

NEW ZEALAND ASSOCIATION OF ECONOMISTS (INC.)
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ASymmetric information

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

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REMINDER: NZAE ANNUAL CONFERENCE
27TH, 28TH AND 29TH JUNE 2007 IN CHRISTCHURCH
Visit the Website <http://nzae.org.nz/conferences/>
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/>*

Unstated assumptions?

EDITORIAL

Well, the 47th annual conference proved to be very lively, indicating that the Association and the economics community in New Zealand are in good heart. One comment from an overseas visitor was that economists here seem to be relatively mainstream, whereas larger countries can foster alternatives and splinter groups. Perhaps we are constrained in that any splinter group here is likely to have a membership of only one or two. At the same time, a case could be made that New Zealand should be an outlier, having some distinguishing characteristics of its own.

It is sometimes suggested that individuals filter information to see what they want to see (“selective thinking”, <http://skepdic.com/selectiv.html>), or what supports their preconceived views (“confirmation bias”, <http://skepdic.com/confirmbias.html>). In that context, I left the conference with a distinct impression that much of our economic and econometric analysis relies on unstated assumptions. Moreover, many of these assumptions are such that they fundamentally affect our perceptions and conclusions. Meanwhile we construct complex technical issues for debate and research. We run the risk of ignoring simpler issues and analyses which could be more fruitful, more useful, and more readily incorporated into multidisciplinary debate on policy issues. It is important for our own relevance that we stay aware of the limitations of our knowledge and techniques.

On another theme entirely, I would like to acknowledge the sterling work of the organising committee for the AWH Phillips Symposium, to be held on 9-11 July 2008 in Wellington. This is a massive event for New Zealand and marks the 50th anniversary of the publication of Bill Phillips’ paper in *Economica* on what is now called the Phillips curve. You are all encouraged to visit the Symposium web site to see what is in store for us. It is at: <http://www.phillips08.org.nz/>

Mention should also go to Dawn Gorman, who has relinquished her position as the NZAE treasurer after many years of solid service. Thanks, Dawn, for all your input into the Association. You have been a big help. Best wishes for the future.

by Stuart Birks, Massey University

Members are invited 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.

What would you choose?

Imagine you are faced with a choice of career. You are offered an option to spend your working life using, teaching, or developing a body of thought which bases much of its reasoning on a particular assumption about human behaviour. That assumption is that individuals obtain satisfaction solely from the consumption of economic (commonly marketed) goods and services. The more they consume, the better off they are. Unless explicitly considered, the following are, by default, considered irrelevant in any analysis: participation in family life; contact with others; conversation; enjoyment of non-economic goods; peaceful reflection; lack of stress; freedom of choice; independence; striving and sense of achievement; or any other aspect of life. Would you choose that career?

A “not to be missed” classic from the satirical publication *The Onion*:

“Housewife Charged In Sex-For-Security Scam”

<http://www.theonion.com/content/node/39495>

John Kenneth Galbraith (1908-2006) By Jim Alvey j.e.alvey@massey.ac.nz

John Kenneth Galbraith, the well-known economist and public intellectual, died on 29 April 2006. He was a writer, economist, diplomat, and one of the “beautiful people” in the 1960s.

Galbraith was born in Canada and completed his early life and education in a farming area in southern Ontario. It was only after completing his undergraduate education (at the Ontario Agricultural College, which is now the University of Guelph) that Galbraith moved to the USA. He completed his PhD at the University of California, Berkeley. Soon after, Galbraith began teaching at Harvard and acquired US citizenship. He served in various governmental roles during World War II. After the war, Galbraith was appointed by Harvard as a professor of economics and he spent the rest of his academic life there (Emeritus Professor after 1975).

The discipline of a rural upbringing was applied by Galbraith to writing. He wrote early in the morning on most days. Such work habits, combined with a natural aptitude, led to him producing some 33 books including *American Capitalism; The Concept of Countervailing Power* (1952), *The Affluent Society* (1958), *The New Industrial State* (1967) and *Economics and the Public Purpose* (1973). Galbraith became a public intellectual and attracted wide attention in almost all of his activities. In 1972 he reached a peak of recognition within the economics profession when he served as President of the American Economic Association.

Galbraith placed stress on the historical evolution of capitalism and the need for economic theory to adapt to the changes in economic “reality.” He wrote in the institutionalist tradition of Veblen, although he preferred to call himself a Post-Keynesian (Galbraith was a leading figure in the *Journal of Post Keynesian Economics*). One of his persistent themes was the rise of big business. Much of his work focussed on the US economy. Galbraith’s analysis was controversial and his policy prescriptions were even more so. He portrayed the American economy as dominated by large corporations. Galbraith argued that the “planning system” of the top thousand corporations (in a symbiosis with the government) controlled the American economy. Further, he rejected the notion that consumer sovereignty applied within the “planning system” (even if consumers played a role in the residual “market system”). Thus, Galbraith labelled the process of demand-driven production portrayed by neoclassical economics as the “accepted sequence”; opposing this, he described the “revised sequence” in which producers manipulated demand to ensure that their production was sold. The latter sequence, Galbraith said was a recent economic phenomenon which neoclassical economists conveniently chose to ignore; it had arisen in the twentieth century in developed capitalist economies because large, vertically-integrated firms had freed themselves from market constraints. His socialist solution was not to increase competition but to recommend more democratic controls over the “planning system.” Throughout his writings Galbraith consistently opposed anti-trust laws (on this occasion joining with libertarians and Austrians); such laws, he said, ignored the existence of such firms and their superior efficiency.

He rose to prominence after World War II and had considerable influence in public affairs in the 1950s, 1960s and 1970s. In the battle of ideas, Galbraith often had to compete with Milton Friedman. The pair had many campus debates. In later years, Galbraith conceded that Friedman was quicker on his feet than him (but he went on to say that he, Galbraith, wrote better). Galbraith was never publicity-shy and wrote and starred in his own television series in 1977 called *The Age of Uncertainty*. Once again, Friedman was not to be out-done; he wrote and starred in his own series in 1980 (*Free to Choose*). Over the years, the profession swung strongly behind Friedman rather than Galbraith. This is evident not just in the award of the Nobel Prize to one but not the other.

Why was Galbraith a pop icon and increasingly marginalized by economists? Four aspects stand out. First, after his early book called *A Theory of Price Control* (1952) was ignored, he decided to pitch most of his publications at the general public rather than his economist colleagues. Several of Galbraith’s books were best sellers. It is an oversimplification to say that Friedman published scholarly works in prestigious journals, like the *American Economic Review* and the *Journal of Political Economy*, whereas Galbraith published non-scholarly books published by Penguin (see C. Crook “John Kenneth Galbraith, Revisited” *National Journal* May 12, 2006). Nevertheless, a survey of Galbraith’s writings shows that he rarely published in the top mainstream journals after the 1950s (see S. Dunn and S. Pressman “The

Economic Contributions of John Kenneth Galbraith” *Review of Political Economy* 17(2)(2005): 161-209). Second, and to some degree linked to the first, was his negative views of mainstream economics and the capitalist economy. Galbraith showed a lack of interest in the neoclassical economics literature and rejected its methodology (which had become increasingly abstract and mathematical). Indeed, in his writings he became increasingly critical of mainstream economics, and the nature of modern American capitalism. Thus, Galbraith’s populism came at a substantial and increasing price. Third, he was an interventionist, a supporter of big government. As Friedman has remarked on many occasions, “the tide has turned.” Friedman, rather than Galbraith, was on the winning side of the ideological war. Fourth, there was a disconnection between Galbraith’s colourful writing and economic reality. As Galbraith himself asserted, he did write well and had some flashes of inspiration. Reflecting his literary bent, Galbraith’s writings often included memorable phrases such as “countervailing power” and “the affluent society.” Nevertheless, his writings often lacked testable hypotheses; those testable hypotheses and predictions that he suggested have often been refuted (one famous prediction was the convergence of capitalism and the centrally planned economies).

During the last thirty years, Galbraith’s respect within the profession has fallen away considerably. His works are now largely ignored outside of some heterodox circles. Friedman deserved to win many of the battles of ideas.

No account of Galbraith is complete without mention of his politics. He was an activist for the socialist side of American politics. Galbraith was a former speech writer for a number of Democratic candidates for the office of President of the US. He served as a Presidential adviser. President Kennedy appointed him to be Ambassador to India; Galbraith served in that office for a little over two years.

On a personal note, I would like to mention that I heard a lecture by Galbraith in 1991, in my years at Toronto. He was bright and enthusiastic (except when it came to the administration of George H.W. Bush). The symposium was called “the economics of peace” and his lecture, like many others of his, was published. Many of Galbraith’s statements on that evening echoed his earlier writings. Galbraith’s hair was entirely grey, his voice was a little weak and his stoop lowered him to just 2 or 3 inches over 6 feet (in his early adulthood, Galbraith stood at 6 feet 8 inches). The lecture was at night and, due to his tiredness, he did not stay for refreshments and informal questions afterwards. Still, I remember thinking how well he had performed at 82 years of age.

In recent times Galbraith was less active on the lecture circuit and in writing. His lifespan of 97 years was impressive (surpassing von Hayek (92) and von Mises (92)). No doubt Milton Friedman, who is 93, will want to surpass him here as well.

(Note: Paul Samuelson will be 91 on 15 May)

The Family Wage...

It would appear that the concept of the family wage is not entirely dead. There is at least one mechanism in the US whereby an employee’s remuneration package depends on family composition:

...employers in the United States provide a substantial amount of compensation to their employees in the form of health insurance. According to a 2003 survey, employers spent an average of \$6,700 and \$2,900 for a family and single health plan, respectively, above and beyond the employee’s contribution [7].

[7] Kaiser Family Foundation, 2003, “Employer Health Benefits: 2003 Annual Survey.” Kaiser Family Foundation and Health Research and Educational Trust.

From p. 209 of Nicholson S, Pauly M V, Polsky D, Baase C, Billotti G M, Ozminowski R J, Berger M L, and Sharda C E (2005) “How to Present the Business Case for Healthcare Quality to Employers”, *Applied Health Economics and Health Policy*, 4(4), pp.209-218.

From the 2BRED File

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

If there has been one word that has focused the minds of the international community in the last two decades it has been *globalization*. The very word now carries a pejorative overtone. Greens and church groups, Marxists and indigenous rights campaigners, human rights activists and environmentalists have coalesced in a loosely woven network of disparate dissidents around the rallying cry of this word.

Of course the global movement of people, goods and ideas is scarcely new. Early man went walkabout from Africa 100,000 years ago give or take an odd fortnight. Technology (albeit often military in origin) spread across the globe as did religions, ideas, innovations and trade. When we take a long view and relate it to the staggering improvements in human welfare (even those in the last 50 years) we could ask: so what's so wrong with globalization? Of course we can all make a list of the downsides, even after acknowledging the problem of the counterfactual.

Martin Wolf has tried to abstract from the passionate debate that can inhibit reasoned discussion and in *Why Globalization Works* (New Haven: Yale University Press 2004) addresses the critics and lays the blame for failure on policies and politics, not global market forces. At no point does he cower from facing hard questions and suggesting solutions that could make matters better. He combines his talents as an economist and journalist to produce a readable volume that “slices and dices both the critics and the cheerleaders of economic globalisation” (Rogoff).

Now attentive readers of *2BRED* will recall my exhortations in the last column to read Stephen Levitt's *Freakonomics*. Well this next book comes with the recommendation from Levitt: “required reading”. So if I recommended Levitt and he recommends Harford, then I believe that the transitivity axiom requires that I recommend Harford. This is not a difficult task. *The Undercover Economist: Exposing why the rich are rich, the poor are poor and why you can never buy a decent used car*, by Tim Harford (New York: Oxford University Press 2006) which, apart from winning the 2006 *2BRED* award for the longest sub-title, is an excellent read. I have long held that this is the sort of book that should be the text for Economics 101 if we want students in Econ 201. Proving that the marginal cost curve cuts the average cost curve at its minimum point for a 101 class always struck me as the way to maximize the bums on seats in a marketing or business communications course next semester. It surely would not turn the class on to economics!!

But Harford will. He has a superb knack of taking the everyday and leading the reader through the simple economics of a cup of coffee, traffic congestion, second hand cars, why some countries are poor, why China grows so fast and why globalisation beats the alternative. As a trained economist and a lead writer for the World Bank, he combines a sharp eye, great logic and clear writing. The book is relieved of heavy scholarly footnoting and referencing, but the extensive notes to the Chapters document the sources of his stories and shows a command of the serious (but boring?) literature that underpins his writing.

A novel way of viewing issues in the development of economics comes from **David Colander, Richard Holt and J. Barkley Rosser** in their book *The Changing Face of Economics: Conversations with Cutting Edge Economists* (Ann Arbor: University of Michigan Press, 2004). Interviews, which make up this book, can vary from the insightful to the maudlin. These are much more in the former camp you will be relieved to know. The book grew from a perceived need to demonstrate to the post-Keynesian fringe of the profession that the mainstream did have new and exciting developments going on inside it. So if you want to catch up with thinking of those who are arguably among the front runners and see how their work is contributing to recent developments in economics, this could be a great place to start. Of course there will always be debate about who should be included but with McCloskey, Binmore, Gintis, Frank, Rabin, Brock, Foley, Norgaard, Axtell, Young, and commentaries by Arrow and Samuelson, then one has a formidable selection (if somewhat

yanquentric). But this one is more for your scholarly moments than to add to the bedside table.

Without a doubt one of my favourite writers is **Thomas Sowell**. And what a prolific writer. A quick check at <http://www.tsowell.com/> confirms that he produces a new volume about every 18 months. And I realise I have been slipping behind in keeping you up to date – my apologies, dear reader. I solemnly undertake to do better and enrich **2BRED** with more Sowellian gems in future columns. In the meantime, permit me to cover my tracks a bit and take you back. ***The Vision of the Anointed: Self-Congratulation as a Basis for Social Policy*** (New York: Basic Books, 1996) had escaped my notice, more is the pity.

In this book Sowell paints a picture of a small but influential elite intelligentsia, who aided by politicians and the media have increasingly set the social policy agenda in their vision. A blend of liberalism (in the US sense of the term), political correctness and social engineering. In short, a bunch of well meaning folk who are out to make the world a better place according to their vision of how which should think and behave.

The privileged students of the Sorbonnes of Paris who led the recent riots, tore themselves from their books to protest against labour market reforms. Their vision was a world where strong labour market regulations were there to protect the weak from the exploitations of greedy business. As a number of more astute commentators observed, the irony that by preserving the existing laws they were entrenching their favoured status at the expense of the poor unemployed Muslim migrant worker, did seem to be lost on them in the excitement of the revolutionary moment.

This example typifies the approach taken by Sowell. He examines the vision created by a group in society and then explores the ramifications in a wide range of social policy and judicial rulings. He carefully looks at the evidence and compares “the promised benefits of policies based on that vision (with) the grim and often bitter consequences of those political and judicial decisions”. Tax dollars can be invested in the industries of the future, irresponsible mothers taught parenting skills, criminals can be rehabilitated, pay equity can be achieved by legislation, sentences are reduced because the victim had a childhood less happy than that of the anointed. In short, as Sowell argues, in a world where reality is seen to be socially constructed, there is no end to the scope for deconstruction and recreation to fit the vision.

Nicely Worded

Reporting on a fall in the \$NZ:

ANZ senior currency dealer Mark Elliott said there was no single event which triggered the fall.

*"On currency markets **there's not a symmetrical relationship between information and market movements.***

"A lot has to do with the underlying psychological position of the market."

("Exporters cheer as kiwi heads south", NZ Herald, 8 March 2006)

Research Assessment Exercises Criticised

Donald Gillies is critical of what he sees as a bias towards conventional paradigms as a result of research assessment exercises. He sees them as resulting in what is effectively a two-stage peer-review process because it is easier to publish more conventional material.

See Gillies D (2006) "Why Research Assessment Exercises Are a Bad Thing" *post-autistic economics review*, issue no. 37, 28 April, article 1, pp. 2-9,

<http://www.paecon.net/PAEReview/issue37GallagherZarsky.htm>

"Happiness lies not in the mere possession of money; it lies in the joy of achievement, in the thrill of creative effort."

Franklin D Roosevelt, Inaugural Presidential Address. Washington DC, 4 March 1933.

Conference papers are now available at: <http://www.nzae.org.nz/conferences/2006/>

Your NZAE conference reporter attended two conferences in consecutive weeks, the second being that of the Public Health Association. The contrast was marked. For the NZAE, people are generally detached from the issues they are researching, whereas this is not the case for the PHA. This can have a big impact on the way the issues are perceived. There is a danger on the one hand of abstracting too much and not seeing key aspects, and on the other hand of being too emotionally involved to take a balanced view.

The NZAE conference included a preponderance of presentations that were primarily technical descriptions of research undertaken. The analysis was generally based on economic models and/or the quantitative estimation of such models. The PHA conference included a heavy practitioner input, qualitative analysis and/or sweeping subjective assessment.

Save for a sub-group of “academic” papers, the technical standard at the PHA conference could not match that at ours. On the other hand, many of their presenters had a direct, real-world experience in their subject areas, along with a significant emotional commitment to the issues. Economists may well discount such factors, except that economics is but one input into policy debate. Our advice has to be relevant for, and convincing to, this sort of people. While we could present serious criticisms of their approaches and reasoning, they could and did present some damning criticisms of us in return.

I mention this here because of a related comment at an all-day Families Commission seminar a month ago. A qualitative researcher said she was pleasantly surprised to see quantitative researchers focusing on definitional problems with their data and the way in which such data may not represent the diverse range of situations that we should be investigating. Put simply, qualitative research can focus on the specific characteristics of individual cases. Quantitative research requires aggregation, and this sometimes involves making heroic (i.e. clearly unrealistic) assumptions.

As long as economists stay detached from the issues, we may not appreciate our heroism. How often do we unthinkingly assume a high degree of structural stability, with all observations assumed to be from the same structure? Hence perhaps all countries, or all states within the US, or all firms in an industry, are expected to have the same parameter values. Where differences are assumed, these are often handled using a “vector of control variables”, as if these actually control for their respective effects in the functional form applied (such as additive-separable in a multivariate linear regression).¹

Conversely, economists should be concerned at the dearth of structured assessment and the lack of reasoning to underpin some of the policy recommendations at the PHA conference. Economics, carefully applied, could make a big contribution in these areas.

Problems with a broad-brush approach were also mentioned at the NZAE conference. When discussing the NZ economic situation and its place in the world, some commented that we may be out of step or lagging behind other countries. The presumption is that we should be going with the crowd, but, as others suggested: i) if we take say 20 year intervals, we find very different views about what is desirable, and ii) if New Zealand is an outlier, is it desirable that we do the same as others?

A second area of criticism for policy recommendations for New Zealand was that analyses based on static models can only give comparative static results. In reality, significant policy issues lie in the dynamic adjustment paths and timing.

A third identified problem may be implicit in much economic and econometric thinking. There is a type of reasoning that goes: “If assumption X holds, then our analysis shows Y. We make assumption X, and therefore we have demonstrated that Y applies.” How often do we forget the conditions required for our conclusions to hold?

¹ A Google Scholar search for “vector of control variables” +economics’ on 5 July returned about 1480 hits.

And here are some brief comments on a few of the many papers presented:

Andrew Coleman's two papers (5 and 37) were each based on very simple but useful points. The first paper was about the "law of one price" which states that the difference in price between two locations cannot be more than the transport cost between the locations. He pointed out that this is true when there is surplus transport capacity between the two locations. When operating at full capacity, the supply curve is vertical and the price equals the opportunity cost of using the transport.

The second paper argued that it is not right to assume that the price difference between two locations is a measure of transport cost between the two locations. He gives the example of the New York and London prices of gold. If trade is just between the two cities, then, due to arbitrage, the price in one centre cannot exceed the price in the other by more than the cost of transporting gold from one to the other due to arbitrage. However, consider a third option of trade with Paris. Imagine it costs 10c to send gold from New York to London or Paris, and it costs 3c to send gold from London to Paris. If both London and New York sell gold to Paris, the Paris price will equal the New York Price plus 10c and the London price plus 3c. In other words, the London price will be 7c higher than the New York price, but it does not cost 7c to send gold from New York to London.

Both papers caution us that we cannot say as much as we would sometimes like from the results of our analyses. He highlights the importance of interpretation of results and the need for more thought about possible underlying structures. This is valuable as a warning against simply identifying an issue and immediately estimating a model. While he then put considerable effort into gathering data to illustrate his points, he also showed that valuable findings can come simply from careful reflection, and they do not need highly sophisticated, complex techniques. It has been claimed that, of two theorems that explain the same amount, the simpler one should be considered superior (Occam's Razor). Perhaps we should say the same about techniques.

Dorian Owen and **Clayton Weatherston** (paper 42) focused on the selection of suitable instrumental variables when assessing the impact of institutions on long-run economic performance. I followed up later with a question, if the problem is essentially statistical, why is it important to consider the specific meaning of variables chosen, rather than just their statistical characteristics? Here is Dorian's reply (thanks, Dorian):

On the point you raised about choosing instrumental variables for endogenous regressors, it's true that, for the IV method to provide consistent estimates, the instrument(s) should satisfy certain technical statistical requirements, i.e. be 'relevant' (highly correlated with the endogenous regressor) and exogenous (uncorrelated with the error term in the structural equation). On the face of it, it would seem that these statistical issues could be judged on the basis of statistical tests. By including statistical tests of both relevance and exogeneity we attempt to do that in our paper. But, perhaps because of the poor power properties of exogeneity tests, the uncertain properties of some of the tests of relevance, and not much knowledge of the effects of minor departures from exogeneity, researchers tend to bring in subjective evaluation of the plausibility of the instrument choice. These are usually focused more on the plausibility of the exogeneity assumption. This is particularly the case because variables that may very sensibly be regarded as 'exogenous' or 'predetermined' in an economic sense, such as geographical variables (changes in income per capita are not going to affect a country's latitude!), may not be quite so plausibly exogenous in the statistical sense (i.e., uncorrelated with the error term) because geographical variables, such as latitude, could plausibly affect income through lots of different mechanisms and, if these are not explicitly included in the structural model, their influence can end up in the error term and therefore correlated with the selected instrument, latitude, even though latitude is 'predetermined'. It's therefore common to try come up with explicit arguments about the nature of the variables selected as instruments and the mechanisms involved, to try to subjectively assess whether the exogeneity assumption is more or less plausible.

John Gibson et al (paper 53) compared estimates of the effects of school zoning on house prices with and without consideration of spatial autocorrelation. They found marked difference in results, suggesting that a previous study's may have markedly overestimated the

effects of zoning. They noted the publicity given to the earlier results, and we should all be aware of the significance that can be given to such research findings. They also mention that there are other amenities that, if also taken into account, are likely to further reduce the apparent effect of zoning.

We could take this to indicate several things, not least that results can depend heavily on the specification of a problem and the estimation methods used. How, using an econometric analysis of general house sales price data, are they to distinguish the clustering effect of a school and other amenities from the effect of a specific zoning requirement? Moreover, given that location decisions are made at different times but have long-term impacts, might zoning have affected the quality and amenity of various neighbourhoods? If so, would econometric models pick up the full effect of zoning? If zones are likely to change, would the effect of a zone be felt more strongly within the zone than on the boundary, and if so, might that be wrongly considered as part of the spatial autocorrelation? Are there simpler tests of the effects of zoning if it is considered, *ceteris paribus*, to have a lump sum impact on all houses? For example, if a zone boundary runs down the middle of a street, is there value in comparing prices on either side? If spatial links are to be considered, might there be other determinants only loosely related to school zones? In Palmerston North there has been emphasis placed on houses being in the hospital area or on the Massey hill, or in a particular suburb. How might such factors affect the adjustment for spatial autocorrelation?

In other words, how valuable are econometric techniques for addressing these issues? How much confidence should we place in any of these results? In terms of efficiency of research, are we making claims beyond our capabilities, and do the results justify the effort expended? It seems at times as if a fundamental question is being overlooked. Namely, does econometrics really have a valuable contribution to make to our understanding of the relationships between variables, or are the required assumptions overly restrictive?

AND NOW A FEW PHOTOS:

Grant Scobie,
NZAE president,
presiding at the
AGM





Left: Lynda Sanderson, the honours/masters category Jan Whitwell Prize winner

Below: Philip Liu, the PhD category Jan Whitwell Prize winner, receiving his prize from Frank Scrimgeour



Right: The winning poster in the inaugural NZIER post-graduate poster competition, "A Fisheries Case Study in the Galapagos Islands", by Santiago A. Bermeo Alvear



Below: Thanks to Dawn Gorman for her many years as treasurer for the Association.



Two new NZAE Distinguished Fellows

The Association made two Distinguished Fellows Awards at its 47th Annual Conference dinner on 29th June. This award is given in recognition of lifetime contributions to economics, especially those of particular significance to New Zealand.

The awards went to **Professor Peter Lloyd** of Melbourne who is Emeritus Professor of Economics at the University of Melbourne, and to **Professor John Gould** of Auckland who is Emeritus Professor of Economics at Victoria University of Wellington. Professor Gould was unable to attend, so his presentation will be made at a later date.

Professor Lloyd was born in Manaia. He studied at Victoria and Duke Universities, and has held positions at Victoria, Michigan State, the Australian National University and currently the University of Melbourne.

Already by the early 1970s his work on international trade between firms was being recognised. His aim was not theory for its own sake, but rather to make a difference in the real world through improved policy advice.

Professor Lloyd is well known in policy circles in the Asia-Pacific region. He has undertaken extensive work on Australian and New Zealand issues, ANZCERTA, the WTO, APEC and many other organizations.

Professor Gould is particularly well-known for his work on New Zealand economic history and the international experience of economic growth. Using leading edge scholarship in economic history, he was able to make significant advances in our understanding of New Zealand's experience.

His article in the 1966 *Encyclopaedia of New Zealand* remains one of the best vehicles for distinguishing romanticism from historical reality in assessing the impact of the First Labour Government and his studies of *The Rake's Progress: The New Zealand Economy Since 1945* (1982) and *The Muldoon Years* (1985) will endure as informed and judicious analyses.

These two awards bring the total number of Distinguished Fellows of the Association to ten. Past awards have been made to Professors Sir Frank Holmes, Conrad Byth, John McMillan, Peter Phillips, Gary Hawke, Lewis Evans and Doctors Brian Easton and Roderick Deane.



Peter Lloyd receives his award from Grant Scobie. Ralph Lattimore prepares to give the presentation speech.



Campbell Live of 7 June 2006 ran an item on fake news. Here are some selected extracts:

Narrator: "These days in the United States you can't always be sure the news is the news. It might be what's known as fake news."

Wayne Hope, Media Studies Lecturer, "The motive of fake news is to make corporate interest look like the public interest"

Narrator: "It tries to look and sound like journalism, but it isn't."

Narrator [re: NZ]: "Commentators say the closest thing we regularly see to fake news is adverts that try to look like the news."

In other words, it may be a problem in the US, but it is not in New Zealand. Coincidentally, this issue had arisen in two media interviews I gave in the week before Mother's Day (14 May). The first interview was with Caitlin Cherry for National Radio, broadcast just before 8am on 11 May. It was on the results of a TNS survey sponsored by floor care company Bissell looking at housework and cleaning habits of over 1000 New Zealanders. Not surprisingly, it found that couples do not always agree on housework. Caitlin Cherry's closing line in the item was, "So it seems, if you can afford it, it might be best to get a cleaner." I subsequently asked her if it was an advertising item, and she was horrified at the suggestion. "Gosh no, definitely not an advertising piece! Meant to be humourous, it was just a throwaway last line."

The second interview was with Matt Loh of the *Sunday Star-Times*. He started by saying that he was not writing an advertising piece, although he was asking for comment on the results of a TNS survey of 250 mothers and fathers on the value of mothers. It was conducted for AMP, whose media release ended by stressing the value of taking out life insurance on mothers. "...[I]t is such a cause of concern that one in three mothers has no life insurance cover and many more are underinsured. It is a potentially dangerous situation for some families." One of my comments omitted from the published article² was that there is far greater chance of loss through separation than by death. To be fair, though, it was not strongly promotional. I did notice a full page advertisement by AMP later in the same section of the paper, however. Incidentally, the caption was, "It's not easy being a mother, if it were easy, fathers would do it."

Terms that spring to mind could include engineered news, or advocacy research, but of course it is nothing like the experience in the United States, or is it? Perhaps there are other matters that are of greater concern. One could be the share of newspaper copy in local newspapers that is sourced as NZPA. Another might be the interviewers who do not have time to research their topics, but just want a quick sound bite on which to hang their own opinions. Yet another might be the heavy focus on the "human interest" angle, while failing to describe the important issues (a particular problem with social issues, perhaps in contrast to such topics as banking and finance). And a fourth concern might be the dominant view that an issue suddenly becomes "news" (even if it is research done 3 or 4 years earlier), only to be set aside a day or so later. This is hardly a sound basis for an intelligent and informed electorate.

And for another angle:

Overseas expert to push your agenda...

You want to promote a particular policy position, try bringing in an overseas expert to speak at a seminar/conference, give some media interviews and possibly meet some key MPs and public servants. As one recent example, obesity in NZ again hit the headlines in April this year, with comments from an overseas professor, Philip James³:

It was not enough to tell people to change their diet. The Government should change food pricing so that unhealthy foods were more expensive and "good" food was cheaper.

Then on 17 July we see in *The Press*⁴:

² Loh H-S M (2006) "Study: Dads don't rate mums' work", *Sunday Star Times*, 14 May, p.A4

³ Andrew K (2006) "Kiwi food causes weight gain, says expert", *The Dominion Post*, 3 April, <http://www.stuff.co.nz/stuff/0,2106,3624666a11,00.html>

⁴ Hayman K (2006) "Call to cut GST on fruit, vegies", *The Press*, 17 July, <http://www.stuff.co.nz/stuff/0,2106,3734120a7144,00.html>

“The nation's largest health board wants GST on fruit and vegetables scrapped, a fat tax on junk food, and an annual weigh-in for primary school kids.”

“The Canterbury District Health Board (CDHB) is calling for a new obesity taskforce for tough action to combat the obesity epidemic, criticising current resources as “grossly inadequate”.

It says the implementation of the Health Ministry's action plan Healthy Eating – Healthy Action (HEHA) as “fragmented and haphazard”.”

The Politics of Prevarication

How can politicians or public servants avoid acting on an issue? Jonathan Lynn and Antony Jay gave one example¹, describing:

...the traditional four-stage strategy, the standard Foreign Office response to any crisis:

Stage One: *We say that nothing is going to happen.*

Stage Two: *We say that something may be going to happen, but we should do nothing about it.*

Stage Three: *We say that maybe we should do something about it, but there's nothing we can do.*

Stage Four: *We say that maybe there was something we could have done but its too late now.*

For a New Zealand example, see the *Government Response To Law Commission Report On New Issues In Legal Parenthood*.² Discussing sperm and egg donors, it is stated that care should be taken about intervening because of the danger of unanticipated consequences:

1. Para 14 “introducing new definitions would risk creating unanticipated consequences”
2. Para 16 “Enacting an explicit presumption... would risk creating unintended consequences”

Note also Steve Maharey using a standard block earlier this year³: “A **one-size fits all** approach isn't the answer to dealing with differences in achievement between boys and girls...” This particular angle is selectively used. While Leanne Dalziel has advocated different rules for different sectors or industries (see *AI No.25*, p.4), she wants to replicate public sector initiatives in the private sector with respect to getting more women on boards⁴. She does not suggest that this might have “unanticipated consequences”, or that a one-size fits all approach is oversimplified.

¹ Lynn J and Antony Jay A (1989) *The Complete Yes Prime Minister: The Diaries of the Right Hon. James Hacker*, London: BBC Books (p.177)

² Ministry of Justice (2006), <http://www.justice.govt.nz/pubs/reports/2006/govt-response-law-commission-legal-parenthood/chapter-5.html> (for part of the report) Whole report at: <http://www.justice.govt.nz/pubs/reports/2006/govt-response-law-commission-legal-parenthood/govt-response-270206.pdf>

³ Maharey S (2006) “Government determined to lift boys' achievement”, announcement, 20 April <http://www.beehive.govt.nz/ViewDocument.aspx?DocumentID=25515>

⁴ Dalziel L (2006) “Options to get more women on boards explored”, News Release, 28 April, <http://www.beehive.govt.nz/ViewDocument.aspx?DocumentID=25580>

The Answer to Our Problems?

“Economic Man is a marvelously convenient pawn for building academic theories. But Economic Man has one fatal flaw: he does not exist ... When we turn to actual human beings, we find, instead of robot-like logic, all manner of irrational, self-sabotaging, and even altruistic behaviour ... Nonetheless, neoclassical economics sidelined such psychological insights.” Enter behavioural economics...

Lambert C (2006) “The Marketplace of Perceptions”, *Harvard Magazine*, March-April, <http://www.harvardmagazine.com/print/030640.html>

Let's get scientific by Stuart Birks

Judging by the speech by Friedrich August von Hayek when he was awarded the Nobel Prize, in 1974 economics was in some trouble.¹

The Pretence of Knowledge

*The particular occasion of this lecture, combined with the chief practical problem which economists have to face today, have made the choice of its topic almost inevitable. On the one hand the still recent establishment of the Nobel Memorial Prize in Economic Science marks a significant step in the process by which, in the opinion of the general public, economics has been conceded some of the dignity and prestige of the physical sciences. On the other hand, the economists are at this moment called upon to say how to extricate the free world from the serious threat of accelerating inflation which, it must be admitted, has been brought about by policies which the majority of economists recommended and even urged governments to pursue. **We have indeed at the moment little cause for pride: as a profession we have made a mess of things.***

*It seems to me that this failure of the economists to guide policy more successfully is closely connected with their propensity to imitate as closely as possible the procedures of the brilliantly successful physical sciences - an attempt which in our field may lead to outright error. It is an approach which has come to be described as the "scientistic" attitude - an attitude which, as I defined it some thirty years ago, "is decidedly unscientific in the true sense of the word, since it involves **a mechanical and uncritical application of habits of thought to fields different from those in which they have been formed.**"*

*... while in the physical sciences the investigator will be able to measure what, on the basis of a prima facie theory, he thinks important, **in the social sciences often that is treated as important which happens to be accessible to measurement.** This is sometimes carried to the point where it is demanded that our theories must be formulated in such terms that they refer only to measurable magnitudes.*

It can hardly be denied that such a demand quite arbitrarily limits the facts which are to be admitted as possible causes of the events which occur in the real world.

Of course, economics has moved on since then, as can be seen in health economics when considering analysis to guide health care decisions. Quoting from Haro et al²:

*Randomised clinical trials (RCTs) have long been considered the gold standard research methodology for proving the clinical efficacy, safety and quality of medical and pharmaceutical interventions. However, the limitations of RCTs are increasingly receiving attention in the literature. Because **RCTs have specific and detailed inclusion criteria and low external validity**, it has been recommended that observational studies should routinely be conducted post-RCT as a necessary complement to the experimental data.*

*... **A major strength of observational research is that it provides a means to rigorously address issues of real life effectiveness within the context of a naturalistic setting outside the restrictive experimental environment necessarily generated by clinical trial protocols.***

This is very good, but wait, there is more...

Mason et al³ "distinguish between **treatment cost-effectiveness** (the incremental costs and benefits of a treatment) and **policy cost-effectiveness** (combining treatment cost-effectiveness with the cost and magnitude of change achieved by an implementation method)." There are parallels with the concept of "diffusion" of innovation. Hence there are several questions that can be asked, such as:

- How much will it cost and how long will it take for practitioners to adopt the treatment?
- How many practitioners will adopt the treatment?

¹ <http://nobelprize.org/economics/laureates/1974/hayek-lecture.html>

² P.12 of Haro, J. M., Kontodimas, S., Negrin, M. A., Ratchiffe, M., Suarez, D., & Windmeijer, F. (2006). "Methodological Aspects in the Assessment of Treatment Effects in Observational Health Outcomes Studies", *Applied Health Economics and Health Policy*, 5(1), 11-25.

³ P.2988 of Mason J, Freemantle N, Nazareth I, Eccles M, Haines A, Drummond M. When is it cost-effective to change the behavior of health professionals? *JAMA* 2001;286(23):2988-2992

- How many patients will they see for whom the treatment is applicable?
- For how many of these will practitioners recommend the treatment?
- What take-up rate will they have?
- How effective will the treatment be for these patients?

Perhaps RCTs are to health treatments roughly what R&D is to the diffusion of innovation, just the first step in the process of getting new developments to the public.⁴

⁴ R&D ⇒ innovation ⇒ diffusion of innovation

Need a variable, just construct an index *By Stuart Birks*

There seems to have been a proliferation of indices recently. Just to hand at present I have references to a Healthy Housing Index, a Financial Liberalisation Index, an Index of Globalisation, a Control of Corruption Index, a Corruption Perceptions Index, a Health Utility Index, a Human Development Index, the Australian Unity Wellbeing Index, and two forms of the Economic Living Standards Index (ELSI). Several of these are used as variables in regression analyses, which could be problematic.

The construction of an index requires three steps: i) the constituent items have to be selected; ii) weights must be assigned to these items; and iii) values for each of the items must be determined. Unless there is a specific basis for each step, it may be possible to construct numerous indices meeting the same criteria, but giving different results.

The three steps, when applied to construct a price index, yield index values which have a clear meaning. Namely, the values give the relative cost of purchasing a specified bundle of goods and services, a bundle that has been determined to be representative of spending patterns, compared to the cost in the base year. The same cannot be said for some of the newer indices. I will illustrate with the short form of the ELSI index (ELSI_{SF}).¹

There is a manual for this index on the MSD web site.² It describes the construction of the index. It is based on questions about possession of such items as a telephone or a washing machine, activities such as visiting a hairdresser or going away for a holiday, and economizing measures, followed by respondents' self-assessment of their situation.

While the selection of items for the CPI is based on people's spending habits, it is hard to see an equivalent justification for the particular items selected for ELSI_{SF}. This is important, because we could imagine two or more alternative selections which may yield different results, but over which we would have no basis for claiming that one selection is superior to the other(s). Similarly, we could have two selections, with one containing all the items in the other, plus some more. It may be possible to change the results (in terms of people's relative scores, for example) simply by adding more items.

Telephone

- a Yes – have it
- b No – because I don't want it
- c No – because of the cost
- d No – for some other reason

All questions were given equal weights. Adding or removing questions of one type would alter their and others' relative weights in the overall index. However, the composition of the index has no specific justification to compare with the CPI's relative quantities purchased.

For the CPI, the values assigned are the prices that are observed. There is a clear basis for these values, and a precise interpretation of the results of the calculations. There is no such interpretation for an ELSI_{SF} score. For example, with the telephone question, response c scores 0, and all others score 1. For the standard of living questions (see over), a to e score from 4 down to 0.

¹ This index is discussed in more detail at: http://econ.massey.ac.nz/cppe/issues/A_Word_of_Caution_on_ELSI.pdf

² Jensen, J., Spittal, M., & Krishnan, V. (2005). *ELSI Short Form: User Manual for a Direct Measure of Living Standards*. Retrieved 21 July, 2006, from <http://www.msd.govt.nz/documents/work-areas/csre/elsi-short-form-manual.doc>

Not only are the absolute values arbitrary, but so are differences in values as we move from a to e in the second example. Why should the difference between a and b be given the same value as the difference between d and e? If we were to change these, then our index values, and possibly the ordering of values, would change.

It is therefore possible to derive indices with i) different orderings, and/or ii) different relative values while maintaining the same orderings, simply by varying arbitrary aspects of the index. However, any analyses that look for quantitative relationships between such variables and others rely on their cardinality.

A further point arose in discussion with Arthur Grimes, following a comment he made at the NZAE conference keynote address by Lucrezia Reichlin. She described an econometric analysis using an index. Arthur questioned what would happen if the variables making up the index had opposite effects and did not move together. Another way to see this point is that an index is an aggregate, and there can be problems with aggregates if the elements i) do not have the same impact on other variables, and ii) do not move together (i.e. there is not a constant “representative element of the index”). This suggests that indices can be problematic even when there is a specific statistical reason for the weightings. We should not assume that their components have identical relationships with other variables under analysis.

To summarise, we may be artificially constructing numerous variables, the interpretation of which requires great caution. We could reasonably expect some courageous research and associated political and media attention arising from the use of these variables.

Generally, how satisfied are you with your current material standard of living?

- a Very satisfied
- b Satisfied
- c Neither satisfied nor dissatisfied
- d Dissatisfied
- e Very dissatisfied

Shopping as unpaid work? [SB]

There was an interesting oblique reference to unpaid work in June on the opening of Sylvia Park, “New Zealand’s largest shopping mall”.³ The mall is making special efforts to attract men.⁴ This was reported on TV as providing a crèche for men. Apparently men and women shop differently. Men take much shorter time, and so it is felt that malls have to do something to keep them there while their women shop.

I am not one to wholeheartedly embrace gender stereotypes as universal truths, despite some apparent gender differences. However, if this is true, some of our analyses may be flawed. Unpaid work is commonly measured in terms of time expended. This is a crude measure given the different motivation to do unpaid as compared to paid work, the lack of accountability and supervision, and simultaneously undertaken activities. It is particularly crude when gender comparisons are made using time in unpaid work without consideration of the less time available on average to men after allowing for time spent on paid work. It is also probably a crude measure when compared, one for one, with time spent in paid work.

It would now seem that there may also be a further gendered inaccuracy arising from use of time. We read in the second article, “AUT associate professor of marketing Margaret Craig-Lees says it's not that men don't shop, but that they shop differently”. If they simply did not have the time for shopping, there would be no need to provide facilities for them. Presumably, therefore, the extra time women spend on shopping is an indication either that they are less efficient at shopping, or that they see shopping as both work and leisure. In either event, perhaps we are overstating women’s unpaid work contribution when we measure it on the same scale as men.

³ Gibson A and Bond G (2006) “War of malls get bigger”, *The New Zealand Herald*, 3 June, p.C1

⁴ Gibson A and Bond G (2006) “Park's creators offer attractions to lure mall-shy men”, *The New Zealand Herald*, 3 June, p. C4

http://www.nzherald.co.nz/section/story.cfm?c_id=3&ObjectID=10384821

Universal Suffrage [SB]

Maori men were the first group in New Zealand to get universal suffrage. It was granted as a result of legislation passed in 1867. It was a marked change in the criterion for suffrage, and some representatives voiced their concerns, as can be found in *New Zealand Parliamentary Debates, Second Session of the Fourth Parliament, Legislative Council and House of Representatives, First Volume*, Wellington: Government Printer, 1867.

Hon Major Richardson when moving the second reading of the Maori Representation Bill, 6th September 1867: *Objection is also raised to manhood suffrage, which is one of the provisions of this Bill, and I must acknowledge that I do not love that system; but the difficulty starts up at once, how are you to avoid it, and I may say that the promoters of the Bill do not see their way to do so.* (p.807)

Hon. Colonel Russell: *The first objection to which I shall allude, is that to which my honorable friend has already called attention, namely, direct manhood suffrage ...* (p.810)

Reporting the Hon. Mr Mantell: *The proposed manhood suffrage he also strongly objected to. They already had a franchise narrowly approaching it, but he was sorry to see the principle openly adopted ...* (p.814)

However New Zealand was not the first to take this step, as seen by a report on p.4 of *The Daily Southern Cross* for 10 October 1867 (via PapersPast, <http://paperspast.natlib.govt.nz/>). It is damning of the outcome, and includes the following, “... in the great colony of Victoria, where universal suffrage reigns, the results are just the opposite of all that Mr. Bright, for instance, has laboured for — expensive government, protected interests, and taxes enormous in amount and oppressive in incidence ...”

One for some analysis? [SB]

Reported in the *New Zealand Herald* of 3 June, a major food retailer is using its dominant position to lower the price of goods it purchases.¹

The price of a weekly food shop will go up and jobs will be threatened because of hardball tactics by the new Australian owners of Woolworths and Foodtown supermarkets, say food and beverage companies.

Suppliers say Woolworths Australia has threatened to ban their products or downgrade their position on shelves unless it gets discounts of 10 to 15 per cent.

Suppliers, who spoke on condition of anonymity, say the usual terms are around 5 per cent.

Rather than risk losing 43 per cent of the grocery market, suppliers say they accepted the demand. But many warned their margins were so tight they would have to put up prices to cover Woolworths' demands.

If Woolworths and Foodtown are able to buy products at a significantly lower price than their competitors, they would be at a marked advantage. Unless the discount reflects cost differences for suppliers (due to the higher volumes supplied), they are being forced into price discrimination. There is a real chance that the chains will be able to undercut competitors and increase their profit margins.

The Consumers' Institute comment is reported. It “welcomed Woolworths' aggressive pricing, but was concerned that brand choice could be reduced because of the company's hard line on suppliers”. This could be only part of the effect. In time there could be a reduction not only in brand choice, but also in choice of retail outlets.

However the brand choice issue merits more consideration. Much attention is given to the relationship between the number of suppliers and the nature of competition in a market. Should we also be thinking about the ability of wholesalers and retailers to control which goods and services are made available to the public and what their prices will be? Moreover, in some cases, the price received by the manufacturer is well below half the retail price of a good. If the distribution sector operates on a percentage mark-up pricing basis, how relevant are marginal cost pricing theories, and how efficient is the distribution sector?

¹ Fox A (2006) “Grocery hard line threatens food bills”, *New Zealand Herald*, 3 June, p.A3, http://www.nzherald.co.nz/section/story.cfm?c_id=1&ObjectID=10384842

What is aid for – economic development or social engineering? [SB]

Someone has drawn my attention to a recently published article entitled, “Nongovernmental Ogres? How Feminist NGOs Undermine Women in Postsocialist Eastern Europe”.² The author, Kristen Ghodsee, although a feminist, is critical of the harm done by feminism in Eastern Europe. Here are a few selected extracts:

...many women in Bulgaria reject the idea that "Bulgarian women" as a whole have unique, gender-based problems. And women's NGOs not only disregard the fundamental problems, but may actively obscure them. (P.47)

Just like the communists who tried to abolish private property by administrative decree, the international community tried to create a new "gendered" subjectivity virtually overnight by importing the "best practices" from the West. (P.50)

In the world of NGO funding, countries that have the direst "women's issues" tend to receive a larger share of the aid. Thus, it is in the interest of local women's NGOs to play up women's problems and downplay their successes. (P.51)

By focusing exclusively on patriarchy at the micro-sociological level, these Western-influenced women's NGOs and the middle-class women who often run them help create the perception of the victimized woman, and indirectly benefit from that perception. For some, the business of looking after women's issues has been lucrative. Middle-class women can make careers out of their "civil society"-building activities by emphasizing the problems women in their country face in order to secure the grants to "fix" them, despite the evidence that shows that some Bulgarian women are doing very well. In addition to the successes of women who work in particular sectors such as tourism, almost all of the classic indicators for gender discrimination in a society show no problems in Bulgaria ... Nonetheless, Bulgarian women's NGOs are forced to focus on such stock phrases as the "feminization of poverty" in order to attract external donor funding. (pp.55-6)

The irony is that women's NGOs may help to create the class divisions among women that the women's organizations then help to obscure. (P.58)

This article could be compared to a PhD thesis by Regina Scheyvens on the empowerment of women in the Solomon Islands.³ Her concern seemed to be less about economic development than social change. Hence, "*... many past development efforts aimed at women ... may have alleviated women's burdens, [but] they have not attempted to challenge the existing structures in society which have accorded women secondary status ... women need greater access to power. An approach which focuses on empowering women to help them challenge the status quo was, therefore, established as providing a good model for development agencies to follow.*" (p.ii)

It is surprising that she advocates change in pursuit of her own preferred agenda, given that she is also critical of the social impact of western intrusion, "*... societies which are economically and technologically more sophisticated than theirs undermine the importance of their culture ...*" (p.4) Moreover, she contends, "*... subtle strategies, rather than outright confrontation, proved to be most effective in catalysing change in women's lives.*" (p.ii)

Perhaps Marilyn Waring could tell us, at least with respect to New Zealand, the real objectives of our aid programme. As announced on 9 September 2004, she was given the task of reviewing NZAID. The review was intended to “check that NZAID is achieving the government’s aim of a more effective aid programme”.⁴ So what is our aid going for – economic development or (subtle?) social engineering?

² Ghodsee K (2006) “Nongovernmental Ogres? How Feminist NGOs Undermine Women in Postsocialist Eastern Europe”, *The International Journal of Not-for-Profit Law*, Vol.8(3), May, pp.44-59, http://www.icnl.org/knowledge/ijnl/vol8iss3/art_2.htm

³ Scheyvens R A (1995) *A Quiet Revolution: Strategies for the Empowerment and Development of Rural Women in the Solomon Islands*, Thesis in partial fulfilment of the requirements for the degree of Doctor of Philosophy in Development Studies at Massey University.

⁴ <http://www.beehive.govt.nz/ViewDocument.aspx?DocumentID=20869> Her report is at: <http://www.nzaid.govt.nz/library/docs/nzaid-waring-review-full-report.pdf>

CPI up 1.5% in the June quarter 2006! [SB]

On 17 July the June quarter CPI result was announced. There was an increase in the price level of 1.5%. Each quarter a figure is given, but it is just an estimate. We are never told how accurate that estimate might be. Was it really 1.5%? Might it be 1.4% or 1.6%? How confident can we be that the “right” prices have been observed?

I mention this because, out of curiosity, I conducted a small experiment at my local supermarket. Every few days over a period of 55 days, when I remembered, I noted down the price of 1kg blocks of Edam cheese at the Palmerston North Pak ‘n Save. There are five different brands on sale, although sometimes one or two brands are unavailable. Only Anchor had the same price every time. The others fluctuated (up and down) by sometimes about 20%. I also noted different prices in other supermarkets, and presumably prices vary over the country.

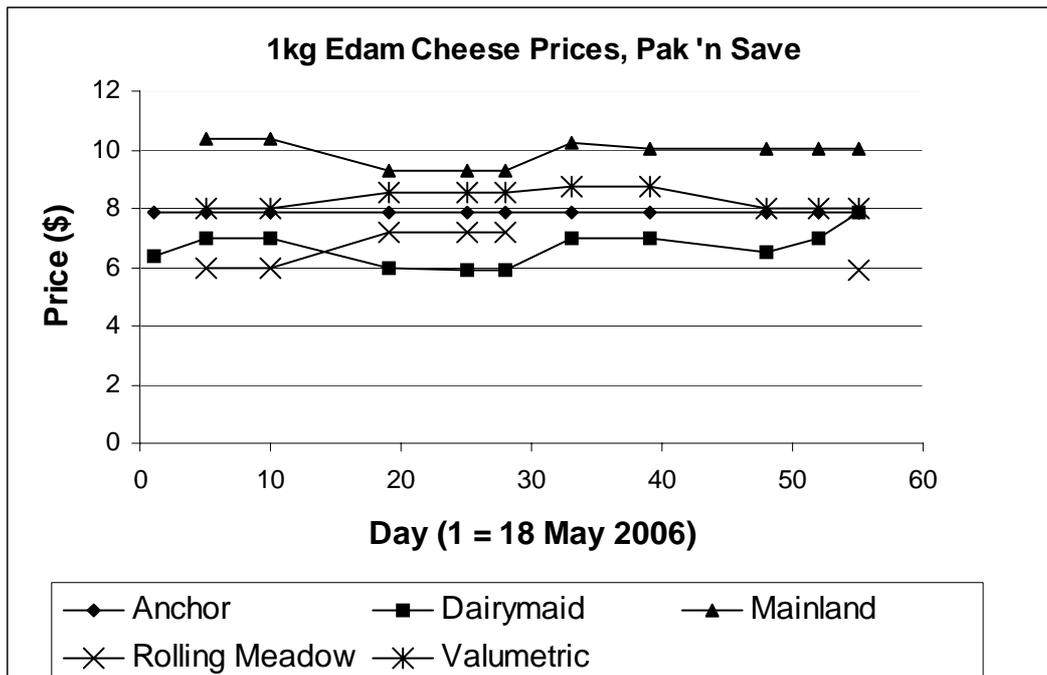
Of course, fluctuations may average out over a large number of products, but even so, the resulting indices may not reflect the true real spending power of our money. Should we be collecting data on the lowest observed price for an item? If people choose to stockpile when the price is low, over what time period should we be observing? Are

	Day	Anchor	Dairymaid	Mainland	Rolling Meadow	Valumetric
18-May	1	7.84	6.38	na	na	na
22-May	5	7.84	7	10.38	5.98	7.99
27-May	10	7.84	7	10.38	5.98	7.99
6-Jun	19	7.84	5.98	9.28	7.16	8.57
12-Jun	25	7.84	5.88	9.28	7.16	8.57
15-Jun	28	7.84	5.88	9.28	7.16	8.57
20-Jun	33	7.84	6.98	10.22	na	8.76
26-Jun	39	7.84	6.98	10.01	na	8.76
4-Jul	48	7.84	6.48	10.01	na	7.99
8-Jul	52	7.84	6.98	10.01	na	7.99
11-Jul	55	7.84	7.85	10.01	5.88	7.99

prices equally volatile at all times? Moreover, if people only buy when the price is low, fruit and vegetables are in season, or items are on special, should we have the same bundle of goods all year round, or should we have “equivalent” “seasonally adjusted” bundles of goods?

There is also one point for teachers of economics to note. Some textbooks still talk about menu costs and shoe-leather costs associated with inflation. Does this make any sense if prices are generally moving up and down all the time? To what extent might a small upward trend in the overall level of prices result in an increase in the volume and magnitude of price changes and resulting uncertainty?

Perhaps someone from Statistics NZ can explain how these issues are addressed.



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 the University of Waikato. 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 the University of Waikato as at July 2006.

Compiled by Mark Holmes (holmesmj@waikato.ac.nz)

Sayeeda Bano has a research agenda that includes *International Trade and Local Regional Development* (with Richard Money Penny). This investigation uses a combination of trade methodologies, including an extended gravity trade model, to test a number of hypotheses concerning key determinants of trade and trade in health services. *Trade Relation between Japan, New Zealand and East Asian Nations: An Application of the Gravity Trade Model* analyses New Zealand's trading relations with Japan and the East Asian nations. The strength of trade relations between these countries is examined using inter-industry and intra-industry trade intensity indices. In addition, an extended gravity model of trade is applied to estimate the extent to which Japan-East Asian and New Zealand trade can be explained in terms of "natural factors" such as population, GDP, culture, productivity and distance. Further projects include *Exchange rate volatility and trade intensity - Evidence for New Zealand* (with Mark Holmes) and *The Evolution and Determinants of India-New Zealand Bilateral Trade and Trade Potentials: An Empirical Analysis* (with Nawal Paswan).

Bridget Daldy has an interest in *Diabetes Research* (with David Simmons). She has recently joined the Te Wai Rona project that is evaluating the cost of preventing diabetes in the Maori population in the Waikato and central North Island. Current evidence suggests that approximately 40% of Maori may develop type 2 diabetes. It is therefore very important to investigate ways to reduce this incidence and hence reduce the cost implication of variety of health complications, such as heart disease, kidney failure and circulatory problems that lead to amputations. As part of her PhD research, Bridget is also investigating *Links between Computer-based Training and the New Zealand Wage Structure*.

Richard Dutu has an interest in *The Costs of Inflation in Australia and New Zealand*. This project evaluates the costs of inflation in Australia and New Zealand by looking at how inflation affects the hold-up problem between buyers and sellers and search externalities (congestion and thick market externalities). A second project is concerned with *Directed Matching, Money and Inflation* (with Benoit Julien and Ian King). This study derives the equilibrium output and money demand in a monetary model where buyers randomize over which seller to visit. It can be shown that the Friedman rule achieves the first best terms of trade, but does not satisfy the Hosios rule. Finally, Richard is working on *The Recognizability of Money* (with Ed Nosal and Guillaume Rocheteau). This study looks at how buyers can circumvent the asymmetric information problem on coins in the metallic system by signaling themselves to sellers. This investigation considers how recognizability of money impacts the velocity of money, output and welfare.

John Gibson is investigating *Health and Wealth Effects of Migration* (with David McKenzie and Steven Stillman). This Marsden-funded project uses the natural experiment provided by an immigration lottery to measure the effects of migration on income, wealth and health. The experimental estimates are also used as a benchmark for assessing more typically used econometric methods of evaluation. *Poverty mapping in China* (with Scott Rozelle,

Susan Olivia and Jikun Huang) is combining survey and census data to create finely disaggregated maps of poverty and inequality in China. The project *Savings and retirement adequacy in New Zealand* (with Grant Scobie and Trinh Le) involves working with both cross-sectional and longitudinal data to look at the likely adequacy of retirement incomes based on existing levels of wealth and patterns of saving.

Arthur Grimes (Adjunct Professor) is currently working on *Housing Market and Infrastructure Issues* with Motu. Together with Philip McCann and Jacques Poot from Waikato, Arthur and other Motu researchers have just been granted a four year FRST research grant to examine the economic impacts of major infrastructure investments across New Zealand. They will examine examples of transport infrastructure (road and rail), broadband, social infrastructure (e.g. rural hospitals), primary produce processing plants and major irrigation schemes. In the housing field, Arthur is collaborating with Mark Holmes on *An Examination of Regional Convergence of House Prices Across the UK*. This work will be extended to testing for convergence of house prices across major Australasian cities, including Auckland. Arthur also has a grant from the Centre for Housing Research Aotearoa New Zealand (CHRANZ) to examine housing supply responses across Auckland over 2000-2005. A forthcoming Motu Working Paper examines the relationship between house prices, rents and the socio-economic status of communities.

Mark Holmes (Acting Chairperson) is currently working on *Real Convergence Among EU Accession Countries* (with Ping Wang). This work involves the development and utilisation of panel data unit root and cointegration tests for convergence involving the ten countries that joined the EU in 2004. A second project is titled *Regime-switching Stationary Behaviour* (with Nabil Maghrebi). This investigation looks into the extent to which real interest differentials and the real exchange rates of G7 economies shift between regimes of stationary and non-stationary behaviour. Mark also has an interest in *Testing for Strong and Weak Ricardian Equivalence in the OECD economies*. This project considers the extent to which OECD public savings are offset by private savings. Further joint research is being undertaken with respect to *Exchange Rate Uncertainty and Trade* (with Sayeeda Bano), *Regional House Price Convergence* (with Arthur Grimes) and *Sentiment Switching and the Business Cycle* (with Brian Silverstone).

Warren Hughes is working on the project *Strategic Decisions using Probability Assessment and Bayesian Revision*. A probability assessment framework is outlined for a prototype corporate decision involving a conditioning event. The decision may, for example, involve a new-product launch (strategic decision) dependent on the outcome of market research (conditioning event). The framework illustrates how Bayesian revision could be employed as related "news" arrives intermittently to revise current probabilities prior to decision implementation. The unique contribution of this study will be the utilisation of the Analytic Hierarchy Process to ascertain a set of consistent and coherent probabilities for the event/sample spaces at all stages of the decision process.

Pamela Kaval is currently working on the following projects. *The True Ecosystem Service Value*. Currently, economists are learning that ecosystem services are important when determining the true economic value of resources. However, there is currently no specific model that has been applied. In this project, Pam is creating a new model that can be applied to value specific ecosystems. The case study in this investigation focuses on a specific wetland. *Improved Policy Interventions for Encouraging the Voluntary Use by Landowners of Practices Protecting and Enhancing Biodiversity* (with Terry Parminter). This is a four-year interdisciplinary study combining social behaviour and economic valuation applied to voluntary biodiversity corridors. *Developing a Methodology and Benefit Transfer Database to Value and Rank Projects Aimed at Protecting Indigenous Biodiversity from Exotic Pest and Disease Incursions* (with Brian Bell, Geoff Kerr, Basil Sharp and Frank Scrimgeour). This project aims to determine the value of ecosystems before and after exotic pest or disease incursions.

Bonggeun Kim has an interest in *The Accuracy of Long-term Recall Data*. In the context of non-classical measurement errors, this project assesses the reliability of retrospective recall to replace panel data. Early results suggest that retrospective recall is a poor substitute for

genuine panel data in a conventional longitudinal analysis in a linear regression model. A second project is concerned with *The Spatial Analysis of Wage and Housing Prices*. An examination of the wage gap between metropolitan and non-metropolitan areas shows that the empirical patterns of wage differentials across areas can be fully explained by a simple spatial equilibrium model that incorporates a compensating wage differential, and a dynamic tendency for more able workers to gravitate to cities. Bonggeun is also investigating *Differential Time and Money Pricing as a Mechanism for In-kind Redistribution*. This investigation considers a mechanism for public in-kind redistribution that can make the consumption of a specific good independent of income, yet increasing in relative strength of preference or need.

Steven Lim is investigating *Structural Change in the Chinese Economy: The Rise of Capital-Intensive Manufacturing* (with Jason Le Vaillant-Coats). The project considers the change in China's comparative advantage as it moves from a labour- to a more capital-intensive industrial base. A dynamic model of structural change is being developed to demonstrate how the two industrial sectors interact. Time series data on sector size will be used to test the model. *The Determinants of Aboriginal Art Prices* (with John Tressler and Andrew Webber) involves hedonic models that can accurately predict the price of a piece of art sold at Sotheby's auctions, given such characteristics as media, materials, names of artists and marketing variables. *Estimating the Socio-Economic Impacts of HIV/AIDS* (with Michael Cameron). Most studies estimating the direct and indirect costs faced by households fail to take into account broader impacts on society, including impacts on households who do not directly care for an HIV-infected individual. This paper addresses this gap in the literature.

Philip McCann is currently working on three broad themes of research in collaboration with scholars from UK, USA, Italy, Finland and Japan. One theme focuses on *The Relationship Between the Geographical Flows of Human Capital and Regional Innovation Performance*. The empirical analysis of these interrelationships takes place via choice modelling (probit and logit) and also via simultaneous equations systems. The theoretical analysis involves transactions costs frameworks. A second theme of research is on *The Determinants of the Location Behaviour of Foreign Direct Investment FDI*. Using UK data we are empirically analysing these issues via multinomial and conditional logit models. The theoretical analysis involves transactions costs frameworks. A third theme of research concerns *Geographical Knowledge Spillovers*. The empirical analysis of these issues involves cross-sectional analysis using random-effects models, and the theoretical analysis involves optimisation models.

Dan Marsh has major research interests are in economic aspects of *Biotechnology and Innovation, Water Resources, Project Appraisal and Development Assistance*. Some of Dan's recent work has focused on the description and analysis of the innovation system for biotechnology in New Zealand focusing on the major actors and the linkages among them. Dan is also involved in policy and modelling work looking at the environmental impact of agriculture in New Zealand. His research has attracted interest from Rotorua Lakes Water Quality Symposium and he has been involved in the Dairy Industry Strategy for Sustainable Environmental Management.

Ric Scarpa is working on *The Willingness to Pay for Animal Welfare in Europe* (with Giuseppe Nocella and Lionel Hubbard). This study investigates preferences for four types of meat (lamb, pork, chicken and beef) across five EU countries. Respondents are asked to answer choice-modeling questions on consumer behaviour for meat from animals bred with different animal welfare standards. We speculate on the differences across countries and use psychological constructs to enrich standard econometric analysis. A second project is *Household Theories and Choice-model Responses in Couples* (with Ian Bateman, Alistair Munro and Nesha Beharry). Theories of household behaviour make different predictions in terms of willingness to pay across members of couples. These predictions are tested in samples of responses from choice models designed for non-market valuation of environmental goods. Suitable measures of prevalence, persuasion and polarization are developed and computed from survey responses. *Finite Mixing in Count Models of Total Demand for Visits* (with Mara Thiene). In this project, the demand for total visits to outdoor

destinations can often be thought of as heterogeneous. Finite mixing of count models affords several modeling advantages. This study investigates the performance of this approach already used in marketing and health economics in data for outdoor recreation in the Alps, where evidence of finite heterogeneity has already been found in previous studies.

Frank Scrimgeour (Acting Dean) is working on a number of projects related to the economics of natural resources and the environment. Firstly there are *Projects on Conservation* (with Pam Kaval and external colleagues) that focus on optimal pest management and issues of conservation strategy. Secondly, there is the project *Pollution Control Strategies Focused on Nitrogen Pollution in the Waikato* (with Ramelan Thiagarajah). Thirdly there is ongoing research on *Energy Consumption Patterns with a Current Focus on the Impact of Higher Energy Prices on the Agricultural Sector* (with Les Oxley). *Regional Economic Analysis* is the focus of projects with both Environment Waikato and Katolyst, the regional development agency. There are several projects focused on Maori and property rights. One involves Shaun Awatere considering how Maori values are incorporated into resource management decision making. Another multi-year project (with Agresearch, Lincoln and Massey partners) involves consideration of the role of strategy, structure conduct and performance and their impact on agribusiness performance in New Zealand.

Brian Silverstone has current interests that are related mainly to the panel and firm-level analysis of the NZIER's "Quarterly Survey of Business Opinion". Current projects include *Insights into Business Confidence with Firm-Level Panel Data* (with James Mitchell) which relates the business confidence responses of firms to their other survey responses and macro variables and to determine the variables that firms associate with business confidence. The project *Capacity Utilisation, Pricing Intentions and Inflation* (with Andrew Coleman, Troy Matheson and James Mitchell) uses firm-level data to gain a better understanding of the relationship, if any, between pricing intentions and capacity utilisation. A range of questions is being addressed. For example, are prices sticky? How frequently are prices changed? Do prices fall as well as rise? Can abrupt changes in a firm's capacity utilisation and pricing intentions be explained? Finally, the investigation *Sentiment Switching and the Business Cycle* (with Mark Holmes, Waikato) uses Markov-Switching analysis to identify turning points in New Zealand's economy activity. Answers to the following questions are being sought. Does a fall in business confidence lead to the probability of a recession? Are the responses to other surveys, such as expected output, a better signal about subsequent turning points?

Anna Strutt is considering *Implications of Trade Reform for Nitrogen Pollution in OECD Countries* (with Allan Rae). This project investigates the impact of trade reform on nitrogen pollution from agricultural production in OECD countries. *Trade and Labour Migration* (with Jacques Poot and Jason Dubbeldam) will review existing work and gaps that exist in the literature in this field. *New Zealand's Agricultural Exports and Tariff Rate Quotas* (with Allan Rae) examines the impact of quota restrictions on New Zealand's agricultural trade and models the implications of reform in these markets.

Treasury Working Papers

Nine new papers released 28 July 2006

The latest working papers, policy papers and related links can be found at:

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

New Zealand Hansard

Recent coverage at: <http://www.clerk.parliament.govt.nz/hansard/Hansard.aspx>

Questions for Written Answer at:

<http://www.clerk.parliament.govt.nz/Publications/QuestionsForWrittenAnswerIndex.htm>

Hansard searchable back to 1987 at: <http://www.vdig.net/pr/hansard.html>

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: iking@business.otago.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.

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

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

Stephanie Ward (Treasury); **Rebecca Barnes** (Treasury); **Linda Sule** (Treasury); **Mark van Zijl de Jong** (Treasury); **Kevan Scott** (Treasury); **Dirk van Seventer** (Dept Of Labour); **Amy Cruickchank** (Treasury); **Craig Fookes** (Treasury); **Angus White** (Treasury); **Nicholas McNabb** (Treasury); **Martin Brown-Santirso** (Statistics NZ); **Michael Ryan** (MAF); **Nick Hallett** (Ministry Of Economic Development); **Johannah Brandson** (NZIER); **Rachel Burgess** (Dept Of Labour); **Joanna Hendy** (MOTU); **Kelly Lock** (Motu Economic & Public Policy Research); **Melanie Morten** (Motu Economic & Public Policy Research); **Yun Liang** (Motu Economic & Public Policy Research); **Reuben Irvine** (Covec Limited); **Aaron Schiff** (Covec Limited); **Fraser Colegrave** (Covec Limited); **Irene Pender** (Tairāwhiti Polytechnic); **Daryl Collins** (Treasury); **Jon Cotton** (The Dept. Of Building & Housing); **Nathaniel Robson** (Victoria University).

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