

# Asymmetric information

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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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## CONTENTS

Editorial	2
An Interview with Dennis Rose	2
Award of Life Membership	8
From the 2B RED File	9
Conference Photo's	10
'Frames'	12
(Motu) "Warm Up New Zealand: Heat Smart"	13
Fine Lines	14
Blogwatch	15
The Government Economic Network (GEN)	16
The Five Minute Interview	17
Research in Progress	18
NZEP	19
New Input Output Tables	19
NZAE Information	19



# EDITORIAL

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This issue contains the first in a series of extended interviews with New Zealand economists. An edited version of the interview of Dennis Rose, conducted by Gary Hawke, is published here. The complete interview is available in pdf form from the NZAE web site. I'd like to thank Katie Makale for carrying out the tricky task of transcribing the interview. The subject of the 'five minute interview' in the present issue of AI is Les Oxley. In acknowledging the important role played by his school teachers, Les provides a link to an obituary of one of them, Cec Thompson. I strongly recommend readers to follow the link for information about this impressive man. In addition to his usual book reviews, Grant Scobie has provided a description of one of his favourite diagrams, which comes from a joint article with Andrew Coleman. The first in the series was a two-quadrant diagram, so Grant has gone 'two better' by describing a four-quadrant diagram. Stuart Birks contributes his regular opinion piece 'Frames'. The recent NZAE conference at Palmerston North also provided two opportunities to hear Stuart's stimulating views on methodology. The contribution from Motu is an evaluation of 'Heat Smart', by Arthur Grimes. Statistics New Zealand provide a brief discussion of the most welcome new input-output tables. Paul Walker continues to report on interesting Blogs. The recent activities of the Government Economic Network (GEN) are also reviewed. This issue describes the research carried out in the School of Economics and Finance at Victoria University of Wellington. A future issue will describe the activities of the newly established Chair in Public Finance, also at Victoria University and held by Norman Gemmill. Many congratulations go to Frank Scrimgeour for being awarded Life Membership of NZAE. The citation, written by Grant Scobie, is included below. Stephen Turnovsky and Leslie Young were made Distinguished Fellows of NZAE, and their citations will be published in *New Zealand Economic Papers*.

If any readers would like to contribute occasional or regular pieces to *Asymmetric Information*, I'd be very pleased to hear from them.

# AN INTERVIEW WITH DENNIS ROSE

Gary Hawke

**Q: When did you become interested in economics?**

A: Well, I first found out about economics when I failed sufficient units in my degree to need another subject. I started economics in my third year at university.

**Q: Which university was that?**

A: Canterbury University College. In my first year I failed mathematics, one of the prerequisites for economics. In my second year, I failed English II, because of Old English requirements, which completely foxed me. So by the third year, I was looking for something else, and I started economics and I took to it from the beginning.

**(Q: The economists were presumably Weststrate, Wolfgang Rosenberg and Alan Danks?)**

A: Yes they were the three major figures for me in economics. Weststrate was pretty much institutional economics. He started with Robinson Crusoe and worked his way onwards, ...

**(Q: He was presumably writing *Types of Economies*...)**

A: He was writing the *Portrait of a Modern Mixed Economy* The *Types of Economies* came later...<sup>1</sup> He would have been working on the *Portrait* at the time. His Stage I lectures were very much focused on the institutional frameworks of economics. Wolfgang Rosenberg was lecturing on Keynesian economics at stage II, and I also did development economics under him at the Masters level. I had a warm relationship with Wolfgang...

**(Q: Yes, such a nice person...)**

A: Yes, he was one of the lecturers who frequently mixed with students, turned up at meetings and invited people to his home. Alan Danks was the principal lecturer at the Masters stage. He was very much a Marshallian, marginal analysis, and he was masterly in terms of building up supply and demand schedules and following through into particular applications.

**Q: What books did you use?**

A: Well, we had Samuelson at Stage I and Hansen's *Business Cycles and National Income* at Stage II... I'm trying to think what was our main text at Masters level...

**(Q: Did you look at Marshall's books themselves?)**

A: ... my copy of Marshall's *Principles* ... was purchased in Christchurch so we will at least have referred to it. Other books dating from my master's year are; Meade *Planning and the Price Mechanism*, Tinbergen *The Dynamics of Business Cycles*, Hicks, *Value and Capital*, Robbins *The Nature and Significance of Economic Science*, Marsh *World Trade and Investment*, and Lewis *The Theory of Economic Growth*... I was also influenced by David Fieldhouse, D.K. Fieldhouse, who was lecturing in history at stage II and offered a tutorial paper on the industrial revolution. That was an important bridge into economics because it was basically the human and social impact of the British industrial revolution. He was a great lecturer, and a wonderful tutorial taker.

**(Q: So you did an MCom?)**

A: No, I did an MA, and I left that year without doing a thesis. My NZIER motor industry study was accepted many years later as a thesis. Zyg Frankel told me that you were able to submit some other published work as a thesis, and so at this stage I did.

<sup>1</sup> Cornelis Weststrate *Portrait of a Modern Mixed Economy* (Wellington, New Zealand University Press, 1959 second edition 1966); *Types of economy : a comparative study of seven types of economic life* (Christchurch, University of Canterbury, 1963).

Members are invited to submit brief articles on any issue of interest to NZAE members, and/or comments and suggestions.

Enquiries and contributed articles should be sent to John Creedy ([john.creedy@vuw.ac.nz](mailto:john.creedy@vuw.ac.nz); [John.creedy@treasury.govt.nz](mailto:John.creedy@treasury.govt.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*

**Q: And am I right in thinking that when you started looking around, you had a choice of employers? Those were the days when graduates chose their employers.**

A: I'll tell you a story! Lisa, my late wife, was from Wellington, and up until the year between my papers and when I was going to go back and do my thesis, I'd always worked on building sites around town, and Lisa said "well, it would be better if you got a job closer to where I am, so that we could meet up". And so I said "yes okay, I will", so I went to the State Services Commission looking for vacation employment, and they said "well, there are several departments you could go to", and identified Industries & Commerce, Treasury (difficult to get into, but possible), the Reserve Bank, and Stats. And I said "which is closest?" (overlapping voices, laughing) And Stats was around on the Terrace, at the top of Mason's Lane opposite St Andrew's. And so I walked around there. At that stage I had also been contemplating looking for possible employment, and noticed somebody was advertising for a person to be doing some accounting work out in the Pacific Islands. I can't remember just what it was, but I mentioned it when I went into Stats, and the man who first saw me misunderstood what I was saying, I think. Anyway, he went off, and brought back John Kominik who was a dominant influence for several years. John was head of the National Accounts Branch, and he grabbed me as a vacation worker and set me working on an economic classification of the public accounts, to fit within the national accounting framework as a sub account. And I took to them, and at the end of the holidays, decided I'd hang in there -. And so, I worked for several years, primarily on that, but also on the annual national accounts compilation, which was the base workload for the branch – which was quite small – and also on the inter-industry studies, which were being done from there and at that stage, were at the twelve industrial sector level

**(Q: Which year was that? Was it '52 or...)**

A: No, the 1952-53 Study had been published in early 1957. I joined Stats at the end of that year coinciding with the election of a Labour government under Walter Nash, the Nordmeyer period. At that stage we were working on the on the 1954-55 Study and I did the building/construction sector within that. But the main thing was the classification of the public accounts, and that came out as the Accounts of the Government Sector, I think, from '54/5 through to about '59/60. ... John Baker was the government statistician, and a permanent member of the Official's Committee on Economic Policy, which was supported by a working party. He had difficulty staffing this working party, and somewhere, probably about my third year, he got me on some job, and then said "would you go to this meeting?" And so for several years I became the departmental representative on that interdepartmental working party, which took me up, then, to the Official's Committee and up to the Cabinet Economic Committee, and that over years, basically...

**(Q: Was that about 1960?)**

A: That's about 1960, through to '64.

**(Q: So end of the Labour government, beginning of...)**

A: End of the Labour government, yes, and particularly the Holyoake administration. John Marshall was chairman of the committee, and Holyoake was a member. Ted Greensmith would have been chair of the Official's Committee and Jack Lewin was the Industries and Commerce person there. So, yes, that became a main part of my workload at Stats. I also in about 1962 succeeded Steve Kuzmich as what they called Chief Research Officer, who had responsibility for the research and technical sections. The technical section was basically sample design work, and the research was index number construction and regression, and so on. I worked there for two years and then in '64, went to Industries and Commerce.

**(Q: Before you leave Stats... Technical stuff, were there mathematicians around at the time? Did you get involved in that?)**

A: Yes, there were two... people who were there, a Ken Steel and a Brian Steele, one of them had an 'e' at the end and I've forgotten which. Colin Gillion was there briefly, and Des O'Dea was there at some point. On the index number side, there was a man we called Bowie, Beaumont, I don't recall his given name. He had a quite severe stutter, but I really found him interesting because of his depth of knowledge and his feel for the heft of data, one way or another. I'd found this whilst preparing answers to questions asked of the Government Statistician as an expert witness at General Wage Order Hearings. I'd take something that I'd done to Bowie and he'd sit there and then he'd play the figures away around this problem, from outside the box, plug a few numbers up and connect them and see whether they seemed to come back into the same ballpark as I generated. And that was a very instructive exercise. At some point when I was in the Research Office, we had another gentleman, whose name I've forgotten, building up a dividend yield index. He was adamant that we needed to bring this forward from the base up to the present by the time consuming process of following every unit through. Steve, who was above me as an Assistant Government Statistician, thought he saw a shortcut and sent down a letter with index number formulations saying "why don't we do this?" This was the first time I'd really had to focus on index number theory so I sat down with Bowie who was, essentially, an intuitive man. I finally demonstrated to Steve's satisfaction that, no, there was no shortcut, we had to go the long way around. Bowie was relieved that I had confirmed his intuition.

**(Q: Compared with the government stats now, it does sound a bit remote, doesn't it?)**

A: It does, it does indeed. It was from there, by the way, that I did my first paper with the Economists' Association, which was on the government accounts. I think that was in 1961, I'm not sure.

**(Q: It couldn't have been the Economists' Association, as early as that. It must have been the Illustrated New Zealand...)**

A: No, I've got a copy of the paper at home, I'll find out what date was on it. Frank Holmes chaired me. On this occasion my memory serves me well, the paper is dated February 1961. In its early years the NZAE held two conferences each year. One in Wellington in February and then a mid-year residential conference at one of the university campuses, Lincoln and Massey originally. [NZAE originated in the late 1950s, some years before NZEP]

**(Q: I didn't think the Economists' Association started as early as that, because I thought it was not all that long before the beginning of the New Zealand Economic Papers, and that, I'm pretty confident, is about 1965/66.)**

A: That's about right. The first issues of NZEP were edited by Frank Holmes with Paul Hamer operating from NZIER as Business Manager. Volume 1 No. 2 is dated Autumn 1967.<sup>2</sup> ... I'm also thinking the Economists' Association was functioning at that time because Tom Shand made some derogatory remarks about Wolfgang Rosenberg and Frank, as President, agreed to convey the Association's feeling on this matter

**Q: Industries and Commerce ... what did you actually do there?**

A: Again, I was carrying forward in the interdepartmental working party world...

**(Q: Still the Cabinet Committee, I think?)**

A: Cabinet Committee, yes, but I'd changed departments. And again, that was at working party and official's committee level and occasionally at the Cabinet Committee level – less so than from Stats because Jack Lewin was normally the man who would do that. So there was that round of activity. We also did a number of other exercises. There was a question of differential freight rates on the inter-island ferry, as a possible form of assistance to South Island manufacturers. Could it be justified?..."

2 My memory was fallible. NZAE dates from 1959, quite a long time before the first issues of *NZ Economic Papers*.

**(Q: So regional developments...)**

A: Regional development was a major concern at Industries and Commerce. At some point, the Canterbury manufacturers had been arguing for lowering of freight rates, and somebody pointed out that a general lowering of freight rates would also increase the advantage of Auckland, competing into their patch, and at that point they came up with the thought of a differential. Ivan Thomas, head or deputy-head of the railways department, as it then was, publicly advocated this. It was an interesting exercise, but it was also an interesting problem because it came onto our desk, Harry Holden and myself, from the Minister without any indication as to his thinking. We went through the various options and said "if you want this in any way, then you clearly need some research." And I think that's the way the Minister went. But it was interesting to me as an example of the ... political process of identifying an issue, "is this worth doing some work on, or not?" And it's also about communication, you know, it's come down as a letter without anyone further up the department or...

**(Q: Any interdepartmental process. I mean an apology of the public service is that in the early 60s, everything was done intra-departmentally, and nobody ever consensused things until it got to the Ministers. But here, you've got a single Minister getting advice from a busy department on this issue. I mean, I think if you'd gone and talked to the Treasury, even in the early 60s, they'd have been fairly negative about the idea of, you know, differential freight rates...)**

A: Sure, and that was the nature of the battle at that time, because there was a firm tension between Industries and Commerce and the Treasury on a wide range of policy issues. I got myself burned on that inter-departmental frontier over the issue of foreign investment. ... At Industries and Commerce I was assistant economist, assistant to Harry Holden, who was the economist, and I had two branches under me. They each had about two or three staff, they were very small units. Mike Roberts, who became head of Tourism, and died on Erebus, headed the external unit and was followed by Frances Lee. Derek Homewood was in there too, at some point. So they had an ongoing work programme around various issues. ...

**(Q: Were you involved in NAFTA, at all, the New Zealand Australia Free Trade Area...?)**

A: Yes, I was involved in NAFTA, in the sense that John Marshall, the responsible minister, was interested in Peter Elkan's proposals for duty draw back. And that was worked up at working party level.

**(Q: How long did you stay at [Industries and Commerce]?)**

A: I was only there two years, so '64 through '66 ... I was enjoying the work there when one of my staff said "I suppose you'll be applying for that job at the Institute?" I said "what job at the Institute?" They were advertising for a staff member and so I went and saw Jim Rowe...

**(Q: He was the Director...)**

A: He was the Director. He must have been just appointed, yes. He was looking for an editor of Quarterly Predictions. I wasn't so keen on editing Quarterly Predictions, but I'd been involved in short-term forecasting, including balance of payments forecasting, from both Stats and Industries and Commerce. And so I went up there to do that, and started work on the motor industry at that point.

... I was interested in the motor industry as a case study of the problems of protected manufacturing development. There were obvious economies of scale which stood against operating such an industry in a small economy, but it employed a significant number of people, was long established, pre-dating tariff protection, and seemed a logical part of an industrialization strategy. ... I worked over several years on that industry, visited all the plants, we got survey responses from them, all but one, I think. And basically came up with a tariff proposal that was sensitive to the level of local content. It was predicated on the thought that government should be extending a steady level

of effective protection to that industry at a level consistent with some agreed national benchmark. The Canadian government had been developing similar kind of work, because their industry was sitting across the way, across the lake, from Detroit and required to compete with Detroit. There was a lot of work going on at that stage on measuring the effective rate of protection and on the role of protection within development policy. My paper explored tariff mechanisms that would deliver a constant level of effective protection at various levels of local content. That work was picked up by UNIDO [United Nations Industrial Development Organization], and I did a couple of jobs for them – somewhat difficult jobs, I must say – one was on low cost vehicle manufacturing in the Asian region, India, the Philippines, Indonesia ...

**(Q: Did you go from that position to the Director of the NZIER?)**

A: I went to Director after Jim left, yes. Jim did one five year term, same as Conrad had, and I did my five years...

**(Q: Was that the first you'd worked with people like J.T. Andrews and Gert Lau?)**

A: Yes, I had first encountered Jim Andrews during a period when Jim was absent from the Institute... he was up in Fiji teaching in Suva for a while. (Q: Jim Rowe?)

A: Jim Rowe, yes I was acting Director during that time – and Jim Andrews was the Chairman and we met regularly so that he could sign the cheques. He was a marvellous person

**(Q: He was certainly very keen on...)**

A: I used to go up to his house deliver the cheques and talk about whatever was happening, and he obviously took a liking to me. And I certainly regarded him as a good man. He was Chairman at the point that I was appointed. Gert Lau I'd known for longer because he used to come into Stats, collecting data - overseas investment, was a hobby horse of his – and he used to come in to get data on the balance of payments and related...

**(Q: You had a business manager there [at the Institute]?)**

A: We had a Secretary, A. J. McDonald, who managed the accounts and the office. The trustees took the main responsibility for ensuring the money was there. Gert Lau in particular, was the one who kept an eye on membership, and dealt with the perennial problem of takeovers, collapsing the number of members and their contributions – that was an issue. Other trustees were also in there. I was party at various points to discussions on finance. It was during Jim Rowe's term as Director that we first started to do some contract work, and at some point, I enunciated the principle that I thought we should be aiming for a three way revenue split, equal bundles of member contributions, contract revenue, and a government contribution. We'd had a significant government input originally, because they'd provided the house that we were in, and when we moved from the University campus, they cashed up that contribution. So they had put in a significant block of capital at that point. And I put a three-way funding proposition to the Trustees, instancing the level of state assistance to the DSIR research institutes. Henry Lang who was an ex-officio trustee, as Secretary to the Treasury – said "we'll look at this". He came back with a proposition that the Reserve Bank would make a contribution that was much smaller than a third, but would nonetheless, be a definite government sponsored contribution. So yes, I was involved in funding issues. I disliked the thought that if one relied too much on contract work the public good content of our work would be put at risk...

**(Q: What did you do when you ceased to be Director of the NZIER?)**

A: I spent five years self-employed. It was partly a rebalancing of lifestyles – to provide Lisa with an opportunity to get out into the workforce, so I was working from home and taking on responsibilities for a proportion of the cooking, and all the rest, including a more active role as a parent at Maturanga the co-operative school that my children attended. It was also in that period that I did the UNIDO jobs and also, with some time conflicts, a series of projects in the Pacific, including – the work that lead up to the South Pacific SPARTACA. I did the essential



design work on that, and pre-sold it to the Australian bureaucracy – I regard that as one of my achievements.

**(Q: Who actually were you working for? Who were you consulting for?)**

A: I was working with Ken Piddington and it was funded by the Commonwealth Secretariat. Earlier, by the way, when I was still at the Institute, I had drafted a paper for a Colombo Plan Conference on joint ventures and aid programmes. I chaired a group comprising Don Brash, Peter Ady from Oxford, Ashok Desai from the University of the South Pacific and Helen Oliver from the Institute. We were exploring the boundary between development aid programmes and commercial activity. Aid programmes tended to focus on public infrastructure, but if the aim of the intervention was to stimulate economic development you had to explore the commercial frontier.

**(Q: And you put that together with that consortium when you were a self-employed consultant?)**

A: No. That was back at the Institute. Foreign Affairs commissioned us to do that for the Colombo Plan Secretariat. So, back to the consultancy period: My work on regional issues in the Pacific Islands led in time to jobs for specific countries, including Papua New Guinea. I helped them prepare for one re-negotiation of their trade and commercial relations agreement with Australia. I also worked with the Fijian government, assisting Fred Sevele who became Prime Minister of Tonga, but was at that point an economist with the South Pacific Commission. We were working on commodity stabilisation schemes for the Fijian government. So yes, I got a raft of Pacific work – too much in fact because I was meant to be the anchor at home. That, and Lisa's wish to undertake more study precipitated my decision to seek a full-time paid job. But during that period, I also worked with the Arts Council. They had got me in originally to help them with some of their funding applications to Treasury, but that went on to a survey of arts institutions in New Zealand and a report on institutional funding policy, which I am told was dug out of the files recently.

**(Q: And then when you had to get a job back in Wellington, that's when you joined the Planning Council?)**

A: Yes Peter Rankin approached me from the Planning Council...I had presented a NZAE paper with Ken Lowen on employment policy. We were arguing that New Zealand needed to pace the process of tariff reduction in a way which did not unnecessarily damage employment. And one was hoping one could manage the transition in a way that enabled the emerging growth centres to take up the slack. So, we had a strong employment concern Peter had come to a presentation, I think the Wellington Manufacturers Association, had invited me to speak, and Peter was there, and introduced himself. Subsequently the Planning Council asked me to peer review Eric Haywood, Peter's and Bryan Philpott's first exercise around the modelling systems that were used in what became the National Sectoral Programme. So I did that, and at some point said "I'm on the market",

**(Q: Did this go back to Frank's time, or had Ian Douglas taken over as...)**

A: No, Frank was Chairman ... Graham Ansell was Director. Frank and I had had contact over a very long period and we'd always been on good terms, but we were not soulmates.

**(Q: You weren't a student of his?)**

A: I wasn't a student of his and I saw him as coming from a somewhat different philosophical position. I had worked extensively with Frank from the Institute because we regularly did work with the Monetary and Economic Council, and I used to do background pieces around the short term economic situation, but I was also involved in some others, the most important of which was the labour market report, where Frank acknowledged the contributions of Brian Brookes and myself. I think he took quiet pleasure in writing these two names into his transmittal report to Mr Muldoon. The paper explored institutional linkages in the labour market and the way in which demand pressures translated

through into the inflationary process and employment. There was one chapter, which I had drafted, which I used to quote for years afterwards as the "Monetary and Economic Council's view on this matter

**(Q: Had you worked with Bryan Philpott before?)**

A: With Bryan I go a long way back. I had known him when he was at the Meat and Wool Board's Economic Service, and I had had contacts there from Stats. We were on one job for John Baker, there was a difference between measures of dairy farmers' income as surveyed by the NZ Dairy Board and by the Stats tax based survey of dairy farms. These differences were causing problems. On that I was dealing with Stan Revell. The Producer Board people were physically very close, working in Massey House - up above Parsons bookshop. So I certainly knew Bryan at that point and had socialized with him. And then, I think it was in 1968, Bryan Philpott delivered a paper up at Waikato, a modelling paper in which he claimed in passing that agriculture was employment intensive. I asked him about capital intensity (he confirmed that agriculture was capital intensive), and managed to flip an argument that opponents had been using against the manufacturing sector for a long time. So I said "what you seem to be saying is that you've got lower rates of return per unit of labour and per unit of capital in the agricultural than in the manufacturing sector. What do you make of that?" And Bryan floundered for a while. I remember afterwards meeting Peter Elkan, who said "that was lovely Dennis, the problem is, Bryan's data's wrong, it's not true." So, I knew Bryan from back then, and at the Planning Council, of course, we had a much closer working relationship. Bryan was always enormously supportive to me ...

**(Q: And Eric Haywood, you presumably had known him from the Institute?)**

A: Yes, at that stage he was working at the Reserve Bank. When I was at the Institute we used to lunch together occasionally because I'd picked up on his indicator work at the Reserve Bank

**(Q: You were always, from the beginning concerned with the national sectoral programme?)**

A: My concern in coming to the Planning Council was basically around employment policy. I thought the situation was deteriorating...

**(Q: And which year was this?)**

A: That was 1980 or 1981. The invitation had come from the Council where Peter Rankin had got me to review the paper that Eric Haywood, he (Peter), and Bryan Philpott had put together. It was basically around forecasting the economy using Eric's little macro model, SD-Macro, linked up to Bryan's one, the Project on Economic Planning Victoria Model and its descendants. That was the beginning of that programme of linking up system dynamics modelling with Bryan Philpott's models, both the old linear programming model, Victoria, and the general equilibrium model, Julianne, developed by Adolf Stroombergen. That continued right through my period there, and indeed afterwards, up until the point where, in the 90s, from BERL, we prepared a set of labour market forecasts.

**(Q: There was one other key figure who subsequently moved into business management in the university, Dr. Bob Cavana?)**

A: Yes, Bob had written a manual on system dynamics at the University of Bradford- there were two schools, one English and one American that had developed SD modelling systems, and Bob had written a small SD manual at Bradford. He was very interested to stay engaged. So that was the core team at NSP, with Adolf Stroombergen playing a major role in developing and running the CGE general equilibrium model. And so we went through several rounds of that, gathering in data across all the sectors of the economy building up the exogenous assumptions which had to be fed into the model, running the models and then writing up the story line. That was very much around the planning of sectoral development. That had been a longstanding interest

of mine, which goes right back to Industries and Commerce days, because it was the drawing of a balance, as I saw it then, between manufacturing and other emerging sectors on the one hand, as against the natural advantage of pastoral sectors. It's always seemed to me that the chief dilemma that New Zealand has faced is trying to extend the high income status which pastoral advantage brings to the nation across an expanding population base. That implied that you had to be growing other industries, and at that stage manufacturing was very much the one that was in the forefront because it had strong advocacy out of Industries and Commerce, and in development terms it seemed natural to continue...

**(Q: How much did you pick up from the import substitution industrialization thesis from overseas? And how much was this a local development?)**

A: It came to me originally as a local development. The key figures for me were John Baker, the Government Statistician, whose *War Economy* and strong advocacy of import licensing during the period that I was in the statistics department, was predicated basically on a closed or constrained frontier economy, with high demand, stimulating growth in general and particularly in manufacturing. John Baker had his version of that. Bill Sutch had a somewhat different version and Wolfgang Rosenberg another. Indeed it was, for a time at the core of official policy making. Henry Lang had done a paper with John Baker, I used to see Henry on the working party and officials committees – and we were going through the aftermath of the Nordmeyer budget and through into the early 60s, and that inter-sectoral play was always, always there.

**(Q: And Wolfie? Do you see Wolfie as distinct?)**

A: Well, Wolfie had generated that series of books, "what everyone needs to know about". He'd taken that phrase over from Alan Danks, who had used it in a book on Social Credit. In 1965 Wolf published "*What Every New Zealander Should Know About the Effects of Import Controls and Industrialisation in New Zealand*" and followed that up in 1968 with "*A Guidebook to New Zealand's Future*". His later book, "*The Magic Square*", gets a couple of pages in the recent history of the Jewish community<sup>4</sup>, including photos of Wolf and the Magic Square (on the reverse of a photo of Karl Popper!) It was a response to Rogernomics, and it's basically talking about the need to expand production, maintain employment, and control the balance of payments and inflation....

**(Q: That must have been very late...)**

A: That's late. That's 1986...

**(Q: Because he certainly covers what everybody should know about full employment in the 60s...)**

A: In the 60s, that's right...

Wolfgang certainly had that vision of the high demand frontier constrained economy. There's no question about that. That was in his mind. As to international stuff, there was the Latin American...

**(Q: The import substitution...)**

A: The import substitution thesis. I read quite a lot of that, partly under the stimulus of Peter Elkan, who played an interesting role in all this. The Institute published his *Meaning of Protection*, for which I wrote a foreword and, at Gert Lau's suggestion, a layman's summary of the argument. Peter had always seen a dilemma at the heart of the case for protection. There was a need to, get a big enough manufacturing sector to start to pick up some of the economies of scale, but he also saw economies of scale as coming from integration with the international economy, so that was actually an argument for high levels of imports as well.

3 *The magic square : what every New Zealander should know about Rogernomics and the alternatives* / W. Rosenberg ; introduction by Jim Anderton. ( Christchurch, New Zealand Monthly Review Society, 1986. ISBN:0473003910)

4 The classic history is M.L. Goldman *History of the Jews in New Zealand* (Wellington, Reid, 1958) but I think the reference is to a more recent publication, perhaps Stephen Levine *The New Zealand Jewish Community* (Lanham, MD. Lexington, 1999). Leonard Bell and Dianna Morrow eds. "*Jewish Lives in New Zealand*", Godwit, 2012

And also, coming from Hungary, he had an extraordinary ability to feel for market-based mechanisms which were constrained in some way or another. We talked earlier about his duty drawback arrangement with Australia, which was designed to open up segments of the tariff in a way which would stimulate more or less parallel value flows, so that within the textile industry, for example, both countries would know they were not losing out to the other, but they that were benefiting from specialization. He did one on wage setting within the inflationary period, an attempt to trim back negotiated individual industry wages to an acceptable norm by some formula, which all negotiators would know was going to bite. His *New Model Economy* is full of such devices – that's what it's about. ...

**(Q: Did he keep in touch with other Hungarians? Did you ever hear him talk about Kornai *Overcentralization in economic administration*<sup>5,6</sup>...)**

A: No, I didn't. . He went back to Hungary at one point. I certainly came across Kornai but I don't recall that as coming from Peter. Kornai in fact was a quite major influence for me, his *Anti-equilibrium* ...

**(Q: Oh, go on. Because before that he wrote the *Overcentralization in economic administration*, which was published in the 56 period, in Hungary, and it was... he had to rapidly rejuvenate himself... he ended up as the chief planner in Hungary...)**

A: Yes, I always found him a very interesting writer, and I read extensively around his stuff over that period... also Prebisch and Balassa. Sutch certainly quoted Prebisch on occasion.

**(Q: Did Sutch read him?)**

A: I assume so. Whilst I was at the Institute, I wrote the *Pacific Viewpoint* article on manufacturing development that we discussed earlier. In 1970 I spoke at the AGM on '*Manufactured Exports, Import Substitution and Industrial Development*' and then in 1973 we completed a contract research unit report on *Farming and Inflation* which Rory O'Malley, Colin Gillion and I did. The last chapter of that is an attempt to encapsulate, from the farmer's perspective, the dilemmas that were flowing out from the New Zealand protected development model. So those issues had been with me long term, and one of the points of going to the Planning Council stemmed from my acknowledgment that the high demand protected economy had a limited shelf life and that we would benefit from managing the transition out as well as we could. It certainly was the core of what Peter had been doing...

**(Q: Peter Elkan?)**

A: Peter Elkan, that's right. It was at that stage, with Ken Lowen, that I'd come up with the thought that New Zealand should be trying to phase down the protective structure, at a pace that was commensurate with the green growth. Not green in the modern sense, but the growth shoots of the emergent economy. And that gave me an interest in the sectoral programme. There was always a question as to how well one could actually model what was going on and how well that modelling connected with the kind of decisions that were going to have to be made by policy makers and then by people who were actually making things. Related issues were discussed in the overseas literature on the foreign exchange constrained economy, in which the achievable level of exports was a critical parameter. The achievable level of exports determined the attainable level of imports and you wanted to use those imports in ways that would maximize domestic added value. That gave you a policy interest in the composition of imports. As we move into the 80s the idea of the foreign exchange constraint as the fundamental driving force in this was lost in the wider arguments about institutional and policy flexibility including the role of floating exchange rates. ... Coming forward to the 80s, I remember sitting at the Planning Council and Conrad Blyth, who had been up to talk to somebody in Treasury,

5 Janos Kornai *Overcentralization in economic administration : a critical analysis based on experience in Hungarian light industry* / translated by John Knapp. (London: OUP, 1959)

6 Jonas Kornai *Anti-equilibrium. On economic systems theory and the tasks of research* (Amsterdam, North-Holland Pub. Co., 1971 [1972])

coming back to me and saying “Dennis, they don’t believe there’s a foreign exchange constraint!” Conrad was shaken by this. In my recent paper on interest rates I referred back to Treasury’s judgement, in its 1984 Briefing Paper, that there isn’t a foreign exchange constraint, there is no need to worry about the balance of payments, basically on the grounds of the consenting adults argument, that you’ve got to assume these people are making appropriate trade-offs, and why would you think that that would not lead to a satisfactory outcome? I argue now that our high ratio of net international liabilities suggests that New Zealand’s external policy framework is delivering an unsatisfactory outcome, but just what it is that’s causing the problem is not so clear but it is, I think still related to the fundamental problem of developing, alongside naturally advantaged resource based sectors, others, that are foot loose, but still choose to produce in New Zealand. At the moment, I’m seeing that as partly related to the problem of exchange rate fluctuations. I know we live in a world of floating rates... I know it’s very difficult to do anything about this, but I’m hypnotized by things like the report earlier this year about the size of losses from a company, which I’m sure is operated intelligently and managing its risks as well as it can, and they’re still getting hit by tens of millions in reported exchange losses, when their net tangible assets are only about \$60 million. So, these are big events, and it means that any foot loose industry is permanently at risk, and is under a constant temptation to offshore its operations in one way or another, so that I do think that we still have an unresolved development issue in New Zealand.

**(Q: The main thing in the 60s, the first export incentives were actually incremental incentives, tied to the increase in non-traditional exports)**

A: Increase, that’s right...You started to get some silly movement above some base..).

**(Q: Yes, anybody who’d read Kornai, would know that you’d start to get people calculating how much have I increased my exports this year? Because that will be the base from which my incentives will be calculated next year. So you actually start getting game playing going on there. Muldoon actually agreed to the abolition of sectoral incentives at the time of devaluation in 1967, and his cabinet colleagues showed him the error of his ways and he then went back and told Treasury that was not what he’d ever intended, and that was absolute nonsense and they would be continuing them. Furthermore, they’d start to pay them related to total exports rather than the increase in exports. They were still tied, if I remember right, to so-called new exports, so that the pastoral schemes could get in under the NSF, as we called them in those days, the non-solid fat products, but they couldn’t get subsidies for butter and cheese and all of that, because of the mark-ups that were associated with them.)**

A: It would be interesting to revisit these issues and compare New Zealand’s experience with the import substitution ideas of Prebisch, which were based on the idea of development, on the idea that you were developing faster growing sectors which were going to become the leading sectors for the economy. It doesn’t seem to me that, even Bill Sutch really thought that manufacturing was going to overtake agriculture and become the leading sector. We were starting from where we were, building a more varied and greater range of employment opportunities alongside the efficient pastoral sector. That said, in the *Pacific Viewpoint* article, I’ve actually got manufacturing net output overtaking that of the pastoral sector by 1970.

**(Q: Ah, you do ...)**

A: But it was the dilemma of getting exports from a small industrial base.. The Prebisch type argument was informed by the examples of history, the UK, the US, Japan, Russia, had all gone through industrial, revolutions. They are all big countries that remain dominant producers for themselves as well as for export. Their theory of the stages of development could almost have

been run as a closed economy model. During the 1960s and 70s the World Bank put a lot of emphasis on export led development, originally very much around the spectacular examples of Hong Kong and Korea and, the early export breakouts from the developing world, as it then was. New Zealand’s links out to the world were so strong that manufacturers were going to have to be able to foot it internationally, apart from those who were protected by distance and closeness to their final customers

**(Q: And social policy? The other thing that the Planning Council was greatly exercised with was *From birth to death, and eventually the Royal Commission on social policy. What did you think of what was going on in those sorts of areas?*)**

A: I had an interest in those areas but I wasn’t particularly active. One early issue was equal pay, the gender and equality issue. I did a paper for an Industrial Relations Centre seminar on equal pay, back in 1970. The Labour Department had estimated what the cost of equal pay would be – by simply saying “well, if women are paid the same average rate as men, then it will go up by this amount”, and that gave them a pretty big number. I was concerned to take account of influences such as education attainments, length of career service, and so on. These implied that even if you got equality of rate job for job, you were going to get an average female rate that was actually below the average male rate, I was putting the difference at about 80, which turned out to be fairly accurate, but that was a major issue at that time. On redistributive policy, I was interested, but never got particularly involved. I thought full employment was the thing that you went for. To me that was the prime interest area, so that I didn’t put in a lot of work on the ground that was being covered in the Royal Commission on social policy.

**(Q: The Frank Castles thesis? The welfare workers, welfare state, did that really come to your attention much? Castles argued Australia and New Zealand were different in that we’d built our social security system on the basis of the court of arbitration rather than on the Inland Revenue Department. That accounts for quite a number of things – flat rates instead of income related, social security being the most obvious one.)**

A: No, not a lot. As I mentioned earlier, John Baker used to give evidence to the Court of Arbitration, which played a key role in determining income shares in the frontier constrained economy. ...

**(Q: Do you actually look back on the 80s as a period in which thinking actually changed? Or was it just that the outcome of familiar ideas changed with different people?)**

A: No, I think it evolved. Thinking changed a lot. We saw the breakdown of a collection of ideas which I still see as Keynesian, in terms of our understanding of how the economy worked, and the breakdown of the post-war consensus. It was partly around what governments can do. John Baker’s *War Economy* is a very interesting read. Government was acting... basically playing a part in an international conflict of enormous proportions, it dominated everything. For a period of several years the government was, perforce, heavily involved on front after front, and by and large, it was pretty successful. That style of management persisted through into the 50s and 60s – the government was delivering full employment, it had taken that as part of its role and it was carrying forward doing things that were necessary, as it saw them. But the stresses and strains that developed were calling that into question, over a wide spectrum – I remember a conversation with Shirley Smith. She was saying “Denny, the longer I live, the less things I think a government can do”, which was really quite surprising coming from her, an admission that her faith in the ability of government to call the right shots was diminishing. And that was part of a much more general phenomenon. Rational expectations and the more general argument that in a basically atomistic economy the individual actors are making judgement calls in the light of what’s relevant to them. For governments to try and do better than that, you have to justify why something else



has to be done. And that's a fundamentally different perspective from where we had been, which started from a presumption that there were things that government was meant to be doing...

**(Q: And we all agreed on them...)**

A: We all agreed on them...

**(Q: And governments could act on them...)**

A: This was heading back towards the night-watchman state, with a set of minimum functions for the government. Now we never got there, but some people were strongly influenced by that ideal, and the policy fraternity in general was strongly influenced by the thought that you could usefully get to a much less regulated environment. ...

**(Q: Was there anything unique about New Zealand, do you think?)**

A: It was possibly unique in the speed with which we went for it under Rogernomics.. It was picked up and run pretty much to the hilt, it seems to me, so I would say yes, there was...

**(Q: It was a bit of a response to Muldoon... the swinging of the pendulum after the...)**

A: Yes.... I remember Rod Deane talking to the Economists' Association on that process, he was strongly supportive of the speed with which they were going, and reporting that Roger Douglas was a strong proponent of speed as the precondition of getting through before coalitions formed against you..

**(Q: Your father was a Labour candidate in Ashburton in 46, 49. Am I right, in thinking I remember you as a fellow member of Socialist Forum...It was run by Conrad Bollinger with Hec McNeil and others and we used to meet in Conrad's house?)**

**(Q: And, of course, I do remember you in the Vietnam years. When I was in the UK, you were still around, and you were particularly involved in the Peace Power and Politics Conference with Tony Ashendon and Co. in the year 67, 68 was it?)**

A: Okay, ... I went through university never linking up with the Socialist club, as I think it was called. Towards the end of my time at Canterbury it morphed into the 'Radical Club' and I was

associated with that during my last year at Canterbury, but it was pretty moribund at that point.

**(Q: And you mentioned Winston Rhodes and Lawrence Baigent... they would have been...)**

A: Yes... I'd become very involved in the nuclear disarmament issue at that stage. ...

**(Q: I remember Hector McNeil.)**

A: Hector McNeil, yeah.

**(Q: And Nigel Taylor**

A: Hector also introduced me to the New Zealand Council for Civil Liberties, where I acted as chairman for quite a few years with some very stimulating associates including Walter Scott and Shirley Smith. Those left leaning associations stimulated my interest in what was going on in our own economy, but also internationally, including the developing world and the East-European economies. The interest is always in people who are trying to get an appropriate resolution between market relations and the stream of social and political objectives that have to be mediated from the centre. So, for example I took an interest Branko Horvat's *'The Political Economy of Socialism'*, a Yugoslav economist who wrote on "actually existing socialism" advocating the decentralisation of power and decision making. Well functioning societies depend upon their critics

**(Q: There's something there about the interest in economics and the interest in socialism, isn't there, that links all the market socialists in a way?)**

A: Yes, that's right, but an interest in the problems under review should not be confined to socialists. I've never adopted that as a working label for myself, although I share many of those ideals. Accepting that the economy that I work in is essentially capitalist and is, to some degree open for change, for better or worse, the challenge is to identify issues on which I can make a difference. Right across the political spectrum and in every type of social system the balance has to be struck between the atomistic, usually market moderated, system that gives us our daily bread and the need for central coordination and decision in pursuit of collective goals.

## AWARD OF LIFE MEMBERSHIP TO FRANCIS (FRANK) SCRIMGEOUR

It is with great pleasure that the Association honours Frank Scrimgeour with the award of Life Membership of the New Zealand Association of Economists.

From his farming origins in Golden Bay, Frank commenced his academic career at Lincoln University where he gained First Class Honours and was awarded the Sir Malcolm Burns Prize for outstanding student contributions to Lincoln College. This dedication to wider communities was to become a hallmark of Frank's subsequent career. He went on to complete a PhD at the University of Hawaii. Many people may not know he also holds a Bachelor of Divinity from the Melbourne College of Divinity.

His professional career began at the Meat and Wool Boards' Economic Service, but this was soon followed by over five years in development work with the Christian Leaders' Training College in Mt Hagen, Papua New Guinea.

Frank has spent more than two decades at the University of Waikato, first as an active member of the Economics Department, then Chair of several departments and finally as current Dean of the Waikato Management School. In addition to a heavy administrative load, he has maintained his highly productive career as an economist publishing

widely in international journals and generating an extensive number of research papers, conference proceedings and consulting reports.

In making this award we wish to honour Frank for his service to the profession, the academic community, the wider New Zealand community and the Association, in particular. His contribution to all of these groups has been outstanding.

Notably Frank has:

1. Provided numerous acts of high quality service to the Association. He has frequently refereed journal articles of New Zealand Economic Papers, and he has undertaken many functions on behalf of the Association.
2. Played a major role in the leadership of the Association serving as a Councillor (1998-2005), Editor (1998-2001), Vice President (2005-2007) and President 2007-2009). In addition he served as President of the New Zealand Agricultural Economics Society (1993-94 and 2004-05) and as a Councillor of the Australian Agricultural and Resource Economics Society (1992 and 2003-05).
3. Chaired the largest economics gathering ever held in New Zealand - the 2008 NZAE/ESAM Conference in honour of AW Phillips
4. Contributed to the broader community through his church, and as a member of the Trust Board of World Vision.

In all these endeavours he has shown genuine human understanding, concern for the wellbeing of others, always tempered with a quiet sense of humility.

The Association honours Frank for his broad economic citizenship and has pleasure in awarding him Life Membership of the Association.



# FROM THE 2B RED FILE

by Grant M. Scobie

(grant.scobie@treasury.govt.nz)

As a social commentator, political scientist and policy analyst, **Charles Murray** has never shrunk from plain language, and has seemingly revelled in the “notoriety.” His earlier work (Losing Ground” arguably contributed to a rethinking of the US welfare system. His latest work **Coming Apart: The State of White America, 1960-2010** ( New York: Crown Forum, 2012) is no exception. The stated objective is “to induce recognition of the ways in which America is coming apart at the seams- not seams of race or ethnicity, but of class.” Murray draws on a fascinating array of social statistics to argue a version of the “rich got richer while the poor got poorer.”

He paints a vivid picture of the dichotomy between the upper classes in their gated communities who are isolated from the erosion of family and community values that characterise the lower (white) classes. Clearly spatial segregation is one indicator, and the author makes intriguing use of zip codes to identify the pockets of privilege (the Superzips) in contrast to Fishtown, PA which typifies a declining white lower class community with the usual litany of ills from high unemployment, teenage pregnancy, vandalism –in short, a Putmanesque loss of social capital. Overall it is a readable, well documented and referenced account of a major chasm in American society that has developed in the last half century – full of intriguing social statistics, although a bit light on the “where to now and so whats”. Shades of Remuera and Patea?

Could Adam Smith have possibly been wrong? Surely the “invisible hand” was a ground-breaking insight that has become a pillar of modern economics. The butcher, baker and candlestick maker all pursue their grubby self-interests – but wait – in so doing we are all better off (whether it is new products, lower prices, open on Saturdays, etc). End of story. But now enter stage right: **Robert H. Frank (2011) The Darwin Economy: Liberty, Competition, and the Common Good** (Princeton, NJ: Princeton University Press).

Frank’s thesis is that competition is typically a good thing (beats the alternative?). But it can be wasteful and inefficient (a theme promoted by those favouring state monopolies; eg ACC!) Being a very large elephant bull seal is good for the individual seal especially if, as a consequence, they win the mating rights to the harem; but it is not necessarily good for the group (“prodigious size is a clear handicap for bulls as a group, making them far more vulnerable to sharks and other predators” p.8). Every bull seal would vote in favour of a proposal to reduce their bulk by one half; it is relative size that matters.

In contrast to the good Glaswegian professor, Darwin recognised that in the process of competition, the interests of individual animals “were often profoundly in conflict with the broader interests of their own species” (p.17). This leads Frank to conclude that eventually, Smith will be seen as a special case of Darwin.

Finally for this edition of **2BRED**, I persuaded **Gırol Karacaoglu**, the recently appointed Deputy Secretary (Macroeconomics) and Chief Economist for the Treasury to be a guest columnist. Here is his review of **Daron Acemoglu and James A. Robinson (2012) Why Nations Fail: the origins of power, prosperity, and poverty** (New York: Crown Publishers).

What is the fundamental explanation for differences in the prosperity of nations around the world? Why are some poor and others rich? Traditional explanations centre on three big themes: nature, culture, ignorance.

Based on a careful study of evidence across time and geographies, Acemoglu and Robinson systematically dismiss all three explanations, as general explanations of differences in the prosperity of nations. They propose, and carefully support, instead an alternative explanation based on the economic and political institutions adopted by different countries.

We know that saving, education, capital accumulation and technological innovation are among the critical factors that are associated with high rates of economic growth. However, these are the symptoms of economic growth – they are growth. They are not the causes of growth. Why do some countries develop or adopt these key ingredients of growth in abundance while others are starved of them?

The central thesis of the book is that economic prosperity is associated with “inclusive” economic and political institutions, while “extractive” institutions typically lead to stagnation and poverty.

Inclusive (or good) economic institutions tend to be free (as distinct from unregulated)-market-supporting institutions that enable, allow, encourage and incentivise participation by the great mass of people in economic activities that make best use of their talents and skills, invest and innovate, make the choices they wish, and freely contract and exchange; that secure private property rights, and provide a level playing field, as well as an unbiased system of law; and that encourage a process of ongoing “creative destruction”.

All of the above ingredients, including critical public services and economic infrastructure, rely heavily on the state. Since all economic institutions are created by society, why don’t we all choose good economic institutions? Why do different countries end up with different kinds of economic institutions?

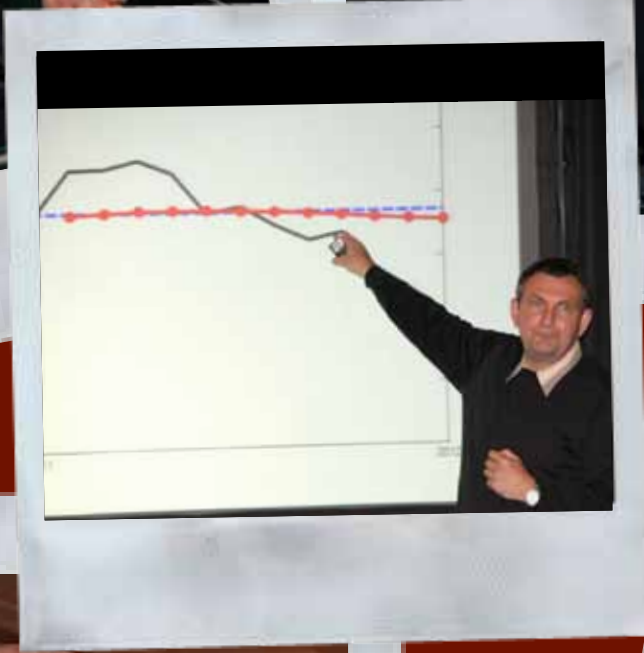
Ultimately the answer lies in politics – in the structure of political power and influence. The economics and politics of poverty and prosperity are inextricably linked. Economic institutions do not only fundamentally determine the size of the aggregate pie; but they also determine how this pie is divided among different groups and individuals. Bad institutions arise when the groups with political power and influence benefit from bad institutions. And it is very difficult to change bad (extractive) political institutions that exploit economic resources for the benefit of the few, because such change redistributes economic opportunities from the few to the many.

Why do some countries end up with good political and economic institutions that persist, while others end up with bad ones? The answer generally lies in a mix of history and critical historical turning points.

## Any lessons for New Zealand?

We are blessed with great economic and political institutions, that reflect our history. We inherited some of the fruits of the industrial revolution, as well as inclusive political institutions, through the immigrants; there was not much to extract and take away from NZ; and it was in the interest of all concerned to build and maintain an inclusive political and economic system. That explains why, according to Acemoglu and Robinson, New Zealanders have been, and remain, among the richest people in the world.

We can protect, and build on, that legacy, by protecting our inclusive political and economic institutions, and building on this platform by constantly improving the capabilities, opportunities and incentives of all New Zealanders to participate in economic life productively.



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# “FRAMES”

by *Stuart Birks*, [k.s.birks@massey.ac.nz](mailto:k.s.birks@massey.ac.nz)

## Reservations, qualifications and adjustments

In my last column I mentioned Keynes's advice on reservations, qualifications and adjustments to be added to formal analyses when they are used to assist in real world situations. This is important advice.

Theoretical representations and results of empirical analyses are not precise descriptions of the real world. This applies to both mainstream and alternative economics approaches, and in fact to any analysis, whatever the discipline. They all involve framing, with its selection, emphasis, exclusion and elaboration.

Consider perfect competition as an example. I shall briefly outline just a few of the considerations that could be added. This is not a criticism of mainstream economics. It should be viewed as recognition of the inevitable limitations that arise from the application of any analytical structure.

Mainstream economic analyses rely on the concept of perfect competition as a basis for evaluative criteria. Market failure is identified in comparison to this “ideal”. Economists could ask whether perfect competition is the right “ideal”.

It is considered an ideal because a perfectly competitive economy is Pareto Optimal (an issue in itself). Sen (1977) contends this result was derived as an intellectual exercise. The aim was to see if there were assumptions under which individuals acting according to their self-interest could produce a “best” outcome for society. It was not an attempt to describe the world we live in. Nevertheless, it has come to be seen paradoxically as both an ideal and a representation of the real world, how people should behave and how they do behave.

It may have serendipitously become the ideal to use, but there are many grounds for discomfort. Here are a few.

The finding is based on static analysis. Consequently the points of interest are equilibria or optima. Little can be said about paths and timing of adjustment to or between these points. There are numerous possibilities, including path dependence such that a particular equilibrium or optimum may not be attainable, or lags in adjustment could be unacceptably long. In addition, an ideal path over time may not equate to a series of static equilibria. Disequilibrium positions in economics indicate that some plans are not realised, in which case people have incentives to change their behaviour. These changes may be desirable when seen from a longer perspective.

Static analysis can also be considered as starting from a blank sheet of paper. While initial conditions affect the equilibrium outcome, they may not incorporate complex psychological and behavioural influences of past events and experiences. Some of these dimensions are considered in historical institutionalism.

Common criticisms of mainstream economics include the assumptions of rationality and exogenous preferences. Lawson (2003) stresses these and other concerns with his concepts of atomism and closed systems with event regularities. Each of these assumes away phenomena which might be considered important in the real world. Rationality is commonly defined within a narrow theoretical structure. Other behaviour could be considered rational once additional aspects are included. Alternatively, behaviour may be influenced by instinctive or subconscious factors, or heuristics. Exogenous preferences ignore the context in which people make decisions, including social, cultural and group influences on perceptions and behaviour. Atomism, with individuals acting independently and in isolation, rules out many of

these aspects. Closed systems also exclude outside influences. Event regularities allow for prediction, but may be unrealistic given the behavioural dimension and learning from experience observed with humans.

Standard optimal conditions are based on marginalism, with opportunities to substitute one good or input for another continuously as relative prices change. This assumption cannot hold if there are indivisibilities in inputs or outputs, or a finite number of production technologies and capital-labour ratios. Marginalism in the form of marginal cost pricing may not be realistic, even if possible, given the chain of distribution and the associated use of percentage mark-ups.

Another puzzling aspect is the view of markets operating on their own, with politics and government seen as distinct rather than integral components in a wider system. One reason given for governments in New Zealand stepping back in the post-1984 period was that businesses had been concentrating their energies on lobbying for favours rather than improving competitiveness in markets. Governments have the means to affect economic activity and are major economic actors themselves.

Economic ideas are also the result of a production process, with dominant thinking being shaped by economic, political and social forces (and not just by rational agents in a market place for ideas). Points such as these have often been made, but have yet to achieve sufficient traction to impact on mainstream perspectives.

Campbell (1998) writes of the restrictive nature of ideas: “The key insight of historical institutionalism is its theory of constraint, that is, its explanation of how ideas and institutions limit the range of possible solutions that policy makers are likely to consider when trying to resolve policy problems.” (p.378)

Ekstedt and Fusari (2010) consider people's changing perceptions and behaviour: “Social reality is much more highly subject than nature to non-repetitive change as a consequence of the steadily increasing constructive, creative, innovative action of human beings.” (p.11) and “the pace of social change makes the principle of falsification totally unreliable, practically meaningless, in social enquiry.” (p.13)

And Hodgson (2001) considers resilience in the face of an uncertain future, describing: “W. Ross Ashby's 'law of requisite variety'. This is the idea that a system has to contain sufficient variety to deal with all the potential variation in its environment.” (p.334)

If receptive to such challenges, economics faces an exciting future.

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## “WARM UP NEW ZEALAND: HEAT SMART” EVALUATION

Arthur Grimes

Evaluation results of central government's Warm Up New Zealand: Heat Smart (WUNZ:HS) programme have recently been published.<sup>1</sup> The programme, which started in 2009, provided co-funding for retrofitting insulation and clean heating to houses built prior to 2000. The principal purposes of the scheme were to improve energy efficiency and to improve health outcomes; employment benefits were also mooted given that the scheme was begun during the recession.

Approximately 100,000 houses were treated with insulation in the first two years of the programme, and 24,000 houses received clean heat treatment (some of which also received insulation). A further 78,000 were targeted to receive insulation treatment over the next two years, with an extra 37,000 clean heat treatments. Total fiscal cost over the four years was projected at around \$320 million.

By any scale, this is a large public policy intervention. What were its effects on energy, health and other outcomes? What were its total costs? Did the benefits outweigh the costs?

These questions were addressed in an evaluation of the scheme involving researchers from Motu, University of Otago (UoO), Covic and Victoria University of Wellington. Professor Philippa Howden-Chapman (UoO), who had pioneered research into insulation and clean heat treatment in New Zealand, was a member of the research team. Previously, she and colleagues had conducted randomised community trials of insulation and clean heating interventions in different areas of New Zealand. Randomisation in her trials involved the timing of the receipt of treatment. All participants had to agree to provide relevant records for evaluation purposes. By the end of each programme, all participants received treatment.

These studies showed significant beneficial impacts of insulation treatment on energy use and health outcomes, and benefits from clean heating. However, the number of treated houses in some of these studies made it difficult to obtain statistically significant results in some areas with relatively rare outcomes, such as hospitalisation rates; and treatments were mostly targeted towards at-risk groups (e.g. those with respiratory conditions such as asthma) raising issues about the generalisability of the results to the general population.

The WUNZ:HS programme – with its target of treating almost 200,000 houses and its universalist approach (all households were eligible for subsidies, with community services card (CSC) holders eligible for a greater percentage contribution to costs) – offered an ideal setting to test the impacts of insulation and clean heat treatment in a much larger setting, enabling more statistical precision.

However, the programme was announced as a first-come-first-served scheme with no evaluation element initially built into the scheme. The only information that subsidy recipients had to provide was data directly related to the treatment, plus their CSC status.

Installers provided details to EECA on the insulation and clean heating installed. Thus there were no health or energy data available to assist evaluation, and no control houses against which to compare the treated houses.

Faced with this situation, the researchers chose the first 46,655 houses to be treated (those treated to May 2010). Quotable Value New Zealand matched control houses to each treated house according to a list of requirements (e.g. treated and control houses had to be: in the same census area unit, built in the same decade, of the same type, constructed of the same materials, and have the same number of floors and bedrooms). Suitable control houses were obtained for 67 per cent of treated houses; of these, between 1 and 10 control houses were obtained for each treated house.

Researchers obtained metered monthly energy records from four energy companies (Mercury Energy, Meridian, Genesis and Trustpower) which they matched to treated and control houses on a confidentialised basis. Energy records provided coverage of energy use both before and after treatment; records were obtained for approximately half of the matched houses.

Similarly, health and pharmaceutical records were obtained on a confidentialised basis from the Ministry of Health and Pharmac. The information included pharmaceutical use, hospital admissions (decomposed into admission type), and cost of treatment. Health records were obtained for 87 per cent of matched houses.

Researchers ran a difference in difference regression for each set of data. For energy, the monthly data enabled researchers to interact treatment effects with external temperature to gauge impacts in different parts of the country and in different seasons. The health study paid particular attention to differences in health outcomes according to socio-economic (CSC) status and according to whether prior hospitalisation for a condition had taken place.

The energy study showed that insulation treatment caused a statistically significant, but small (0.7-1.0 per cent) fall in metered energy consumption. The small drop in energy use is consistent with an economic model in which energy efficiencies were obtained from the insulation so that the effective price of heating fell, in turn resulting in increased consumption of heat (that is, a warmer house). Greatest energy savings were experienced in cool areas. Measured energy use was shown to increase slightly with the installation of clean heat installation (no data were available on non-metered energy use).

Consistent with having warmer houses, health outcomes improved. Small impacts were detected for pharmaceutical and hospitalisation costs, with greater effects for CSC holders. The size of the study meant that, for the first time, significant mortality effects were detected; mortality was lowered for those who had previously been hospitalised with circulatory illness. No discernible health impact was detected from clean heat installation (although all these houses had insulation).

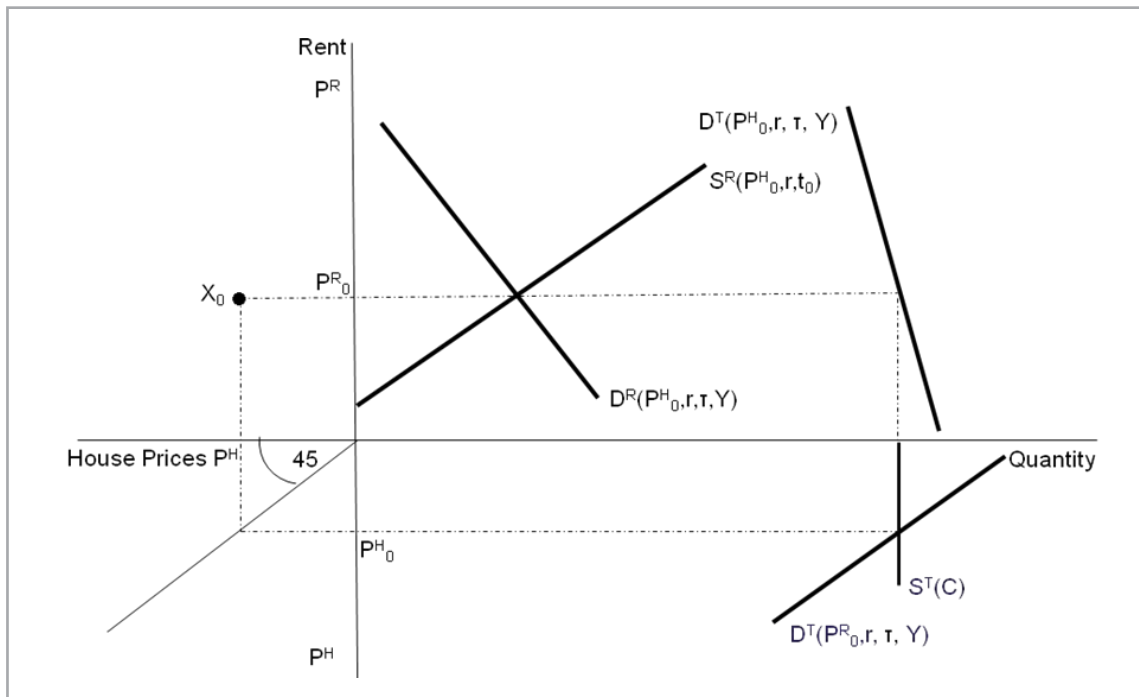
The evaluation also included analysis of the effects of WUNZ:HS on employment and industry. Small benefits were detected on these fronts.

The researchers estimated that 74 per cent of the installations were “additional”, that is, installations that would not have taken place in the absence of the scheme. Using this estimate of additionality, combining the health, energy and industry benefits, and combining the direct and indirect programme costs (including costs of raising taxation), the study found an overall benefit:cost ratio of 3.9 for the programme and a net present value of close to \$1 billion. The largest of the benefits (71 per cent of the total) came from the reduction in mortality – a benefit that had not hitherto been quantified and which had not been at the heart of the mooted benefits of the programme.

<sup>1</sup> See: [http://www.motu.org.nz/news-media/detail/reports\\_on\\_warm\\_up\\_new\\_zealand\\_heat\\_smart\\_now\\_available](http://www.motu.org.nz/news-media/detail/reports_on_warm_up_new_zealand_heat_smart_now_available).

# FINE LINES: A FAVOURITE DIAGRAM

by Grant Scobie



This is a four quadrant diagram of the housing market, where the four variables of interest are the price of houses,  $P^H$ , rents  $P^R$ , the quantity of rental houses,  $Q^R$ , and the total quantity of houses,  $Q^T$ . All houses are assumed to be identical, after standardising by an adjustment for quality, floor area and so on. The north-east quadrant depicts the supply of rental housing ( $S^R$ ) and the demand for rental housing ( $D^R$ ) as functions of the rent. Both these relationships are drawn for an initial price of houses (denoted  $P^{H_0}$ ). A change in the price of houses shifts the demand and supply of rental housing. In addition, the supply function for rental housing has as arguments the real interest rate ( $r$ ) and taxes on rental income ( $t$ ). The demand for rental property is shifted by the real interest rate, real incomes ( $Y$ ) and a variable to capture the effect of subsidies to owner occupancy ( $\tau$ ).

The rental demand curve ( $D^R$ ) is downward sloping because: a rise in rents encourages renters to economise on rental space by having more individuals share a dwelling (an “intensification effect”); higher rents slow the rate at which new households form and enter the rental market (a “formation effect”); as rents rise for a given price of houses, some existing renters choose to become home owners (a “substitution effect”). The intersection of the supply and demand curves for rental housing determines the market clearing rent (denoted  $P^{R_0}$ ), and the quantity of rental housing ( $Q^R$ ).

The demand curve  $D^T$  in the north east quadrant represents the total demand for housing. It traces the demand as rent varies for a fixed level of house prices and is steeper than the rental demand curve to reflect the way that substitution between renting and ownership is netted out at the level of total housing demand.

The south-east quadrant shows the supply of housing,  $S^T(C)$ , as a function of the unit cost of a house,  $C$ . This is shown here as being fixed (vertical at a given quantity), but in general supply is an increasing function of  $C$ . The south-east quadrant also displays the downward sloping demand for housing, where each point on the curve corresponds to the level of total demand ( $D^T$ ) when the rental market (in the north-east quadrant) is in equilibrium.

The initial equilibrium position in the housing market occurs at a price that equates the supply and demand for housing in the south-east quadrant. When the three curves in the north-east quadrant are drawn incorporating this housing price, the equilibrium rent is shown ( $P^{R_0}$ ). In the north-west quadrant the intersection point marked  $X_0$  corresponds to the equilibrium values of the house price ( $P^{H_0}$ ) and the rental price  $P^{R_0}$ .

The real value of a graphical model is to help ensure internal consistency when a number of changes are involved – too many to keep straight in one’s head! Suppose a tax is imposed on investors in rental housing. The initial impact is to shift the rental supply curve upward in the north-east quadrant. With a fixed stock of housing, reduced demand for housing results in a fall in house prices. This shifts the demand for rental housing down since ownership is more attractive than renting. Furthermore, the ‘post tax’ rental supply curve shifts to the right (after an initial upward shift). The change in rents leads to an inward shift of the rental demand curve in the SE quadrant. At the same time the total demand for housing shifts to the right. The new equilibrium leads, by tracing round the four quadrants, to a new  $X$  point in the top left hand quadrant that is north-east of the initial position. At this point the house prices are lower and rents higher than prior to the policy change. Other policies may well result in different changes to the two equilibrium prices and would therefore trace out a different sequence of  $X$  values. The analyses can easily be extended to the case where the stock of housing can adjust in the longer run.

Of course in practice, the challenge is to quantify those effects – but that is for another day.

For further details of this diagram, see Andrew Coleman and Grant Scobie (2009) “A Simple Model of Housing Rental and Ownership with Policy Simulations.” New Zealand Treasury Working Paper WP 09/05.



# BLOGWATCH

by Paul Walker ([paul.walker@canterbury.ac.nz](mailto:paul.walker@canterbury.ac.nz))

To start our look at the blogging universe we go to the “Becker-Posner Blog” <http://www.becker-posner-blog.com/> which recently wrote about New York Mayor Michael Bloomberg’s proposal to ban sugary drinks larger than 16 ounces from restaurants, street carts, movie theatres and stadiums. Becker concludes, “[...] even when consumer decisions are not in their self-interest, it is questionable whether that provides sufficient grounding for government efforts to regulate and tax these decisions” <http://www.becker-posner-blog.com/2012/06/controls-over-consumer-choices-becker.html>. Posner, on the other hand, writes that “I agree with Becker that one must be hesitant to recommend governmental intervention in personal choice. Government lacks good information about consumer preferences in a country as vast and diverse as the United States, and government is buffeted by interest groups. But the case for some government intervention in the obesity epidemic (and it is an epidemic—obesity begets obesity, as I’ll suggest) seems to me compelling” <http://www.becker-posner-blog.com/2012/06/bloomberg-sugar-and-obesityposner.html>.

Steve Sexton at the “Freakonomics” blog <http://www.freakonomics.com/> looks at another campaign to “protect” consumers. In this case it is the Californian proposal for a law that mandates cigarette-like labelling of food derived from GE plants. Sexton argues that such a law could limit food choices and hurt the poor <http://www.freakonomics.com/2012/06/22/how-california-s-gmo-labeling-law-could-limit-your-food-choices-and-hurt-the-poor/>.

One essay that is getting a lot of coverage in the blog world is Deirdre McCloskey’s ‘Factual Free-Market Fairness’ <http://bleedingheartlibertarians.com/2012/06/factual-free-market-fairness/> at “Bleeding Heart Libertarians” <http://bleedingheartlibertarians.com/>. “No. The master narrative of High Liberalism is mistaken factually. Externalities do not imply that a government can do better. Publicity does better than inspectors in restraining the alleged desire of businesspeople to poison their customers. Efficiency is not the chief merit of a market economy: innovation is. Rules arose in merchant courts and Quaker fixed prices long before governments started enforcing them.”

At “VoxEU.org” <http://www.voxeu.org/> Simon J Evenett looks at the increasing use of protectionist measures by G20 countries. He writes that “[t]here has been a steady stream of protectionist measures introduced since the last G20 summit – at least 110 measures have been implemented, 89 of which were imposed by G20 members. This report demonstrates that the amount of protectionism in 2010 and 2011 was considerably higher than previously thought. An additional 226 protectionist measures were found in those two years, representing a 36% increase on the number of beggar-thy-neighbour policies implemented during 2010 and 2011” <http://www.voxeu.org/index.php?q=node/8094>. Also at VoxEU.org Jeffrey Frankel writes on ‘The death of Inflation Targeting’ <http://www.voxeu.org/index.php?q=node/8106>. He says that “[i]t is with regret that we announce the death of Inflation Targeting. The monetary regime, known affectionately as “IT” to its friends, evidently passed away in September 2009. That the demise of IT has not been officially announced until now testifies to the esteem in which it was widely held, its usefulness as a figurehead for central banks, and fears that there might be no good candidates to assume its position as preferred anchor for monetary policy”.

At the “Stumbling and Mumbling” blog [http://stumblingandmumbling.typepad.com/stumbling\\_and\\_mumbling/](http://stumblingandmumbling.typepad.com/stumbling_and_mumbling/) Chris Dillow writes on “Economics” and Rationality’ [http://stumblingandmumbling.typepad.com/stumbling\\_and\\_mumbling/2012/06/economics-rationality.html](http://stumblingandmumbling.typepad.com/stumbling_and_mumbling/2012/06/economics-rationality.html). He argues that “[o]ne of the great irritations of our age is the tendency for non-economists to tell us what’s wrong with economics”. On a related matter Matt Nolan at the “TVHE” blog

<http://www.tvhe.co.nz/> considers some ‘Principles for talking to macroeconomists’ <http://www.tvhe.co.nz/2012/06/06/principles-for-talking-to-macroeconomists/>. He comments on a set of principles for non-economists to keep in mind when talking about the New Zealand economy with macroeconomists.

Also at the “TVHE” blog Matt Nolan is worried by ‘The missing price of food’ <http://www.tvhe.co.nz/2012/06/20/the-missing-price-of-food/>. He says “ [...] the people of the world are simultaneously threatening to eat all the worlds resources – while being obese. If that sounds non-nonsensical to you then you would be right – this is the nature of discussing the allocation of resources without taking account of prices”. Prices matter, who would have thought?

For the macro-Austrians out there Peter Lewin writes a piece at “The Freeman” <http://www.thefreemanonline.org/> on ‘Austrian Capital Theory: Why It Matters’ <http://www.thefreemanonline.org/features/austrian-capital-theory-why-it-matters/>. Lewin argues that while Keynes was talking about the “capital stock” and arguing that by stimulating spending on outputs one can increase productive investment to meet that spending, thus adding to the capital stock and increasing employment, Hayek was accusing Keynes of paying insufficient attention to the nature of capital in production. Hayek pointed out that capital investment does not simply add to production in a general way but rather is embodied in concrete capital items. That is, the productive capital of the economy is not simply an amorphous “stock” of generalized production power; it is an intricate structure of specific interrelated complementary components. Stimulating spending and investment, then, amounts to stimulating specific sections and components of this intricate structure.

At the “Fairplay and Forward Passes” blog <http://fairplayandforwardpasses.blogspot.co.nz/> Sam Richardson asks ‘Who saw this coming?’ <http://fairplayandforwardpasses.blogspot.co.nz/2012/05/who-saw-this-coming.html>. He explains, “I have to admit, I thought we, as a country, might just have gone a bit over budget in the hosting of the Rugby World Cup. Rugby New Zealand 2011 didn’t though!” That’s the good news about the Rugby World Cup [RWC]. On the downside Sam notes that the RWC was an economic disaster for the Manawatu. <http://fairplayandforwardpasses.blogspot.co.nz/2012/05/rwc-in-manawatu-economic-disaster.html>. At long, long, last!, he writes, a city council has produced an objective analysis that considers not the ex-post gross impacts but the ex-post net impacts! And guess what the outcome is? The headline from the Manawatu Standard says it all – ‘Analyst: RWC was economic disaster’. At the “Offsetting Behaviour” blog <http://offsettingbehaviour.blogspot.co.nz/> Eric Crampton is also worried by disaster. In Eric’s case the problem is a zombie apocalypse ... and the making of a TV show about it <http://offsettingbehaviour.blogspot.co.nz/2012/06/post-apocalyptic-bureaucracies.html>.

Also at “Offsetting Behaviour” Eric puts forward a ‘Dairy Puzzle’ <http://offsettingbehaviour.blogspot.co.nz/2012/06/dairy-puzzle.html>. The puzzle being, “[d]airy products are cheaper in New Zealand than in Canada, where the dairy cartel keeps prices high.

But the Dairy Farmers of Canada VP Ron Versteeg points me to an interesting puzzle: FAO stats showing NZ consumption of some dairy products is lower than that in Canada”.

Over at the “Groping towards Bethlehem” blog <http://gropingtobethlehem.wordpress.com/> Bill Kaye-Blake cries ‘The eurocrisis is dead. Long live the eurocrisis!’ <http://gropingtobethlehem.wordpress.com/2012/06/20/the-eurocrisis-is-dead-long-live-the-eurocrisis/>. He writes, “[s]o, Greece. They had the election, and the scary party didn’t win. Yay! Now we can all go back to ... to what?”

<http://www.nzae.org.nz>

# GOVERNMENT ECONOMICS NETWORK

by Joey Au (GEN Secretariat)  
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**GOVERNMENT  
ECONOMICS  
NETWORK**

## About the Government Economics Network

In September 2011 we launched the Government Economics Network (GEN).

GEN was established to promote the better use of economics in the public sector in New Zealand. It aims to cater to economists and non-economists through a range of events and training opportunities, focussed on using economics in policy advice.

The Network has three aims:

1. support economics training and professional development;
2. develop linkages between economists; and
3. strengthen economic advice to government.

Congratulations to Girol Karacaoglu (Chief Economist at the Treasury) for being appointed *Head of the Government Economics Network* by the GEN Governance Group.

## Completed

The Government Economic Network has already achieved its first year goals of:

- 200 members.
- Two economic training courses.
- Annual conference.
- 10 seminars.

Less than a year old, we have held a number of training courses, seminars and a sold out inaugural annual conference. We currently have over 300 members.

We have already held four very well attended training courses this year.

1. **Econometric Analysis of Cross Section and Panel Data** by Prof William Greene.
2. **Introductory Economics for Policy** by Dr Veronica Jacobsen.
3. **Research Without Tears** by Prof John Creedy.
4. **Income Distribution and the Role of Value Judgements** by Prof John Creedy.

Our seminars have also been well attended and have been delivered by a number of different agencies across the public sector and also private economic consulting firms. A list of our current and past seminars can be found here:

<http://www.treasury.govt.nz/economy/gen/events>

The 2011 GEN inaugural annual conference sold out. The Secretary to the Treasury, Gabriel Makhlouf and the Minister of Finance both gave the opening address and noted their support for GEN. We attracted one of the top young economists in the world rated by the New York

Times and the Economist magazine, Professor Raj Chetty, as the keynote speaker.

## Plan ahead

### Seminars:

We have already lined up a few more agencies to do a seminar this year focussed on the application of economics to policy.

### Training:

We are currently developing an *Applied Microeconomics for Policy course*. This teaching will take a case study approach to get participants to learn the use of microeconomic theory, tools and techniques in a policy context. On completion of this course participants will be able to identify and use economic concepts, tools and techniques, and to comprehend and assess what economics can contribute to policy analysis.

### Conference:

This year's annual conference is taking place on 14 December at Te Papa in Wellington. We have attracted the Chief Economist from the Department from Work and Pensions in the UK to talk about welfare reform and Martin Weale, Monetary Policy Committee Member from the Bank of England. More information about the conference will be provided in due course and on our website.

### Database of ongoing research:

We are currently developing a database containing all the ongoing research across the public sector, universities, and research institutions in New Zealand. The plan is to make this database freely available to everyone.

## Get involved

GEN is basically run by a group of volunteers with a personal commitment to building economics capability and strong belief in what GEN is trying to achieve. We are always looking for more people to get involved and help, especially with this year's annual conference in December.

For more information about the Government Economics Network please visit our website [www.gen.treasury.govt.nz](http://www.gen.treasury.govt.nz) or email us at [gen@treasury.govt.nz](mailto:gen@treasury.govt.nz).

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- Central heating/air conditioning and security services included in lease
- Wired for internet/phone
- 32 square metres
- Well-maintained, newer building
- Colourful, attractive space
- Negotiable timeframe
- Stair access only

Enquire with Glenda Shaw, [glenda.shaw@motu.org.nz](mailto:glenda.shaw@motu.org.nz) or 04 939 4250



<http://www.nzae.org.nz>

# THE FIVE-MINUTE INTERVIEW ... WITH LES OXLEY

## 1. When did you decide that you wanted a career in economics?

When I was in the 6th form at high school in England. I attended a comprehensive school (Dinnington High School) and was lucky enough to be able to take economics at 'O', 'A' and 'Special' level, but more so, to be taught by three teachers all with degrees in economics. This was almost unheard of at the time and is still quite rare even now in many places in NZ.

## 2. Did any particular event or experience influence your decision to study economics?

One of my economics teachers was 'Cec' Thompson see his obituary: <http://www.telegraph.co.uk/news/obituaries/sport-obituaries/8653233/Cec-Thompson.html>

He had such energy and enthusiasm for economics it was infectious. Following a successful and pathbreaking career in rugby league (he rose from a penniless upbringing in orphanages to become one of the first black men to play rugby league for Great Britain), he gained a degree in economics and diploma in teaching from Leeds University, when he was 39. He brought his own commitment and drive to succeed in life into the classroom and we were simply mesmerised by him – perhaps he hypnotised us with his huge, constantly waving, hands (a great asset for a rugby player.)?

I was, however, torn between studying economics and going to art school. Again it was a couple of art teachers at high school that fuelled that interest. I had some talents it seems and, at that time, was drawn towards the works of painters Francis Bacon, Lucien Freud and the sculpture Alberto Giacometti (you can see him and his works on the Swiss 100 Franc banknote).

## 3. Are there particular books which stimulated your early interest in economics?

It was really reading history books that (further) stimulated my interest in economics. Even at high school I saw history and economics as complements – institutions matter; individuals matter; technologies matter. Ultimately, this emerged in my professional life with my ongoing research on economic history initially on the British Industrial Revolution, but latterly New Zealand.

## 4. Did any teachers, lecturers or supervisors play a significant role in your early education?

See my answer to question 2 above.

## 5. Do you have any favourite economists whose works you always read?

Daron Acemoglu and Oded Galor.

I'm not a blogger (reader or writer) so I tend to read and learn through the more old fashioned technologies of conferences, working papers, journal papers and books.

## 6. Do you have a favourite among your own papers or books?

I think it would be the 1996 SJPE paper ("Technological epochs and the British Industrial Revolution, 1700-1992") with David Greasley (University of Edinburgh). This paper really started our



ongoing and successful research programme in economic history (cliometrics). David gave me some data one day and asked me to 'have a look at it.' I ran a few time series tests on the univariate series (I had no idea what the data were – even their frequency or duration) and said, 'something happens around observation 80.' "What do you mean – 'something happens'?" Well, there is a break in the series where they turn from stationary to non-stationary. David replies with, 'well, Les, you have just (re) discovered the Industrial Revolution using macroeconomic (annual industrial production) data'. And as they say, the rest is (economic) history...

## 7. What do you regard as the most significant economic event in your lifetime?

The Thatcher years. I started my economics career as a lecturer at the University of Edinburgh in the same year Margaret Thatcher was elected. I left the UK for NZ in the same year the Conservative reign ended. During that time, the trade union movement was effectively neutered, first with the miners and Arthur Scargill and then more widely. The introduction of the Poll Tax, privatisation, the rise of experimental monetary policy – much of which would soon be exported to the old Dominions in the same way as 'culture and British values' were exported there in the 19th century.

## 8. What do you like to do when you are not doing economics?

I try to make time to read detective novels, especially Ian Rankin. Rankin's novels are set in Edinburgh and having lived there for 18 years, many of the places he writes about are places I've walked past, drunk in, eaten in, etc. He also writes plots where, with careful reading, you can work out the villain – I hate those novelists who only give clues in the last few pages!

I like to walk our dogs especially in the bush and I enjoy keeping my garden under control even though the latter mainly involves sitting on a mower for periods of time, or using some tool that either cuts or shreds or chops. I'm also a bit of an IT junky and like to keep my house and office wired (or likely wireless). Having recently become an Apple convert, it's not so hard. Finally, my continued interest in art means I seek out exhibitions and collections when I can, but this would normally be in Europe rather than NZ.



# 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 on the various campuses in Victoria University (SEF). 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.

## Victoria University of Wellington

**Prof Morris ALTMAN** Morris Altman is completing experiments on consumer behaviour, testing and modelling the neoclassical assumptions on the insignificance of non-economic variables to decision-making. He is also completing experiments and modelling psychological and social determinants of wages, especially of wages above the reservation wage. In addition, Morris is modelling non-conventional benchmarks for optimal economic outcomes. He is also completing an encyclopedia of behavioural economics for Praeger Publishers and is writing papers and a book integrating ethical considerations into modelling choice behaviour. Finally, he is developing an alternative to the Economic Freedom Index, one which better predicts and explains economic outcomes.

**Dr Martin BERKA** I have recently been trying to understand in depth the relationship between productivity and prices at sectoral levels in Europe. I am also working on a model of business cycles in emerging countries that would better match some of the finer and newer empirical aspects of these countries which I am also developing.

**Dr Stephen BURNELL** Monetary and banking theory, microeconomics, dynamic general equilibrium models. Currently, research banking and monetary policy in New Zealand; the demand for cash and transactions costs, optimal fiscal policy; and telecommunications and interconnections agreements.

**Dr Paul CALCOTT** Social regulation and its alternatives. Environmental and paternalist intervention. The economics of torts.

**Dr Chia-Ying CHANG** My current research focuses on two areas. One focus is on banking crises, especially on the linkages of banking systems and international financial markets. Another focus is on market frictions, especially on how the frictions might affect decision making.

**Dr Brandon CHEN** Brandon Chen is currently working on how institutional investors' trading behaviour can have an impact on corporate governance. For example, if the stock prices are informative enough (due to informed trading) to "pose a threat" to the CEO, then shareholders do not have to incentivise the CEO with large number of shares/stock options. The CEO would still work as hard to improve firm value. The informational efficiency of stock prices could thus serve as a useful monitoring mechanism and affect many other dimensions of a firm's governance environment such as board structure, the CEO's bargaining power, or even the contractual relationships between the CEO and creditors.

**Prof Law EVANS** Microeconomics, industrial organisation and econometrics. The operation and performance of markets and organisations.

**Prof Graeme GUTHRIE** Graeme Guthrie is using real options analysis to investigate corporate investment behavior and its implications for the properties of stock returns. He is using similar theoretical techniques to examine various aspects of housing markets, and urban growth more generally. His current work in this area focusses on explaining the U.S. housing boom and bust, and identifying the determinants of urban sprawl.

**Prof Viv HALL** Viv Hall is currently researching: stylised facts of contemporary New Zealand business cycles, jointly with Stuart McKelvie; recessions and recoveries in New Zealand's Post-Second World War business cycles, jointly with John McDermott; and dating and properties of New Zealand's Classical real GDP business cycles, 1947-2012.

**Prof Dean HYSLOP** Analysis of labour markets; Applied microeconomics analysis

**Dr Michael KEEFE** Michael Keefe's research is focussed on Initial Public Offerings, Capital Structure and Cash Holdings. In recent work, Michael shows the importance of revealed private information in explaining the IPO underpricing puzzle has been over-estimated in the academic literature. Furthermore, the economic importance of private information increases in hot IPO markets, which is consistent with agency costs increasing during economic expansions. In other recent work, Michael and co-author Robert Kieschnick show that the market value of firm cash holdings increase during economic expansions and investment opportunities. The importance is magnified for young and small firms that conduct R&D. Overall, they show that cash is more valuable for financially constrained firms with investment opportunities.

**Dr Mohammed KHALED** Exploration of the presence and dynamics of stock market inefficiency arising from predictability based on past returns, calendar anomalies, firm size effects and mood factors (seasonal affective disorder, lunar cycles, Friday the 13th). Other research interests include: measuring the weighted aggregate cost of capital, test of stock market efficiency using unit root versus variance ratio tests, testing independence of auditors when they supply non-audit services to their clients, consumer demand models, and measuring economies of scale and scope in production.

**Dr Jacek KRAWCZYK** Computational economics, mathematical modelling, dynamic games, optimal control theory and viability theory; applications of the above to monetary policy, portfolio management, environmental and energy economics.

**A/Prof Martin LALLY** Martin's area of interest is asset pricing with a particular focus on risk of capital. Current research projects include combining estimates of the market risk premium from multiple markets to generate statistically superior estimates, determining the optimal time for a participant in a defined-benefits pension scheme to exit the scheme, and the implications of debt policy for beta gearing formulas.

**A/Prof Hai LIN** My research in progress includes: predictability of NZ stock market returns using international predictors; Momentum spillover from stocks to corporate

bonds; predictability of US corporate bond returns; pricing of liquidity risk in fixed income markets.

**Jerry MUSHIN** Jerry Mushin is continuing work on exchange rates, monetary policy, and the effects of monetary unions.

**A/Prof Ilan NOY** Ilan Noy's empirical research focuses on: financial crises and their impacts - most recently on the impact of fiscal and monetary expansions in the post-crisis period and on banking regulation and banking crises; capital flows - most recently on the impact of capital controls in Brazil; and the economics of natural disasters - most recently on the long-term impact of the 1995 Kobe earthquake and on post-disaster foreign aid.

**Dr Vladimir PETKOV** Dynamic games, contracts, environmental economics.

**Dr John RANDAL** Stock price modelling, derivative pricing, financial time series analysis. Current research includes the application of robust statistics to financial data, in particular for volatility estimation, and analysis of the leverage effect.

**Dr Leigh ROBERTS** I am currently investigating whether it is better for New Zealanders to take out fixed interest or floating interest mortgages, and if fixed interest is better, for which term? I am also looking at determinants of mortgage rates in New Zealand.

**A/Prof Jack ROBLES** Jack Robles is currently engaged in two main lines of research. Jack is working with Brad Graham on two papers in law and economics. Both papers concern investigate the incentives that different fee arrangements give to lawyers. In this first such paper, Jack and Brad investigate the impact of "Sunshine laws" which require that lawyers report hours worked even when working on a contingency basis. In their second paper, Jack and Brad investigate the construction of an optimal contract when client and attorney have a repeated relationship. Jack's second line of research is at the intersection of energy economics and industrial organization. In this line, Jack is concerned with energy markets which include both hydro and thermal (e.g. gas burning) producers of energy. Jack's current paper on this subject extends the standard finite horizon model to an infinite horizon. In the near future, Jack intends to extend the standard model to study predatory pricing, and the impact of including reservoir current capacity in the production function.

**Dr Yigit SAĞLAM** My current research is concentrated on three areas. The first is water management, auctions, and transportation. My work on water pricing is mainly on sectoral price discrimination and water shortages. In particular, I model the frequency of water shortages and investigate how different options such as desalination and efficient pricing can help avoiding water scarcity. My second area is the theory and structural estimation of auctions. My main interest in auctions is spectrum auctions and their effect on the degree of competition in the telecommunications market. Finally, I have been involved in a transportation project where the focus is on jointly estimating the residential location, car ownership, and mode of transport using GIS data from New Zealand Transport Agency.

**Dr Stefanie SCHURER** Stefanie's research contributes to building a bridge between economics and psychology. She is interested in analysing the effects of moods, attitudes, and personality traits on economic outcomes, and asks whether moods and attitudes could potentially be changed. A crucial component of her research is to investigate how feelings of depression and anxiety are passed on across three generations, and whether the experience of depression of a parent during childhood impairs education outcomes and income potentials of the child in adulthood. She also finds that feelings of depression are quite persistent over time, and chronically ill individuals tend to have a higher demand for health care services than individuals who have other chronic illness such as diabetes or asthma. Currently, she quantifies the overall economic burden of depression in New Zealand in collaboration with Compass Health, a primary care fund-holder in the Greater Wellington Region, and the financial support of Victoria University of Wellington. Stefanie also considers other attitudes that appear to correlate strongly with investment in health or education. One of these attitudes is sense control which measures to what degree an individual has fatalistic beliefs. She finds that individuals who have a fatalistic attitude about the outcomes in their life tend to invest less in their health such as a good diet, exercising regularly or avoiding smoking, although the reasons why this is the case appears to differ between men and women. Probably one of her most exciting research project is the analysis of the intergenerational transmission of gender role attitudes. Daughters who grew up with mothers who held and expressed very traditional beliefs about gender when they were 5 years of age do not only have lower education outcomes, but also are less likely to work full-time during adulthood, while sons tend to marry more traditional wives. Such results are tale-telling of how gender inequalities of economic opportunities are potentially perpetuated over many generations. Stefanie is specialised in the analysis of panel and cohort data, which allow for a life cycle perspective of economic choices. Recently she started working with GP practice administrative data from New Zealand.

**A/Prof Christoph THOENISSEN** My current work analyses the role of financial frictions in the business cycle. Some of the issues that I'm interested address whether explicitly accounting for financial frictions in macroeconomic models alters our understanding of what drives the business cycle. What is the role of the banking sector? How do shocks originating in the financial sector propagate through the economy and how do financial shocks propagate from one country to the next? These issues are important, not just because they help us to better understand the effects of financial frictions, but also because they inform the optimal policy response to such shocks.

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NZEP has a keen interest in research on important issues relevant to New Zealand, Australia and the Asia-Pacific. The journal also publishes survey articles, book reviews and welcomes articles that explore important policy initiatives affecting the region and the implications of those policies. Authors are invited to submit their manuscripts to NZEP online (<http://www.tandf.co.uk/journals/rnzp>).

For those with an interest in league tables, the top ten articles downloaded via the Routledge Taylor-Francis platform in 2011 were (1) Volume 44: Ananish Chaudhuri, *Reflections of a journal editor*; (2) Volume 45: Simon Kemp, Gabrielle Wall, *Psychology and economics: An introduction to the special issue*; (3) Volume 43: Nan Jiang, Basil Sharp & Mingyue Sheng, *New Zealand's emissions trading scheme*; (4) Volume 43: Philip McCann, *Economic geography, globalisation and New Zealand's productivity paradox*; (5) Volume 45: Peter E. Earl, *From anecdotes to novels: Reflective inputs for behavioural economics*; (6) Volume 40: Bai Juhong & Tim Maloney, *Ethnicity and academic success at university*; (7) Volume 45, Juan A. Lacomba, Francisco Lagos, Tibor Neugebauer, *Who makes the pie bigger? An experimental study on co-opetition*; (8) Volume 45: Ti-Ching Peng, *Overcapitalization and cost escalation in housing renovation*; (9) Volume 45: Seamus Hogan, Hamish Kidd, Laura Meriluoto, Andrew Smith, *The fixed price offer mechanism in Trade Me online auctions*; (10) Volume 45: James Horrocks, Andrea Kutinova Menclova, *The effects of weather on crime*.

These rankings can be contrasted by the top ten articles downloaded via EBSCOhost databases in 2011 which were (1) Volume 43: Philip McCann, *Economic geography, globalisation and New Zealand's productivity paradox*; (2) Volume 43: Nan Jiang, Basil Sharp & Mingyue Sheng, *New Zealand's emissions trading scheme*; (3) Volume 44: Malcolm Abbott, *The long term development of New Zealand's electricity supply industry*; (4) Volume 44: Michael Littlewood, *Pre-funding a government's future financial obligations - the New Zealand Superannuation case study*; (5) Volume 42: John Fitzgerald, Tim Maloney & Gail Pacheco, *The Impact of Recent Changes in Family Assistance on Partnering and Women's Employment in New Zealand*; (6) Volume 42: Johannes Van Biesebroeck, *Governments at the Bidding Table*; (7) Volume 42: Martin Lally, *Free Cash Flow Models, Terminal Values and the Timing of Asset Replacements*; (8) Volume 41: Susan St John, *KiwiSaver and the Tax Treatment of Retirement Saving in NZ*; (9) Volume 44: Robert A. Buckle, *Introduction: Tax policy reform New Zealand style*; (10) Volume 43: Anthony J. Makin, Wei Zhang & Grant M. Scobie, *The contribution of foreign borrowing to the New Zealand economy*.

Mark Holmes ([holmesmj@waikato.ac.nz](mailto:holmesmj@waikato.ac.nz)), Editor-in-Chief.

## 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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## NEW INPUT-OUTPUT TABLES

Statistics New Zealand plans to release input-output tables for the year ended March 2007 on 31 July. These tables are a powerful analytical tool that describes the structure of the New Zealand economy.

Input-output tables have many uses, including:

- estimating the effect on key economic variables from changes in government policy;
- examining the impact of changes in producer prices or wages on the CPI; and
- exploring the reliance of industries on imports and estimating their contribution to exports.

The input-output tables are consistent with the published annual national accounts and will be broken down into approximately 100 industries and 200 products. They will be produced using the updated ANZSIC06 industry classification, which is designed to better reflect the modern New Zealand economy. The last set of input-output tables published was for the March 1996

year and used the older ANZSIC96 industry classification. Supply and use tables (a subset of input-output tables) were also published for the March 2003 and 2007 years. Statistics NZ is aiming to produce annual input-output tables in the future, dependent on user demand and available resources.

The tables will be spreadsheet based and accessible via the National Accounts landing page on the Statistics NZ website. They will be published in basic prices and will include the following analytical tables, with explanatory information and examples of how they can be used:

**Table 1:** Supply of products by industry and imports

**Table 2:** Use of products by industry and final use (domestic consumption, investment and exports)

**Table 3:** Use of imported products by industry and final use

**Table 4:** Transactions between industries and final use

**Table 5:** Total requirements – the extra output required from each industry if an industry increases its output

**Table 6:** Ultimate use of industry output – the final use of each industry's output, whether consumed directly or further processed by other industries.

**Table 7:** Input coefficients of industries – the proportion of an industry's value added that relies on different primary inputs e.g. salaries and wages, imports etc.

**Table 8:** Input coefficients of final use – the relative proportion of primary inputs attributed to final uses

**Table 9:** Import coefficients of industries and final use – the direct and indirect use of imports for particular products, by industry and final use.

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