Report on

PhD CONFERENCE IN ECONOMICS AND BUSINESS
NOVEMBER 3-5, 1993
PERTH

by

Kenneth W Clements

Economic Research Centre
Department of Economics
University of Western Australia
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The objective of the PhD Conference Series is to help with the training of promising, young doctoral students in economics and business by giving them the opportunity to gain feedback on and exposure for their research. In addition, the conference enables the students to meet with their peers and share common problems encountered in their research.

The sixth conference in the series was held in November at the University of Western Australia and was jointly organised by the Economic Research Centre, the Research Centre in Accounting and Finance at UWA and the Centre for Economic Policy Research at the Australian National University. The Conference involved 25 PhD students from all of the major universities and also attracted some of Australia’s most prominent economists, who acted as discussants of the papers. An Innovation at this year’s Conference was the several sessions on accounting and finance, which seemed to nicely complement the economics sessions.

The Conference had the benefit of lectures from three well-known researchers. Professor Helen Hughes of the ANU presented the Invited Lecture in Development Economics on “The Lessons of Development”. Professor Robert Mundell of Columbia University presented “Regionalism vs Multilateralism in the World Economy” as the Invited Lecture in International Economics, which attracted considerable media attention (see Appendix 4). The after-dinner speaker was Dr Andy Stoekel of the Centre for International Economics in Canberra who talked on the experience with deregulation in Mexico and New Zealand and its implications for Australia.

Daranee Chenhall did a magnificent job as Conference Secretary and deserves full credit for the excellent administrative arrangements.

The Conference would not have been possible without the financial support of the following sponsors:

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We are very grateful to these Institutions for their generous support.

Appendix 1 of this report contains the Conference Programme and the abstracts of the papers are given in Appendix 2. Appendix 3 lists the names of the participants and Appendix 4 presents some press clippings.
APPENDIX 1

THE PROGRAM

Wednesday November 3

6.00pm - 7.00pm   Reception at the Lawrence Wilson Art Gallery, University of Western Australia

Thursday November 4

9.15am - 9.30am   Opening Session
                   Chairperson: Ken Clements, Economic Research Centre
                   Department of Economics, University of Western Australia
                   Opening address by Fay Gale, Vice-Chancellor,
                   University of Western Australia

                  9.30am - 11.00am   Session 1: Macroeconomics
                                             Session 2: Development Economics

                  11.00am - 11.30am  Tea/Coffee

                  11.30am - 1.00pm   Session 3: Labour Economics
                                             Session 4: Capital Structure

                  1.00pm - 2.15pm    Lunch in the Tropical Grove

                  2.15pm - 3.45pm    Session 5: Invited Lecture In Development Economics

                  3.45pm - 4.15pm    Tea/Coffee

                  4.15pm - 5.45pm    Session 6: Topics in Economic Theory
                                             Session 7: Applied Econometrics

Friday November 5

9.00am - 11.15pm   Session 8: Intertemporal Economics
                                             Session 9: Economic Rationality
11.15am - 11.30am  Tea/Coffee
11.30am - 1.00pm  Session 10: **Econometric Methodology**
                 Session 11: **Accounting and Economics**
1.00pm - 2.15pm  Lunch at Matilda Bay
2.15pm - 3.45pm  Session 12: **Invited Lecture In International Economics**
3.45pm - 4.00pm  Tea/Coffee
4.00pm - 5.30pm  Session 13: **Asian Economics**
                 Session 14: **Quantitative Finance**
7.00pm for 7.30pm **Conference Dinner** at Kingswood College
                    Master of Ceromones: David Treloar, Division of Economics, Commerce, Education and Law, University of Western Australia
                    Speaker: Andy Stoeckel, Centre for International Economics

Details of the papers for each session are given below.
THE SESSIONS

1. MACROECONOMICS

   Chairperson: Adrian Pagan, Economics Programme, RSSS, Australian National University

   Kevin Daly, Faculty of Business and Technology, University of Western Sydney, Macarthur, “The Exchange Rate and Fiscal Financing: A Multi-Country Empirical Analysis”

   Penny Neal, Department of Economics, University of Adelaide, “Credit Rationing In Australia: Theory and Evidence”

   Discussants: Doug McTaggart, School of Business, Bond University

   Ross Milbourne, School of Economics, University of New South Wales

2. DEVELOPMENT ECONOMICS

   Chairperson: Frank Harrigan, Department of Economics, University of Western Australia

   Benjamin Buetre, Department of Agricultural Economics, University of Sydney, “Structural Trade Adjustment in the Philippines and Its Implications for Australia”

   Farzana Naqvi, Centre of Policy Studies, Monash University, “An Evaluation of Petroleum Products Pricing Policy In Pakistan In a CGE Model”

   Discussants: Peter Dixon, Centre of Policy Studies, Monash University

   John Piggott, Department of Economics, University of New South Wales

3. LABOUR ECONOMICS

   Chairperson: Paul Miller, Department of Economics, University of Western Australia

   Cushla Paice, Economics Programme, RSSS, Australian National University, “Do Larger Workplaces or Companies Pay Higher Wages?”
Ross Booth, Department of Economics, Monash University, “The Economic Effects of Labor Market Intervention in Professional Sport — The AFL”

Discussants: Glenn Withers, Office of EPAC

Jeff Borland, Department of Economics, University of Melbourne

4. CAPITAL STRUCTURE

Chairperson: Dave Allen, Department of Finance, Curtin University of Technology

Li-Ann Woo, School of Banking and Finance, University of New South Wales, “Factors Affecting Sustained Access to the Equity Markets”

Patricia McBride, Graduate School of Management, University of Melbourne, “Capital Structures of Australian Listed Companies: A Pilot Study”

Discussants: Rob Trevor, Australian Graduate School of Management, University of New South Wales

Don Anderson, Department of Commerce, University of Queensland

5. INVITED LECTURE IN DEVELOPMENT ECONOMICS

Chairperson: Robin Ghosh, Department of Economics, University of Western Australia

Helen Hughes, National Centre for Development Studies, Australian National University, “The Lessons of Development”

6. TOPICS IN ECONOMIC THEORY

Chairperson: Takashi Takayama, Department of Economics, University of Western Australia

Chia-Ao Chang, Department of Economics, University of Western Australia, “A Two-Sector Model of Efficiency Wages”

Neil Campbell, Department of Economics, The Faculties, Australian National University, “Intermediate Goods Protection and Product Quality”
Discussants:  Paul Chen, Department of Economics, The Faculties, Australian National University

Don Wright, Department of Economics, University of Sydney

7. APPLIED ECONOMETRICS

Chairperson: Darrell Turkington, Department of Economics, University of Western Australia

Boyd Hunter, Economics Programme, RSSS, Australian National University, “The Determinants of Neighbourhood Income In Australia between 1976 and 1991”

Clive Morley, Graduate School of Business, Royal Melbourne Institute of Technology, “Diffusion Models of Tourism Demand”

Discussants: Ron Bewley, Department of Econometrics, University of New South Wales

Antony Selvanathan, School of International Business Relations, Griffith University

8. INTERTEMPORAL ECONOMICS

Chairperson: Bob Greig, Economic Research Centre, Department of Economics, University of Western Australia

Estela Alminaza-Varua, Department of Agricultural Economics and Business Management, University of New England, “Welfare Measurement for Natural Resource Accounting”

John Ablett, Department of Econometrics, University of New South Wales, “A Set of Generational Accounts for Australia: One Way of Assessing the Intergenerational Effects of Fiscal Policy”

Discussants: John Kennedy, Department of Economics, La Trobe University

Phil Lowe, Reserve Bank of Australia
9. ECONOMIC RATIONALITY

Chairperson: Paul McLeod, Faculty of Economics and Commerce, University of Western Australia

Gillian Hewitson, Department of Economics, La Trobe University, “Rational Economic Man: A Feminist Evaluation”

Mark Stewart, Department of Economics, Melbourne University, “Fiscal illusion (the Flypaper Effect) and Government Spending in Australia”

Partha Ganguli, Department of Economics, University of Sydney, “Rational Pricing Decisions and Price Inertia”

Discussants: Patricia Apps, Law School, University of Sydney
Jeff Petchey, WA Ministry of Premier and Cabinet
Bob Leeson, Department of Economics, Murdoch University

10. ECONOMETRIC METHODOLOGY

Chairperson: Michael McAleer, Department of Economics, University of Western Australia

Getachew Tessama, Department of Econometrics, University of New England, “A Monte Carlo Analysis of Alternative Estimators of the Tobit Model”

Kang Hao, Department of Econometrics, Monash University, “Testing for Structural Change in Linear Regression Models: A Selective Review and Comparison”

Discussants: Adrian Pagan, Economics Programme, RSSS, Australian National University
Denzil Fiebig, Department of Econometrics, University of Sydney

11. ACCOUNTING AND ECONOMICS

Chairperson: Bryan Howieson, Department of Accounting and Finance, University of Western Australia

Alan Teixeira, Department of Accounting and Finance, University of Auckland, “The Reclassification of Earnings Components”
Christine Jubb, Department of Accounting and Finance, University of Melbourne, “An Optimal Audit Fee Model”

Discussants: Greg Clinch, Australian Graduate School of Management, University of New South Wales

Geoff Kingston, Department of Economics, University of New South Wales

12. INVITED LECTURE IN INTERNATIONAL ECONOMICS

Chairperson: Bob Gregory, Economics Programme, RSSS, Australian National University

Robert Mundell, Columbia University, “Regionalism vs Multilateralism in the World Economy”

13. ASIAN ECONOMICS

Chairperson: Ian vanden Driesen, Department of Organisational and Labour Studies, University of Western Australia

Stephen Lim, Department of Economics, University of Adelaide, “Economic Reform and Chinese Socialism”

Titin Suwandi, National Centre for Development Studies, Australian National University, “Towards a Model of Indonesian Banking after Deregulation”

Discussants: Bob Gregory, Economics Program, RSSS, Australian National University

Ian Harper, Graduate School of Management, University of Melbourne

14. QUANTITATIVE FINANCE

Chairperson: H Y Izan, Research Centre for Accounting and Finance, Department of Accounting and Finance, University of Western Australia

Ram Bahr, Faculty of Business and Technology, University of Western Sydney, Macarthur, “Predicting the Short-term Forward Interest Rate Structure Using a Parsimonious Model”
David Walsh, Department of Economics, University of Melbourne and School of Economics and Finance, Curtin University of Technology, “Optimal Trading Strategies with Private Information”

Discussants: Kim Sawyer, Department of Finance, Royal Melbourne Institute of Technology

Carl Chiarella, Department of Economics and Finance, University of Technology, Sydney
APPENDIX 2

THE ABSTRACTS

A SET OF GENERATIONAL ACCOUNTS FOR AUSTRALIA:
ONE WAY OF ASSESSING THE INTERGENERATIONAL
EFFECTS OF FISCAL POLICY

John Ablett
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Behind concerns in Australia about the continuing viability of the current social security system is the fundamental question of how fiscal policy affects the Intergenerational distribution of wealth. To provide a framework for addressing this question, this paper presents a set of generational accounts for Australia, following an approach developed in the U.S. by Auerbach, Gokhale and Kotlikoff. Generational accounts show, for each generation distinguished by year of birth, the present value of average expected remaining lifetime payments to government, given assumptions about future fiscal policies, growth and demographic change. In the paper, generational accounts are used to model intergenerational redistribution related to policies in the areas of public health care and old age benefits.

WELFARE MEASUREMENT FOR NATURAL RESOURCE ACCOUNTING

Estela Alminaza-Varua
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Widespread public interest in the environment emerged relatively recently in most parts of the world. It was stimulated by growing concerns about specific environmental issues such as the loss of wildlife species through agricultural and mining operations about the capacity of the biosphere to maintain and sustain life; and exhaustibility of resources and degradation of the upper atmosphere.

In an attempt to improve the Gross National Product (GNP) measure to include environmental goods and services, a method known as Natural Resource Accounting (NRA) is currently being explored in many countries. NRA comprises a variety of techniques to present information on natural resources, the environment and the value of services from resource use (Gilbert and James, 1987). NRA should provide the basis for explaining the role of the environment in the performance of the economy. In essence, it attempts to modify the statement of the national Income accounts by including data on
natural resources, to recognise that resources are an integral component of the economic system. However, the literature in NRA appears to be dominated by accounting procedures and physical resource depletion.

The overall objective of this paper is not to engage in a debate concerning how a proper environmental account should be formulated, but to illustrate how the central principles and concepts on NRA can be included in a neoclassical framework to adjust GNP. NRA In a broad sense refers to the adjustment of the national income accounts for defensive expenditures and for the degradation and depletion of natural resources. The focus of this paper is the government defensive expenditures. Defensive expenditures are costs of environmental activities to protect against unwanted side effects of production and consumption. As currently practiced, expenditures by the government and the private sector to redress some of the environmental problems are treated as final expenditures. As such, they are added to the stream of income generated by economic activities and constitute an increase in the level of GNP. Some critics of the GNP measure argue that these expenditures are more appropriately treated as intermediate expense rather than as additions to the income stream in the GNP calculations. An optimisation model, using the neoclassical framework of Income accounts, is developed in this study to capture some of the principles of NRA to adjust the GNP accounts.

PREDICTING THE SHORT-TERM FORWARD INTEREST RATE STRUCTURE USING A PARSIMONIOUS MODEL

Ram Bahr
Faculty of Business and Technology
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A number of parsimonious models are fitted to the structure of 90 day forward rates as implied by the prices of 90 day bill futures contracts. A five parameter polynomial form out performed the Laguerre functional form used by Nelson and Siegel (1987) and Hall’s (1989) model.

The preferred polynomial form is applied to weekly data to elicit estimates of the five parameters for observations in the sample period January 1987 to December 1990. These estimated parameters constituted five time-series. These parameter time series are modelled using three alternative techniques: ARIMA, Kalman filter and VAR modelling. An ARIMA model is used to produce one week ahead forecasts for each of the five polynomial parameters. These forecast parameters are in turn used to produce one week ahead forecasts of the forward rate structure.

The efficacy of the one week ahead structure of 90 day forward rates is tested using weekly spot 90 day and 180 day bill rate data. The spot 90 day bill rate and the implied 90 day forward 90 day rate are used as the forecast targets.
Mechanisms to allocate player talent include (i) a free market; (ii) geographical zoning; (iii) a player draft; (iv) a salary cap, or some combination of these. An evaluation of the outcomes provided by each of the above, must be in terms of the objectives of all interested parties, including (i) the AFL; (ii) the AFL clubs; (iii) the players; and (iv) the supporters. Having determined the criteria by which to assess the outcomes, one must examine the various ways these can be measured. I review the overseas literature on player draft systems in US baseball, hockey, football and basketball to gain insights into how I might try to evaluate the AFL player draft/salary cap system as compared with the market outcome.

The Philippines’ incentive structure created by restrictive and protectionist trade policies is biased against the agricultural and trade sectors. Government policies have accorded high protection rates on non-exportables and manufacturing while agriculture and primary industries were penalised. Previous research suggests that these policies have led the Philippines away from areas where it has a comparative economic advantage resulting in the misallocation and underutilisation of the country’s scarce capital resources. This paper presents a multi-sectoral general equilibrium model of the Philippine economy which is designed to measure the sectoral impact of various policy options. The implications of these policies for trade between the Philippines and Australia are explored.
This paper offers an explanation for the proposition that removing protection from a firm can induce an improvement in product quality. A model is developed which is applicable to a vertically separated industry with the quality of the final good being dependent upon the quality of the Intermediate goods (components) used in its production. This model is used to consider removal of protection from the upstream firm (the supplier) which gives the downstream firm (the assembler) greater bargaining power since the option of turning to a foreign supplier becomes more attractive. It is shown that if the supplier and assembler bargain over both a ‘basic price’ and a ‘quality premium’, then for protection removal to cause an improvement in quality, it is necessary for the supplier to have a technology which has decreasing marginal costs of quality with increased output. It is also shown that if the bargaining is restricted to only the quality premium then removing protection unambiguously results in an improvement in quality.

The exploration of efficiency wage models has mostly focused on the relationship between wages and effort (or efficiency, quality etc). This paper first reviews the basic model that uses this approach, and then renews the direct approach of Leibenstein (1957) where a direct link between wages and productivity is postulated. The implications of efficiency wages in the framework of two-sector models are derived. It is shown that the direct approach of Leibenstein can be used to derive the same results as are obtained using the indirect approach. In particular, it is shown that the efficiency wage solution, which is characterised by a higher wage than the competitive outcome, would result in unemployment. The derivation of these results may be achieved without the wage-effort relationship as is required in the indirect approach. It is also shown that the efficiency wage may differ between sectors according to the characteristics of the production function. In particular, the efficiency wage differential may be explained by a difference in the wage-effort relationship in the framework of the Indirect approach. Similarly, in the framework of the direct approach, the wage differential may result from a difference in the marginal product of labour between the two sectors. Accordingly, the information needed before the efficiency wage models can be applied to the explanation of Inter-industry wage differentials can be readily identified. Specifically, we need to know the
wage-effort relationship and how it differs between sectors. Or equivalently, we need to know how the production function differs between sectors.

**THE EXCHANGE RATE AND FISCAL FINANCING: A MULTI-COUNTRY EMPIRICAL ANALYSIS**

Kevin Daly  
Faculty of Business and Technology  
University of Western Sydney  
MACARTHUR

The paper examines the extent to which innovations in the stance of fiscal policy and its methods of financing impinge upon the exchange rate. The empirical analysis of this paper adopts the vector autoregressive approach which constitutes an unrestricted reduced form of some unknown structural model. Using quarterly data over the period 1973 - 1987, models are estimated for six countries. Preliminary findings suggest that higher government spending which is financed by higher current taxes depreciates the exchange rate in all countries studies. This finding corroborates those of Plosser (1982).

**TESTING FOR STRUCTURAL CHANGE IN LINEAR REGRESSION MODELS: A COMPARISON**

Kang Hao  
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Monash University  
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This paper investigates the structural change problem in linear regression models. Different test procedures are examined and their relationship is inspected. The fluctuation test of Ploberger et al. (1988) and the supF test of Andrews (1993) seem of special interest since both possess some desirable properties asymptotically but belong to a different class of test procedure. In this paper we suggest a modified form of the fluctuation test and our Monte Carlo results provided some evidence in support of the modified fluctuation test. It is also found that the supF test can be expressed as weighted average of modified fluctuation tests.
RATIONAL ECONOMIC MAN: A FEMINIST EVALUATION

Gillian Hewitson
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The abstract Individualism of neoclassical economics requires sexual indifference: the economic actor is allegedly universal and hence disembodied. However, in this paper it is argued that the sex of the economic actor is vitally important: the coherence of neoclassical economics relies on its masculinity. The figure of Robinson Crusoe, the exemplar of rational economic man, is used to illustrate the argument. The paper draws on recent feminist and poststructuralist theory, and can be situated within, although it extends, the recent work of such theorists as Donald McCloskey, Arjo Klamer and Jack Amariglio.

DETERMINANTS OF NEIGHBOURHOOD INCOME IN AUSTRALIA BETWEEN 1976 AND 1991

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The increasing levels and concentrations of poverty in Australian neighbourhoods raises the possibility of a US situation where poor persons are trapped by the ghetto. If living in a poor area affects the expected income (through lowering the returns to education etc.) then it is possible that some Australians also experience neighbourhood effects similar to those observed in the US ghettos. This paper explores the possibility that residence in particular Australian neighbourhoods influences individual incomes using data on urban collector districts from the past four censuses.

THE MARKET FOR AUDIT RVICFS: SOME UNRESOLVED ISSUES

Christine Jubb
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University of Melbourne
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Within the last decade there have been substantial supply side changes to the market for audit services. It is proposed to examine the contraction in the number of upper tier (so called “Big 9” to “Big 6”) public accounting firms in terms of explaining the forces behind the “urge to merge”, why particular merger partners were chosen rather than others and the resultant impact on audit fees, product specialisation and differentiation,
cross-subsidisation between audit and non-audit service fees, market share changes and competition. In order to undertake this analysis, it is intended to first refine previously developed audit fee models to achieve industry contextual models within an Australian setting.

ECONOMIC REFORM AND CHINE SOCIALISM

Steven Lim
Department of Economics
University of Adelaide
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The paper highlights aspects of the recent Chinese economic reforms. The paper begins by outlining the ideological underpinnings of China’s strategies of socialist development and seeks to determine the factors accounting for the failure of Maoism, the dominant pre-reform development strategy. In response to the failure of Maoism, the optimality of the current reform trajectory is examined. A dynamic model suggests that the current leadership must commit itself to a policy of raising national income and curtailing the politicisation of daily life. However, in the long-run, even such changes as these may not be sufficient to ensure the survival of socialism in China.

CAPITAL STRUCTURES OF AUSTRALIAN LISTED COMPANIES:
A PILOT STUDY

Patricia M. McBride
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This study attempts to identify firm characteristics which vary with the capital structures of four large Australian companies over the period 1968 to 1992. Capital structure is measured at book value and is related to proxy variables which attempt to measure characteristics suggested by theory. The analysis is performed cross-sectionally, by industry and separated by sub-period. Preliminary results suggest that the impact of characteristics which determine capital structures differ between sub-periods and by industry.
DIFFUSION MODELS OF TOURISM DEMAND

Clive Morley
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Royal Melbourne Institute of Technology
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The data used to model tourism demand is typically time series and the dynamic structure of tourism demand will be an important part of any well specified model. In this paper a theoretical basis for the dynamic structure of tourism demand is propounded and developed through the application of diffusion models to tourism. The standard diffusion model is extended by incorporating the possibilities of repeat visits and changing populations to allow it to be applied to data on the number of tourists who choose a destination. The model is used to analyse the dynamic structure of tourism to Australia since 1972.

AN EVALUATION OF PETROLEUM PRODUCTS PRICING POLICY IN PAKISTAN IN A CGE MODEL

Farzana Naqvi
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In Pakistan, the Government administers both supplies and prices of three major forms of commercial energy: petroleum, natural gas and electricity. The interaction of various market forces determines energy demand except in certain periods of the year when electricity is rationed. Various considerations influence setting of energy prices: equity, economic growth, balance of trade and the need to generate revenues. As a result of the multiple objectives of the pricing policy, there are various distortions in the energy prices in Pakistan.

ORANI is a Johansen style multi-sectoral model developed for policy analysis in Australia. We have adapted ORANI to simulate the economic effects of alternative energy pricing policies in a general equilibrium framework. The model computes the effects of changes in energy prices on sectoral prices and outputs, imports, exports, GDP, government revenues, energy consumption levels, household utility levels, etc. under various scenarios of energy prices.

We present an experiment that evaluates the economic impact of distortions in prevailing prices of petroleum products. We simulate the effects of removing various types of distortions in the prices of petroleum products. The results help to answer two questions: How far do prevailing energy prices achieve the objectives of energy pricing policy? What is the economic cost of achieving these objectives?
CREDIT RATIONAL IN AUSTRALIA THEORY AND EVIDENCE

Penny Neal
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This paper canvasses theories and presents empirical evidence which demonstrates that asymmetric information and/or the existence of implicit contracts between borrowers and lenders gives rise to nonprice credit rationing as an equilibrium phenomenon in the Keynesian state of rest tradition even in deregulated financial markets. Also demonstrated is that, if banks are profit maximisers, the Walrasian market clearing equilibrium will not be attained either when the financial sector is totally deregulated or when the central bank provides access to lender of last resort facilities or deposit insurance. Implications for monetary policy are discussed.

DO LARGER WORKPLACES OR COMPANIES PAY HIGHER WAGES?

Cushla Paice
Economics Programme
Research School of Social Sciences
Australian National University
CANBERRA ACT 2600

Employer-size wage differentials are examined with Australian data which distinguishes between the size of company and the size of workplace. The empirical relevance of this distinction is assessed using two data sources.

FISCAL ILLUSION (THE FLYPAPER EFFECT) AND GOVERNMENT SPENDING IN AUSTRALIA

Mark Stewart
Department of Economics
University of Melbourne
PARKVILLE VIC 3052

Work in the U.S. and Canada has found the flypaper effect to be evident at the national as well as the sub-national government level. This paper used the methodology developed by Logan (1986) to examine how the payment of inter-governmental grants has affected Australia’s national government own purpose expenditure.
TOWARDS A MODEL OF INDONESIAN BANKING AFTER Deregulation

Titin Suwandi
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Australian National University
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This paper documents the steps taken by Indonesia in deregulating its financial sector since 1983, and analyses the effects of deregulation. It notes the gains in terms of competition and financial deepening from the deregulation measures. It also points out the problems in the form of historically high real interest rates, real exchange rate appreciation, and high level of non-performing loans in the portfolios of Indonesian commercial banks. The paper seeks to explain the weakness in the post-deregulated banking sector in terms of a model of bank behaviour that exhibits adverse risk selection in an environment where the central bank guarantees bank deposits. The paper then draws some conclusions about the institution of prudential supervision of banks early in the process of financial deregulation.

THE RECLASSIFICATION OF EARNINGS COMPONENTS

Alan Teixeira
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University of Auckland
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Earnings components are often segmented according to their nature. Accounting standards direct this process with reference to operating, abnormal and extraordinary items. Within the New Zealand environment the actual components placed into these segments varies between firms. The different disclosure classifications appear to be unrelated to the nature of the underlying transactions.

In studies of where earnings levels are regressed against returns, accounting researchers typically use a measure of accounting earnings that excludes abnormal and extraordinary items (and almost always excludes reserve accounted items). If the observed differences in categorisation are Important, and unrelated to differences in the economic nature of the underlying transactions, then naive adoption of disclosed operating earnings might include or exclude components of earnings that are reflected in returns. This paper proposes the reclassification of earnings components so that earnings components are realigned across firms.
A MONTE CARLO ANALYSIS OF ALTERNATIVE ESTIMATORS OF THE TOBIT MODEL

Getachew Tessama
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In recent years, many types of Tobit models have been suggested and various estimation methods proposed. However, little attention is given to the finite-sample properties of the various estimators.

This paper examines the small-sample properties of some of the estimators of the Tobit model. These estimators include, among others, the maximum likelihood estimator, the Heckman’s two-step estimator, the weighted Heckman two-step estimator and nonlinear least squares. The paper investigates the effects of sample size, degree (level) of censoring and distributional assumptions of the error structure of the model.

OPTIMAL TRADING STRATEGIES WITH PRIVATE INFORMATION

David Walsh
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Recent theoretical developments on informed trading in securities markets have lead to contrasting results on the size of trade that informed traders will use. Based on one set of assumptions, some researchers have shown that informed traders may trade large trades. Based on a different set, other researchers suggest that informed traders trade small.

This study develops its argument somewhat differently from previous studies in that it looks at the motivations of the informed trader in a dynamic sense; that is, with information that has a life that allows multiple trades. It examines how the informed trader jointly maximises trading profit and information asymmetry, with Information asymmetry proxied by the (Copeland and Galai, 1983) call option held by the informed trader. This maximisation would seem to ensure that the results are in a (partial) dynamic trading equilibrium.

The results indicate that optimal trading strategies may be better characterised by trading volume (i.e., per unit time) than by trading size. More importantly, the optimal trading strategies developed here seem to be simple equilibrium results and unique solutions seem to exist in some cases, depending on the market structure and level of competition for Information assumed.
Firms are faced with the choice of using an initial public offer (IPO) or a direct placement (DP) when raising primary equity. The IPO differs from the DP as the public at large is invited to subscribe to the offer, which is subject to prospectus provisions under Australian Corporations’ Law. In contrast, a DP is made to large private or institutional investors, and by virtue of certain issue characteristics, lies outside the prospectus provisions. Currently, little is known about the factors affecting the choice of distribution method, or whether particular firms have a preference for a given method. Further, neither the academic nor the professional literature report the relative merits or the extent to which each method is adopted in Australia.

These comparative questions have been overlooked by Australian researchers who have focused on the IPO. Yet, direct placements are a significant form of financing, measured both in terms of the dollar value of funds raised and the level of institutional holdings evidenced in the newly listed firm. The objective of this paper is to establish how the alternate methods of raising primary equity in Australia differ by assessing the adoption rates (1983-91), the speed to which funds were raised and the relative costs of issuance.
APPENDIX 3

THE PARTICIPANTS

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Link dollar to US currency: expert

By MARK BEYER

AUSTRALIA has been advised to link its currency to the US dollar which is expected to strengthen over the next few years as the US economy leads a slow world recovery.

Robert Mundell, Professor of Economics at New York’s Columbia University and an internationally-renowned Chicago School economist, said the US economy would grow at an average rate of just 2.5 to 3 per cent over the next decade.

However, even this modest rate would be greater than that achieved in Europe and Japan because the economic cycle had not hit bottom, he said.

Europe was still in recession and Japan was in great difficulty with a poor export performance, low company profits in major industries and a pressing need for structural reforms.

In particular, the interlocking “family” style of corporate ownership in Japan was no longer appropriate.

Professor Mundell said China was the big unknown but he suggested the Chinese economy was growing at an annual rate of about 13 per cent.

He said next month’s APEC summit in Seattle would be crucial to China’s economic prospects which would depend on its continued ability to export, especially to the US.

He expected the Clinton Administration would adopt a more pragmatic policy to China, with less emphasis on human rights than it had applied to date.

Professor Mundell said the expected pick-up in US economic growth would be good news for Australia because of the likely boost to commodity prices.

This should lead to a stronger Australian dollar, he said.

Professor Mundell expected the greenback also would strengthen against the German mark and the Japanese yen.

He described the yen as greatly overvalued and said this was one reason why Japanese exporters were struggling.

In the area of currency management, he stopped short of suggesting a formal link between the Australian dollar and the US dollar.

Instead, he suggested the Reserve Bank should have a “de facto stabilisation policy” against the US dollar.

In practice this meant the Reserve Bank should tailor its monetary policy and, therefore, the level of interest rates, to influence the currency.

Professor Mundell said this policy was premised on the US being the world’s most stable economy, with steady growth and consistently low inflation.

He said it should be abandoned if the US pursued an inflationary growth strategy.

Professor Mundell is in Perth as a guest of the UWA Economic Research Centre and is participating in the PhD conference in economics and business at UWA.
Pacific-US monetary union tipped

By JOHN MCLWRAITH

THE United States could eventually look to economic or monetary union with Pacific countries like Australia in the wake of the NAFTA (North American Free Trade Association) agreement, a visiting economist said yesterday.

Professor Robert Mundell, professor of economics at Columbia University, said the move would be a possibility if the Europeans succeeded in cementing their own bloc.

Australia had been mentioned as a possible candidate for such union during the Bush administration and there was every reason to believe the idea would surface again.

The APEC (Asia Pacific Economic Co-operation) conference sponsored by Australia and planned for Seattle was an indication of this trend, he said.

Professor Mundell, whose work on exchange rates and the international monetary system has had considerable influence on the move towards European monetary integration, also sees a continuing, if modest, improvement in the US as being likely to fuel further progress in Australia's recovery.

He will hold talks with officials of the Reserve Bank, Treasury and other bodies during his visit to Australia.

His particular areas of expertise have been in international capital flows (which now far exceed trade flows from country to country) and floating exchange rates.

Pointing to the highly divisive nature of the US debate over NAFTA, Professor Mundell said he believed the nation would move towards joining trade and monetary blocs and that the rejection of NAFTA would be a serious blow.

Professor Mundell pointed out it was inevitable the US would seek to reinforce economic alliances in the Pacific in the face of "Fortress Europe".

The key to this process was improved relations with China and he agreed Australia would have immense opportunities in China. He noted that Australia's competitive position in world trade had improved markedly in recent years.

If anything, the Australian dollar was a little undervalued, but he would urge the Reserve Bank to try to keep it at low levels while Australia experienced high unemployment and a big foreign deficit.

Professor Mundell is gloomy about prospects in Europe and Japan and does not expect significant growth until 1996.
Perspective on APEC’s future course

ECONOMIC, trade and foreign ministers representing the 15 members of the Asia Pacific Economic Cooperation Council met in Seattle next week as a precursor to the heads of government meeting hosted by President Clinton.

It is the first time that APEC leaders will meet as a group to discuss economic issues affecting the Asia Pacific region.

American officials maintain that the Uruguay round of trade negotiations is the most important single issue for the region, and thus the ministerial discussion.

But according to US Assistant Secretary of State for East Asia and Pacific Affairs, Winston Lord, the United States sees APEC as the cornerstone of regional co-operation together with existing organisations such as ASEAN and the proposed North American Free Trade Area.

Mr Lord said last week that the APEC meeting would raise consciousness in the US of the importance of Asia to its prosperity and security.

It’s a theme taken up by one of the world’s most renowned economists, Professor Robert Mundell of New York’s Columbia University. He is visiting Australia as a guest of the Economic Research Centre at the University of Western Australia.

A leading member of the Chicago school, Professor Mundell is mentioned frequently as a potential winner of the contentious Nobel Prize for economics, even though some critics suggest his frequently inelastic attitude detracts from the general brilliancy of his work on monetary systems.

The Uruguay link is not illusory because Mundell is a sometime adviser to the Bank of Uruguay and is very conscious of the concerns of smaller countries about the development of major trading blocks.

Professor Mundell commented in an interview in Perth that the United States’ interest in developing APEC was driven by its view of the growth of Europe as an economic block and what that would mean for its own economy in the next few decades.

But APEC would reflect ultimately a number of groupings rather than a totally unified bloc — say the US, Canada, Japan and China, then the ASEAN partners, perhaps Oceania, and then Korea and Taiwan.

It was improbable that each of these groupings would have the same views on every APEC issue, Professor Mundell said.

“There will be a degree of integration but it will never go as far as the European situation.”

He forecast that the Seattle summit would result in a fairly frank discussion between the US and Japan on the future of free trade.

But the real issue for the future would be the impact of China, where the economy was the equivalent of two Koreas but would record real measured economic growth of around 13 per cent a year for much of the rest of the decade.

“I can see China doubling its measured gross national product every five years from now on: the growth rate will taper off but it will still be fairly phenomenal.

“Thus China will play a huge role in the development of APEC because it has a population with a high level of education, there’s been a big freeing up of controls, taxation is low and, of course, the Chinese are very capable entrepreneurs.”

Professor Mundell said he did not believe that the antipathy expressed by Malaysia’s Prime Minister, Dr Mahatir, to the Seattle summit would have long-term relevance; he felt Malaysia would always be more comfortable in a more narrow group of countries.

“Malaysia is not going to be the determining factor in the development of APEC. The real question will be whether China wants to form a group which excludes the US and Japan.”

The US expects the Chinese said.

China’s economic growth in the shorter term would depend on its ability to export, especially to the United States.

As a result, the Clinton Administration would have to take a more flexible approach to China, which would mean less official concern about human rights. But the prospect of a new trade group does not blind Professor Mundell to some fairly basic Australian issues.

Australia should abandon its free floating currency and peg the dollar to a basket of the US dollar, the yen and the Deutschmark, he says.

The basket should be dominated by the US dollar — probably 80 per cent — and the yen and Deutschmark, 10 per cent each.

Unless Australia made the move, it would suffer a relatively rapid increase in inflation and, consequently, a rise in interest rates as the Government battled to contain currency fluctuations.

Deregulation of the Australian dollar had not produced the real gains expected of it and had caused significant disadvantages in terms of fiscal management, Professor Mundell said.

He expected the US rate of economic growth to be around 3-4 per cent a year for the next decade.

This would continue to maintain the US economy’s record of being the most stable in the world and would be better than the rate in Europe and Japan.

“In a country like Australia,” he said, “you cannot afford to let inflation grow and a stable US-Australian dollar link is crucial to maintain reasonable economic performance.”

“With unemployment rates of 11 per cent, an increase in inflation is not acceptable and further depreciation of the Australian dollar against the US dollar would spark more inflation.”

But in talks around the country, Professor Mundell is warning against a formal $A/$US link, arguing instead for “de facto stabilisation” through the Reserve Bank.