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# ASymmetric information

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

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# *Neo-nihilism?*

EDITORIAL

I was thinking about a central theme of this issue of *AI*, namely that, to make strong, valid comments, we should recognise how little we know. It could be called the neo-nihilist school of economics, or, for those familiar with “Fawlty Towers”, the Manuel school of economics, given his central line in one episode, “I know nothing”. Socrates would have approved, judging by the Apology (see *AI* No.23, p.24).

We would have some advantages over other places in the development of such an approach. It requires a generalist perspective. Specialists rely heavily on an assumption that information from elsewhere is acceptable, and they are therefore limited in the extent to which they can question. Here in New Zealand we, individually, have the freedom to take a broader perspective than in larger centres. We are relatively remote (despite the internet), with a small economics community that encourages diversity of interest and intermingling of people who cover the whole spectrum of economic applications. It could prove to be a real strength. It would be much harder elsewhere to survive as a generalist academic when competing with many specialists, especially where it can be hard to be in contact with a broadly based community.

Let us not forget also the dictum, “publish or perish”. This could serve as a sober warning and a severe constraint to potentially free-thinking economists elsewhere. Fortunately for some of us in New Zealand (this writer included), the difference in the futures that we face here through either publishing or perishing is hardly of any great significance.

For many of the issues to be addressed in New Zealand, we do not possess large databases as exist in some other countries. This constraint could actually give us, over time, a competitive advantage in analyses that draw on a range of perspectives, including those from the academic, private and public sectors, using limited data. While large databases exist overseas, even there many economic questions arise in situations for which there is little information. The difference between there and here is that academics with large databases will have strong incentives to avoid issues for which there is a dearth of data.

As an additional step towards neo-nihilism, we could note that one problem with the time dimension in relation to ideas is that we have a view of progression, rather than perspective. With progression, we can ignore thinking from the past because the present has evolved from and improved on it. Too often we take this position, thereby restricting ourselves. With perspective, on the other hand, other views are still of value, and the past gives us a means of seeing the present through others’ eyes. There are a few short illustrations in the following pages.

As a closing word in this editorial, Gary Buurman and I have co-edited *AI* since Issue No.6. He is retiring this summer, and so this will be the last issue to receive his careful scrutiny. His quality editing and sharp insights have been invaluable, and his contribution has been far more significant than his low profile would suggest. Thank you Gary, it has been most rewarding working with you.

by Stuart Birks, Massey University

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

**Why a Higher Minimum Wage Doesn't Add Up** by *Gail Pacheco*  
(*gail.pacheco@aut.ac.nz*)

Keynes states that “the ideas of economists and political philosophers, both when they are right and when they are wrong, are more powerful than is commonly understood”<sup>1</sup>. Unfortunately it is the latter that appears to be rife in terms of the minimum wage debate, and not just wrong ideas / assumptions, but also the lack of ideas.

The current Employment Relations Policy of the Labour government indicates that Labour wish to continue to strengthen the minimum code of employment rights by continuing to make annual adjustments to the minimum wage. In particular, it proposes increasing the adult minimum rate to \$12 gross an hour over the next four adjustments. Such an increase, (approximately 36%), surely warrants more public discussion on its perceived merits and demerits. However, there is limited explanation or justification provided from the main political parties in terms of these proposed increases.

What exactly have the major political parties and interest groups (Labour, NZ First, the Council of Trade Unions (CTU), Employers and Manufacturers Association (EMA)) assumed in their discussion of these proposed increases? Are the claims being supported by empirical evidence? Have they actually analysed the key issues and how the labour markets will respond to these increases?

On 9 September Winston Peters gave a speech on ““Dealing with Economic Reality” and he stated that “most importantly—we must break the low wage cycle and start to force wages up, beginning with a minimum wage of \$12 an hour”<sup>2</sup>. Therefore, it seems that NZ First believes, i.e. implicitly assumes, that the way to improve pay in NZ is just to legislate higher wages. Helen Clark also presented raising the minimum wage as a positive move when addressing the CTU on 18 October this year when she said “We have raised the minimum wage every year since coming into government, and it will continue to rise. Indeed the aspiration over the next four adjustments is to see it move close to \$12 an hour for the adult rate”<sup>3</sup>. Therefore, it seems that neither political party is yet to address the potential negative impacts of the higher minimum wage.

These include reduced employment for the affected groups of workers, reduced work hours (the EMA ran a snap survey on businesses which revealed that 75% of them felt that the proposed increases would affect them badly<sup>4</sup>), a reduction in enrolment rates (Pacheco and Cruickshank, 2005<sup>5</sup> found the elasticity of educational enrolment with respect to the minimum wage for 15-24 year olds over the time period 1986 – 2003 ranged from -0.0228 to -0.0399 and was significant at the 1% level), spillover effects on those earning above the minimum wage, etc..

The CTU appears to be the group that is the foremost supporter of higher minimum wages. They believe that “a low minimum wage entrenches a low-wage, low-skill, low technology approach to employment, and this is not the direction New Zealand needs to be heading,”<sup>6</sup> They appear to assume that raising the minimum wage is a step towards addressing skill shortages. This of course ignores the human capital effect that a higher minimum wage increases the indirect costs of upskilling, reducing the incentive. Also, empirical evidence on who exactly earns the minimum wage indicates that it is the least qualified and least skilled subgroup of employees that will be the most vulnerable to minimum wage hikes. Using Income Survey data from 1997 to 2004, the minimum for youth without qualifications (i.e. no school qualifications) has increased from 0.60 to 0.84 of the median wage level<sup>7</sup>. Also at risk when the minimum wage is raised are youth in general (16-17 and 18-19 year olds). Over the

<sup>1</sup> p.383 “The General Theory of Employment Interest and Money” Keynes 1964.

<sup>2</sup> [http://www.nzfirst.org.nz/content/display\\_item.php?t=1&i=2093](http://www.nzfirst.org.nz/content/display_item.php?t=1&i=2093)

<sup>3</sup> <http://www.beehive.govt.nz/ViewDocument.aspx?DocumentID=24262>

<sup>4</sup> [http://www.nbr.co.nz/search/search\\_article.asp?id=13233&cid=0&cname=Results](http://www.nbr.co.nz/search/search_article.asp?id=13233&cid=0&cname=Results)

<sup>5</sup> [http://www.nzae.org.nz/conferences/2005/QA3-Gail\\_A.\\_Pacheco\\_and\\_Amy\\_A.\\_Cruikshank.pdf](http://www.nzae.org.nz/conferences/2005/QA3-Gail_A._Pacheco_and_Amy_A._Cruikshank.pdf)

<sup>6</sup> Statement by CTU secretary, Carol Beaumont.

[http://www.nbr.co.nz/search/search\\_article.asp?id=13242&cid=0&cname=Results](http://www.nbr.co.nz/search/search_article.asp?id=13242&cid=0&cname=Results)

<sup>7</sup> Source: PhD work in progress by Gail Pacheco.

8 year time period 1997 – 2004, the relative minimum for these groups has gone from 0.60 and 0.54 to 0.85 and 0.88 respectively. Therefore, the current levels of minimum wage in NZ appear to be set closer to the median wage level and are already at a very effective level for these groups of workers.

To calculate which types of workers will be the most hurt by the higher minimum wage, the same data set has been combined with the Household Labour Force Survey to investigate who is being paid the minimum or below it. It was found that 5.75% of the sample over the period 1997 – 2004 were paid either around the minimum wage (i.e. at the minimum wage or higher, but less than 10% above the minimum wage) or below the prevailing minimum.<sup>8</sup> These consisted of, as expected, proportionately more women, Maori and Pacific Islanders, employees aged under 25, part time workers (77% of the sample worked full time, while only 50% of minimum wage workers were full time employed), workers in the retail sector or accommodation, cafes and restaurants (these workers accounted for more than 40% of minimum wage earners) and workers in the textile industry and the agriculture, forestry and fishing sector.<sup>9</sup>

However, the numbers that the government probably needs to pay the most attention to are the groups of workers that are earning below the minimum and specifically how the characteristics of these workers have changed as the minimum has increased every year over the last six years. Again, using the Household Labour Force Survey and Income Survey data, changes across the time period 1997 – 1999 (when no increases were made to the nominal minimum for either adults or youth) to 2002 – 2004 finds that the sub minimum group is much more likely to be aged 16-24 (barely 1.46% of the sub minimum group were aged 16-17 for example, in 1997-1999, whereas this age group accounted for 16.02% of those earning below the minimum in 2002-2004). The sub minimum group is also significantly more likely to have more qualifications in the latter time period and less likely to be working full time, along with reduced usual total weekly hours.<sup>10</sup> These changes are an indication that the recent rises in the minimum wage have reduced hours for affected workers and perhaps forced some into part time employment.

Further evidence of employers being forced to pay sub minimum wages is backed by the increase in the number of adult and youth minimum wage complaints, investigations and breaches disclosed since 1997. For example, there were 15 adult minimum wage breaches disclosed in 1998 and this had increased to 106 by 2003.<sup>11</sup>

Another angle that could be pursued in terms of why the minimum should be raised, is one that is taken by the Green Party. They state that one of the key measures they would like to see implemented to help end child poverty include raising the minimum wage from \$9.50 to \$12.00 an hour.<sup>12</sup> Research does show that there is a strong empirical link between the poverty status of the household and having a minimum wage earner in the household in New Zealand. In particular, it was found that 51% of workers affected by the minimum wage belonged to the bottom three deciles of the household income distribution.<sup>13</sup>

However, to check whether raising the minimum wage will impact significantly on poverty, a simple simulation was run again using the Household Labour Force Survey and Income Survey data. Using a poverty threshold of \$250 for real equivalent weekly household income<sup>14</sup>, the best case scenario would constitute the minimum wage earner receiving a 10% increase in their earnings when the minimum wage is raised 10% and no loss in employment or hours of work. To begin with, the initial poverty rate was 14.88% and under the best case scenario, the hypothetical poverty rate fell to 14.81%. Hence, assuming the best possible

<sup>8</sup> Source: PhD work in progress by Gail Pacheco.

<sup>9</sup> “Impact of the Minimum Wage on Expected Profits” Pacheco and Naiker, *International Review of Applied Economics*, forthcoming (2006).

<sup>10</sup> Source: PhD work in progress by Gail Pacheco.

<sup>11</sup> Source: Employment Relations Service.

<sup>12</sup> <http://www.greens.org.nz/searchdocs/other8654.html>

<sup>13</sup> “The Link between Poverty and Minimum Wage Incidence in New Zealand” Pacheco, PhD Conference in Business and Economics, Papers and Proceedings, 2005.

<sup>14</sup> Figure derived from using the informal poverty measure of 50% of median household income.

outcome for increasing the minimum wage and also assuming no indirect effects of the higher minimum wage for those earning above the minimum wage and for non workers as well, there was still just a 0.46% decline in the poverty rate.<sup>15</sup>

Given this lack of a positive impact of the higher minimum wage and the definite concerns in terms of the negative impacts (which will most likely impact on those who are already proportionately overrepresented in the low paid group – i.e. youth, Maori and Pacific Islanders, the least qualified, etc), it seems that before the proposed increases to the minimum occur, more discussion needs to take place on what the perceived benefits and problems would be with raising the minimum wage. The fact that we have not seen the negative employment effects of the higher minimum wage in the most recent years is possibly because the good economic growth we have had over this time has masked the impacts of the large increases in the adult and youth minimum wage (i.e. the demand for labour has shifted to the right).

Consequently, Keynes statement made nearly 70 years ago is as relevant to today's micro policies as it was to yesterdays' macro policies. Economists must intervene in this debate to ensure that "Madmen in authority"<sup>16</sup> do not persist with wrong assumptions.

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<sup>15</sup> "The Link between Poverty and Minimum Wage Incidence in New Zealand" Pacheco, PhD Conference in Business and Economics, Papers and Proceedings, 2005.

<sup>16</sup> p.383 "The General Theory of Employment Interest and Money" Keynes 1964.

## **A NEW DATA BASE FOR NEW ZEALAND**

Ever needed to know what interest rates were in the 1920s? How many people were on benefits in the 1960s? And what was the Consumer Price Index in 1878? By how much has real public spending on health per capita risen since from 1870 to 2001? Do the police solve a higher proportion of reported crime today than in 1870? What was the money supply in 1910?

The Treasury has developed a database of long-term data for New Zealand. About 400 social, demographic and economic variables have been used to compile a series of annual data tables stretching as far back as 1840 right up to the present. Each table is contained in an Excel spreadsheet, allowing users to download the data and conduct further analysis. Information on the source of each variable is provided in the spreadsheet, with detailed citations attached to each file.

This data base has been made available now on the website of Statistics New Zealand and will be maintained and updated by them as part of their Official Statistics Research and Data Archive Centre (**OSRDAC**)

See: <http://www.stats.govt.nz/tables/ltds/default.htm>

If you have any suggestions or corrections please send them to Dr Grant Scobie, Principal Advisor, Policy Support and Analysis Section, The Treasury who was responsible for the development of the data base. Email: [grant.scobie@treasury.govt.nz](mailto:grant.scobie@treasury.govt.nz) or ph +64 4 471-5005.

## **Seminar Series at Massey**

The Department of Allied and International Economics at Massey University is running a seminar series at 12.00 noon on Wednesdays during the first and second semesters. Visitors are welcome, and anyone wishing to present a paper is invited to contact our seminar series organizer, Shamim Shakur, at: [s.shakur@massey.ac.nz](mailto:s.shakur@massey.ac.nz)



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Communities once observed as marginalized are now identified as potentially resurgent as they engage in or are encouraged to participate in activities leading to new levels of economic development. The symposium seeks to identify common themes in the economic engagement activities of such communities. The focus will be on extended discussion of research frameworks and methods.

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- Indigenous communities,
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## Would textbook economics suggest raising taxes? by Stuart Birks

Alan Bollard has a dilemma. We want lower inflation, but we also want a lower exchange rate and a reduced current account deficit, which he describes as being generally seen as at an unsustainable level.<sup>1</sup> We are near full employment, but we want increased growth. We want reduced consumption, but increased investment.

If he raises interest rates, that will encourage more capital inflow and a high exchange rate. That may be why his speech of 14 October included attempts to dissuade foreign investors with warnings of downside exchange rate risk. Even if that were successful, he would still be in a bind, and he hinted at that with his words of caution about expansionary fiscal policy. Textbook economics, other than that which is purely monetarist, might suggest that too much of the responsibility is on his shoulders. What about taxes and the fiscal dimension?

We currently see inflation as essentially a monetary phenomenon, but there are non-monetary factors at work also. Mention has been made in the media of the inflationary effects of rising oil prices, and some attention has been paid to the effects of skills shortages, but less has been said about the government's pay equity and minimum wage policies.

Many years ago a paper by Arthur Grimes in *NZEP* described cost-shift inflation.<sup>2</sup> If relative prices are to change, and prices are sticky downwards, the net effect is an upward movement in the price level. If attempts are made to alter relative prices or wages in ways not supported by market forces, then additional pressures will arise to restore prior relativities. So, if the government wishes to disregard market forces<sup>3</sup>, or if market forces are operating to adjust relative prices, there can be inflationary consequences.

According to the textbooks, a restrictive fiscal policy could give reduced consumer spending and lower interest rates. The latter may result in a lower capital inflow and hence a lower exchange rate. This could maintain business confidence and high employment, along with investment, as overall demand will still be high, but more of it will be from overseas.

Of course, there are disincentive effects of high taxes, and they may increase pressures for pay increases, not to mention the political problems. However, there are also timing factors. It is said that interest rate changes are slow to take effect due to fixed interest mortgages. An income tax increase could be felt in pay packets much sooner.

What is happening with overseas borrowing? A reduction in the current account deficit will be associated with reduced net capital inflows. Is the borrowing occurring for beneficial reasons? Much of it appears to be by banks as they finance their lending. Is it risky for overseas lenders? This might depend on who is bearing any exchange rate risk, but banks should be fairly safe borrowers and the lending may be short-term. Are the banks bearing a risk? If they are lending for mortgages, then they are likely to be fairly safe, unless people are unable to pay, and they have borrowed a large part of the price of their houses, and the housing market takes a dive. So it is the small borrowers who are bearing most of the risk.

Meanwhile there are other changes which can exacerbate this problem. For example, a new development proposed in relation to the New Zealand share market allows investors to trade in selected shares while putting up only ten percent of the price. The rest is made available to them as a loan.<sup>4</sup> While it is another way to encourage borrowing, it may not be for the wisest of reasons. These developments are essentially structural changes, which will affect the way the economy operates, further reducing our understanding of prevailing economic relationships.

At the same time, we are now hearing calls for tax cuts from several quarters, including Treasury. These are presented in the context of long-term strategies. However, the Reserve

<sup>1</sup> Bollard A (2005) "Imbalances in the New Zealand economy", Address to the New Zealand Credit and Finance, Rotorua, 14 October, <http://www.rbnz.govt.nz/speeches/2111459.html>

<sup>2</sup> Grimes A (1979) "Demand-Shift Inflation Theory: A Preliminary Examination in the New Zealand Context", *New Zealand Economic Papers*, Vol.13, pp.56-74.

<sup>3</sup> See Birks S (2004) "Pay Equity and Equal Employment Opportunities", *Asymmetric* No.21, November, pp.10-12.

<sup>4</sup> Hunter T (2005) "Broker to offer new option for NZ share investors", *Sunday Star-Times*, 23 October, <http://www.stuff.co.nz/stuff/0,2106,3453426a13,00.html>



Bank is obliged to focus on the shorter term. In that context, there may be value in considering a tighter fiscal, looser monetary approach.

### **Economics and the Housing Bubble** by Stuart Birks

Economic theory has a simple explanation for the rising house prices and how events will turn out in the future. There is an increased demand for housing, but supply can only change through new construction. There are constraints to house building capacity due, among other things, to the limited number of skilled building workers. Once the capacity is reached, the supply curve becomes vertical, prices of new houses rise, but building does not increase. Builders and building workers can charge a premium for their services, so that the cost of new construction rises along with the price of existing houses.

A drop in building consents is seen by some public commentators as a problem, but really builders will still be working at capacity (lower down the vertical part of the supply curve). It is just that they will not be able to charge such a high premium. As a consequence, we will see a fall in the price of houses (in real terms at least). If people had been more patient about getting houses, there would not have been the blip in the first place.

As a further complication, there is a difference between the physical and the economic life of housing. An increase in the housing stock, with additional housing being newer and possibly of better quality, will result in a shorter economic life for some housing at the bottom end of the market. In other words, a building boom may not be associated with increasing prices for all housing, and will not generate as large an increase in overall housing stock (or oversupply) as might have been imagined.

So it is all very simple really, and economic theory can explain it all. There is just one small problem. According to a Radio New Zealand news bulletin of 15 November, there is already a slow down in the building industry, with building firms laying off staff.<sup>1</sup>

Of course, this may be an example of inaccurate news. Alternatively there may be a good economic explanation that we could give, in retrospect, for why we are observing something unexpected. However, explanations in retrospect are not much use. Policy is a matter of using information from the past to identify concerns in the future and to suggest effective remedies.

I came across an example of economic explanations the other day in a paper by J O'Connor.<sup>2</sup> Describing market imperfections in the labour market he writes on the behaviour of self-interested capitalists in a situation reminiscent of the tragedy of the commons:

*...capitalists may have short-time horizons and hire workers with life-time horizons, such that work time is optimum in the short run but shortens a man's working life in the long run. Historically, hours laws can be traced to the irrationality of individual capitalists in the labor market and the need for the State to preserve the labor power for all capitalists from the depredations of individual capitalists. (p.372)*

This is just one of several examples of failure of unregulated markets justifying government intervention presented in the paper. O'Connor then continues:

*We offer so many examples...only to emphasise the fact that faced with real concrete situations it is often possible to 'justify' any particular government interference after the fact – justify it in terms of orthodox criteria. (p.373)*

*“To what extent are economists providing knowledge, as opposed to expositions which merely look and sound convincing?”*

<sup>1</sup> Radio New Zealand, (2005) “Slow-down in the building industry”, 15 November, <http://www.radionz.co.nz/news/bulletins/radionz/200511150834/2e78e6af>

<sup>2</sup> O'Connor J (1969) “Scientific and Ideological Elements in the Economic Theory of Government Policy”, *Science and Society*, Vol.33, pp.385-414, reprinted in Hunt E K and Schwartz J G (eds.) (1972) *A Critique of Economic Theory*, Harmondsworth: Penguin, pp.367-396



## From the 2BRED File

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

What's wrong with the economics? Before you rush to give me the obvious answer: “*economists*”, let me assure you that I was not actually asking you that question; rather, I was referring to the title of a new book. *A Guide to What's Wrong with Economics* edited by *Edward Fullbrook* (London: Anthem Press, 2004). A total of 27 economists from eight countries in five continents have each written short chapters outlining what they see as the limitations of the neoclassical model. The basic theme of the book is that neoclassical economics is too restrictive, burdened with too many unrealistic assumptions, incapable of incorporating the richness of human behaviour, and generally outdated in view of the fact that much of its foundations were laid in the latter part of the 19th century. The world has changed since then, and the standard toolkit is simply no longer useful.

I have to admit I found the overall theme of the damnation of neoclassical economics a little harsh (although perhaps that view is rather too defensive given my rather solid upbringing on neoclassical economics). The editor claims that in addition to being irrelevant those promoting neoclassical economics have succeeded in blocking appointments within university departments of anyone who had a contrary view, denying them opportunities to publish in professional journals and restricting the economics curricula that universities offer.

Despite these unsupported assertions, and a failure to recognise that neoclassical economics has in fact encompassed an increasing number of extensions including uncertainty game theory, dynamics, imperfect competition to name but a few, the book does contain many chapters well worth a read. My favourite would have to be by Paul Ormerod, the author of *Butterfly Economics*. His view is that economics is constantly reinventing itself, and increasingly models allow the results of actions by others to influence economic behaviour. Inevitably there is a lag as academic economists retool, address new lines of research, and incorporate broader thinking into courses traditionally built on orthodox neoclassical economics. So perhaps a stick of gelignite and a fresh start is not called for - well, at least not quite yet! In fact the market for ideas is flourishing, just as neoclassical models would have predicted!

To reinforce the point that all economics is trapped in some 19<sup>th</sup> century time warp, consider the question of happiness. Economists are now trying to make sense of what all this research on happiness really means. Does it have any theoretical underpinning? Can it help explain behaviour? Does it assist in designing and implementing better policies? *Richard Layard* in *Happiness: Lessons from a New Science* (London: The Penguin Group, 2005) provides a readable overview of the subject. He starts with the apparent paradox that if we ask people for a subjective assessment of how happy they feel, we find that this has not changed in 50 years despite rising incomes. So apparently income is not a good measure of happiness. Even the most diehard neoclassicist would not have argued this; so in some ways the book is built on a strawman. Nevertheless it surveys the field, and you will come away with endless snippets: eg, the average happiness score is a maximum when having sex and that score is twice as high as it is for working (though clearly this can't be the case at the margin or we see more substitution out of work). Seriously, Layard makes a cogent case for keeping unemployment low, a major source of unhappiness (as recognised by economists of course when they used to calculate the Misery Index); we should devote more to eliminating world poverty, and we should strive for a better work-life balance in our public policies. Will spending \$US9.40 + shipping for a second hand version of this happy book make you happier? Probably worth a chance.

I recently spent an hour or so browsing the shelves of the bookstore at the University of Glasgow. With driving northerly rain and a maximum temperature of 6° that day, spending time in the quiet warmth of the bookstore seemed like a good way to use a vacation afternoon. I noted down references to quite a few new books, a number of which will doubtless make an appearance in future 2BRED columns. However one that really caught my eye was: *The travels of a T-shirt in the global economy: an economist examines the markets, power, and politics of world trade* written by *Pietra Rivoli*, a Georgetown University professor of

economics (New Jersey: John Wiley and Sons: 2005). How could anyone resist taking a book with that title from the shelf to have a quick browse?

And one quick browse was all it took to convince me that on return to New Zealand I needed to place an inter-library loan request. Believe me, this is a gem. It is a wonderful blend of economic history, development, growth, technological change, rent-seeking, globalisation, public policy and trade distortions; all of this written in a thoroughly entertaining and informative style. It traces the whole history of the global cotton industry from farm production, through processing, textile manufacturing and international trade. Those of you who were at the recent NZAE conference in Christchurch will recall hearing an eloquent argument made by distinguished fellow John McMillan for greater use of stories by economists. This volume is replete with stories written at first hand from the author's travels. She engaged farmers in Texas, politicians in Washington, girls working in the textile mills of Shanghai, and clothing sellers in the urban markets of Dar-es-Salaam.

My favourite section is a discussion of the policy response by the British government to a flood of hand-made Indian cotton calicoes and muslins that began to pour into Britain in the mid-1600s. They were brightly coloured, cheap, light and washable; in short a boon to the British consumers accustomed to prickly, heavy, woollen uncomfortable garments. Naturally the imports threatened the existing British woollen industry and the inevitable clamour for protection arose. The woollen industry was able to have an Act passed by Parliament in 1689 which reserved cottons for use in the summer only.

*All persons whatsoever to wear no garment but what is made of sheep's wool from the feast of all Saints to the feast of Annunciation.*

A further Act introduced in 1699 required that:

*all magistrates, the judges, students of the universities, and all professors of the common and civil law must wear garments made of woollen manufacture at all times of the year.*

Eventually these laws were withdrawn so that by 1700 only one group of consumers was subject to such restrictions. An Act passed in that year required that:

*no corpse of any person shall be buried in any shirt, shift, sheet or shroud other than what is made of sheep's wool only.*

To my mind, this is economic storytelling at its best.

#### **Flax** (from p.2 of the *Manawatu Herald* of 12 November 1895)

We notice that our contemporary *Wanganui Herald* devoted a leader last Friday to the Flax Industry. We are glad to see that the importance of this trade is getting impressed on the conductors of Government journals, as it would have been better for the colony had some days of the past session been devoted to consideration as to how the industry might be helped than in the way many days were wasted. It is rather amusing to find that the *Herald* appears to have wholly misunderstood the action of the Government in this matter, and by mistake endeavours to praise instead of condemning it. "We are pleased to notice the Government have, through the Gazette, notified that a bonus of £1750 is offered for a machine or process for drawing New Zealand hemp" says the *Herald*, apparently oblivious that the amount was offered a twelve month ago, resulting in a number of inventions being submitted to experts, but none of which were considered worthy of the bonus allotted to it. Before anything was done, Mr J. G. Wilson and those conversant with the flax trade declared the bonus too paltry to induce first-class engineers to compete, and events proved them to be correct. The experts, we believe, also reported that in their opinion the amount offered was inadequate. That the Government repeat that which has been shown to be useless in the past is not a matter for commendation, but for condemnation, for which we claim our namesake's support, as it properly urged "we trust this offer will result in the invention of an improved method of preparing *phormium tenax* fibre that will enable it to become one of the colony's stable products, as its preparation gives employment to a very large number of persons and thus relieves the congested labour markets of the colony, which latter could afford to give £10,000 for an improvement that would enable it to export 25,000 tons of dressed New Zealand flax fibre a year at reasonable profit." The industry is so important, its value in absorbing unskilled labour of so great an advantage, that it is a great surprise to those who believe in the professions of Ministers to find so little done to assist those who are endeavouring to develop it.

## Citation

### Len Bayliss, NZAE Life Member

Len Bayliss, then an economist at the Reserve Bank, played an important role in the creation of the New Zealand Association of Economists. Supported strongly by Alan Low, then the Bank's Economic Adviser, Len promoted this objective at the 1957 annual meeting of the Bank and university economists. His amplified proposal was well supported at the 1958 meeting, and Len became the Secretary of a promotion committee, chaired by Professor Horace Belshaw. The committee prepared a draft constitution which was sent to every known economist in New Zealand. This was further debated at an inaugural meeting at Victoria University College on 4th December 1958 which resolved unanimously to establish the Association.

Shortly after this, Len was seconded for a tour of duty with the Bank of England. In 1961, after a brief secondment to the Treasury, he joined the staff of the newly formed independent 'watchdog', the Monetary and Economic Council, for 5 years. He then became the Chief Economist of the Bank of New Zealand until 1982. He was selected to be a member of the Targets Advisory Committee of the National Development Conference in the late 1960s. In 1976, he was seconded for 20 months to the newly-formed Prime Minister's Advisory Group. After leaving the Bank in 1982, Len became an independent consultant. He was a director of the Hugo Group and of Integrated Economic Services. From 1983 onwards, he also became a director of a number of public companies, including the BNZ, Tower and BNZ Finance.

Len's resignation from the BNZ was a much publicised event as he had developed a high profile as a prolific and respected commentator on policy issues. His early magazine articles in the 1950s were often written under a nom-de-plume. However from 1963/64, when he first appeared on television, he was regularly engaged in public commentary and debate.

Monetary policy has always been Len's major interest. He was the major author of a Monetary Council report on the NZ financial system in 1966 which severely criticised existing policies and recommended orthodox alternatives. In the next decade, he campaigned vigorously against direct controls. His appointment to the Prime Minister's Advisory Group, led by Bernard Galvin, in 1975, gave him the opportunity to play a major role in effecting a major liberalisation of the financial system.

From 1978, Len vigorously promoted the case for wider economic liberalisation and was a strong critic of the "Think Big" programme. At a time when public criticism was muted, he made a significant contribution to preparing the ground for public acceptance of the need for reform. He has also been particularly active in public debate on issues of superannuation policy, pressing for public acceptance here of the OECD's approach to providing for retirement.

International recognition of his contributions was reflected in the award of a Senior Anzac Fellowship by Australia in 1985 and by other study awards from the governments of the USA, Japan and West Germany.

## OUT OF THE FRYING PAN...

In a Reuters report on 16 September 2005<sup>1</sup>:

*"Who Runs Your World?" was the question put by Gallup International and the BBC World Service to more than 50,000 people in 68 countries in what was billed as one of the biggest surveys of public opinion ever conducted... One of the most striking findings was international disillusionment with politicians. They achieved extremely low confidence ratings, with only 13 per cent trusting them. There was a global desire to put more power in the hands of intellectuals such as writers and academics, the survey showed.*

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<sup>1</sup> Reuters (2005) "Few people trust politicians, global survey shows", 16 September, <http://www.stuff.co.nz/stuff/0,2106,3412071a10,00.html>

## Two Extracts by Alfred Marshall

### Alfred Marshall on Demand and on Mathematics

From Marshall A (1890) *The Principles of Economics*, Book 3, On Wants and Their Satisfaction, Chapter 1<sup>1</sup>:

*Until recently the subject of demand or consumption has been somewhat neglected. For important as is the inquiry how to turn our resources to the best account, it is not one which lends itself, so far as the expenditure of private individuals is concerned, to the methods of economics. The common sense of a person who has had a large experience of life will give him more guidance in such a matter than he can gain from subtle economic analyses; and until recently economists said little on the subject, because they really had not much to say that was not the common property of all sensible people. But recently several causes have combined to give the subject a greater prominence in economic discussions.*

*The first of these is the growing belief that harm was done by Ricardo's habit of laying disproportionate stress on the side of cost of production, when analysing the causes that determine exchange value. For although he and his chief followers were aware that the conditions of demand played as important a part as those of supply in determining value, yet they did not express their meaning with sufficient clearness, and they have been misunderstood by all but the most careful readers.*

*Secondly, the growth of exact habits of thought in economics is making people more careful to state distinctly the premises on which they reason. This increased care is partly due to the application by some writers of mathematical language and mathematical habits of thought. It is indeed doubtful whether much has been gained by the use of complex mathematical formulae. But the application of mathematical habits of thought has been of great service; for it has led people to refuse to consider a problem until they are quite sure what the problem is; and to insist on knowing what is, and what is not intended to be assumed before proceeding further.*

### Alfred Marshall on Price Level Changes

In response to a query on the reasons for falling prices and the rise in the value of gold in the late 1880s<sup>2</sup> Marshall wrote:

*It is interesting to note the causes which Tooke gave (History of Prices, Vol. II. pp. 348-9) for "the decline and comparatively low range of prices from 1814 to 1837... Of Tooke's six causes, the first was a series of good harvests following on a series of bad harvests; we have to look in a different direction for the cause of the recent fall in the prices of agricultural produce. And his fourth cause, relating to a rise of the foreign exchanges, is inapplicable to present circumstances. But the remaining four causes are worth quoting in detail. They are --*

*"(2) The removal of obstacles from the several sources of foreign supply; a great extension of some of them; and the discovery of new ones.*

*"(3) A great reduction of the charges of importation, by the low freights and insurances incidental to a state of peace; and the improved, and cheaper, and more rapid internal communications.*

*"(5) Improvements in machinery, in chemistry, and in the arts and sciences generally, all tending to reduce the cost of production of numerous articles, or to provide cheaper substitutes.*

*"(6) A reduction of the general rate of interest, and a more extensive application of individual accumulations to reproductions at a diminished cost."*

*If to these we add the setting free of middlemen's stocks by the telegraph etc., and if we refer the fall of freights, etc. to the development of steam traffic rather than to the cessation of war risks, we have, I think, a very fair account of **those causes of the recent fall of prices which have not their origin in changes in the supply of money.***

<sup>1</sup> <http://socserv2.socsci.mcmaster.ca/~econ/ugcm/3ll3/marshall/prin/prinbk3>

<sup>2</sup> P.4 of Marshall A (1926) *Official Papers*, Published For The Royal Economic Society By Macmillan And Co., Limited St. Martin's Street, London, <http://www.questia.com/PM.qst?a=o&d=10349826>

## Structural Stability and Consistent Data Series by Stuart Birks

Forecasting in terms of time series or econometric estimation is very restrictive. It requires structural stability, which limits us to using only recent data. It also requires accurate data. Quite how limited the suitable data are is indicated below. We should be aware of the amount of potentially relevant information has to be set aside when using these forecasting techniques. For example, historical experience and commentary may be useful for identifying issues, relevant questions, and perspectives, and data from periods where structures were somewhat different may still be helpful, despite the structural changes. For example, they may provide the only information we have on responses to unusual events. We should therefore be thinking about alternative methods for incorporating such information into policy analyses and evaluations. So what of the data? Here are three illustrations of the problem.

### 1) Balance of Payments

Statistics NZ *Key Statistics* table 9.06 on the Balance of Payments highlights data measurement problems.<sup>3</sup> Taking the quarter with the largest (but not overly exceptional) problem as in the September issue of *Key Statistics*, we have these figures for the December 2004 quarter (\$m):

1) Current Account Balance	-3059
2) Balance on Capital Account	178
3) New Zealand Investment Abroad	-5038
4) Foreign Investment in New Zealand	672
5) Net Errors and Omissions	-2830

Reserve assets are considered in (3).

As [positive values of] (1) and (2) measure net inflows, (3) measures an outflow and (4) measures an inflow, we should have:  $(1) + (2) - (3) + (4) = 0$

The errors and omissions are equal to the extent to which the figures do not match.

Errors and omissions of nearly \$3 billion for a quarter may be a concern. Of equal concern is the change in net errors and omissions between the table given in the September issue and that in the October issue of *Key Statistics*. Instead of -\$2,830m we have -\$847m, a revision of \$2 billion. It might be suggested that these are recent data, but the March 2004 figure was also revised from \$331m to -\$540m, a change of \$871m.

### 2) Employment and Filled Jobs

Employment data are provided from the quarterly Household Labour Force Survey.

The industry coding system has recently changed from New Zealand Standard Industrial Classification (NZSIC) to the Australian and New Zealand Standard Industrial Classification (ANZSIC) and the data are not comparable.<sup>4</sup> Also:

*"An additional impact of the change is that it will no longer be possible to provide NZSIC statistics. However, this should not present a major problem for users, given that the NZSIC system is now somewhat dated, and a six-year ANZSIC time series is available."*

There would seem to be data problems preventing us from having long series to use for model estimation and forecasting. Also, it seems that structural change is such that we might not want to be using data from any extended time period as a basis for estimation, and presumably we cannot forecast far ahead on the basis of structural stability.

Not only are there classification issues, but we also have two distinct data sources on jobs:

- i) The **Household Labour Force Survey** (HFLS) gives figures on **"employment"**.
- ii) The **Quarterly Employment Survey** (QES) gives figures on **"filled jobs"**.

The QES does not include agriculture, although it does include forestry and mining. Agriculture Forestry and Fishing combined provided about 7% of total employment in June 2005, so the omission is likely to be less than that. There are some other measurement differences between the series.

In June 2005, total employment is estimated at 2,052,600, while total filled jobs equals 1,650,200. In Education, there were 130,500 filled jobs, compared to 165,800 employed.

<sup>3</sup> The tables from the September and October issues are attached.

<sup>4</sup> <http://www.stats.govt.nz/products-and-services/papers/hlfs-changes-to-industry-coding>

How confident can we be when using such figures for analysis?

### 3) Incomes

Data on incomes are provided in the QES and the New Zealand Income Survey.

On 13 October there was a piece on National Radio about the gender pay gap. It referred to new data released by Statistics New Zealand. Newstalk ZB also covered the issue<sup>5</sup>:

*Unions are expressing dismay at the widening gap between men's and women's pay...Overall, women earn 82 percent of what men do - down from 86 percent in 2004. Council of Trade Unions Vice President, Helen Kelly, says the growing gap is significant and of huge concern.*

National Radio had Shenagh Gleisner (Chief Executive of the Ministry of Women's Affairs) and Judy McGregor (Human Rights Commissioner for EEO) talking on the matter.

Data from the June Quarterly Employment Survey were released on 8 August, and from the Income Survey on 6 October. The 82 percent figure can be calculated from table 10 of the June Income Survey spreadsheet. However, the two sources give very different figures.<sup>6</sup> The table shows average hourly earnings from both sources (for June, employment survey data are for total hours combining ordinary and overtime rates). While the Income Survey showed a fall of about 4% in the gender pay gap, the QES showed a rise of nearly 1%.

	Emp Survey		Inc Survey	
	2005	2004	2005	2004
Male	22.31	21.65	21.16	19.58
Female	19.32	18.58	17.35	16.80
F/M%	86.60	85.82	81.99	85.80

The Income Survey covers about 800 men and 800 women. The QES technical notes

state, "QES statistics are derived quarterly from approximately 18,000 surveyed business locations in a range of industries and regions throughout New Zealand." They also point out that median measures are probably a better indicator than averages because of the skewed distribution of earnings.

Median income was mentioned in a comment on the Income Survey<sup>7</sup>:

*Commentary ...*

*Median hourly earnings also rose, up \$0.76 to \$16.10, with increases of \$1.00 (to \$17.50) for males and \$0.60 (to \$15.00) for females. Comparing female earnings with male earnings, the ratio of median hourly earnings was 85.7 percent in the June 2005 quarter. When the survey began, in the June 1997 quarter, this ratio was 83.0 percent. It reached its highest point in the June 2002 quarter (87.8 percent), but has been falling slowly since.*

In summary, there are conflicts between the two sources, and the Income Survey gives different results when considering average and median incomes.

We could also ask whether a chief executive of a Ministry should be selectively using data to publicly take what could be considered a political position.<sup>8</sup> Would such a person be giving fair and balanced advice to her Minister?

<sup>5</sup> NewstalkZB (2005) "Pay Gap Between Sexes Widening", 12 October, <http://xtramsn.co.nz/news/0,,11964-4884147,00.html>

<sup>6</sup> In the technical notes to the June 2005 QES, Statistics New Zealand point out, "It is important to note that the data from the New Zealand Income Survey is not directly comparable with the QES." <http://www2.stats.govt.nz/domino/external/pasfull/pasfull.nsf/7cf46ae26dcb6800cc256a6200a2248/4c2567ef00247c6acc2570540016f914?OpenDocument>

<sup>7</sup> <http://www2.stats.govt.nz/domino/external/pasfull/pasfull.nsf/7cf46ae26dcb6800cc256a6200a2248/4c2567ef00247c6acc25709100182692?OpenDocument>

<sup>8</sup> Paradoxically, it was Ruth Dyson, formerly her Minister, who presented a more guarded view of the data. See Wood A (2005) "Gender pay gap 'dangerous' for families", *The Press*, 14 October, <http://www.stuff.co.nz/stuff/0,2106,3442878a11,00.html>



**And While on the Topic, Here are Some More Data Changes:**

1) From the Commentary on the June 2005 Quarter “Hot Off the Press” report on the Economic Survey of Manufacturing<sup>9</sup>:

***Discontinuity in the meat and dairy product manufacturing industry***

*Restructuring within the dairy industry has resulted in a discontinuity in both the meat and dairy product, and the total manufacturing series. Prior to the September 2002 quarter, the main dairy product manufacturers in New Zealand sold their export products to a producer board, which then exported the products. Products were sold to the producer board when they were produced. Dairy product manufacturing sales tracked the production cycle and included an end-of-year payment in the June quarter. From the September 2002 quarter, dairy manufacturers have been able to export directly and have had the ability to build up stocks. The result is that dairy product manufacturing sales are now more likely to track dairy product export sales than the production cycle...*

2) And from: <http://www.stats.govt.nz/quick-facts/industries/manufacturing-stats.htm>, “The latest manufacturing census was in 1994-95”. There is now an annual enterprise survey, but this covers the whole economy at a highly aggregated level. The 2004 results can be found at: <http://www2.stats.govt.nz/domino/external/pasfull/pasfull.nsf/7cf46ae26dcb6800cc256a62000a2248/4c2567ef00247c6acc257092000bf34e?OpenDocument>

Table Builder has some more detailed data, but after 2003 they switched from counting employment in terms of full-time equivalents to using the number of employees.

3) From p.12 of Business New Zealand (2005) *Manufacturing Perspectives*<sup>10</sup>:

*In recent years manufacturing’s share of GDP has reduced, both in New Zealand and many other developed countries. In part this is because many manufacturing firms now outsource their HR, accounting, transport, maintenance, cleaning and other service functions: an OECD report in 2000 noted that manufacturing firms accounted for two-thirds of total outsourcing in the economies of developed countries...As well, technological development and productivity growth in the manufacturing sector have reduced the cost of manufactured goods, a further reason for the decline in manufacturing’s contribution to GDP.*

There are two important points about perceptions here. 1) The size of the sector depends on the measure and the extent of division of tasks within and between organizations. 2) Contribution to GDP can fall because of improved productivity, and it does not necessarily reflect quality changes as it is only based on prices.

4) And here is something else to look out for<sup>11</sup>:

***Why is the Budget now presented GST-exclusive?***

*The Public Finance Amendment Act passed in December 2004 requires expenditure items in the 2005/06 Estimates to be shown on a GST-exclusive basis (except existing multi-year appropriations). Spending was previously appropriated as GST inclusive, where applicable.*

*Although the Government pays out GST on appropriations, it then receives it back through the tax system. It is a neutral transfer. Removing GST from appropriations better reflects net government spending in a particular area. This change does not affect the fiscal forecasts in the Economic and Fiscal Update as these have always been presented GST-exclusive.*

*In comparing past funding levels with current funding levels, please keep in mind the removal of GST from 2005/06.*

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<sup>9</sup> Statistics New Zealand (2005) “Hot Off the Press Economic Survey of Manufacturing June 2005 quarter Commentary”, 16 September, <http://www2.stats.govt.nz/domino/external/pasfull/pasfull.nsf/7cf46ae26dcb6800cc256a62000a2248/4c2567ef00247c6acc25707d007e119f?OpenDocument>

<sup>10</sup> At <http://www.businessnz.org.nz/file/897/MANUFACTURING%20PERSPECTIVES.pdf> and [http://www.ema.co.nz/071205\\_Manufacturing\\_Perspectives.pdf](http://www.ema.co.nz/071205_Manufacturing_Perspectives.pdf)

<sup>11</sup> <http://www.treasury.govt.nz/budget2005/summary/newspending.asp#overview>



# ANNOUNCEMENT

## The A R Bergstrom Prize in Econometrics: 2005

We are pleased to announce two awards for the **A R Bergstrom Prize in Econometrics** for 2005: to **Ryan Greenaway-McGrevy**, PhD student, University of Auckland, for his paper "Evaluating Long Horizon Forecasts"; and to **Leo Krippner**, PhD student, University of Waikato, for his paper "A New Framework for Investigating the Relationships between the Yield Curve, Output and Inflation".

The object of the Prize is to reward the achievement of excellence in econometrics, as evidenced by a research paper in any area of econometrics. The Prize is open to New Zealand citizens or permanent residents of New Zealand who, on the closing date for applications, have current or recent (i.e. within two years) student status for a higher degree. The Prize is awarded once every two years, with a value of NZ\$1,500.

The citations that accompany each award read as follows:

**Ryan Greenaway-McGrevy's** paper addresses the important question of why the long horizon regression often produces forecasts that are more accurate than iterative VAR forecasts. It is shown that in the presence of estimator inconsistency, the probability limit of a long horizon forecast cannot be greater than that of an iterative VAR forecast, because the iterative VAR is misspecified. Results from small sample Monte Carlo experiments show that the long horizon forecast performs particularly well under negative endogeneity, and suggest that a long horizon forecast approach is an attractive alternative to iterative VAR forecasts.

**Leo Krippner's** paper presents theoretical and empirical work, designed to provide a new, more rigorous framework for relationships between the yield curve, output and inflation. The underpinning macro-finance literature in this area is in its infancy, and this paper works to develop a volatility-adjusted orthonormalized Laguerre polynomial (VAO) model which encompasses the Nelson-Siegel class of yield curve model as a specific case, and to reflect a more specific economic underpinning akin to the generic affine model of Berardi and Esposito. The in-sample empirical results from a VAO(3) model, provide a useful initial contribution towards the long-term aim of providing a manageable additional tool for central banks, when evaluating their projections and monetary policy decisions.

The Adjudication Committee for the 2005 Award comprised Professor Viv B Hall of Victoria University of Wellington, Professor Les Oxley of the University of Canterbury, and Dr Jin Seo Cho of Victoria University of Wellington.

V.B. Hall & P.C.B. Phillips  
October 2005

The Prize is supported by funds provided by the following sponsors:

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In addition, royalties from the Festschrift Volume *Models, Methods and Applications of Econometrics: Essays in Honour of A.R. Bergstrom*, P.C.B. Phillips (ed.) Blackwell, Cambridge MA and Oxford UK, 1993, are applied to support the prize.

## Democracy and Parliament

### 1) Rousseau on democracy:

*...there is no government so liable to civil war and internecine strife as is democracy or popular government, for there is none which has so powerful and constant a tendency to change to another form or which demands so much vigilance and courage to maintain it unchanged.*<sup>1</sup>

**2) and a view by Celia Feinnes**, in the preface to the description of her travels through Britain about 1697, where she writes of the value of travel in Britain, including:

*But much more requisite is it for Gentlemen in the service of their country at home or abroad, in town or country, Especially those that serve in parliament to know and inform themselves y<sup>e</sup> nature of Land, ye Genius of the Inhabitants, so as to promote and improve Manufacture and trade suitable to each and encourage all projects tending thereto, putting in practice all Laws made for each particular good, maintaining their priviledges, procuring more as requisite; but to their shame it must be own'd many if not most are Ignorant of anything but the name of the place for which they serve in parliament; how then can they speake for or promote their good or Redress their Grievances ?*<sup>2</sup>

**3) and this from Richard Prebble's valedictory speech**, 28 July 2005<sup>3</sup>:

*When I first arrived and knew nothing I received half an hour for my maiden speech and now under the Standing Orders my valedictory is officially 10 minutes. Most speeches are just 5 minutes. I defy anyone to explain ACC reform, the Resource Management Act Amendments or taxation changes in 5 minutes.*

*There are many MPs, through no fault of their own, who have not spoken in total 20 minutes this session. They cannot represent their constituents or give value for the cost to the taxpayer of an MP in less than 20 minutes a year. Our parliament does not sit long enough.*

*While we meet for more days of the year than the great parliaments, we are in session for fewer hours. The most powerful legislature, the US senate, still has unlimited speaking time but they meet all hours and even on Sunday. To be a real check on the executive, this House must meet for more hours.*

*Not to pass more laws, there are already 1,441 Acts of Parliament and an estimated 40,000 pages of Statute Law and that's not counting the 2,850 regulations in force. No wonder small business complains of red tape. No MP could possibly read all the legislation we pass each year.*

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<sup>1</sup> From Book III, Chapter 4 of Rousseau J-J (1968) *The Social Contract*, Harmondsworth: Penguin, translated by Maurice Cranston. The original was published in 1762.

<sup>2</sup> [http://www.visionofbritain.org.uk/Travellers/chap\\_page.jsp?t\\_id=Fiennes&c\\_ID=2&cpub\\_ID=0](http://www.visionofbritain.org.uk/Travellers/chap_page.jsp?t_id=Fiennes&c_ID=2&cpub_ID=0)

<sup>3</sup> In Hansard, plus: <http://www.act.org.nz/news-article.aspx?id=27253>

## Democracy in Small Nations

AI No.23 (pp.10-11) described how New Zealand governments may have limited choices when selecting ministers. This is with 120 or more MPs in Parliament. How much more constrained will smaller nations be?

**Fiji** has a 71 member House of Representatives and a 32 member Senate.

**Tonga** has a Parliament of 30: *The King and the Legislative Assembly have the power to enact and repeal laws. The assembly comprises the 12 Cabinet Ministers, nine representatives of nobles and nine representatives of people.*<sup>1</sup>

**The Cook Islands** has a Parliament of 25, *The Cook Islands Parliament is based on the Westminster system with a 25-member Parliament and prime minister as the head of government. The cabinet consists of seven ministers.*<sup>2</sup>

**Samoa** has a Legislative Assembly of 49, with a Cabinet of no fewer than 8 and no more than 12. Interestingly, universal suffrage to Samoans 21 and over was granted in 1990.

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<sup>1</sup> <http://www.pmo.gov.to/index.php/articles/58>

<sup>2</sup> <http://www.the-cook-islands.com/tourist-information/government.html>

## Miscellaneous

### A French Revenue Raiser (and Gender-Based Taxation)

From p.5 of *The Daily Southern Cross* of 29 July 1865 (See PapersPast at: <http://paperspast.natlib.govt.nz>), an extract from *The Times* comparing the French and English armies. There were objections in the French Legislature about the burden of the army:

*The complaints of the remonstrants referred not so much to the pecuniary charge of the army as to the burden entailed by the system of conscription and its incidents...though the system of substitutes is now well established, it only implies so much taxation. A man who declines to serve in person pays in money, so that an excessive levy represents a proportionate tax.*

(The “excessive levy” refers to the large number of men called up.)

### A Fixed-Price Contract

By the late 1200s, serfdom was being phased out in England, as illustrated in a document from 1278 by the Abbey of Peterborough.<sup>1</sup> I wonder if his heirs still farm the same land:

*Let all know that we have manumitted and liberated from all yoke of servitude William, the son of Richard of Wythington whom previously we have held as our born bondman ... We will moreover and concede that he and his heirs shall hold the messuages, land, rents, and meadows in Wythington which his ancestors held from us and our predecessors...-that he shall have and hold these for the future from us and our successors freely, quietly, peacefully, and hereditarily, by paying thence to us and our successors yearly 40s. sterling, at the four terms of the year, namely; at St. John the Baptist's day, 10s., at Michaelmas, 10s., at Christmas, 10s., and at Easter, 10s...*

<sup>1</sup> <http://www.fordham.edu/halsall/source/manumission.html>

### Workplace Health - Grinder's asthma

*'Grinders are subject to the casualty of stones flying in pieces while in rapid revolution, by which they are often killed on the spot; and also to a fatal disease called the "grinder's asthma," created by the inspiration of the particles of steel thrown off in grinding.*

*'The asthma is fatal to all the class; so that in a class of men, amounting to several thousands, few arrive at the age of forty-five, and very few survive forty-five! When grinding was not a distinct branch of business, but was performed by men who were engaged in other departments, and who were exposed only for a short time to the grinding wheel, the "grinder's asthma" was not known as a disease peculiar to the grinders; but when, by the division of labour, grinding became a sole employment, several grinders were observed to die to complaints nearly similar, now common, and called the "grinder's asthma." About thirty years ago, the steam-engine was first adapted for the purposes of grinding; and then the grinders worked in small low rooms, where there were ten or twelve stones, while the steam-engine, unlike the stream which formerly supplied the wheel, allowed no period of relaxation. Hence, at the present time, out of twenty-five hundred grinders, there are not thirty-five who have arrived at the age of fifty; and not double that number who have reached forty-five. . . . After lingering through months, and even years of sickness, the grinder dies: but as they are in general aware that their life must be short, many of them think it ought at least to be merry; hence they abandon themselves to habits of intemperance and dissipation.'*

From Allen T (1831) *A New and Complete History of the County of York*, London: Henton, Vol. iii, p.33-40 [reprinted in Evans L and Pledger P J (1966) *Contemporary Sources and Opinions in Modern British History*, Vol.1, Melbourne: Cheshire, p.6]

### Reward and Effort

From p.36 of Barber W J (1967) *A History of Economic Thought*, London: Penguin, discussing Adam Smith and labour as a basic measure of value:

*Smith was drawing attention to a highly relevant point that now receives little direct attention in the analysis of long-period economic change: namely that the extent of economic improvement should be judged not solely by changes in the size of the total bundle of goods but also in the effort required to produce the bundle.*

**Lessons from Health Economics, the AHES Conference,  
Auckland, 29-30 September [SB]**

The Australian Health Economics Society held its conference in Auckland on 29<sup>th</sup> and 30<sup>th</sup> September. Here are a few brief observations.

Parallel sessions had the luxury of twenty minutes for presentation, ten minutes for a discussant, and ten minutes for discussion from the floor. There was a common feature to many of these sessions in that the discussants seemed the most interesting. There was a reason for this. Generally, papers report on detailed analyses that involved estimating models or gathering large amounts of data through surveys. Inevitably, there are limitations to these approaches, and many simplifying assumptions have to be made so as to draw conclusions. It is hardly surprising, then, that someone else can challenge the findings merely by pointing out the simplifications, omissions, distortions and other shortfalls, such as alternative interpretations, lack of generality, and questionable policy significance. All this is only to be expected, as indicated by the editorial to this issue of *AI*.

Presenters can avoid this problem by giving a paper which, for a particular approach or set of studies, highlights the simplifications, omissions, distortions, etc.. One such paper (by Tim Moore) was very appealing. It discussed “cost of illness” studies. While he took a positive view, suggesting how they could be improved, the comments could be interpreted rather as indicating the weaknesses of many such studies. The discussant (Marian Shanahan) still managed to point out some additional weaknesses of these studies, such that improvements may be undesirable. She emphasised the political appeal of cost of illness studies. It is easy to get public outrage and political attention by putting out study findings claiming costs of billions of dollars. They are not very helpful, though. They say nothing about options for reducing the amount of illness, or the costs of those options. Similar criticisms could be raised about studies, such as Susan Snively’s, on the costs of family violence.

Coincidentally, there was a piece in the *Dominion Post* of 3 October, “Arthritis costing NZ \$2.3 billion a year”<sup>3</sup>:

*The study, the first to examine the costs of the disease in New Zealand, was commissioned by Arthritis New Zealand. The group hopes the findings will convince the Government to boost funding for arthritis services.*

Another paper (by Ian McRae) looked at the GP labour force in Australia. Much has been made of the increase in the proportion of female GPs, along with their shorter working hours. This means that more GPs will be needed to replace retiring men. However, this study also found that older GPs (including men) put in fewer hours, so there is a work effort aspect to the aging GP workforce, and also younger male GPs are also seeing fewer patients and working shorter hours. This latter point could be very significant. Is the increase in female workforce participation (and changing gender roles) leading to men reducing their commitment to work so as to more closely match women's attitudes to work? This could have far-reaching implications. A colleague also suggested that, with later retirement, workers may pace themselves more through their working lives.

A third paper (by Bruce Hollingsworth) indirectly illustrated a point in the piece in this *AI* by Gail Pacheco on minimum wages. It is one thing to identify a statistical association between two variables, and quite another to use that as a basis for policy interventions.

To give fictitious data, imagine a prevalence of 18 percent for some negative measure for low income groups, compared to 16 percent for high income groups. This indicates a possible relationship between income and the prevalence of this problem. Does this justify policies to improve the income of low income groups? Quite aside from the issue of the costs of the problem and the costs of alleviating the problem, income may be the wrong measure to look at. Changing income may not be effective, and even if it is, the best that could be achieved is a two percent improvement for those on low income, and no gain for those on high income. We might consider this to be fairly minimal in terms of addressing the problem.

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<sup>3</sup> Saunders A (2005) “Arthritis costing NZ \$2.3 billion a year”, *The Dominion Post*, 3 October, <http://www.stuff.co.nz/stuff/0,2106,3430680a11,00.html>

## Restorative Justice

While there is currently talk of restorative justice, it relates to individual offenders and victims. There is a reference to a system operating at the time of King Alfred of Wessex (the late 800s) in Stenton F M (1947) *Anglo-Saxon England* (2<sup>nd</sup> edn), London: OUP:

*Among the English, as among all Germanic peoples, it was a fundamental convention that the killing of a free man brought his kin into immediate action in order to avenge his death, or to enforce the payment of his wergild....[U]nlike most continental codes, Old English legal sources never offer any definition of the kin...There is just enough evidence to show that in King Alfred's time it included maternal as well as paternal kinfolk, and a legal text of the twelfth century makes it plain that the former paid one-third, and the latter two-thirds, of any wergild which fell on the family group. The association of the father's and the mother's kin in the payment, and it may be added, in the receipt, of the wergild... (p.312)*

## The French Finally Catch Up with the English

The Magna Carta brought a uniform system of weights and measures to England in 1215.

Clause 35 of the Magna Carta reads:

*Let there be one measure of wine throughout our whole realm; and one measure of ale; and one measure of corn, to wit, "the London quarter"; and one width of cloth (whether dyed, or russet, or "halberget"), to wit, two ells within the selvedges; of weights also let it be as of measures.*<sup>1</sup>

France achieved the same through an announcement by the National Convention in 1793<sup>2</sup>:

*The National Convention, convinced that uniformity of weights and measures is one of the greatest benefits that it can offer to all French citizens...decrees the following:*

*Article 1. The new system of weights and measures, based on the measure of the Earth's meridian and on decimal division, will be uniformly used in the whole of the Republic.*

<sup>1</sup>This version is from: <http://www.cs.indiana.edu/statecraft/magna-carta.html>

<sup>2</sup>From *Gazette nationale ou le Moniteur universel*, no. 214, 2 August 1793, vol. 17, p. 287, reproduced at pp.86-87 of Dwyer P G and McPhee P (eds) (2002) *The French Revolution and Napoleon: a sourcebook*, London : Routledge.

## Helen Clark on Mothers – Was She Consistent?

In the Leaders' Debate on TV3 on 11 August 2005, Helen Clark said:

*One of the things about Working for Families is to make it possible to have a one income family where one partner, if they choose, to stay home with the children. That's how it's structured, is it's the greatest benefit to one income families, and we want our people to have that choice, if they want to stay home and look after their kids, and many make that choice, so we're supporting that choice.*

This should be compared to her Statement to Parliament of 1 February<sup>1</sup> where she called for increased female labour force participation:

*In last year's Statement I highlighted the need to increase women's participation in the workforce, and a number of steps have been taken to do that. The Working for Families Package means that a single parent family, for example, along with other family types, will always be better off at work, full or part time, than being dependent on a benefit... thousands more families have got help with their childcare costs. That helps more women return to work. But still more needs to be done.*

<sup>1</sup> <http://www.beehive.govt.nz/ViewDocument.cfm?DocumentID=22087>



# research in progress...

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

## ... economic research at the University of Otago as at November 2005.

Compiled by Chris Haig ([CHaig@business.otago.ac.nz](mailto:CHaig@business.otago.ac.nz))

**Robert Alexander:** i) (with Yingtong Guo, Jilin University) *Savings, growth and investment across Chinese regions* - this project analyses the correlations among saving, investment and growth rates across the provinces of China and examines how Chinese saving behaviour is related to the under-development of social security and insurance markets in that country.

ii) (with Arlene Ozanne) *Ageing, wealth and the property market* - as part of a general examination of the economic effects of an ageing population in the New Zealand context, we study the evolution of real estate prices and wealth.

Stephen Dobson: (**with Peter Dawson, University of Bath**) *Patterns of managerial employment and re-employment* - using data on English football managers this study seeks to determine whether there are important characteristics that systematically affect displacement duration.

**David Fielding:** i) (with S. Torres, University of Leicester) *Structural models of social and economic development* - this project extends existing work on inequality and economic development by developing structural models to identify bi-directional relationships between income inequality and other indicators of social and economic development.

ii) (with A. Shortland, University of Leicester) *Economic consequences of the Intifada* - this project looks at the different ways in which the intensity of the Israeli-Palestinian conflict interacts with economic factors. It includes studies of the impact of the conflict on different sectors of the Israeli economy, on investment and on capital flight.

iii) (with P. Mizen, University of Nottingham) *Relative price variability and inflation* - this project examines the functional relationship between relative price variability (RPV) and inflation deriving some implications for monetary policy. We examine the empirical evidence using several alternative non-parametric procedures and derive implications for the 'optimal' value of inflation that minimizes RPV.

**Murat Genç:** *Box-Cox transformation in estimating production functions* - the aim of this project is to investigate the performance of Box-Cox transformation in estimating production functions using Monte-Carlo simulations to compare the performance of Box-Cox transformation with other flexible functional forms.

**Paul Hansen:** i) (with Franz Ombler, Point Wizard Ltd) *A new method and software for scoring additive multiattribute value models with ordered categorical attribute scales (also known as 'point' or 'scoring' systems)* - the method and software, which we refer to as COMPAIR ('COMplete PAIrwise RAnking') and *Point\*Wizard* respectively, involve only pairwise rankings of alternatives, from which single attribute value scores ('points') are obtained. While minimising the decision maker's processing load in terms of the number of pairwise rankings explicitly performed, potentially *all*  $N(N - 1)/2$  pairwise rankings for  $N$  alternatives are identified (thereby defining a complete overall ranking), where  $N$  can be all possible alternatives representable by the model being scored or a subset of alternatives. New Zealand and international patents are pending.

ii) (with Julian Hayes, Dunedin School of Medicine) *Cost-utility analysis of laparoscopic-assisted colectomy for cancer* - there is good evidence that, compared to open colectomy (OC), laparoscopic-assisted colectomy (LAC) results in improved short-term clinical outcomes, and in the case of cancer, equivalent long term survival. In the context of the New Zealand public hospital system, the next issue is the relative costs of the two procedures. In particular, relative to OC, is LAC cost-effective? The aim of this study is to answer this question.

**Mohammad Jaforullah:** *A comparison of production frontier methods using Bangladesh handloom textile industry data* - a number of production frontier models can be formulated and estimated to obtain a measure of technical efficiency of an individual firm or an industry. The aim of this study is to investigate whether and to what extent technical efficiency measures from different widely used models vary from one another.

**Alan King:** *Uncovered interest parity and exchange risk* - this project investigates the theoretical implications of the nature of exchange risk on the risk-adjusted uncovered interest parity (RAUIP) relationship and attempts to establish whether it is likely that RAUIP may actually be a dis-parity relationship in practice. The implication of such a finding would be that the actual risk premium would not then be observable.

**Stephen Knowles:** i) *Social capital and foreign aid* - the aim is to determine whether countries with high levels of social capital give more foreign aid than others. It is often argued that in countries with high levels of social capital (as measured, for example, by trust, civic norms and membership of community groups) levels of cooperation and altruistic behaviour will be higher. This research explores whether such altruistic behaviour extends to giving foreign aid.

ii) *Social capital and informal and formal institutions* - there is a growing literature which analyses, using cross-country data, whether institutions or geography is the most important deep determinant of economic development. This research project adds informal institutions, which it is argued is a similar notion to social capital, to the list of potential deep determinants of economic development.

**Dorian Owen:** i) (with Clayton Weatherston) *Fundamental determinants of economic growth and development* - a new generation of empirical studies has recently attempted to identify the fundamental factors that underpin long-term growth and development. The key contenders are a country's geographical characteristics, the quality of its institutions, the extent of its integration with world markets, and the soundness of its macroeconomic policies. This project applies recent developments in the methodology of econometric model selection to test, in a more rigorous manner, what fundamental factors matter most for different aspects of economic development.

ii) (with Clayton Weatherston) *Model selection methods in empirical growth modelling* - this research examines different aspects of the problems involved in selecting useful empirical growth models in the light of recent criticisms of existing practices in the empirical growth literature.

**Arlene Ozanne:** i) *The determinants of international labour migration to New Zealand* - this study aims to provide empirical evidence on the economic and non-economic factors that play a role in the migrant worker's decision to migrate at the individual and household level by examining macro data for New Zealand.

ii) *Do immigrants lower the wages of natives? A case study of New Zealand* - this study re-examines the economic impact of migrant workers on the local labour market. The approach taken is based on the analysis of relative changes in average wage rates of different skill and age groups of workers.

**Carlyn Ramlogan:** (with John Goddard, University of Wales, Bangor) *Convergence in the developing world* - building on previous cross sectional estimates, this research uses a number of panel unit root tests to test the convergence hypothesis across countries in Latin America, Africa and Asia. The sensitivity of the results to the different tests is also analysed.

**Frank Stähler:** i) (with Thorsten Bayindir-Upmann, University of Bielefeld) *Market entry regulation and international competition* - for a closed economy, it is well known that entry is socially excessive in a homogeneous commodity market implying that each incumbent firm's output is too low. However, the question of optimal market entry regulation becomes more complicated in an international setting, in particular if countries are not symmetric. In such a



framework, the political issue of whether to allow for market entry or to regulate market access is superimposed by strategic considerations. We investigate how governments may strategically (ab)use market entry regulation as a substitute for trade policy.

ii) (with David de Meza, London School of Economics) *Free entry, investment and social inefficiency* - standard models of oligopolistic competition and free market entry assume that each active firm has to carry a fixed cost and that entry decisions are made such they are common knowledge when it comes to output decisions. We consider the less investigated case that the size of entry costs determines the marginal cost of production. In this sense, an entrant invests in a certain technology with entry. Furthermore, we distinguish two cases. In the first case, entry decisions and output decisions are made simultaneously in sense of a simultaneous choice of technologies and capacities. In the second case, these decisions are made sequentially so that technology choices are common knowledge before output levels are determined. We then investigate how the results differ from the social optimum.

**Paul Thorsnes:** i) (with Paul Sicilian, Grand Valley State University) *A property-rights approach for unifying the teaching of externalities, moral hazard, and market power* - we show how several concepts that are treated separately in general economics texts – externalities, moral hazard, and collusion – submit to a unified approach based on a standard analysis of property rights. Unifying the analysis of these concepts is time-efficient and emphasizes the common economic intuition, reinforcing economic principles while demonstrating the power of basic economic reasoning.

ii) *Allocating residential land to nature reserves: Large-lot and cluster zoning vs. a market in development rights* – a regulatory floor on lot size (large-lot zoning) offers an administratively easy way to limit development densities that equitably distributes the resulting rents. Cluster zoning, which restricts the number of lots on a large parcel but not their size, gives the land developer flexibility in the allocation of land, increasing efficiency and aggregate rents. A market in development rights extends this flexibility across parcels, while maintaining the equitable distribution of rents. The land-development authority can influence the land allocation through standard tools: zoning and placement of infrastructure. However, the cluster-zoning allocation may prevail as developers choose to preserve land on site to capture proximity benefits.

**Niven Winchester:** i) *The economic impact of proposed changes in the global trading environment on the New Zealand economy* – this research takes stock of how several proposed changes in the contemporary global trading environment will influence New Zealand by drawing on a model of global production and trade.

ii) *Capital-skill complementarity and rising wage inequality in the UK* - the consensus in the literature investigating the causes of increased wage inequality in developed nations since 1980 is that skill-biased technical change is responsible for the widening of the wage distribution. A shortcoming in this literature is that technical change is commonly determined residually; that is, those changes in relative wages unexplained by other factors are attributed to changes in technology. This research addresses this problem by specifying a CGE model that accounts for complementarities between capital and skilled labour, which allows changes in technology to be specified in terms of changes in factor endowments.

***Treasury Working and Policy Perspective Papers***

***The latest papers are listed at:***

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

## New Zealand Economic Papers

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

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

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

Write to: [ip.king@auckland.ac.nz](mailto:ip.king@auckland.ac.nz)

*Unfortunately the June 2005 issue (Volume 39 #1) has been delayed, but will be posted out about the end of this year, with the December issue also being a few months late. After that it is hoped that we will be just about back on schedule.*

## ...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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**W**elcome! to the following people who have recently joined NZAE...

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