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Economics and Finance Newsletter

Dear all,

Welcome back to the final term of the year. At the end of the Royal Wedding, I am sure that the last few weeks have been gruelling with exam preparation. But as the exam period approaches its end, most of you must be relieved by now. Hope it all went well with you. At least we are not aware of any major concerns during the exam period. Now it is busy time for academic and admin staff as we mark/moderate/finalise marks/grades for all of you. There are also a number of workshops/conferences taking place in the next few weeks (please see the details below) as the academics switch from teaching to research mode. This certainly highlights the research strength of the department.

I am also very pleased to announce that Shivani Patel has won the election and will be acting as the President of the Economics and Finance Society. She will be assisted by Pankhuri Bhatnagar

who will be back to the University after a very successful placement at

American Express. I would also like to welcome more enthusiastic students from level 1 (who will be progressed to level 2 at the end of the summer) to participate in the activities organised by the E&F society throughout the year. We still have a couple of positions for the E&F society to fill in. Please contact Shivani (ec09ssp1@brunel.ac.uk) for further details.

If you would like to contribute to this newsletter in any way, please do not hesitate to contact me.

Good luck with your exam results.

Sarmistha Pal

E-mail: Sarmistha.pal@brunel.ac.uk
 (prepared with the help of Eesha Phakey & Shivani Patel)



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E&F society Election news

Economics and Finance Society Officers

President: Shivani Patel

Vice President: Pankhuri Bhatnagar

Secretary: RON (EGM needed to fill position)

Treasurer: Meera Patel

Web Officer: RON (EGM needed to fill position)

Events Coordinator: Mary Anthony Yogathas

Hello Members!

As your newly elected President I would just like to thank you all of you that voted for me! I hope you' r e all enjoying your last week of the year and have great summers planned ahead. I hope to make the students much more aware of the society next year and look forward to all of your contributions! As you can see we still have some positions available on the society panel and so if any of you are interested please let me know. Next year should be full of events and we look forward to continuing the Societies sponsorship from CIMA. Fresher's Fayre will be our next event and although its got a long while to go if any of you have any ideas please let me know.

*Have a great summer,
Shivani*

How to find a dissertation topic for an undergraduate dissertation?

Are you thinking about the question you would like to address in the level 3 dissertation?

It is often tempting to think about a journalistic question, e.g., 'Will China replace the US as superpower?' or 'Going Green: Can it revive the UK economy?' You can write very nice newspaper article on these topics but would be hard pressed for a question that can be systematically analysed using economic/financial theory that you have learnt.

An academic question is one that can be answered with systematic analysis and resulting insights that have social significance. It is important to look for a question that is neither too ambitious like 'How can we eradicate poverty?' nor too trivial like 'Increasing electricity generation in the UK?' An example of a good academic question is 'Does foreign aid, or for that matter corruption, has a positive impact (can you think of some reason why corruption can have a positive influence? Market failure?) on economic growth?' If you would like to tackle this question theoretically, there are various growth models in which you can plug in the relevant variable—foreign aid or some measure of corruption, and analyse its impact. Those interested in corporate finance and corporate governance may consider applications of agency theory, e.g., 'what determines managerial compensation?' or 'Does introduction of corporate governance laws improve firm value?'

Finding the appropriate question is extremely important and takes a very long time. The process of finding a good academic question is also the process of finding a possible answer. So, the earlier you start, the better it is. Choose something that you are instinctively interested in and also that it has sound economic/financial theory. You have chosen several modules in level 2 and level 3 – why not choose a topic of your interest from one of these modules? Literatures develop around very specific questions. So, the easiest way to approach the dissertation is to acquaint yourself with the literature that has already articulated a very clear academic question. You could try to go and articulate a new question yourself but that would take a long time. Unfortunately, you would not have the time to articulate a new academic question while doing an undergraduate dissertation at Brunel.

The best way to introduce yourself to a literature is to look for a survey article. A survey article tends to review all the questions and sub-questions in an area and lays them out for you to explore in a dissertation. The survey would also tell you which questions have been fully explored and where there is gap in the literature. A good dissertation is able to explore these remaining gaps in the literature. Journal of Economic Literature, Journal of Economic Perspective, Journal of Economic Surveys are the journals that exclusively publish survey articles. You would also find survey articles in some of the top journals like American Economic Review, Journal of Political Economy, Quarterly Journal of Economics. The field journals (journals dedicated to specialised areas, e.g., Journal of Public Economics, Journal of Labour Economics, Journal of Health Economics, Journal of Macroeconomics, Journal of Development Economics, Journal of Finance) too publish survey articles in specific areas. But make sure that you ascertain that the survey article is sound and is published at a good journal. There are lots of bad articles that get published in Economics.

Also, while you are choosing the topic, please ensure that you revise the background skills that you would require for the dissertation. For an empirical issue, which most of you will undertake, this would require you to refresh your knowledge of empirical techniques (e.g., your knowledge of EC2007) you learnt during the degree scheme or of computer software like Excel, Eviews.

Dissertation is an invaluable component of your job search and also has increasing returns to scale production process. If you invest the fixed cost early enough, you can virtually ensure a good result.

Sarmistha Pal

May 2011

Why We Should Tax the Tall and the Fat

Taxes play a number of roles. First, they are a way to raise revenue to finance public goods. Maintaining law and order or invading another country is not cheap and it is easier to finance such projects by compulsory levies than by voluntary contributions. Second, taxes can be used to discourage undesirable behavior. Many countries, for example, levy 'sin' taxes on alcohol and tobacco to discourage their consumption and thus to reduce their harmful effects. Finally, taxes redistribute income from those who are (relatively) rich to those less fortunate. The taxes that we all pay reflect these various objectives: virtually all of us pay taxes but those of us who are relatively well-off and those who engage in 'sinful' activities such as smoking, drinking or driving a car tend to pay more, sometimes a lot more, than others.

The current tax system, however, is far from perfect. Consider redistribution. Surely, it is only fair to tax the rich and subsidize the poor. Life is a lottery in many respects. If we care about equality, we should therefore redistribute so that those who happen to have drawn the short straw are compensated for their bad luck. This argument, however, only holds if distribution of earnings is sufficiently random. Earnings are not random, however: they reflect one's wage (which may be, to some extent, determined by luck) as well as effort (broadly defined to include both the amount of hours that one works as well as their investment into education and other human capital). If we tax effort, we will discourage people from working and acquiring human capital. Therefore, a fair and egalitarian tax system should tax the income-earning ability but not effort.

The problem is that it is not always easy to tell what part of one's income is due to luck or effort. We do know, however, that some people tend to earn more than others. It is well known that men tend to earn more than women and whites tend to be paid better (and find jobs more easily) than members of ethnic minorities. There is more: a well-known paper by Daniel Hamermesh and Jeff Biddle (*American Economic Review*, 1994) found that attractive people get higher wages. Another study, by David Jonhston (*Economics Letters*, 2010) concludes that women with blond hair get paid more than women with hair of other colors. And, finally, tall men and women also earn more; this is in addition to enjoying other benefits such as having higher education and being on average more confident, happier and less likely to suffer various psychological problems (see the discussion in my own paper with Michèle Belot in *Economics and Human Biology*, 2010).

Therefore, a fair and egalitarian tax system should take into account characteristics that are related to tax-payers' ability to earn high wages. Beauty is highly subjective and hair can be dyed. Height, in contrast, does not change during a person's adult life and can be measured easily. It would make, therefore, an ideal criterion for setting tax rates. This insight is not mine: a similar idea was originally formulated by George Akerlof (*American Economic Review*, 1978) and a recent article by Gregory Mankiw and Matthew Weinzierl (*American Economic Journal: Economic Policy*, 2010) fleshes this proposal out.

Not surprisingly, this idea is controversial: one person that I tried to convince about its merits even likened it with the Nazi predisposition to decide one's fate based on their physical characteristics. Yet the labor market puts a premium on certain physical characteristics, even on those which (unlike education or hair color) workers can do little about. Taxing according to height would only correct for

this inherent unfairness of earnings distribution. Under the present system, two persons with the same income usually pay the same tax. Under height-dependent tax, the taller one would be taxed more. This is fair because, holding everything else constant, the taller person has an easier time to earn a given level of income while the shorter person has to work harder for it.

Now how about the role taxes play with respect to discouraging undesirable behavior? One particularly pressing issue these days is the increasing prevalence of obesity. This has grave consequences: obese people are significantly more likely to suffer from heart disease and diabetes. This, in turn, is costly for the public purse (plus it lowers the wellbeing of obese people and their families). The increase in obesity rates reflects unhealthy life style choices: mainly caloric intake that is too high and too little exercise. We already have so-called sin taxes on alcohol and tobacco that seek to remedy this. In the UK, the VAT rate is higher (20%) for sugary drinks and salty and fatty snacks than for other food (0%). A recent Finnish paper ("Health and distributional effects of differentiated food taxation," by Kaisa Kotakorpi, Jukka Pirttilä, Tommi Härkänen, Pirjo Pietinen, Heli Reinivuo and Ilpo Suoniemi) argues that taxing sugar at a relatively modest rate of 1€ per kilogram would result in a 6% reduction in the prevalence of type-2 diabetes as well as lower incidence of heart disease in Finland. They also argue that these higher sin taxes should be complemented by lower taxes on healthy food such as fruit, veg and fish (which is already the case in the UK).

Sin taxes, however, are a blunt instrument. Taxing sugar would also affect the prices of other foodstuffs (bread, for example). More importantly, this change would hit equally those who are obese and those who are not: two persons can have very similar sugar intakes and yet have very different BMIs (body mass index, a common measure of obesity, computed by dividing one's weight in kilograms by the square of their height in meters), depending, for example, on how much exercise they do. Taxing them based on their BMI, therefore, should be preferable to taxing sugar, fat and/or alcohol content of foodstuffs and beverages.

Income tax should therefore depend on how far one is from the median height (1.75m for men and 1.62m for women in the UK) and also on how far their BMI is from the ideal range of 20-25. One problem, however, is that a person's current BMI reflects their life-long choices. Therefore, linking income tax with the level of BMI would unfairly penalize them for their actions before this reform. To avoid this, the tax could be levied according to one's height and the annual change of BMI. Variations in one's BMI within the 20-25 range should be ignored, while those with BMI above 25 should be taxed more if their BMI increases. This obesity penalty should be further increases for those with BMI over 30 (the threshold for between being overweight and obese).

If this idea catches on, being audited by the tax authorities may soon mean that you would need to strip down to your underwear to have your height and weight checked.

Jan Fidrmuc, Head of Research, Department of Economics and Finance (height 1.83m, BMI 29.6)

Comments and questions: jan.fidrmuc@brunel.ac.uk



Conference news:

Brunel Macro Research Centre (BMRC) annual conference: Tuesday 24 May 2011 Macro and Financial Economics: Theory and Applications

You can download the pdf files of the papers from the QASS site:

http://www.qass.org.uk/callforpapers_brunel_11.htm

Program for the main sessions:

http://www.qass.org.uk/2011-May_Brunel-conference/2011_MainSessions.htm

Program for the parallel sessions:

http://www.qass.org.uk/2011-May_Brunel-conference/2011_ParallelSessions.htm

Centre for Economic Development and Institutions (CEDI) annual conference Thursday 26 May 2011

Venue: Gaskell Building, Room GB239

Programme

10.00 – 10.25: coffee

10.25 – 10.30: welcome

10.30 - 11.25: Abigail Barr (University of Oxford), 'Using lab-type experiments to investigate public servant motivation and accountability relationships.'

Discussant: Fernand Gobet (Dept. of Psychology, Brunel)

11.25 – 12.20: Peter Martinsson (University of Gothenburg), 'What influences donations? Field experimental evidence from Cahuita National Park'

Discussant: Juergen Bracht (University of Aberdeen)

12.20 – 1.10: lunch

1.10 - 2.05: Daniel Clarke (University of Oxford), 'Microinsurance decisions: Evidence from Ethiopia.'

Discussant: Ioana Chioveanu (Brunel University)

2.05 – 3.00: Pieter Serneels (University of East Anglia), 'Experimental evidence on the impact of malaria on agricultural worker productivity, labour supply and earnings' (co-authors: Andrew Dillon and Jed Friedman)

Discussant: Yannis Georgellis (Kingston University)

3.00 – 3.30: tea

3.30 - 4.25: Michal Bauer (Charles University, Prague), 'Warfare increases egalitarian and parochial motivations' (co-authors: Alessandra Cassar, Julie Chytilova and Joseph Henrich)

Discussant: Michelle Baddeley (Cambridge University)

4.25 – 5.20: Philip Verwimp (ECARES, Brussels), 'Does conflict affect preferences? Evidence from field experiments in Burundi.'

Discussant: Jan Fidrmuc (Brunel University)

Centre for Empirical Finance (CEF) Annual Conference 25 May 2011

on “Empirical Finance: Some Recent Methodological Developments and Applications”

Venue Darwin Room, Hamilton Centre, Brunel University, West London on 25 May 2011

Programme

10.00 Registration and coffee

10.30-11.30 Karim Abadir, Imperial College

"Lies, Damned Lies, and Statistics? Examples From Finance and Economics"

11.30-12.30 George Kapetanios, Queen Mary, London

“Forecasting financial distress in emerging markets: a dynamic probit analysis”

12.30-13.30 Lunch

13.30-14.30 Walter Distaso, Imperial College

“Conditional Alpha and Realized Betas”

14.30-15.30 Luis Gil-Alana, University of Pamplona

“Fractional Integration and Cointegration in US Financial Time Series Data”

15.30-16.00 coffee break

16.00-17.00 Michael Funke, Hamburg University

“Off-the-record target zones: Theory with an application to Hong Kong's currency board”

17.00-18.00 Carlo Altavilla, University of Naples “Parthenope”

”Monetary Policy Analysis in Real-Time. Vintage Combination from a Real-Time Dataset”