*Journal of Economic Perspectives—Volume 21, Number 1—Winter 2007—Pages 237–244*

# Recommendations for Further Reading

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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 a copy of the article (and possibly a few sentences describing it) to Timothy Taylor, c/o *Journal of Economic Perspectives,* Macalester College, 1600 Grand Ave., Saint Paul, Minnesota, 55105.

## Smorgasbord

The Bureau of Labor Statistics has published a fascinating report: "100 Years of U.S. Consumer Spending: Data for the Nation, New York City, and Boston." "As the 20th century began, the U.S. population was 76 million. . . . The median age in the country was 22.9 years, 23.3 for men and 22.4 for women. . . . Labor force participation was 80.0 percent for men and 20.6 percent for women. . . . Annual expenditures for the average U.S. family averaged $769. Of this amount, 42.5 percent ($327) was allocated for food, 14.0 percent ($108) for clothing, and 23.3 percent ($179) for housing. That left $155 for all other items. . . . [O]nly 19.0 percent of U.S. families owned a home, while 81.0 percent were renters." The report then traces these and other trends through nine time periods up to the twenty-first century. May 2006, Report 991. At ⟨http://www.bls.gov/opub/uscs/home.htm⟩.

Lant Pritchett argues *Let Their People Come: Breaking the Gridlock on Global Labor Mobility*. He writes: "The industrial world currently transfers something on the

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order of $70 billion a year in overseas development assistance. . . . A recent World Bank study has estimated the benefits of the rich countries allowing just a 3 percent rise in their labor force through relaxing restrictions. The gains from even this modest increase to poor-country citizens are $300 billion—roughly four and a half times that magnitude of foreign aid. What does it cost the rich countries to achieve these massive gains? Actually, according to these same estimates, the current rich-country residents *benefit* from this relaxation on distortions to labor markets—so the net cost is in reality a net *benefit* of $51 billion." He discusses six "accommodations" to encourage international labor mobility. From the website: "These include greater use of temporary worker permits, permit rationing, reliance on bilateral rather than multilateral agreements, and protection of migrants' fundamental human rights." Available as a free download at the Center for Global Development website, ⟨http://www.cgdev.org/content/publications/detail/10174⟩.

Clifford Winston has published *Government Failure vs. Market Failure: Microeconomics Policy Research and Government Performance*. "For more than a century, the primary market failure policies implemented by government have included antitrust policy and economic regulation to curb market power, so-called social regulatory policies to address imperfect information and externalities, and public financing of socially desirable services that the private sector would not provide. . . . Wolf (1979) introduced the term nonmarket failure to indicate some type of government failure and suggested that government failure may be of the same order of importance as market failure. An additional thirty years of empirical evidence on the efficacy of market failure policies initiated primarily by the federal government, but also by the states, suggests that the welfare cost of government failure may be considerably greater than that of market failure." September 2006. Available as a free download from the AEI-Brookings Joint Center for Regulatory website at ⟨http://www.aei-brookings.org/publications/abstract.php?pid=1117⟩.

Carolyn M. Hoxby presents "School Choice: The Three Essential Elements and Several Policy Options." "Three elements are essential in a school choice programme if it is to produce *general* improvements, not merely a reallocation of quality among students. The three essential elements are: 1 supply flexibility; 2 money that follows students; and 3 independent management of schools." "The prices that we set in a school choice scheme should attempt to fulfill a couple of purposes. First, prices should be set to guarantee that the playing field is level for competing suppliers of education. For instance, if a school happens to enroll students who are unusually expensive to educate it should not thereby become incapable of providing competition for schools that have not enrolled expensive-to-educate students. . . . Second, prices should be set to encourage families to make individual choices about human capital investment that are optimal." August 2006. Available through the website of the New Zealand-based Education Forum, at ⟨http://www.educationforum.org.nz/documents/publications/hoxby_2006.pdf⟩.

Pamela Loprest and Sheila Zedlewski investigate "The Changing Role of Welfare in the Lives of Low-Income Families with Children." "Reforms passed in 1996 ended welfare as we knew it. . . . The dramatic decline in welfare caseloads represents the most stunning post-reform outcome. Caseloads declined by over 50 percent in just a few years. . . . Work and work-related activity among current welfare recipients increased dramatically from 1997 to 2002. In 1997, 20.9 percent of recipients were working, compared with 29.2 percent in 2002. . . . Among single parents living alone, poverty declined for current welfare recipients. Deep poverty (income below 50 percent of the federal poverty level) dropped by over 16 percentage points between 1997 and 2002 (from 69 to 52.6 percent) . . . For single parents living alone, poverty levels remained fairly flat for recent welfare leavers and increased for the nonwelfare families." Urban Institute, Occasional Paper Number 73, posted August 30, 2006, to ⟨http://www.urban.org/publications/311357.html⟩.

Nicholas Eberstadt criticizes "The Mismeasure of Poverty." "To summarize the evidence from physical and biometric indicators: Low-income and poverty-level households today are better-fed and less threatened by undernourishment than they were a generation ago. Their homes are larger, better equipped with plumbing and kitchen facilities, and more capaciously furnished with modern conveniences. They are much more likely to own a car (or a light truck, or another type of motor vehicle) now than 30 years earlier. By most every indicator apart from obesity, their health care status is considerably more favorable today than at the start of the War on Poverty. Their utilization of health and medical services has steadily increased over recent decades. . . . The official poverty rate is incapable of representing what it was devised to portray: namely, a constant level of absolute need in American society. The biases and flaws in the poverty rate are so severe that it has depicted a great period of general improvements in living standards—three decades from 1973 onward—as a time of increasing prevalence of absolute poverty. We would discard a statistical measure that claimed life expectancy was falling during a time of ever-increasing longevity, or one that asserted our national finances were balanced in a period of rising budget deficits." *Policy Review*, August/September 2006, No. 138. At ⟨http://www.policyreview.org/138/eberstadt.html⟩.

Dennis Rasmussen asks, "Does 'Bettering Our Condition' Really Make Us Better Off? Adam Smith on Progress and Happiness." From the abstract: "Adam Smith is almost certainly history's most famous advocate of commercial society, but he frankly admits that the relentless pursuit of wealth is a major obstacle to tranquility and contentment and hence that, at first glance, the higher living standards that people "enjoy" in commercial society seem to come only at the cost of their happiness. I argue that the solution to this apparent paradox can be found in Smith's account of the positive political effects of commerce: dependence and insecurity are the chief obstacles to happiness and have been the hallmarks of most of human history, and so the alleviation of these ills in commercial society constitutes a great step forward. Money really cannot buy happiness, but the liberty and security that commercial societies tend to provide help to assuage the greatest sources of misery." *American Political Science Review*, August 2006, 100(3), pp. 309–318.

The Congressional Budget Office provides background on "Research and Development in the Pharmaceutical Industry." "Average prices of new drug products have been rising much faster than the rate of inflation, and annual R&D spending has grown faster still. Nevertheless, introductions of innovative new drugs have slowed. At the same time, drug companies have been able to charge high retail prices for new drugs that are only incrementally different from older drugs whose prices have fallen. . . . [I]t may cost hundreds of millions of dollars to develop an innovative new drug that then will cost only a few cents per dose to manufacture—and the price of the drug will have no obvious connection to either cost. Comparative information about drug quality from unbiased, head-to-head clinical trials of competing drugs is seldom published, although it would help drug purchasers make the best choices—and in turn improve the market signals that guide private companies' decisions about research and development. An understanding of how such factors interact with the industry's R&D process is necessary to recognize the underlying causes of any failure of the market to encourage a socially optimal level of drug R&D." October 2006. At ⟨http://www.cbo.gov/showdoc.cfm?index=7615&sequence=0⟩.

Ola Olsson explores the conditions in which "Diamonds are a Rebel's Best Friend." "I will try to explain why revenues from diamond mining have constituted a major impediment to social and economic progress in countries like Angola and Sierra Leone while they have been a cornerstone in the more successful development strategies of, for instance, Botswana and Namibia. I argue that two factors appear to have the greatest explanatory power in this regard; the strength of institutions of private property, as well as the nature of the extraction process." *World Economy*, August 2006, 29:8, pp. 1133–50. This article makes an interesting complement to the article by Debora L. Spar on "Continuity and Change in the International Diamond Market" in the Summer 2006 issue of this journal.

## From the Federal Reserve

Marcela Meirelles Aurelio studies "Going Global: The Changing Pattern of U.S. Investment Abroad." "Investors typically allocate only a small share of their portfolios to foreign assets. This pattern of investment behavior, known as 'home bias,' is puzzling because it causes investors to miss opportunities to diversify risks. . . . Recent evidence suggests that home bias might actually be declining. . . . Overall, the share of U.S. investments allocated to foreign assets swelled from 40 percent of GDP in 1990 to 89 percent in 2005." *Economic Review*, Federal Reserve Bank of Kansas City, Third Quarter 2006, pp. 5–32. At ⟨http://www.kc.frb.org/Publicat/Econrev/PDF/3Q06mma.pdf⟩.

In "Understanding Unemployment," Guillaume Rocheteau explains: "One of the most popular models used by macroeconomists today is the search-matching model of equilibrium unemployment. We explain this model, and show how it can be applied to understand the way various policies, such as unemployment benefits, taxes, or technological changes, can affect the unemployment rate." *Economic Commentary*, Federal Reserve Bank of Cleveland, October 15, 2006. At ⟨http://www.clevelandfed.org/research/com2006/1015.pdf⟩.

Mark Doms and Meryl Motika discuss reasons for "The Rise of Homeownership." "After decades of relative stability, the rate of U.S. homeownership began to surge in the mid-1990s, rising from 64% in 1994 to a peak of 69% in 2004, near which it has hovered ever since . . . [S]ome of the explanation likely stems from innovations in the mortgage market that resulted in greater access to credit, lower down payment requirements, and easy and low-cost access to the equity in a house, which makes homeownership more attractive." *FRBSF Economic Letter*, November 3, 2006. At ⟨http://www.frbsf.org/publications/economics/letter/2006/el2006-30.html⟩.

Rebecca Hellerstein, Deirdre Daly, and Christina Marsh ask, "Have U.S. Import Prices Become Less Responsive to Changes in the Dollar?" From the abstract: "The failure of the dollar's depreciation to narrow the U.S. trade deficit has driven recent research showing that the transmission of exchange rate changes to import prices has declined sharply in industrial countries. Estimates presented in this study, however, suggest that 'pass-through' to U.S. import prices has fallen only modestly, if at all, in the last decade. The authors argue that methodological changes in the collection of import data and the inclusion of commodity prices in pass-through models may have contributed to earlier findings of low pass-through rates." *Current Issues in Economics and Finance*, Federal Reserve Bank of New York, September 2006, 12(6). At ⟨http://www.newyorkfed.org/research/current_issues/ci12-6.html⟩.

## Sound and Pictures

Hans Rosling, a professor of international health in Sweden, delivers a wonderful lecture on global trends in health, demography, and economics. The talk is intrinsically interesting. For example, he points out that the world has made a transition over recent decades from being divided into two groups, long life/small family and short life/large family, into a world where most countries outside of Africa have long lives and small families. But especially striking is that Rosling has founded a nonprofit software provider called Gapminder to provide vivid moving illustrations of how countries' health and economic statistics evolve over time. Recorded February 2006. Rosling's presentation is available at the Technology Entertainment Design website at ⟨http://www.ted.com/tedtalks/tedtalksplayer.cfm?key=hans_rosling⟩. The software website is ⟨http://gapminder.org/index.html⟩.

The World Bank runs B-SPAN, an Internet-based broadcasting service, on which you can watch a number of its conferences. For example, presentations are available from the Annual Bank Conference on Development Economics (ABCDE) in Tokyo in May 2006. In his keynote address, Joseph Stiglitz talks about "Aid for Trade." From the website overview: "A new trade framework is needed as trade globalization by itself has proved to be not sufficient to increase trade for developing countries. Stiglitz called for the existing multilateral structure (involving the International Monetary Fund, the World Bank, the International Trade Centre, UNCTAD, and UNDP) to be consolidated into a new 'Global Trade Facility.'" At ⟨http://info.worldbank.org/etools/BSPAN/index.asp⟩.

At the Library of Economics and Liberty website, Russ Roberts is offering podcast interviews that you can play or download. Want to listen in on 43 minutes of conversation with Milton Friedman about *A Monetary History of the United States, 1870–1960* and *Capitalism and Freedom*? Or 47 minutes with Sam Peltzman on regulation? Or 57 minutes with Richard Thaler on "libertarian paternalism"? These and many more available at ⟨http://www.econtalk.org⟩.

## About Economists

The Nobel Prize website presents a readable and informative essay summarizing "Edmund Phelps's Contributions to Macroeconomics." "How should fiscal and monetary policy resolve the conflict between the goals of low inflation and low unemployment? How should society trade off consumption today against consumption in the future, i.e., how much should be saved in order to increase future consumption? Edmund Phelps has made major contributions to the analysis of both of these tradeoffs. In particular, he had the insight that also the balance between inflation and unemployment reflects a fundamentally *intertemporal* problem. Phelps pointed out that current inflation depends not only on unemployment but also on inflation expectations. Such dependence is due to the fact that wages and prices are adjusted only infrequently. Consequently, when adjustments are made, they are based on inflation forecasts. Thus, the higher the anticipated rate of inflation, the higher the unemployment required to reach a certain actual inflation rate. . . . Phelps's contributions from the late 1960s and early 1970s radically changed our perception of the interaction between inflation and unemployment." October 9, 2006. At ⟨http://nobelprize.org/nobel_prizes/economics/laureates/2006/ecoadv06.pdf⟩.

Douglas Clement offers a wide-ranging and provocative "Interview with Martin Feldstein." Feldstein on the long-term fiscal outlook: "[T]here's nothing about long-term interest rates that suggests that the markets are afraid that Social Security and Medicare are really going to create large fiscal deficits. Now maybe they're right." On national savings: "Well, that process of mortgage refinancing is reversing now, and with mortgage rates significantly higher, a full percentage point higher than they were a year ago, there isn't the incentive for people to refinance. . . . I think there'll be a natural turnaround in the savings rate. If that happens relatively quickly, it will cause a significant slowdown in aggregate demand in this country. Of course, many people are saying that we need to improve our trade imbalance, and in order to improve our trade imbalance, we have to save more. I think this is where the saving will come from." On executive compensation: "I guess in the boards that I've served on I've never felt that excess compensation was a serious problem. There was a recent NBER paper explaining why there's been this *n*-fold increase in executive compensation for the top companies. Well, lo and behold, the top companies are *n*-fold larger than they were 20 years ago, and so if you think about the compensation in proportion to the size of the business, in part because of mergers, in part because of just growth and the big ones growing more than others, that gives you an explanation of what's going on." *The Region*, Federal Reserve Bank of Minneapolis, September 2006, pp. 13–21. At http://www.minneapolisfed.org/pubs/region/06-09/Feldstein.cfm.

Aaron Steelman conducts a thoughtful "Interview" with Guillermo Calvo. On exchange rates: "The exchange rate can be thought as of a *bridge* between the domestic and international economy. Exports have to go over that bridge, and if exchange rates are highly volatile and noncredible, coupled with incomplete futures markets, the life of the exporter can be very difficult. That will have negative effects on trade and, consequently, on growth." On inequality and growth: "I can imagine the mechanism: Inequality causes political tension, which causes politicians to pursue policies that cater to the poor by taxing capital, which induces capital flight, which lowers growth. Eventually, the situation gets so bad that even left-of-center governments change policies and adopt a more market-oriented approach. That works for a while—you get increased growth but income distribution deteriorates again. That's the story and it seems to fit the facts. If it's true, then it's a real trap. It's not clear how you get out of it." On a Latin American currency union: "I think it is a bit premature for Latin America to adopt a currency union. But this doesn't mean that the region shouldn't begin taking steps toward that goal. For instance, Europe did not adopt its currency union overnight. It took many years, indeed decades, to establish how the system was going to work and then to implement it." *Region Focus*, Federal Reserve Bank of Richmond, Summer 2006, pp. 44–48. At http://www.richmondfed.org/publications/economic_research/region_focus/summer_2006/interview_web_exclusive.cfm.

John Toye writes an "Obituary: Hans Singer and International Development." Hans Singer "served the UN for 22 years with deep energy and commitment and a cornucopia of policy ideas. . . . [H]e made his mark almost at once, with a study of the terms of trade of developing countries that was completed by the end of 1948. The official requirement was to look at recent changes in their terms of trade, but Singer on his own initiative added a historical dimension to the report. Using British trade data, he pointed out that the terms of trade for countries exporting primary commodities had been declining for 100 years . . . This doctrine has long been known as the "Prebesch–Singer thesis' because it appeared in the writing of Raul Prebisch, of the UN Economic Commission for Latin America, at about the same time as Hans published it." *Journal of International Development*, 2006, 18(6), pp. 915–23.

## Discussion Starters

Barun Mitra discusses "Saving the Tiger: China and India Move in Radically Different Directions." "Since the 1970s, India has enacted tough laws and mobilized huge resources to stop hunting and trading in tiger parts. But the policy of prohibition has not secured the future of tigers." Meanwhile, in China, "special tiger breeding bases have been set up under public and private management. More than 4,000 tigers are in captivity in China today, and an effort is underway to build a genetic profile of every tiger in captivity so that the number of pure subspecies can be documented and increased. This will enable breeders to meet the international demand for pure-bred tiger cubs and young adults of particular subspecies." *PERC Reports*, September 2006, pp. 3–6. At ⟨http://www.perc.org/perc.php?subsection=5&id=822⟩.

In the *Economist*, in a middle-of-the-issue "Survey of the World Economy," Pam Woodall begins: "Last year the combined output of emerging economies reached an important milestone: it accounted for more than half of total world GDP (measured at purchasing-power parity). This means that the rich countries no longer dominate the global economy. . . . Emerging economies are driving global growth and having a big impact on developed countries' inflation, interest rates, wages and profits. As these newcomers become more integrated into the global economy and their incomes catch up with the rich countries, they will provide the biggest boost to the world economy since the industrial revolution. Indeed, it is likely to be the biggest stimulus in history, because the industrial revolution fully involved only one-third of the world's population. By contrast, this new revolution covers most of the globe, so the economic gains—as well as the adjustment pains—will be far bigger." A section late in the survey is headed: "Playing Leapfrog: If today's rich world does not watch out, it could become tomorrow's relatively poor world." "The New Titans," *The Economist*, September 16, 2006.

Edmund Phelps, the most recent Nobel laureate, has written "Dynamic Capitalism: Entrepreneurship is Lucrative—And Just" for the op-ed page of the *Wall Street Journal*. "The main benefit of an innovative economy is commonly said to be a higher level of productivity—and thus higher hourly wages and a higher quality of life. There is a huge element of truth in this belief, no matter how many tens of qualifications might be in order. . . . I would, however, stress a benefit of dynamism that I believe to be far more important. Instituting a high level of dynamism, so that the economy is fired by the new ideas of entrepreneurs, serves to transform the workplace—in the firms developing an innovation and also in the firms dealing with the innovations. The challenges that arise in developing a new idea and in gaining its acceptance in the marketplace provide the workforce with high levels of mental stimulation, problem-solving, employee-engagement and, thus, personal growth." October 10. At ⟨http://www.opinionjournal.com/editorial/feature.html?id=110009068⟩.

■ *Thanks to Larry Willmore and others for suggestions, and to Jesse Dylan Keith for assistance in checking quotations and sources.*