

Economics

Department Alumni Newsletter

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Bob Stonebraker, editor

Goodbye Marvin

No more eight a.m. lectures on equilibrium GDP and fiscal policies. No more last-minute student questions about moving along versus shifting demand curves. After more than twenty-five years of toiling in the trenches of Keith Hall, Marvin Huff has retired. No more meetings to attend; no more exams to grade. Just family and travel and fishing and ham radios and cycling and bowling.

Oh yes, and *golf*. A mere month into retirement, Marvin had already carded his first hole-in-one; a lazy seven-iron on the 17th at Meadow Lane that pounced onto the green and rolled gently into the cup. Knowing Marvin's penchant for tall tales -- *he's reeled in more people with his shaggy dog stories than Indiana County has Christmas trees* -- our immediate reaction was disbelief. Luckily a trio of witnesses, including our own John Cross, allayed our suspicions. What's next? A cameo on the Senior's Tour? A junket with Tiger Woods?

Moving Day

It's coming. While Marvin Huff patrols the links, the rest of us are launching into relocation mode. With knocked-down boxes piled on skids in the hallways, most of us have begun sorting through the dark recesses of our desk drawers and file cabinets. Custodians arrive each day to find wastebaskets stuffed with long-forgotten exams and musty handouts from 1976. The *Free Books* table inside the department doors is littered with two-foot stacks of assorted reference books and outdated texts.

Of course, every department has its pack rats. Almost as rapidly as the rest of us dump our accumulated baggage, Jim Dyal combs through the piles of abandoned refuse to rescue priceless publications -- *"salvaging classics for posterity."* As the clutter in other offices gradually retreats, the Dyal disarray mushrooms. Already crammed beyond what his new *and larger* office can accommodate, he has commandeered increasing numbers of hallway lockers to billet his overflow possessions -- a sort of archives annex.

On a more somber note....

Contract negotiations between the State System of Higher Education (SSHE) and the faculty union (APSCUF) remain stalled. Although a new agreement was to be in place last July, negotiators are far apart. Management disputes almost every article in the current labor contract (*all 125 pages of it*). Negotiations have been tangled in the past. A 1985 impasse was especially messy -- but this one is worse. With progress about as rapid as continental drift, frustration levels are rising to flood levels and the tempers of ordinarily mild-mannered academics are fraying at the seams. Is resolution right around the corner? We hope so.

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JOBS: U.S. vs. Europe

Americans groan about inflation, but fear the specter of unemployment far more. Few economic events unleash the personal tragedy of a once-secure job biting the dust -- which, of course, is a major reason President Clinton has been riding high in the political polls.

Although his economic policies may have made little or no difference, Clinton has certainly benefitted from the sustained burst of job creation over the last four years in the U.S. The official unemployment rate has plunged from 7.5 percent during the 1992 election year to 5.4 percent thus far in 1996. Pockets of joblessness remain, especially around Indiana and other rural counties in Western Pennsylvania, but the national picture is unusually bright by historical standards. Only one other year -- 1989 -- in the last twenty-five can match our current 5.4 percent level.

The lower rates are no surprise. Modern neoclassical macroeconomists make much ado over the tendency for markets to return to their *natural* rate of unemployment. *Prolonged* unemployment should not persist. Job seekers will eventually accept lower wages and, in turn, the lower wages will increase the willingness of firms to hire. When oil shocks drove unemployment well above its natural level in the mid and late 1970's, few economists foresaw long-term disaster. Once the oil crisis eased and we crawled through a deep recession in the early 1980's, most predicted a gradual, though perhaps fitful, return to the lower rates of earlier days.

The theory worked well in the U.S., and neoclassical economists have wasted no time in patting themselves on their backs. Unfortunately, neoclassical predictions have been less successful in Western Europe. Unemployment rates in most European Union (EU) countries continued to climb through the 1980's, and these high rates have persisted through the 1990's. Although the recession of the early 1980's lasted longer in the EU than in the U.S., their economies did recover and have been growing at rates comparable to those of the U.S. in the 1990's. Yet, their unemployment rates remain lodged at historically high levels.

The turnaround is quite remarkable. As the following table shows, unemployment rates in EU countries were well below ours through most of the post-war period. Policy makers in countries like Germany, France, and Sweden routinely sneered at "high" U.S. unemployment rates. No more. With joblessness stuck at above ten percent, the sneers have turned to jealousy.

Average Unemployment Rates

	<i>U.S.</i>	<i>Britain</i>	<i>France</i>	<i>Germany</i>	<i>Sweden</i>
<i>1950-1974</i>	4.8	2.0	2.2	3.1	1.8
<i>1975-1990</i>	7.1	8.3	7.7	5.1	2.2
<i>1996</i>	5.4	7.5	12.6	10.1	8.8

Why? Some economists initially blamed *labor market rigidities* in the EU. Strong unions in these countries limit managerial flexibility and make lay-offs difficult. Government programs raise the cost of

labor and could make employers reluctant to hire. For example, government regulations require employers to fork over large pensions and social security contributions for current workers, and generous unemployment packages reduce the incentives for jobless workers to find new positions quickly.

However, other economists note that these potentially burdensome programs are not new. They were already in place during the 1950's and 1960's -- a period of very *low* unemployment in EU countries. Other economists suggest that *hysteresis* offers a better explanation.

Huh? Hysteresis? Hysteresis is the tendency for things to persist through history; the idea that current levels of a variable (like unemployment) might depend upon past levels of that variable. In this case, high unemployment in the past might beget high unemployment in the future. Larry Summers and Olivier Blanchard of Harvard cite several channels through which this might occur.

High rates of unemployment can pressure governments to legislate more generous benefits for unemployed workers. With increased benefits, jobless workers become choosier and stay unemployed for longer periods of time. Also, the longer a worker remains unemployed, the harder it becomes to find a new job. Long-term unemployment causes valuable job skills to wither and could wreck a worker's attitude and motivation. In addition, employers may become more skeptical, fearing the long-term unemployed are "damaged goods." In each case, new jobs become harder to find.

The recession of the early 1980's lasted far longer in EU countries than in the U.S. According to Summers and Blanchard, the unusually long recession created a new pool of long-term unemployed workers; hysteresis took over from there. It's not a pretty picture. And, without a hefty and sustained economic expansion, the picture is not likely to change. What's worse, any expansion strong enough to dent long-term unemployment might also re-ignite the inflationary pressures of the 1970's.

Our own employment outlook is far brighter. The U.S. unemployment rate is lower than Europe's, and is likely to remain lower, at least for the immediate future. But flipping *nyah nyahs* across the Atlantic at this point would be a mistake. All is not well in the U.S. either.

In EU nations, the hard-core unemployed live on the government dole. Because such long-term government largesse is absent in the U.S., jobless workers must seek substitutes. One substitute is gainful employment, but another is crime. Yes, *crime*. When unskilled, unemployed workers have no alternative source of income, crime becomes an increasingly attractive venture. Such people have much to gain from crime, and relatively little to lose if apprehended and imprisoned. Our unemployment rate is less than one-half that of many EU countries, but our imprisonment rate is five times higher than Europe's.

Is the U.S. unemployment rate low simply because our hard-core unemployed are in jail? Some pundits suggest the answer is "yes." Are they correct? Does it matter? You decide.

The Economics of Courtship

In high school and college I avoided the front row. I aimed for a seat about three-fourths of the way back by the windows. Windows are always a desirable diversion, but I was interested in something else. I was interested in *girls*.

From my vantage point, almost every co-ed in the room was arrayed in front of me. Ones in the very back were hidden, but girls rarely sat there anyway. I could face the chalkboard, pretend to be looking at the instructor, and ogle away.

I'd select ones I might like and ask them for a date. In fact, I asked *lots* of them for dates. I had to. Most turned me down, so I kept trying new and different ones. I squandered many years mooning over girls who repeatedly rejected my advances. Friends gleefully teased that my low batting average at romance was caused by a simple lack of animal magnetism. Quite frankly, it was all very depressing.

The power of economics

Ah. Then I learned some economics. With the help of some very attractive equations and graphs, I discovered that it wasn't me at all. The cause of my distress was not some inadequate amorous aptitude - I was simply the innocent victim of powerful economic forces that were beyond my control.

Economics and romance? *Of course!* Remember, economics is about choices; all kinds of choices. The same maximization models that elucidate corporate pricing policy can explain the romantic rejections of my youth. Simple. The girls I coveted were in my school classes; they were girls of my same age. Regrettably, girls my age were not interested in boys my age. They wanted older men. They still do. Sixteen year-old girls are far more likely to accompany 18 year-old boys than the reverse. Women marry older men; men rarely marry older women.

WHY? The sixteen year-old girls claimed it was "a maturity thing." Girls matured faster and, therefore, needed more mature male companions. *Bunk.* Even if the argument is valid at age sixteen; it is certainly *not* valid at age 35. Scientists would be hard-pressed to prove that 35 year-old men are less mature than 35 year-old women. Yet, the same older-man bias exists at age 35 as at age sixteen. Moreover, if maturity is an important trait in a mate, why wouldn't men be drawn to more mature, older women just as women are drawn to more mature, older men?

No. An economist wants something more substantive. An economist wants an argument about relative costs and benefits. And we have one; one that springs from the role of men and women in the economic marketplace.

Looking for success

Let's face it. Both men and women want a successful mate. Nobody wants a dog. In a traditional world women specialized in child-bearing and in-house production, while men specialized in outside market production. As a result, men wanted women who would be successful mothers and cooks, while women wanted men who would be successful bread-winners.

However, the requisite talents for such success are not manifest at the same ages. A woman's likely proficiency at child-bearing and cooking are often apparent as soon as she reaches physical maturity. Not so with men. The eventual fortune of a Bill Gates or a Michael Jordan could not have been predicted at age sixteen. A man's ability to be a successful bread-winner is likely to be evident only after years of experience.

If so, women will not want to risk tying the knot with an untried youth. Why gamble with a mere child when older men are much safer marital bets? Less talented women may have little choice, but the most enticing ones will be able to command the attention of seasoned market veterans. The most sought-after women will mate with older men. Similarly, the men most confident of eventual market success will not

marry at early age. They understand that, if they hold out, their future financial feats should enable them to snare far more alluring partners.

Does it make sense? Do I have a good excuse for my substandard success in pitching woo? According to economists Ted Bergstrom and Philip Bagnoli, the answer is *yes!* In a recent study published by the *Journal of Political Economy*, Bergstrom and Bagnoli examine marital age gaps in 90 countries from 1950 to 1985. The average age for husbands exceeded that of their wives in every country during every time period. More importantly, the patterns in age gaps are precisely what the above theories would predict. For example:

- 1. The age difference between husbands and wives should be falling over time as labor market opportunities for women increase.** As women specialize less in raising families and begin to compete in the labor force, the age difference between men and women in marital relationships should shrink. As the market success of women becomes a more valuable piece of the marital pie, men -- like women -- will find it advantageous to look for a proven veteran rather than an unproven child. The data support this hypothesis. The age gap between husbands and wives fell over the 1950 to 1985 period in almost every country.
- 2. The age difference between husbands and wives should be smaller in developed countries where women have better labor-market opportunities.** In the U.S., the average age difference was 1.9 years. The average for Western Europe, Canada and Australia was 2.5 years. However, in less industrialized and more traditional societies, the age gap was higher. Men were an average of 3.5 years older than their wives in the sample countries from Latin America and Asia, and 5.7 years older than their wives in the African countries studied.
- 3. Men with the least chance of economic success should marry at an earlier age.** Men expecting to be a financial flop have no incentive to wait for marriage. The longer they wait, the clearer their lack of pecuniary prospects will become -- better to marry quickly before potential mates catch on. Indeed, Bergstrom and Bagnoli discover that, all else equal, men at the lower end of the U.S. income distribution married at an earlier age.

By the way, I did, eventually, catch on to the game. I renounced females my age and married a younger woman.

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How Fast is *Too* Fast?

After much debate and wrangling, Pennsylvania has returned its maximum speed limit to 65 miles per hour. Good. I missed it.

Although recent alumni cannot remember, motorists routinely sailed down interstate highways at 65 and 70 m.p.h. -- *legally* -- in the 1960's. The 55 m.p.h. limit was born in the throes of the energy crisis in the early 1970's. Amid much weeping and gnashing of teeth, with mandatory gas rationing looming in the wings, President Nixon declared a nationwide maximum of 50 m.p.h. in December 1973. OPEC, not safety, drove the legislation. *Fifty is thrifty* slogans soon hit the airwaves, but Congress substituted the more palatable 55 m.p.h. limit in the 1974 Emergency Highway Energy Conservation Act.

And it stuck. Congress extended the limit with 1975 legislation that denied federal highway funds to any

state exceeding the 55 m.p.h. level. By this time, lower speeds were also credited with saving thousands of lives. Traffic fatalities plunged by 9,100 in the first year alone. The measure was so popular that it passed the Senate with a unanimous 85-0 vote.

But, the bloom began to wither. By the early 1980's the energy crisis was history -- thanks largely to some belated price deregulation -- and average speeds were inching up. Pressure mounted to restore the higher pre-OPEC speed limits and several rural states all but refused to enforce the federal 55 m.p.h. mandate. For example, wide-open Montana kept the 55 m.p.h. limit on the books, but dropped the fine for violations to \$5 and ignored all but the most egregious speeders.

With falling oil prices and abundant gasoline, proponents of the 55 m.p.h. limit ditched their conservation arguments and stressed safety instead. What about the thousands of lives saved by lower speeds? Did they not matter? After all, *speed kills*.

Does slower mean safer?

Or does it? Were those lives saved by lower speeds? Or were other factors at work? When gas prices rose in the 1970's, motorists responded by staying home and/or using public transport. With fewer cars on the road, fatalities would have dropped regardless of speed limit changes. Similarly, safer vehicles and highways could have cut fatalities. Studies trying to identify the importance of lower speeds gave mixed statistical results.

The University of Chicago's Sam Peltzman and CMU's Lester Lave added theoretical fuel to the fire. Peltzman argued that regulatory attempts to improve safety are often counteracted by offsetting consumer behavior. For example, drivers routinely become more alert and cautious in potentially dangerous situations. Could the reverse also be true? Might not drivers be *less* alert and/or *less* cautious at seemingly safer lower speeds? If we become more careful at high speeds and less careful at low speeds, changes in legal limits are not likely to have much impact.

Lave claims that high speeds are less dangerous than variable speeds. If everyone travels at 65 m.p.h., everyone is relatively safe. If all travel at the same speed, the risk of collision is small. However, if some travel at 70 m.p.h. while others plug along at 40 m.p.h., risks rise rapidly. Brake lights fly on, drivers weave in and out of lanes trying to pass, and dangers mount. Slow drivers are as large a hazard as fast ones.

According to Lave, lower speed limits can aggravate variability problems. While some motorists will slow to the lower limit, others will continue to drive at the older, illegal speeds. If people are more apt to stick to a 65 m.p.h. limit than to a 55 m.p.h. limit, the faster speed limits might actually reduce variability and *increase* safety.

Bowing to the shaky statistical and theoretical support for the 55 m.p.h. limit, Congress reversed course. In 1987 it allowed states to opt for 65 m.p.h. limits on rural interstates and, last year, eased restrictions further. Although many states raised legal limits quickly, Pennsylvania chose to wait and see. Would safety be compromised? Would fatalities rise?

Impacts of 65 m.p.h

The apparent impacts are minimal. Purdue's Patrick McCarthy found that safety *was* compromised when speed limits on interstates in the state of Indiana rose. However, he found that safety on *other* Indiana highways and roads improved. Why? The higher speeds allowed on interstates diverted traffic from other highways. The added congestion caused more accidents on the interstates. However, the drop in

congestion elsewhere meant fewer accidents on other roads. The net effect was zero. A second study by Berkeley's Ted Keeler found that higher speed limits did impair safety slightly, but only in congested, urban areas. If these studies are correct, Pennsylvania's recent decision to adopt the 65 m.p.h. limit on controlled-access highways in rural areas should not measurably affect safety.

But, if lower speed limits do not decrease highway fatalities, what will? Must we accept the continuing carnage? Maybe. We have no easy solutions. Keeler found, as expected, that fatalities rise rapidly with alcohol consumption, but attempts to eliminate drunk driving have met with only marginal success. Interestingly, Keller discovered that fatalities fall as education levels rise. College graduates are less likely, all else equal, to be involved in fatal accidents. He also found that requiring frequent testing for license renewals increases safety, but these effects are quantitatively small.

Any other ideas? Economist Gordon Tullock has floated what he considers foolproof proposal, but is not holding his breath for it to be adopted. Using the Peltzman notion of offsetting consumer behavior, Tullock offers a cheap and easy solution to reckless driving. Simply affix a sharp dagger on every steering wheel -- a dagger that is pointed directly at the heart of the driver. Would it work? Should we do it?

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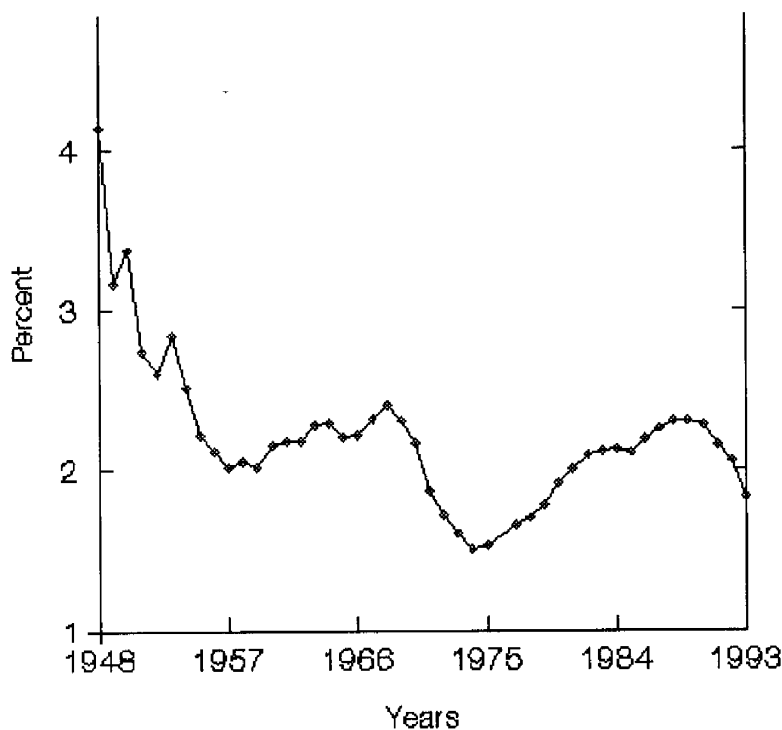
Economics Majors...

where did they go?

What happened? Where are the economics majors? The crush of majors in the 1980's has withered into the drought of the 1990's. The plunge is nationwide. And, we don't know why.

Such cyclical trends are not new. The chart below maps economics as a percent of all undergraduate degrees from 1950 through 1993. The percent dropped quickly through the late 1940's and 1950's. But, this was also the period of expanding business programs. Before World War II, undergraduate business schools were relatively rare. Students interested in accounting, marketing and management chose economics by default. There was a second, but shorter, dip during the Vietnam War years. Economics is often considered an "establishment" major; perhaps anti-war and anti-establishment sentiments among college students fueled this second dip.

Economics as a Percent of all Undergraduate Degrees



Other changes are harder to explain. For example, why did the relative share of economics degrees rebound in the 1960's. Why did it rise again during the late 1970's and 1980's? Why has it plunged in the 1990's?

Cyclical trends in popularity bedevil other disciplines as well. The number of undergraduate history degrees plunged from 44,663 in 1971 to 16,049 in 1985 -- a drop of 64 percent. Yet, by 1993 the number had rebounded to 27,774. What's going on? What drives student choices? In truth -- *we do not know*. The process by which students select majors remains one of life's great mysteries. Nonetheless, we keep plugging away at ideas.

At least we can reject several hypotheses. For example, the size of the school, its emphasis on teaching, and the types of curricula requirements and options seem irrelevant. The recent decrease in economics majors is across-the-board. It affects big schools and small; those that emphasize teaching and those that stress research. It is equally evident in departments with very different course requirements and options.

What remains is a melange of speculations, each with its own set of adherents and support. Among the conjectures are:

1. The mean-reversion theory.

Excluding the early post-war years, the percent of economics degrees has cycled around a mean of just over 2.0 percent. Although temporary disturbances push the percent up and down in the short run, perhaps there are "natural" forces that keep drawing it back to this long-run mean. Vanderbilt University's Robert Margo and John Siegfried offer several possible equilibrating mechanisms.

Labor market forces. A temporary surge in economics graduates might depress starting salaries and signal potential majors to look elsewhere for disciplines with more lucrative employment opportunities. Likewise, a drop in graduates should drive wages up and attract more majors.

Class size. An increase in majors might increase class sizes in economics relative to other courses. This could lower the quality of instruction and make economics a less attractive field in which to major. Similarly, a decrease in majors should lower class sizes and reverse the trend.

Grading policies. Excess demand for courses allows professors to demand more from students. When the number of majors increase, course requirements might rise and grading standards stiffen. As the reputation for difficulty grows, the number of student reverts to its earlier level.

According to this theory, the drop in economics majors is of no concern. It is a temporary blip that will soon resort to its higher long-term mean. Perhaps. But, what caused the temporary blip in the first place?

2. The decline in business majors theory.

The recent decline in economics majors mirrors a similar decline in business majors. For example, the number of business majors at IUP has been falling for several years. Although enrollments in IUP economics classes are down, they are not down *relative to business enrollments*. Nationally, the percent of high school seniors taking the SAT who were planning to major in business fell from 23 percent in 1987 to 14 percent in 1994.

Remember, few high school students are exposed to *real* economics and choose it as a major. Most of our majors are converts -- students majoring in other fields who, after taking Principles of Economics, see the light and change majors. Since the College of Business provides the largest single pool of students to our introductory classes, it is also our largest single source of potential majors. When students abandon the business ship, economics gets swamped in the wash.

Logical? Yes, but there is still an unanswered question. Why did business enrollments drop?

3. The economic trauma theory.

Perhaps interest in economics is inversely related to the degree of economic trauma in society. Perhaps student interest in economics peaks when economic problems multiply. Certainly, economic issues dominated the headlines in the 1970's and 1980's. From the energy crisis and stagflation to the tax debates and twin deficits, economic held center stage in the media circus from the end of the Vietnam War until recent years.

However, the 1990's have been relatively calm. With the federal deficit down and inflation and unemployment rates cruising at historically-low levels, economic issues have taken a back seat in recent political debates. While macroeconomic concerns dominated the presidential campaigns of the last twenty years, the current candidates battle more over drug policies and family values. Perhaps economics is a more attractive major when GDP is going down the tubes. Margo and Siegfried do find that the number of economics majors increases when the unemployment rate increases, but the size of the effect is quite small.

4. The financial services theory.

How about employment opportunities? Any good cost-benefit analysis would predict an increase in majors when employment opportunities boom and a drop in majors when jobs are scarce. Past surveys identified the financial service industries as the largest employer of new economics graduates. According to Rachel Willis from the University of North Carolina and Paul Pieper from Illinois, employment trends in the financial service sector lead trends in the number of economics majors.

The boom in economics degrees through the late 1970's and 1980's correspond with a boom in financial service sector employment. From 1975 through 1988, employment in finance, insurance and real estate

grew at 3.5 percent annually, well above the 2.5 percent rate for the U.S. as a whole. However, since 1988, employment in these areas has slowed considerably, as has the number of new economics majors. Could the stock market crash of 1987 have pulled the plug on the lure of Wall Street?

5. The Alex B. Keaton theory.

Colleague Will Radell suggests Hollywood might be changing the allure of economics. The television sitcom *Family Ties* sat atop the Nielson ratings for most of the 1980's. Each week the young, attractive, and intelligent Alex Keaton, played by the then-unknown Michael J. Fox, pounded his liberal, ex-hippie parents with conservative economics. Alex's passion for economics satisfied two universal ambitions of youth -- rebellion against parental authority and financial success.

Alas. *Family Ties* bit the dust and Michael J. Fox went on to make a second fortune filming *Back to the Future* and teen werewolf movies. Alex P. Keaton, economics major par excellence, is gathering dust in a studio archive, and the number of economics majors has tumbled. Will Fox's recent return to prime time TV resurrect interest in *Family Ties* re-runs? Can we entice new celebrities to champion marginal analysis?

What's next? Will the trend reverse? At IUP, the answer is *probably*. Enrollment in the Eberly College of Business has begun to turn around and is likely to spur a resurgence of demand for our own courses in the coming two years. As more prospective business majors pour through Principles of Economics, we expect increasing numbers to recognize the magnificent splendor of our discipline and convert.

In the meantime, the drop in demand has not been all bad -- our class sizes have returned to more manageable levels. For example, we can now close our principles classes at 40 to 45 students rather than the 50 to 60 of the 1980's and we can close some of our upper-level electives at 15. Macro and Microeconomic Analysis courses that routinely handled 25 to 30 students per term in the 1980's and early 1990's are now running around ten to 15 students. Not only does this enable more student- faculty contact, it has allowed several of us to successfully experiment with more interactive styles of teaching. Small classes have been a nice change of pace. I'll miss them.

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