is a synthesis of studies analysing the Household Savings Survey. This survey was funded by the Retirement Commission. The publication contains new information and brings together already published material. It has some interesting findings. For example:

"We examine in some detail the difference between Maori and European/Pakeha individuals. The fact that Maori are on average ten years younger alone explains nearly 70% of the difference in the net worth levels." (p.108)

"We find that the distribution of net wealth is significantly altered by the inclusion of human capital as an asset. [Using estimated lifetime earnings as a measure of human capital] For a young adult this could easily amount to four times the level of their reported assets..." (p.108)

"...those in the upper 40% of the pre-retirement income distribution appear to save at a rate greater than that prescribed by our approach to adequacy...Those relying on New Zealand Superannuation are from the lower income quintiles, and for them the preferred strategy is not necessarily to try and save more; that would reduce their current consumption levels, which are already low...Across the entire population, 25% would make no further savings for retirement if their preferred strategy is to achieve consumption smoothing. Over half of these come from the lowest income quintile." (p.111)

<http://www.vuw.ac.nz/ips/publications/new-books/HH%20Wealth.pdf>

Debasing the Liquid Gold

According to one explanation, the nursery rhyme "Jack and Jill" was an early lesson in tax policy. Jack and Jill (or Gill as the proper word) are measures of wine - Gill being a full measure and Jack being a half measure. The Gill was introduced in the 13th century to measure individual servings of wine.

When Charles I of England scaled down the "jack" (at that time a two-ounce measure) so as to collect higher sales taxes "up the hill", the Jill, by definition twice the size of the jack, was automatically reduced also and "came tumbling after."

The tax measure was so unpopular that it is thought to be one of the main reasons why the king "broke his crown" and was dethroned.

For more speculation and other explanations, see:

<http://www.rooneydesign.com/JacknJill.html>

http://www.rhymes.org.uk/jack_and_jill.htm

http://nurseryrhymes.allinfoabout.com/jack_and_jill.html

http://en.wikipedia.org/wiki/Jack_and_Jill_%28song%29

Economics as a discipline? By Stuart Birks

In recent years several writers have voiced concern at a perceived debasement of academic standards. Mark Bauerlein, referring to social constructionism, is one¹:

When someone holds a belief philosophically, he or she exposes it to arguments and evidence against it, and tries to mount arguments and evidence for it in return. But in academic contexts, constructionist ideas are not open for debate. They stand as community wisdom, articles of faith.

E J Mishan's similar but more general assertion, eight years earlier, bears repeating²:

Over the last three decades ideological doctrines have infiltrated the curricula of many of the larger universities. Spurious academic subjects ... putatively designed to 'raise consciousness' and strengthen commitment to credos of 'emancipation', manifestly fail to meet the stringent requirements of scholarship. Certainly the doctrines of these ideologically inspired 'studies' are not regarded by their proponents as provisional and refutable hypotheses. Clearly arrangements being made for their systematic propagation in these circumstances do not comport well with the idea of a university as a forum for open-minded enquiry and impartial scholarship.

I was interested, therefore, to come across a paper by Joan Robinson³ in which she said the following (p.309):

Professor Ferguson, in The Neoclassical Theory of Production and Distribution, asserts that belief in neo-classical theory is a matter of faith. 'I personally have the faith', he declares...

There is a problem of the indivisibility of capital, which then causes difficulties if we wish to apply marginal analysis. Hence (p.315):

Professor Ferguson concludes his account of 'reswitching' thus: 'The question that confronts us is not whether the Cambridge Criticism is theoretically valid. It is. Rather the question is an empirical or econometric one: is there sufficient substitutability within the system to establish neo-classical results?' And he states in the Preface: 'Until the econometricians have the answer for us, placing reliance upon neo-classical economic theory is a matter of faith.'

I am reminded of Peter Phillips quoting Hoover, who makes an even stronger claim of scientists: "even accumulated falsifications or anomalies do not cause scientists to abandon an approach unless there is the prospect of a better approach on offer"⁴. Socrates would content that it is better to acknowledge what we do not know rather than to cling tenaciously to unsupported and contradicted beliefs.⁵

Robinson concludes (p.317):

No doubt Professor Ferguson's restatement of 'capital' theory will be used to train new generations of students to erect elegant-seeming arguments in terms which they cannot define and will confirm econometricians in the search for answers to unanswerable questions. Criticism can have no effect. As he himself says, it is a matter of faith.

About the same time, Sumner Rosen made a similar point⁶

Long ago economists opted for a separation of their studies from fundamentals. In so doing they adopted a prevailing American view that the fundamentals are not in question. The older fashion of joining economic and political concerns into political economy passed from the scene. (p.417)

¹ Bauerlein M (2001) "Social Constructionism: Philosophy for the Academic Workplace" *Partisan Review*, Vol.68(2) <http://www.bu.edu/partisanreview/archive/2001/2/bauerlein.html>

² p.202 of Mishan E.J. (1993) *The Costs of Economic Growth*, Revised Edition, Westport: Praeger

³ Robinson J (1970) "Capital theory up to date", *Canadian Journal of Economics*, Vol.3, pp.309-17

⁴ Phillips P C B (2003) "Laws and Limits of Econometrics", *The Economic Journal*, 113 (March), pp.C26-C52

⁵ See paragraphs 7-9 of <http://classics.mit.edu/Plato/apology.html>

⁶ Rosen S M, "Keynes without gadflies", in Roszak T (ed.) (1968) *The Dissenting Academy*, Vintage, pp.62-91. Reprinted in Hunt and Schwartz (1972), pp.397-419. Page number refers to the latter.

Edward de Bono, in his book, *The Happiness Purpose*⁷, referred to religions as examples of meta-systems. It would seem that the body of economic thinking could serve some of the same functions.

Decision is easy when a powerful meta-system provides the values...It is in this area of simplifying decisions that meta-systems tend to be most powerful in action. And it is this practical power in action that gives meta-systems their appeal. People tend to take up a belief or meta-system because it reduces the confusion of their lives by making decisions so much easier. (p.23)

As another parallel with economics, deBono's proposed new meta-system is based on the principle that the legitimate purpose of life is happiness. However, he might disagree with economists as to how this is to be achieved.

And while on the topic of religion, there is an interesting hint of possible political motives for the adoption of utility theory in Jeremy Bentham's *Introduction to the Principles of Morals and Legislation*. That, along with related issues, is discussed on p.13.

⁷ deBono E (1979) *The Happiness Purpose*, Harmondsworth: Penguin

A thought about our assumptions – is there a paradox? [SB]

Economic theory seems to be caught between addressing **what is** and trying to explain **what should be**. It is often unclear which it is attempting to do. Should businesses be profit maximizing, or are we explaining market behaviour because firms are (assumed to be) profit maximizing? This has implications for the issue of rational economic agents. Are they rational, or should they be rational? If we are describing how they should be, (given certain assumptions about objectives), can we use the same models to predict behaviour? Should we distinguish between the two sets of questions?

The issue can be taken a step further. If people are assumed to be rational and well informed, then it would follow that advice from economists is of no benefit to them. Niskanen and Downs, among others, have developed theories which assume that, just like consumers and producers, public servants and politicians are self-interested. Should we not also take the additional step of assuming that they are equally rational? If all these people are rational, is there any need for policy advice from economists? Does economics then have anything to add to our understanding? Conversely, if economic advice can improve public sector policymaking, shouldn't it also be based on a view of the economy whereby individual economic agents may be poorly informed, irrational, and in need of economic advice (affordability and quality aside)?

Education

1) In Leeson E (ed) (1994) *The Macmillan Anthology of English Prose*, Pan Macmillan, there is a piece by Sydney Smith, "Female Education" from the *Edinburgh Review*, 1808. He points out, "A century ago, who would have believed that country gentlemen could be brought to read and spell with the ease and accuracy which we now so frequently remark, - or supposed that they could be carried up even to the elements of ancient and modern history?" (p.276)

2) There is a description of early universities in the US in Furnas J C (1969) *The Americans: A Social History of the United States 1587-1914*, London: Longman. It includes:

When, in 1801, Yale contemplated setting up a chair of chemistry and natural history – its first venture into exact science – the appointment went to a young alumnus, Benjamin Silliman, who, though most promising, knew nothing about either chemistry or natural history. (p.542)

Judge Tapping Reeve's famous law school at Litchfield, Connecticut, set up in 1784, eventually had as faculty two men – Reeve and a colleague, James Gould – neither of whom had ever attended law school. (p.542)

Charity, Tax and Contributing to the Public Good *By Stuart Birks*

A book used in New Zealand schools states¹: “All through the 19th century people in New Zealand who were poor, sick or old had only charity or their families to turn to for help. There was the idea that if you were helpless it was somehow your own fault.”

This is applying a modern connotation to the concept of charity. Other views may have prevailed in the past and in other places.

One insight can be found in Williams E N (1965) *A Documentary History of England Vol.2 (1559-1931)*, Harmondsworth: Penguin. Following the Poor Law Act 1598, churchwardens, and four substantial householders of every parish who were to be Overseers of the Poor, were to meet every month “upon the Sunday in the afternoon after divine service”. They could get permission to be absent due to sickness or other just excuse. Otherwise, “...upon pain that every one of them absenting themselves without lawful cause as aforesaid from such monthly meeting for the purpose aforesaid, or being negligent in their office or in the execution of the orders aforesaid being made by and with the assent of the said Justices of the Peace, to forfeit for every such default twenty shillings” (pp.32-33).

It is interesting that they were not to be paid for their work, but rather fined for failing to do the work. The discussion in the book suggests that the Act was only intended for emergencies, and was rarely used before 1660. Instead, “It has been estimated that over ninety per cent of the money spent on public welfare in the period before the Restoration came out of private pockets” (p.31).²

Other documents indicate that communities in England tended to care for their own, and it was only some time into the 19th century that central government took a greater interest in these matters. A further clue to this, and to the extent to which economic and social change undermined more traditional structures for providing public services, can be found in the same book. Williams gives examples of steam transport allowing grain imports from the US from the late 1870s, followed by refrigeration and meat imports from Australia and New Zealand.

Whether the landowners had been reduced to poverty or had saved themselves in the City, they now ceased to perform their paternalistic functions in the economy of the countryside. On arable lands, the amount contributed by landlords to improvements fell by forty or fifty per cent. And this economic abdication led to a fall in local influence, and thus (as will be seen) in political power. The reduction in the Earl of Pembroke’s gifts to charities in this period is vivid evidence of this. On his Wilton estate, he gave £206 for fuel in 1882, and £93 in 1902. His clothing donations were £207, and then £104. His gifts to the Church of England Schools fell from £1,100 a year in the early 1870s to £400 a year in the early 1900s, and then to £2 in 1909...Land was not only retreating before business, it was also handing over to the welfare state. (p.246)

This change in perceived social obligations, or the ability and manner of meeting those obligations, does not necessarily mean that current practices are better than those of the past. I spent a short time following up on the idea of contributing to public provision of services through supply of labour rather than payment of taxes. This is interesting because we could consider people requiring or having available not only money, but also time. Those earning most money may have very little free time, and the latter is also a valuable asset. In partial recognition of this, the UK (at least when I was there) operated an earned income rebate system, whereby income earned through work was taxed at a lower rate than unearned income

¹ P.25 of Naumann R (2002) *New Zealand History Basics 2: My History//My People*, New House Publishers

² For an account from 1577, see William Harrison’s description of provision for the poor in Holinshead’s *Chronicles* at: <http://www.fordham.edu/halsall/mod/1577harrison-england.html#Chapter%20IX> Harrison specifically recognizes an obligation to help what could be called the “deserving poor”, so at least in England in 1577 the poor were not all blamed for their circumstances.

from investments, for example.³ In part, the thinking was that, of two people with the same income, one not working would have the option of earning more through supply of labour, and so was better off than one who was already working.

More common now is a system where people's contribution to public activity is based on taxation, which relates to monetary activity and income. It does not generally consider the effort required to earn income, and it generally does not consider people's availability of time or capability of making direct contributions instead. In other words we are taking a narrow approach, and could consider time, or some substitution between time and money contributions. A traditional form of this was the *corvée* system. Briefly:

During the feudalization of the late Roman Empire, the corvée system was part of the social and economic system, but towns and all individuals were able to liberate themselves by money payment instead of services. In France the royal corvée, compulsory work on public roads, was introduced in the 18th cent. Both the royal and the seigniorial corvée bore heavily and almost exclusively upon the peasants and helped cause the French Revolution. In the 19th cent. the corvée was used to build public works, particularly the Suez Canal (1869).⁴

To give one possible criticism of labour contributions: Should people be forced to work for nothing? But what is happening when people are earning the money which is paid in taxes? You can more clearly identify the time sacrifice with *corvée*, but there could be a time sacrifice with any tax on earned income.

And for a second possible criticism: *Corvée* was very unpopular and led to the French Revolution. However, it was the unfair allocation and lack of benefits in return which led to the opposition. *Corvée* to maintain local roads lasted much longer, and there was an extremely long history of a similar system in Egypt.

While the system was sometimes misused, the same could be said at times for taxation, but it gives a different connotation to schemes such as "work for the dole". Instead of suggesting that the state should give people money and get nothing in return, it could be argued that people should contribute to public services according to their means, including available time (a relatively abundant resource for the unemployed). Considering personal income taxes alone, employees in the paid workforce are generally working between one and two days a week to fund public provision of goods and services. Those who are unemployed or not in the workforce are making no such time sacrifice.⁵

Further aspects of labour contribution can be found in descriptions of military service in Israel. Here are some basic details⁶:

All eligible men and women are drafted at age 18. Men serve for three years, women for 21 months...Upon completion of compulsory service each soldier is assigned to a reserve unit. Men up [to] age 51 serve 39 days year period time which can be extended in times emergency.

Married women are exempt, and there are some other variations to the basic requirement.

Also from the above source:

The original function of the reserves, as conceived by policymakers during the 1950s, was to serve as the principal fighting force during time of war. Over time this concept has

³ The UK is not unique in considering different treatment for income from work. There are some limited in-work benefits in some countries indicated on p.7 of: http://europa.eu.int/comm/employment_social/publications/2004/cev103004_en.pdf Contributions in the form of time include military service and jury duty. Many countries maintained a system of national service for some time after World War II, although this is now the exception. The burden fell primarily on men at a time when distinctions between men's and women's roles in society were considered acceptable.

⁴ <http://www.encyclopedia.com/html/c1/corvee.asp>

⁵ Taxation is not the only area where prevailing perceptions of economic activity are one-sided, considering either just the rewards, or just the effort required, not both. Others are the general difference in consideration of paid and unpaid work, and in comparisons of GDP. Radically different conclusions can be drawn by taking an alternative perspective, as indicated by the expression, "same ball, different spin".

⁶ From: <http://www.globalsecurity.org/military/world/israel/army.htm>

changed and now 80 percent of reserve duty is for purposes of maintenance and administration operational work, which is not connected to combat. This change in concept is a result of the IDF not having to pay the real cost of its reserve forces. This cost is in fact passed on to the taxpayer and the economy as a whole.

This is a valid economic point. The supply of labour may be less efficient than the supply of money to hire the most suitable labour, but what of those who can supply labour but not money? At the same time, should we assume that tax revenue is always used most efficiently?

There is another aspect to military service in Israel. An Israeli Defence Force document mentions a social function (which may be facilitated by the security situation, and hence not readily applicable in other countries):

David Ben Gurion, Israel's first Prime Minister and Defense Minister, used to say the IDF is not only a means of defending the country, but also a means of integrating and building Israeli society. In Israel, the army contributes a valuable and dynamic social function alongside its military and security role, including a commitment to education and social values. Society is involved to an unparalleled extent in the military. In a country that has housed millions of Jewish immigrants and refugees from all over the world, one cannot overemphasize the role the army has played as a social leveler. People from all social, economic and political backgrounds perform military service side by side, with the same conditions and rights.

This highlights another dimension which may be overlooked by economists as a result of our current concept of utility, that of individuals as part of a wider community. This is discussed elsewhere in this issue of *AI*.

In addition to indicating that we may have a distorted perception of the past if we view it through the lens of current views, these examples raise issues about the nature of society and community, and various methods of contributing to public services by donation, supply of labour and taxation. Current thought may not embrace the full range of options and aspects that these suggest, in which case we are, by default, overlooking some potential policies and some dimensions of social organization.

Accuracy of valuations [SB]

An interesting example of valuations appeared in the *Sunday Star-Times* on 18 December last year¹:

“The valuations go to the heart of how much the company is worth, because different valuations valued the vineyards at between \$51 million and \$90m, depending on how they were carried out.”

Similarly, a valuation of Capital Properties was discussed in the *Dominion Post* of 19 October.² “Deloitte has said that the fair value is between \$1.48 and \$1.73”. The article’s author gave reasons why valuations can be so variable.

More recently, valuations for shares in Calan Healthcare Properties Trust have hit the headlines. First, there was a “consensus valuation of \$1.10 a unit based on the research published prior to ING’s announcement of the market stand by the four NZX brokers who report on Calan”³, then, shortly afterwards, Ferrier’s valuation of \$1.48.⁴

If this is the sort of information guiding people’s decisions, how good will their decisions be? If the valuations used by economists to analyse policy options and outcomes are as variable as these, how confident can we be about our results. To what extent are these valuations the results of advocacy research by hired guns?

¹ Ninness G (2005) “Vineyard valuations get shareholders' tongues wagging”, 18 December, *Sunday Star-Times*, <http://www.stuff.co.nz/stuff/sundaystartimes/0,2106,3515249a6445,00.html>

² McKay B (2005) “The tricky art of apt valuation”, *The Dominion Post*, 19 October, <http://www.stuff.co.nz/stuff/0,2106,3448840a1865,00.html>

³ [http://www.ingproperty.co.nz/WEB/webp.nsf/content/Announcements on 31 January 2006](http://www.ingproperty.co.nz/WEB/webp.nsf/content/Announcements%20on%2031%20January%202006)

⁴ Gibson A (2006) “ING needs to increase Calan bid by 11c a unit, says analyst's report”, *The New Zealand Herald*, 27 February, http://www.nzherald.co.nz/section/story.cfm?c_id=3&ObjectID=10370191

Utility – a narrow concept? By Stuart Birks

There are some intriguing aspects to utility. It is now central to conventional economic approaches to consumer behaviour, commonly taking individuals as independent with exogenous preferences in terms of available goods and services. It might not have turned out that way (see the piece on Hume in this issue of *AI*). It was once presented as one of several alternatives. In chapter 2 of his book, *Introduction to the Principles of Morals and Legislation*, Jeremy Bentham suggested asceticism as one alternative, identifying this approach with two different groups:

*There are two classes of men of very different complexions, by whom the principle of asceticism appears to have been embraced; the one a set of moralists, the other a set of religionists. Different accordingly have been the motives which appears to have recommended it to the notice of these different parties. Hope, that is the prospect of pleasure, seems to have animated the former: hope, the aliment of philosophic pride: the hope of honour and reputation at the hands of men. Fear, that is the prospect of pain, the latter: fear, the offspring of superstitious fancy: the fear of future punishment at the hands of a splenetic and revengeful Deity.*⁵

The mention of morals is interesting in that, in a note in the previous chapter (in the 1823 edition), Bentham voiced concern about people's perception of the term "utility", suggesting it was not clear enough at showing, among other things, "*the standard of right and wrong, by which alone the propriety of human conduct, in every situation, can with propriety be tried*"⁶

The positioning of religion as an alternative to utility is also interesting in another context. He was writing at a time of political upheaval, with revolutions in France and America, and when there were calls for reform in Britain which, once introduced in 1832, only extended the vote to 14% of adult males. At the same time, there was rapid population growth, urbanization, and increased education. In that context, the power of the established church was in decline, and his approach to utility was useful in that it offered an alternative perspective.⁷ We could link this to Rosen's assertion, "Economists have historically worked on a foundation consisting of the central issues of their era and the central values of the writer"⁸. If this is so, then economists should not hold on to the apparent fundamentals as an act of faith, as these fundamentals may well be time and place specific.

Looking closer to the present and outside the bounds of economics, there are currently alternative paradigms which can lead us to question the general applicability of our conventional utility-based perspective. On p.9 of *AI* No. 20 there is a brief outline of a perspective on happiness by a psychologist, Martin Seligman. He gave three aspects, the second of which would overlap with David Hume's "reflection". His third I had subconsciously redefined and split into a "feeling of belonging" and a "sense of purpose".

On mentioning this to a friend, she immediately linked them to Abraham Maslow's "hierarchy of needs". Starting with the most basic, the classes of need are i) physiological, ii) safety, iii) needs of love, affection and belongingness, iv) needs of esteem, v) needs for self-actualisation.⁹ Perhaps this is why I had picked belonging and purpose.¹⁰

⁵ <http://www.la.utexas.edu/research/poltheory/bentham/ipml/ipml.c02.html>

⁶ <http://www.la.utexas.edu/research/poltheory/bentham/ipml/ipml.c01.html>

⁷ Incidentally, while we generally take an individualistic approach and consider society as a collection of individuals, Bentham also wrote in Chapter 1: *By utility is meant that property in any object, whereby it tends to produce benefit, advantage, pleasure, good, or happiness...: if that party be the community in general, then the happiness of the community: if a particular individual, then the happiness of that individual.*

⁸ P.417 of Rosen S M, "Keynes without gadflies", in Roszak T (ed.) (1968) *The Dissenting Academy*, Vintage, pp.62-91. Reprinted in Hunt and Schwartz (1972), pp.397-419. Page number refers to the latter.

⁹ See: <http://honolulu.hawaii.edu/intranet/committees/FacDevCom/guidebk/teachtip/maslow.htm>.

Edward deBono also considered the value to people of attachment to something, "Man is so successful that too little of his time is taken up with eating and so more is left for wondering about his purpose in the world. One of the prime functions of a meta-system is to give him a purpose..." (deBono E, 1979, *The Happiness Purpose*, Harmondsworth: Penguin pp.22-23)

We could speculate on how consideration of these two might influence the policy advice given by economists. It links to one of the stated benefits of military service in Israel. It might indicate that public service provision through taxation (as it is currently viewed) denies the payers a feeling of participation and acknowledgement of their contribution. Do people see their tax contributions as something to take pride in, or to avoid as far as possible? Are taxpayers ever thanked for their contributions?¹¹ Might public labour input by those who are unemployed or not in the workforce of, say, eight hours a week give a sense of contributing to society? Do restructurings and increased credentialism and accountability meet or work against people's needs? There is an entire avenue of investigation to be pursued here which might be overlooked in conventional economics.

¹⁰ These are by no means exceptional outside economics. One relative concept of poverty specifies an inability to participate in the normal activities of a society. In New Zealand, the Labour Government has emphasised "inclusion" as an important social criterion (see Birks S, 2000, "'Inclusive' Versus 'Exclusive' Approaches", pp.i-v of CPPE Issues Paper No.9 at: <http://econ.massey.ac.nz/cppe/papers/cppeip09/cppeip09.pdf>).

¹¹ Lack of acknowledgement could be a factor in the free-rider problem.

Whose preferences? By Stuart Birks

A newly published health economics paper adds to the literature that raises interesting questions about recognizing people's preferences.¹ The authors are discussing valuations of health states, and in their conclusion they state, "There are some real concerns with use of largely uninformed general population values" (p.207).

They discuss alternatives, such as "those who are actually in the state (i.e. the patient)" (p.202). This can be problematic, "There is evidence of significant discrepancies in health state values by illness experience and in general the evidence points to patients giving health states a higher value than do members of the general population" (p.202).

They present three causes of discrepancy:

- i) Patients and the general population do not value the same states. For example, the public may not have a clear picture of the state. Hence they are expressing preferences over different things.
- ii) They use different measuring rods. There can be "response shift" as people respond differently when their circumstances change, such as moving into the state. In addition, there is a, "distinction between patient and general population perspectives. A general population sample is being asked to take an *ex ante* perspective and imagine or predict the likely impact of a theoretical future state on their utility, whereas patients are being asked to adopt an experiential perspective where they are asked to value their current state of health. There may be important normative reasons for favouring one over the other. People are not very good at predicting future preferences." (p.203) People's preferences are likely to change if they become directly involved.
- iii) "Patients experience shifts in values that are not anticipated by the general population." (p.202) Hence, "People are likely to adapt to their state of health in a number of ways, both physically and emotionally...The response shift literature...refers to psychological adaptations..." (p.203) People experiencing events may also view them in a distorted way, as with "peak-end" effects where peaks and end states are particularly significant.

These factors apply not only to health issues, but to perspectives and policy issues in general. Young and old people may have quite different perceptions of old age, for example. This leads to some uncomfortable questions. It is argued that it may be inappropriate to simply take expressed preferences from the general population as a basis for evaluating health policies. Reasons for this include, i) people's lack of knowledge, and ii) the possibility that their preferences could be different if they were directly affected. At the same time, those who are directly affected may have distorted impressions also.

¹ Brazier J, Akehurst R, Brennan A, et al. Should patients have a greater role in valuing health states? *Appl Health Econ Health Policy* 2005; 4 (4): 201-208

How should we approach policy issues generally? Should we aim to identify the people affected, determine their preferences, correct for any possible distortions, and then determine the best course of action? Should we use a wider group of people, ensure they are properly informed about the issues, then determine their preferences and so on?

To put this another way, are there questions about whose preferences should be used, considering people's degree of involvement and level of understanding? Should there then also be further processing of preferences to eliminate distortions? As the authors assert, "A social perspective does not imply the use of general population values any more than welfare economics implies patient values" (p.204), and "There are some real concerns with the current use of largely uninformed general population values" (p.207).

These seem to be legitimate points, and they are being asked in the health area at least. If they are legitimate there, can we justify ignoring them elsewhere, as in general elections. We currently have a system where virtually all adults have a vote, although most issues would involve some people more than others, and the level of understanding of issues varies widely over individuals and over issues. Universal suffrage, with equal weight given to each individual, is a relatively new system, being only about 100 years old, and it is radically different from previous systems where people's say was based on factors such as property ownership, citizenship, membership of an elite group, levels of education, and sex. Should we all have a vote on all issues? Should everyone's vote always have the same weight? At the very least, there is a contradiction between a body of literature which discusses whose preferences should be considered and a political system which ignores such issues.

This could have wider significance also in terms of people's perceptions of their place in society, and the mandate given to government to intervene in our lives. To personalise this, you could ask yourself who should be deciding how the government can intervene in your life. It raises fundamental issues of the roles of individuals and the state, and the way individuals are perceived within the state. Some relevant aspects are discussed elsewhere in this issue of *AI*, as with the changed views of charity, and of the social responsibility of wealthier members of the community, and the recognition of individual contributions to the public provision of goods and services.

We could also consider the quality of expressed preferences, and the extent to which we should be comfortable with decisions and resource allocations guided by these preferences. In the light of the above, it seems paradoxical that we use governments, elected through questionable and simplistic methods of assessing society's preferences, to correct for the failures of markets, which are based on complex and detailed expressions of preferences.

Economics in Literature

H G Wells book, *The History of Mr Polly*, (a good read) was published in 1909. Chapter 7.3 presents a presumably fictitious academic account of the behaviour of the lower middle classes of the day. It is too long to reproduce here, except for a short extract:

A great proportion of the lower middle class should properly be assigned to the unemployed and the unemployable. They are only not that, because the possession of some small hoard of money, savings during a period of wage earning, an insurance policy or suchlike capital, prevents a direct appeal to the rates. But they are doing little or nothing for the community in return for what they consume; they have no understanding of any relation of service to the community, they have never been trained nor their imaginations touched to any social purpose. A great proportion of small shopkeepers, for example, are people who have, through the inefficiency that comes from inadequate training and sheer aimlessness, or improvements in machinery or the drift of trade, been thrown out of employment, and who set up in needless shops as a method of eking out the savings upon which they count. They contrive to make sixty or seventy per cent, of their expenditure, the rest is drawn from the shrinking capital...the day when a man might earn an independent living by unskilled or practically unskilled retailing has gone for ever.

I have heard similar accounts for the present day.

The book can be found online at: <http://etext.library.adelaide.edu.au/w/wells/hg/w45hm/>

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 Auckland University of Technology. 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 Auckland University of Technology as at March 2006.

Compiled by Gail Pacheco, gail.pacheco@aut.ac.nz

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Message from the editor of *New Zealand Economic Papers*

Many of you will be wondering what has happened to *NZEP*. My first year as editor was difficult. It started with few contributed papers, although a good number of quality papers have subsequently been processed. However, the year ended with the printer going out of business without warning. Nevertheless, both issues have been compiled. The June 2005 issue is now being printed, and the December issue is with the typesetter. You should receive both issues shortly.

As for the future, I have every reason to be optimistic that subsequent issues of the journal, starting with the June 2006 issue, will be approximately on time. We now have a healthy stock of good papers at various points in the pipeline – four of which are expected to come through very shortly indeed. Barring unforeseen circumstances and, for the moment, putting asymmetric information aside, the future looks bright and timely.

Thank you for your patience.

Ian King, Editor, ip.king@auckland.ac.nz

...about NZAE

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

Nicola Chandler (BERL); **David Grimmond** (Infometrics Ltd); **Angus Charteris** (MFAT); **Suella Hansen** (Network Strategies Ltd); **Michael Quinn** (The Treasury); **Mark Robinson** (student).

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