

THE LOWE DOWN

LOWE INSTITUTE OF POLITICAL ECONOMY

A bi-annual newsletter summarizing the programs and activities of the Lowe Institute.

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A more effective way to train workers

by Anna Eames, CMC '13

Professor Serkan Ozbeklik's past research has covered topics from abortion to Teach for America, but his most recent work for the Lowe Institute explored the effectiveness of job training programs. He and his co-editor used data from Job Corps, which provides vocational and educational training to disadvantaged youths entering the workforce. They were interested in using new econometric techniques to examine the distributional impact of Job Corps training on future earnings.

Their hypothesis was that they would find a heterogeneous impact over the distribution, and indeed their research showed that participants who had higher wages to begin with got more out of the program than people who started with lower wages.

"We were expecting to find a heterogeneous impact—different impacts for people with different wages—and that's what we found in the data," said Ozbeklik.

Until recently, researchers have only looked at the average impact of job training programs on all participants, but Ozbeklik pointed out that such an approach does not tell the whole story. To understand how any public policy affects different types of people, a researcher must look at the effect of the program throughout the distribution—in this case, the earnings distribution—rather



than just at the mean impact.

The next step was to conduct subgroup analysis, looking at the success of program participants based on race, gender, education, age, and other observable factors. Even after controlling for "observable characteristics," the data still showed a heterogeneous impact by the job training program. The variance in wages *within* the subgroups was even greater than the variance *between* subgroups. For example, wages differ more within the white population than they differ between whites and African Americans.

Ozbeklik thought that "unobservable characteristics" such as self-discipline and patience

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Message from the director



Dear students, faculty, and Board members,

We have recently wrapped up another exciting year at the Lowe Institute. I would like to briefly update everyone on the recent events and student achievements over the 2011-12 academic year.

I would like to congratulate the members of the 2012 graduating class at the Claremont Colleges. I would like to single out some seniors that have worked many hours at the Lowe Institute. Chase Gray, the editor of the Lowe Down this year, has worked as a writer on the student run publication for many years. Chase will be working for Deloitte in New York City. Aisling Scott has worked extensively with Professor Chaudhary at Scripps College on a variety of research projects. Aisling will be attending a PHD program in economics and business at the Haas School at the University of California at Berkeley. Jane Brittingham is one of our senior leaders who has worked extensively on constructing and forecasting various economic indicators for the Inland Empire. Jane has recently accepted a position at the Federal Reserve Board of Governors in Washington D.C. Peter Meyer has been a jack of all trades and has worked at the Lowe Institute for several years. Peter will be returning to his home state of Hawaii to work for a bank with the same name.



The Lowe Institute sponsored the Third Annual Southern California Conference in Applied Microeconomics. The conference was attended by more than 40 academic economists in the Southern California region. Michael Greenstone, an economics professor at MIT, gave the keynote address on “*Can Adaptation Save Us from Climate Change?*” The talk was well attended by faculty and students. We also held the Spring Senior Thesis Conference on May 1. The event was organized by Professor Janet Smith. Many underclassmen attended the conference to get some ideas about writing their senior thesis in the future.

We are also excited about our Coachella Valley Forecast Conference. The Conference will be held May 15th at the Miramonte Resort in Indian Wells. The Lowe Institute will team up again with the UCLA Anderson Business School to discuss future economic activity in the United States, California, and the Coachella Valley with government and business leaders in the area. Several Lowe Institute research assistants assisted Professor Keil in constructing gross domestic product estimates for the Coachella Valley. This is the first time that we are aware that GDP estimates have been constructed for this region.

We are excited about our upcoming summer program. We will hire approximately ten students this summer who will work as research assistant at the Lowe Institute. We will again provide basic training for students to learn the basic techniques of forecasting economic and financial data using econometric software packages. The students will hone their skills working on economic data for the Inland Empire.

I hope that everyone has a fun and productive summer!

Regards,
Marc D. Weidenmier

Interview with Oana Hirakawa

by Shree Pandya, CMC '14

Last fall, CMC welcomed a new assistant professor, Oana Hirakawa. CMC students have good reason to be excited for her presence, as she adds specializations in entrepreneurship and international trade to the Robert Day School of Economics and Finance. This semester, she can be found on campus teaching two sections of Intermediate Microeconomics.

Originally from Romania, Hirakawa has been a resident of Southern California for the past 12 years. “I’m a local,” she joked. After receiving her undergraduate degree in Engineering and Applied Science from the California Institute of Technology, Hirakawa went on her to pursue her M.A. and PhD in Economics at the University of California, San Diego.

“We had a rich data set because it allowed us to track workers through time.”

Hirakawa enjoyed her time as a teaching assistant while earning her doctorate. “Many times, that was the best part of my day,” she recalled. Based on her experiences teaching at UCSD, Hirakawa discovered that she wanted to be at a place where she could teach small classes. “While I enjoyed talking to my students in office hours, I was frustrated by the class sizes.”

Her time here has “been perfect so far,” Hirakawa says. “I think it’s probably a pretty general experience for new professors to spend all of their time on teaching their first semester – it’s your first time teaching a certain class, and it’s a new environment. That’s my situation right now, but I enjoy it.”

Prior to her arrival at CMC, Hirakawa presented at the 2011 Southern California Conference in Applied Microeconomics, sponsored by the Lowe Institute. Her paper, titled “The Success of Entrepreneurial Networks: Evidence from Brazil,” compared how networks among early employees in new firms correlated with firm success.

“We had a rich data set because it allowed us to track workers through time,” Hirakawa said. “Looking to see if people worked together previously, we had a measure for each new firm to indicate how ‘tightly fit’ they were. We used this to predict firm survival and growth in the first six years.” Going into the study, there were “several stories” to explain the success of firms. One idea was that “reaching out to someone outside your immediate circle predicts greater success because it indicates that your idea is good enough to incur higher search costs.” Those willing to look outside their immediate networks have a larger talent pool to choose from and a greater chance of finding employees best matched to the firm. “This line of thought was in many theoretical papers,” explained Hirakawa.

The idea did not pan out in the study results. To Hirakawa, the result was surprising and statistically strong. “Firms in which initial employees had worked together do better in terms of survival. They’re also larger in birth, and the size persists for several years,” she said. “For survival, we found that working with someone you know makes you more willing to make invest in the idea. This is important when opening a firm as entrepreneurs have to put in some of their money – they’re much more confident when working with people they know.”

Hirakawa finds her ability to pursue joint interests in entrepreneurship and international trade at CMC extremely gratifying. “I got very lucky,” she grinned. For students interested in taking classes in entrepreneurship, she will be teaching a course on the subject next spring. Until then, you can find her at her office in Bauer North, in the classroom teaching Intermediate Microeconomics, or enjoying the beautiful California weather.

The Lowe hosts successful SCCAM conference

by Shree Pandya, CMC '14

On April 13th, CMC hosted the third annual Southern California Conference in Applied Microeconomics (SCCAM). Professor Heather Antecol spearheaded the organization of the conference, and Kelly Lockhart Spetnagel, Program Coordinator for the Lowe Institute, coordinated the logistics. The Lowe hosted the conference alongside the Berger Institute for Work, Family, and Children and the Robert Day School of Economics and Finance.

The conference began with an unexpected bout of terrible weather. Luckily, the economists present were a hardy bunch. They cheerfully attended the continental breakfast in Harvey Mudd's Galileo Hall, followed by a session on public economics with Antecol and one on environmental economics chaired by J.R. DeShazo of UCLA.

In the first session on public economics, Dr. Jan Brueckner of UC-Irvine presented on "Beaches, Sunshine, and Public Sector

Pay: Theory and Evidence on Amenities and Rent Extraction by Government Workers." She was followed by Dr. Josh Tasoff of CGU, who focused on the intersection between psychology and economics in his presentation on "Over-optimism and Nudges: A Mail-In Rebate Experiment."

Dr. Manisha Shah, also of UC-Irvine, delivered the first presentation on environmental economics. Shah, a Faculty Research Fellow at the National Bureau of Economic Research, addressed "Risk-Taking Behavior in the Wake of Natural Disasters." Dr. Paulina Oliva of UC-Santa Barbara, followed with a presentation on "The Effect of Pollution on Labor Supply: Evidence from a Natural Experiment in Mexico City."

At noon, the conference-goers headed to lunch in CMC's Founders Room, where they were joined by various students, staff, and faculty of the Claremont Colleges. Dr. Michael

Greenstone, the 3M Professor of Environmental Economics at MIT, presented the lunch keynote. He addressed the question, "Can Adaptation Save Us from Climate Change?" In his concluding remarks, he urged the audience to remember that climate change will make a large impact over the next century and that mitigation will continue to be challenging. Adaptation, he argued, will be a big part of the solution to climate change, but it is a costly course of action with an uneven global impact.

Following lunch, a larger group of conference participants braved the downpour of rain and headed back to



Galileo Hall to attend presentations on health, development, and labor economics. These sessions were chaired by Mireille Jacobson of RAND, Kitt Carpenter of UC-Irvine, and Kelly Bedard of UC-Santa Barbara, respectively.

The third session on health economics was kicked off by Dr. Abby Alpert, an associate economist at the RAND Corporation. Her current research focuses on anticipatory responses to Medicare Part D, a federal program that subsidizes the cost of prescription drugs for Medicare beneficiaries in the United States. She is also studying the effects of Medicaid reimbursement rules on generic drug price competition. Her presentation was on “The Anticipatory Effects of Medicare Part D on Drug Utilization.”

CMC’s own Dr. Eric Helland then spoke about “The Causal Effects of Fetal Exposure on Height: Evidence from State Prohibition Laws,” a paper he co-authored with Dr. Mary Evans, also of CMC, and Dr. Jonathan Klick of the University of Pennsylvania. The authors used a dataset of U.S. World War II enlistees to discover whether individuals displayed significant differences in height if conceived before or after the implementation of state-

level alcohol prohibition. Height is the primary indicator used by doctors to diagnose fetal alcohol syndrome. Their results indicated that individuals conceived just after prohibition went into effect were taller than those born before and that this result was statistically significant.

The session on development economics began with a presentation from Pomona’s Dr. Tahir Andrabi, who detailed his paper “Are Public Schools ‘Bad’? Test Scores and Civic Values in Public and Private Schools.” Dr. Andrabi’s presentation focused on Pakistani public and private schools in particular. Dr. Prashant Baradwaj of UC-San Diego then spoke on “The Gender Gap in Mathematics: Evidence and Analysis from Middle/Low Income Countries.”

The final session on labor economics started with Dr. Laura Gee, also of UC-San Diego, who presented “Getting a Job from a Friend: Weak Ties on Facebook’s Social Network.” She was followed by Dr. Michael Hilmer, of San Diego State University, who addressed “Fame and the Fortune of Academic Economists: How the Market Rewards Influential Research in Economics.” It was a fitting final presentation for the day.

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might be more important than race and gender. To explain that conclusion, he used the econometric methodology of quantile treatment estimation.

In looking for a research topic, Ozbeklik wanted to apply new econometric techniques, and the data set he obtained for this research provided the necessary detail on Job Corps participants and their earnings over time. “The first set of results was very promising, and we kept continuing, and at the end I think it turned out to be a very good paper,” he said.

Ozbeklik also cited a separate paper in which he looked at the effect of non-cognitive skills on future wages. That research found test scores in non-cognitive skills such as self-esteem and patience are much more important in determining future wages of low-skilled workers than are test scores related to cognitive skills.

The implication for public policy is job training programs such as Job Corps, as they are currently structured, do not work as well for people who enter the program with low earnings and skills. Emphasizing non-cognitive skills would allow such programs to have a greater impact on participants who start on the lower end of the earnings distribution.

According to Ozbeklik, cognitive skills are set around the age of six or seven, whereas non-cognitive skills can be learned later in life. Therefore, courses that focus on improving emotional intelligence, or even skills such as how to dress for a job, might have a bigger impact on those with lower incomes.

“Our results suggest that...restructuring the program so that it has more, or just equal, emphasis on non-cognitive skills as well as educational and vocational training...might get a huge return,” said Ozbeklik.

Lessons for the Eurozone from the history of fiscal union: Michael Bordo at the Athenaeum

by Chase Gray, CMC '12

Michael Bordo returned to the Athenaeum on March 5, 36 years after his first visit, to give a talk entitled “Whither the Euro: Some Reflections from the History of Monetary and Fiscal Unions.” A professor of economics at Rutgers University, Bordo is also a research associate at the National Bureau of Economic Research, associate editor of the *International Journal of Central Banking*, and a member of the Shadow Open Market Committee. He studied under Milton Friedman at the University of Chicago, where he earned his Ph.D. in 1972.

Bordo’s speech was timely given the recent structural default of Greece and the potential for contagion effects in Portugal, Spain, Ireland, Italy, and elsewhere. He opened with a discussion of optimum currency area theory, which dictates that a monetary union must also be a fiscal union if it does not have full labor mobility. The eurozone does not have complete labor mobility but it also lacks a fiscal union to make transfers between countries. The Maastricht Treaty established the eurozone as a monetary union of what are now 17 European nations.

The eurozone should take lessons from previous fiscal and monetary unions, Bordo argues, to ensure the European integration project can continue. He surveyed the history of fiscal unions in four countries: the United States, Canada, Argentina, and Brazil, to establish best practice and suggest a way forward for the eurozone.

The United States in the 1780s was a lot like the eurozone today in the extent of its monetary and fiscal integration. The federal government could not raise taxes and relied on transfers from state governments. The system failed and the government, along with many of the states, defaulted on domestic debt and debt owed to France for loans made during the Revolutionary War. Alexander Hamilton, the first secretary of the treasury, came up with a package of reforms in 1790 that included four key elements: consolidate state and federal debt, secure sufficient taxes to service debt, create a sinking fund, and establish the first Bank of the United States.



Another crucial development occurred in 1837 following a global financial crisis. Eight states declared insolvency after five years of depression but were refused bailouts by the federal government. The short-term impact hurt the states and the central government as both were cut off from British funding, the key source of capital at the time. It took many years for them to regain access to capital markets.

Virtually all states adopted balanced budget amendments in response to the 1830s crisis. In all subsequent instances of state bankruptcy the federal government stuck to the policy it enacted in 1837. The “no bailout” clause worked.

Canada’s federal government, established in 1867 by the British North America Act, had more power than the US government from the outset. Ottawa issued Dominion of Canada bonds serviced by a federal taxing authority. Canada had a fiscal union in place from the outset.

During the Great Depression the country set up a fiscal federal

transfer mechanism and mandated equalization payments that transferred resources from more successful provinces to less successful ones. Canada, unlike the United States, does not have an explicit “no bailout” clause. Bordo suggests that if Ontario got into trouble, “too big to fail” would be exercised immediately.

A number of provinces had excess debt in the 1980s and 1990s that led to rising risk premia and ratings downgrades. In the 1990s the provinces and federal government undertook major fiscal retrenchment. Canada is now the most fiscally prudent member of the G-7.

Argentina has a less successful history of fiscal union. Bordo noted “the fiscal history of Argentina is really great because every bad thing you can do has been done there. They adopted the Hamilton package when they set up shop in 1810, but within ten years they looted their sinking fund, spent their gold reserves, and defaulted on their debt to the British.

The Argentine provinces borrowed excessively from provincial banks in the 1980s. The banks discounted the debt at the central bank, which then printed money, leading to hyperinflation. The Convertibility Law of 1991 solved the hyperinflation problem by creating a currency board and tying the Argentine peso to the dollar. The government was unsuccessful at solving its federal fiscal deal, however. The federal government could not control

provincial spending. It defaulted in 2002 after absorbing growing provincial debts.

Brazil and Argentina faced many of the same issues through the 1980s and 1990s. The states, municipalities, and federal district took on too much debt and the federal government bailed them out. Increased federal debt caused a speculative attack on the Brazilian real and a national debt crisis in 2000. The government passed a fiscal responsibility law that year that increased federal control. It has worked thus far and, according to Bordo, “Brazil may be on the road to graduating to advanced country status.”

There are three crucial lessons for the eurozone from past fiscal unions. First, a central tax authority is needed to service national debt. The history of fiscal unions makes a strong case for a Eurobond but it must be serviced by taxes collected by some pan-European fiscal authority with far greater power than the EFSM or EFSF. Second, the union must have a credible “no bailout” clause. Third, the monetary union must have a viable fiscal regime. A successful monetary union needs a successful fiscal union. Europe got it backwards. Whether any of these developments will occur in the eurozone depends on the political willingness of the member states to commit to the notion of a common European political entity and subsume substantial sovereignty to it.

March Madness at the Lowe

by Chase Gray, CMC '12

The Lowe Institute teamed up with Claremont Sports Connection and the College Programming Board to hold the 3rd Annual March Madness 5C Bracket Pool. Students were encouraged to fill out an NCAA tournament bracket on Yahoo Sports using an econometric model of their own creation, although employing a model was not required.

Harvey Mudd swept the top three spots in this year's pool. Isabel Frances-Bush (HMC '12) took home the \$150 first place prize. Scott Ogilvie (HMC '12) came in second and Eva Gao (HMC '14) finished third. Lorcan McGonigle (POM '13) won the award for best econometric model based on point spreads. He used a random forest model that included variables for

points scored per game, points allowed per game, and seed placement.

107 people entered the competition and 52 correctly picked Kentucky to win the tournament. Ohio State and North Carolina were also widely chosen to take home the trophy.

Mike Greim (PZ '13) organized this year's event for the Lowe Institute. He found the event successful at encouraging students to apply skills learned in econometrics courses to real world events. In addition to continuing the March Madness bracket pool next year, the Lowe hopes to expand the competition to other sporting events.

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Calendar of Events

3 • 1 • 12 Winter Meeting Lowe Institute Board of Governors - California Club, Los Angeles, noon

3 • 5 • 12 Lowe Athenaeum Speaker Series - Michael Bordo - MMC Athenaeum, CMC, noon

4 • 13 • 12 Southern California Conference in Applied Microeconomics - Harvey Mudd College, Claremont, 8:00 AM

4 • 18 • 12 Spring Meeting Lowe Institute Board of Governors - California Club, Los Angeles, 5:30 PM

5 • 1 • 12 Spring Lowe Senior Thesis Writer's Conference - MMC Athenaeum, CMC 5:30 PM

5 • 15 • 12 CMC-UCLA Coachella Valley Forecast Conference - Miramonte Resort, Indian Wells, CA 8:00 AM



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