

# Asymmetric information

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

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**New Zealand Association of Economists Inc.**

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# EDITORIAL

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I'm sure all readers of *Asymmetric Information* know of the deaths in recent months of two major figures in New Zealand economics, Sir Frank Holmes and Roger Kerr. The present issue contains an obituary of Sir Frank, and the next issue will include an obituary of Roger Kerr. In this issue, Mary Hedges shares some reflections on her period as President of NZAE. It is good to see that some economists continue to read and write books and, as ever, Grant Scobie shares his enthusiasm for a selection of books from his extensive reading. Stuart Birks returns with a regular opinion piece that he has called 'Frames'. We also have regular contributions from Statistics New Zealand and Motu, respectively on quality change and the CPI and firm performance. Paul Walker keeps an eager eye on Blogs. Before his recent move to a research chair in Public Finance at VUW, Norman Gemmell, in his role as Chief Economist at the Treasury, established the Government Economic Network (GEN). The nature and aims of the network are described in this issue. It is also good to see that, despite severe difficulties, there is considerable Research in Progress at Canterbury. If any readers would like to contribute occasional or regular pieces to *Asymmetric Information*, I'd be very pleased to hear from them.

## OBITUARY



### **Sir Frank Holmes – Public Economist**

For sixty years, Frank Holmes was a colossus of New Zealand's social and economic development.

His achievements were based on his standing and expertise as an economist and he was a leader of the economics profession in New Zealand. When he began his career, the principal professional associations were linked to

Australia, the Economic Society of Australia and New Zealand, and section G of the Australasian Association for the Advancement of Science. Frank was prominent in both. He maintained personal and professional links in Australia as the Australasian institutions declined in the 1960s, but as usual he was quick to recognise the path of change and he was among the founders of the New Zealand Association of Economists. He was the founding editor of its journal, *New Zealand Economic Papers*. Characteristically, he wanted *NZEP* to have an inclusive character, just as he argued for the main criterion for membership of the Association to be a genuinely enquiring interest in economic thinking.

Sir Frank emerged from the Deep South. His university study at Otago was interrupted by war. He flew a plane before he drove a car, and served in the Pacific. His accounts tended to emphasise bombing volcanoes rather than enemy soldiers but his diaries

show that the missions were serious and dangerous. When he returned to Otago, Frank joined the concentration of talent that crowded into the universities. He switched to economics and never looked back. He claimed that his student record was not distinguished because he was more concerned to pursue the holder of what now seems a quaintly-titled position, 'lady vice-president' of the Students' Association. Frank's own career in student politics flourished when the president of the Association vacated the position, learning that pursuit of the truth was not adequate excuse for appearing to advocate sexual freedom in Dunedin. But it was the acquisition of Nola which Frank always counted as the main benefit of his time in Dunedin. He migrated to Auckland to complete his University of New Zealand bachelor's and master's degrees in economics.

Until Nola's death earlier this year, she and Frank were a renowned and inseparable dance couple, flowing effortlessly across the dance-floor. Nola was however an independent person and pursued her own teaching career and hobbies. They also provided for a family, amidst postwar shortages, and then in Linden, Karori and Lowry Bay with a brief interlude (and later beach holidays) in the Bay of Plenty. Frank would explain the time of his arrival at the university as dependent on the state of the domestic economy, and Nola described how their infant son sat on the floor with a pencil and scraps of paper saying, "Go away. I'm busy." Frank was a teaching economist, but not to the exclusion of his family.

When he left the University for the second time, Frank said two significant things. First, that nobody who had contributed to his first farewell should feel obliged to contribute again. And secondly, that his heart was in the university and would remain so. It did. He never left. He returned, and directed the Master of Public Policy programme. He had been instrumental in its development from an earlier Diploma in Public Administration, a change which led the then Leader of the Opposition, Robert Muldoon to say that there would be only one Master of Public Policy in New Zealand, which was wittier than most of his spontaneous reactions but no more accurate.

Frank was very keen on injecting thought into all processes involved in public policy which was the basis of his enthusiasm for the MPP and the earlier DPA. He was also a good teacher across the range of university studies. He joined the then Victoria University College in 1952 and as a young lecturer had a good rapport with students. Lectures were mostly in the early morning and from 4 pm onwards. Frank lectured 6-7, and would meet the students down town before proceeding up the hill when the bar closed at 6 in time for the scheduled 6.10 start. Fortunately, in a small college lecture halls were not far from latrines.

As a teacher, Frank was good at guiding students to where interesting things were happening in the discipline, even in fields in which he was not himself interested or well-equipped, such as econometrics. While his own links were to Britain rather than the US, he was quick to recognise how the centre of the discipline shifted to the US in the 1940s and 1950s, and he advised students and recruited staff accordingly.

In 1959, Frank succeeded Horace Belshaw as Macarthy Professor of Economics. He was then able to lecture at less unsociable hours, but the university switched to full-time hours in the early 1960s anyway. Frank described his experience as head of department as being essentially an unrelenting effort to find appropriate staff to put in front of classes as burgeoning

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

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student numbers coincided with the small cohorts of the 1930s and 1940s and uncompetitive salaries. He nevertheless presided over a growing department which had four chairs by the time he ceased to be head in 1967. He also contributed in faculty and university affairs. The university council was sadly misguided when it maintained an established chimerical dream of a future in engineering rather than embrace Frank's vision of a future as a university with particular strengths in social sciences and public affairs. Robert Muldoon compounded the error about 15 years later when he vetoed Frank's appointment as chair of the University Grants Committee in retribution for uncongenial advice from the Planning Council chaired by Frank.

Frank generated a long list of publications. Most drew on the economics literature to generate commentary and recommendations on policy issues. When he returned to the university as Professor of Money and Finance in 1972-77, Frank thought he should become more academic and he produced a sound discussion of the New Zealand financial sector. But even that was not at the leading edge of the theoretical literature. Frank always wondered whether he had been wise to give up his plans in the 1950s to undertake a PhD but his forte was in applied work, and through the Institute of Policy Studies he generated a stream of studies of New Zealand's external economic policy and of social issues, especially but not only in health and superannuation. Nobody will be able to study New Zealand's economic and development without using material written by Frank. Furthermore, he greatly stimulated similar material from others. With long-time friend and ally, former Treasury Secretary, Henry Lang, and John Roberts, who Frank attracted to the university to teach the DPA, he was instrumental in founding the developing the Institute of Policy Studies. He was still a senior associate when he died.

It was as a public economist contributing to public affairs that Frank made his biggest contribution. He was diverted from any PhD project when in response to the unexpectedly strong showing of Social Credit in the 1954 election, the government established a Royal Commission and Frank was offered a post as one of its two major secretaries. Belshaw advised that the opportunity offered much more than a PhD, no doubt remembering his own experience in the 1930s, when service on a Monetary Commission added to the skills and experience he had as professor at Auckland and enabled him to embark on an international career as a development economist. Sir Arthur Tyndall, judge of the Court of Arbitration, chaired the Commission, and he took advantage of the government's wish for a wide-ranging enquiry which would securely bury Social Credit and led the Commission into a searching and thorough review of New Zealand's institutions and processes for all of economic policy. Frank was his principal ally. The Commission had to spend a lot of time on the claims of Social Credit and its contending factions, but Frank ensured that his colleague, Mac MacGregor, undertook most of that work, while he focused on management of the exchange rate, interest rate, monetary policy and other enduring issues. Perhaps it was recognition of the unfair distribution of work at the Commission that led Frank to recruit Mac to a retirement job at the university. The government's hope for a burial was more or less delivered as far as Social Credit theory was concerned but not for the last time, political activity long outlasted the invalidation of ideas.

The Royal Commission directly contributed to changes in how the Reserve Bank managed monetary policy and to the ability of Treasury to inject economic thinking into fiscal policy. It also led to the creation of an independent centre for economic research, N.Z. Institute for Economic Research, and after some delay, to the creation of a quasi-autonomous monitor of economic policy, the Monetary and Economic Council. Frank served two terms as its foundation, part-time, chair (1961-64).

The Monetary and Economic Council issued regular reviews of the current economic outlook for New Zealand. It issued one of the first serious studies of New Zealand's growth record and potential. It made major contributions to formulating policy towards economic integration with Australia before the New Zealand Australia Free Trade Agreement of 1965 which eventually led to Closer Economic Relations of Australia and New Zealand in the 1980s, probably the single most important policy development for New Zealand in the twentieth century. It contributed to debate about New Zealand's response to Britain's likely and eventual actual entry to the then EEC. Frank had recognized the significance of the EEC and advocated a positive response, when he spent some time on leave in London in the later 1950s, when Henry Lang was economic attaché at the High Commission. As a leader of the New Zealand economics profession, Frank participated in its light-hearted annual toast to 'the General' after de Gaulle's veto of British membership of the EEC but he was a leader in a more intellectual approach to the formulation of a sensible New Zealand response. The Council also studied New Zealand's financial development, drawing on Frank's academic work with the Bankers' Association staff college, and with the efforts of central banks to develop capabilities in South East Asia, Australia and New Zealand Bankers' courses.

While the Monetary & Economic Council continued under other chairs, (and Frank returned 1970-72), he had established a reputation which made him an obvious choice to chair a Task Force on Economic and Social Planning in 1976. In any case, after leaving the Monetary & Economic Council, Frank remained engaged in policy issues. He was active in the National Development Conference which was convened in 1969, partly in response to the Council's advocacy of "indicative planning" in an effort to reconcile the planning of different sectors of society and economy. Frank was a government-appointed member of the NZ Council for Educational Research. He had served the Parry Committee which was part of the process by which the components of the University of New Zealand became distinct universities. He readily extended his competence to the education sector as a whole – he was quick to recognize the development of the economics of education as a distinct sub-discipline. He was therefore the natural choice to chair the Advisory Council on Educational Planning which was more or less the educational arm of the National Development Conference. When the government changed in 1972, the task was magnified and he chaired the Education Development Conference which set out to map appropriate educational developments for the late twentieth and early twenty-first centuries. Progress was stalled for some time, but the work of the conference was eventually picked up, somewhat modified, in the 1980s. Frank's work in education continued. In the mid-1980s, he advised the then Trade Development Board on the benefits to be derived from the sale of educational services overseas and assisted it to implement the recommendations. He also chaired Consult New Zealand Education Ltd, the forerunner of New Zealand Education Ltd., another early component of the development of educational exports which are now a major component of New Zealand's external earnings.

The principal concern of the Task Force on Social and Economic Development was to integrate economic and social policy, and it resulted in the establishment of the New Zealand Planning Council. Frank was recruited from the university to be its foundation full-time chair. It absorbed the Monetary & Economic Council while establishing an Economic Monitoring Group to maintain independent economic commentary. The Council extended its role to social policy and began exploring how to maintain the benefits of a welfare state while restoring the primacy of individual initiative. It also attempted to maintain economic rationality in the face of the "growth projects" and

generally advocated a “more market” approach economic policy. Not surprisingly, despite Frank’s diplomatic skills, it fell out with Robert Muldoon. In the 1980s, the overall agenda of integrating social and economic policy was done more rapidly and with less adjustment assistance than the Council advocated. Like many of his contemporaries, Frank would have preferred a different balance of change and continuity but he knew that change had been unduly delayed. He continued to seek an optimal path especially in health and superannuation policy.

Frank’s first employment was as a diplomatic trainee with the predecessor of the Ministry of Foreign Affairs and Trade. When he joined the university he retained his interest in international affairs. One of the benefits of his war service was that he hitched a ride with the Air Force to an International Affairs meeting in Pakistan while the New Zealand delegation, including some colleagues at Victoria University, crashed at Singapore. Frank was eventually National President of the NZ Institute of International Affairs and its first life member.

Frank was the New Zealand contact for Asia Pacific economists as soon as they began to think about the implications for this part of the world of the growth of the EEC and the spread of economic integration in the North Atlantic. Kojima of Japan was the first to become prominent in advocating Asia Pacific free trade, and Frank was the New Zealand participant in the Pacific Trade and Development Conference from 1964. (That Kojima was a professional imperial dancer, who was still performing in the 1980s, may have created a further bond.) Frank was easily able to participate in the Pacific Basin Economic Council and in business councils when they began forming in the later 1960s. He also led New Zealand’s participation in the Pacific Economic Cooperation Council from its foundation in the 1980s. With the Institute of Policy Studies, he wrote a series of studies of how best to develop economic integration with New Zealand’s partners – Australia, Canada (as a proxy for the USA), Asia and Europe. Frank’s understanding of the changed position of Asia in New Zealand’s economic relations made him an obvious choice to be the foundation chair of what has become the Asia New Zealand Foundation. Frank combined clear vision of New Zealand’s changed international environment with an equally clear analysis of both potential and obstacles in New Zealand.

When he first left the university, Frank became planning and economic manager for Tasman Pulp and Paper Ltd. He was recruited by Geoff Schmitt who he knew well from his previous role at Treasury, but Geoff resigned on the day Frank arrived following a major disagreement with Bowater UK who held management control. Frank’s motivation was not entirely personal since forest products constituted a major part of the NAFTA agreement signed in 1965 and Tasman was at the forefront of a new outward orientation of New Zealand economic policy. For three years, he was active in forest product development in Australia and New Zealand.

When he left the Planning Council, Frank resumed his private sector career. He was director and chair of a number of private sector boards, including chairing the Norwich Union Group in New Zealand and the National Bank of New Zealand’s Southpac Merchant Finance subsidiary. Characteristically, he combined activity with study. He wrote two volumes of a 3-volume history of the National Bank of New Zealand. In 1983, he founded The Hugo Group, a venue for discussion of policy issues by business leaders, and he chaired it from 1989 to 2009. He became a distinguished fellow of the Institute of Directors to accompany his accolades as an economist – honorary degrees from VUW and Otago, the NZIER Prize in Economics, fellowship of the NZ Institute of Management, and a distinguished fellowship of the NZ Association of Economists. His knighthood was awarded for services to economics and education in 1975.

Frank’s career as an economist would be hard to reproduce now. It was built on using economic thinking to manage practical affairs. For the most part, it did not lead to publications in professional journals. Nevertheless, it certainly created new knowledge and disseminated it effectively. Frank led rethinking of the appropriate balance of private and collective activity, taking a thoughtful approach to the role of the state. Perhaps most notable of all was his role in reshaping New Zealand’s stance in the international economy, making a positive response to European integration with a more open trading stance and recognition of the enhanced role of the Asia Pacific region. He regretted some of the effects of increasing specialization but he found ways to preserve what was valuable. The Economic Society sought to combine in one conversation professional economists and business people. The NZ Association of Economists sponsors professional economic debate and organizations like the Hugo Group provide links between economic thinking and business issues. Frank was always a bridge of rare quality.

## NEW ZEALAND ECONOMIC PAPERS

by Mark Holmes

Since September, NZEP has been included in RePEc (Research Papers in Economics). This will serve to increase the visibility of NZEP. This is a collaborative effort of hundreds of volunteers in 75 countries to enhance the dissemination of research in economics. The heart of the project is the decentralized database of working papers, journal articles and software components. Among other things, NZEP now has citation-based impact factors that draw on the RePEc database. For more information, you can visit <http://ideas.repec.org/top/top.journals.simple.html>.

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

*New Zealand Economic Papers* has been published regularly since 1966. For many, it might be of interest to reflect on the list of Chief Editors over the years (I am grateful to Brian Silverstone for passing this information onto me). Of course, an invaluable service to NZEP over the years has also been provided by current and past Associate Editors and Editorial Board members.

NEW ZEALAND ECONOMIC PAPERS, CHIEF EDITORS			
Year	Volumes	Editor	University
1966 - 1967	1 - 2	Frank Holmes	Victoria
1968 - 1969	2 - 3	Ian McDougall	Massey
1969 - 1973	3 - 7	Albert Brownlie	Canterbury
1974 - 1977	8 - 11	Gary Hawke	Victoria
1978 - 1979	12 - 13	Allan Catt	Auckland
1980 - 1983	14 - 17	Brian Silverstone	Waikato
1984 - 1986	18 - 20	Paul Wooding	Otago
1987 - 1988	21 - 22	David Giles	Canterbury
1989 - 1990	23 - 24	Lewis Evans	Victoria
1991 - 1994	25 - 28	Tony Endres	Auckland
1995 - 1997	29 - 31	Dorian Owen	Otago
1998 - 2001	32 - 35	Frank Scrimgeour	Waikato
2002 - 2004	36 - 38	Tim Hazledine	Auckland
2005 - 2006	39 - 40	Ian King	Otago
2007 - 2010	41 - 44	Ananish Chaudhuri	Auckland
2011 -	45 -	Mark Holmes	Waikato

# PRESIDENTIAL THOUGHTS IN RETROSPECT...

When John invited me to write a brief article reflecting on my term as President I had reservations. However, the more I thought about it the more I realised that there were many aspects of the role that I was going to miss and that maybe I should write something on these. The difficulty is in separating out the role of President from my time on Council, the latter preparing me for the former.

One of the great privileges of being on Council was spending time with and getting to know the Life Members and Distinguished Fellows. These are the people who played important roles in the Association and in the profession respectively and their knowledge and experience about the background of a number of current activities was enlightening. They always seemed to be very aware of current initiatives and positive over the direction and innovations of Council. If they didn't agree with something they were also ready to offer constructive alternatives. Being in a position to gain this historical background, grounded in the current reality was incredibly useful. My advice to any economist would be to spend time with those who have gone before, learning from their experience and don't ever be afraid to ask questions. In fact the benefits I gained (and will continue to gain) from these and other senior people reminded me of an article by David Colander (a keynote speaker at the 2004 Annual Conference) 'Surviving as a slightly out-of-sync Economist' reprinted in his book *The Lost Art of Economics*. In that David explained:

"Where one learns about institutional realities is in late night, informal discussions with older economists. In these conversations, the older economists take down their guards and tell younger economists how the economics profession really works. Unfortunately, many graduate students and young assistant professors have not spent enough time in bars."

(Colander, 2001, p. 108)

Another fascinating aspect of the role was seeing the steady flow of new membership forms that come through. This really highlighted to me the diversity of our membership in terms of the background of our members and also the types of roles they currently hold. In fact, this is one of the greatest strengths and weaknesses of the Association. It is a strength in that it enables unique networking opportunities that many of our colleagues overseas can only envy. At the same time it makes it very difficult to deliver conferences and other events that will meet the needs of this diverse membership. Rather than being all things to all people we run the risk of not actually satisfying anyone – hence it becomes a weakness.

The last few years have seen a number of major administrative changes within the Association as we moved to bring our systems into the twenty-first century. This has given us the opportunity to look at what we do and how we can do it better. The improvements in moving the journal to Taylor and Francis, upgrading the quality of printing for *Asymmetric Information* and updating our administration and finance systems have all contributed to the more professional approach of the Association.

None of these activities would have been possible without the extraordinary goodwill and commitment of the Council members, our Secretary-Manager (Bruce McKivvet) and our Treasurer (John Gallagher). These people deserve the credit for the forward momentum evident in the Association.

On a more personal note I have loved my time on Council and as President. It gave me opportunities and contacts that I doubt I would have had otherwise. The people I got to work with on Council have been terrific colleagues and the experience has broadened my views on what economics is and what we as economists can contribute. As I now start to let go in my role as Immediate Past President I find there are things I miss already. While it was a role I took on with some trepidation I now find I am reluctant to let parts of it go. On the positive side I have built relationships with people that will continue into the future and if I get that without having to do the work it seems like a pretty good deal. I wish my successor, Stephen Knowles, all the best and look forward to becoming one of the 'oldies' who watches from the sidelines and provides support and background information when required.

Mary Hedges | Immediate Past President

## 2012 ANNUAL CONFERENCE

The Association's 2012 Annual Conference is being held **Wednesday 27 June to Friday 29 June**. The conference was originally planned to be held in Hamilton, but difficulties in securing sufficient space in conference facility there has led to the conference being moved to **the Convention Centre in Palmerston North**.

The original choice of Hamilton was made in response to feedback from our members that we should occasionally take the conference outside of the three main centres. With Hamilton now not available, our choice of Palmerston North for the 2012 conference reaffirms that commitment, which we hope our membership will support with their attendance.

A change for the 2012 conference is that we are re-introducing having some of the sessions have discussants. At the time of submission of an extended abstract, submitters will be asked to indicate if they would like to be considered for inclusion in a discussed session. A condition of being included in such a session will be a willingness to act as a discussant on another paper.

**The call for papers will be made in January, 2012.**

# FROM THE 2B RED FILE

by Grant M. Scobie ([grant.scobie@treasury.govt.nz](mailto:grant.scobie@treasury.govt.nz))

Tis always a pleasure to include new books by and for Kiwis. This time we start with a long awaited re-run, earlier editions of which have always had a place on my shelf. *Ralph Lattimore and Shambubeel Eaqub (2011) The New Zealand Economy: An Introduction* (Auckland: Auckland University Press). There are two bonus chapters by guest contributors: Gary Hawke on Technology in the New Zealand Economy, and Philip McCann on Cities and Globalisation: Is Auckland Special? Professor Hawke predictably traces the economic history of major technological changes, and concludes that in future our task will continue to be to adapt advances in knowledge generated offshore and use them to our advantage. Professor McCann focuses his economic geography lens on Auckland, concluding yes it is important, but so are regional centres and we need be sure they are all well linked.

But I stray from the body of the text, which like its forerunners is as informative and a compact a story as you will find anywhere about the New Zealand economy. It has a chapter devoted to each of the major elements of the economy, trade, industrial policy, labour markets capital markets and so on. Each chapter is built around one or more key data series, and a discussion that variously gives some historical perspective and importantly interprets developments in the New Zealand economy in the context of global economic development.

One can always find areas that seem to have bypassed – the role of education, the formation of human capital and the returns to schooling struck me as one such topic. But covering the universe in 170 pages is an unrealistic expectation. And there is tons of material here for the school and introductory university courses which is its prime market.

In conclusion let me draw your attention to an impressive feature. Volumes such as this suffer severely from the “rapidly out of date” problem. So while the authors have obviously laboured hard to minimise the data and publication lags, the statistical material ends in 2010 as a rule, and here we are racing into 2012. So the authors have provided a link to a website where all the underlying data are available and they undertake to update this quarterly. Whether or not the price you paid for the book is in part an implicit contract to have future updates of the data (for an unspecified period) is not immediately obvious. Do I have a claim if the quarterly updates stop next year? I shall leave these question for those more versed in contract law than I.

But wait: there is more Kiwiana. Between running a managed fund, a philanthropic foundation and riding motorcycles into obscure parts of the globe, one member of our profession somehow finds time to write books. In fact Gareth Morgan and various co-authors have managed seven books on public policy issues since 2006 (covering pensions, saving, investments, climate change etc) and five books (co-authored with Jo Morgan) relating their motorcycling adventures.<sup>1</sup> I get tired just recounting that sort of output.

So off goes our inimitable economist into the arcane world of taxes and welfare. Gareth Morgan and Susan Guthrie (2011) *The Big Kahuna: Turning Tax and Welfare in New Zealand on its head* (Auckland: Public Interest Publishing Co.). As an aside, I have grappled with the connection to the theme of the book of the Hawaiian word *kahuna*, which apparently referred to a priest,

witch doctor or other respected leader; I am sure it will be totally obvious to the readers one or more of whom will doubtless relieve my ignorance.

So what does tax and welfare look like turned on its head? (I assume the authors don't want us to conclude that it looks exactly as it does now if you look at the proposal upside down). The book starts with a race through the history and philosophy of redistribution from Plato to the Romans, through Smith, Mill and Marx to Galbraith, Rawls and Nozick. It then moves to set out what are fairly widely held principles of a good tax and transfer system: horizontal and vertical equity, efficiency, adequacy, and individual responsibility. The authors then assess New Zealand's current system, and not surprisingly find it comes up short.

This then lays the foundation for the grand entrance of the Morgan-Guthrie new world. Leg one of the double act is a comprehensive capital tax CCT (on everything that doesn't move and a few things that do) based on a minimum assumed rate of return. This would result in wage and salary income, capital income and the imputed return on all capital being taxed at a uniform rate. The transfer side is essentially the negative income tax (a favourite in my graduate school days) reheated and given a fancy name: UBI = unconditional basic income. Pay everyone a tax free basic income sufficient “to live with dignity”. All earned income would be taxed at a flat rate ( $t$ ) so the breakeven point comes when one's income is  $= (1/t)*UBI$ . In one sweep the clutter of rules and discretion that clog our current transfer system is gone. The rules are clear: set three parameters and stand back: the flat tax rate, the imputed return on capital, and the UBI. But then oops...we will need “complementary policies... to meet higher than average needs in particular situations” (p. 214) which sounds like a crack in the dam, and an invitation to regress to the current system. Which is to say that the political economy of all this is what really matters in the end – if a simple world of CCT with UBI were so superior surely we'd have seen it somewhere on the planet.

But let us not discourage brave souls from starting with a clean sheet of paper; their arguments will highlight the shortcomings of the current system and help us make improvements in mincing steps (rather than the big bang theory). And that seems to be the way world actually works.

Allow me a final gripe – there is no index (I can live with that) but not with the diabolical referencing system done with 477 endnotes involving endless repetition and with no way easily to find a particular reference. They had to work to make a system as cumbersome and obtuse as this when there are easy and helpful ways available.

But don't let that turn you away from reading a worthwhile addition to the debate on a topical theme, written in an accessible style, and well illustrated with examples.

1 I understand their next book is Jo and Gareth Morgan *Travels with the Emperor: Happy on a Harley 50 Fathoms down in the Southern Ocean* (Auckland: Aquatic Publishing (forthcoming).

# “FRAMES”

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

## Analytic versus synthetic: “Top-down” or “bottom-up”?

Forty years ago, in the context of national economic planning, Richardson distinguished between what he called analytic and synthetic approaches to forecasts (Richardson, 1971, p. 445). They could be termed alternatively “top-down” and “bottom-up” approaches.

He described the analytic approach as using a model to estimate overall growth, after which growth in the component elements can be deduced. The synthetic approach built on individual firm or industry estimates of future economic activity to construct an overall growth estimate.

Parallels can be drawn with applied economic analysis, whereby, under an analytic approach, our starting point would be a theory or model. We would then proceed to estimate the parameters and diagnostics, testing hypotheses and/or drawing policy conclusions. This is making the real world fit our theories, and is by far the most common approach. An alternative, a synthetic approach, would be to look at the real world evidence, seeing how individuals think and behave, and trying to form a picture of patterns and relationships.

While an analytical approach can appear to be more structured and may be expected to provide results largely in line with previous thinking, a synthetic approach is less constrained by an initial theoretical framing of the issues. Both approaches have their strengths and supporters.

To quote (emphasis added):

“Progress in economics does not depend only upon rigorous analysis, observation and measurement; it requires also that effort of imagination that enables us partially to escape from conventional categories of thought. Being realistic is not merely a question of testing hypotheses, important though this is; it also requires sustained and strenuous effort to *consider whether our inherited stock of theoretical constructions do not distort our vision of the plain facts of economic life.*” (Richardson, 1971, pp. 433-434)

Similarly Minsky (2008, p. 109) writes:

“In all disciplines theory plays a double role: it is both a lens and a blinder. As a lens, it focuses the mind upon specified problems, enabling conditional statements be made about causal relations for a well-defined but limited set of phenomena. But as a blinder, theory narrows the field of vision.”

In practice, analytic and synthetic approaches are both useful. Ideally a blend is required. However, at least in recent decades, economists have tended to focus on the analytic. Some point to the lack of a clear theoretical framework in the synthetic approach, seeing it as unstructured and lacking method. Some have taken this to the extreme, suggesting that analysis is real research only if it is clearly building on a model or theory. However, by focusing primarily on one approach, we may be missing low hanging fruit from the other. It is important to be open to alternative explanations and to recognise the limitations that come from adhering to the conventions. If nothing else, synthetic approaches may produce alternative hypotheses, after which analytic methods can be used to see if results can be replicated.

The analytic approach has a further limitation, as evidenced in Hamilton’s for “theoretical pluralism”. If each theory presents an artificial structure which, it is hoped, is a simplified analogy for some real world phenomena, then a better understanding may be obtained through the use of several theories. Hamilton made this point, while also highlighting another limitation of quantitative models:

“Researchers should carry with them a large repertory of theoretical orientations. They should be able to work with those theories, to think easily in those terms, and be able to apply them to any research materials at hand. One should pay special attention to theories that are no longer in favor, those that, possibly for the wrong reasons, have been rejected.” (Hamilton, 1996, p. 218)

He is not only calling for pluralism. He suggests that past theories may still be relevant, and we can find much of interest in economics that was written long ago. We could also consider the repertoire of available theories to include those from other disciplines. However, this faces an additional barrier, that of from communication across groups, each with their own language, perspectives, conventions and beliefs.

Hamilton continued:

“Tocqueville, describing the “characteristics of historians in democratic times,” said that they “attribute hardly any influence to the individual, but, on the other hand ... assign great general causes to all petty incidents.” One senses an “instant truth” here, the generalization bias having been carried to its extreme not by historians but by economists, political scientists, and sociologists. Although not popular, although virtually heretical, the “role of the individual” is a hypothesis deserving attention and thought, rather than the instant dismissal that is so often the case.”

In econometric terms, significant individuals could be considered as “outliers”, whereas we are looking for general patterns and universal rules. Consequently, as they fall outside a “narrowed field of vision”, they are likely to be omitted from our studies even though they may be highly relevant. This is one of the problems with “top-down” research. A similar point is made in favour of action research, which emphasises the importance of case-specific as compared to general factors (Birks, 2010).

An analytic approach imposes a structure by framing the issues according to economic theory. We may be more constructive and influential in wider debate if we start from that debate as it exists, seeing if we can improve on the quality of discussion from that basis. Of course, this might mean that we economists are also compelled to consider aspects that we might otherwise have overlooked. However, it can be more persuasive to talk in terms of the perspectives held by the target audience, and a plurality of perspectives may more accurately reflect reality.

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# ACCOUNTING FOR QUALITY CHANGE IN THE CPI

This article looks at how quality adjustment is used so that the consumers price index (CPI) measures only 'pure' price change. The CPI measures the changing cost of purchasing a fixed basket of goods and services. This basket needs to be representative of the spending habits of New Zealand households, and remain at a fixed quality so that changes in the CPI represent only price change.

The CPI has many uses, including:

- monetary policy setting;
- to adjust New Zealand superannuation and other Work and Income benefit rates;
- for wage negotiations; and
- as part of compiling official estimates of economic growth.

The Boskin Commission report on the CPI in the United States of America (Boskin et al 1996) points out the importance of a high quality CPI and the potential consequences of mismeasurement. Quality change is highlighted as an important consideration to ensuring an accurate CPI.

## Maintaining the quality of the CPI

Statistics New Zealand uses quality adjustment methods that are consistent with international best practice outlined in the International Labour Organisation's (ILO) resolution on CPIs (International Labour Organisation, 2003). These practices are used to ensure that the CPI is fit for purpose. These practices, which address both the representativeness of the CPI basket and the requirement to maintain a fixed quality, include:

- Updating the CPI basket and weights once every three years – the latest, 2011 CPI review was published in October 2011 (Statistics New Zealand, 2011a);
- Product and retail outlet samples are periodically reviewed – product specifications and brand shares were reviewed as part of the 2011 CPI review; retail outlets were last reviewed in 2006 and from 2011 these will be continually reviewed on a rolling basis;
- Quality adjustments are made when products tracked in the index have changed characteristics;
- Hedonic modelling is used to quality-adjust for used cars.

## Quality adjustment

The ILO resolution on CPIs states that it is necessary to monitor the characteristics of the products being priced to ensure that any relevant differences can be excluded from the estimated price change. These changes can be in the size, performance, or functionality of the product. Quality assessments put a monetary value on the change in characteristics between the old and new item, as perceived by the consumer. Statistics NZ uses several different techniques or methods, depending on the type of good or service being tracked.

## Product or outlet change

At times, the products scheduled to be priced are not available – they may be temporarily out of stock or permanently removed from sale. If a product is temporarily out of stock the price is carried forward from the previous period and alternative products are identified for possible use. Generally speaking, if the product is still unavailable at the next pricing period, the product, or if necessary the outlet, will be replaced by one of the products that was previously identified as a suitable replacement. If a class of item is removed from sale from an outlet, then it will in future be

tracked, where possible, in a similar outlet.

## Cheapest available specifications

For many products in the CPI basket, a specific product of a specific brand is tracked consistently. For others, the cheapest available option is tracked, regardless of brand. This is done for items that are deemed to have little quality difference across different brands, and for which consumers are unlikely to show much brand loyalty (and hence buy whichever brand is cheapest). For these items, tracking the price of one particular brand would not accurately represent consumers' buying patterns as well as the 'cheapest available' specification would.

Examples of where this method is used are frozen peas, white bread, white flour, standard homogenised milk, cheddar cheese, standard eggs, butter, and sugar.

All fresh fruit and vegetables are priced on the basis of cheapest available, as long as the variety chosen is of suitable quality for most uses. This mechanism also allows for a consistent pricing pattern in products where specific brands are not reliably available at all sampled retailers.

## Explicit quality adjustments

### Procedures to account for changing pack sizes

A common example of a quality adjustment is related to a change in pack size. For example, tea bags usually sold in boxes of 100 bags may come with 10 percent extra due to a promotion run by the distributor. In this case, consumers receive the benefit of an extra 10 bags, hence the recorded price would be adjusted to reflect the value to the consumer of the extra tea bags.

Similarly, 'quantity specials' are also taken into account. For example, if a loaf of white bread was \$2.00 in March 2011, and three loaves of white bread were \$4.80 in April 2011 (the single price remained \$2.00), then the price per loaf has decreased from \$2.00 to \$1.60, hence a 20 percent fall in price would be shown. These promotions are usually temporary, and the price might revert back to \$2.00 in May 2011, at which point the price series is adjusted again. Such quantity specials are used only where they are considered to be representative of the quantities likely to be purchased by households.

### New cars

Prices for new cars are one area where explicit quality adjustments are applied. When distributors report changes to the models being sampled, Statistics NZ asks for the 'perceived' dollar value of these changes to customers. To ensure the adjustments are consistent, they are checked against records of previous adjustments. When there are changes to the engine, Statistics NZ estimates the value of the quality change, based on maximum power and torque. The values of all changes between the two models are combined – in practice, this sometimes means an improvement and a removal of a feature cancel each other out.

Most quality adjustments to new car prices are made to remove the effect of improved or additional features, which increases the quality of the vehicle. In these cases, the value of the changes is removed from the retail price of the updated model to generate the quality adjusted price.

If, on the other hand, the quality adjustment is due to a removed or diminished feature, the value of the changes is added to the retail price of the updated model. In the 10 years from 2001 to 2011, most adjustments for lower quality were due to reductions in engine power or torque.

As part of an article for the October 2011 issue of Price Index News (Statistics New Zealand, 2011b), the index for new car prices was recalculated using the retail prices for the vehicles, rather than the quality adjusted prices. Over the 10-year period from the June 2001 quarter to the June 2011 quarter, the index based on retail prices increased 19.1 percent. The quality adjusted price series, which is used to calculate the CPI, decreased 1.5 percent over the same time period. The strong difference between these two price series – which implies an annual average increase in quality of 1.9 percent – illustrates the importance of quality adjustments in the CPI.

#### Option cost method

A method used for some products, is to base quality adjustments on the market value of optional features, or a proportion of the market value of optional features.

#### Hedonic regression models

Statistics NZ uses a statistical technique called hedonic regression to calculate the price index for used cars. The method was implemented in the September 2001 quarter. A used car can be seen as comprising a bundle of price-determining characteristics. Once these characteristics are identified and measured, the hedonic function can be interpreted as breaking down the car's price into the implicit prices and quantities of each characteristic. The price index can then be derived from the estimated price over time, after controlling for the changing quality composition of the cars being sold from quarter to quarter. An article in the July 2011 issue of Price Index News (Statistics New Zealand, 2011c) gives more detail of the methodology used.

#### Implicit quality adjustments

For some products, quality is implicitly controlled by calculating price change based only on products which are available in consecutive time periods. The 'product or outlet change' section described methods used when products are unavailable. If a product is unavailable for two consecutive time periods, and it is deemed unlikely to be stocked again, then a suitable replacement product, identified at the first instance of unavailability, will be used as a permanent replacement. Any difference in price between the original and the replacement product is assumed to reflect a difference in quality. This technique is called the 'overlap' method.

For rapidly changing products, such as flat-panel television sets, a quality assessment is required whenever a model is superseded and replaced.

The 'comparable replacement' method is used when the replacement product is judged to be very similar in quality to the old product, such as a newer model with only small superficial changes. In this case, any change in shelf price between the old and new models is shown in the price index.

When the replacement is judged to be of different quality to the old product, the method used is to infer the pure-price movement from products that are directly comparable from within the same region as the product being replaced. This is called the 'class mean imputation' method.

#### Future developments

Research is currently underway which aims to use retail scanner data to measure price change for some consumer electronic items, such as personal computers. This data contains sales values, quantities, and detailed information on the characteristics of the products. A number of methods can be used to construct price indexes from this data, including hedonic regression, which models and controls for the implicit prices of characteristics, and

recently developed methods such as the Rolling Window GEKS method proposed by Ivancic, Diewert, and Fox (2009). By using scanner data, all products sold across an entire period (such as a month) could be incorporated in the price index calculation, rather than the current approach of collecting ticket prices for samples of specifications in the middle of the quarter. See Krsinich (2011) for an explanation of the research currently underway in this area.

#### Conclusion

It is essential that the CPI is fit for its main uses, as these uses involve key decisions affecting monetary policy setting, indexation of benefit rates, and wage settlements. It must accurately represent consumer spending, and capture and adjust for the changes in quality of the products being priced. At Statistics NZ, practices that align with best practices from the ILO's resolution on CPIs are followed to ensure the CPI is fit for purpose. These include periodic reviews of the basket, outlets, and pricing specifications. Different methods are used to make quality adjustments, depending on the type of item and how to best represent consumer spending, and research is being undertaken to try to improve these methods.

#### For more information about quality adjustment in the CPI, please contact:

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Phone: (04) 931 4600 | Email: [info@stats.govt.nz](mailto:info@stats.govt.nz)

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# INTERNATIONAL ENGAGEMENT AND FIRM PERFORMANCE

By Richard Fabling

High quality data are critical to Motu's research and we go to great lengths to ensure that the data we use are fit for the question at hand. Statistics New Zealand's prototype Longitudinal Business Database (LBD) is a prime example of data capable of providing valuable insights into numerous policy-relevant questions. The LBD is a research database which links together a wide range of administrative and survey data sources including employment data from the Linked Employer-Employee Dataset, detailed overseas merchandise trade data from the New Zealand Customs Service, sales data from GST returns, firm performance data from IR10s and the Annual Enterprise Survey, information on business practices from a range of Statistics New Zealand's surveys (R&D, innovation, Business Operations Survey), and other information including participation lists for government assistance programmes. These data are linked at the firm level, allowing users to draw together information about many dimensions of firm activity and performance over a period of up to a decade.

Two recent papers by new Motu Senior Fellow Richard Fabling and Lynda Sanderson (Treasury, University of Waikato) provide examples of how the richness of this data can be exploited. These papers use the LBD to examine the relationship between internationalisation, firm performance and outcomes for workers. Both papers are concerned with explaining the productivity premium that internationally-engaged firms have over their domestically-oriented comparators. Understanding the sources and evolution of these differences provides one foundation for public policy supporting entry into international markets. Often cited in the policy debate is the argument that internationally-engaged firms become conduits for foreign knowledge that can be applied to domestic production processes. This knowledge may then spill over to domestically-orientated firms (serendipitously or through supply chains), giving them access to technologies that they otherwise would not have. These arguments are predicated on "learning effects" for the internationally-engaged firms.

In "Exporting and performance: market entry, expansion and destination characteristics," Fabling and Sanderson look at the effect of entering new export markets on firm performance, while in "You could be mine: foreign acquisition and the performance of New Zealand firms," they examine the impact of foreign buyouts on domestic businesses (both are available as Reserve Bank Discussion Papers).

These papers rely on the LBD's extensive coverage in several ways. Firstly, the data allow Fabling and Sanderson to compare firms which entered exporting or were subject to international acquisition with a control group of firms with "similar" initial characteristics (industry, recent prior domestic and export performance, and so on) but which did not enter exporting (or get bought by a foreign entity). These firms are compared across a broad range of outcomes for several years following export entry (acquisition), exploiting both the longitudinal dimension of the data and the breadth of information available for each firm.

Both papers conclude that internationalising firms are indeed larger and have higher productivity than domestically-focused firms, and that these traits exist prior to internationalisation. That is, better performing firms self-select into exporting and are more likely to be purchased by foreign buyers. This result is perhaps not surprising – in particular, modern theories of international trade contend that the fixed costs of exporting can only be borne by the best producers. The novelty of Fabling and Sanderson's work is in the examination of the dynamics of subsequent performance improvements.

For exporting firms, capital investment and expansion of the labour force are key parts of this story. Firms entering into exporting for the first time exhibit rapid growth in employment with a more than proportionate rise in capital investment, so that labour productivity rises by around four percent relative to matched control firms, while employment expands by an average of ten percent over three years. Among existing exporters expanding into new geographic markets, capital investment occurs prior to entry and employment gains are more modest. Overall, export market entry appears to raise aggregate labour productivity through a combination of capital deepening and resource-reallocation as the most productive firms expand into export markets.

In contrast, the results from the FDI paper are more muted. Fabling and Sanderson find no evidence that foreign buyouts affect firm survival or productivity, but acquisition does appear to have a mildly positive impact on employment, average wages and gross output. The authors consider whether the weaker results are perhaps due to heterogeneity in the motivations for buyouts – for example, if firms are targeted due to perceived under-performance relative to their peers we might expect to see improvements in productivity following acquisition. Similarly, it may be that high-performing firms suffer from dislocation following acquisition and take time to return to normal or, alternatively, that these firms experience large inflows of investment from the new parents which allows them to expand. The beauty of the LBD is that the data is of sufficiently broad coverage that subgroups of firms with different initial characteristics can be analysed separately. Doing so, the authors conclude that there is some heterogeneity in outcomes according to initial firm size, productivity, wages and capital intensity, but that the subgroup outcomes do not contradict the aggregate findings.

Development of the LBD is ongoing and, with funding from Motu's PGSF grant *Integrated economics of climate change*, Statistics New Zealand is currently integrating the Agricultural Production Survey into the database. With this investment, Motu researchers hope to improve our understanding of productivity growth in the agricultural sector and its relationship with changes in land use and other environmental outcomes.

# BLOGWATCH

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

As will be well known by now Roger Kerr died on the 28th of October. The extent of his influence is shown by the postings marking his passing on blogs around the world. Tyler Cowen at Marginal Revolution <<http://marginalrevolution.com/marginalrevolution/2011/10/roger-kerr-passes-away.html>> wrote "Roger had a huge influence on my life", while legal scholar Richard A. Epstein said "Today New Zealand ranks near the top on most indices of economic freedom. Much of the credit for that improvement goes to Roger, whose dedication and wisdom has made the world a much richer place." <[http://www.nzbr.org.nz/shop/Library+by+type/Articles/Roger+Kerr+1945-2011+An+Appreciation/x\\_show\\_article/1.html](http://www.nzbr.org.nz/shop/Library+by+type/Articles/Roger+Kerr+1945-2011+An+Appreciation/x_show_article/1.html)>. Back in April of this year Chris Trotter wrote of Kerr, "Roger Kerr, mouthpiece for the Neoliberal Nazgul of the Business Roundtable, deserves our admiration for his unceasing promotion of the capitalist narrative. Oh that the Left had such a fearsome ideological warrior." <<http://bowalleyroad.blogspot.com/2011/04/mislaid-narratives.html>>. Postings on other sites include Stephen Franks <<http://www.stephenfranks.co.nz/?p=3856>>, TVHE <<http://www.tvhe.co.nz/2011/11/02/rip-roger-kerr/>>, Don Brash <<http://www.scoop.co.nz/stories/PA1110/S00467/act-pays-tribute-to-roger-kerr.htm>>, Greg Lindsay <<http://www.incise.org.au/2011-10-29/roger-kerr-1945-2011/>>, Winton Bates <<http://wintonbates.blogspot.com/2011/11/what-motivated-roger-kerr.html>>, Bryce Wilkinson <<http://www.nzbr.org.nz/Roger+Kerr+The+Working+Man+and+the+M+an+and+His+Work.+Eulogy+by+Bryce+Wilkinson.html>> and Offsetting Behaviour <<http://offsettingbehaviour.blogspot.com/2011/11/roger-kerr.html>>.

Sir Frank Holmes also died recently. Colin James pays tribute at <<http://wellington.scoop.co.nz/?p=39578>>, Yahoo! News notes Sir Franks passing, <<http://nz.news.yahoo.com/a/-/top-stories/10757054/noted-economist-sir-frank-holmes-dies/>> and TVNZ has an item also, <<http://tvnz.co.nz/national-news/sir-frank-holmes-dies-4481027>>.

Somewhat strangely economic blogging has caught the attention of the World Bank. There is a new working paper out from the bank on "The Impact of Economics Blogs" by David McKenzie and Berk Özler <[http://www.wds.worldbank.org/external/default/WDSContentServer/1W3P/IB/2011/08/29/000158349\\_20110829130036/Rendered/PDF/WPS5783.pdf](http://www.wds.worldbank.org/external/default/WDSContentServer/1W3P/IB/2011/08/29/000158349_20110829130036/Rendered/PDF/WPS5783.pdf)> Their findings: "There is a proliferation of economics blogs, with increasing numbers of economists attracting large numbers of readers, yet little is known about the impact of this new medium. Using a variety of experimental and non-experimental techniques, this study quantifies some of their effects. First, links from blogs cause a striking increase in the number of abstract views and downloads of economics papers. Second, blogging raises the profile of the blogger (and his or her institution) and boosts their reputation above economists with similar publication records. Finally, a blog can transform attitudes about some of the topics it covers." So start blogging, its got to be good for you!

If you'd like to play with the data or replicate the paper's results, the data are available at <[https://blogs.worldbank.org/impacitevaluations/files/impacitevaluations/impact\\_of\\_economics\\_blogs\\_replication\\_data.zip](https://blogs.worldbank.org/impacitevaluations/files/impacitevaluations/impact_of_economics_blogs_replication_data.zip)> <[https://blogs.worldbank.org/impacitevaluations/files/impacitevaluations/impact\\_of\\_economics\\_blogs\\_replication\\_dofiles.zip](https://blogs.worldbank.org/impacitevaluations/files/impacitevaluations/impact_of_economics_blogs_replication_dofiles.zip)>.

There is addition discussion of this topic at VoxEU.org, <<http://voxeu.org/>>, where Paolo Manasse notes that economists make it their business to know about incentives. Indeed they devote entire blogs to the subject. But what, he asks, are the incentives for top economists to 'waste' time on these blogs in the first place? <<http://voxeu.org/index.php?q=node/7173>>

In New Zealand the economics of the rugby world cup has attracted the attention of Sam Richardson at his "Fair Play and Forward Passes" blog <<http://fairplayandforwardpasses.blogspot.com/>> On the economic impact of the cup Richardson writes, "And while we are on the economic

impact figure, there is a wealth of research that has shown that large sporting events rarely generate anywhere near the economic impact that is promised. Even if the economic impact of \$411m actually materialises (I'd say it is unlikely, but let's say it did), it would add no more than 0.2% to the nation's Gross Domestic Product. That is not a misprint. It is a very, very small impact. Surprising, really, that it gets the coverage it has received thus far." <<http://fairplayandforwardpasses.blogspot.com/2011/09/economic-impacts-of-rugby-world-cup.html>>

Richardson also comments <<http://fairplayandforwardpasses.blogspot.com/2011/10/one-measure-of-spending-and-it-is-not.html>> on the report by Paymark, who cover about 75% of all credit card transactions in the country, that spending on credit cards during the world cup "was up by \$195 million." Of this \$195m, the amount spent by tourists was \$70m up on the same period last year. \$70 million does seem that much of an increase. This suggests that the impact of spending by overseas visitors would appear to be quite a bit less than initially projected.

At Offsetting Behaviour and continuing the rugby theme, Seamus Hogan suggests a change to the rules to with uncontested scrums. "So my suggestion is to similarly change the rules to eliminate any advantage to arise from having a front-row player injured: Allow any team to request non-contested scrums at any point in a game, either because they have run out of specialist front-row players, or simply because they are being too heavily beaten by the superior scrimmaging of the opposition. Then, to reinstate the advantage that the team with the dominant scrum would have, allow the team that had not requested non-contested scrums to place one fewer players in the scrum. Currently the rules require teams to place at least seven players in the scrum, so I am proposing either increasing this to eight for the team requesting non-contested scrums, or reducing it to six for the other team." <<http://offsettingbehaviour.blogspot.com/2011/10/rules-that-create-wrong-incentives.html>>

At the TVHE blog <<http://www.tvhe.co.nz/>> Matt Nolan wants a real inflation measure. Matt argues, see <<http://www.tvhe.co.nz/2011/10/24/give-me-a-real-inflation-measure/>>, that the CPI is made up of two types of price changes: relative price changes and persistent pressure on the price of all goods and services to increase. He wants a better measure of the latter price pressure. But how to sort out one from the other? Ricardo Reis and Mark W. Watson have put forward a method they claim can distinguish between relative good prices and pure inflation <<http://voxeu.org/index.php?q=node/867>>.

At the Economics Today blog, <<http://razzakw.blogspot.com/>>, Weshah Razzak blogs on relationship between the market and government <<http://razzakw.blogspot.com/2011/10/market-and-government.html>>. Looking at Chinese growth data Razzak argues that before 1980, the Chinese economy grew slowly and it was not until mid to late 1980s that real growth started. This growth increased in the 1990s, and really sped up from 2000 onwards. Government intervention in the economy and society was greater between 1950-1970 than it has been since the mid 1980s onwards. Thus Chinese economic growth since 1990s has been associated with less, not more, government intervention. Bill Kaye-Blake is "Groping towards Bethlehem" <<http://gropingtobethlehem.wordpress.com/>> but on the way he has been arguing that "Sci-fi needs economists" <<http://gropingtobethlehem.wordpress.com/2011/11/03/sci-fi-needs-economists/>>. Bill has been reading a story which effectively finds the end of scarcity - the protagonists do away with constraints on space, energy, time and mortality.

In the August Blogwatch column mention was made of the reporting by Olaf Storbeck at the "Economics Intelligence" blog, <<http://economicsintelligence.com/>>, of the accusations of self-plagiarism levelled against Bruno Frey. Now Storbeck offers "A summary of the Bruno Frey affair" <<http://economicsintelligence.com/2011/07/07/a-summary-of-the-bruno-frey-affair/>> and reports on "Bruno Frey: More cases of self-plagiarism unveiled" <<http://economicsintelligence.com/2011/09/12/bruno-frey-more-cases-of-self-plagiarism-unveiled/>>. He also writes "On the merits of repeating oneself – A conference in defense of Bruno Frey" <<http://economicsintelligence.com/2011/10/27/on-the-merits-of-repeating-oneself-a-conference-in-defense-of-bruno-frey/>>.

# GOVERNMENT ECONOMICS NETWORK

by Joey Au and Norman Gemmell  
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Most people would agree that good government requires good advice built on high-quality information and robust analysis. Economic analysis is an integral part of developing the evidence-based that policy advice requires.

The New Zealand public service is rightly proud of the quality of its advice. However, there is scope to improve the level and utilisation of economic skills across the public service. Three broad areas where there is scope for improvement stand out:

## Strengthening economic capability

A greater focus on professional development for public servants trained in economics is needed, and as well as building greater awareness of economic concepts and frameworks across the public sector.

## Utilising economists more effectively

Skilled economists could be used more effectively and provide mentoring to junior staff. Smaller departments might also benefit from leveraging off the economics capability in bigger agencies and support in thinking about how to use their more limited economic capacity.

## Greater influence on policy

Economists can have greater influence on decision making by Ministers. The key messages emerging from economic analysis need to be communicated well in order to influence policy-making.

Recognising the scope for improvement, in 2011 a group of senior economists from public service departments established a network – The **Government Economics Network** (GEN) – to strengthen economic capability across government and to improve the use of economics in public policy analysis.

The GEN provides a mechanism to share resources and knowledge across the economics profession in government to help respond strategically to the concerns above. The network has three aims:

## 1 Support economics training and professional development

- For non-economists: support public sector agencies to foster interest in, and understanding of, economics issues and approaches, and applying economic tools in policy development and analysis.
- For economists: support public sector agencies to maintain and develop economics-based policy staff (professional development). This could include developing or arranging economic courses at an advanced level to help public service economists to refresh their theoretical economics and to stay up-to-date with methodological developments, including research techniques.

## 2. Develop linkages between economists

- Promote discussion and collaboration amongst lead economists and more junior economists across the public sector, including sharing approaches to economic issues and providing opportunities for peer review;
- Share resources across the public service in order to get better and cheaper access to economic databases and training services; and
- Strengthen links between public service economists and academic, think tank and private sector economists.

## 3. Strengthen economic advice to government

- Provide a repository for expert advice and guidance on economic issues and techniques which are common across government (eg. discount rates, value of life, measuring social costs, collecting and analysing data); and
- Provide advice from the economics profession to Chief Executives on the economic skills needed to maintain policy capability.

## Inaugural GEN Annual Conference

The Government Economics Network is holding its inaugural Annual Conference on the 14th December 2011. This will focus on the use of economics in public policy analysis. We are proud to present Professor Raj Chetty as the keynote speaker at the conference. Raj Chetty is a professor in the Economics Department at Harvard University. He was recently named one of the “top young economists doing work on real-world problems” in the New York Times and one of the best young economists of the past decade by the Economist magazine.

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

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 University of Canterbury. 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.

## Research in the Department of Economics and Finance at the University of Canterbury

As a consequence of the 22 February earthquake, the Department's usual place of work, the Commerce Building, will require major remediation to return it to code compliance. Failing that, the diggers will pick it apart. In the first semester of 2011, department members mostly worked from home. Since July, we have been working in temporary buildings constructed on a former playing field, getting used to open-plan workspaces. Teaching and research, however, continue. Here is a list of current faculty and their research interests.

**Steve Agnew:** *Teaching Fellow, MBS (Massey)*

Steven's current research interests are the impact of the interaction between ethnicity, gender and socio-economic status on student attainment in secondary school economics, assessment in first year economics classes, the impact of socio-economic status on financial literacy levels of secondary school students, and the correlation between student financial literacy levels and their financial decision making.

**Warwick Anderson:** *Lecturer, Ph.D. (Canterbury)*

Warwick's research interests are in the area of event studies and the associated time series analysis. More broadly, Warwick has ongoing research interests in aspects of financial distress, and in dividend policy.

**Jędrzej Białkowski:** *Senior Lecturer, Ph.D. (Europa-Universität Viadrina)*

Jędrzej is engaged in research projects with well-established academic institutions in Germany, Netherlands, Poland and United States. This international cooperation resulted in a number of papers and publications in reviewed journals. He has published in journals such as *Journal of Banking and Finance*, *Journal of Derivatives*, and *Quantitative Finance*. His research focuses on the derivatives products, risk management, algorithm trading and behavioural finance. Recently, he has started a new project on Socially Responsible Investing (SRI) mutual funds.

**Glenn Boyle:** *Professor of Finance, Ph.D. (Texas)*

Glenn's primary research interests are in topics related to agency problems and incentives, corporate governance, real options, and financial regulation. Some current examples include projects on the remuneration of bureaucrats, the value of partial information in an auction setting, and a post-reform history of NZ boards of directors. Glenn is also co-chair of the Australia-New Zealand Shadow Financial Regulatory Committee, a director of consulting firm Sapere Research Group, and a lay member of the NZ High Court.

**Jeremy Clark:** *Associate Professor, Ph.D. (Cornell)*

Jeremy's current research focuses on the effects of increasing social heterogeneity on social capital indicators such as volunteering and local support of schools in New Zealand, and tax compliance in the United States. He also has an ongoing interest in using lab experiments to test the predictions of cooperative bargaining theory as applied to environmental policy conflicts, as well as in the potential efficiency of addressing environmental externalities using uniform standards under complaints-driven enforcement.

**Eric Crampton:** *Senior Lecturer, Ph.D. (George Mason)*

Eric blogs at *Offsetting Behaviour*, New Zealand's most widely read academic economics blog. His current research interests include the correlates and consequences of voter ignorance, the pernicious effects of dodgy cost-benefit analyses on public policy outcomes, youth minimum wages, and election stock markets. He is Visiting Fellow with the Centre for Independent Studies, Member of the Mont Pelerin Society, and serves on the editorial advisory board of the *Journal of Entrepreneurship and Public Policy*.

**Huong Dieu Dang:** *Lecturer, Ph.D. (Sydney)*

Dieu's research interests include credit rating, financial distress, corporate governance and financial institutions.

**Kuntal Das:** *Lecturer, Ph.D. (UC Santa Cruz)*

Kuntal's research interests are in international economics, macroeconomics and applied econometrics. Current projects include central bank intervention and exchange rate volatility, effects of capital account liberalization, and the structure of sovereign debt.

**Susmita Roy Das:** *Post-Doctoral Fellow, Ph.D. (Virginia)*

Susmita's current research interests include Labour Economics, Development Economics, and Applied Microeconomics.

**John Fountain:** *Senior Lecturer, Ph.D. (Stanford)*

John's main research interests are the following: (1) concepts of beliefs in decision and game theory in joint work with Glenn Harrison, Lisa Rutsrom and Steffen Andersen; (2) a transactions-costs approach to current and historical NZ high Country land allocations, leases, rents and governing institutions; and (3) the grand synthesis of microeconomics, Bayesian statistical decision theory, and scoring rules. Also, John's office space was foundational evidence in support of the hypothesis that certain modes of personal organisation can be immune to large earthquakes, with no visible change in his 5<sup>th</sup>-floor office over a period spanning both a Richter 7.1 and a 6.3. He teaches an eclectic 3<sup>rd</sup> year Health Economics paper and also an introductory and interdisciplinary Game Theory paper, complete with edited screen and audio capture versions up for global consumption by thousands at proudlydimal on YouTube.

**Alfred Guender:** *Associate Professor, Ph.D. (North Carolina)*

Alfred is currently exploring the role of monetary policy in explaining the UIP puzzle. He approaches this topic from two different angles, one being a standard New Keynesian framework where he compares the merits of targeting and instrument rules. The other angle takes the workhorse model of modern finance, introduces stochastic volatility, and appends a simple instrument rule to the model with a view to examining whether the sum of these can explain the phenomenon that the currencies of high-interest rate countries often appreciate. Another line of research focuses on designing a price level index which could serve as an alternative to using the CPI as a target variable in stabilization policy.

**Philip Gunby:** *Senior Lecturer, Ph.D. (Western Ontario)*

Philip's current research interests include: the economics of education, occupational health and safety, the economics of standards and technological change, and how people process information about uncertain situations. Philip is finishing two projects with Michael Wilkinson about the amendments to the HSEA. He is also working on projects with Nigel Healey, and a paper with James Graham, about aspects of higher education policy in New Zealand. Together with John Fountain he is studying the relative effectiveness of different methods of presenting and thinking about uncertainty. He and Alan Woodfield have also begun a theoretical and empirical investigation of how competing schools use information to attract students, including an investigation of how different policy regimes, such as zoning restrictions, affect educational outcomes. Philip is also working on the economics of learning from technological disasters.

**Stephen Hickson:** *Teaching Fellow, M.A. (Canterbury)*

Stephen's research has focused on economics education - in particular assessment. He is also working with Andrea Menclova and Alan Woodfield on research into health and safety sentencing.

**Seamus Hogan:** *Senior Lecturer, Ph.D. (Canterbury)*

Seamus's current research interests include electricity markets, the economics of sport (particularly the analysis of on-field strategy in cricket), the mathematics of equilibria in oligopoly games, and work with Laura Meriluoto on auction theory applied to on-line auction mechanisms. He also has an interest in tax policy, mostly manifested as blog posts as an occasional blogger on Eric Crampton's *Offsetting Behaviour* blog.

**Philip McGuire:** *Senior Lecturer, Ph.D. (Chicago)*

Philip's current research interests include the following: tenure review in the South Island high country; flat income tax cum demogrant; the erosion of the American corporate income tax; how pensions and mortgages came to dominate the American financial system.

**Andrea Menclova:** *Senior Lecturer, Ph.D. (New Hampshire)*

Andrea joined the Department in October 2006. Her research interests lie in the areas of Health Economics, Public Economics, and Applied Microeconometrics. Her current projects include studies of the economics of childbearing, the socio-economic determinants of health outcomes in New Zealand, and the effects Health and Safety legislation.

**Laura Meriluoto:** *Senior Lecturer, Ph.D. (Simon Fraser)*

Laura's research is in industrial organisation and applied microeconomic theory, looking at topics as diverse as email pricing, spam control, the fixed-price-offer mechanism in on-line auctions, and diffusion lines in fashion industry.

**Les Oxley:** *Professor of Economics, Ph.D. (Tilburg)*

Les's research interests include modelling and testing theories of economic growth, financial econometrics, the knowledge economy/society, intellectual property, energy economics, and cliometrics. For his contributions, he was elected Fellow, Royal Society of New Zealand (FRSNZ) in November 2004, following the award of Elected Fellow, Modelling and Simulation Society of Australia and New Zealand, (FMSSANZ), in August 2000. He received the Biennial Medal, (Socio-economic Systems) from the International Environmental Modelling and Software Society (iEMSS) in 2006. Les is also an Affiliate, Motu, Wellington, New Zealand and Research Associate, Centre for Applied Macroeconomic Analysis (CAMA), ANU, Australia. He is one of the founding Editors, and currently Managing Editor, of the Journal of Economic Surveys (Wiley-Blackwell), Senior Editor, Mathematics and Computers in Simulation (Elsevier) and is on the editorial boards of several international journals, including Environmental Modelling and Software (Elsevier).

**Bill Rae:** *Lecturer, Ph.D. (Canterbury)*

Bill's research interests are financial time series analysis, in particular graphical modelling of multivariate financial time series and long memory in financial time series, international financial market integration, and the application of extreme-value theory to portfolio risk management.

**Bob Reed:** *Professor of Economics, Ph.D. (Northwestern)*

Bob is currently Head of Department. His research interests include the relationship between taxes and economic growth of U.S. states. Related, but not in a way that is obvious to the naked eye, is his research on the properties of panel data estimators in finite samples; and his simulation studies comparing the performance of alternative model selection strategies. The goal of the latter research is to come up with practical recommendations for (i) selecting across alternative model specifications, and (ii) deciding which panel data estimator should be used in particular data environments. He also has an interest in replication studies, and currently serves as Replication Co-editor of Public Finance Review. In addition, he is developing research collaborations with scholars at Chinese universities. That work has led to research on Chinese Overseas Mergers and Acquisitions, including a new methodology for estimating event studies when firms list their shares on more than one market; and estimating the effect of improvements in agricultural techniques on income inequality in rural China.

**Debra Reed:** *Senior Tutor, Ph.D. (Purdue)*

Debra teaches introductory finance and corporate finance at the advanced undergraduate level. Although a U.S. citizen, she has so strongly integrated into the local culture that she changed her Facebook profile picture to a silver fern for the duration of the Rugby World Cup!

**Maroš Servátka:** *Senior Lecturer, Ph.D. (Arizona)*

Maroš is a founder and Deputy Director of the New Zealand Experimental Economics Laboratory (NZEEL). He specializes in experimental and behavioural economics. Maroš is interested in what ways do fairness considerations and psychological factors, such as guilt, spite or reciprocity govern decisions of economic agents. Currently, he is working on a research program examining whether informal agreements foster trust and cooperation in the absence of formal contracts (co-authored with Martin Dufwenberg and Radovan Vadovič). In this program Maroš and his co-authors propose a new theory of negotiations and test it using laboratory and field experiments. His other projects include a couple of behavioural studies of firm boundaries (with Hodaka Morita), a real-effort experiment on gender competitiveness (with Bram Cadsby and Fei Song), a series of experiments exploring the effects of status quo in economic decision making (with James Cox and Radovan Vadovič), and a labour market experiment testing the effects of exogenous revenue shocks on long-term relationships between firms and their workers.

**Alan Stent:** *Senior Lecturer, Ph.D. (NSW)*

Alan's current research interests are valuation and real option analysis. He has a working paper combining risk neutral valuation with arithmetic Brownian motion, and is working on an application in real estate.

**Steven Tucker:** *Senior Lecturer, Ph.D. (Purdue)*

Steven is a founder and Director of the New Zealand Experimental Economics Laboratory (NZEEL), which is a state-of-the-art, unique-to-NZ, experimental economic research facility. Steven uses experimental economic methods to study research questions in a range of fields in economics such as industrial organization, financial economics, and macroeconomics. His research has dealt with a wide range of topics, e.g., explored factors that mitigate asset market bubble formation and studied mechanisms to provide public goods through voluntary contributions, to provide debt relief to developing countries, and to allocate foreign aid to address weakest-link international public goods.

**Richard Watt:** *Associate Professor, Ph.D. (Madrid)*

Richard's research is centred on applied microeconomic theory. The principal areas of application that he is researching are the economics of risk bearing (in particular, risk preferences, downside risk aversion, and the economics of insurance) and the economics of copyright (most recently, optimal/efficient pricing of copyrights, and contracts for access to copyrights under asymmetric information). He is also researching on the topic of optimal management of academic journals using a two-sided market perspective, and recently has been involved in experimental research concerning insurance fraud.

**Alan Woodfield:** *Adjunct Associate Professor, M.Com. (Canterbury)*

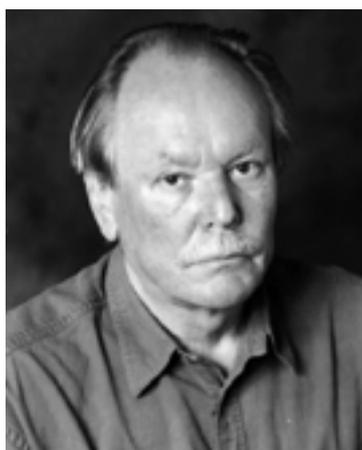
Alan's current research mainly concentrates on a long-run empirical study of sentencing in respect to Health and Safety in Employment Act offences in NZ in conjunction with Andrea Menclova and Stephen Hickson. Past work looked at the level of total employer financial liability, and they have a draft working paper in preparation dealing with the composition of sentences in terms of fines and awards to victims. A comprehensive database has been extended to deal with post-December 2008 cases when a new High Court guideline judgment imposed sentencing starting point ranges for fines at historically high levels. Stephen has been applying our econometric models to this database with a view to determining the extent to which sentences comply with the new guidelines and to compare actual sentences with those forecast by models estimated over earlier periods.

## NZAE SPECIAL INTEREST GROUPS

As part of the NZAE Council's efforts to add value to members, a number of special interest groups have been established and forums held. Groups include Auckland business economists, Christchurch economists, CGE modellers, and first year co-ordinators. Anyone interested in hosting a forum or establishing a group, please let me know.

Mary Hedges, Immediate Past President

# LEANZ LAUNCHES THE C W MAUGHAN FUND



The Law and Economics Association of New Zealand has launched the C W Maughan Fund to commemorate the life and work of C W “Bill” Maughan and to give members and supporters the opportunity to support law and economics education in New Zealand.

The C W Maughan Fund will be used to promote the development of law and economics education

in New Zealand, in particular by funding overseas study of law and economics by current or aspiring academics.

C W “Bill” Maughan will be remembered by some as an official at Treasury and subsequently as an economics lecturer at Massey University. Bill helped organise and took part in the study day at Massey which preceded the foundation of LEANZ and published several articles in *The New Zealand Law Journal* and *New Zealand Business Law Quarterly*. He then moved to the University of Bournemouth in England where, after stimulating interest and publication in law and economics, he was diagnosed with bone cancer and died in 2001.

Karl Maughan, son of Bill and well-known artist, is to donate the proceeds of a painting to the fund and LEANZ has transferred a lump sum into the Fund.

Anyone who wishes to commemorate any part Bill played in their lives, or who would like to support the growth of law and economics education in New Zealand can do so by following the instructions below. A charitable donation receipt will be sent, enabling donors who are New Zealand taxpayers to claim a charitable donation rebate.

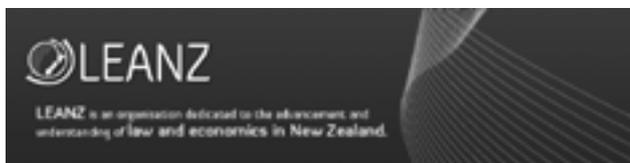
If making a donation by cheque, please make your cheque payable to “C W Maughan Fund”, and send it with your name and address or email address to:

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Branch: North End, Wellington  
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## 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.

## WEB-SITE

The NZAE web-site address is: <http://nzae.org.nz/>  
(list your job vacancies for economists here).

## MEMBERSHIP FEES

Full Member: \$120 | Graduate Student: \$60 (first year only)  
If you would like more information about the NZAE, or would like to apply for membership, please contact:  
Bruce McKeivitt - Secretary-Manager,  
New Zealand Association of Economists  
PO Box 568, 97 Cuba Mall. WELLINGTON 6011  
Phone: 04 801 7139 | fax: 04 801 7106  
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## MEMBER PROFILES WANTED

Is your profile on the NZAE website? If so, does it need updating?  
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The screenshot to the left shows a contour plot of a log-likelihood function for a GARCH(1,1) model fitted to a typical equity return series.

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