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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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# *The Way Forward*

## EDITORIAL

Well, this is our first attempt as new editors. We would like to thank all the contributors to this issue. Their willing participation is due in no small part to the groundwork done by the original editor, Nancy Devlin. She has done an excellent job in getting *Asymmetric Information* started and through its first five issues. We hope that we can continue in that tradition.

Our aim is to inform and to generate discussion on areas of interest. If you feel motivated to respond to any of the topics raised in this issue, please email us. There is certainly more to be said on future directions for economics as a profession in New Zealand and on the quality of policy advice.

We can also include notices of speakers, conferences, appointments, awards, courses, etc..

Any other suggestions would be gratefully received. For example, one possibility is to publicise possible seminar presenters, either visitors to New Zealand or members who would like to sound out their ideas to other economists in the country.

by Stuart Birks and Gary Buurman, Massey University

### **Wishing John Yeabsley a Speedy Recovery**

Members of the Association were concerned to hear about John's heart attack when he was in Botswana. It is a great relief to know that he is recovering well. Our thoughts and good wishes go out to him and his family. We hope to see him once again fit and running along Lambton Key in the not too distant future. Take care, John.

From the Council and members of the NZAE

### **New Zealand Economic Papers Progress Report from Frank Scrimgeour**

There are numerous publications at various stages of review but currently there is no backlog of new submissions. Papers have been accepted for publication in NZEP December issue from:

- 1) Prof Les Oxley, Waikato Management School, University of Waikato
- 2) Prof John Creedy, University of Melbourne
- 3) Prof S Haslett (Massey University) and Dr M Pickford (Commerce Commission)

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.

# Is Economics a Profession?

by Veronica Jacobsen (veronica.jacobsen@nz.arthurandersen.com)

Professions typically discipline themselves voluntarily by adopting ethical standards or, alternatively, seek government enforcement of those standards on the grounds that poor quality services can cause harm to the client. This of course was the basis for the oath instituted by the students of Hippocrates after he died. Hippocrates had instructed all comers in medicine, so that by the time he died there was a glut of practitioners on the market. It was not coincidental that the oath also included a clause restraining trade by limiting those who could be instructed in medicine.

This combination of potential harm and monopoly provision underlies regulated occupations that designate themselves as 'professions'. At the same time of course, it applies equally to other regulated trades from real estate agents in New Zealand to barbers in North Carolina.

Is economics a profession and should it be regulated? I used to start discussions with other professionals on the subject of regulation with a tongue-in-cheek diatribe against the 'know-nothing cowboy economists' out there in the market providing poor advice that harmed the clients, under-cutting higher quality economists (such as me, of course) and bringing economists in general into disrepute. I would end with a passionate call for strict regulation of economists by a professional body as the only means of ensuring standards and protecting clients. The problem with this sort of disingenuous approach, was that I got a lot of sympathetic noises and total agreement that regulation was the way to go.

Of course the argument was, and is, spurious. While it may be true that poor economic advice can cause harm, the important question is to whom the advice is

being given. Most regulated professions implicitly, and sometimes explicitly, assume that the client is poor and ignorant with no means of judging the quality of the advice. Calls to regulate lawyers for example are based on a 'need' to protect the unemployed pregnant solo mother, conveniently ignoring the effect of monopoly regulation on the price she has to pay for these 'high quality' services (and that she may use cheaper, unregulated substitutes or no advice at all) and the fact that other clients, such as large corporates, hardly need the same level of so-called 'protection'.

Unlike legal, financial or medical advice, economic advice is seldom provided to individuals. Clients are typically corporates, industry organisations, governments, NGOs and intergovernmental agencies such as the World Bank. They have both the incentives and the capacity to judge the quality of the advice they have been given by their consultants and their employees. Naturally, certain information such as level of education (BA or PhD?) and university (Harvard or Chicago?) are useful as an (imperfect) means of initial screening. Membership of a regulated profession generally depends on the achievement of certain qualifications, so that membership itself provides little additional information to prospective clients or employers. Additional professional examinations often simply represent a means of licensing new entrants so that the licence can be revoked for breaches of professional regulations.

These professional regulations are themselves typically designed more to protect the profession than the clients. They create barriers to entry that restrict

others from offering the same services (limiting external competition) and create limits on internal competition by measures such as bans on advertising, limiting the structure of firms to partnerships, restricting the services that can be provided or even reviewing prices.

Like other goods and services, the strongest mechanism for assuring quality of economic advice is the competitive market. The market for economic advice soon sorts the wheat from the chaff as clients and employers gather information on the quality of economic advice they receive. A reputation for high quality economics is a carefully nurtured and closely guarded asset by both individuals and firms in this unregulated market that generates repeat business by consumers. Word-of-mouth recommendations, publications and advertising are all used by economists to signal their quality to consumers of their services.

Unregulated professions often develop voluntary associations which screen members, signal their quality to the market and provide assurances to consumers. The Master Builders' Federation is a familiar example. The economics profession does not have such a body. Its professional associations (such as the New Zealand Association of Economists) represent groupings of members with similar interests and concerns. Anyone who pays the subscription can become a member and they do not purport to signal quality. The lack of voluntary certification like the Master Builders' suggests that professional economists have little demand for these services and rely on the competitive marketplace to signal their quality.

Nor is there any pressure for the monopoly provision by economists. This

may be economically irrational, but perhaps economist are more subtle than lawyers or doctors. First year courses in economics are enough to weed out all but the determined and act as a brake on supply that pushes up the prices of survivors.

Nor are there calls to homogenise the profession by certifying only those who pass a qualifying exam. On the contrary, the world of unregulated economists is full of contestable economic ideas from the crazy to the profound, from those trained in formal economics to DIY enthusiasts. From this diversity of ideas, some survive and flourish, only to be improved upon or taken over eventually by newer and better ones. This heterogeneity permits innovation, specialisation and differentiation into niche markets.

Economists should be the last profession to call for regulation. We of all people should know that regulation involves a dance with the devil. While it can confer monopoly rents, it invites interference by government and competitors alike that stifles internal and external competition, imposes significant direct and indirect costs on the profession and on consumers without providing any real assurance of quality.

Stuart Birks' note raising the question of whether economics should consider itself a profession brings to mind a favourite story about the former USSR. The Russian President and a visitor were watching the inevitable and interminable May Day parade as phalanxes or ever more dangerous weaponry passed before them. At the end of the procession were four shabby men dressed in grey coats. 'Gosh', said the visitor, 'who are they and what are *they* doing in a parade showcasing the military power of the Soviet Union?' 'Ah,' said the President, 'they are our economists. Just think of the damage *they* can do.'



*"The enjoyment of life covers many things: the enjoyment of ourselves, of home life, of trees, flowers, clouds, winding rivers and falling cataracts and the myriad things in Nature, and then the enjoyment of poetry, art, contemplation, friendship, conversation, and reading, which are all some form or other of communion of spirits." - Lin Yutang<sup>1</sup>*

The concept of "utility" has a central place in much of economic theory. Textbook definitions commonly describe it in terms such as, "satisfaction", "happiness", or "enjoyment", with preferences assumed to be "given". I'd like to take a step back and consider whether our viewpoint might be overly restrictive, limiting the options we consider.

Lin Yutang's description is far more colourful than the economist's indifference curve representation of preferences for apples and oranges. When we make our simplifying assumptions, we should be careful that we are not omitting important dimensions. I won't go so far here as to include consideration of social capital and the aesthetic qualities of our natural environment, for example, although they are potentially highly relevant in that they cannot be assumed to be unrelated to economic activity. There are other restrictive assumptions which are closer to home and merit explicit statement.

In economic theory we commonly assume a similar mathematical form for utility and production functions, indifference curves and isoquants. It may be fruitful to extend the parallels.

Issues of technical progress and efficiency in production receive a lot of attention. Technical progress can shift isoquants nearer to the origin. Can we shift indifference curves? If individuals "produce" utility through consumption, should we not also consider technical progress and efficiency in consumption? People may be able to become more or less efficient in generating utility. Hence people could develop expensive tastes and require a lot of money, or have cheap tastes and need less money, for example.

Perhaps it is possible to "learn to like" something, as in developing an interest, practicing until a level of proficiency is reached, or simply acquiring a taste for something. If so, then one could select low cost or high cost activities or products. An investment in human capital could be an investment in developing the ability to enjoy more and/or cheaper activities (homelife, flowers,

winding rivers, contemplation, friendship, and reading).

Some processes may be hard to reverse, so that options may be lost as well as gained. For example, a skilled worker cannot unlearn those skills and resume unskilled work exactly as before. Similarly, someone who has married or started a family can separate or have no contact with the children, but they are not the same as the person for whom these things never happened.

We therefore make decisions which affect our prospects for future enjoyment of life, not only in terms of attainable material standards, but also in terms of what those standards might mean to us.

Relative approaches to satisfaction can be measured in relation to expectations. Perhaps it is efficient to shape our expectations to more closely match what we can attain.

In any event, if utility functions are of value as analytical tools, then we should at least acknowledge that they may be moving. If so, they would be of limited value for intertemporal welfare decisions unless the pattern of movement can be predicted.

J K Galbraith voiced skepticism of the value of increased consumption:

*"What is called a high standard of living consists, in considerable measure, in arrangements for avoiding muscular energy, increasing sensual pleasure, enhancing calorific intake beyond any conceivable nutritional requirement. Nonetheless, the belief that increased production is a worthy social goal is nearly absolute."*<sup>2</sup>

There is another dimension that we could consider. Production as described in linear programming assumes fixed factor proportions and a limited range of options. Differentiable isoquants are in fact a limiting case of this approach where the number of available processes tends to infinity. What if there is a parallel in consumption? This could be possible if there are a finite number of alternative lifestyles that people could select from. People might be set in their consumption patterns with little substitution unless there are extreme changes in circumstance, after which a major shift could occur. If so, then policymakers should be wary of generating such shifts. Possible examples might be poverty traps, benefit dependency, and discouraged workers following long periods of unemployment.

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<sup>1</sup> Lin Yutang (1938), *The Importance of Living*, London: Heinemann, 1970 reprint, p.118

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<sup>2</sup> Galbraith J K (1967) *The New Industrial State*

On the other hand, perhaps the issue is actually more basic than economists assume. To again quote Lin Yutang:

*"If one's bowels move, one is happy, and if they don't move, one is unhappy."*<sup>3</sup>

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<sup>3</sup> Lin Yutang, op. cit., p.112

# web-sites

for economists

This column has provided some excellent links to site of interest to general economists and to economics teachers. I'd like to narrow the focus just a bit and take you on a brief journey of web sites of interest to natural resource and environmental economists.

One of the best overseas sites is that of the US-based Resources for the Future (RFF) at <http://www.rff.org/>. RFF is a non-profit think tank that conducts economic research on environmental and natural resource issues. From the home page, you can jump right into their extensive library of research summaries and published articles. You just click on the general topic that you're interested in and you are taken to a list of research summaries, articles from their newsletter *Resources*, and discussion papers. For example, a visit to their section on climate change revealed dozens of papers, including such topics as the impacts of carbon abatement policies on technological innovation, an analysis of the international interactions of taxes and environmental policy, and dynamic general equilibrium modelling under uncertainty.

Another excellent site is that of the economics section of the World Conservation Union (IUCN) at <http://economics.iucn.org/>. The IUCN is a union of governments, government agencies, and non-governmental organisations working together with scientists and experts to conserve nature. The site is a virtual clearinghouse for papers on biodiversity conservation. There are over one hundred papers in Adobe Acrobat format available for download through the site, covering every conceivable topic in the area of biodiversity conservation.

I would like to be able to direct you to a single site where you could find all manner of practical information, contacts and upcoming conferences, but I have never found one. I thought I might have struck gold in the Land and Resource Economics Network at <http://www.ems.psu.edu/MnEc/resecon/>, but this site appears to be neglected by its

authors at Pennsylvania State University in the United States. Still, it is useful in being the home of the RESECON mailing list and for providing documentation and details for joining and using the list.

Coming back closer to home, the New South Wales Environmental Protection Authority publishes Envalue, a searchable database of environmental valuation studies, at <http://www.epa.nsw.gov.au/envalue/>. The site couldn't be easier to use. You simply choose the general topic from the left frame, which then opens to show you subtopics (sometimes in more than one level). The results of your search are then shown in a summary table in the right frame, with columns for author, year, country, location and method. You can click on any entry to see more detailed information on the study, including a complete citation, some key details and a series of comments on the method used and the results. The government of Québec, Canada has recently opened a very similar site at <http://www.evri.ec.gc.ca/evri/> which is also well worth a look, though it is less likely to include New Zealand studies. Another similar site for New Zealand non-market valuation studies is in development at Lincoln University, but details were not available in time for this review.

Finally, I can't help but to put in a plug for my own modest effort at returning something of value to the resource and environmental economics community. If you or your students are looking for citations in resource economics, marine economics or wildlife economics, you are welcome to search my online citations databases <http://econ.massey.ac.nz/alexander/econ/citations.htm>. It is not the largest database of citations around, but it is accurate, relevant and contains full abstracts. Searches can be conducted directly online and the results downloaded to your system in a variety of formats.

web-site review by Rob Alexander  
R.R.Alexander@massey.ac.nz



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# From our foreign correspondents

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## **The Australian Annual Conference of Economists- reflections on opportunities for Trans-Tasman collaboration**

**By Benedikte Jensen, NZ Treasury  
(Benedikte.Jensen@treasury.govt.nz)**

In late September, I attended the Australian Annual Conference of Economists at La Trobe University. Here are some personal reflections on some of the highlights from the conference.

I talked informally with Max Corden (John Hopkins University) and Peter Lloyd (University of Melbourne) about New Zealand's trade policy strategy. These types of events present a rare opportunity to exchange information on current research interests, test ideas on research questions, and identify people with related research interests. There was also a lively contingent of trade policy researchers from the University of Nottingham, led by David Greenaway. David presented some innovative research that modelled dynamic trade-induced productivity effects and their consequences for manufacturing employment in the United Kingdom.

Bob Gregory (ANU) gave the Presidential Address on "Our Children's future in a country of growing labour market inequality". Bob raised some interesting questions about the implications of growing earnings and employment disparities for intra-familial transfers. Are returns to skill really benefiting the young worker with the latest skill-set? Bob's research showed that real wage trends had disproportionately benefited middle-aged workers over the last few decades. These earnings and employment effects suggested that many Australian 'children' would require income support from their parents until they were at least 34. Of course, this may not seem like such a revelation to those of you whom

are already supporting extended families well into your retirement!

Bob's address prompted me to reflect on opportunities for Trans-Tasman collaboration on income distribution research. At the New Zealand Treasury, we are researching changes in the distribution of household income, and decomposing these changes into components driven by changes in household composition, individual attributes, employment effects and so forth. It would be useful to compare and contrast the New Zealand experience with what has been happening in Australia.

The conference concluded with a one-day business symposium. This session highlighted for me the importance of exposing New Zealand policy makers to international perspectives, sometimes critical of the New Zealand approach (although this was not the focus of the sessions). Warwick McGibbon (Brookings Institution, Stanford University) talked about the global economic outlook and implications for the Australian economy. Over the coffee break, Warwick mentioned that he has undertaken a critique of New Zealand's monetary policy, comparing it with the operation of monetary policy in Australia. Naturally, I asked him to email me the relevant publication. The session on regulatory policy highlighted the differences in approach taken by Australian regulators. Once again, it was useful to reflect on what we can learn from the Australian experience.

Neil Campbell (Massey) and I were the only New Zealanders attending the conference. I was struck by the potential benefits from closer collaboration with the Australian academic and policy communities. Why don't we propose to combine forces with the Australian Association? We could still retain our local Economist's association, but we would benefit from holding joint conferences and becoming more "plugged-in" to Australian debate and discussion. I certainly enjoyed the experience! I would be interested in hearing your views on this

proposal. A book of abstracts of papers from the Australian Conference of Economists may be downloaded from the University of La Trobe Business School web-site at:

<http://www.business.latrobe.edu.au/esac>.

Unfortunately, copies of the full papers are accessible only by contacting individual authors.

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**NABE Annual Meeting, San Francisco, 25-29 September.**

**By Donal Curtin (economicsnz@xtra.co.nz)**

NZAE members working as economists in the corporate business world should have a look at what's offered by the US based National Association for Business Economics (or NABE). Details of the organisation and its activities can be found on the NABE site, [www.nabe.com](http://www.nabe.com). In short it's got a little over 3,000 members, very largely in the US but a smattering worldwide including 3-4 in New Zealand.

Its purpose in life is to assist "people who use economics in their work: private industry, non-profit and trade associations, consultants, government and university researchers", and as one would expect its focus is on practical applied economics. Its journal, *Business Economics*, is useful - the contents of the latest (October '99) issue give a flavour of its orientation with four articles on the chemical industry, two on applied business economics, and regular columns in a 'Business Economics in the Workplace' section including 'The Business Economist at Work' where a member explains what they do in their job. There are

also book reviews and pointers towards interesting Web sites.

NABE also runs an annual meeting, usually in mid to late September, this year held over Sept 25-29 in San Francisco on the theme 'Targeting Business Risks & Opportunities'. I attended and found it well attended (for those interested in networking with other business economists), and had some high calibre speakers - highlights included Prof Alan Blinder from Princeton (and formerly Vice Chairman of the Fed), Peter Bernstein, author of *Against the Gods: The Remarkable Story of Risk* (John Wiley, 1996), William Raduchel, Chief Technology Officer at America Online, who gave a stunning speech on the implications of the Internet for business and academia, and Michael Milken (yes, *that* Michael Milken) who has now developed a range of educational and health service companies as well as the not-for-profit Milken Institute.

For members with an interest in US economic policy issues, NABE also runs a policy conference in the northern spring: the next one is scheduled for Feb 22-23 in Washington on the topic 'The Surplus Conundrum' and goes into all the issues relating to the forecast US fiscal surpluses.

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**The Money, Macro and Finance Study Group Annual Meeting 1999 (Oxford)**

**By Weshah Razzak (razzakw@rbnz.govt.nz)**

This is the oldest conference on these subjects in the world. Professor Harry Johnson established this group more than thirty years ago. Thirty sessions, including 100 papers, were organised. The papers were all refereed.

Lectures were given by:

Professor Kenneth Singleton (Stanford),

Professor Peter Kenen (Princeton),  
Professor Charles Goodhart (London School of Economics)  
and John Vickers (Bank of England).

I presented my paper on the forward exchange rate in inflation- targeting regimes.

In this report, I summarise what I regard as the most important points from the most important papers only. These are the sessions that I attended. Most papers are not available, but I have a list of them if anyone is interested.

1. The manager of Modelling and Forecasting at the Bank of England (Neal Hatch) gave a quick but interesting presentation of their model(s).

\* The Bank of England uses many different models to derive and evaluate its forecasts and policy scenarios. One of the models is a large-scale model, which includes 150 variables. Testing whether policy conclusions are robust to different modelling assumptions is a valuable exercise.

\* The BoE models the exchange rate as a jump variable, which I think is the correct way of modelling the exchange rate in an open economy with a freely floating exchange rate because this is consistent with the empirical evidence and theory (e.g., Dornbusch).

\* The BoE model includes money. This also makes a lot of sense.

2. The Chief Economist of the Bank of England, John Vickers, gave a very interesting paper titled "Monetary Policy and Asset Prices". He addressed three questions:

\* Should asset prices be included in the measure of inflation?

\* What can asset prices tell us about the stance of monetary policy?

\* Do movements in asset prices have any information about future inflation?

Vickers concludes that:

\* Asset prices should not be included in the measure of inflation. Asset prices are naturally volatile. Including them in the inflation measure may add unnecessary volatility.

\* Policy makers should not go bubble hunting because bubbles may not even exist.

\* The information content of asset price movements may be important for the conduct of monetary policy. If asset prices have information about future inflation then it is important that the central bank watches them.

3. Charles Goodhart (LSE and BoE monetary policy committee) gave a paper titled "Monetary policy Adjustment with Asset Price Fluctuations." He stresses the following:

\* Monetary policy should only react to asset price movements when they contain information about future inflation. Thus, monetary policy should only react to asset price movements if a stable relationship between CPI inflation and asset price inflation is identified. This is an excellent point and is applicable more generally. For example, if the relationships between inflation and the output gap or inflation and money growth are unidentified, or are unstable then such relationships are not informative for monetary policy.

\* Goodhart acknowledges that the econometric analysis in his paper is problematic.

\* This leads to questions about results. He found asset price inflation to be reasonably correlated with inflation in the UK, but not in the US. He thinks this is interesting.

\* He finds the output gap to be uncorrelated with inflation. In his words "the output gap totally collapsed". He thinks this is interesting. As I have stated before, I believe this is also true in New Zealand, and I have explained why this is so. Monetary policy that successfully achieves the inflation target renders inflation low and less volatile. It follows that the correlation (precisely the covariance) between inflation and the output gap, which is more variable, is close to zero.

4. A paper titled "Catching-up of East Germany Labour Productivity: Lessons for EMU" by Ray Barrell and Dirk Willem te Velde (NI ESR) is interesting.

\* The authors find that East Germany's labour productivity has converged to that of West Germany because West German firms have located in East Germany.

\* They also find that Ireland's labour productivity converges to that of the UK because of increasing investment in education.

5. Stilianos Fountas (National University of Ireland, Galway) and Agapitos Papagapitos (University Of St. Thomas, Minnesota) presented "The Monetary Transmission Mechanism: Evidence and Implications for European Monetary Union." They find that the traditional channel from interest rate to

investment is insignificant. However, they find evidence of lending/credit channels.

6. Daniel Thornton, Vice President at the Federal Reserve Bank of St. Louis, presented a paper titled "The Fed's Influence on the Federal Funds rate: Is It Open Market or Open Mouth Operations?" The paper draws heavily on Guthrie and Wright's paper on this issue for New Zealand. Thornton finds minor evidence of open mouth operation effect in the US data.

7. Jorg Bibow (University of Hamburg) presented a paper titled "Reflections on Current Fashion for Central Bank Independence." This is a very strange paper in the sense that the author argues that there could be more risk associated with CBI than that associated with inflationary bias. The author does not have a model. The author does not present any empirical evidence.

8. Stephen Millard and Shamik Dhar of the Bank of England presented a very good paper titled "A Limited Participation Model of the Monetary Transmission Mechanism in the UK." This is a general equilibrium model with money and rational agents. They find:

- \* The liquidity effect to be small and insignificant. This means that changes in the quantity of money have only a small impact on interest rates. They were puzzled by this result, however, the empirical evidence from the US is similar.
- \* Money is neutral in the long run.
- \* Money quickly affects the price level.
- \* The effect of money on real wages implies that the labour market is inflexible (sticky wages).

9. David Cobham (University of St. Andrews), Stefania Cosci (University of Molise and LUISS, Rome), Fabrizio Mattesini and Jean Marin Serre (Universite' d' Auvergne) presented some qualitative evidence of "informal" central bank independence effects on inflation. The literature on CBI suggests that higher independence lead to lower inflation rate. These authors argue that we may observe

episodes of low inflation without formal changes in central bank independence. Therefore, they argue that informal independence is a more useful device or concept than formal independence to use in these cases. The evidence they examine for informal independence includes:

- \* division of responsibilities between government and CB
- \* prestige of the CB
- \* technical skills of staff
- \* degree of consensus on objectives
- \* external constraint(s)
- \* mechanism of accountability

They find that the Bank of France experienced a slow but resisted rise in informal independence; the Bank of Italy also experienced a significant increase in informal independence. They find a decline in the informal independence of the Bank of England as evidenced by significant variability in monetary policy and monetary policy objectives.

10. Peter Kenen's lecture was about the new financial architecture.

Professor Kenen is a seasoned economist who has a lot of influence on, and interaction with, the IMF. He discussed at length whether the system needs reconstruction, renovation or a minor repair.

- \* He argues that there is a big difference in size between emerging markets and the G10 and this causes a serious problem.
- \* The incentives to reform are weak.
- \* Emerging markets' reliance on the IMF is a problem.
- \* When conditions change IMF policy recommendations must change too.
- \* He is sympathetic to those who argue that the IMF conditions imposed on countries are stiff and inflexible, which may have made it difficult for the East-Asian countries to act during the crisis.
- \* He is sympathetic to those who argue that the IMF policy recommendation to the East-Asian countries not to use fiscal stimulus was wrong.
- \* He summarises his understanding of the Asian crisis as follows: Rapid growth led to

asset booms, computer chip prices fell and subsequently expected future growth declined. The exchange rate pegs and the fact firms did not hedge exposures led to decline in exports. The peg regimes were abandoned and there was a massive loss of reserves. All this led to a credit crunch.

Peter Kenen predicts that the IMF's job will be more difficult than ever in the future, because the US Congress will block future funding of the IMF.

I asked Professor Kenen what he thinks about a potential currency union between Australia and New Zealand. Professor Kenen is one of the early writers on currency areas in 1960s. He said that the Australian dollar is dominated by particular commodity shocks that are not relevant to New Zealand. So, New Zealand may needlessly suffer from such shocks if they enter in a monetary union with Australia. That was his major concern. However, he said he

would have to study the matter more closely in order to answer the question properly. There are, of course, many other issues.

11. A paper by Lynne Evans and T Kenc (University of Durham) titled "Welfare Cost of Monetary and Fiscal Shocks" shows that monetary shocks have negative welfare effects while fiscal shocks have positive welfare implications. The welfare costs are sensitive to assumed attitudes towards risk and to propensities for intertemporal substitution. There are many technical issues involved in this paper that might have a direct impact on the results.

## **Marsden PhD Scholarship in Economics, 2000**

### **Department of Economics, University of Otago**

Applications are invited for a 3-year PhD scholarship tenable in the Department of Economics at the University of Otago from 1 January 2000. The holder of the scholarship will work, under the supervision of Professor Dorian Owen and Dr Stephen Knowles, as part of a team investigating the effects of social capital and mutual trust on economic performance across countries (and regions within specific countries). The project is funded by the Marsden Fund, which is administered by the Royal Society of New Zealand.

Applicants should have (or expect to obtain in 1999) the equivalent of a good (First class or Upper Second class) Honours degree in economics or econometrics, a good background in applied econometrics, and an interest in empirical modelling of economic growth.

The scholarship from the Marsden Fund is valued at NZ\$15,000 per annum and is free of income tax. NZ-resident PhD fees will also be covered. The Marsden Fund scholarship will be supplemented by a scholarship from the Economics Department's Donald Reid Fund worth NZ\$3,000 per annum. The scholarship is for a period of three years. Additional income from tutoring and/or research assistance will also be available. Computing facilities will be provided and data requirements and thesis preparation costs will be funded. Funding will also be available for attendance at NZ and Australian conferences to present the results of the research.

Applications should include a CV and details of two referees (including email addresses) and should be directed to Dr Stephen Knowles, Department of Economics, University of Otago, PO Box 56, Dunedin as soon as possible, and preferably by 10 December 1999. Alternatively, applications can be sent by email ([sknowles@commerce.otago.ac.nz](mailto:sknowles@commerce.otago.ac.nz)). It is suggested that applicants ask their referees to send reports directly to the above address as soon as possible.

For enquiries or requests for additional information contact Stephen Knowles (email: [sknowles@commerce.otago.ac.nz](mailto:sknowles@commerce.otago.ac.nz) or phone (03) 479 8350).

## ENROLMENTS IN ECONOMICS STUDIES IN NEW ZEALAND UNIVERSITIES: AN UPDATE

James E Alvey (J.E.Alvey@massey.ac.nz) and Leanne Smith (L.M.Smith@massey.ac.nz)

In 1998, we outlined (*Asymmetric Information* 3: 9) the research that we had commenced on economics enrolments in New Zealand universities. That research has now almost been completed. We wish to report our principal findings below.

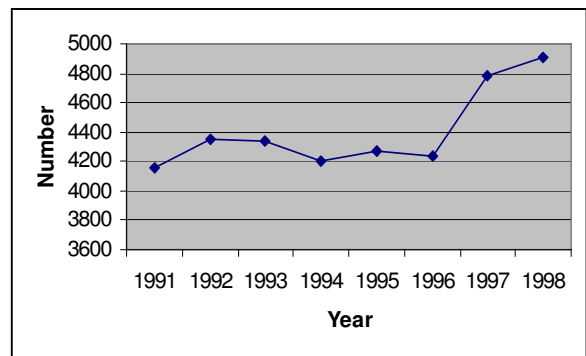
Seven universities were approached to participate in the survey (AIT will become the 8<sup>th</sup> university in 2000). One academic economist from Lincoln told us that “students *can* major in economics ...[but] the Registry *does not* keep records of numbers of students who complete majors in economics.” For this reason, apparently, Lincoln did not participate in the statistical part of the survey, even though questions on enrolment in the major comprised only the first two out of the five statistical questions. Of the remaining six institutions, several indicated that the statistical questions were difficult to answer because their registry did not keep records of majors or did not keep them over the duration of a student’s enrolment. Even more disturbing is the fact that the quality of the data supplied by the institutions actually declined further in 1998, when we sought an update.

Despite these difficulties there were some interesting, albeit tentative results. First, in a recent Australian study (Lewis and Norris, *Economic Papers*, March 1997) it was suggested that there was a link between high school economics enrolments and university economics enrolments. Seventh Form economics enrolments in New Zealand dropped from 7376 in 1991 to 6814 in 1998, or a 7.6% decrease over the period. If Lewis and Norris are correct that there is a correlation between trends in high school and university enrolments, there has probably been an absolute decline in undergraduate university economics enrolments in New Zealand. Nevertheless, the decline has been less severe than in Australia (where enrolments in high school economics had declined by 45% during 1991-96 and university economics enrolments fell by 13% during the same period).

Second, we obtained some non-robust figures on first year and total undergraduate (first, second, and third year) enrolments in economics degrees (majors). One university could not provide figures on economics majors over the period 1991 to 1998, but over 1996-8 it showed a 16% growth in first

year enrolments. Of the remaining five institutions, there was a growth of 25% in first year enrolments over the period 1991-98. Until 1996 there was only 2% growth but there was a growth of 22% in the period 1996-8. Our major concern here is that, without the results from all seven, a biased conclusion may be drawn from the figures for five institutions.

### Undergraduate (Year 1-3) Total Enrolments (Headcount) in Economics Majors in Five New



### Zealand Universities

Third, concerning total enrolments in the economics major we also obtained some results, with the same reservations about the data (see graph below). A similar pattern of results emerged for total enrolments as for first year enrolments in the major. In the institution which provided only recent figures, there was a 12% growth over 1996-8. For the other five universities there was an 18% growth over 1991-8. Enrolments were almost steady until 1996, when the growth phase began.

Fourth, the overall teaching load (including elective and service teaching) for the six universities has increased from 2554 EFTS in 1991 to 2900 EFTS in 1998, or an increase of 13.5% over the period. This is a better result than occurred in Australia (3% increase during 1992-96). Fifth, honours enrolments in New Zealand are sufficiently small that it is difficult to draw firm conclusions from fluctuations in their number. In the three honours programmes that were elite in character, and for which data was available, there was an increase in enrolment from 36 to 43, or 19%, over 1991-8. This included an increase of 54% over 1996-8. In addition, a new honours programme began with a steady enrolment of 20

students. In one other programme, the figures of honours and masters students were combined, showing an increase from 8 to 13 students over

1991-8.

Finally, what conclusions do we draw? First, much more attention needs to be given to gathering and disseminating reliable raw data on enrolments in economics majors in New Zealand Universities; the NZAE has a role to play here. Without such data, provided on a consistent basis, it is impossible to say much confidently

about the current state of enrolments in economics, never mind the causes of the fluctuations. Second, some institutions have done very well; others, as Nancy Devlin pointed out (*Asymmetric Information* 3, 2-3), have languished. Third, overall, there does seem to be a cycle in economics enrolments.

## DR GRANT SCOBIE MOVES TO TREASURY

The Treasury recently appointed Dr Grant Scobie to the position of Adviser in the Policy Coordination and Development (PCD) directorate of the Treasury. PCD is an internal Treasury “think tank” charged with analysing economic growth and income distribution trends and issues, and applying new economic ideas and findings. Initially, Dr Scobie will be analysing the apparently low level of savings in New Zealand, and exploring the extent to which alternative policies might stimulate household savings.

Dr Scobie has worked in over 30 countries as an economist, consultant, academic, and manager.

He has just returned to New Zealand after nearly five years as Director General of the International Centre for Tropical Agriculture (CIAT) in Colombia. CIAT is the world’s largest agricultural research centre, with 650 staff in 14 countries, and focuses on expanding sustainable food production in developing countries. New Zealand supports CIAT as part of our foreign assistance programme.

As Professor of Economics and Chair of the Department at Waikato University from 1990-1995, Dr Scobie focused on producing high-quality economics graduates, and oversaw the development of the first combined Law and Economics courses at both graduate and undergraduate level in New Zealand. Dr Scobie also taught extensively on the University’s MBA programme. Between 1976 and 1982, he was an Associate Professor at North Carolina State University, USA.

Dr Scobie was also a founding director of SER Consulting Ltd, a economic consulting practice with an extensive client list in New Zealand and overseas.

Dr Scobie has published extensively in the 5

areas of macroeconomic policy, agriculture in developing countries, the economics of research and development, science policy, resource and environmental policy, and trade policy in developing countries. In 1994, he won the C.M. Kelly Award for Economic Writing in Australasia jointly with the Treasury’s John Janssen for a paper entitled *Liberalising New Zealand’s Economy: Rehabilitation and Recovery*.

From 1993 to 1998, Dr Scobie was a Lay Member of the High Court of New Zealand, and was a member of the Todd Taskforce on Funding Tertiary Education and Training in 1993-94.

Dr Scobie has a Bachelor of Agricultural Science from Massey University, a Masters in Agricultural Economics from the University of New England, Armidale, Australia, and a PhD in Economics from North Carolina State University.





## POLICY ADVICE TO MINISTERS

by Gary Buurman (G.B.Buurman@massey.ac.nz)

In 1997 the State Services Commission began a project on improving the quality of policy advice. Three papers that contribute to the project are released on the web at [http://www.ssc.govt.nz/documents/Occ\\_Papers\\_Content\\_Screen.htm](http://www.ssc.govt.nz/documents/Occ_Papers_Content_Screen.htm). Some of the concerns are:

- Inability of the public service to define outcomes the government seeks;
- Inadequate human resources in some policy units;
- Inattention to implementation issues;
- Counter-productive departmental patch protection.

The project identifies five contributing factors:

- Lack of clarity from ministers on desired outcomes;
- Insufficient incentives for cooperation on policies that 'cut across' departments;
- Variations in standards of leadership;
- Under-investment in capability development leading to shortages;
- Inadequate and/or ineffective use of information, research, evaluation and consultation techniques as policy inputs.

Occasional Paper 7 concerns evaluation. One perceived problem is a new focus on the actual output of advisory departments rather than on the outcomes that government is seeking. Few departments evaluate the extent to which the policy outputs they produce contribute to the priorities of the government. Many factors affect outcomes and there are problems with causality. It can be tempting to simply not evaluate. Outcome evaluation is not a strong feature of New Zealand policy because of low demand (in that ministers were not interested in evaluation); funding problems; a fluctuating policy environment with a three year election period and a lack of skilled evaluators.

Occasional Paper 9 mentions a perception by ministries that advice presented is not underpinned by robust information and research (p.3). Concerns about the quality of advice include short timeframes that inhibit in depth research and a shortage of policy advisors skilled in information management and use

(p.5). Brevity is required in the presentation of advice, particularly in cabinet papers. These papers are generally not referenced with information sources. Thus there is no assurance that the contents are not just informed guesswork and this makes it difficult for ministers and their advisors to crosscheck different assertions.

The State Services Commission is serious about this project and there are implications for economists including:

*A lack of evaluation in policy areas.* This does not only apply to traditional areas of economics. What about evaluating the effect of laws and the legal system, structures and institutions, etc.?

*Poor quality research and the problem of bias.* Myrdal stated (p.18) that there is no necessary connection between superficiality and the extent of bias, and that biases in research emanate from the influences exerted by society, from our personal involvement in what we are studying and from a tendency to apply approaches with which we are familiar. Myrdal was talking about the LDCs, but No.9 (p.8) mentions advice based on theoretical frameworks, extant information, current practice, and dependable sector interest groups. Thus policy can be out of touch with actual conditions.

Policy research in the private sector and in universities is not immune from the difficulties found by the SSC.

### REFERENCES:

Myrdal, G. (1970), *An Approach to the Asian Drama: Methodological and Theoretical*, (Vintage: New York).

State Services Commission (1999), *Looping the Loop: Evaluating Outcomes and Other Risky Feats*, Occasional Paper 7, (State Services Commission: Wellington).

State Services Commission (1999), *Essential Ingredients: Improving the Quality of Policy Advice*, Occasional Paper 9, (State Services Commission: Wellington).



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# research in progress...

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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 **Otago University**. The objective of this section is to share information about research interests and ideas **before** publication or dissemination - each person was invited to provide details only of research that is **new** or **in progress**.

## ... in the Department of Economics at Otago University as at October 1999.

**Names:** Robert Alexander, Murat Genç and  
Mohammad Jaforullah

[ralexander@commerce.otago.ac.nz]

**Research currently in progress:**

**Title:** "Maori disadvantage in the labour market"

**Aim:** Our aim is to determine whether Maori fare less well than non-Maori primarily because they possess less human capital in terms of educational attainment and labour market experience or whether they receive smaller labour market rewards for their skills. Given that returns to measurable skills are large and potentially growing in today's labour market it is important to understand whether a skill gap is the primary determinant of labour market disadvantage or whether there does exist a significant element of discrimination.

**Hypothesis:** In New Zealand, with the notable exception of Sylvia Dixon who has focussed on wage dispersion throughout the work force, research has mainly dealt with labour market status defined qualitatively. Overseas there has been considerable research which attempts to explain the apparent labour market disadvantage of various ethnic groups. Most studies attempt to explain wage disparities. On the basis of the hypothesis that there is neither racial discrimination in the labour market nor racial differences in the willingness to supply labour, wage differences between Maori and non-Maori ought to be explainable in terms of variables such as age, experience, location and educational attainment.

**Method:** We plan to use data from the HLFS and the complementary Income Survey and propose including all those in the labour force, that is the employed and the officially unemployed. Those in receipt of an unemployment benefit are in the labour force, but have zero market income. The modelling approach involves combining a discrete choice model with continuous variables.

**Name:** Erkin Bairam

[ebairam@commerce.otago.ac.nz]

**Research Interests:** Labour economics; production functions, theory and applications; exports and economic growth.

**Research currently in progress:**

**1. Title:** "A new variable-scale-elasticity, variable elasticity of substitution production function"

**Aim & method:** This new function is devised in such a way that it takes into account dynamic aspects of the production process (in particular their effects on marginal productivities of inputs) and relates these dynamic

changes to vintage physical capital and human capital approaches. At present the model is being tested on OECD data.

**2. Title:** "Economic benefits of education, a microeconomic approach"

**Aim & method:** The theoretical part of this research has shown that net benefits of education is a decreasing function of the worker's degree of risk aversion, the elasticity of substitution between labour and capital, the price elasticity of product demand and the share of labour in total costs. I'm interested in testing the model but, at present, finding appropriate/ suitable data is proving to be very difficult.

**Name:** Murat Genç

[mgenc@commerce.otago.ac.nz]

**Research currently in progress:**

**Title:** "Box-Cox transformation in estimating production functions"

**Aim:** To investigate the performance of Box-Cox transformation in estimating production functions.

**Method:** Monte-Carlo simulations to compare the performance of Box-Cox transformation with other flexible functional forms.

**Name:** Paul Hansen

[phansen@commerce.otago.ac.nz] & Nancy Devlin  
[ndevlin@commerce.otago.ac.nz] (with Paul Kind and Alan Williams, University of York)

**Research currently in progress:**

**Title:** "A tariff of health state preferences for New Zealand"

**Aim:** To generate a full social tariff of health state valuations. These valuations or 'weights' are multiplied by length of life in each health state to estimate Quality Adjusted Life Years (QALYs) in the economic evaluation of health services.

**Method:** A random sample of the adult population were asked to value various sets of health states (using the EQ-5D; a system which describes health in terms of five 'dimensions', with three levels in each) using a visual analogue scale approach. A key focus of this research is exploring effects and implications of logical inconsistencies in individuals' valuations. From the observed preferences, preferences over the full set of states are interpolated using a random effects model. Values are anchored at 1 (full health) and death (0) with

health states considered worse than death having negative values.

**Related research also being undertaken as part of this project:**

- (a) modelling the determinants of health state valuations
- (b) respondents' perceptions of the health state valuation exercise
- (c) the distribution of health status in the sample using the EQ-5D.

**Name:** Mohammad Jaforullah  
[mjaforullah@commerce.otago.ac.nz]

**Research interests:** Applied econometrics and microeconomics

**Research currently in progress:**

**Title:** "A comparison of production frontier methods using Bangladesh handloom textile industry data"

**Aim & method:** 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. Some of these are deterministic and some are stochastic in nature. Moreover, either econometric or DEA (data envelopment analysis) methods can be used to estimate the models. 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. Data to carry out the study come from the textile industry of Bangladesh.

**Name:** Alan King  
[aking@commerce.otago.ac.nz]

**Research currently in progress:**

**1. Title:** "Balance-of-payments constrained growth: introducing supply" (with Erkin Bairam)

**Aim and method:** To extend Thirlwall's law of (long run) economic growth by explicitly allowing for supply-side influences. The new model is then evaluated (in comparison with Thirlwall's law) to see whether either specification represents a valid cointegrating relationship.

**2. Title:** "Uncovered interest parity and exchange risk"

**Aim and method:** To investigate the theoretical implications of the nature of exchange risk on the risk-adjusted uncovered interest parity (RAUIP) relationship and to attempt 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

**Name:** Stephen Knowles  
[sknowles@commerce.otago.ac.nz]

**Research interests:** Applied analysis of economic growth.

**Research currently in progress:**

**Title:** "Government intervention and economic growth, with reference to East Asia" (with Arlene Garces)

**Aim:** To determine the effect of a variety of types of government intervention (especially interventions common in East Asia) on economic performance.

**Method:** Cross-country regressions examining the effect of different measures of intervention on economic growth and total factor productivity.

**Name:** Stephen Knowles  
[sknowles@commerce.otago.ac.nz] and Dorian Owen  
[dowen@commerce.otago.ac.nz] (with Quentin Grafton, University of Ottawa)

**Research currently in progress:**

**Title:** "Social capital, mutual trust and economic performance"

**Aim and method:** The recent development of the concept of 'social capital' has led to high expectations that it can provide a more central role to social organisation in economic analysis. Social capital is rooted in mutual trust. It is argued that economies with low levels of mutual trust will waste resources in carrying out transactions and monitoring contracts, leaving less resources to boost well-being. This project will investigate, using econometric techniques, the role of social capital as a determinant of long-run economic performance, from a cross-country perspective and for selected individual countries.

**Name:** Stephen Knowles, Paula Lorgelly and Dorian Owen

**Research currently in progress:**

**Title:** "Are educational gender gaps a brake on economic development? Some cross-country empirical evidence"

**Aim:** The World Bank has argued that female education has a greater impact on labour productivity than male education. This project aims to test this hypothesis.

**Method:** To include male and female education in a neoclassical growth model and estimate the model using cross-country data. The model can be reparameterised so that the gender gap in education enters the model. The interpretation of the coefficient on the gender gap depends crucially on what other education variables appear in the equation. The empirical results suggest that female education has a significant positive impact on labour productivity across countries and are robust to various sensitivity analyses, including the use of instrumental variables to control for potential endogeneity.

**Name:** Dorian Owen  
[dowen@commerce.otago.ac.nz]

**Research interests:** Empirical modelling of economic growth, applied monetary economics.

**Research currently in progress:**

**Title:** "Modelling economic growth using multi-country panel data"

**Aim and method:** This project aims to apply the recent developed techniques designed to examine long-run relationships between non-stationary variables in panel data sets to examine the determinants of economic growth. These methods allow us to focus on the crucial long-run relationships emphasised in growth theory, while exploiting the richer set of data provided in multi-country panels (compared to pure cross-section or pure

time-series data) and dealing appropriately with non-stationarity in the time-series dimension of the data.

**Name:** John Parker

[jparker@commerce.otago.ac.nz]

**Research interests:** Innovation, patents, pharmaceuticals and the multinational corporation.

**Research currently in progress:**

**Title:** "Pharmaceutical effective patent life in New Zealand"

**Aim:** To determine the trend in effective patent life of New Zealand marketed drugs and to recommend appropriate law changes to compensate for patent time lost. Effective patent life is the interval between drug registration and patent expiry.

**Hypothesis:** That drug development and registration intervals have been rising over time.

**Method:** To collect and update patent and registration information for a large sample of New Zealand marketed drugs and to analyse the time trend of effective patent life. To collect information on other countries' patent law changes to compensate for patent time lost to provide a comparative basis for appropriate reforms here.

**Name:** Martin Richardson

[mrichardson@commerce.otago.ac.nz]

**Research interests:** Commercial policy; applied microeconomics; industrial organisation.

**Research currently in progress:**

**1. Title:** "Unilateral liberalisation in a multilateral world"

**Aim:** In recent years a great deal of emphasis has been focussed on multilateral and regional fora for trade liberalisation. Increasingly, however, countries have appeared to liberalise unilaterally. This paper will review some of the arguments put forward for unilateral liberalisation and suggest some reasons why it might have increased at the same time that co-ordinated liberalisation has also increased.

**Method:** Review

**2. Title:** "Trade policy and parallel imports" (with Dan Knox)

**Aim:** Earlier work demonstrates that when countries individually choose whether or not to permit parallel imports a global Nash equilibrium involves parallel importing into all operational markets i.e. global uniform pricing. When they can also prevent "parallel exports" then any Nash equilibrium involves global price discrimination. This project examines parallel importing in a broader model of trade policy setting.

**Method:** Linear I.O. model.

**3. Title:** "Quality and congestion"

**Aim:** This work looks at the issue of quality upgrading of a resource when congestion is an issue and monetary pricing is not permitted. This follows from recent concerns in NZ that congestion from foreign visitors is reducing the utility to New Zealanders of the conservation estate.

**Method:** A vertical differentiation model with two types of (heterogeneous) consumer.

**4. Title:** "Cultural quotas" (with Paul Hansen)

**Aim:** This work proposes to look at so-called 'cultural quotas', such as requirements that a minimum percentage

of NZ radio airtime comprise NZ performers, in a model of horizontal differentiation. In such a model, radio stations are endogenously located in some space corresponding to consumers' tastes and we propose to examine the effects on that location choice of what are effectively locational quotas.

**Method:** A horizontal differentiation model of locational choice.

**Name:** Joe Wallis

[jwallis@commerce.otago.ac.nz]

**Research interests:** Leadership and agency failure, public sector reform and the economics of voluntary organisations.

**Research currently in progress:**

**1. Title:** "Local government policy in the 1990s"

**Aim & method:** The local government reforms implemented in New Zealand in 1989 sought to ameliorate institutional weaknesses in this sector by reducing the number and variety of local bodies and subjecting them to the same managerial and financial disciplines that were being applied in the core government sector. The 1990s, however, appear to have been marked by a fundamental disagreement between "minimalist" and "activist" advocacy coalitions about the direction in which these reshaped local authorities should develop. A range of public submissions are being studied to assess the extent to which both groups draw on identifiable economic and political theories to substantiate their arguments. A data base is also being constructed from the annual reports of city councils which could be drawn on to determine at the national, regional and local level whether local authorities have moved in a minimalist or activist direction.

**2. Title:** "The role of voluntary organizations in the provision of supported employment services"

**Aim & method:** Recent developments in social capital theory have been used to strengthen the case for a bottom-up perspective on policy implementation which relates the effectiveness of government agencies to their capacity to build "networks of civic engagement" based on norms of trust and reciprocity. This perspective is particularly relevant to those policy areas such as the supported employment for the disabled in which there is no dominant policy or agency but rather a multiplicity of governmental directives and organizations involved from both the public and private sector. A number of case studies are being conducted of voluntary associations in this area. They will try to apply a social capital-based, bottom-up approach, to develop a clearer picture of the constraints and coping strategies their managers face while, at the same time, generating some data on the social costs and benefits of supported employment.

**Name:** Paul Wooding

[pwooding@commerce.otago.ac.nz]

**Research interests:** International trade policy, monetary policy

**Research currently in progress:**

**Title:** "A small country in a big world: the New Zealand response to globalisation"

**Aim:** To provide a critical evaluation of current views on the appropriate response of a small country like

New Zealand to the pressures exerted by 'the global economy'.

**Method:** Application of recent work in international trade theory and policy to a small country.

### ROBERT A. MUNDELL: NOBEL LAUREATE in ECONOMICS: 1999, by Grant Scobie

The Royal Swedish Academy of Sciences awarded their 1999 Nobel Prize in Economics to Professor Robert A. Mundell of Columbia University "for his analysis of monetary and fiscal policy under different exchange rate regimes and his analysis of optimum currency areas." Some call Robert Mundell the father of the theory of optimum currency areas because he first asked and answered the question: When is it advantageous to go beyond flexible exchange rates and use single currency in a specific international region? Also, the Mundell-Fleming model of an open economy transformed macroeconomic research in the 1970s.

It is most notable that Mundell proposed a common currency for Europe in the early 1960s, even before flexible exchange rates were an international fixture. In essence, the introduction of the euro in 1999 put Mundell's theories into practice.

Mundell pointed out the advantages of a common currency-lower transaction costs and more stable pricing-and also covered the disadvantages in great detail. Just as Europe must today, Mundell, worried about the difficulties of maintaining high employment in all countries under a common currency system. In balancing the advantages and disadvantages, Mundell defined the optimum currency area as a group of countries where population migration ensures full employment in the entire region even if one country faces a unique shock.

All students of international economics are assuredly introduced to some form of the Mundell-Fleming model of an open, or free trade economy. This model extended the popular Hicksian IS-LM model, addressing the potential impact of both monetary and fiscal policy under alternately fixed and flexible exchange rates. He made seminal contributions to our understandings of the dynamic effects of capital mobility and the forces that tend to cause foreign and domestic interest rates to equalize.

The Nobel committee made a point of stating that "Mundell's contributions serve as a superb reminder of the

significance of basic research. At a given point in time academic achievements might appear rather esoteric; not long afterwards, however, they may take on great practical importance." In essence, the Nobel Prize in Economics continues to be given to those who made great and far-reaching theoretical advances in largely academic venues. To earn a Nobel Prize, however, this work must also have an eye toward practical applications and real world relevance. Certainly, Mundell's contributions to economics fit the bill as pathbreaking and relevant. The awarding of the 1999 Nobel prize economics is most apropos in light of current concerns about global financial markets and discussions about both the advantages and problems of international trade, flexible exchange rates, and capital mobility.

Robert A. Mundell was born in Canada in 1932. After completing his undergraduate education at the University of British Columbia and the University of Washington, he began his postgraduate studies at the London School of Economics. Mundell received his Ph.D. from M.I.T. in 1956 with a thesis on international capital movements. After having held several professorships, he has been affiliated with Columbia University in New York since 1974.

[Adapted from material in a biography of Prof. Mundell by The Dismal Scientist].

Useful related web sites include:

- A. Nobel Prize site with descriptions of Mundell's work <http://metalab.unc.edu/nobel/economics99.html>
- B. Mundell's home page <http://www.columbia.edu/~ram15/index.html>
- C. International Economics Mundell's 1968 textbook <http://www.columbia.edu/~ram15/ietoc.html>
- D. Winners of the Nobel Prize in Economics <http://nobelprizes.com/nobel/economics/economics.html>

## ...about NZAE

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

Membership fees: full member: \$90  
graduate student: \$45

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

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PO Box 568  
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fax: (04) 801 7106

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

**Carolyn Stevens** (Institute of Chartered Accountants); **Mark Brice** (Reserve Bank of NZ); **Aaron Drew** (Reserve Bank of NZ); **Mike Frith** (Reserve Bank of NZ); **Yuong Ha** (Reserve Bank of NZ); **Gaylene Hunter** (Reserve Bank of NZ); **John McDermott** (Reserve Bank of NZ); **Christopher Smith** (Reserve Bank of NZ); **Charles Elworthy** (European Academy in Schloss Wartin); **Geoffrey Mason** (Bank of NZ); **Maureen Janett**

(Auckland Institute of Technology, Faculty of Business); **Frances Harris** (Business & Economic Research Ltd)  
**Kelvin Sanderson** (Business & Economic Research Ltd); and **Sarah Mackay** (Environment Waikato)