

# MIND | WORK

LEADING SCHOLARSHIP FROM SANTA CLARA UNIVERSITY SCHOOL OF BUSINESS

## From the Dean

Thomas Carlyle called it ‘the dismal science,’ but he was off-point because the study of economics in the Leavey School of Business is as intriguing, challenging, important, and relevant to the average citizen as it is to the scholar.

In this issue of *Mind|Work*, you’ll learn what our Santa Clara University economists have to say about global warming and Durfar, nuclear brinkmanship, and racial wage discrimination as a legacy of slavery, among others. From examining welfare-to-work programs to investments in emerging economies, our economists demonstrate that their discipline informs our mission to educate men and women of competence, conscience, and compassion as leaders who can make a difference in the world. As our faculty uncover root causes of poverty and plenty around the world, their students, equipped with this knowledge, learn to affect change at basic levels.

These articles about current economic thinking, like all features in each issue of ▷

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**DON'T BLAME THE WEATHER:** Michael Kevane has found scant evidence that climate change is responsible for widespread violence in the Darfur region of Sudan. On the wall behind him are tabaq (woven food plate covers) and camel-ornament gourds from Sudan.

## Was It the Weather?

### Lower Rainfall-Darfur Violence Connection Tenuous

The conflict in Darfur — which has killed 200,000 people and uprooted more than two million since it began in 2003 — has been cited as a consequence of global warming by, among others, former Vice President Al Gore and United Nations Secretary General Ban Ki-moon. They argue, in essence, that climate change has reduced rainfall in this part of Africa, causing a violent confrontation over scarce resources. Michael Kevane, chair of the Department of Economics at SCU's Leavey School of Business, disagrees.

“There’s no reason to say this is the world’s first climate-change crisis,” Kevane says, “and doing that takes away responsibility for some of the actors responsible for the violence.” ▷

# was it the weather?

Along with Leslie Gray of SCU's Environmental Studies Institute, Kevane has written a paper, "Rainfall in Darfur Prior to the Conflict of 2003." It was presented at a political economy workshop at Stanford in December 2007 and is now being finalized for future publication.

The paper should not be taken as an anti-global warming document, he says. Rather, it attempts to demonstrate that the rainfall records for the area, backed by other information, show that in this case the climate change argument "has no compelling evidence at present."

Darfur is a fairly dry region in Western Sudan, where average rainfall is 6-8 inches per year in the north and 9-10 inches in the south. In the 30-year period preceding the conflict, from 1972-2002, rainfall in Northern Darfur was down from the prior 30-year period, which is the basis for the climate-change argument.

But Kevane argues the decline is not out of line with historic rainfall variations that people have coped with before, and that no violence occurred after the exceptionally dry years of 1984 and 1990, which would argue against the idea of a "weather shock" starting the violence. Furthermore, satellite images culled from the last 25 years show an

overall greening trend that suggests the area's biomass has been holding up despite the reduced rain.

The climate-change theory, he says, also doesn't take into account how people adapt to different weather patterns. "There's a wide range of livelihood strategies that people can pursue. One of them is urbanization, because

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"Calling this the world's climate-change crisis takes away responsibility for some of the actors responsible for the violence."

Michael Kevane  
Chair, Department of Economics

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people in cities are less dependent on rainfall. In fact, during this period, we've seen a lot of circular migration with people moving back and forth between the cities and the countryside."

He adds that the largest cities in Darfur have nearly quadrupled in size since 1972 and now have populations in the 200,000 range.

Kevane and Gray have both spent considerable time in Sudan and Kevane is generally considered a leading economic authority on that nation. In his view, the explanation for the violence is human behavior rather than the weather: the governmental elite, based in the capital of Khartoum, has consistently marginalized peripheral groups, such as the people of Darfur, and has repeatedly shown its willingness to use large-scale violence against civilian populations.

"There has been a 50-year pattern of violence that has enmeshed that part of Africa — Libya, Chad, Sudan," he says. "The political explanation for the violence is that an attack on the airport by rebel groups in February 2003 triggered a reaction that led to the *janjawid* (an irregular militia based in the north) attacking the populations in the south."

"Every Sudan expert I know of is comfortable with the political explanation." ▶

## Real Estate and Recession

### A Peak in Land Values Can Predict the Next Downturn

You could look it up. Back in 1997, Fred Foldvary published an article in the *American Journal of Economics and Sociology* that predicted a recession in 2008.

Now that it seems he's right, Foldvary, lecturer in Economics at SCU's Leavey School of Business, allows that the prediction could have been off by a year or two, but that the reason for making it — the connection between real estate cycles and the general business cycle — still holds true.

"Macroeconomists are not always familiar with the real estate literature," Foldvary observes, "and I wanted to use it to come up with a better explanation for the causes of business downturns." Not all are real estate-related, he says, but there is a clear connection between the end of a real estate boom and the start of a recession.

Foldvary outlined his analysis in a paper called "The Real Estate Cycle and the Depression of 2008," published in the journal *GroundSwell*. It was adapted from a talk he gave to the

graduate business student Real Estate Network in the spring of 2007. He had previously presented a "Yellow Pad" economics-department paper and seminar, "A Synthesis of the Austrian-school and the Georgist Theories of the Business Cycle, and its Empirical Testing" in Fall quarter 2007.

Drawing on the studies of real estate economist Homer Hoyt, who identified an 18-year cycle of real estate in Chicago,



**LAND AND THE ECONOMY:** Fred Foldvary's research traces an 18-year cycle in real estate values and indicates that when land values peak, an economic recession can be just around the corner.

Foldvary looked at the year of the last real estate bust and came up with the prediction for 2008.

Typically, Foldvary says, real estate values have peaked a year or two before a recession. Up to that point they have dominated the economic boom that preceded the depression, so a real estate slowdown is a harbinger of things to come for the overall economy.

A variety of factors drive the overall real estate boom, including low interest rates, a limited supply of land, and the "humongous" public subsidy in the form of taxpayer-supported infrastructure and tax breaks for homeowners, Foldvary argues.

Through all this, however, it is the price of land that's going up, not the buildings, and the continued increase in prices can be maintained only if there is a belief that it will continue.

Of course, Foldvary writes, it always runs into a reality check. "Mortgages are paid from wages and profits, so eventually real estate prices stop rising." When that happens, sales volume drops, new construction is dampened, the demand for furniture, appliances and office equipment goes down, unemployment and interest rates rise, and a recession is around the corner.

In the current situation it's apt to be a nasty one, he predicts, because the growth in secondary loan markets made the boom bigger than usual, so the downturn is apt to be correspondingly more severe.

While he expects the recession to play itself out in the absence of bad policy decisions, Foldvary doesn't expect policymakers

to learn much from it. "One thing I can predict with absolute confidence," he writes, "is that government chiefs and even most economists will not learn the right lessons from the collapse, and history will repeat itself as it always has."

What are the right lessons? Foldvary says many are contained in the work of the 19th century author Henry George, who wrote a book, *Progress and Poverty*, that called for a single tax on land. While that may be too simple, Foldvary says a higher tax on land

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"There is a clear connection between the end of a real estate boom and the start of a recession."

*Fred Foldvary*

Lecturer in Economics

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would have the benefit of dampening fluctuations in the real estate cycle and creating less of a boom-and-bust situation.

But given the lobbying power of the real estate industry and the voting power of mortgage-deducting homeowners, is there any chance of that happening?

"No," Foldvary says. "Zero." ▀

# Following the Money

## Why Asian Capital Is Moving to Wealthier Nations

Ever since the Asian financial crisis of 1997, investment rates have remained lower in many East Asian countries in spite of the fact that many of the nations have high savings rates and available funds. Instead, much of that savings has been invested abroad, particularly in the United States.

A popular (at least in some sectors) explanation for this is that the economic imperatives of developed industrial nations are adversely affecting capital investment in Southeast Asia. German Chancellor Angela Merkel alluded to this in discussions of the global economic imbalances and the responsibilities of the United States during the G-8 summit last year.

"The idea that U.S. borrowing is sucking funds out of the emerging economies has been a centerpiece of such discussions," notes Helen Popper, Santa Clara University associate professor of economics. "But in looking into this we've found that — despite its heavy borrowing — the role of the United States has been limited. U.S. macroeconomic conditions seem to play little or no role in shaping the behavior of any of the major categories of private capital flows."

In a paper titled "Capital Flows, Capitalization, and Openness in East Asian Emerging Economies," Popper and her co-author, Alex Mandilaras of the University of Surrey, UK, reach a different conclusion.

Rather than being shaped by the more developed industrial nations, investment patterns in these emerging economies seem to be affected more by the relative openness and accessibility of their own markets, Popper and Mandilaras found.

On the surface, it would seem that Asian money should be flowing into Asian countries where it could earn a higher return. According to the International Monetary Fund, the return to capital for the decade between 1994-2003 was 15 percent in emerging Asia, as opposed



**WHERE THE MONEY GOES AND WHY:** Helen Popper has examined the flow of Asian capital and concluded it leaves the region because of poor financial infrastructure, not U.S. economic conditions.

to 8 percent in Europe and 10 percent in the United States.

Since capital would be expected to flow to the area of highest return, this has been a long-standing puzzle, but Popper found

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“When emerging economies lack sufficient financial infrastructure, savers in those countries send their assets abroad.”

*Helen Popper*

Associate Professor of Economics

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that while U.S. conditions played a part in determining overall economic activity in the region, the larger role for capital flows was played by the inefficiency of the financial

markets in the nations themselves. In essence, the Asian nations are importing financial services from more developed nations.

“When emerging economies lack sufficient financial infrastructure to match borrowers and lenders efficiently in their own countries, savers in those countries send their assets abroad, despite high domestic returns to capital,” she concludes. The good news for the Asian countries is that as their financial markets mature, they can expect to retain more of the native capital.

Economists elsewhere have done theoretical work speculating that internal financial infrastructure may be at the root of the Asian financial situation. What Popper and Mandilaras have done is compile and analyze a broad range of data to determine whether that approach holds water empirically.

After crunching the numbers, they found that what matters most in the investment patterns of these nations is their internal situation.

“What I think is interesting,” Popper says, “is that this is not a story about the United States. It’s about the lack of access and fully functioning financial infrastructure within the region itself.” ▶

# Going With the New Project

## How Information Needs Can Drive Product Decisions

**M**innesota Mining and Manufacturing (3M) has had a company rule that 10 percent of annual sales must come from projects introduced in the past year and 30 percent of sales from projects less than four years old. It was faithful to that policy even though such a rule might, in some cases, result in a less-profitable newer project being selected over an existing product with an established profit record.

The history of corporations holds a number of such examples, and Dongsoo Shin, associate professor of economics in the Leavey School of Business, is offering some reasons for this phenomenon. It is a part of his overall research emphasis on extending research on information-gathering issues within organizations using rigorous analytical tools and game theory.

In a paper titled “Information Acquisition and Optimal Project Management,” which has been accepted for publication in the *International Journal of Industrial Organization*, Shin argues that in many cases such decisions have a lot to do with the processes and incentives that govern a corporation’s acquisition of information.

“There needs to be a reward for the agent who gathers information on the new project to get the best information and report it truthfully,” Shin says. For the fact-finding agent, often a sub-unit within the company, that reward takes the form of “information rent.” In other words, having gone to great effort to get the information, the agent gets a payback on his or her knowledge, which becomes more valuable to the company.

But “information rent” can be provided to the agent only if the company moves forward with the new project, thus creating value for acquiring the information. If the information-gathering agent anticipates that the company is unlikely to choose the new project, there’s less incentive to aggressively collect necessary information (or aggressively engage in R&D activity).

Shin contends — and has developed a detailed mathematical mechanism to make the point — that this, in turn, creates an incentive for top company executives to significantly commit to the new project or technology earlier on, simply to get the best possible information. Having done that, they are unlikely to change their minds once a new project is chosen over more conventional ones. An example would be Sony’s insistence on using the Chromatron picture-tube technology in the 1960s, even when its planning team warned that it would be more expensive and less profitable than the tubes the company was already using.

Looking at the options, Shin concludes that the optimal process for acquiring information on new projects — that is, the one likely to generate the best outcome — is most likely to occur when the information-gathering task on a new project is partially integrated to the implementation task, thus partially linking the information-gathering reward to the final outcome.

The reason the partial mix approach works better is twofold, he says. If the tasks are totally separated, the agent who gathers the information never gets to implement the project, and so has no incentive to gather information in the first place. On the other hand, if information-gathering and implementation are always integrated (the fact-finder gets to implement the new project), the company is providing too much information rent. The optimal mechanism, therefore, is “partial integration of the two tasks.”

“As the top management you must commit to this mechanism,” Shin explains. “The moment you do so, the expected payoff for information becomes higher and cost of information becomes lower, and that drives the sub-unit of the company to pursue it and report it better.” ▶



**POWER OF INFORMATION:** Dongsoo Shin’s research looks at the relationships between information incentives and new-product business decisions in today’s corporate world.



**LET THE DATA SPEAK:** Mitchener took more than a year to hand-collect information from around the world.

## The Effect of Empire In the Matter of Trade, the Impact Was Substantial

Back in the day when the sun never set on the British Empire, England — along with other European countries, and to a lesser extent the United States — was widely assumed to have reaped considerable economic benefit from their colonies. But what were the economic effects of empire?

For more than a century that question has largely gone unanswered, in part owing to a lack of accumulated hard information to measure the impact of empire relationships on economic outcomes. Now Kris James Mitchener, associate professor of economics at the School of Business, has worked with a colleague to compile the information and reach a conclusion with respect to how empires impacted trade.

“Once we looked at the data and took into account many other influences, it turns out that being part of an empire had a very large effect on trade flows,” Mitchener observes. “On average,

it doubled total trade relative to countries not in empires.”

Mitchener and Marc Weidenmier of Claremont McKenna College outlined their findings in a paper called “Trade and Empire,” which is forthcoming in *Economic Journal*, published by the Royal Economic Society.

In reaching a conclusion about empire’s positive impact on trade, Mitchener stresses that he is not advocating imperialism as a form of political organization and that the ultimate effects of empire on the development and growth of ex-colonies are likely ambiguous. Rather the researchers are simply attempting to unearth and evaluate economic relationships that have eluded scholars thus far. “We are collecting data to answer questions that previous scholars have not attempted to

quantify. We let the data speak rather than imposing priors on what we expect the outcome to be,” he says.

Compiling the information in the first place was a daunting task. Mitchener and Weidenmier focused on the period from 1870-1913, which is generally considered the Age of High Imperialism. Fortunately for them, the British government at the time was an efficient bureaucracy and had compiled extensive statistical abstracts on its own trade and that of other countries, including neighboring European nations with colonies.

Unfortunately, those Board of Trade statistics were available only in hard copy in scattered locations, from Berkeley to Harvard, to various places in England. Mitchener says

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The colonial legacy continues to exert an influence on trade flows today.

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it took more than a year to hand-collect the information (along with supplementary data from France) and evaluate it. But in the end, they had trade data and other country or colony information on 21,000 different trade pairings, including 880 distinct country pairings, which reflected more than 90 percent of the global trade during this period.

Having this wealth of information enabled them to evaluate trade patterns within and without empires and to factor in

# Why It Didn't Happen

## The Limits of Rationality in Preventing Nuclear War

other issues such as wars, currency unions, the gold standard, country size, distance, and various geographical indicators. While some of these also influenced trade in a statistically meaningful way, Mitchener says that empire was the most important institutional factor.

So why did empire increase trade? Their study highlights the importance of two channels, in particular. The colonial connection led to lower transaction costs via the creation of common currency areas within empires, the use of a shared language, and the development of lasting connections (social networks) among traders. Empires also established preferential trade agreements, which sometimes created favorable terms for trade within empires and discriminated against goods from other countries. Mitchener states that research related to his suggests that the colonial legacy continues to exert an influence on trade flows today.

Mitchener thinks the statistical information he and Weidenmier have compiled should provide a basis for other research into the economic relationships of the first era of globalization: 1870-1913. As part of the three-year National Science Foundation grant Mitchener received to work on this project and related research, he and his collaborators will put all their data online so that future scholars will be able to make use of the rich information they have collected.

"No one had ever tried to measure the contemporaneous effect of empire on trade," Mitchener says. "Before we collected these data from archival sources, you couldn't really properly answer this question. We were fortunate that British civil servants were so fastidious in originally compiling these data more than 100 years ago." ▶



**GAME THEORY AND WAR:** Alexander Field has done a detailed examination of why mathematical game theory failed to predict the occurrence of nuclear war or explain why it hasn't happened yet.

**W**ith his death approaching in 1957, the great mathematician John von Neumann confided to a friend that he was "absolutely certain" there would be a nuclear war that would end all human life. He wasn't alone in that thinking. Soon afterward, the British novelist C.P. Snow told the *New York Times* that without massive and speedy disarmament, it was a "mathematical certainty" there would be a nuclear war.

Von Neumann, Snow and many others turned out to be wrong (at least so far), and in a paper just completed, "Schelling, Irrationality and the Event That Didn't Occur," Alexander J. Field looks at some of the reasons. Field, the Michel and Mary Orradre Professor of

Economics, concludes that mathematical theory failed in predicting the answer to the greatest life-and-death question of the twentieth century.

"When you look back at the Cold War period, it's surprising how widespread and unrelenting was the pressure to launch a nuclear first strike," Field says. "Even a pacifist like Bertrand Russell pushed for it; the logic was so overwhelming it would happen."

It's the failure of that logic to predict events that interests Field, and he argues in considerable detail that the economist and Nobel Prize winner Thomas Schelling, failed when he tried ▶

## why it didn't happen

to buttress the case for deterrence using game theory, because game theory provides a more compelling rationale for a first strike.

Game theory assumes that the players (in this case, the nuclear superpowers) will both behave rationally in the sense of acting efficiently to advance their material self-interest. It might be rational for you not to attack because you feared retaliation, but this requires attributing irrationality to your opponent who must in turn, if deterred,

What instead seems to have overridden the logic for a first strike and allowed mutual deterrence to work were more human factors: We do often hesitate before striking first and we are ready to hit back. "The failure accurately to predict is not due to a defect in the logic," Field writes in his paper. "The problem is with the implied behavioral assumptions."

Field argues that within the politics of academia there is a premium placed on using

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"What overrode the logic for a first strike and allowed mutual deterrence to work were more human factors."

*Alexander Field*

Michael and Mary Orradre Professor of Economics

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attribute some irrationality to you. One ends up assuming that you and your opponent are both rational and irrational — a theoretically incoherent position, but one that might have some truth.

Followed ruthlessly to its conclusion, game theoretic reasoning offers little support for holding off until attacked and an overwhelming case for first strike. Von Neumann himself believed this, arguing, with respect to the Soviets, "If you say why not bomb them tomorrow, I say why not today? If you say today at 5 o'clock, I say why not one o'clock." A rational opponent should be attacking you already and in any event would not retaliate if you hit first. In fact, Field notes, during the Cold War there were ongoing concerns on the part of national security planners about whether a president would have the will to retaliate after a first strike by the other side when the retaliation would serve no purpose other than vengeance.

game theory to explore real-world problems because it presumably brings a more analytical focus to the discussion. The problem is that in some cases, such as analyzing nuclear deterrence, the approach doesn't yield useful results because of what it leaves out.

"The bottom line of this paper," Field says, "is that nuclear war has been avoided not because we were rational, but because we were human." ▶

### Additional Research Papers from the Economics Faculty

The papers below are posted on the Social Science Research Network Web site ([www.ssrn.com](http://www.ssrn.com); requires free registration). On the site, you can search by title or abstract ID#, or by author and review more papers than we have listed below.

#### Carolyn Evans

Tight Clothing: How the MFA Affects Asian Apparel Exports (ID# 492363)

#### Alexander Field

Beyond Foraging: Evolutionary Theory, Institutional Variation, and Economic Performance (1095944)

#### Fred Foldvary

The Ultimate Tax Reform: Public Revenue from Land Rent (1103586)

#### John Ifcher

An Overlooked Impact of Welfare Reform: The Effect on General Assistance Recipients (1096613)

#### Michael Kevane

Titanium Hoes? Farmers, Wealth, and Higher Yields in Western Sudan (1115512)

#### Kris Mitchener

The Great Depression as a Credit Boom Gone Wrong (959644)

#### Helen Popper

Inflation and Relative Price Dispersion in Equity Markets, Goods and Services Markets (259624)

#### Dongsoo Shin

Optimal Task Design: To Integrate or Separate Planning and Implementation? (899192)

#### William Sundstrom

Decline and Rise of Interstate Migration in the United States (425593)

# The Pursuit of Happiness

## How Working Mothers Feel After Welfare Reform

In the decade since President Bill Clinton signed the welfare reform bill of 1996, the evidence indicates that the new law reduced welfare rolls and put more single mothers into the work force. But has it made them happier?

No one has really asked until now. But in a working paper titled “The Happiness of Single Mothers After Welfare Reform,” John Ifcher, senior lecturer in the SCU Economics Department, tackles the question.

“From the perspective of government, welfare reform has been a success,” Ifcher says. “But what about the mothers themselves? Would it be fair to solve the problems of the system at the expense of less-educated, single working mothers?”

Ifcher’s tentative conclusion, based on a close reading of two separate but widely respected surveys of subjective well-being, is that the percentage of single mothers who say they’re happy has increased a bit since welfare reform became law.

“The numbers move, but this seems to be a break,” Ifcher contends. “You can clearly rule out that they’re worse off, and while we’re not finished totally, the indicators are that they are happier on average.”

His research draws on two long-standing surveys that measure self-judged well-being: the General Social Survey (GSS), which has been conducted nearly every two years since 1972, and the World Values Survey (WVS), which has been taken on a regular basis since 1985.

Because neither survey specifically identifies welfare mothers, Ifcher uses the figures for single mothers with a high school education or less — that is, the women who fit the demographic most affected by the welfare reform law. He says, and most colleagues so far have agreed, that this is an acceptable proxy.



**QUANTIFYING WELL-BEING:** John Ifcher has looked at nationwide surveys of subjective well-being to attempt to determine how single mothers view their lives since the passage of the 1996 welfare reform bill.

Happiness is measured by the number of respondents who describe themselves as being either “very happy” or the next level down, “pretty happy” in the GSS or “quite happy” in the WVS. In the GSS, 78 percent of less-

Ifcher notes. And, he says, there was no increase in reported well-being among members of a comparison group — less-educated single women without children — in the WVS and GSS over the same time period, thus bolstering the theory that welfare reform and a change in employment status increased happiness.

In some respects, that finding contradicts standard economic theory, which assumes that hours worked reduce well-being. It also seems to go against the idea that quality of life would suffer as working single mothers struggle to deal with childcare, manage their busy schedules, and get adequate sleep.

On the other hand, Ifcher observes, surveys have generally shown that people are happier when they’re working, and that seems to have been the case here.

In combination with other surveys showing that welfare reform has reduced welfare rolls without harming the financial status of the mothers affected, Ifcher’s work would seem to back up the contention that welfare reform was a success. But, as he puts it, there’s another avenue to explore:

“This still leaves one very important question unanswered: the impact of these policies on children,” he says. ■

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The finding that welfare reform and a change in employment status may increase happiness contradicts standard economic theory.

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educated single mothers put themselves in those categories, up from 75 percent, and in the WVS the figure is 96 percent, up from 82 percent.

“It was striking that an increase was found in two high-quality nationally representative surveys that are unrelated to each other,”

# A Bias in the System

Types of Government May Be Related to Trade Protection



**DEMOCRACY AND FREE TRADE:** Carolyn L. Evans has found evidence that “majoritarian” democratic governments with strong district interests are more likely to support protectionist trade policies.

In an increasingly globalized world, trade and tariff policy can have vast consequences, yet there has been surprisingly little research into how the structure of the democratic governments that make those policies may be related to policy outcomes.

Carolyn L. Evans, associate professor of economics at SCU's Leavey School of Business, is contributing to the research on relationships between electoral systems and trade policy with her recent paper, “A Protectionist Bias in Majoritarian Politics: An Empirical Investigation.” The paper — completed in December 2007 and now under review — supports the theory that countries

with “majoritarian” forms of government, such as the United States, tend to take more protectionist positions than countries, such as the Netherlands, with “proportional” systems of government.

Evans observes that a standard assumption of most economists is that the best outcome for many countries is free trade with no tariffs. “If you can produce a product in your country for ten dollars or import it for five, it's better to import it and focus on producing goods where you can be more competitive,” she says.

In a majoritarian system of government, where legislators are elected by specific districts, which they solely represent, that's

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The implications could affect nations re-examining their governmental systems as well as emerging nations in the process of developing a constitution.

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less likely to happen, Evans found. In the situation just described, legislators may direct tariff protection to their home districts and such protection would raise the price of the imported product to a level closer to the domestic one.

For example, she notes, “If you have a congressman in a district with a given industry, it's in his interest to protect that industry, since he's accountable only to the people in that district — even though it means that everyone else in the country pays more for that industry's product.”

In a proportional political system, where legislators are either elected by the country as a whole or proportionally by parties in specific districts, there seems to be less of a tendency for protectionist policies. Evans says that may be because when a politician is elected by the whole country, he or she may tend to be more responsive to the overall national interest, rather than the interests of specific groups.

This general theory was put out in a 2005 paper by Gene Grossman and Elhanan Helpman, and what Evans has done is to evaluate tariff information from a number of democratic countries to see if the theory holds up.

Doing this required extensive formulas and tables to take into account other factors, such as a country's legal origins, colonial history, per capita income level and geographic location. "You have to be sure that the bias toward protection is because of the governmental system and not some other factor," she says.

The implications of this research could affect nations re-examining their governmental systems as well as emerging nations in the process of developing a constitution. For such countries it could be important to understand the possible relationship between forms of democratic government and trade policy.

Evans, who served as an economist with the Federal Reserve Bank of New York, the White House Council of Economic Advisers, and the Federal Reserve Board of Governors before coming to SCU, sees that trade issues

such as protective tariffs have a serious real-world impact.

"When I was with the Council of Economic Advisers, I observed first-hand the interest that many different groups take in trade policy and its effects," she says. "My research is trying to provide some insight into how the structure of government may be related to trade policy decisions in different countries." ▶

## A Pattern of Wage Discrimination Where and Why It Persisted in the Pre-Civil Rights South

U.S. Census figures show that in 1939 the median weekly earning of white men in the American South with less than a high school education was \$17.50. For black workers, the figure was \$9.62 — 38 cents a week less than the federal minimum wage, which didn't apply to agricultural employees.

The existence of such a significant wage gap has been well known to economists, but William A. Sundstrom, professor of economics and associate provost for faculty development at Santa Clara University, has been digging deeper into the available information. His findings, "The Geography of Wage Discrimination in the Pre-Civil Rights South," were published in the June 2007 issue of the *Journal of Economic History*.

Sundstrom concludes that the severity of such discrimination varied even within the region, but with certain factors being fairly consistent. "Ideology and culture mattered," he writes. "Areas with a strong tradition of paternalistic and hierarchical race relations, as well as a potentially tight-knit white employing class, did exhibit greater wage discrimination."

For the purpose of Sundstrom's research, the mother lode of information was the 1940 U.S. Census — the first ever to report wage

and income data. It enabled him to break down income figures by small sets of counties across the south, controlling for various factors known to affect wages, such as levels of education.

To get additional insight into racial attitudes, Sundstrom then used a county-by-county breakdown of the vote for Strom Thurmond in the presidential election of 1948, eight years later. Thurmond ran on an explicitly segregationist platform in protest of the Democratic party's civil rights position that year, so the vote he received could be taken as an indication of the depth of that feeling in an area.

Wage discrimination, Sundstrom found, was generally worse in areas that had a strong plantation history, in areas where Thurmond did well in the 1948 election, and in areas where blacks made up a larger proportion of the work force. It primarily took the form of a division of labor that limited the kinds of jobs open to black workers.

"In plantation areas that had a lot of slave labor, there was a history of social pressure and collective enforcement of discrimination by white society," he observes. "History matters."

Free-market theorists would argue that in an open, unregulated marketplace, economic ▶



### UNDERSTANDING WAGE DISCRIMINATION:

William Sundstrom has looked at census data and election returns to pinpoint the causes and conditions that led to wage discrimination in the South before the Civil Rights movement.

discrimination would eventually disappear as competitive employers tried to hire and keep the best employees. Yet in the South, that didn't really begin to happen until the passage of federal civil rights laws (including employment discrimination laws) in the 1960s.

Instead, the discrimination persisted, abetted by historical traditions, local racial attitudes, and a large pool of available black workers. The latter consideration actually made some sort of market sense.

"According to the market theory of discrimination you would expect to see this," Sundstrom says. "When there are more blacks in the labor pool, black workers are forced to seek jobs from the more bigoted white bosses, who pay them less."

Sundstrom sees this paper as supplementing other research he has done African-American labor market discrimination. He previously had looked at unemployment

trends (blacks typically have double the unemployment of whites), but found that the wage discrimination issue continues to pose especially challenging questions for economists. By looking at detailed patterns, he hopes to shed light on why discrimination occurs and lasts.

"This is part of a set of literature that has convinced me that discrimination can persist in labor markets over time, contrary to free market views," Sundstrom says. "That leaves a place for public policy, such as equal employment opportunity laws."

It also raises new questions begging for further research. "If wage discrimination varied so dramatically and persistently across the South," Sundstrom asks, "what prevented black workers from picking up and moving to locations where they were treated more favorably?" ▶

*Mind|Work*, are just a sample of the broad inquiry conducted by Leavey School of Business researchers. Many of you have asked "Where can we learn more?" I'm pleased to point you to our companion Web site ([www.scu.edu/business/mindwork/](http://www.scu.edu/business/mindwork/)) where you can read the original research papers of these and other Leavey scholars and find out how to contact individual faculty members to explore some ideas more fully.

As always, let us know what you think about this issue and the topics covered. We look forward to hearing from you.

All the best,



Barry Z. Posner, Ph.D.

Dean and Professor of Leadership

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