Journal of Economic Perspectives—Volume 26, Number 1—Winter 2012—Pages 243–250

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, with occasional exceptions, 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, preferably by e-mail at ⟨taylort@macalester.edu⟩, or c/o *Journal of Economic Perspectives*, Macalester College, 1600 Grand Ave., Saint Paul, Minnesota, 55105.

Smorgasbord

W. Brian Arthur discusses the scope of "The Second Economy." "I want to argue that something deep is going on with information technology, something that goes well beyond the use of computers, social media, and commerce on the Internet. Business processes that once took place among human beings are now being executed electronically. They are taking place in an unseen domain that is strictly digital. On the surface, this shift doesn't seem particularly consequential—it's almost something we take for granted. But I believe it is causing a revolution no less important and dramatic than that of the railroads. It is quietly creating a second economy, a digital one. . . . Now this second, digital economy isn't producing anything tangible. It's not making my bed in a hotel, or bringing me orange juice in the morning. But it is running an awful lot of the economy. It's helping architects

■ *Timothy Taylor is Managing Editor,* Journal of Economic Perspectives*, based at Macalester College, Saint Paul, Minnesota. His e-mail address is ⟨taylort@macalester.edu⟩ and he blogs at ⟨http://conversableeconomist.blogspot.com/⟩.*

doi=10.1257/jep.26.1.243

design buildings, it's tracking sales and inventory, getting goods from here to there, executing trades and banking operations, controlling manufacturing equipment, making design calculations, billing clients, navigating aircraft, helping diagnose patients, and guiding laparoscopic surgeries. Such operations grow slowly and take time to form. . . . Is this the biggest change since the Industrial Revolution? Well, without sticking my neck out too much, I believe so. In fact, I think it may well be the biggest change ever in the economy. It is a deep qualitative change that is bringing intelligent, automatic response to the economy. There's no upper limit to this, no place where it has to end. . . . I think that for the rest of this century, barring wars and pestilence, a lot of the story will be the building out of this second economy, an unseen underground economy that basically is giving us intelligent reactions to what we do above the ground." *McKinsey Quarterly*. October 2011. Free registration needed, at ⟨http://www.mckinseyquarterly.com/Strategy/Growth/The_second_economy_2853⟩.

Choices, published by the Agricultural and Applied Economics Association, has a set of six short readable articles with diverse views on the subject: "Should Soft Drinks Be Taxed More Heavily?" For example, Jason Fletcher writes: "[S]oft drink consumption has increased by almost 500% in the past 50 years, and recent data suggest it represents 7% of overall energy intake in adults and often larger proportions in children . . . a 16% share of calories in youth ages 12–19 and 11% in children ages 2–11. . . . We know that soda consumption is an important share of total consumption, and ample evidence suggests that maintained reductions in consumption of approximately 100 calories per day—less than a can of soda—could halt weight gain for 90% of the population . . . Fletcher continues: "[W]hile individuals in states with higher soda taxes have lower soda consumption, these individuals completely offset the reductions in calories from soda by consuming other high-calorie beverages, such as milk and juice." October 2011. At ⟨http://www.choicesmagazine.org/choices-magazine/policy-issues/should-soft-drinks-be-taxed-more-heavily⟩.

Zsolt Darvas tells "A Tale of Three Countries: Recovery after Banking Crisis." "Three small, open European economies—Iceland, Ireland and Latvia with populations of 0.3, 4.4 and 2.3 million respectively—got into serious trouble during the global financial crisis. Behind their problems were rapid credit growth and expansion of other banking activities in the years leading up to the crisis, largely financed by international borrowing. This led to sharp increases in gross (Iceland and Ireland) and net (Iceland and Latvia) foreign liabilities. Credit booms fuelled property-price booms and a rapid increase in the contribution of the construction sector to output—above 10 percent in all three countries. While savings–investment imbalances in the years of high growth were largely of private origin, public spending kept up with the revenue overperformance that was the consequence of buoyant economic activity. During the crisis, property prices collapsed, construction activity contracted and public revenues fell, especially those related to the previously booming sectors. . . . [T]he crisis hit Latvia harder than any other country, and Ireland also suffered heavily, while Iceland exited the crisis with the smallest fall in employment, despite the greatest shock to the financial system. . . . There were marked differences in

policy mix: currency collapse in Iceland but not in Latvia, letting banks fail in Iceland but not in Ireland, and the introduction of strict capital controls only in Iceland. The speed of fiscal consolidation was fastest in Latvia and slowest in Ireland. Recovery has started in all three countries. Iceland seems to have the right policy mix." *Bruegel Policy Contribution*, December 2011, Issue 2011/19. At ⟨http://www.bruegel.org/download/parent/663-a-tale-of-three-countries-recovery-after-banking-crises/file/1534-a-tale-of-three-countries-recovery-after-banking-crises/⟩.

The Committee on Economic and Environmental Impacts of Increasing Biofuels Production of the National Research Council has published "Renewable Fuel Standard: Potential Economic and Environmental Effects of U.S. Biofuel Policy." Some findings: "Only in an economic environment characterized by high oil prices, technological breakthroughs, and a high implicit or actual carbon price would biofuels be cost-competitive with petroleum-based fuels." "RFS2 [renewable fuel standards] may be an ineffective policy for reducing global GHG [greenhouse gas] emissions because the effect of biofuels on GHG emissions depends on how the biofuels are produced and what land-use or land-cover changes occur in the process." "Absent major technological innovation or policy changes, the RFS2-mandated consumption of 16 billion gallons of ethanol-equivalent cellulosic biofuels is unlikely to be met in 2022." A "prepublication copy" can be downloaded (with free registration) at ⟨http://www.nap.edu/catalog.php?record_id=13105⟩.

Kathleen Short describes "The Research Supplemental Poverty Measure: 2010." Here's a table from that report summarizing how the new supplemental measure of poverty from the U.S. Census Bureau differs from the official measure:

	Official poverty measure	*Supplemental poverty measure*
Measurement units	Families and unrelated individuals	All related individuals who live at the same address, including any coresident unrelated children who are cared for by the family (such as foster children) and any cohabitors and their children
Poverty threshold	Three times the cost of minimum food diet in 1963	The 33rd percentile of expenditures on food, clothing, shelter, and utilities (FCSU) of consumer units with exactly two children multiplied by 1.2
Threshold adjustments	Vary by family size, composition, and age of householder	Geographic adjustments for differences in housing costs and a three parameter equivalence scale for family size and composition
Updating thresholds	Consumer Price Index: all items	Five year moving average of expenditures on FCSU
Resource measure	Gross before-tax cash income	Sum of cash income, plus in-kind benefits that families can use to meet their FCSU needs, minus taxes (or plus tax credits), minus work expenses, minus out-of-pocket medical expenses

Current Population Reports P60-241. November 2011. At ⟨http://www.census.gov

/hhes/povmeas/methodology/supplemental/research/Short_ResearchSPM 2010.pdf⟩.

Thorstein Beck has edited an e-book on *The Future of Banking*. It includes 12 readable essays by expert economists, based on their academic research. As one example, here is Neeltje van Horen on "The Changing Role of Emerging-Market Banks." "Although many in the West are not familiar with emerging-market banks, they are by no means small. In fact, the world's biggest bank in market value is China's ICBC. The global top 25 includes eight emerging-market banks. Among these, three other Chinese banks (China Construction Bank, Agricultural Bank of China, and Bank of China), three Brazilian banks (Itaú Unibanco, Banco do Brasil, and Banco Bradesco) and one Russian bank (Sberbank). While excess optimism might have inflated these market values, these banks are large with respect to other measures as well. In terms of assets all these banks are in the top 75 worldwide, with all four Chinese banks in the top 20. Furthermore, in 2010 emerging-market banks as a group accounted for roughly 30% of global profits, a third of global revenues, and half of tier 1 capital." She points out that these banks have in some ways been sheltered from the financial turmoil of the last few years, are located in fast-growing countries with high domestic savings rates, and thus are poised to continue rapid growth. Vox. October 25, 2011. At ⟨http://www.voxeu.org/index.php?q=node/7147⟩.

From the Federal Reserve

Jun Nie and Ethan Struby ask: "Would Active Labor Market Policies Help Combat High U.S. Unemployment?" By "active" labor market policies, they mean government support for job training, job search, incentives for private firms to hire, or even direct job creation. In contrast, "passive" policies are unemployment benefits or early retirement. "The level of spending on labor market policies differs widely across OECD countries. Between 1998 and 2008 in 21 OECD countries, total expenditures on passive and active labor market policies as a fraction of GDP ranged from about 4 percent in Denmark to 0.25 percent in the United Kingdom (Chart 3). The United States is near the bottom of this list, spending slightly less than 0.5 percent of GDP on labor market policies during this time. In addition, the fraction of spending on active versus passive policies differs across countries. Outside the United States, the average country in Chart 3 devoted 59 percent of labor market policy expenditures to PLMP [passive labor market policies] and 41 percent to ALMP [active labor market policies]. In the United States, however, 70 percent of expenditures went to PLMP and 30 percent went to ALMP." They present some evidence supporting greater spending assistance for job training and for job search. *Economic Review,* Federal Reserve Bank of Kansas City, Third Quarter 2011, pp. 35–69. At ⟨http://www.kansascityfed.org/publicat/econrev/pdf/11q3Nie-Struby.pdf⟩.

Christopher J. Neely tells of the international exchange rate intervention to stabilize the value of the Japanese yen in the aftermath of the March 2011 earthquake

in "A Foreign Exchange Intervention in an Era of Restraint." Neely reports that the major central banks of the world have carried out only three exchange rate interventions since 1995: an intervention after Japan's quake in March 2011, an intervention soon after the start of the euro in September 2000, and an intervention in the yen after East Asia's financial crisis in 1998. He tells what happened in each case, and sums up: "Since 1995 most advanced governments/central banks have used intervention only very sparingly as a policy tool. Examination of coordinated interventions during this period shows that intervention is not a magic wand that authorities can use to move exchange rates at will. It can be a very effective tool in certain circumstances, however, to coordinate market expectations about fundamental values of the exchange rate and calm disorderly foreign exchange markets by reintroducing two-sided risk." *Review,* Federal Reserve Bank of St. Louis, September/October 2011, pp. 303–324. At ⟨http://research.stlouisfed.org/publications/review/11/09/303-324Neely.pdf⟩.

Inequality around the World

The OECD has published *Divided We Stand: Why Inequality Keeps Rising.* "In OECD countries today, the average income of the richest 10% of the population is about nine times that of the poorest 10%—a ratio of 9 to 1. However, the ratio varies widely from one country to another. It is much lower than the OECD average in the Nordic and many continental European countries, but reaches 10 to 1 in Italy, Japan, Korea, and the United Kingdom; around 14 to 1 in Israel, Turkey, and the United States; and 27 to 1 in Mexico and Chile. "Benefits had a much stronger impact on inequality than the other main instruments of cash distribution—social contributions or taxes. . . . The most important benefit-related determining factor in overall distribution, however, was not benefit levels but the number of people entitled to transfers." "However, redistribution strategies based on government transfers and taxes alone would be neither effective nor financially sustainable. First, there may be counterproductive disincentive effects if benefit and tax reforms are not well designed. Second, most OECD countries currently operate under a reduced fiscal space which exerts strong pressure to curb public social spending and raise taxes. Growing employment may contribute to sustainable cuts in income inequality, provided the employment gains occur in jobs that offer career prospects. Policies for more and better jobs are more important than ever." December 2011. The report can be read for free online, although the software for doing so is a bit awkward, and an overview chapter can be downloaded as a PDF, at ⟨http://www.oecd.org/document/51/0,3746,en_2649_33933_49147827_1_1_1_1,00.html⟩.

The September 2011 issue of *Finance & Development* has four articles about economic inequality around the world. For example, Branko Milanovic writes "More or Less: Income Inequality Has Risen over the Past Quarter-Century Instead of Falling as Expected." "The view that income inequality harms growth—or that improved equality can help sustain growth—has become more widely held in recent

years. . . . Historically, the reverse position—that inequality is good for growth—held sway among economists. The main reason for this shift is the increasing importance of human capital in development. When physical capital mattered most, savings and investments were key. Then it was important to have a large contingent of rich people who could save a greater proportion of their income than the poor and invest it in physical capital. But now that human capital is scarcer than machines, widespread education has become the secret to growth. And broadly accessible education is difficult to achieve unless a society has a relatively even income distribution. Moreover, widespread education not only demands relatively even income distribution but, in a virtuous circle, reproduces it as it reduces income gaps between skilled and unskilled labor. So economists today are more critical of inequality than they were in the past." At ⟨http://www.imf.org/external/pubs/ft/fandd/2011/09/⟩.

The *World Development Report 2012* from the World Bank is centered on the theme: "Gender Equality and Development." The report suggests considerable worldwide progress in gender equality in education and health. "Although boys are more likely than girls to be enrolled in primary school, girls make better progress—lower repetition and lower dropout rates—than boys in all developing regions. . . . Gender now explains very little of the remaining inequality in school enrollment . . ." "In most world regions, life expectancy for both men and women has consistently risen, with women on average living longer than men . . . On various other aspects of health status and health care, differences by sex are small. In many low-income countries, the proportion of children stunted, wasted, or underweight remains high, but girls are no worse off than boys. . . . Similarly, there is little evidence of systematic gender discrimination in the use of health services or in health spending." The report also points out where a high degree of gender inequality persists: for example, lack of female participation in certain occupations and in political leadership. Also, gender bias at birth remains strong in many places: "In China and India, sex ratios at birth point to a heavily skewed pattern in favor of boys. Where parents continue to favor sons over daughters, a gender bias in sex-selective abortions, female infanticide, and neglect is believed to account for millions of missing girls at birth. In 2008 alone, an estimated 1 million girls in China and 250,000 girls in India were missing at birth." Available by searching at WorldBank.org.

About Economists

Douglas Clement has a wide-ranging "Interview with Daron Acemoglu" in *The Region* (Federal Reserve Bank of Minneapolis). On the Dodd–Frank financial reform legislation: "I think the problem with the Dodd–Frank Act is that the amount of good it contains seems to be dwarfed by the amount of additional minute details it contains. That fails to achieve the intent of the regulation. It also gives better regulation a bad name, because people who are opposed to regulation can easily point to the page after page after page of paperwork and procedural things that Dodd–Frank wants you to do. And I am not convinced that the Dodd-Frank Act is

going to prevent the next financial collapse if the financial system actually continues on its current trajectory." On economic growth and political institutions: "But later in college and graduate school, I started working on issues related to human capital, economic growth and so on. But then after a while, I sort of realized, well, you know, the real problems of economic growth aren't just that some countries are technologically innovative and some aren't, and some countries have high savings rates and some don't. They are really related to the fact that societies have chosen radically different ways of organizing themselves. So there is much meaningful heterogeneity related to economic outcomes *in the political structures* of societies." September 2011, pp. 18–31. At ⟨http://www.minneapolisfed.org/publications_papers/pub_display.cfm?id=4733⟩.

George S. Tavlas discusses the nineteenth century American economist Alexander Del Mar in "The Money Man." James Tobin called him "one of the most important U.S. monetary economists of the 19th century"; Robert Mundell called him "too hot to handle." Del Mar was a co-founder in 1865 of the *New York Social Science Review: Devoted to Political Economy and Statistics*, often thought of as one of the first economics journals published in the United States. He was also the first director of the U.S. Bureau of Statistics in 1866—which later evolved into the U.S. Department of Commerce. Del Mar was far ahead of his time in thinking of money as a unit of account and a yardstick of value. In 1886, he proposed that the government should commit to increasing the money supply by 3 percent annually—thus scooping Milton Friedman's similar proposal by about seven decades. *American Interest*, November–December 2011, pp. 110–14. At ⟨http://www.the-american-interest.com/article.cfm?piece=1112⟩.

Discussion Starters

Jeffrey Frankel has a readable overview of the arguments over "The Curse: Why Natural Resources are Not Always a Good Thing." "It is striking how often countries that are rich with oil, minerals or fertile land have failed to grow more rapidly than those without. Angola, Nigeria and Sudan are all awash in petroleum, yet most of their citizens are bitterly poor. Meanwhile, East Asian economies, including Japan, Korea, Taiwan, Singapore and Hong Kong, have achieved Western-level standards of living despite being rocky islands (or peninsulas) with virtually no exportable natural resources. This is the phenomenon known to economists as the 'natural resources curse.' The evidence for its existence is more than anecdotal. The curse shows up in econometric tests of the determinants of economic performance across a comprehensive sample of countries." Before suggesting some policy responses, Frankel reviews five possible reasons behind the "curse": 1) Commodity prices fluctuate a lot, so an economy that depends on commodity exports will be hit by a series of shocks; 2) An economy focused on natural resources diverts land, labor, and capital from other sectors of the economy, like manufacturing; 3) Natural resource endowments can foster corruption and weak institutions, as different groups

jostle for control of the income from the resources; 4) High exports of natural resources can lead to currency appreciation which then disadvantages all other exports; and 5) Natural resources can be depleted. *Milken Institute Review*, Fourth Quarter 2011. Available (with free registration) at ⟨http://www.milkeninstitute.org/publications/⟩.

Ahmad Faruqui and Jennifer Palmer look at how households react to variable pricing of electricity in "Dynamic Pricing and Its Discontents." "[A]lmost all analyses of pilot results show that customers do respond to dynamic pricing rates by lowering peak usage. Indeed, in 24 different pilots involving a total of 109 different tests of time-varying rates—covering many different locations, time periods, and rate designs—customers have reduced peak load on dynamic rates relative to flat rates, with a median peak reduction (or demand response) of 12 percent. . . . In other words, the demand for electricity does respond to price, just like the demand for other products and services that consumers buy." "At the national level, an assessment carried out for FERC [Federal Energy Regulatory Commission] two years ago showed that the universal application of dynamic pricing in the United States had the potential for quintupling the share of U.S. peak demand that could be lowered through demand response, from 4 percent to 20 percent. Another assessment quantified the value of demand response and showed that even a 5 percent reduction in U.S. peak demand could lower energy costs $3 billion a year." *Regulation*, Fall 2011, pp. 16–22. At ⟨http://www.cato.org/pubs/regulation/regv34n3/regv34n3-5.pdf⟩. This paper is a useful complement to the paper by Paul Joskow in this issue.

The U.S. Government Accountability Office reported on: "Horse Welfare: Action Needed to Address Unintended Consequences from Cessation of Domestic Slaughter." "Since fiscal year 2006, Congress has annually prohibited the use of federal funds to inspect horses destined for food, effectively prohibiting domestic slaughter. . . . Since domestic horse slaughter ceased in 2007, the slaughter horse market has shifted to Canada and Mexico. From 2006 through 2010, U.S. horse exports for slaughter increased by 148 and 660 percent to Canada and Mexico, respectively. As a result, nearly the same number of U.S. horses was transported to Canada and Mexico for slaughter in 2010—nearly 138,000—as was slaughtered before domestic slaughter ceased. . . . GAO analysis of horse sale data estimates that closing domestic horse slaughtering facilities significantly and negatively affected lower-to-medium priced horses by 8 to 21 percent; higher-priced horses appear not to have lost value for that reason. . . . Comprehensive, national data are lacking, but state, local government, and animal welfare organizations report a rise in investigations for horse neglect and more abandoned horses since 2007." In November 2011, President Obama signed a new agriculture bill into law that will probably allow U.S. horse slaughter facilities to re-open. June 2011. At ⟨http://www.gao.gov/new.items/d11228.pdf⟩.