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Asymmetric information

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PAST ISSUES

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Conference 2013
3 – 5 July
in Wellington

EDITORIAL

John Creedy (john.creedy@vuw.ac.nz; John.creedy@treasury.govt.nz)

This issue of AI begins with Bob Buckle's obituary of Conrad Blyth, who died in August. This is followed by Brian Silverstone's interview of Alan Bollard, carried out shortly after Alan retired as Governor of the Reserve Bank. Our regular and much-valued contributions follow from Grant Scobie ('2B Red'), Stuart Birks ('Frames'), Paul Walker ('Blogwatch'), Mark Holmes (NZEP) and Motu. In this issue, 'Fine Lines' is contributed by Sholeh Maani. Many congratulations go to Norman Gemmell for his NZIER Award; the Citation and Norman's response is included here. In view of the Award, it also seemed appropriate to have Norman as the subject of the 'Five Minute Interview'. News of the busy Government Economics Network is again included, and the economics department at Waikato provides this issue's report of Research in Progress.

OBITUARY

Conrad Alexander Blyth (1928 – 2012)

Conrad Blyth, Emeritus Professor of Economics, Distinguished Fellow and former President of the New Zealand Association of Economics (NZAE), died in Wellington surrounded by his family on the 7th August. Conrad was an influential leader and pioneer of the New Zealand economics profession. He had a major influence on the development of two institutions of significance for New Zealand economics (the New Zealand Institute of Economic Research, NZIER, and the Department of Economics at University of Auckland). He was involved in several New Zealand policy review processes and institutions (as Chairman of the NDC committee on industrial protection, as a member of the Ross Committee on Taxation, the National Research Advisory Committee, and the New Zealand Planning Council and Economic Monitoring Group). By example, teaching, and encouragement he fostered the development of numerous young New Zealand economists who established successful careers in various parts of the world.

Conrad played a significant part in the internationalisation of the New Zealand economics profession. In addition to positions he held in New Zealand, at various times he held positions at Cambridge University, the Australian National University (ANU), the National Institute of Economic and Social Research in London, and the OECD in Paris. He was, at various times, a member of expert groups for UNCTAD, the Commonwealth Secretariat, and the Institute of National Affairs of Papua-New Guinea. Through his New Zealand and international roles, Conrad enhanced our understanding of economic growth, business cycles, and the significance of commodity prices in economic development. He influenced attitudes toward New Zealand's development strategy and the policy momentum that eventually led to the dismantling of import protection and subsidies, and to the internationalisation of the New Zealand economy.

Conrad was born in Dunedin and attended the University of Otago where he graduated MA with First Class Honours in economics in 1951. Although Conrad's undergraduate degree was in both history and economics, the opportunity to be a paid tutor in economics influenced his choice of post-graduate study. History nevertheless was an enduring interest. He was particularly generous in his acknowledgement of the influence Harro Bernadelli (a former student of Schumpeter) had in sparking his interest in the study of business cycles, introducing him to the international research literature on capital theory, and for encouraging him to study New Zealand trade with the Pacific Islands for his Master's thesis. Bernadelli also introduced him to Hayek's *Road to Serfdom* and libertarian ideas. These were themes that were central to his career as an economist and to his influence on New Zealand economic policy.

His interest in these topics flourished as a PhD student at Cambridge University (which he attended on a Cambridge Studentship) and as an Assistant Lecturer and Fellow of Pembroke College where he experienced at close quarter, the playing out of the famous Cambridge capital debates. His

Members are invited to submit brief articles on any issue of interest to NZAE members, and/or comments and suggestions.
Enquiries and contributed articles should be sent to John Creedy (john.creedy@vu w.ac.nz; John.creedy@treasury.govt.nz).

PhD thesis was on the theory of capital and was supervised by Richard Goodwin. Piero Sraffa may also have played an advisory role in some capacity. His approach was influenced by the ideas of the "Austrians", Böhm-Bawerk and Wicksell which were also introduced to him earlier by Harro Bernadelli. During his time at Cambridge he published articles on capital theory in *Econometrica* and *Economica.* He published research on the post-war US business cycle in the *Economic Journal* and *Review of Economics and Statistics.* The study of business cycles appealed to Conrad not only from the point of view of explaining them, but also as a basis for macroeconomic forecasting, and during this time he published a book with Allen & Unwin on *The Use of Economic Statistics.*

The late 1950s and early 1960s was to prove to be a watershed for the New Zealand economics profession. The NZAE, BERL, the Monetary and Economic Council, and the NZIER were all established in a short period. As the first Director of the NZIER in 1960 and the third President of the NZAE in 1964-65, Conrad was at the vanguard of some of these important developments.

The NZIER was established in 1958 as a result of the initiative of Horace Belshaw, Macarthy Professor of Economics at Victoria University College, and a quartet of Wellington businessmen, who were encouraged by the recommendations of the Royal Commission on Money, Banking and Credit Systems 1956 and the Reserve Bank of New Zealand, and by the support of the Prime Minister, the Hon. Walter Nash. It was another year before Conrad was appointed as Director and yet another year before he was able to arrive in Wellington and commence in this new role. On arrival in July 1960, he became aware of some impatience on the part of NZIER members who had paid two years' subscriptions before seeing anything for their contributions. He would recall with amusement the fact that on arrival he was faced with the practicalities of getting office accommodation in a house in Kelburn adjacent to Victoria University that was partly occupied by a student tenant. And in a memoir written for the 50th anniversary of the NZIER, he recalled that no one told him that it would be wise to arrange to take a car from England with him on the ship due to the continued shortage of cars and foreign exchange in New Zealand at that time. Despite these challenges, Conrad quickly revealed a capacity unostentatiously to acquire resources and get things done, and he quickly brought the Institute to life. Conrad gave 28 years, one-third of his life, to the NZIER as Director from 1960-1965, as Trustee Member of the Board from 1973-1979, and as a Board Member from 1989-2006.

Conrad made New Zealand economic growth the NZIER's research theme under his leadership. Conrad was well versed in the 1950s revival of growth theory, Solow's work on factor productivity and technical change, and was familiar with how the Cambridge Department of Applied Economics functioned, and perhaps the work of people like Alan Brown for example (who he cites in his 1975 *Economic Record* obituary of Bill Phillips). In the first NZIER research paper *Economic Growth 1950-1960*, Conrad provided the first published growth accounting decomposition and estimates of aggregate and sectoral labour productivity growth in New Zealand and exposed New Zealand's relatively slow labour productivity growth. An impressive and cohesive programme of growth research, policy analysis, seminars and public engagement followed from this initial study. Ground-breaking research included tackling measurement problems, deriving measures of effective production, investigating output employment and productivity growth. He was familiar with Chenery and Clarke's work that demonstrated how programming models can be applied to development problems and the allocation of resources on a national scale. He applied these ideas in developing the Blyth-Crothall linear programming model of the New Zealand economy to investigate alternative growth policies.

Throughout this period, Conrad found it difficult to escape the arguments over the impact of protection and import licensing on New Zealand's productivity and income growth. His solution was to float the exchange rate and dismantle protection and in a 1964 book which he edited, *The Future of Manufacturing in New Zealand*, he considered how the economy might develop in response to "a liberalized environment ... with no quantitative import licensing and no discrimination in tariffs or in export incentives, but with an adjustment of the exchange rate". These were, at the time, controversial views and on one occasion during a series of lectures to farmers' organisations, he discussed the possible use and functions of a free market for foreign exchange. The upshot was that the Chairman of the Board of the Institute, who was also CEO of one of the banks, received a telephone call from the Prime Minister asking if the banks were trying to pressure his government to devalue the currency.

Before leaving the UK, Conrad visited the National Institute of Economic and Social Research in London and received advice from Christopher Saunders, the Director, who was in the process of launching the National Institute Review which contained macroeconomic analysis and forecasts of the British economy. Influenced perhaps by this work and his interest in business cycles, Conrad started the *Quarterly Survey of Business Opinion* (QSBO) and *Quarterly Predictions* (QP). QP was started using the NZIER's own quarterly estimates of national income and expenditure and is now in its 48th year. The idea for the QSBO arose, it seems, from suggestions by Colin Simkin, Professor of Economics at Auckland University, and Harro Bernadelli, who were familiar with the Munich based ifo Institute's konjuncturtest, although the original survey form was modelled more on the Bank of NSW-ACMA survey form. The QSBO is now in its 53rd year. Fifty years later the NZIER remains one of New Zealand's premier economic monitoring and forecasting organisations.

Through Conrad's leadership and with the advantage of its close proximity to Victoria University and cooperation with the University Economics Department (by then headed by Frank Holmes) and the Applied Mathematics Laboratory of DSIR, the Institute emerged as an incubator for young economists. Research Assistants at the Institute during Conrad's time as Director included Rosemary Atkinson, Graham Crothall, Brian Easton, Colin Gillion, Kerry McDonald, David Sewell, and Stephen Turnovsky. McDonald and Easton were to become the fourth and fifth Directors of the NZIER respectively.

After his term as Director of the NZIER, Conrad spent the next seven years overseas. He was a Professorial Fellow at ANU from 1965-1968 where his time there briefly overlapped with that of Bill Phillips. While at the ANU his work on business cycles continued. He assisted the Bank of New South Wales in revising its own survey of business opinion and wrote a monograph on American business cycles from 1946 to 1950. He was also appointed a member of the Ross Committee established in 1967 to review New Zealand's tax system and which made the first tentative suggestions of a GST type of tax. He then returned to the UK as Deputy Director at the National

Institute of Economic and Social Research (NIESR) from 1968 to 1972. One of his achievements at the NIESR was to persuade the UK Treasury to finance research at the Institute to develop a set of leading economic indicators along the lines of the well established NBER indicators for the US. Des O'Dea was recruited to undertake the research and the British Central Statistical Office was to eventually publish these indicators.

Conrad returned to New Zealand in 1972, this time as Professor and Head of the Department of Economics at the University of Auckland. Conrad remained a Professor at Auckland and continued to teach after his official retirement in 1993 until 2002 with one break from 1979- to 1982 when he was at the OECD. On this occasion he was Head of Department until 1977 and was again to have a significant influence on the development of the New Zealand economics profession and policy debates.

As was the case when he was Director of the NZIER, Conrad had to face the difficulties of recruitment of economists in New Zealand. He nevertheless succeeded in appointing people who would go on to have successful academic careers, including Robin Court, Roger Bowden, Ken Jackson, and Claudia Scott. Jas McKenzie was seconded from Treasury for two years. Later in his term Carl Walsh was recruited for a period of three years. Alan Catt, who had previously been Conrad's Deputy Director of the NZIER and first Editor of Quarterly Predictions and who had subsequently spent four years at the IMF, was recruited from Waikato University in 1977. His earlier mentor, Harro Bernadelli, was a member of staff during this time, as was Bill Phillips. Conrad was later to write an obituary of Bill Phillips which was published by the *Economic Record* in 1975. In 2009, Conrad also contributed entries for Horace Belshaw and Malcolm Fisher in the *Biographical Dictionary of Australian and New Zealand Economists*.

Conrad returned to the theme of New Zealand economic growth in his inaugural lecture where he took a different to that which he took while he was Director of the NZIER. He argued that industrialization was taking place "naturally" in New Zealand and that protective policy was playing little part. He distinguished between primary manufacturing protected by transport costs and secondary manufacturing dependent on real wages. Employment and output in primary manufacturing, he argued, had tended to follow the development of the farming export sector while the growth of the secondary sector, on the other hand, had followed the decline in real wages relative to those in other industrial economies. Conrad discussed industrialization and other issues, including the alternatives of monetarism and free markets in a series of essays he wrote as the inaugural economics writer for the *NZ Listener* during 1976 and in 1977 (a role he relinquished when he went on leave at the end of 1977 and which was taken up by Brian Easton).

Conrad's interests in business cycles and the role of commodity prices in economic development were manifest in his macroeconomics and comparative economics lectures, Master's classes on the Great Depression and business cycles, and in graduate research theses he supervised. He introduced a course on the history of economic thought at the third-year level. Conrad was particularly proud of the later achievements of his students. Research theses done under his supervision included those by Jon Altman (later to become Professor and Director of the Centre for Aboriginal Economic Policy Research at ANU), Anna Garden, and Alan Bollard (later to become the seventh Director of the NZIER, Secretary to the Treasury and Governor of the Reserve Bank) in the 1970s, Suella Hansen and Martin Hames in the 1980s, and Alasdair Scott, Helen Kerr, Julian Williams, Jonathan Reeves, and David Bates in the 1980s. Hugh Fletcher (later to become CEO of Fletcher Challenge and a member of several corporate Boards and the Reserve Bank Board) was also a student in his classes and wrote a memorable course paper on the question as to whether the Great Depression could happen again.

During this period and in the 1980s, Conrad's internationally recognised expertise on the development of island economies and the impact of commodity price fluctuations led to his appointment to a number of international inquiries. He was appointed to an IMF-sponsored inquiry into the nature and feasibility of commodity price forecasting. In 1985 he was a member of an UNCTAD group of experts chaired by Nicholas Kaldor, a former Cambridge colleague, to report on the problems of low and unstable commodity prices for non-oil commodity producers. Conrad was to later recall that the group divided into a Kaldor group advocating price stabilisation and a group led by Hendrik Houthakker which argued that stabilisation would not work. Conrad's friendship with Kaldor survived his joining the Houthaker group. In 1982 he was appointed to a Commonwealth Study Group that reported on the problems of the world financial and trading system and included recommendations under the title "Towards a new Bretton Woods" published by the Commonwealth Secretariat.

As a result of the part he played in a United Nations Development Advisory Team in 1974, Conrad was to undertake several further research visits to Papua-New Guinea during the 1980s and 1990s. He saw Papua-New Guinea as a case study of the effect the international business cycle had on commodity prices and a developing economy. His interest in this topic was reflected in his supervision of graduate theses written by Alan Bollard and Jon Altman.

After his first term as Head of the Department of Economics at Auckland University, Conrad took leave to join the OECD as Director, Social Affairs and Industrial Relations, from 1978 to 1982. On returning to New Zealand a third time, he was again Head of the Department of Economics in Auckland from 1982 to 1986 and served on the University's Senate and several University standing committees. And he was to again play an active role in New Zealand economic policy debates.

While serving with the OECD, Conrad had been invited to become the new, full-time Chairman of the NZ Planning Council (an initiative of Sir Frank Holmes and the Hon. Brian Talboys, Deputy Prime Minister). He declined when Prime Minister Rob Muldoon insisted the Chairman must reside in Wellington, and instead agreed to be the part-time Deputy Chairman and Convenor of the new Economic Monitoring Group (EMG). Other members of the EMG were Gary Hawke, who was awarded Distinguished Fellow of the NZAE in 2005, and David Smythe, an Auckland stockbroker.

The Planning Council and the EMG were established with the purpose of providing an alternative source of economic policy evaluation and proposals, a role similar to that of the earlier Monetary and Economic Council. While endeavouring to manage the difficult task of balancing its role as critic and also trying to influence change, the EMG published a series of reports which concluded that faster, sustainable economic growth required an extensive liberalization of the economy. During Conrad's membership of the Group it published reports that included: *Foreign exchange constraints, export growth and overseas debt* (1983), *Strategy for growth* (1984), *Government* *deficit and the economy* (1984), *Foreign exchange market (1985) and The regulated economy* (1985), topics that Conrad had been concerned with 20 years earlier as Director of the NZIER. Although the writing was not as forthright as some may have liked, the themes were clear enough and the Council and the EMG played a role in the development of thinking that underpinned the thrust of economic reforms that were to follow over the next decade.

While Conrad was in favour of the eventual economic policy revolution that was to take place during the late 1980s and early 1990s, in later years as an observer of the liberalization process, he considered that the particular sequence of market reforms, along with the size of the government budget deficit and high inflation, contributed to unexpected costs and delayed benefits from reform. These concerns were reflected in his 1986 NZIER AGM address entitled *The Economic Consequences of Mr Douglas* and his introductory chapter, "The Economists' perspective of economic liberalisation", written for a book on New Zealand's reforms edited by Alan Bollard and Bob Buckle, two of his former students, and published in 1987 by Allen & Unwin. The complications to price signalling that high inflation can cause was also a prominent theme in his book on New Zealand inflation published in 1977 by Allen & Unwin.

In a career which spanned academia, public policy, research institutes, international advisory groups, and several countries, Conrad has had an enduring influence on the New Zealand economics profession, institutions, and the careers of many younger economists. And in a manner comparable to Horace Belshaw (who was appointed University of Auckland's foundation Professor of Economics in 1927 and Macarthy Chair of Economics at Victoria University in 1951) before him and his contemporary Sir Frank Holmes (who succeeded Belshaw as Macarthy Chair of Economics in 1959), Conrad was able to bring his academic insights and skills to bear effectively on New Zealand economic debates and policy. The NZ Association of Economists appropriately recognised Conrad's outstanding contributions when they awarded him, along with Sir Frank Holmes, one of two inaugural Distinguished Fellows of the Association in 2004. Conrad is survived by his wife, son, two daughters, and six grandchildren.

Bob Buckle,
14 November, 2012.

Sources: Antony Endres, Suella Hansen, Michael Walls; Rachel Barrowman, *Victoria University of Wellington: 1899 – 1999*, Wellington, Victoria University Press, 1999; Robert A. Buckle, "Conrad Alexander Blyth: Citation for the Award of Distinguished Fellow of the New Zealand Association of Economists", *New Zealand Economic Papers*, 38 (2), 2004, pp. 147-149 (a fuller version read at the Distinguished Fellow Award dinner in Wellington in 2004 is available from the NZAE website: http://www.nzae.org.nz/nzae-news/distinguished-fellow/conrad-blyth-awarded-distinguished-fellow-of-the-nzae/); *A History of the Economics Department of the University of Auckland*, 2006 version, University of Auckland Library; and *The evolving Institute: 50 years of the NZ Institute of Economic Research*, 1958 – 2008, pp 59, http://nzier.live.egressive.com/sites/nzier.live.egressive.com/files/The-evolving-institute.pdf

AN INTERVIEW WITH ALAN BOLLARD

(Wellington 15 October 2012)

Brian Silverstone

Alan Bollard's outstanding professional career to date has included leadership roles as Director of the New Zealand Institute of Economic Research (NZIER), Commerce Commission Chairman, Treasury Secretary, Reserve Bank Governor and, shortly, Executive Director of Asia-Pacific Economic Co-operation (APEC). He has Honorary Doctorates from Auckland and Massey Universities.

FORMATIVE INFLUENCES

Q: When did you decide on a career in economics?

A: Well, Brian, there was no sudden blinding moment of insight in my case! I certainly did not start off thinking about a career in economics. Indeed, I didn't know what economics was all about as it was not a school subject. I enrolled at Auckland University in 1969 intending to do a degree in history, english and political studies. To assist my history, I wanted to do an economic history paper which required Economics I. That is how I got into economics and I found I liked it much more than I had expected. Perhaps it was because I am a tidy person. I liked the way neoclassical economics fitted together: there was a marginal rate of something that equilibrated to another marginal rate of something else and it all locked together. I thought that was a very organised way of looking at the world. Of course, ever since then I have spent my time learning that life isn't like that. But it was an interesting starting point and I just went on from there. Economics was also, perhaps, a reaction to my parents who were scientists. I tired of all their science talk, but I was interested in social science, that is, explaining how people behave.

Q: So did you drop out of history?

A: I don't remember making a decision about majoring in economics. I did a year or so of english, history and political studies and after that I moved towards economics and mathematics. Political studies, english and history at Auckland were all well taught at that time - lecturers like Bob Chapman, C.K. Stead and Keith Sinclair. The Maths Department probably taught me more about econometrics than the Economics Department.

Q: Are there any particular books which stimulated your interest in economics?

A: I have always read widely. I enjoy reading books about economists and economic history, especially where they put issues in context and show some of the drama of learning. I also enjoy books that appeal to the general public. My father took me to hear J.K. Galbraith in Auckland in the 1960s. His *Age of Uncertainty* was the economists' equivalent to Kenneth Clark's *Civilisation*, putting history in its context, showing where Marx fits in, where Keynes fits in and so on. I also enjoy biographies such as Skidelsky's three-volume *John Maynard Keynes* and Sylvia Nasar's biography of John Nash, *A Beautiful Mind*. There is also great a biography of Alfred Marshall as well as one on Charles Babbage. When I was researching the global financial crisis, I read several interesting biographies of Franklin Roosevelt. Central Banking has its share of eccentrics - read Liaquat Ahmed's fine *Lords of Finance*.

Q: Many people can point to a teacher, lecturer or supervisor who has had a significant influence on their education, perhaps taking it in a different direction from what they had in mind? Did you have this experience?

A: Not so much in my case. Colin Simkin was a traditional lecturer and Peter Phillips also lectured me. John McRae was a young Scottish lecturer who came to the Auckland Economics Department with a lot of enthusiasm for development economics which was also one of my main interests. Reading Gunnar Myrdal's *Asian Drama* was an eye-opener. I went to Tonga to do fieldwork for my masters degree and to one of the Cook Islands for my PhD. When Conrad Blyth came to Auckland he brought enthusiasm and intellect. My PhD was supervised by Roger Bowden and Conrad Blyth together with Fred Fisk from ANU.

NZIER DIRECTOR (1987-1994)

Q: Elsewhere you have reflected in detail on your time at the NZIER (Bollard 2009), but could you nevertheless outline the circumstances of your Institute appointment, the challenges and the major outcomes of your tenure as Director?

A: The Institute was going through a difficult phase when I returned from the UK in 1984. Brian Easton was the Director. He was very invigorating, full of enthusiasm and a great thought-provoker. Unfortunately, the Institute was running into financial problems, made more pressing by the macroeconomic reforms at the time. Both the Secretary of the Treasury and the Reserve Bank Governor removed themselves from the Board of Trustees. They also removed official funding from the Institute. This was somewhat ironic as the funding had been originally promised to the Institute from the government in the late 1950s but deliberately channelled through the Reserve Bank so there would be a degree of independence for the Institute. Now the Reserve Bank was claiming it was up to them to decide on whether or not funding should continue.

The loss of funding was very hard for the Institute given its limited resources. Meanwhile Brian Easton left, and David Mayes came in as Director for a year and then left quite abruptly. The first I knew about his departure was when Institute Chairman Ray White came to my home. He said the Institute Board had just met in emergency session and wanted to appoint me as Director starting the next day. My first task was to prepare a plan to close down the Institute if it proved necessary: an unusual way to begin a chief executive job! It was a crisis and rather stressful, but we got through it. It wasn't easy.

I had to learn not only to manage myself and other people, but also how to build a sensibly-funded private research programme mainly through consultancy. At the same time, many New Zealand firms who had felt a public benefit duty to support the Institute no longer felt that way. They were also suffering during this period of radical change. The trading banks were starting to employ economists and producing free economic forecasts. Understandably, firms questioned whether it was worth them paying money to be a member of the Institute. This meant I had to spend considerable time marketing our services.

On a positive note, we had some interesting work to do given the extent of restructuring in the public and private sectors at the time. Looking back on our work, we kept the forecasting side going and we did considerable work on state-owned enterprises and industrial structural change. We had a great team of economists, many of whom have since gone into chief economist and similar roles throughout New Zealand. Under my successor, Alex Sunderkov, the Institute became increasingly orientated towards commercial consulting. MOTU has picked up on the growing public funding and filled some of that gap. More recently, under Jean-Pierre de Raad, the Institute has returned to straddling public good, public research and consulting.

Q: One of your interests while at the Institute was the refurbishment of one of the Phillips machines, your memorable demonstration at the 1991 NZAE Conference at the University of Waikato and, ultimately, its installation in the Reserve Bank Museum. How did your interest in Phillips and the Phillips-Newlyn machine emerge?

A: I met Bill Phillips in 1974 in Auckland. He was the quiet chap who came into the room on a walking frame, sat down and did not say very much. Then afterwards, someone said 'that's the famous Bill Phillips'. I saw him a few times, but that was about all. He lectured my wife, Jenny Morel, on the Chinese economy.

I love seeing visual presentations of data and interesting ways of analysing it. The Phillips-Newlyn machine called the MONIAC (standing for 'Monetary National Income Analogue Computer') is a great expository device, developed in a period when computing was in its infancy**.** So what did Phillips do? He took a black box and turned it into a white box - something one could see right through. It is a complex and very sophisticated machine. When it was built in 1949, it was probably the only way to solve an economic system of that sort with differential equations.

I read an article in *The Economist* in 1987 saying that London School of Economics (LSE) had rebuilt one of its two machines. I contacted the LSE and said 'what about giving New Zealand the other machine'. They were very good about the request. It was a big exercise. I had to raise a lot of money so that we could get it to a model rebuilder in London, get it transported to New Zealand and into a rundown garage in Halstead Street in Wellington for assembly. We had quite a difficult time putting it together as it was so complicated. I had help from David Mayes, Institute staff, and others.

Recently, the Institute generously lent the machine, on a long-term basis to the Reserve Bank Museum. This is an appropriate place as the Bank has the engineering resources to maintain the machine. It is demonstrated regularly by enthusiastic economists. Go and see it! In 2010, the University of Trento in Italy held a conference devoted solely to the Moniac. Most of the papers (edited by Vela Velupillai 2011) are available as free downloads.

Q: You have now embarked on a biography of Bill Phillips. Is this venture intended for a general audience, an academic audience or both? Do you anticipate new insights?

A: A biography of Bill Phillips is something I have had in mind for some time. I have been gathering material for decades and I am now using my brief period between jobs to make a start. I am writing for a general audience and I hope any intelligent reader will find it fascinating. Phillips led a most interesting life, both intellectually and physically. For me, the really interesting thing is how his background, and the events around him, influenced what he was doing and thinking. One interpretation, which I don't accept, is that he was an electrician with a screwdriver in his pocket and went about fixing things. He was a lot more than that. He was creative. He was brilliant. He was a genius. One does not rub shoulders with a genius many times in life. I am enjoying trying to understand the man.

One has to be careful in recreating someone's life after the event that you don't falsely attribute motives or events. For example, I see no evidence that Bill Phillips decided early on that he wanted to change the world or to become a great economist. He is not well known in New Zealand, maybe a reflection on our cultural views about commerce, economics and higher learning. If he had been a rugby player or mountaineer it would be different. I made several approaches to Te Papa Museum to offer them the Moniac machine so that New Zealanders could own it and see it. It was, after all, good enough for a Moniac machine to be in the British Science Museum just metres away from the Babbage analytical engine. Te Papa rejected the offers.

COMMERCE COMMISSION CHAIRMAN (1994-1998)

Q: What was the background to your appointment as Chairman of the Commerce Commission?

A: The invitation to be Chairman came out of the blue. I had been at the Institute for a decade. It was a very interesting period because at that time business in New Zealand was coming off import licensing and regulatory controls and was subject much more to 'the market'. There was a question about what competition trade-offs would work for a small open economy. New Zealand was caught between allowing large companies to dominate industries and exploit economies of scale on the one hand, and having the benefits of competition and open entry on the other. We were able to apply some basic economic principles around competition and contestability. It was a particular period for two classes of company in New Zealand: big utilities that had been corporatised and smaller New Zealand businesses who were having to cope with a new Fair Trading Act which prohibited misrepresentation.

Q: What cases within Commerce Commission activities (Fair Trading, Consumer Credit, Business Competition and Regulated Industries) do you most recall and with what success?

A: Under the Fair Trading Act we had to deal with some cowboy operations. That should have been fairly straightforward, but at first the district court struggled with some of the concepts. We tried to help educate judges in a very subtle way, because to my surprise they refused to accept offers of formal training courses. Things eventually improved, but it did take a while.

The Commerce Act is different. It is more complex, analytically difficult and legally complicated. We faced issues around behaviours such as price-fixing, misuse of market dominance and intentions to lessen competition. One of the classic cases I remember was the prosecution of North Island meat companies for fixing the prices they would pay farmers for animals. These practices had persisted, and some business people felt there was no harm in price fixing. These were very long and costly cases.

Another class of issues related to dominant behaviours. A major case related to new entrants trying to set up services at the Port of Nelson. This case went through the High Court, taking many long tedious years, but finally reaching a resolution. There were also business acquisitions and mergers to adjudicate. One of the most memorable was Air New Zealand and Ansett. Air New Zealand wanted to take over the failing Ansett operations. By a split decision - my vote - we ruled that they couldn't take over domestic operations but they could take over the Australian operations.

We built up economic talent in the Commerce Commission headed by Michael Pickford so that we could establish economic frameworks to guide our thinking. We did quite a bit of work defining and measuring (as far as possible) producer and consumer surplus, Harberger triangles, static and dynamic public benefits and costs. It was more founded in microeconomics than previously. In addition, we employed better quality investigators and lawyers to take the cases through the courts. I had to learn, that just because you are trying to enforce the law, you cannot assume you will win cases.

There were also big issues in areas like health, where there were district health board issues caught by the Commission, and particularly difficult ones like electricity and gas and above all, telecommunications. It was the period just after Telecom had been privatised but before some of the technical developments were in place, so Telecom was in a dominant position. They also learnt pretty quickly the techniques of legal obfuscation and delay. When I came in, the Commerce Commission was in almost permanent dispute with Telecom with a no-win situation for either side.

We had to rationalise quite a bit of that. But then they and other telecommunication firms did engage in long, tedious litigation some of which did deliver some interesting concepts such as Baumol-Willig pricing. Overall, it was quite hard to get economic concepts though courts. It was something else I had to learn.

TREASURY SECRETARY (1998-2002)

Q: Incoming executives usually have the opportunity to review directions and, hopefully, 'make a difference'. Did you initiate any major changes in organisation or direction during your time at the Treasury and, if so, how did they work out?

A: Good question! I'm not sure about the answer though. I was invited to take the Treasury position and was there for five years. It is a very hard job indeed, harder, I think, than being Reserve Bank Governor. You are juggling lots of balls in the air all with various analytical, policy and political consequences. The Reserve Bank Governor's responsibilities are clearly laid out in the Act. But the Treasury Secretary has to be able to operate in a very ill-defined space. I look back on that period and now think that I might have done things a little differently. At that time, I was partly repairing scars from the difficult period of reform in the 1980s and 1990s. The Treasury had some important achievements in that period, but that came at a cost. I felt they paid too much attention to microeconomic issues and not enough to macroeconomics. There was a feeling that if you got all the microeconomic settings right, you should not have to worry about other things. Of course, you do.

When I arrived, I felt the culture was very influenced by contractual managerialism. I wanted to open things up and I think we had some success in that. I reduced the levels of hierarchy, although that took a while to achieve. I think it paid dividends, though, as people felt freer about the things they wanted to say. The culture was evolving from a 'there is no alternative' mindset.

I was not the innovator at the Treasury. Graham Scott and Murray Horn were the innovators. I was trying to make the organisation work better in a challenging political environment. When I was appointed, Winston Peters was Treasurer, Bill Birch was Minister of Finance and it was the last years of the National Government under Jenny Shipley. They were trying to privatise some assets with fragmenting support. The subsequent Labour Government under Helen Clark and Michael Cullen both distrusted Treasury, and it took quite a long time to connect with them. This was all challenging and exhausting. Another very difficult period was the crisis around Air New Zealand getting into financial strife and, at the same time, the attack on the World Trade Centre in New York in September 2001 (9/11).

On my first day as Secretary I had 13 appointments, and life went on like that for five years. Treasury is a bit of a factory as well. It could be producing 10 or 20 policy papers every week for ministers. You cannot get your head around everything. You have to be able to rely on colleagues. You have got to know where you can make a difference and affect outcomes. You also need to be the one who is trying to ensure the best possible spending around government activities. Every other part of government has good reasons why it should spend more, so that is a big challenge, and I wonder whether I could have done better there.

Q: What Treasury projects do you particularly recall and with what success?

A: I think we improved macroeconomic forecasting during my time as well as more work understanding the drivers of growth. I feel we might have achieved better budgetary control, but we were really entrenching the Fiscal Responsibility Act which has since proved its worth. At the time, our approach was quite radical. It is now the standard recommendation for countries seeking to act in a fiscally responsible way. We did a lot of work on productivity, growth and comparative studies. I got in talented people including Bob Buckle, Geoff Lewis, Grant Scobie and David Skilling to think about the bigger picture. Although we built up credible frameworks from this work, it didn't deliver easy policy outcomes.

Looking back, I am a bit self-critical about my time at the Treasury. From hindsight, I think we should have paid more attention to private decision-making that seemed short-term rational, but has not proved socially optimal in the longer term. I am thinking particularly about the household sector which was starting to build up large imbalances at the time due to its lack of savings, as opposed to the government sector. The institutional view in Treasury was people will make rational decisions and they should be left to do so. But we have learned from the global financial crisis that there are externalities to consider: broader macroeconomic, retirement income, financial and exchange rate implications. We could have framed the debate in a better way.

RESERVE BANK GOVERNOR (2002-2012)

Q: As Bernard Hodgetts (2012) has interviewed you on most aspects of your Reserve Bank Governorship, I have just a few questions. In the public - and in many political minds - the Reserve Bank is usually portrayed as an institution pursuing single-mindedly a price stability target without regard to other aspects of economic activity. Yet Clause 4(b) of the Policy Targets Agreement says that 'In pursuing its price stability objective, the Bank .... shall seek to avoid unnecessary instability in output, interest rates and the exchange rate'. Why has the Bank apparently failed to get across the message that its price stability goal is in fact constrained - or supposed to be constrained - by the very matters (such as output, employment, interest and exchange rates) that observers say should be taken into consideration in setting monetary policy?

A: This is a challenging question. The Reserve Bank Act 1989 was written in a way that allows one to elevate the relationship between monetary policy and prices above other macroeconomic variables. This interpretation was probably more useful during the Bank's initial experience with targeting: if you need to be an inflation-buster, then that should be your message; *strict* inflation targeting. Nowadays, New Zealand and the 22 other countries that have since adopted a monetary policy framework based on the Reserve Bank Act, would all regard themselves as being *flexible* inflation targeters, meaning that although there is a primary objective of price stability, there are other secondary objectives or, as some view it, constraints.

So the Reserve Bank would maintain that it is a flexible targeter using Clause 4(b) of the Act to conditionalise monetary policy decisions. As an example, were we too slow to increase the Official Cash Rate (OCR) during the housing boom of the 2000s? From hindsight 'yes', though arguably from foresight 'no', because we were taking into account other things such as the exchange rate. It is all being discussed again at the moment. Asset price stability, for example, might be a candidate for inclusion in Clause 4(b). Incidentally, it is easy for many New Zealanders to believe that the Reserve Bank can simply pull levers, such as 'just drop the OCR and the exchange rate will fall'. We know there is no simple relationship like that, though some New Zealanders will not accept that.

Q: Professor Milton Friedman's famous and influential 1967 presidential address to the American Economic Association included two sections: 'what monetary policy cannot do' and 'what monetary policy can do'. Monetary policy cannot, he said, peg real interest or unemployment rates for more than very limited periods while monetary policy can both prevent money itself from being a major source of economic disturbance and provide a stable inflation background for the economy. Four decades on, and from your experience, to what extent would you agree with Friedman?

A: Nowadays, we have a different tool (the short term overnight interest rate rather than the money supply as the key instrument) and there have been data advances and modelling developments. Putting these points aside, I would agree with Friedman on this point about what we can and cannot do. We see examples of this with the global financial crisis and the subsequent unorthodox monetary policies. It does worry me when you see a central bank being forced into taking action because the other arms of government are not able to implement fiscal policy properly. There are still a lot of people who think the Reserve Bank can do things it cannot do. My parting shot as Governor was to say 'get real about what the Reserve Bank can achieve'. In New Zealand this has historically been about influencing the exchange rate. There has been a view that 'no one else can bring it down, so you must be able to undertake this task.'

Q: Any frustrations with fiscal outcomes in New Zealand?

A: Yes, at times, but nothing like what the Federal Reserve and European Bank must be going through because we have not been in a really difficult fiscal state. There was an increase in spending in the last couple of years of the Labour Government that from hindsight has been unhelpful. Our fiscal position has taken a hit during the global financial crisis, of course, but is recovering gradually.

Q: In early 2006, well before the global financial crisis broke in August 2007, you received a report on 'Supplementary Stabilisation Instruments' (2006) as part of a Finance and Expenditure Committee Inquiry into whether there might be useful tools 'with a direct bearing on the housing market ... which could supplement the central role of interest rates in managing inflation'. What, ultimately, was the outcome of this Inquiry? With hindsight and with the Reserve Bank (2007) submission to the Committee in mind, were there any lost monetary policy opportunities from this Inquiry?

A: We should distinguish the Reserve Bank work from the Inquiry itself. We had prepared several pieces of work on stabilisation instruments. From this we concluded that there were wedge tools that might close the gap between the cost and use of funds and in ways that might lessen exchange rate pressures. We were, however, quite worried how such tools would work practically and the distortions they would bring. We also pushed for changes in the tax treatment of property that would make the tax situation more neutral to investment decisions. We have picked up on what has come to be called macro-prudential tools and we have come to regard those as possible supplementary short-term measures. The Inquiry on Housing was useful, but some of the recommendations around planning were resisted, such as land supply in Auckland. I know it is a difficult topic, but if Auckland wants to develop as a major metropolitan area and not impose a high cost structure on New Zealand, it will have to take much harder decisions.

Q: Michael Bordo, in his interview with Aaron Steelman (2011), blames 'United States housing policy back to the 1930s and government regulators being captured or not being on the ball' as the proximate causes of the 2007 global financial crisis (GFC). In New Zealand, there have, since 2009, been numerous regulatory changes relating to finance companies with some of these changes under the jurisdiction of the Reserve Bank. Do these measures, in hindsight, reflect the fact that 'light-handed' financial regulation was a failure and that Michael Bordo was substantially correct regarding regulators 'not being on the ball'?

A: This is a very wide-ranging question with commentators devoting whole books such as Howard Davies (2010) *The Financial Crisis: Who is to Blame?* and my GFC experience *Crisis: One Central Bank Governor and the Global Finance Collapse* co-authored with Sarah Gaitanos (2012, 2nd edition). The GFC stemmed from a complex interaction of causes, and attempts to put blame on particular people or institutions usually trivialises this complexity. The behaviour of regulators, however, is certainly part of the story. It varied considerably in different countries. For example, the failure of investment banks in the United States was a completely different story to the finance company debacle in New Zealand. I agree with Bordo that the regulatory problems in the States are connected to the housing market and to the 'American dream' of home ownership. I have always felt, however, that bank regulators should not try and be too clever, because there are usually ways around regulations in the capital markets. Indeed one of the core things that highly-paid, well-resourced investment bankers do is to arbitrage around regulations.

Finance companies in New Zealand were not actively regulated. They are now being regulated by the Reserve Bank alongside building societies and credit unions. This is going to be a very hard sector to regulate efficiently because firms are small, diverse and entrepreneurial. We shouldn't be trying to regulate risk out of the New Zealand capital market. Our main aim has been to make the risk as transparent as possible. This is being done indirectly through trustee supervisors. It is not a great model, but we could not think of a better one.

For me, though, bank regulation is far more important. When I arrived at the Reserve Bank I thought this area needed some rejuvenation. And we have done that. We did face-off a challenge from the Australians who wanted to control the regulatory side in New Zealand. The GFC showed that we were right to insist on our own policy tools. There remains a risk that we could go in the opposite direction and become over-regulated in response, say, to the pressures from Europe with consequent deadweight costs on the banking sector. Remember that next time the crisis will be different!

Q: In also discussing causes of the global financial crisis, Paul Krugman (2009) analyses the blindness of many economists 'to the very possibility of catastrophic failures in a market economy'. There was, he said, a misplaced belief that assets were priced correctly for risk, that financial market behaviour through incentives could be trusted together with a failure to appreciate the long history of financial crises. Is this fair comment?

A: Krugman combines a number of assertions here. Were economists blind to catastrophe? The good economists I know have always allowed that such things are possible, but have also pointed to the practical problems about modelling and predicting major failures. We have models that are better at explaining cyclical behaviour rather than large sudden change, and certainly they have not been good at demonstrating financial-induced catastrophes. I guess Krugman is correct that some economists did not know their history or thought that regulation would preclude that happening again. I guess a lot of economists, myself included, were certainly surprised at the speed and severity of events such as the massive price movements in many financial markets.

Q: Then you get the situation where the credit agencies changed the rating for institutions abruptly from AAA to junk bond status.

A: The record of the credit rating agencies on sub-prime was very poor and reflects the fact that they and the investment banks had considerable trouble estimating tail-end risks and the contagion effects. With globalisation, events can be triggered quickly across the world. I recall someone asking Alan Greenspan about the subprime market pre-GFC and Greenspan responding that it was pro-efficiency and pro-stability (based on the immense size of the sub-prime market). Maybe Paul Krugman wrote about this beforehand. Some people think credit agency ratings are predictive when it is well-known that they are not a lead indicator - they have always been reactive. Do I think we should continue to have agencies rating finance companies and banks? Yes.

Q: The Reserve Bank Museum was your idea, Alan. Has it met or exceeded your expectations, has the level of interest continued and what further developments, if any, would you like to see?

A: It has met my expectations. Prior to the museum, we had a large, high-ceiling, ground-floor banking hall that was no longer used. The museum is a great space with a well-designed layout. To me, it has been especially useful in showing the roles of a full-service central bank. There are not many full-service central banks worldwide doing monetary policy, bank and financial sector regulation, payment and settlement systems, foreign reserves management and currency. The museum helps to instil a sense of history and contributes to the broad area of financial literacy. Go and visit it!

RESEARCH AND PUBLICATIONS

Q: During your leadership roles, you maintained a very wide range of research interests resulting in many books, monographs, papers and presentations. These interests have included agriculture; economic and political reform; industry structure and development; markets, regulation and pricing; trade and tariff policy; the role of technology; business dynamics; computer simulation and the global financial crisis. What pleases you particularly from these interests?

A: I consider myself an applied economist and lucky to have been able to work and enjoy a range of research interests starting with development policy at the South Pacific Commission, industry policy in the UK, a wide range of policy topics at the Institute, fiscal policy at the Treasury and monetary policy at the Reserve Bank. Next I am going to be focussed on trade policy at APEC. I am interested in how policy impacts and how it makes a difference, ultimately, to people's lives. I also enjoy putting economic issues within the bigger picture, and explaining it in intelligible ways. This is the approach, for example, that I took with *Crisis* (Bollard 2012).

Its not all crisis; I like some economic fun as well. I enjoyed co-authoring (with Graeme Davidson and Greg Allum) a computer software game *Oikonomics* (*Oik*) designed to simulate an economy pretending you are Minister of Finance. It got sold in an educational version in the United States and pirated in Taiwan which was flattering. (We didn't make any money out of it though). Don't ask me for a copy - it is now technically obsolete. For some time, I have had a novel in progress called *The Rough Mechanical*, a novel of war and post-war experiences, with just a hint of economics. It will be self-published electronically (through Xlibris), hopefully before Christmas 2012.

Q: Unlike most academics, you have been in a position to see the results of your research implemented in either actual policy changes or, at the very least, influence debates. Could you give some examples of where you believe your work has resulted in either actual policy changes or has influenced debates?

A: That is quite a hard question because in good systems single people do not usually make a single difference; it is teams, processes and institutions that make a difference. I have never done anything particularly innovative like some of the pioneers of economic policy in New Zealand, nor been a leader of new thinking. I have, however, tried - with others - to make things work better. I would point to the work at the Institute in the 1980s designing better state-owned enterprises, a better competition framework at the Commerce Commission, improved macroeconomic surveillance of the New Zealand economy at the Treasury, working through the consequences of macroeconomic imbalances for a small open economy and improved bank regulation at the Reserve Bank. Some of this sounds a bit general, but that's the nature of public policy economics.

APEC EXECUTIVE DIRECTOR (2013-)

Q: In response to the announcement of your appointment as Executive Director of the APEC Secretariat, you are reported as saying that you were looking forward to working with the 21 member economies 'to achieve APEC's common objective to expand free and open trade and investment in the region' and 'achieving reinvigorated growth and development through greater cooperation'. What major aspects of New Zealand's reforms, if any, and from your wider experience, would you be likely to encourage the APEC Secretariat to consider?

A: There are reforms that New Zealand has done that are now relatively common around the Pacific Rim. I am not, however, really going into this position thinking what APEC can learn from New Zealand. It may be the other way around. APEC is an umbrella over a whole bunch of different systems, economies, forms of governments and economic policies which are all trying to unite within some broad framework. I am still trying to feel my way to an understanding what it is that APEC can do to further promote economic prosperity in the region - international integration, harmonisation of rules, good regulatory practice - those sort of things. In the first instance, I shall be listening. The APEC economies have been through massive growth, but I don't think it is easy to say how much of that is due to APEC, how much to national factors, and so on.

OVERALL (1984-2012)

Q: Your return to New Zealand in 1984, and your subsequent leadership roles at the Institute, Commerce Commission, Treasury and Reserve Bank, coincided with the Fourth Labour Government's economic reforms. Looking back, and keeping in mind that the reforms covered a dozen major areas, what do you think were amongst the major achievements from the reform period and, perhaps, the major wrong calls?

A: To me, there were at least three big advances from the reform period. First, New Zealand got 'real' recognising that the world did not owe it a living. Secondly we got efficiency gains from sensible private investment decisions as opposed to the public sector 'Think Big' programme. Thirdly, there was a consumer revolution through a big increase in consumer surplus resulting from deregulation, competition and choice. These advances contributed to improving the wellbeing of New Zealanders. Against these outcomes, I would, (from hindsight) criticise the speed, sequencing and some of the scarring. From these experiences, I conclude that it is not always the best thing to lead the world. If you can be a good economic follower, as Australia sometimes has been, you may be in a better position. Our recent bank regulation is an example of this approach. Reform ought to be an on-going process, incremental where possible.

Q: Are there any other thoughts that you would like to share?

A: I had a big failure as Chair of the CRI called the Institute of Social Research and Development which we shut down after a few years. If I was back in Treasury again, I would probably do things a bit differently there. Overall, I have had a whole range of economic experiences: I have loved them, been horrified by them, and learned from them. I still have a lot of learning ahead. In many countries you are either a central banker or a treasury official or an academic. In New Zealand we are lucky (and sensible) allowing people to move around.

My biggest worry in life is that I might get bored. It hasn't happened yet!

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FROM THE 2B RED FILE

by Grant M. Scobie
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Earlier in the year we had a budget. Lurking under all the hype and hoopla and endless media comments about such monumental fiscal issues as to whether we should be taxing a 12 year old's earnings from her paper delivery route, is a more substantial issue: namely what should the government actually be doing? If we are serious about bringing our fiscal house in order then it is pertinent to ask if there are areas of expenditure that might be hived off; and likewise, are there seams of untapped revenue waiting to be mined?

A new book grapples with these issues: *Vito Tanzi (2011) Government versus Markets: The Changing Economic Role of the State (Cambridge: Cambridge University Press)*. The author's credentials to address such a topic are impeccable; Tanzi is a former academic, a former undersecretary for finance in the Italian government, and for 20 years served as director of the Fiscal Affairs Department of the IMF.

When one recalls that in the late 19th century, government expenditures in today's core of OECD countries were around 10% of GDP and today are over 40% on average, then Tanzi's contribution becomes highly relevant. He traces the economic and political history of the role played by the state, and has a valuable review of theories of the government behaviour. The final section addresses the outcomes of state intervention: in short what are the benefits of this higher spending? In broad terms one is hard pressed to draw a firm conclusion: there is only the weakest relation if any between the Human Development Index and the share of GDP spent by governments. Based on data for 2000, we find the depressing fact (Table 11.8) that New Zealand's public sector performance index ranked 17th out of 23 countries (suggesting the programme for a Better Public Service might be overdue).

If you enjoyed the Club of Rome report in the 1970s *(Limits to Growth*) you will love this rerun of the same doom and gloom: *Chandran Nair (2011) Consumptionomics* (*Infinite Ideas*). The charismatic author has his own website (http://www.consumptionomics.com/) a heady mixture of self-aggrandisement and environmental evangelism. The short version, if you haven't time to wade through the mish-mash of jumbled economics, goes roughly like this: the West has built its wealth on a capitalist system that is driven by consumption and in so doing has raped the environment. The Asians (meaning China and India in large part) are hell bent on catching and replicating the West's standard of living – but they can't succeed as planet earth does not have the resources to sustain this.

It is never clear if the real worry is capitalism or simply the under-pricing of environmental services. But who can deny there are environmental issues – as Kiwis we periodically need jolting out of our self-righteous clean green, holier than thou approach. Someone needs to calculate by how much we are subsidising foreign consumers of dairy products by under-pricing the use of trout streams as sewers for dairy effluent. So arguably the author does the world a favour by reminding us the environment is not a free good – but with so many dodgy, sweeping claims he might just be over egging the pudding and losing credibility. I leave it to you, the reader, to judge.

If I had to name my current favourite economist, historian, commentator and entertainer all rolled in one I would have little hesitation in nominating Niall Ferguson. Should you not have read anything by him or seen his BBC documentary series, I am sorry, but your life is significantly the poorer. The latest contribution of this amazingly talented, erudite and articulate economist are the 2012 Reith lectures. You can download these on to your iPod (http://www.bbc.co.uk/podcasts/series/reith); and then when you take a long car trip you will have something worthwhile to listen to rather than the chattering classes on talk-back radio. And be sure to check out this book (a friend lent it to while I was recuperating from a winter bug - it is 422 pages of small print so lots of reading): *Niall Ferguson (2003) Empire: How Britain made the modern world (Penguin)*. (I did note a certain irony in Ferguson, a Scot, giving Britain so much credit – readers will recall Arthur Herman's *How the Scots Invented the Modern World: The True Story of How Western Europe's Poorest Nation Created Our World & Everything in It).*

Larry Kotlikoff, who recently graced our remote shores, has an impressive CV as a serious scholar. But if your only sample of his work was his latest book you might be hard pressed to reach that conclusion. It is unclear to your correspondent as to whether *Laurence J. Kotlikoff and Scott Burns (2012) The Clash of Generations: Saving ourselves, our kids and the economy (Cambridge, MA: MIT Press)* is aimed at the politicians, the non-economist lay reader or the airport book stand browsing crowd. Perhaps such hybrids are an inevitable result of co-authorship by a learned professor and a financial journalist. In any event I put sweeping statements such that the USA is bankrupt, and drawing an analogy between the intergenerational effects of economic policy and physical child abuse in the CON column. In the PRO column we could put drawing attention to the present value of future government liabilities, and an interesting chapter promoting a radical reform of the tax system: to wit, eliminating personal and corporate taxes and replacing them with consumption taxes (which, they argue can be progressive with a few tweaks). They refer to this as a "purple tax plan" – something that will appeal to both the Republicans (red) and the Democrats (blue). Given the results of the recent election in the USA, President Obama might well need a purple plan of some sort to avoid the upcoming fiscal cliff. Whether he'd get any guidance by having an aide leave a copy of this book on his seat on Air Force ONE for his next long haul flight is somewhat uncertain.

“FRAMES”

by Stuart Birks, k.s.birks@massey.ac.nz

Efficiency in economics research

A common approach to economics research involves choice and application of a model. This is not the only possible approach. For an alternative, economics concepts can be used in a more general way. This can give analogous representations which may provide insights that are relevant for the real world. To illustrate, consider applying the concept of a production function to the issue of economics research. This is an example of **framing** an issue, giving a particular perspective which, hopefully, will give some useful insights. It is novel because, while economists frequently research behaviour by others, it is less common for economists to look at their own efficiency.

When economists undertake research, they are providing inputs to produce outputs. It would be natural to frame this in terms of a production function. There are some simple and very general points that can be made even with an elementary representation. The efficiency of production will depend on i) what is being produced, and ii) the choice of production level and method.

Output in a period of time is assumed to be a function of quantities of inputs applied over that period. The functional relationship reflects the quality of inputs and the technology that is being used. This gives some basic findings. If the price of an input falls, we are likely to use more of it. If new inputs or production technologies come available, we then face a wider range of possible production methods and products. We are then likely to change the way we produce and perhaps the products that are produced. If there is a change in the relative price of inputs, and if suitable technologies are available, it will be more efficient to change the ratio of inputs by substituting the input that has become relatively cheaper for the relatively dearer one.

When considering research, we could expect responses to changes in input availability and price and in research technologies. So what changes are we seeing? First, consider the nature of data. Mainstream economics emphasises quantitative research, and so data are commonly thought of as numerical. However, data are not just numbers or series of numbers. A broader definition would consider all potentially relevant information as data. There are qualitative as well as quantitative data. There are interviews, academic documents, policy documents, policy debates, news media reports, images, objects and so on. Through the internet, a vast quantity of information from all over the world is now readily available. Access, storage and processing costs, both in time and in money, have improved dramatically.

It might be suggested that the change is not providing the “right” information for use, but this cannot simply be assumed. An approach in which research is seen as the application of a technique implicitly constrains the types of suitable information irrespective of availability and cost. A production function analogy highlights a problem with this attitude. If economists were to consider this situation for the production of some other good in a competitive environment, they might contend that alternatives, perhaps close substitutes, could arise. Producers of these would then drive inflexible, and hence less competitive, producers out of business.

There have also been changes with numerical data, including falling costs of processing information. However, the change for qualitative data in recent years is likely to be more significant simply because of the magnitude of the change from a low base. Much of the policy information would not have been readily available to academic researchers in the past, especially information from other countries. The availability of textual data in electronic form means that large volumes of data can be rapidly accessed and word-searched. Search engines can perform global searches for words and phrases in fractions of a second. Similar documents or sections of documents can be compared almost at the click of a button, and textual data manipulation and storage can be done in ways not even imagined 30 years ago.

Economics research is commonly seen as the estimation of a model, conducting an experiment, perhaps undertaking a survey. This is essentially the application of a technique. Data requirements are set by requirements of the technique. By default, all other available information is being ignored. From an efficiency of research perspective, it could be asked why no consideration is given to the use of other available, relevant data. How can the researcher justify their exclusion? A question such as this suggests issues in the institutional structures and incentives faced by economics researchers. Consideration of these factors could lead us to a different perception of the process of research.

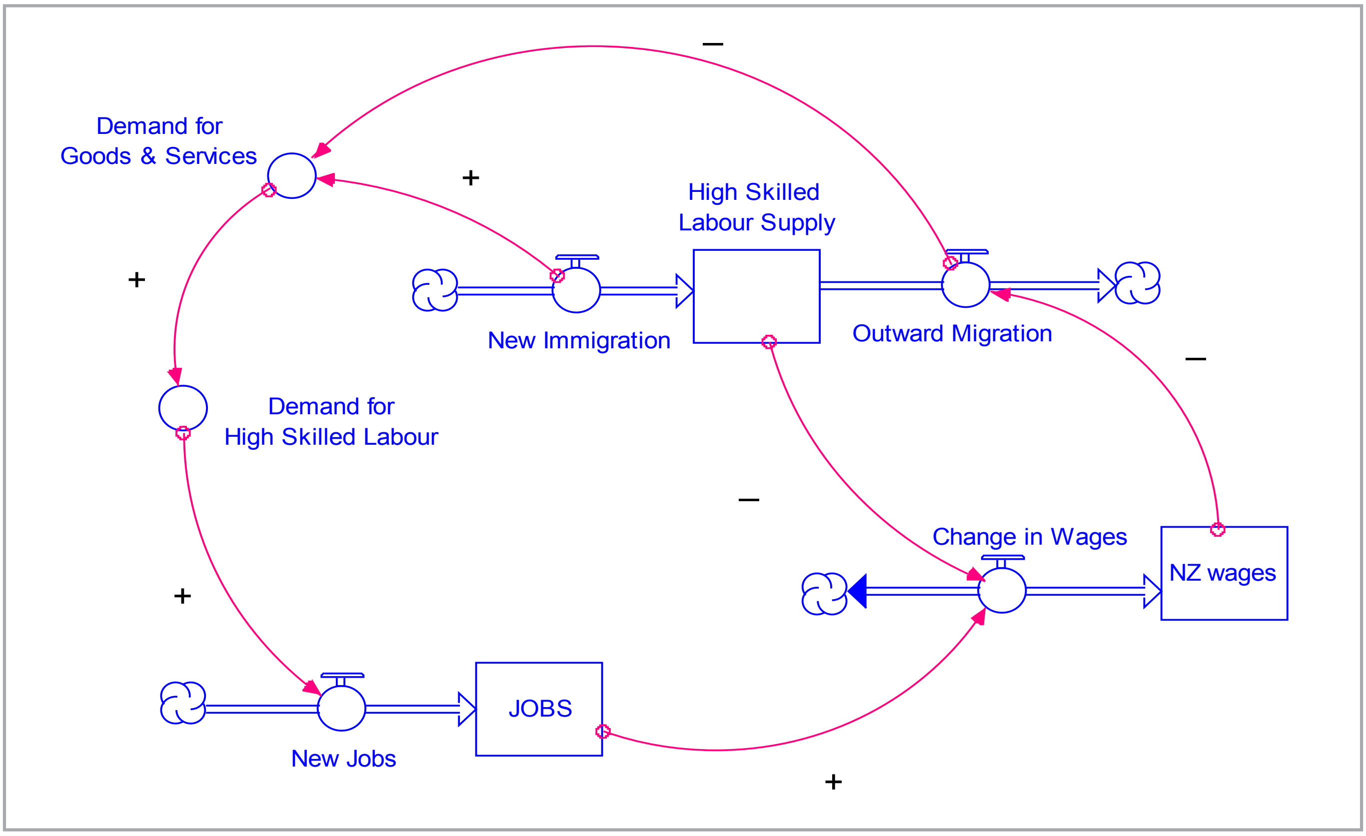
This example illustrates the application of the concept of a production function in a general, informal way. As a tool giving a conceptual structure or representation, it provides important insights into an issue. However, as with any research tool, we should be also aware of its requirements and limitations. For example, points such as the following may be relevant:

- Heterogeneity of inputs;
- Different approaches needed according to the type of data;
- The end result of research from diverse forms of data is more evocative of a composite good;
- There is uncertainty about the nature and quality of the output, and this can persist even after the production is complete;
- There are unlikely to be many of the same product produced;
- The end result may depend on the individual researcher’s skills and training.

Analogies are not precise and complete representations. However, they can give useful insights. The same is true of formal models. When applied as above to research in economics, it raises questions about our conduct of research. Formal approaches may appear rigorous, but they are constrained and their limitations may be overlooked in the rhetoric of economics research. What we see depends on our framing, and all frames are simplified representations, or analogies.

FINE LINES: A FAVOURITE DIAGRAM

by Sholeh Maani



DYNAMIC FLOW MODEL OF IMMIGRATION AND WAGES

This is a dynamic flow model of immigration and wages. Considering the broader effects of immigration is of interest, since a simple analysis of immigration effects, only through increased supply of labour, predicts that the wage rate of domestic workers would decrease. But it is known that immigration has other significant economic effects, such as increasing the demand for goods and services, with an increasing impact on wages. In addition, the labour market itself could create dynamic feedback through outmigration. These inter-relationships can explain why the international evidence on the effect of immigration on domestic wages is mixed and contrasting. International results have a wide range, from showing no effect to small negative effects. (e.g. Borjas, 2003; Card, 2005; Dustmann and Gritz, 2005).

I developed this diagram (Maani, 2009) for a public policy seminar to show the complexities of the relationship between immigration and wages. It shows the effects of skilled-migration in keeping with the New Zealand immigration policy, which focuses on skilled immigration.

The model shows the flow of immigrants in the centre of the diagram, and the well-recognised downward impact on domestic wages through increased supply. The extent to which increased supply of immigrants can impact domestic wages depends on the occupational attainment of immigrants, and the extent to which immigrants are substitutes for domestic labour.

The left-hand side of the diagram shows the added effect of immigration, with an upward effect on domestic wages through increased demand for goods and services and new job creation. This effect can explain why wage decreases may not result after an influx of immigrants.

In addition, a feedback loop is shown on the right-hand side, which shows that if downward pressure on wages is created, outward migration of immigrant or domestic workforce would have an increasing feedback effect on wages. The out-migration part of the diagram is pertinent to New Zealand due to its geographic and institutional proximity to Australia.

Therefore, whether or not immigration results in higher or lower domestic wages depends on the relative magnitude of these broader impacts. A recent estimation of the wage effect for New Zealand (Maani and Chen, 2012) verifies that the overall wage effect from skilled immigration on domestic workforce of similar skill is insignificant.

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BLOGWATCH

by Paul Walker (paul.walker@canterbury.ac.nz)

On the international blogging scene a number of top economists have been blogging about a new working paper on U.S. economic growth by Robert Gordon . Gordon provocatively asks, "Is U.S. Economic Growth Over? Faltering Innovation Confronts the Six Headwinds" <http://www.nber.org/papers/w18315>. Gordon's basic thesis is that long-run economic growth is slowing down. The big ideas of the first two industrial revolutions, roughly the harnessing of energy, urbanisation, clean water, have been used as far as they can. He argues that the recent "computer revolution" is running out of steam, it is unable to raise productivity much more. But Gordon goes further by suggesting that not only do we seem to have run out of productivity-increasing ideas, but in addition "six headwinds" stand in the way of more growth. These headwinds are: 1) Demographics: aging and reduced labour-force participation 2) Plateau in US educational attainment 3) "The most important quantitatively in holding down the growth of our future income is rising inequality." 4) Globalization and outsourcing 5) Energy and environment 6) Household and government debt.

This paper has elicited comments from bloggers such as Gary Becker http://www.becker-posner-blog.com/2012/10/will-long-term-growth-slow-down-becker.html, Richard Posner http://www.becker-posner-blog.com/2012/10/will-us-economic-growth-slow-posner.html, John Cochrane http://johnhcochrane.blogspot.co.nz/2012/08/gordon-on-growth.html, David Henderson http://econlog.econlib.org/archives/2012/09/robert_gordon_o.html, http://econlog.econlib.org/archives/2012/09/gordon_on_growt.html, http://econlog.econlib.org/archives/2012/09/gordon_on_growt_1.html, Ronald Bailey http://reason.com/archives/2012/10/16/is-us-economic-growth-over, Roger Pielke Jr. http://thebreakthrough.org/index.php/voices/roger-pielke-jr/is-economic-growth-coming-to-an-end/, Livio Di Matteo http://worthwhile.typepad.com/worthwhile_canadian_initi/2012/10/is-the-stationary-state-coming.html and Tim Harford http://timharford.com/2012/09/dont-take-growth-for-granted/.

On the local front an important development has been the creation of "The Dismal Science" blog <http://sciblogs.co.nz/thedismalscience/. This blog, which is part of the "Sciblogs" website http://sciblogs.co.nz/, brings together posts from some of the country's top economics blogs, including "Fair Play and Forward Passes" http://fairplayandforwardpasses.blogspot.co.nz/ (written by Sam Richardson), "Groping Towards Bethlehem" http://gropingtobethlehem.wordpress.com/ (Bill Kaye-Blake), "Offsetting Behaviour" http://offsettingbehaviour.blogspot.co.nz/ (Eric Crampton and Seamus Hogan) and "The Visible Hand in Economics" http://www.tvhe.co.nz/ (Matt Nolan, James Zucollo and co-bloggers).

On the local blogs, housing affordability has been a topic of debate. In particular Gareth Morgan's attack on the Productivity Commission's view that land supply is the major determinant of the high cost of housing has been criticised for over emphasising demand. Morgan argues that supply is not the issue, its demand due to the tax status of housing – no capital tax - and actions of the Reserve Bank - directing banks to emphasise mortgage lending - that are the problem. This argument has been countered by Seamus Hogan at "Offsetting Behaviour". Hogan writes that "[u]ltimately, it just comes down to ECON 100 supply and demand. The New Zealand population has been rising, and land-use policies have been preventing supply from keeping up with demand. Maybe those policies are a good thing, and we should be moving away from urban sprawl to high-density living. But it is hard to counter that the cost of such policies will be a steady increase in the price per square metre of housing" http://offsettingbehaviour.blogspot.co.nz/2012/10/gareth-morgan-on-housing-affordability.html. Matt Nolan at the "TVHE" blog writes that "[...] it is incredibly strange to treat the supply and demand factors as mutually exclusive – both can exist. In fact to justify house prices being "too high" while the volume of the housing stock is "too low" REQUIRES a large supply impediment. If what Gareth said was the whole story we would be experiencing overbuilding!" http://www.tvhe.co.nz/2012/11/06/supply-or-demand-why-not-both/. See also a follow-up posting by Hogan at http://offsettingbehaviour.blogspot.co.nz/2012/11/more-on-housing-affordability-supply.html.

At the "Chthonic Wildlife Ramblings" blog http://my.opera.com/chthoniid/blog/ Brendan Moyle offers advice, somewhat sarcastically, on 'How to write a news report on Wildlife Poaching' http://my.opera.com/chthoniid/blog/2012/11/06/how-to-write-a-news-report-on-wildlife-poaching. His "advice": 1) Always support the trade-ban. Trade bans are always right. 2) Tantalise and shock the reader. Everyone needs to be told that wildlife is poached for traditional Chinese medicine. 3) Call for more law enforcement. Obviously nobody has since ever thought of this before. 4) Call for more education. Because nothing kills off demand faster than the constant reminder to people that the wildlife products have medicinal properties in their culture. 5) Make proposals to reduce value of the wildlife. But we've been waiting for this to work for two decades, of course. 6) Mock anyone who expresses doubt.

As the recent scandal involving Lance Armstrong has made clear the behaviour of sportsmen can be harmful to a sponsor's brand and it has been reported that because of this fact a local insurer is to offer corporate sponsors insurance to protect against such brand damaging behaviour. At "Fair Play and Forward Passes" Sam Richardson notes that if insurance is introduced you will change the relationship between sportsmen and sponsors, and not necessarily for the better. Insurance introduces adverse section and moral hazard problems. "The moral hazard issues in this arrangement strike me as being problematic - if you are a sports team and your sponsor takes out insurance against your potential future behaviour being less than desirable, how does that alter your incentives when compared to a deal without insurance? Without insurance, it is in the best interests of the sports team to behave in a way that does not harm the sponsorship arrangement for fear that they may end up losing it. With insurance, the incentives change - teams no longer have the same incentive to preserve their end of the deal, thus the likelihood of misbehaviour increases. And what for the sponsors? Do they enter into deals with safe, trustworthy, dependable and successful teams or athletes, or do their incentives change as well? Instead of lower risk sponsorships, there is likely to be a move towards more risky deals" http://fairplayandforwardpasses.blogspot.co.nz/2012/11/sportspeople-behaving-badly.html.

At "Groping Towards Bethlehem" Bill Kaye-Blake argues that sometimes prices aren't as important as economists often think they are. When it comes to food, research suggests that income and prices are less important for our choices than a lot of other factors. "Some new research suggests that, yes, it's about more than prices. New research has found that healthy eaters spend about the same amount on food as unhealthy eaters (leaving aside for the moment what those categories really mean): [...] This may sound strange coming from an economist, but prices don't play as big a role as you might think. Preferences are much more important" http://gropingtobethlehem.wordpress.com/2012/10/19/a-little-sanity-in-the-great-junk-food-panic/.

Motu Economic and Public Policy Research

NATIONAL WELLBEING AND SUSTAINABILITY MEASURES

Arthur Grimes

Motu researchers and associates have recently been awarded a three-year Marsden Fund grant by the Royal Society of New Zealand. The grant is titled "Testing the validity and robustness of national wellbeing and sustainability measures". Arthur Grimes (Motu and University of Auckland) and Les Oxley (University of Waikato) are the principal investigators, with Jamie Ataria (Lincoln University) and Robert MacCulloch (University of Auckland) as associate investigators.

The study will address a fundamental question: *Are a country's policies and actions sustainably increasing its wellbeing?* Over recent decades, social scientists and ecologists have developed many indicators of national wellbeing and sustainability. What is lacking, however, is an overarching study that tests the adequacy and robustness of these aggregate measures for answering the fundamental question posed here.

Background

Although material prosperity in New Zealand and other nations has increased over the past fifty years, many people still suffer from uncertainties and anxieties, social and economic divisions have widened in many countries, and concern has grown about environmental degradation. Life satisfaction has not changed much in many developed countries despite decades of rising GDP per capita. These observations underpin our research, which is designed to understand and measure whether policies and other actions contribute positively to "sustainable development".

To evaluate outcomes and make cross-country comparisons – and despite well-known difficulties of aggregation over individuals – aggregate indicators inevitably play a role in guiding policy-makers and researchers, since we cannot observe every individual's personal wellbeing. There exists a range of national wellbeing measures from material measures, from Gross National Income per capita; to surveyed happiness and life satisfaction; to composite measures such as the Human Development Index (HDI); to economic sustainability measures such as Genuine Savings; or to ecological sustainability measures such as Ecological Footprint. Each has some theoretical underpinning, but there is no comprehensive study that tests the adequacy of these aggregate measures for answering the question: *Are current behaviours sustainably increasing wellbeing?*

Furthermore, guidance offered by these measures on national performance can differ widely. New Zealand ranks 3rd globally on the HDI, 6th by Gallup for happiness, 33rd for GDP per capita, and almost last amongst developed countries for Ecological Footprint.

In their seminal study, Stiglitz, Sen and Fitoussi (SSF[1]) say that work is required to improve three sets of aggregate measures: **(i)** "better measures of economic performance"; **(ii)** "[a] shift [in] emphasis from measuring economic production to measuring people's well-being"; and **(iii)** "a pragmatic approach towards measuring sustainability". SSF also argue: **(iv)** that there should be greater focus on inequality measures. Furthermore, national measures may be insufficient where groups' world-views differ. For New Zealand, this means that we must consider aggregate wellbeing measures that are valid for Pākehā and for Māori. Sir Mason Durie, for instance, highlights several aspects that contribute to Māori wellbeing but that may not apply to Pākehā; and attitudes to resource development may differ between tangata whenua and settler groups.[2]

To understand whether increases in wellbeing are sustainable, one must have theories and measures of wellbeing and sustainability that can withstand rigorous empirical testing. Our strategy for testing the former set of measures is to use observed physical outcomes such as health outcomes and anthropometric measures of stature as objective and observable indicators of aggregate wellbeing, and to interpret life choices reflected by inter-regional migration as revealed preference indicators of wellbeing as people shift to improve life outcomes in accordance with spatial equilibrium theories.

Sustainability

The most detailed economic indicator of sustainability is Genuine Savings, derived by World Bank researchers from a formal model of how wellbeing can be sustained over time. It focuses on changes in an economy's capabilities (stocks) which constitute the degree to which current generations pass on opportunities to future generations to maintain and enhance their wellbeing (consistent with the Bruntland definition of sustainable development). The theory assumes some substitutability between capital assets – produced, natural, human and social. Together with a PhD student, we will construct a long term Genuine Savings series for New Zealand from the mid-1800s to the present day as an integral part of the research programme.

Testing wellbeing measures

While values of aggregate wellbeing measures are of interest, we need to know how they predict objective (health, anthropometric, migration) outcomes that reflect actual wellbeing of groups within and across countries. There is currently limited work in this regard internationally.

A recent Motu Working Paper[3] made a preliminary contribution to testing the information content of a number of wellbeing indicators. It tested whether aggregate indicators such as life satisfaction indices, inequality measures or the HDI add extra information over and above GNI (or GDP) per capita in explaining net national migration. The tests cover the initial 24 OECD countries over the 50 years to 2010.

For every specification, the paper found that GNI or GDP per capita was significant in explaining net national migration outcomes. However there was also consistent evidence that a national measure of life satisfaction acted positively on net migration over and above the income variable. There was also some weak evidence that greater levels of inequality contribute to net migration outflows. Future work within the research programme will probe the robustness of these results through the examination of more detailed bilateral migration relationships, as well as tests of the information content of aggregate indicators on other objective wellbeing outcomes.

NZAE members and others who are interested in being kept abreast of the results of the research can contact Arthur Grimes at Motu (arthur.grimes@motu.org.nz) to be placed on a research update notification list.

1 Stiglitz J., Sen A. & Fitoussi J-P. 2009. *Report by the Commission on the Measurement of Economic Performance and Social Progress*, Paris.
2 Durie M. 2006. *Measuring Māori Wellbeing*. Wellington: New Zealand Treasury.
3 Grimes A., Oxley L. & Tarrant N. 2012. Does Money Buy Me Love? Testing Alternative Measures of National Wellbeing. Motu Working Paper 12-09.

NZIER ECONOMICS AWARD
CITATION FOR THE NZIER ECONOMICS AWARD 2012

The NZIER Economic Award's Operating Guidelines enjoin the Awarding Panel to "look for outstanding contributions to the advancement of economics and its applications in New Zealand". To qualify for the Award, a contribution "must advance economic matters of direct relevance to New Zealand", and must be "likely to be of long term lasting importance to New Zealand".

The recipient of the 2012 Award has made outstanding contributions in three distinct settings: in contributions to the international literature on fiscal policy (particularly in relation to taxation and public spending) and economic growth, in tax policy-making in New Zealand, and in setting up the Government Economics Network.

Before coming to New Zealand, the recipient of this year's Award established a strong international research reputation in the fields of development economics, growth, and public finance. His empirical work on the impact of human capital and taxes on economic growth, in particular, has helped to make him one of the most widely internationally cited economists in New Zealand, with papers published in such prestigious journals as the American Economic Review, the Economic Journal and the Journal of Public Economics.

In 2007 he joined the New Zealand Treasury as Principal Advisor, Tax Strategy, with a remit to develop the Treasury's medium-term tax policy advice. During his time at Treasury, and as a supporting official to the Tax Working Group, he used his strong analytical, empirical, and public policy skills to open up discussion on hard policy issues, based on applying multi-dimensional frameworks to policy analysis, producing new evidence on the behavioural and distributional effects of different policy options, and rigorously assessing the trade-offs between policy options. He combines a remarkable mix of academic rigour and effective real-world policy-making. He had the vision to first propose the February 2009 Victoria University conference on tax reform, which started the process that led to the creation of the Tax Working Group, which in turn was instrumental in provoking and informing a much-needed public debate on sustainable tax reform. This culminated in the Government's 2010 tax reform, described by the Minister of Finance as the biggest tax reform in 25 years.

His success in economic policy advice was recognised with his appointment in 2010 as Treasury's inaugural Chief Economist. During his time in that role, he set up the Government Economics Network. This was a new initiative for economists in the New Zealand public service, designed to help build the kind of economic capability necessary to support high quality economic policy advice across the public service. Now in his new role as the Chair in Public Finance at the Victoria University of Wellington, with support from three Government departments and PricewaterhouseCoopers, he is again pursuing his joint interests in economic research and policy advice, this time from within the academic research community.

The 2012 NZIER Economics Award is therefore given to Norman Gemmell.

ACCEPTANCE SPEECH BY NORMAN GEMMELL ON RECEIVING THE 2012 NZIER ECONOMICS AWARD

To say that I am delighted and honoured to receive this award from the NZIER would be an understatement. Indeed when Michael Walls called me a short while ago to say that the Panel would like me to accept this award, 'understated' might best describe my reaction. I was so taken aback I was (almost) speechless. Not only because I consider my contributions to economics in New Zealand barely stand comparison with those of the previous recipients that I know – people like Bob Buckle, Arthur Grimes, Grant Scobie. But also perhaps because they, and others such as Gary Hawke, are such iconic New Zealand economists, I had assumed that only those with a long history contributing to New Zealand economics would be eligible. So I feel a real sense of privilege to be bracketed with such respected individuals.

When you receive an award like this it makes you reflect on your career – at least when you're my age! And I was reminded of that biblical parable from the New Testament known as the 'story of the prodigal son' (Luke's Gospel, ch. 15). It goes something like this.

Two sons are working on their, fairly wealthy, father's farm doing the normal things farming families do; and doing pretty well at it. But the younger son gets a bit bored with this life. So he asks his father for his half-share of the family farm inheritance. Father agrees. So, the NT tells us, he sets of for 'the far country' where he has a great time spending the inheritance riotously. You could say he went on his OE to "engaging in excess consumption" of Ferraris, Central Otago Pinot and Kim Kardashian (you're getting a modern Kiwi re-interpretation here!). But when the money runs out, Kim *et al* are not so keen on him anymore. So, dejectedly, he decides to go back to ask his father if he'll take him back – which of course he does unreservedly.

Now, you are probably wondering how this applies to me. Is New Zealand my 'far country' of excess consumption? And who's my Kim Kardashian!?

Actually, for me the 'home country' is economic research – the place where I first discovered the pleasures of applying economic ideas and principles to data. You could probably say that 'testing economic hypotheses' has been the bread-and-butter of my economics research. First stimulated by work with John Creedy (now at VUW) when he was a very young professor of economics at Durham University and I was a post-grad. John taught me so much about how to do empirical research and how to publish it. And he also first stimulated my interest in public economics issues in New Zealand when he arranged for me to visit the New Zealand Treasury in 2002 where we worked on a paper on the

fiscal drag properties of NZ income taxes and GST – published in 2004. Actually this, and a companion

2002 paper, were the first to model the fiscal drag of consumption taxes analytically and led to a number of studies for other countries by ourselves and others.

But perhaps my academic research that has had most influence in New Zealand (certainly it is the most cited) was not specific to New Zealand, but rather relates to the linkages between fiscal policy and economic growth in OECD countries. In the mid-2000s, Treasury asked me to extend that OECD analysis, which excluded New Zealand, by adding New Zealand to the sample. They were trying to persuade Dr Cullen that cuts in corporate and personal taxes would be good for growth (and, incidentally, dissuade him from using recent revenue windfalls to establish Kiwisaver subsidies!).

In doing research I have always believed strongly in two principles. First, if research does not influence others (researchers or policy-makers) then it is an indulgent luxury at taxpayers' expense. Hence publishing and disseminating what we do is an absolute minimum requirement. Second, research on economic policy issues has to be firmly rooted in the second-best world of what is feasible in various political economy contexts. Knowing how to design optimal tax policy should a benevolent dictator seek such advice is not without its merits, but ultimately it is insufficient (and sometimes misleading) when trying to design tax reform that is implementable in a modern democracy.

Which brings me to the 'far country', because for me this was the world of tax policy advice in practice. In 2002, after 20+ years in academic research I was keen to try something different but which still used my basic analytical skills. That led to almost 4 years working on tax policy issues at the UK Treasury and Inland Revenue. That was both new and exciting (not exactly 'riotous living' perhaps, and certainly no Kim Kardashians!), but it gave me some fascinating insights into how politicians and advisers might use, and abuse, 'evidence-based research'. That experience then led to me being offered the chance to come to New Zealand in 2007 and lead Treasury's thinking on medium-term tax reform – in which, at the time, Dr Cullen had expressed some pre-election interest.

For me this was a huge privilege and opportunity to explore 'fresh pastures'. I joined a Treasury tax team that, under Bill Moran's superb leadership, encouraged the idea of evidence-based policy advice; advice that had to be robustly tested by putting it up against alternatives and by subjecting it to the scrutiny of outside experts. This was the process that led to the Tax Working Group in 2009, jointly undertaken by VUW, Inland Revenue's Policy Advice Division and Treasury, and from which the 2010

Budget package emerged. Here I want to pay tribute to Matt Benge and Robin Oliver at IRD whose intimate knowledge of both the theory and practice of good tax policy in New Zealand served as a perpetual standard against which new thinking was tested.

Also, Bob Buckle's public leadership of the TWG process was there for all to see. But what outsiders (and indeed often TWG members) didn't see was his tireless working to bring out the best tax advice from a set of sometimes conflicting analyses or perspectives. I doubt that anyone could have better handled than Bob did as Chairman, the need to incorporate the best economic analysis and evidence with the delivery of an implementable, and politically feasible, tax reform package.

Of course, economists analysing optimal policy are often quick to denigrate the politicians who implement it – or more often don't. Not without good reason perhaps when so many politicians main motivation is keeping themselves in office, which can be at odds with doing what 'good economics' dictates. But in the TWG process and the subsequent build-up to Budget 2010, Ministers English and Dunne were, in my view, models of how an economic advisor would want a Minister to behave. Persistently they gave us *carte blanche* to explore all options; they encouraged, not merely tolerated, careful evidence-based research; and they were willing to take forward to Cabinet reform ideas of which they had been persuaded but that they knew would take some persuasion for their colleagues to agree to. The final 2010 tax reform package contained elements that many sensible economists could legitimately disagree with, demonstrating the political compromises that are usually necessary to deliver any reform. However, without both Ministers' open-minded approach, I doubt that much of what I and others did in advising on the 2010 tax package would have had much traction.

Now, as most of you will be aware, after four years in Treasury, initially as tax adviser and then as Chief Economist, I returned to the 'home country', or my 'first love', of academic research in 2011 to my current role as Chair in Public Finance at Victoria University. This really feels like 'coming home' to applied economic research. There are two really exciting new elements for me. The first is the opportunity to work on New Zealand unit record tax data to try to understand why and how taxpayers respond when tax changes occur. Secondly, one of the challenges of my new Chair is to try to demonstrate that good public finance research can be directly applied to New Zealand and can help with policy in practice. But rather than do it within the public service, I'm now doing it from within the research community.

What attracts me back to public finance research? Mainly it is the ability to show that economic theories, arguments and evidence can truly inform policy debates that, without economists' input, would be misguided or at least less valuable. As an example, if I had time tonight I would show you a chart from the Final Report of the 'Henry Review' – Australia's equivalent or our Tax Working Group, which examined the merits and problems of Australia's tax system recently. That Report has a chart [below] showing the kilometres travelled by car by individuals paying Fringe Benefits Tax (FBT) on that travel.

If I told you that the median distance travelled was about 20,000kms per year, you might expect that the distribution of annual kilometres travelled by FBT payers would be approximately bell-shaped around that median. A few travel large, or small, distances with most bunched somewhere in the middle around 20,000. But the legislated FBT 'tax rate' per km falls, on *all* kms travelled, if you travel more kilometres – in particular it falls once you travel more than 15,000, 25,000 and 40,000 kilometres per year. And guess what? An awful lot of people seem to travel *just over* those distances, and very few *just below*! Taxes change the way people behave, or say they behave, and in ways that non-economists or politicians often seem not to appreciate.

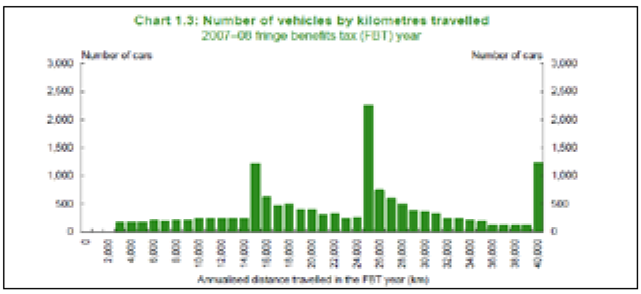
To finish, I leave you with a hypothesis (though hardly an economic one) that someone might like to test one day. My hypothesis is this: "that someone, such as myself, who has made at most a modest contribution to their chosen profession, gains more pleasure when that contribution is recognised by others, than those more famous who have made world-beating contributions"; (a kind of "diminishing marginal utility of recognition" perhaps?) Of course, this hypothesis stems from the worst of all

possible scientific methods – namely generalisation from a non-random sample of one! However, I can certainly say that, to be recognized by the NZIER and the independent Panel, in this award, is an enormous source of pleasure for me. And if, as the award conditions state, my contributions turn out to have "lasting importance for New Zealand", no-one will be more pleased than me.

Since my wife and I came to New Zealand almost exactly 5 years ago, we have felt so welcomed by the country and by so many New Zealanders, several of whom are here tonight. In response, the least I can do as a professional economist is to repay that privilege, by trying to focus my professional contributions on the country that has been so welcoming.

Members of the NZIER Board and the award panel: thank you very, very much. I am truly honoured to receive this award. Rest assured I will refer to it shamelessly in my New Zealand citizenship application to convince them that the country's economic welfare would go into steep decline without me!

Thank you.



Source: *Australia's Future Tax System* ('Henry Review', 2009), Chart 1.3

Government Economics Network GEN Website - www.gen.org.nz

by Joey Au (GEN Committee), (info@gen.org.nz)

In November 2012 we launched our new GEN website – www.gen.org.nz. Special thanks to Michael Chiu and Heena Chhagan for helping me construct this website.

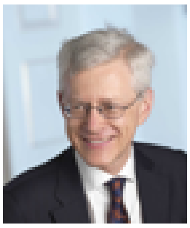
2012 GEN ANNUAL CONFERENCE 14 DECEMBER 2012

Register at www.gen.org.nz for the 2012 GEN annual conference:

WELFARE REFORM, PUBLIC POLICY AND PRODUCTIVITY.

At this year's conference we have two international keynote speakers.

Trevor Huddleston
Department for Work and Pension
Latest Developments in Welfare and Pension Reform in the UK



Martin Weale
Bank of England
Household Behaviour and Policy Analysis

Other informative sessions include discussion of the *Long-Term Effects of Unemployment or Economic Inactivity* by **Tim Maloney** (Auckland University of Technology).

A **Chief Economist Panel** discussion on the *New Zealand Productivity Paradox.*

Norman Gemmell (Victoria University) looks at the history of New Zealand's income tax policy and asks the question *how High (or Low) Should New Zealand's Top Tax Rate be?*

KNOWLEDGE HUBS

Knowledge Hubs was created to provide policy analysts and researchers, the public sector and universities with a vehicle to **share** their policy-relevant research and analysis; **connect** with other researchers and policy analysts; and **discuss** their work and ideas on a particular subject area.

Each Hub is governed by a Board made up of senior staff across different agencies with the broad aims to:

1. **combine** the research efforts of existing agencies working in the same subject area;
2. **collaborate** with other research centres, such as the universities; and
3. **prioritise** and produce policy-relevant research which will lead to better policy advice.

PRODUCTIVITY HUB

New Zealand has experienced a very poor productivity performance compared to other OECD countries.

A new cross-agency initiative, the Productivity Hub, will combine the research efforts of the Ministry of Business, Innovation and Employment, Statistics New Zealand, Treasury, the Reserve Bank, Ministry of Primary Industries, Ministry of Foreign Affairs and Trade, and the relatively new Productivity Commission, on productivity-related topics.

Paul Conway, the Productivity Commission research director, says the community of researchers working on productivity issues in New Zealand is small and spread across a number of organisations. "Working together more closely means we can get greater scale and critical mass."

"We all want to do research for the same purpose – to improve policy and get the economy working better. The timing couldn't be better and we have been overwhelmed by how enthusiastic everyone is about this initiative," Paul says.

As well as bringing public sector researchers together, the Hub aims to collaborate with other research centres, such as the universities. Join us now – www.gen.org.nz

TRAINING

I should like to thank the following individuals for taking part in teaching the GEN Applied Microeconomics for Policy course:

1. John Creedy – The Treasury
2. Bronwyn Croxson – Ministry of Health
3. Joanne Leung & Ian Duncan – Ministry of Transport
4. David Rae – Ministry of Social Development

This course uses a case study approach to show how core microeconomic principles can be applied to public policy questions. Each lecture is built around a core economic principle and associated evidence, using case studies to illustrate how this principle can be applied. Thank you all!!!

SEMINARS

Thanks to Prof Jacques Poot (University of Waikato) we were fortunate to host Prof Klaus Zimmerman and Prof Amelie Constant from IZA. Klaus presented on the Challenges of the Euro Crisis and Amelie presented on Youth Unemployment and Vocational Training. This joint GEN and Motu seminar was very well attended and received.

BOOK REVIEW

Girol Karacaoglu, President of GEN, wrote a review of the book by Daron Acemoglu and James Robinson - Why Nations Fail: The Origins of Power, Prosperity, and Poverty. Read it now – www.gen.org.nz

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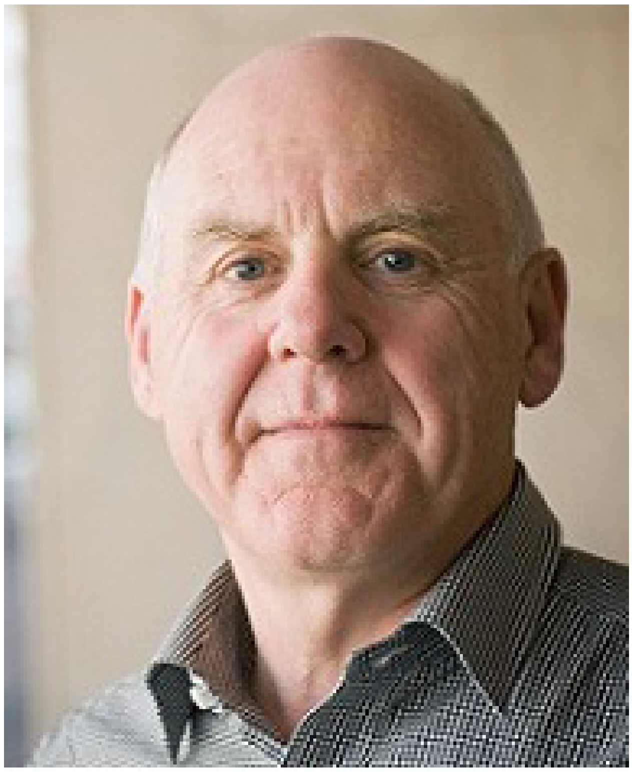
THE FIVE-MINUTE INTERVIEW ... WITH NORMAN GEMMELL



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

   From my earliest days as a 16 year old pupil studying A-level Economics at school in York, England, I knew that this was a new subject I would enjoy. But it was probably only after completing a fairly substantial dissertation between the 2nd and 3rd years of my undergraduate economics degree at Durham University that I knew I wanted to study more. After that, the career kind of 'happened' when, as a graduate student, I was surprisingly asked to take up a temporary economics lectureship that I hadn't applied for!

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

   I began as an economics undergraduate in 1973 – just as the oil shocks were hitting the global economy and macroeconomics was in a bit of turmoil! By the time I was a postgrad in 1976, academic and wider debates over appropriate monetary and fiscal policy responses were in full swing. It was probably this, as much as anything else, that got me interested in tax policy and issues around public sector growth.

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

   Bacon and Eltis's *Britain's Economic Problem* (1976) was not the most intellectually challenging of books but it brought into stark focus the state of the pre-Thatcherite British public sector. Their 'take' was to measure the public 'non-market' sector relative to the 'marketable' sector to get a better assessment of the extent of pressure on public budgets. More generally Max Corden's books and papers, especially on Dutch disease, and William Baumol's papers on the so-called 'Baumol cost disease' stimulated my thinking. I seem to have been attracted to economic 'diseases'!

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

   Though economics was a relatively new subject to the A-level curriculum at my school in 1971, there were already around 30 pupils doing A-level with two specialist economics teachers. Both of them, whose names have long escaped my memory, were wonderful enthusiasts for the subject. At university? Well, as a post-graduate, a certain current editor of AI had a huge formative impact on my development as a PhD student and beyond!

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

   Robert Barro and the Romers (Christina and/or David). Both have interesting things to say about government intervention at the macro level and quite different perspectives. Recently Emmanuel Saez and Raj Chetty's theoretical and empirical work on taxation at the micro level seems hugely important - a Nobel prize coming their way in the next 20 years, surely?

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

   My paper on testing for human capital effects on GDP growth rates published in *the Oxford Bulletin of Economics & Statistics*, in 1996. It was the first to use data on both stocks and flows of human capital to test alternative theories and constructed a new dataset to do so. The results – that the levels of education (primary, secondary, tertiary) that matter for growth differ across countries in intuitively plausible ways – got little attention at the time, but seems to be being re-discovered more recently!

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

   It is difficult to choose but it would be between these three: the oil shocks of the early 1970s - a radically new economic event generating equally radical rethinking of macroeconomics; the Thatcher/Reagan-inspired reforms of the 1980s – marking a turning point in how public finance was perceived, and applied to policy; and the economic rise of China in the last 10-20 years – driving the phenomenon of the so-called 'Great Moderation'.

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

   Enjoying the scenic pleasures of this wonderful country! Having arrived in 2007, there are still lots more places to see. Otherwise, I enjoy films, relaxing with my wife and good friends, Central Otago pinot, and driving fast cars. Unfortunately Kiwi road speed limits and the absence of suitable race tracks near Wellington, curtail much of that. Perhaps it's time to try fast boats?

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

Current Research in Progress by the Department of Economics, University of Waikato

Sayeeda Bano has research interests in international trade and international finance. Topics include economic integration, and closer economic relations (FTAs, CEPs, ASEAN, SAARC, WTO), trade policy issues, intra- and inter-industry trade, trade in services, trade modelling and estimation (various patterns of trade intensities indices, trade potential indices, trade reciprocity indices, static and dynamic revealed comparative advantage, trade complimentarity indices), exchange rate volatility and balance of payments issues (NZ- China FTA, NZ- India FTA, ASEAN-NZ trade, New Zealand Kiwi-Fruit Exports).

Michael Cameron has a wide research agenda that includes topics on the nexus of health, development and population. He is currently leading a HSC-funded project investigating The Impacts of Liquor Outlet Density in New Zealand (with Bill Cochrane and others) and a CIHR-funded project investigating willingness-to-pay for features of hypothetical microbicides to protect against HIV, and is part of MBIE-funded projects on regional demographic change (with Paul Spoonley and others), active ageing (with Peggy Koopman-Boyden and others), and population and land use impacts of climate change (with Andrew Tait and others). He also has ongoing research projects on simulating the interactions between HIV and poverty, simulating scenarios of unpaid care of older people, financial and economic literacy among high school and university-aged students, and small area and stochastic population projections.

Graeme Doole has research interests involving the use of mathematical modelling to improve insight of how best to manage agricultural and natural systems. His current research involves a number of projects. First, he has been investigating cost-effective policy options for improving water quality throughout the Canterbury and Waikato regions by decreasing nitrate leaching from dairy farming systems. Second, he is conducting a review of the use of market-based instruments for biodiversity conservation throughout Australia to inform future policy development. Last, he is involved in an international collaboration between scientists from Australia, New Zealand, and the United States formed to guide the development of cost-effective policy for biodiversity conservation with a focus on the presence of multiple agents.

John Gibson is currently working on three areas of empirical microeconomics: a. impacts of migration to New Zealand on health and wealth of immigrants, and their left behind family in the Pacific, (with David McKenzie at the World Bank, Steve Stillman at Otago and Halahingano Rohorua at Waikato and supported by the Marsden Fund); b. testing Hicksian separability assumptions in food demand equations, using household survey data from Vietnam (with Bonggeun Kim at Seoul National University); and c. assessing the impact of measurement errors in household consumption expenditure surveys (with Kathleen Beegle and Jed Friedman of the World Bank and Joachim de Weerdt of EDI in Tanzania).

Gazi Hassan is an applied macroeconomist. He teaches macroeconomics, applied econometrics and economic modelling to undergraduate students. His research is in the field of empirical growth economics, particularly focusing on the econometric issues arising in estimating growth models to measure the impact of remittances, external capital flows, macroeconomic volatility and real exchange rate overvaluation. His current research project are: a) to investigate the effects sovereign country credit ratings on the real sectors; b) effect of health capital on economic growth; c) behavioural responses of remittances recipient households facing natural disasters; d) remittances inflow and real exchange rate appreciation and e) debt and economic growth.

Mark Holmes is currently focused on three research projects. These are remittances and the current account balances of less developed countries (with Gazi Hassan), adjustment in regional unemployment rates (with Jesus Otero and Theodore Panagioditis) and financial instability and the dynamics of volatility expectations (with Nabil Magrebi and Kosuke Oya). Under his supervision, one PhD student (Lula Mengehsa) is just about to submit her thesis on an investigation of the macroeconomic and monetary effects of dollarisation in Eritrea. Another PhD student (Harold Valera) is about to join Waikato and start his work on inflation dynamics in Asian economies. He is currently Editor-in-Chief of New Zealand Economic Papers.

Steven Lim gained his PhD from the University of Adelaide in 1996, analysing the optimality of China's development strategies and its economic reforms. Since then his research interests have broadened to include economic growth accounting, network effects in e-commerce, the relationship between HIV/AIDS and poverty, the social and community health impacts of trade liberalisation, sustainable community livelihoods, the economics of landmine clearing, economic growth and the environment, the evolution of China's economy, and the role of business in sustainable economic development.

Dave Maré is an Adjunct Professor in the Department of Economics and is a Research Associate with the National Institute of Demographic and Economic Analysis (NIDEA) at Waikato. His current research interests include the economics of immigration, the economic performance of cities, and patterns of labour market adjustment - for individuals and in aggregate. Dave is also a Senior Fellow with Motu Research.

Dan Marsh is Chairperson of the Department. His major research interest focuses around reduction of the environmental impact of agriculture in New Zealand. He has collaborated with Graeme Doole and T. Ramilan in catchment simulation modelling to identify abatement costs and optimal abatement strategies in an upper Waikato dairy catchment. He has conducted several choice experiments to investigate the benefits from policies that would improve water quality in the Waikato hydro lakes. He is also working with a PhD student to use revealed preference data to research the value of water quality in the Rotorua Lakes.

Les Oxley is currently working on several topics. The first, joint with Phillip McCann, University of Groningen, is a Marsden Funded project looking at the drivers of innovation in New Zealand. Using Business Operations Survey data, case studies and theoretical models based upon the New Economic Geography. The second area is another Marsden Funded project, joint with Kris Inwood (Guelph) and Evan Roberts (Minnesota) using data we have collected on the heights and weights of a large sample of New Zealanders from 1869 – to date to construct anthropometric-based alternatives to monetary-based measures of standard of living and wellbeing. The third area, this time funded by the Leverhulme (UK) and joint with David Greasley (Edinburgh), Nick Hanley (Stirling) and Paul Warde (East Anglia) is testing (and forecasting with) various models of sustainable growth e.g., Genuine Savings, using historical data from the UK, 1765-2000 and the US 1869-2000.

Jacques Poot, Professor of Population Economics divides his time between NIDEA, the Department of Economics and VU University Amsterdam, where he is an Adjunct Professor. research interests include all aspects of the economics of population (such as migration, fertility, labour force, and ageing) and especially the geographical dimension of these topics. He currently co-leads two large four-year collaborative research projects, on the economic integration of immigrants in New Zealand, and on migrant diversity and regional disparity in Europe respectively. Professor Poot has been working in recent years particularly on international and internal migration, local labour markets, regional development, housing markets, and forecasting. Furthermore, his work on social and economic impact assessment has led him to apply and further develop methodologies for meta-analysis: the systematic and quantitative synthesis of previous empirical research findings.

Ric Scarpa, Professor of Environmental Economics will be based at the Gibson Institute, Belfast until 2016, while spending the first few months of each year in New Zealand. He has research interests that focus on the development of methods to value non-market goods, especially in the field of environmental goods, such as quality of sites used for outdoor recreation and the rural landscape. He is also generally interested in the econometrics modelling of qualitative choice. His recent effort is directed towards the policy relevance of taste heterogeneity, its geographical variation and the explicit consideration of different attribute processing strategies in qualitative choice modelling. Some of his empirical research is also based on correcting for the disparity between willingness to pay estimates from hypothetical and real choices. Ric is associate editor of the Journal of Choice Modelling and Environmental and Resource Economics.

Brian Silverstone (Research Associate) has joint projects related mainly to the analysis of firm-level responses to the NZIER's Quarterly Survey of Business Opinion (QSBO). These projects include 'Insights into Business Confidence from QSBO' and 'Consensus and Dissension within the QSBO'. Surprisingly, perhaps, the determinants of business confidence have not been studied closely, especially from a firm-level (panel) perspective. Understanding consensus and dissension within a business survey may give additional insights into business uncertainty. Another joint project involves a meta analysis of Okun's law (the empirical relationship between economic growth and unemployment).

Anna Strutt has research interests primarily in area of global computable general equilibrium modelling and policy analysis. She is currently working on a number of projects with Kym Anderson (University of Adelaide and Australian National University), including projections of the global economy to 2030, with a focus on South America, Australasia and Indonesia. They are also working on food security in Asia (with Shikha Jha, Asian Development Bank and Signe Nelgen, University of Adelaide). Anna's other research projects include: Strengthening the resilience of the Zimbabwean economy to higher commodity prices (with Godfrey Mahofa, University of Cape Town, under a World Bank capacity-building project); Modelling trade and sectoral impacts of the global financial crisis (with Terrie Walmsley, Purdue University); Regional trade agreements (with Ganesh Wignaraja, Asian Development Bank Institute); Assessing socioeconomic impacts of infrastructure development and poverty reduction in the Greater Mekong Subregion (with Susan Stone, OECD and Tom Hertel, Purdue University).

John Tressler is continuing his research on the evaluation of research productivity and the economic impact of PBRF. Recent work has included: the evaluation of citation patterns, journal based research evaluation and academic labour markets and the relation between PBRF research assessments and journal based measures of research productivity. This work is being undertaken with David Anderson from Queens University in Canada, John Gibson, Joseph Macri at Macquarie University and Warren Smart at the Ministry of Education.

Steven Tucker is the founder and Director of the Waikato Experimental Economics Laboratory (WEEL), which is being established as a state-of-the-art, experimental economics research facility. He is a senior lecturer in economics and received his Ph.D. from Purdue University in 2002. He joined the University of Waikato in 2012 and worked previously in the Department of Economics and Finance at the University of Canterbury where he was the founder and inaugural director of the New Zealand Experimental Economics Laboratory.

Steven uses experimental economic methods to study research questions in a range of fields in economics such as industrial organization, financial economics, and macroeconomics. Tucker's research deals with topics such as:- factors that mitigate asset market bubble formation; mechanisms to provide public goods through voluntary contributions; mechanisms to provide debt relief to developing countries and ways of allocating foreign aid to address weakest-link international public goods.

NZEP

by Mark Homes

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).

A new contract has been negotiated and signed with Taylor & Francis who will now look after the publication of NZEP until the end of 2017. It is also worth noting that some earlier NZEP special issues will be published by Taylor & Francis as special issue books. The first of these will be *Economic Psychology and Experimental Economics* edited by **Simon Kemp & Gabrielle Wall** which is on track to be published next year.

Mark Holmes (holmesmj@waikato.ac.nz), *Editor-in-Chief.*

ABOUT NZAE

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

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