Finn Kydland Wins 2004 Nobel Prize in Economics

Chancellor Places Congratulatory Call to Norway

The Nobel Foundation has awarded the 2004 Nobel Prize in Economic Sciences to Finn Kydland, the Jeffrey Henley Professor of Economics at UCSB. Professor Kydland shares the Prize with Professor Edward Prescott of Arizona State University, a previous Maxwell Pellish Visiting Professor in the UCSB Economics Department. Kydland and Prescott were awarded the Prize “for their contribution to dynamic macroeconomics: the time consistency of economic policy and the driving forces behind business cycles.”

In 1968, the Sveriges Riksbank (Bank of Sweden) instituted the Prize in Economic Sciences in memory of Alfred Nobel, founder of the Nobel Prize. Each prize consists of a medal, personal diploma, and prize amount.

On October 12 last year, Department members, campus administrators, and members of the press gathered in the Faculty Club courtyard to hear Chancellor Henry Yang place a congratulatory phone call to Professor Kydland in Bergen, Norway where the Laureate was delivering a lecture at the Norwegian School of Economics and Business Administration. “I am obviously delighted to be on the faculty at UCSB and so glad that everyone there is excited about this news,” said Kydland. “I’m a little bit of a shy person in public, but I guess I’ll have to get used to this attention.” The Economics Department is honored to have such an esteemed colleague among its ranks.

Economics Department Welcomes Two New Junior Faculty to the Campus

 Marek Kapicka joined the faculty in 2003, with a Masters degree from Charles University in Prague, and a Ph.D. from the University of Chicago. His research concentrates on macroeconomics, public finance, economic theory, and contract theory.

Javier Birchenall joined the faculty in 2004. He, too, comes to us from the University of Chicago, having earned both his Masters and Doctorate degrees there. His research concentrates on economic growth and development and on population economics.

Chair’s Message

It’s Easy to Spot the Winners!

By Peter J. Kuhn

Anyone who knows UCSB Economics will tell you that, without a doubt, 2004-05 was an especially exciting academic year. For example, in July 2004 we welcomed two new faculty members: Javier Birchenall from the University of Chicago and Finn Kydland from Carnegie Mellon University. Two short months later, we were delighted to learn that Finn Kydland had received the Nobel Prize in Economic Sciences for his research on business cycles. As the academic year progressed, other department members made important discoveries in a variety of areas, including the economics of market bubbles, the economics of education, and of natural resources. Meanwhile, demand for our undergraduate and graduate programs continued at extremely high levels, and standards continued to rise. Finally, with the advent of a new macroeconomics research center and the prospects of adding more new faculty to meet burgeoning student demand, we are more optimistic than ever about the future. I look forward to sharing those developments with you in the next issue of EconNews!
Natural Resource Riches: Blessing or Curse?
UCSB Economists Work to Solve the Mystery

By Robert T. Deacon and Catherine S. Norman

Why are countries rich in natural resources so often home to poor, unhealthy, and politically oppressed populations? Curiously, this perverse effect (dubbed the curse of natural resources) happens most often when resources are naturally concentrated, such as oil and gold, and when the countries where they are located suffer from civil strife or oppressive government. Nigeria is a case in point. Despite earning massive revenues from oil, the country’s per capita income has fallen 30% since 1965 and now stands at less than $1000 per year. Investigators have identified the same phenomenon elsewhere for metallic minerals, hardwood timber, and even bird guano! Some observers speculate that struggles to control these valuable resources cause political instability and that dense concentration of resource wealth leads to concentrated, hence authoritarian, political power.

Until now, research to determine the impact of these struggles on local populations has focused only on average income. Recent research, however, by two UCSB economists—Robert Deacon and Catherine Norman—has shed new light on other factors. One study examined whether a resource curse applies to “human welfare” measures such as malnutrition, life expectancy, literacy, and access to clean water. A second study employed better measures of resource abundance than past research projects. The study also used innovative empirical methods, thus providing a broader set of data than was previously available. Both studies found additional evidence for a resource curse—applying both to income and other welfare measures—and both concluded that the curse operates in part by affecting political institutions.

(For a more complete account of this work, see articles by Bulte, Damania, and Deacon and by Norman in “Resources.”)

Resources:


Robert Deacon is a Professor of Economics who has been at UCSB since 1972. His research interests include natural resource and environmental economics.

Catherine Norman is a 2005 graduate who worked under Stephen DeCanio and Bob Deacon on growth and the environment. This fall, she joined the faculty of Johns Hopkins University.
**ARE COASTAL CALIFORNIA HOME PRICES IN A BUBBLE?**

*Probably...*

By Stephen F. LeRoy

There is no doubt whatsoever that fundamentals justify high real estate prices in California coastal areas. Nevertheless, real estate prices could still have a bubble component—possibly large. After all, fundamentals justified high prices in most historical episodes identified in hindsight as bubbles (an excellent historical review of bubbles is Chancellor (see “Resources”).

For example, in the early 18th century the English crown granted the South Sea Company a trade monopoly with the new world, including the slave trade. Fundamentals at that time justified a high price for such a stock, but most people thought prices rose much higher than was consistent with absence of a bubble. In the 1920s, U.S. stock prices rose to unprecedented levels, but wasn’t that optimism reasonable considering the obvious future importance of electricity and the automobile? Similarly with Japan in the 1980s and the U.S. dot-com/telecom stock price run up in the 1990s.

A major reason to suspect a real estate bubble is that housing rents have been essentially flat in California for five years, while home prices have been rising faster than ever. This is partly due to low interest rates, but only partly. It appears increasingly likely that prices are rising because people expect them to rise, not because homebuyers are becoming increasingly optimistic about fundamentals.

This point is argued more fully in LeRoy (see “Resources”).

*Probably Not...*

By Bill Watkins

I see things a little differently. True, home prices in coastal areas of California have risen at double-digit annual rates. Moreover, this growth occurred at a time when the region’s economy was weak and demographic growth was slow or negative. However, while these growth rates cannot be maintained in the indefinite future, I believe economic fundamentals are likely behind the observed price increases.

To understand why, keep in mind that coastal California is *not* a local housing market. Demographics, wealth accumulation, interest rates, taxes, and increasingly limited supply all play a significant part in the boom. There are compelling reasons, then, for strong coastal California home price growth:

- Coastal California is a desirable location, and significant home demand comes from outside the area.
- Outside demand is often from wealthy retirees, a group whose numbers have been growing as a result of demographics, recent economic growth, and inheritance.
- Falling mortgage rates and tax code changes, particularly the elimination of taxation on large gains from the sale of homes, have strengthened demand.
- Finally, while Coastal California land has always been in relatively short supply, it has become increasingly difficult to develop that land, effectively reducing supply.

Therefore, I have to disagree with Stephen F. LeRoy. My opinion is that we probably are not experiencing a housing bubble.

**Resources:**


**The South Coast**

*The South Coast*

- **nominal median single-family home price**
- **real median single-family home price**

**Stephen LeRoy** is a Professor of Economics who has been at UCSB since 1996. His research is primarily focused on finance.

**Bill Watkins** is the Executive Director of UCSB’s Economic Forecast Project.
Are Middle Schools More Effective? 
*The Impact of School Structure on Student Outcomes*

By Kelly Bedard and Chau Do

Beginning in the late 1960s, middle school supporters argued that sixth grade students would do better separated from elementary school children. In particular, they believed placing young adolescents with high school students hinders social development, while placing them with elementary school students slows academic progress.

Despite the positive rhetoric of middle school advocates, several researchers have raised concerns about academic rigor and individual attention in middle schools. Although there is little if any systematic evidence to either validate or refute these concerns, some researchers have pointed to the decline in sixth grade test scores as evidence that middle schools are failing. More convincing is New York City’s recent effort to improve education quality by eliminating most middle schools and replacing them with K-8 grammar schools. (New York Times March 3, 2004).

In a recent article, Chau Do and I present results that support middle school skeptics. We find that districts that adopt the middle school concept suffer a two percent drop in their on-time high school completion rate. For a program whose goal is to help less able students, this is a surprising result! Moreover, since high school dropouts earn lower wages, are more likely to be unemployed, and more often participate in criminal activities, the negative economic implications of lower high school graduation rates may be far-reaching and multifaceted.


Kelly Bedard is an Associate Professor of Economics who has been at UCSB since 2000. Her research interests include labor economics, economics of education, and health economics.

Chau Do is a 2003 graduate of UCSB and is an economist with the Office of the Comptroller of the Currency, Risk Analysis Division, Financial Access and Compliance.

**UNDERGRADUATE PROGRAM FACTS**

- 2420 UCSB students are enrolled in our four undergraduate majors:
  - Business economics
  - Business economics with accounting
  - Economics
  - Economics/Mathematics
- 642 students graduated with an economics degree in the 2004-05 academic year.
- 87% of graduates were employed full-time one year after graduation; 60% plan to pursue post-graduate education at some point (information from a 2001 poll).

**GRADUATE PROGRAM FACTS**

- Five students received PhD degrees and are now employed at Pomona College, Occidental College, John Hopkins University, Cal State Fullerton, and Korea Customs Service.
- 11 students graduated with MA degrees in business economics this year.
- The National Science Foundation awarded $2.8 million for a PhD program in environmental economics at UCSB.
SNYDER AND KAY LECTURES
“Human Altruism,” “Balancing Family, Career, and Financial Issues”
Thank You Distinguished Donors!

The Economics Department is honored to present two annual lectures through the generosity of distinguished donors. One is the Annual Carl Snyder Memorial Lecture, established by the estate of Mrs. Madeleine Raisch in memory of her husband, who was an economist and author. The other is the Herbert C. Kay Undergraduate Lecture. Herbert C. Kay taught in the UCSB Department of Economics in the 1960s and is now a successful private investor in Los Angeles. Many of Professor Kay’s former students cite his inspiration as a major factor in their own successful career development. Professor Kay established the lectures—featuring dynamic business pioneers—to inspire UCSB undergraduates to become the entrepreneurs and leaders of tomorrow. The series affirms the importance of undergraduate education at UCSB.

2005 Carl Snyder Memorial Lecture
This year’s 47th Annual Carl Snyder Memorial Lecture, presented last March, featured Professor Ernst Fehr of the University of Zurich. One of the world’s leading experimental economists, Fehr believes that human concerns such as altruism and fairness play a central role in economic choices, challenging the long-held notion that human economic behavior is exclusively motivated by self-interest. Fehr described his research on “The Nature of Human Altruism” to a capacity audience in the MultiCultural Center. For more information please see http://www.econ.ucsb.edu/seminar/papers/w05/fehr1.pdf.

2005 Herbert C. Kay Undergraduate Lecture
This year’s speaker was Roger McNamee, a prominent Silicon Valley venture capitalist and investor. A standing-room-only crowd of undergraduates, faculty, administrators, and private citizens gathered in Corwin Pavilion to hear McNamee speak about The New Normal, his recently published book that provides a roadmap for balancing family, career, and financial issues in a time of both uncertainty and increased opportunity.

SNYDER AND KAY LECTURES
“Human Altruism,” “Balancing Family, Career, and Financial Issues”
Thank You Distinguished Donors!

There’s no substitute for hard work!
The department recognized eight exceptional undergraduate students at an awards ceremony on June 10, 2005

Sean S. Weld Memorial Award for Academic Promise and Entrepreneurial Spirit
Spencer Kellogg

The Ramstad Award for Academic Excellence and Leadership
Matthew Kirk

J.M Long Foundation Award for Academic Success in Research and/or Internship
Nicholas Sonnenberg
Gina Sverdlov

Jenkins-Stark Award for Continuing Students
Irene Altman

Department chair Peter Kuhn congratulates James Dewey, recipient of the Distinction in the Major Award for Business Economics.
The Department has strong links with other disciplines; students have an opportunity to benefit from formal links with Environmental Studies, The Bren School of Environmental Science and Management, or Engineering through a 5-year Engineering B.S./Economics B.A. program.

Undergraduate students potentially interested in pursuing a Ph.D. may select a special track (joint program with the Department of Mathematics).

The Department has an active research colloquium program, bringing guest speakers to campus each week during the academic year.

The Department offers several annual visiting lecture programs, bringing notable international scholars and business leaders to campus.

The Department serves as editorial office for three prestigious academic journals: Resource and Energy Economics; Labour Economics, and The International Journal of the Economics of Business.

The department has two endowed chair holders (including the Nobel Laureate) who actively teach undergraduate classes (rare at other universities!)

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**Points of Pride**

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**Henley Breaks Away from the Pack**

*UCSB Econ Alum Has Never Let Up*

It wasn’t that long ago that Jeff Henley walked the UCSB campus as an undergraduate economics major. Today, he is Chairman of Oracle Corporation—a position he has held since January 2004—and serves on Oracle’s Executive Management Committee. Did his success happen overnight? Not at all. It has taken years of hard work and commitment.

Henley was Oracle's Chief Financial Officer and an Executive Vice President for 13 years, from March 1991 to July 2004, and has been a member of Oracle's Board of Directors since June 1995. As often is the case with successful business leaders, it was his prior relevant financial experience that paved the way to more demanding responsibilities with a new company.

Prior to joining the firm in 1991, Henley served as Executive Vice President and Chief Financial Officer at Pacific Holding Company, a privately held company with diversified interests in manufacturing and real estate; and as Executive Vice President and Chief Financial Officer at Saga Corporation, a multi-billion dollar food service company. He also served as Director of Finance at Memorex Corporation in its large storage division, and as Controller of International Operations at Fairchild Camera and Instrument Corporation.

Outside of his duties with Oracle, Henley has numerous other interests. For example, he is Chairman of the Mid-Pacific Region Trustees for Boys & Girls Clubs of America and also a member of the Board of Directors of CallWave, Inc.

Best of all, Henley holds a Bachelor’s degree in economics from the University of California at Santa Barbara and later earned a Master of Business Administration degree in Finance from UCLA. That goes to show that sound educational preparation can really make a big difference. In Henley’s case, seeing is believing!

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**CONGRATULATIONS 2005 GRADUATES!**

The Department of Economics congratulates the 2005 PhD graduating class. The five graduates have gone on to promising careers in Economics:

- **Bevin Ashenmiller** worked under Bob Deacon on the incentives to recycle. She joined the faculty of Occidental College this fall.

- **Ekaterina Chernobai** worked under Steve LeRoy on liquidity in real estate markets. She joined the faculty of CSU Fullerton this fall.

- **Taeil Kang** worked under Perry Shapiro on the Korean education system. He returned to the Korea Customs Service.

- **Fernando Lozano** worked under Peter Kuhn on the long-term effects of high school leadership activity. He joined the faculty of Pomona College this fall.

- **Catherine S. Norman** worked under Stephen DeCanio and Bob Deacon studying growth and the environment. She joined the faculty of Johns Hopkins University this fall.
You Can Be a Part of Futures Filled with Hope and Promise!

Donations to the Economics Department Support These Activities:

Graduate Student Support
including entry-level scholarships designed to attract the most promising students to our campus, and support for continuing students writing dissertations.

Promoting Excellence in Undergraduate Education
by funding awards to top-performing undergraduate students, and creating innovative and challenging undergraduate courses.

Supporting Visiting Scholars
Donations support the visits of top-flight speakers and teachers from around the world to UCSB, enriching the intellectual lives of both students and faculty.

Research Support
Donations to the department provide crucial seed money for new research projects that can eventually yield major institutional grants and benefits to society.

Infrastructure
Keeping the department’s instructional space in North Hall up-to-date and attractive is a constant challenge given our huge enrollments and rapid advances in instructional technology. Donor funds play an important role here as well.

You can see for yourself how your contribution will greatly benefit our future economic leaders. There’s no time like now to support this important mission.

To make a contribution to the Department of Economics, mail this form and your tax-deductible donation to:

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Any questions about making a donation can be directed to:
Kimberly Elliott at (805) 893-3569
or email at kimberly@econ.ucsb.edu

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The Equity Premium Puzzle: 20th Anniversary Conference
The Department of Economics and Professor Finn Kydland’s Laboratory for Aggregate Economics and Finance jointly sponsored a conference on October 28-29, to commemorate the 20th anniversary of the publication of the seminal paper, “The Equity Premium: A Puzzle” by Edward Prescott and UCSB Professor Rajnish Mehra. Since its publication this paper has had an enormous impact on both the practice of portfolio management and the research agenda in Finance.

VISITING FACULTY FOR 2005-06

Ken Aoki
Visiting Researcher
Sophia University

Soren Blomquist
Visiting Professor
Uppsala University

Jeff Dubin
Visiting Professor
CalTech

Lanny Ebenstein
Visiting Associate Professor

Bill Fischel
Visiting Researcher
Dartmouth College

Eric Fisher
Visiting Professor
Ohio State University

Norm Habermann
Visiting Associate Professor

Ed Hopkins
Visiting Researcher
Edinburgh University

Peter Kooreman
Visiting Professor
University of Groningen

Robert Lowes
Visiting Associate Professor

Kathryn Marshall
Visiting Assistant Professor
Ohio State University

Charles Nelson
Visiting Researcher
University of Washington

Hosaeng Rhee
Visiting Researcher
Myongji University

Pepa Tomas
Visiting Researcher
University of Alicante

Wenzhi Zhang
Visiting Researcher, Graduate School of the Chinese Academy of Sciences

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