Elite Annual Events Bring Distinguished Names to Campus

The Economics Department is honored to present two annual lectures through the generosity of distinguished donors. One 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. The second lecture 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.

Carl Snyder Memorial Lecture

2009's featured speaker was Robert Shiller, Arthur M. Okun Professor of Economics at the Department of Economics at Yale University. Professor Shiller has written on financial markets, financial innovation, behavioral economics, macroeconomics, real estate, statistical methods, and on public attitudes, opinions, and moral judgments regarding markets and is best known for the Case-Shiller Home Price Indicies (with Karl Case). His lecture focused on his latest book, co-authored with George Akerlof, Animal Spirits: How Human Psychology Drives the Economy and Why It Matters for Global Capitalism.

UCSB Alumnus Returns as Featured Herb Kay Lecturer

The Department of Economics was proud to have one of our alumni, Paul Sams, as this year’s featured speaker. A crowded Campbell Hall eagerly sat and listened as a former Economics student spoke about how passion and determination guided him in his success. Mr. Sams ’92 is the chief operating officer for Blizzard Entertainment, Inc and is responsible for the entirety of the company’s global business operations.

This includes areas as diverse as customer support, public relations, finance, human resources, marketing, business development, and licensing, among others. Sams joined Blizzard Entertainment after two and a half years at educational software company Davidson & Associates, Inc. One of his largest projects was to help orchestrate Davidson’s acquisition of Silicon & Synapse, which would later become Blizzard Entertainment. After working closely with Silicon & Synapse during the acquisition, Sams officially transferred over in 1996, becoming the director of business development for the rapidly expanding company. Since then, he has steadily taken on additional responsibilities and has helped guide Blizzard Entertainment’s growth into a world-renowned developer and publisher of entertainment software with an unbroken string of #1-selling releases.
Chairs Message

Another Exciting Year!

by Charles Kolstad

The last message I wrote was in the Fall of 2008—much has happened since then! We have a new faculty member, new accomplishments, for the department, and some changes. One is the new webpage—check it out and let me know how you like it: www.econ.ucsb.edu.

We have one new junior faculty member who joined us in the fall of 2009: Paulina Oliva. Paulina received her PhD from UC Berkeley and works in the areas of environmental economics, we very much welcome her join us!

Speaking of environmental economics, I am pleased to say that rankings that appeared in January have consolidated our two Masters degrees into one, and interested alumni. Another recommendation concerned faculty hiring strategies, which we have already implemented. Another recommendation concerned improving the undergraduate program by developing a career counseling center, which would have the additional role or reaching out to alumni in business, providing connections between those majors interested in business and interested alumni. Another recommendation concerned the Masters program. We have already implement ed part of that recommendation by consolidating our two Masters degrees into one degree (the Master of Arts in Economics). It was an excellent outside opinion with excellent and implementable recommendations.

Although many economics-related events and workshops take place throughout the year, we have also hosted many external speakers. One of these was Mark Bates, who spoke on the importance of research in helping to reduce emissions from vehicles. Bates shared his views on the role of research in reducing emissions, and how exciting this work can be for students and researchers alike.

The research productivity of our faculty is not the only thing we care about. The quality of our undergraduate teaching program is also very important. We are particularly proud of our accounting program, which continues to be highly successful and visible.

Uncovering Cheating with Environmental Regulations

by Paulina Oliva

Cheating is a known problem with vehicle emission testing programs in Mexico City. However, its magnitude is difficult to quantize, making it hard to evaluate the program’s effectiveness. In her work, UCSB economist Paulina Oliva uses statistical evidence to document both the presence and prevalence of “donor car” cheating in emission testing centers.

Donor car cheating consists of using a low-emitting vehicle to take the emission test instead of the cheat. This type of cheating requires bribing the technician, who finds a low-emitting vehicle among the ongoing testers and holds it on the testing ramp for a second emission reading. The technician then matches the information on the cheating vehicle registration card to the second set of emissions produced by the donor car. Measuring emissions from another vehicle is necessary, since emissions cannot be typed into the testing computers. Although people may cheat in an array of ways, donor car use is an appealing cheating strategy since it does not require tampering with the cheating vehicle or the measuring equipment.

Despite the lack of physical evidence in vehicles or equipment, donor cars can be detected statistically by analyzing the sequence of emission readings. Donor car cheating results in repeated occurrences of similar consecutive emission readings from vehicles reported to have different vehicle plate numbers and different vehicle characteristics.

To test for cheating, she creates a counterfactual scenario where cheating is not an issue by randomizing the order of readings. In the absence of cheating, it is reasonable to assume that the actual order in which readings are recorded should produce roughly the same number of similar consecutive readings as any other random order. Therefore, evidence of cheating can be detected by comparing the number of occurrences of such sequences in the original data to that on the counterfactual scenario. When performing this test for each emission testing center, she finds that cheating is present in all emission testing centers. She uses an alternative testing methodology to verify the results of the first test and to determine the percentage of cheaters. This second methodology exploits additional information present in the vehicles (model, make, year, etc.) to identify abnormally close consecutive readings. This test yields results similar to what the first testing strategy produced: 76 out of 80 centers show evidence of cheating. In addition, it provides an estimate for the percentage of cheaters; at least 20 percent of the car fleet cheats on the smog check. These are the first estimates of the prevalence of cheating in Mexico City and an important first step towards analyzing the effectiveness of the program.
How many salmon will return to Bristol Bay, Alaska next year?

Ask an Economist!

by Bob Deacon

Just July economists Chris Costello, Olivier Deschenes, Matt Kotchen and Bob Deacon and economics graduate student Corbett Grainger traveled to Bristol Bay, a remote area of Alaska, at the request of renowned fisheries biologist Dr. Ray Hilborn of the University of Washington. The purpose of the trip was to see if standard economic forecasting methods could be applied to the purely biological problem of predicting the number of sockeye salmon that will return to rivers in this area. The Bristol Bay drainage is home to the world’s largest sockeye salmon run, with over 40 million fish returning in a ‘good’ year, but annual numbers can fluctuate wildly. To catch and process the returning salmon, firms engaged in this fishery must decide far in advance how much labor and equipment they will need to employ during the season. Making such decisions with inaccurate forecasts could result in reduced profits, either due to excessive payments for unneeded labor and capital if the run turns out to be small, or loss in revenue due to inadequate capacity to harvest and process if the run is unexpectedly large. To make the exercise meaningful for future management, the economics team based its forecast entirely on data that were available 6 months before the 2009 run began.

Economists normally forecast economic activity by identifying factors that theory suggests should drive the outcome of interest, and then estimating the strengths of these driving relationships statistically, using data from prior periods. Unknown or unobserved factors can be important determinants, of course, and methods for incorporating the influence of these variables from historical patterns in the data are also part of the process. Because sockeye salmon most often return five years after being spawned by the parent population, it is natural to include the size of the salmon run that returned to spawning streams five years ago as a determinant. In addition, the fact that some members of a given cohort often return a year or two early gives additional information on the size of the run that will develop in any year. Purely environmental factors, such as sea temperatures and indicators of food abundance, also play a role. Fishery managers and scientists incorporate many of the same factors in their own forecasts, but are less systematic about the process. While economic forecasters sometimes are the butt of jokes on late night television, their methods are highly refined and data-intensive.

So, how did the economists’ forecast stack up against the actual run, and against forecasts produced by others? The economic method yielded an estimate of 41.4 million fish for the summer of 2009, and the actual number returning equaled 40.4 million. For comparison, forecasts produced by the Alaska Department of Fish and Game and by academic fisheries researchers were far lower, in the 33-35 million range. Only time will tell if the remarkably accurate 2009 ‘economic salmon forecast’ was due to luck or to a superior methodology. The economic team has already produced a forecast for the 2010 run and looks forward to traveling north again next summer to see how well the economic approach predicts the behavior of salmon.

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UCSB Professor Emeritus Walter Mead and his wife, Thelma, have given a $1 million gift to establish the Walter T. Mead Endowed Chair in Economics. Prior to his retirement in 1991, Professor Mead had a distinguished 34-year long career at UC Santa Barbara as a natural resource economist. In 2006 Walter and Thelma established the Mead Fellowship program at UCSB, which provides support for promising entering PhD students.

In January 2009, the Department of Economics sponsored a symposium to honor Walter Mead and his career at UCSB. Former graduate students traveled from around the world to honor both him and his family. Current Mead Fellows and faculty members listened as former graduate students remembered Walter as a graduate advisor, and conveyed the impact that he and his family had on their graduate school and professional life.

To further honor Walter, UCSB alumni Drs. Sue and Gary Wilcox have given a $50,000 challenge grant to establish the Walter J. Mead Research Assistant Endowment. The Endowment will provide graduate student funding and support for the Walter J. Mead Endowed Chair Holder. The goal is to create a $100,000 endowment. If you would like to honor Walter and support the economics department, please contact our development professionals Ann Hagan at 805-893-2774 or at ann.hagan@ia.ucsb.edu or Michael Miller at 805-893-3922 or at michael.miller@ia.ucsb.edu.
From Student to TA
An inside look at the American Economic Association Summer Training Program (AEASTP)
By Cristino Tello-Trillo

Due to my parents’ jobs, I studied in South America and obtained a Bachelor of Social Science degree in Economics from the Catholic University of Peru. I graduated with honors and first of my class. After graduating I started working in Lima as a research assistant. Of course I wanted to pursue graduate studies, but was not sure if I should pursue a Master’s degree first or go directly to the Ph.D. In fact I had many questions in my mind. Will I have what it takes to dedicate 5 – or more years of my life to study a Ph.D.? Am I well prepared to succeed in a graduate program in the US? The American Economic Association Summer Training Program (AEASTP) seemed to be exactly what I needed. A way to get answers to my questions, an opportunity to improve my mathematical and economic skills, to meet with top US professors, and to interact with students coming from different U.S. universities. For me it was a lifetime opportunity.

I was very fortunate! For the summer of 2008, I was awarded a scholarship to attend the AEASTP at UCSB. The program covered eight weeks of highly demanding graduate-level courses in economic theory and applications in addition to a final research project. I enjoyed applying my mathematical and economic knowledge in a challenging academic environment and having rigorous discussions with motivated economic scholars. I also enjoyed learning about cutting-edge research from professors and visiting lecturers, and became particularly interested in using game theoretical models to deal with multilateral and bilateral trade negotiations.

Besides providing a valuable research and academic experience, the program showed me that it is very important to promote academic discussion between students from different cultural, social and educational backgrounds. This will allow for a re-evaluation of your own perspectives and improve your arguments when debating with your peers.

The entire faculty was very supportive and approachable. I always visited and talked to them about the Ph.D. programs and my long-term career plans. They are willing to help, especially during the application process for graduate school. I shared with them my own tips on how to get organized, when to start, and what to do to apply for graduate studies.

In Fall 2009 I started my Ph.D. studies in Economics at Yale University with full funding from the University. I am proudly happy to join such a renowned university, and very grateful to the AEASTP for providing me the motivation, self-confidence, knowledge, preparation and support I needed to continue the journey to higher education. Thank you so much AEASTP.

Health Care Reform
By Ted Frech

As this is being written, President Obama has just signed into law a major health care reform bill. Unfortunately, the quality of the public debate on the issue has been disappointing. It has largely ignored the results of years of intensive and ongoing health economics research and analysis. The demonization of nonprice rationing is an important example. (A personal note: one of my first assignments as government economist was to analyze the national health insurance reforms proposed by the Nixon Administration.)

When health care is subsidized by insurance, the price to the consumer is reduced—sometimes all the way to zero. This leads to excessive demand for health care through what is called moral hazard. It would be extremely wasteful to provide all the health care that is demanded. There are only two practical ways to moderate the waste: The first is using copayments, such as deductibles and coinsurance; relying on a degree of price rationing to moderate demand and allocate care. The second is nonprice rationing of care. When nonprice rationing is used, the plan or the government does not supply all the care that is demanded at the subsidized price. This can be accomplished by managed care systems. Unmanaged care systems are set very low. Few physicians take the waste or is it accomplished by poor access and by waiting time? The latter is especially likely to be inefficient, but the waste doesn’t appear in any budget.

Price controls can exacerbate inefficient rationing. The price of U.S. health care is higher than in other countries, mostly because U.S. physicians, nurses and technicians are paid better. This has led to the idea of forcing lower prices. Substantially reducing prices leads to less care being supplied and more demanded, exacerbating the nonprice rationing problem. The result can be a sort of Potemkin benefit. On paper, the insurance looks good and reported budgetary costs are low, but nonprice rationing is so severe and inefficient that the coverage is not useful and not truly low.
STUDENTS EXCEL
News from the Ph.D. Program

Grant Jacobsen
was awarded a coveted ‘Graduate Opportunity Fellowship’ by the central UCSB Graduate Division. This award will relieve him of teaching assistant duties through the 2009-10 academic year, allowing him to focus on his dissertation research in the areas of Environmental & Natural Resource Economics and Labor Economics. Grant is working on research that will improve understanding of consumer-decisions related to energy and the environment.

Sara Adler
was awarded the new central UCSB Graduate Division, Harold & Hester Schoen Endowed Fellowship as part of her 5-Year financial support package.

Daniel Argyle
was awarded a departmental Andron fellowship as part of his 5-Year financial support package.

Zachary Bethune
was awarded a departmental Andron fellowship as part of his 5-Year financial support package.

Charles De Los Reyes
was awarded a departmental Andron fellowship as part of his 5-Year financial support package. He was also awarded in support of his first year of studies at UCSB a coveted UC Diversity Initiative for Graduate Study in the Social Sciences (DIGSS) fellowship.

Judith Delaney
was awarded a departmental Thomashien fellowship as part of her 5-Year financial support package.

Stefanie Fischer
was awarded a departmental Mead Fellowship in support of her first year of graduate studies here at UCSB.

Gregory Leo
was awarded a central UCSB Graduate Division ‘Regents Special Fellowship’ and a departmental Andron fellowship as part of his 5-Year financial support package.

Ruth Morales
was awarded a departmental Andron fellowship as part of her 5-Year financial support package. She was also awarded in support of her first year of studies at UCSB a coveted UC Diversity Initiative for Graduate Study in the Social Sciences (DIGSSS) fellowship.

Ty Robbins
was awarded a departmental Andron fellowship as part of his 5-Year financial support package.

The Department of Economics Congratulates the 2009 Ph.D. Graduating Class

Belinda Acuña studied under Jati Sengupta in the areas of Development and Labor Economics. She has accepted a position at the FDA - Center for Food Safety & Applied Nutrition as a Staff Fellow.

Elizabeth (Libby) Ashley studied under Charlie Kolstad in the field of Environmental & Natural Resources Economics. She has joined the Food and Drug Administration (FDA) as a Staff Fellow.

Cindy Benelli studied under Ion Sonstelle in the area of Labor Economics. She is now working as a full-time Lecturer in the Department of Economics here at UC Santa Barbara.

Kang Hua Cao worked under Javier Birchennall in the areas of Econometrics and Mathematical Economics. He has accepted a position as a Staff Research Associate in the Institute for Social, Behavioral and Economic Research (ISBER) at UC Santa Barbara.

Benjamin Hansen worked under both Peter Kuhn and Douglas Steigerwald in the fields of Labor Economics and Econometrics. He has accepted a position with MPAQ International, LLC as a Research Associate.

Rosemarie Lavaty studied under Peter Kuhn in the area of Labor Economics. She has been hired as a Staff Fellow with the Food and Drug Administration (FDA)

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Hani Mansour studied under Peter Kuhn in the area of Labor Economics. He has accepted a position as an Assistant Professor at the University of Colorado – Denver.

Ishita Nandi worked under Jati Sengupta and Javier Birchennall in the field of Labor Economics. She has accepted a position at California State University, Channel Islands as a full-time lecturer.

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A recent article co-authored by three Dutch economists (Peter Kooiman, Adrian Soetevent, and Arie Kapteyn), UCSB economist Peter Kuhn sheds light on these important economic questions by examining the consumption behavior of Dutch households who won or nearly won a lottery prize. According to Nobel Laureate Milton Friedman’s influential Permanent Income Hypothesis, households that receive unexpected temporary income (such as, for example, a federal stimulus check) will rationally save the lion’s share of that extra income. This made Friedman highly skeptical of the government’s ability to stimulate the economy, whether by short-term increases in spending or by temporary tax cuts. A competing view is that, especially in recessions, cash-strapped households will spend most of the unexpected income, making government stimulus programs more effective. In addition, if Thorstein Veblen’s famous theory of conspicuous consumption is correct, increased spending by ‘stimulated’ households might directly cause increased spending by their neighbors, who feel compelled to “keep up with the Joneses” in a competition for social status.

In a recent article co-authored with three Dutch economists (Peter Kooiman, Adrian Soetevent, and Arie Kapteyn), UCSB economist Peter Kuhn sheds light on these important economic questions by examining the consumption behavior of Dutch households who have either won a lottery prize, or live close to lottery prize winners. Every week, the Dutch Postcode Lottery allocates a prize to participants in a randomly chosen postcode (containing 19 households on average). About one third of the Dutch population participates in the lottery. A typical participant won about 8 months worth of income if his/her postcode was randomly selected to win. In addition, every week, one winning household is randomly awarded a new BMW. Since the selection of winning postcodes is a random, unexpected, one-time event (and since the winning codes are publicly announced on Dutch Television and elsewhere), this lottery provides a unique opportunity to test a number of hypotheses concerning households’ consumption behavior, including “Veblen effects” and the Permanent Income Hypothesis.

From their survey of 2000 Dutch households living in winning and nearby postcodes conducted between 2003 and 2006, the authors, first of all, found considerable support for Friedman’s Permanent Income Hypothesis: in almost all expenditure categories, winning households’ expenditures were unchanged after they won the lottery. Dutch households also closely resembled Friedman’s ‘rational economic man’ in two other ways: first, as predicted by basic economic theory, the vast majority of BMW winners no longer owned a BMW six months after winning one. Households converted these winnings in kind either into savings or into the consumption items they really wanted, not the ones they were given. Second, the one expenditure category on which winning households increased their spending was durables, including cars. Since durables purchases are really a form of saving, this is also consistent with Friedman’s Permanent Income Hypothesis.

Despite all this evidence of economic rationality among Dutch households (perhaps American consumers are not so prudent?), the authors also found highly suggestive evidence of one aspect of economic behavior that is inconsistent with that model: Veblen effects. In particular, Dutch households who did not hold a lottery ticket but live (literally) next door to lottery winners were significantly more likely to buy a new car after the lottery than households who live far away from lottery winners! While it is possible that these strong effects are driven in part by purely rational factors (for example, family members who live in adjacent homes may share lottery winnings), the most likely explanation appears to be Veblen effects. This seems especially likely since, unlike most other aspects of household consumption, the car a household drives is highly, and repeatedly, visible to its neighbors.

In sum, according to the authors’ results from the Dutch postcode lottery, significant infusions of unexpected temporary income, including not limited to government stimulus spending, are likely to have direct effects on only one type of household spending—the purchase of durables. At the same time, however, stimulus spending may also raise spending indirectly via Veblen effects, which appear to operate only on car purchases. Interestingly, car purchases happen to be the focus of the Obama Administration’s recent “Cash for Clunkers” stimulus program and its subsidy for first-time home purchases.