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Oliver Hartwich on NZ's rock star economy, violent shocks for global economy, Germany the sick man of Europe, the wrong economics, Dilbert and more

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1. New Zealand's rock star economy
A new study examining global economic freedom and competitiveness has New Zealand ranked 3rd after Hong Kong and Singapore.

The **new report** by the US based Cato Institute takes government, the legal structure, sound money practices, free trade, and regulation into account.

As the world is taking note of our good institutional settings, one might hope it will translate into trade and investment opportunities.

But for that, we would need to open up to FDI – which is one aspect where New Zealand typically does not rank highly.

> *Australia is the eighth and New Zealand is the third on CATO Institute's annual index of the world's freest economies, behind only Hong Kong and Singapore, according to its report. It has documented that "global economic freedom fell slightly in this year's report, and it remains well below its peak level of 6.92 in 2007." The average score fell to 6.84 in 2012. In the 2014 list, Hong Kong has the highest rating for economic freedom, with 8.98 out of 10.*

2. John Key, superstar
Just as the aforementioned Cato report praises New Zealand's institutional strength, the London ***Daily Telegraph*** praises Prime Minister John Key as "the poor boy who saved New Zealand's economy".

Without wishing to downplay Key's performance, it is a little odd to write an article about Key's management of the economy without a single mention of Bill English's contribution as Minister of Finance. Nevertheless, it is interesting to note how a British newspaper assesses our government's performance.

They almost sound a bit jealous and recommend their own Prime Minister David Cameron might learn a thing or two from his Kiwi counterpart.

> *Last month, thanks to a tax-cutting programme that has hauled the country out of recession, he swept to a third successive election victory, with personal approval ratings of around 70 per cent. That figure officially makes Mr Key the most popular leader in the Western world. But the 53-year-old ex-banker is no longer just basking in the admiration of his fellow Kiwis. On this side of the world, many British commentators are now backing his radical tax ideas as a blueprint that David Cameron might follow.*

3. Global economy headed for violent shocks
As New Zealand is going from strength to strength, the world economy is still in deep trouble.

The Bank for International Settlements, the central bank of central banks, just issued **a fresh warning** that the next phase of the Global Financial Crisis (which never really ended) is about to begin.

> *The global financial markets are dangerously stretched and may unwind with shock force as liquidity dries up, the Bank of International Settlements has warned. Guy Debelle, head of the BIS's market committee, said investors have become far too complacent, wrongly believing that central banks can protect them, many staking bets that are bound to "blow up" as the first sign of stress.*
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> *In a speech in Sydney, Mr Debelle said: "The sell-off, particularly in fixed income, could be relatively violent when it comes. There are a number of investors buying assets on the presumption of a level of liquidity which is not there. This is not evident when positions are being put on, but will become readily apparent when investors attempt to exit their positions. "The exits tend to get jammed unexpectedly and rapidly."*

4. Germany, the new sick man of Europe?
One of those countries that could trigger the next economic crisis is Germany. Though the Germans may have been feeling good about themselves in recent years for not being French, Greek or Italian, their own economy has been moving in the wrong direction under Chancellor Merkel's leadership.

A rude awakening to the reality of an economy that is hardly growing anymore (if at all) is unavoidable, as an increasing number of German economists warn and the London *Daily Telegraph* **reports**.

> *Growth has averaged 1.1pc since the beginning of the decade, placing Germany 13th out of 18 in the eurozone (or 156th out of 166 countries worldwide over the past 20 years). This chronic weakness been masked by slightly better growth since*

the Lehman crisis, and by the creditor-debtor dynamics of the EMU debt crisis. German looks healthy only because half of Europe looks deathly.

The Hartz IV reforms – so widely praised as the foundation of German competitiveness, and now being foisted on southern Europe – did not raise productivity, the proper measure of labour reform. Data from the OECD show that German productivity growth slumped to 0.3pc a year in the period from 2007 to 2012, compared with 0.5pc in Denmark, 0.7pc in Austria, 0.9pc in Japan, 1.3pc in Australia, 1.5pc in the US and 3.2pc in Korea. Britain has been negative, of course, but that is no benchmark.

5. Teaching the wrong kind of economics
The world might be a better place if we all understood a little more economics.

Problem is, the way economics is taught at high school level is totally flawed – at least in Australia.

An analysis of the Australian economics curriculum reveals that it does not even manage to teach core economic concepts correctly and fails to mention important economists such as Adam Smith.

Griffith University economics professor Tony Makin and lecturer Alex Robson, in their advice to the federal government's curriculum review, say the curriculum incorrectly defines some fundamental concepts including gross domestic product, efficiency and productivity.

They argue that the curriculum omits key concepts, such as the difference between microeconomics and macro-economics, or between recessions and booms. It also fails to include the great economic thinkers, including the father of economics Adam Smith and his coinage of the term "invisible hand" to describe the forces of the free market.

Part of the problem seems to be the decision to combine economics and business in one curriculum, which Professor Makin and Dr Robson say is unusual internationally. "The curriculum ... as it stands is grossly deficient and needs rewriting," they say.

"Australia's curriculum lacks balance and omits core economic principals and essential material across a range of topics. "(The curriculum) is too wordy, is poorly expressed and contains many definitional errors in relation to important economic concepts. Fundamental problems with the existing document suggest that it is beyond redrafting."

6. Prize-worth economics
Should Australian students ever be taught the names of great economists, they might even hear about Jean Tirole. After all, Tirole was just announced as this year's recipient of The

Sveriges Riksbank Prize in Economic Sciences in Memory of Alfred Nobel (yes, there is no Economics Nobel Prize because Alfred Nobel forgot to include economics in his list of prize-worthy causes).

However, **not everyone seems to be completely convinced** by Tirole's work, as economist Peter Klein notes.

> *As a second-year economics PhD student I took the field sequence in industrial organization. The primary text in the fall course was Jean Tirole's Theory of Industrial Organization, then just a year old. I found it a difficult book — a detailed overview of the "new," game-theoretic IO, featuring straightforward explanations and numerous insights and useful observations but shot through with brash, unsubstantiated assumptions and written in an extremely terse, almost smug style that rubbed me the wrong way. After all, game theory was supposed to add transparency and "rigor" to the analysis, bringing to light the hidden assumptions of the old-fashioned, verbal models, but Tirole combined math and ad hoc verbal asides in equal measure. …*
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> *As a student I found Tirole's analysis extremely abstract, with little attention to how these theories might work in practice. Even Tirole's later book with Jean-Jacques Laffont,* A Theory of Incentives in Procurement and Regulation*, is not very applied. But evidently Tirole has played a large personal and professional role in training and advising European regulatory bodies, so his work seems to have had a substantial impact on policy.*

7. Monopoly is good for you

As Jean Tirole researches the theory of market power, a practioner of market power comes to slightly different conclusion. Peter Thiel's new book *Zero to One* makes the case for monopolies, based on a very Schumpeterian idea of entrepreneurship and creative destruction, the **Wall Street Journal reports**.

> *Mr. Thiel's contrarian claim that "monopoly is the condition of every successful business" echoes Joseph Schumpeter, the Austrian economist best known for coining "creative destruction." Schumpeter explained in a 1942 book the key role of temporary monopolies in innovation: "The introduction of new methods of production and new commodities is hardly conceivable with perfect—and perfectly prompt—competition from the start. And this means that the bulk of what we call economic progress is incompatible with it. As a matter of fact, perfect competition is and always has been temporarily suspended whenever anything new is being introduced."*
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> *Many academics and antitrust lawyers wrongly believe big is bad by definition. The Justice Department pursued IBM in the 1970s and Microsoft in the 1990s without understanding that in a dynamic market, where government doesn't protect incumbents, new innovators displace old innovators. Apple undermined the dominance of Microsoft, which had ended IBM's.*

> *Mr. Thiel joins a long-running dispute. Justice Antonin Scalia set off a firestorm a decade ago when he defended monopolies in a majority opinion: "The mere possession of monopoly power, and the concomitant charging of monopoly prices, is not only not unlawful, it is an important element of the free-market system. The opportunity to charge monopoly prices—at least for a short period—is what attracts 'business acumen' in the first place; it induces risk taking that produces innovation and economic growth."*

8. [Divided economists]
It is not just economists and business practitioners disagreeing with each. There is no shortage of disagreement among economists, either.

In the latest **IGM poll of leading economists**, the panel was asked whether they agreed with Thomas Piketty's claim that "The most powerful force pushing towards greater wealth inequality in the US since the 1970s is the gap between the after-tax return on capital and the economic growth rate."

The result: most economists disagree, some strongly so – and a few agree, and even fewer strongly so.

Which probably suggests that it must be an interesting question.

9. The public has no idea about economics either
Okay, so economists disagree on complex questions. That's bad enough. But what's even worse about economic literacy is the fact that ordinary people do not even know basic economic facts.

Case in point: The Pew Research Centre's poll of ordinary Americans on the Federal Budget.

Turns out, Americans have **no idea** what they pay taxes for.

> *Christopher Ingraham of Wonkblog points out that a new Pew Research Center survey shows that most of the public is ignorant about the distribution of federal spending. Only 20% realize that the federal government spends more money on Social Security than on foreign aid, transportation, and interest on the government debt. Some 33% believe that foreign aid is the biggest item on this list, even though it's actually the smallest. It accounts for only 1% of the federal budget, compared to a whopping 17% for Social Security, which is one of the biggest federal outlays and has been for decades.*
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> *The Pew poll is consistent with numerous previous studies that reach similar results, consistently showing that the public massively overestimates foreign aid spending, and underestimates spending on big entitlement programs, such as Social Security and Medicare. British voters are misinformed about their own government's budget in much the same way.*

10. **And finally, Israelis get excited about Germany's price level (and chocolate pudding)**
An Israeli living in Berlin posted a supermarket receipt on Facebook – and reached over a million of his fellow countrymen and women at home. Now Israel is wondering why it is so cheap to live in Germany.

Well, had a Kiwi living in Berlin posted a receipt to his New Zealand friends back home, they would also wonder why in Germany you can buy chocolate pudding for $0.31, a loaf of specialty bread for $1.85 and half a dozen organic eggs $2.24.

So the German economy may be in crisis, and New Zealand has a rock star economy, but German consumers still get **better value for their money.** It probably takes a few economists to explain all of that.

> *Five days ago, a young Israeli posted a grocery shopping receipt on Facebook: It included everyday items like orange juice, eggs, bread, pasta and three cups of chocolate pudding with whipped cream on top that people in Israel have nicknamed "Milky" and costs just 19 cents. The 25-year-old challenged his readers: "Find any supermarket in Israel where you can get all of these things for less." He had filled his grocery bag in Berlin, which is regarded as one of Europe's most affordable capital cities. "See you there!" he wrote.*