Journal of Economic Perspectives—Volume 22, Number 2—Spring 2008—Pages 235–242

Recommendations for Further Reading

Timothy Taylor

This section will list readings that may be especially useful to teachers of undergraduate economics, as well as other articles that are of broader cultural interest. In general, the articles chosen will be expository or integrative and not focus on original research. If you write or read an appropriate article, please send the link or the article itself (and possibly a few sentences describing the article) to Timothy Taylor, Managing Editor, *Journal of Economic Perspectives*, at ⟨taylort@macalester.edu⟩, or by fax to 651-696-6825.

Smorgasbord

Alfred E. Kahn ruminates on "The Threat of Latter-Day 'Progressives' to an Authentically Liberal Economic Policy." "[T]he use of the label 'Progressive' in both 1948 and 2007 has in important measure been a cynical attempt to conceal an often unprogressive, illiberal platform. As I will argue, partly on the basis of my own experience as a regulator, deregulator, and advisor on inflation to a liberal President, there is nothing either 'progressive,' 'liberal' or desirable about—successively—populist protectionism, xenophobia, competition-suppressing regulatory cartelization, repression of energy prices, recourse to price controls as a remedy or preventive of inflation or a rush to rein in or hamper the dynamic market processes of technological change." Kahn adds: "Even after making allowance for my generation's (or at least *my*) especial discomfort, if not bewilderment, when confronted with the decisions forced on consumers by rapidly changing telecommunications technology and service offerings, it seems to me that the task of making intelligent

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choices has become excessively complex even for succeeding generations. . . . Confronted as I am with multi-paged monthly telephone company bills—including wireless—in the $160 range and separate cable company bills in the $80 range, with varying combinations of wireless charges for placing and/or *receiving* calls, varying special discounts for varying periods of time and—one of which I was not even aware until recently—forbiddingly high wireless service termination fees—I am reminded forcefully each time of Oscar Wilde's complaint, 'The trouble with Socialism is it takes up too many evenings'. While resigned acceptance has become the rational choice for most of us individually, I have difficulty accepting that it represents the rational situation for consumers *collectively* . . ." Reg-Markets Center, Working Paper 08-03, January 2008. At ⟨http://aei-brookings.org/admin/authorpdfs/redirect-safely.php?fname=../pdffiles/WP08-03_topost.pdf⟩.

David Roodman has written: "Macro Aid Effectiveness Research: A Guide for the Perplexed." From the abstract: "[T]his paper reviews recent, contending studies of how much foreign aid affects country-level outcomes such as economic growth and school attendance rates. This particular kind of study is ambitious: it is far easier to evaluate a school-building project, say, on whether the school was built and children filled its seats than to determine whether all aid, or large subcomponents of it, made the economy grow faster. . . . Aid has eradicated diseases, prevented famines, and done many other good things. But given the limited and noisy data available, its effects on growth in particular probably cannot be detected." Center for Global Development, December 2007, Working Paper 135. At ⟨http://www.cgdev.org/content/publications/detail/15003⟩.

The World Bank's *Global Economic Prospects* report for 2008 focuses on *Technology Diffusion in the Developing World*. From the "Overview:" "The penetration of older technologies, such as fixed-line telephones, electrical power, transportation, and health care services—many of which were originally provided by governments—is only weakly correlated with income. . . . In part, this reflects the nature of the technologies in question, such as electrical networks, road infrastructure, fixed-line telephony, and sanitation networks. Many of these technologies require an infrastructure that is relatively expensive to create and maintain, and which relies on large numbers of individuals with scarce technical skills. . . . The penetration rates of newer technologies have risen relatively rapidly and are more directly correlated with income than is the case for older technologies. The infrastructure for newer technologies such as mobile phones, computers, and the Internet is generally less expensive to create and requires fewer (though more skilled) workers to maintain. . . . On average, the time it takes before official statistics in a developing country record significant exploitation of a new technology has declined from almost 100 years for innovations discovered in the 1800s to about 20 years today." At ⟨http://siteresources.worldbank.org/INTGEP2008/Resources/complete-report.pdf⟩.

The *Michigan Law Review* has published in its November 2007 issue "An Online Symposium on Pay-to-Stay Programs in Correctional Facilities." From the website: "Approximately fifteen California jails have implemented pay-to-stay programs.

These programs allow some offenders to pay a daily fee in order to serve their sentences in a city-run or privately-managed correctional facility rather than in a county jail. In some programs, benefits include assignment to a private cell with a regular door, separation from violent offenders, access to the jail's movie collection, and the ability to carry an iPod or cell phone." The titles of some of the articles give a sense of the issues: "Pay-to-Stay in California Jails and the Value of Systemic Self-Embarassment," by Robert Weisberg; "It Could Happen to 'You': Pay-to-Stay Jail Upgrades," by Kim Shayo Buchanan; and "The Dirty Little Secrets about Pay-to-Stay," by Laurie L. Levenson and Mary Gordon. Those who were interested by Alvin E. Roth's article on "Repugnance as a Constraint on Markets" in the Summer 2007 issue of *JEP* will find food for thought here. At ⟨http://www.michiganlawreview.org/firstimpressions/vol106/paytostay.htm⟩.

Henry J. Aaron asks: "Budget Crisis, Entitlement Crisis, Health Care Financing Problem—Which Is It?" "The United States must reform its health care financing system, public and private. If it does so, there will be no remaining long-term fiscal problem. Reducing current budget deficits is also desirable. But the long-term problem is health care spending, not a general budget shortfall or entitlements." *Health Affairs*, November/December 2007, vol. 26, no. 6, pp. 1622–33.

Karol Boudreaux and Paul Dragos Aligica have written "Paths to Property: Approaches to Institutional Change in International Development." "Economic development requires the creation of sound political and legal institutions—in particular, secure and functional property rights. Among policy-makers there is still widespread ignorance about how to design, create and secure functional property rights systems in the developing world. Detailed institutional analysis may therefore be more productive than engaging in the old 'nationalisation' versus 'privatisation' debate. . . . Drawing mainly on examples from sub-Saharan Africa, this study explores the avenues of property rights creation and change." Institute of International Affairs, 2007, at ⟨http://www.iea.org.uk/files/upld-release134pdf?.pdf⟩.

The Federal Reserve on Subprime Mortgages

"The Rise and Fall of Subprime Mortgages," by Danielle DiMartino and John V. Duca. "Subprime mortgages are extended to applicants deemed the least creditworthy because of low credit scores or uncertain income prospects, both of which reflect the highest default risk and warrant the highest interest rates. Near-prime mortgages, which are smaller than jumbos, are made to borrowers who qualify for credit a notch above subprime but may not be able to fully document their income or provide traditional down payments. . . . Some 80 percent of outstanding U.S. mortgages are prime, while 14 percent are subprime and 6 percent fall into the near-prime category. These numbers, however, mask the explosive growth of nonprime mortgages. Subprime and near-prime loans shot up from 9 percent of newly originated securitized mortgages in 2001 to 40 percent in 2006. The non-prime boom introduced practices that made it easier to obtain loans. Some mortgages required little or no proof of income; others needed little or no down payment. Homebuyers could take out a simultaneous second, or piggyback, mortgage at the time of purchase, make interest-only payments for up to 15 years, skip payments by reducing equity or, in some cases, obtain a mortgage that exceeded the home's value. These new practices opened the housing market to millions of Americans, pushing the homeownership rate from 63.8 percent in 1994 to a record 69.2 percent in 2004. Although low interest rates bolstered homebuying early in the decade, the expansion of nonprime mortgages clearly played a role in the surge of homeownership." *Economic Letter—Insights from the Federal Reserve Bank of Dallas*, November 2007, vol. 2, no. 11. At ⟨http://www.dallasfed.org/research/eclett/2007/el0711.html⟩.

Kelly D. Edmiston and Roger Zalneraitis discuss "Rising Foreclosures in the United States: A Perfect Storm." "In the second quarter of 2007, the share of outstanding mortgages in some stage of foreclosure stood at 1.4 percent, near historic highs and up from less than 1 percent a year earlier. The number of mortgages entering the foreclosure process reached an all-time high in mid-2007, suggesting that the foreclosure surge is likely to get worse before it gets better. The foreclosure surge was created by a perfect storm of events. First, in recent years the share of subprime mortgage originations increased substantially. . . . Second, foreclosure rates for adjustable-rate mortgages (ARMs) have increased considerably . . . Finally, high loan-to-value originations in recent years, coupled with stagnant or falling home prices, have left many people with insufficient equity to sell or refinance their homes." *Economic Review, Federal Reserve Bank of Kansas City*, Fourth Quarter 2007, pp. 115–145. At ⟨http://www.frbkc.org/PUBLICAT/ECONREV/PDF/4q07Edmiston.pdf⟩.

Richard J. Rosen explains, "The role of securitization in mortgage lending." "A number of hedge funds and banks (including many non-U.S. banks) reported losses related to investments in U.S. subprime mortgage loans or subprime-loan-based securities. As a result, news reports began to feature terms such as MBS, CDO, and SIV. This article demystifies these terms by explaining what the abbreviations stand for and how these financial instruments work." *Chicago Fed Letter: The Federal Reserve Bank Of Chicago*, November 2007, No. 244. At ⟨http://www.chicagofed.org/publications/fedletter/cflnovember2007_244.pdf⟩.

A Fair Tax?

Bruce Bartlett explains "Why the FairTax Won't Work." "One solution to the nation's long-term fiscal problems that has gained support in recent years is the idea of replacing all federal taxes with a 23 percent national retail sales tax called the FairTax. . . . Unfortunately, the administrative problems inherent in this proposal make it impossible to take seriously. . . . Basically, the VAT [value-added tax] solves all of the administrative and compliance problems that FairTax supporters are either ignorant of or just assume away. Virtually all reputable economists who have looked at this issue have concluded that if the United States wishes to adopt a national consumption tax, either as a supplementary tax or a replacement for all or part of the existing tax system, the VAT makes far more sense than something like the FairTax. This has also been the conclusion of every foreign country that examined the issue. *Tax Notes,* December 24, 2007, pp. 1241–54.

Laurence J. Kotlikoff responds with "Why the Fair Tax Will Work." "Let me conclude by asserting that the FairTax will work. And let me reiterate that our nation is in grave fiscal danger. Going forward we desperately need an efficient, transparent, and equitable tax system that has the potential to raise, over time, significantly more revenue than would otherwise be the case and that contributes to limiting spending by making crystal clear who pays for what the government spends." January 15, 2008. Available at ⟨http://www.fairtax.org/site/News2?page=NewsArticle&id=9321⟩.

David G. Tuerck responds with "Memo to Bruce Bartlett: Just Do the Math." "Of Bartlett's mistakes, I will focus on six: misstating the calculation of the effective tax rate under the FairTax; concluding that the removal of existing taxes in anticipation of the FairTax would reduce prices; observing that imposition of the FairTax would raise prices by the inclusive rate, rather than the exclusive rate; implying that the FairTax rebate is intended to compensate consumers for rising prices; alleging duplicity in how [a previous study] handles the rebate in calculating the FairTax rate; and erroneously claiming that the FairTax would impose a burden on the federal government and on state and local government." *Tax Notes,* February 4, 2008, pp. 639–46.

About Economists

Douglas Clement offers an "Interview with Eugene Fama." On stock market bubbles: "Well, economists are arrogant people. And because they can't explain something, it becomes irrational. The way I look at it, there were two crashes in the last century. One turned out to be too small. The '29 crash was too small; the market went down subsequently. The '87 crash turned out to be too big; the market went up afterwards. So you have two cases: One was an underreaction; the other was an overreaction. That's exactly what you'd expect if the market's efficient." On hedge funds and market risk: "The problem is that we don't have very good hedge fund data and the data we have only goes back about 10 years. That's just not enough to come to any conclusions on these issues. So I don't know if it's going to take another half century before we really know. You're talking about returns with such high volatility that it really is going to take that long." On his own work patterns: "I work every day, but I never work a full day. I get up at five o'clock in the morning and I work basically all morning until maybe one o'clock, two o'clock, and then I go play golf, I go windsurfing, I play tennis. And that's it." *The Region:* Federal Reserve Bank of Minneapolis, December 2007, pp. 14–23. At ⟨http://www.minneapolisfed.org/pubs/region/07-12/fama.cfm⟩.

James Grant presented an elegant little talk on "My Hero, Benjamin Grossbaum," who is better-known to economists as Benjamin Graham, father of value investing and author of the 1934 classic *Security Analysis.* On Graham's life: "Some years ago, Fortune Magazine, in a squib it published on the occasion of Graham's induction into the U.S. Business Hall of Fame, said that the thrice-married father of value investing 'leaped from blonde to blonde like an Alpine goat springing from peak to peak.'" On his shaky start: "Between 1929 and 1932, his investment partnership lost 70% of its value. Not until 1936 did it recoup all it relinquished since the Crash. Yet Graham persevered and, along with his partner, Jerry Newman, went on to achieve a brilliant long-term investment record—not excluding those three disastrous years." On the Depression: "And as an educated man, he [Graham] could assume a certain detachment from the times in which he lived. He could see, for example, that the Great Depression was an anomalous catastrophe, one not to be repeated in his lifetime and therefore one against which an investor need not armor himself. It was a fluke." November 15, 2007. At ⟨http://www.grantspub.com/articles/bengraham⟩.

The American continues its series of interesting profiles of young economists. In the November–December 2007 issue, Caren Chesler discusses the work of Iván Werning in "The Theorist." "Previous studies have shown that the most efficient economic system causes inequality to grow. Policies that reduce inequality are believed to have a trade-off: If you punish people too much for doing well—by reducing their incentives to pass on wealth to their children—these people will reduce their effort, to the detriment of the economy as a whole. . . . Werning found that the models at the core of these judgments were incomplete. Allowing inequality to grow, unfettered, is economically optimal only if one looks at just the first generation. But if you take into account the children of first-generation parents, and their children's children, then the most preferable system is *not* one that allows inequality to grow, but one that attempts to stabilize the distribution of wealth. His paper shows that the transmission of wealth should be regulated to prevent an accumulation of luck—that children should essentially be insured against the family into which they are born." At ⟨http://www.american.com/archive/2007/november-december-magazine-contents/the-theorist⟩.

In the January–February 2008 issue of *The American*, Michael Moynihan discusses the work of Ben Olkin in "Graft Paper." "In 'Hit or Miss? The Effect of Assassinations on Institutions and War,' Olken and [Ben] Jones looked at the effects of political assassination, using a strict empirical methodology that takes into account economic conditions at the time of the killing and what Olken calls a "novel data set" of assassination attempts, successful and unsuccessful, between 1875 and 2004. Olken and Jones discovered that a country was 'more likely to see democratization following the assassination of an autocratic leader,' but found no substantial 'effect following assassinations—or assassination attempts—on democratic leaders.' They concluded that 'on average, successful assassinations of autocrats produce sustained moves toward democracy.' The researchers also found that assassinations have no effect on the inauguration of wars, a result that 'suggests that

World War I might have begun regardless of whether or not the attempt on the life of Archduke Franz Ferdinand in 1914 had succeeded or failed.'" At ⟨http://www.american.com/archive/2008/january-february-magazine-contents/graft-paper⟩.

Web Resources

William Nordhaus is director of the G-Econ project, which focuses on geographically based economic data. At the website ⟨http://gecon.yale.edu⟩, you can find a slowly revolving globe which shows economic output all over the world measured in squares of 1-degree longitude by 1-degree latitude.

Guido Imbens and Jeffrey Wooldridge presented an 18-hour course on "What's New in Econometrics" at the National Bureau of Research Summer Institute in 2007. Video of the lectures can be downloaded at ⟨http://www.nber.org/minicourse3.html⟩. For example, the first three lectures cover "Estimation of Average Treatment Effects under Unconfoundedness," "Linear Panel Data Models," and "Regression Discontinuity Designs."

The Tax Policy Center is producing an on-line "Tax Policy Briefing Book: A Citizens' Guide for the 2008 Election and Beyond." From the Introduction: "This Tax Policy Briefing Book offers a broad array of short explanations of important tax issues. Some simply provide background on the current state of tax and budgetary affairs: How much revenue does the federal government raise from which sources? How do Congress and the president decide on a budget? Others explain the key elements of the tax system: What taxes are now on the books? How do they affect individuals, families, and businesses? How do those effects change over time? Still others look forward, evaluating various proposals to improve the federal tax system: What incremental reforms would make the system work better? What impacts would more fundamental reforms have? Finally, a set of entries examines how state and local governments raise funds and how their taxes interact with the federal tax system." At ⟨http://www.taxpolicycenter.org/briefing-book⟩.

Discussion Starters

David Rotman investigates "The Price of Biofuels." Stephen Polasky "calculates that even if all the corn planted in the United States were used for ethanol, the biofuel would still displace only 12 percent of gasoline consumption. 'If I'm doing this for energy policy, I don't see the payback,' he says." "But despite years of research and recent investment in scaling up production processes, no commercial facility yet makes cellulosic ethanol. The economic explanation is simple: it costs far too much to build such a facility. Cellulose, a long-chain polysaccharide that makes up much of the mass of woody plants and crop residues such as cornstalks, is difficult—and thus expensive—to break down." "More than fifteen hundred miles away from the Midwest's corn belt, several California-based, venture-backed startups founded by pioneers in the fledging field of synthetic biology are creating new microörganisms designed to make biofuels other than ethanol." *Technology Review*, January/February 2008. Available (with free registration) at ⟨http://www.technologyreview.com⟩.

Generations of economics teachers have cited Frédéric Bastiat's classic "The Petition of the Candlemakers," in which candlemakers petition their legislators for protection from the unfair competition by sunlight, as a *reductio ad adsurdum* response to pleas for trade protectionism. Now, the European Candle Institute is investigating the possibility of an anti-dumping suit against imported Chinese candles. Bastiat's "Petition" began: "To the Honorable Members of the Chamber of Deputies. Gentlemen: You are on the right track. You reject abstract theories and have little regard for abundance and low prices. You concern yourselves mainly with the fate of the producer. You wish to free him from foreign competition, that is, to reserve the *domestic market* for *domestic industry*." The European Candle Institute writes: "The goal of initiating an anti-dumping procedure is only the establishing of a level playing field. This serves to maintain efficient production locations in Europe, secure European jobs, and to protect European consumers." Bastiat's essay is widely available on the web, including ⟨http://www.econlib.org/library/Bastiat/basSoph3.html#S.1,%20Ch.7,%20A%20Petition⟩. The website for the European Candle Institute is ⟨http://www.eci-candles.com⟩.

The Pew Global Attitudes Survey collects responses from 44 countries in "World Publics Welcome Global Trade—But Not Immigration." "The country with the world's largest economy is the least likely among surveyed countries to embrace global trade. Just 59% of Americans say trade with other countries is having a good effect on the U.S., down sharply from 2002, when 78% believed it was having a positive impact. . . . Roughly eight-in-ten (78%) of those younger than 30, and 58% of those ages 30 to 49, believe that trade has a positive impact on the United States. By comparison, people ages 50 and older are more divided (51% good, 43% bad)." October 4, 2007. At ⟨http://pewglobal.org/reports/pdf/258.pdf⟩.

■ *Thanks for Larry Willmore for suggestions and to Katherine Lim for research assistance.*