

CRONY CAPITALISM



What's Inside

High school essay
contest winner on crony
capitalism

Government job creation

CEO pay levels



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Our mission is to improve the quality of life for Canadians, their families and future generations by studying, measuring and broadly communicating the effects of government policies, entrepreneurship and choice on their well-being.

WELCOME!



Dear Readers,

In the spring 2015 edition of *Canadian Student Review* we are pleased to publish the winning high-school essay from our 2014 Student Essay Contest, entitled “The rise of crony capitalism: how government and business gain at the taxpayers’ expense.” There is still time to enter our 2015 Essay Contest on “National Security and the Role of Government: Safety vs. Privacy in a Technological Age.” The submission deadline is June 1, 2015, and we have 3 different prize categories (Graduate, Undergraduate, and High School). You can find more information on our website: www.studentessaycontest.org.

This issue of *Canadian Student Review* also features thought-provoking articles on the minimum wage, limiting CEO pay levels, and the first article from our regular high-school contributor on government job creation.

We are also including a recent video we produced on medical wait times and a commentary that was published in the *National Post* about oil prices.

You may notice this issue of *CSR* has a different look from previous issues. We are excited to present our new design for *CSR*, and we welcome your feedback on the new look. We hope you enjoy reading these articles.

Best,

Claire Jones

Editor, *Canadian Student Review*



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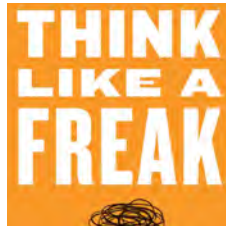


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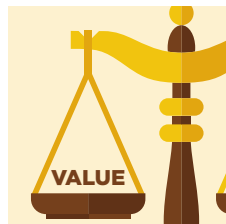


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SCRATCH OUT THE “CAPITALISM”; “CRONY” SUFFICES

Yi Zona Xu and Katina Zheng

High School essay contest 1st place winner

Following the automotive and banking industry bailouts in America after the 2008 financial crisis, fingers have been pointed at the Obama for favoring “cronies” over quicker economic recovery. Expansionary monetary policy is not unheard of, nor is government intervention. However, with one-time global economic strongholds Europe and America flailing under socio-economic forces, the public needs someone to blame. The culprit: crony capitalism.

Guilty verdict

“Crony capitalism” is by no means a newly-observed phenomenon and its undertones trace back to the 1624 *Darcy v. Allein* case that prohibited English monarchies from granting exclusive rights to produce goods (Calabresi and Price, 2014: 8). The term “crony capitalism” itself takes on a variety of nuanced interpretations. Commonly, it is seen as collusion between businesses and government, with firms getting help from high places. However, arguably just as prevalent is a form

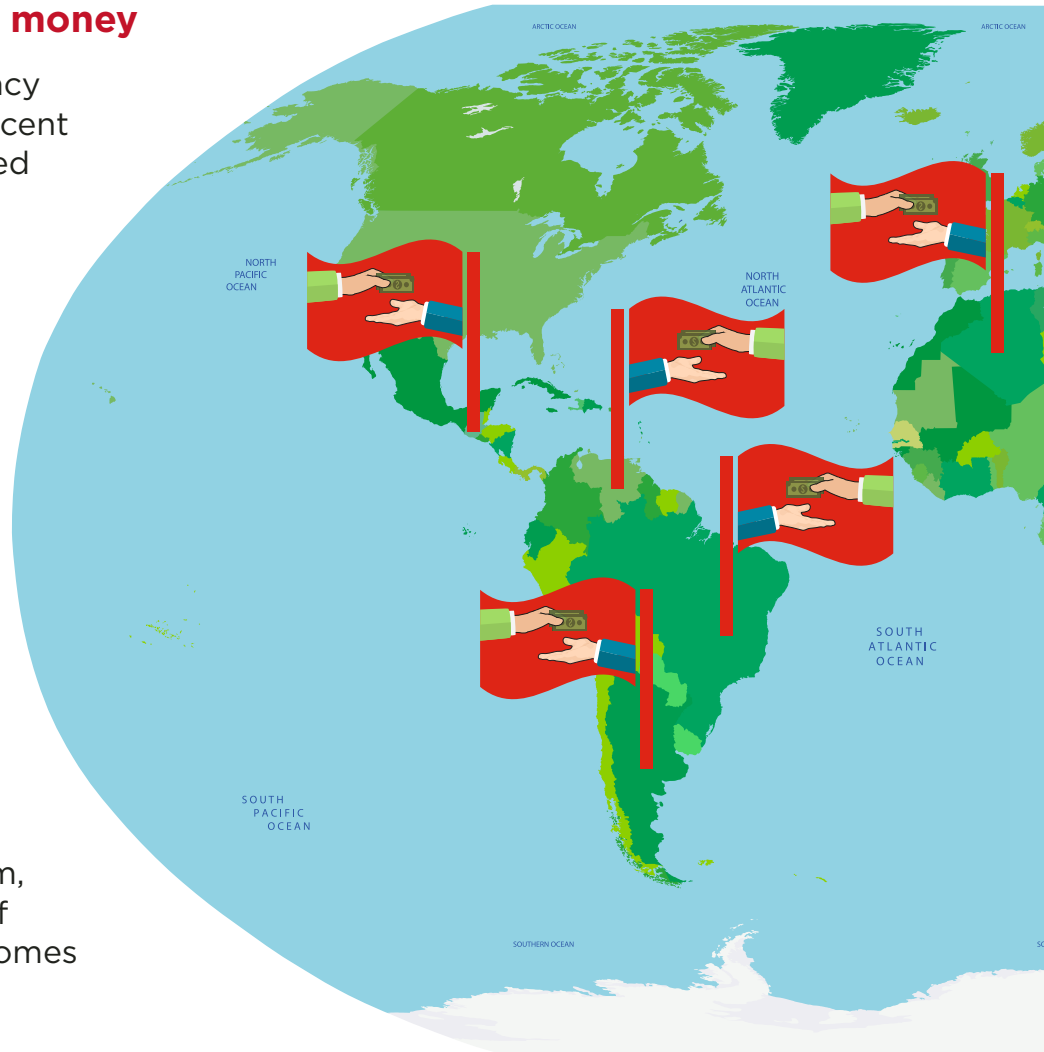
of “implicit cronyism,” where firms manipulate regulatory systems already in place to advance their goals.

Once cronyism takes hold, businesses are no longer rewarded based on quality of output, but rather on how many government strings they can pull.

In either case, once cronyism takes hold, businesses are no longer rewarded based on quality of output, but rather on how many strings they can pull in the seat of government. Meritocracy yields to kleptocracy, and efficiency is lost with the erection of regulatory barriers that distort the price mechanism. Ultimately, a market with asymmetric information results, along with the gradual degradation of the quality of goods and services produced. Cronyism-led growth is fundamentally unsustainable, often leading to social unrest and waste of resources in unproductive rent-seeking behaviour. What can be affirmed is that free markets are not to be blamed for stagnating economic figures; cronyism is.

Explicitly getting the money

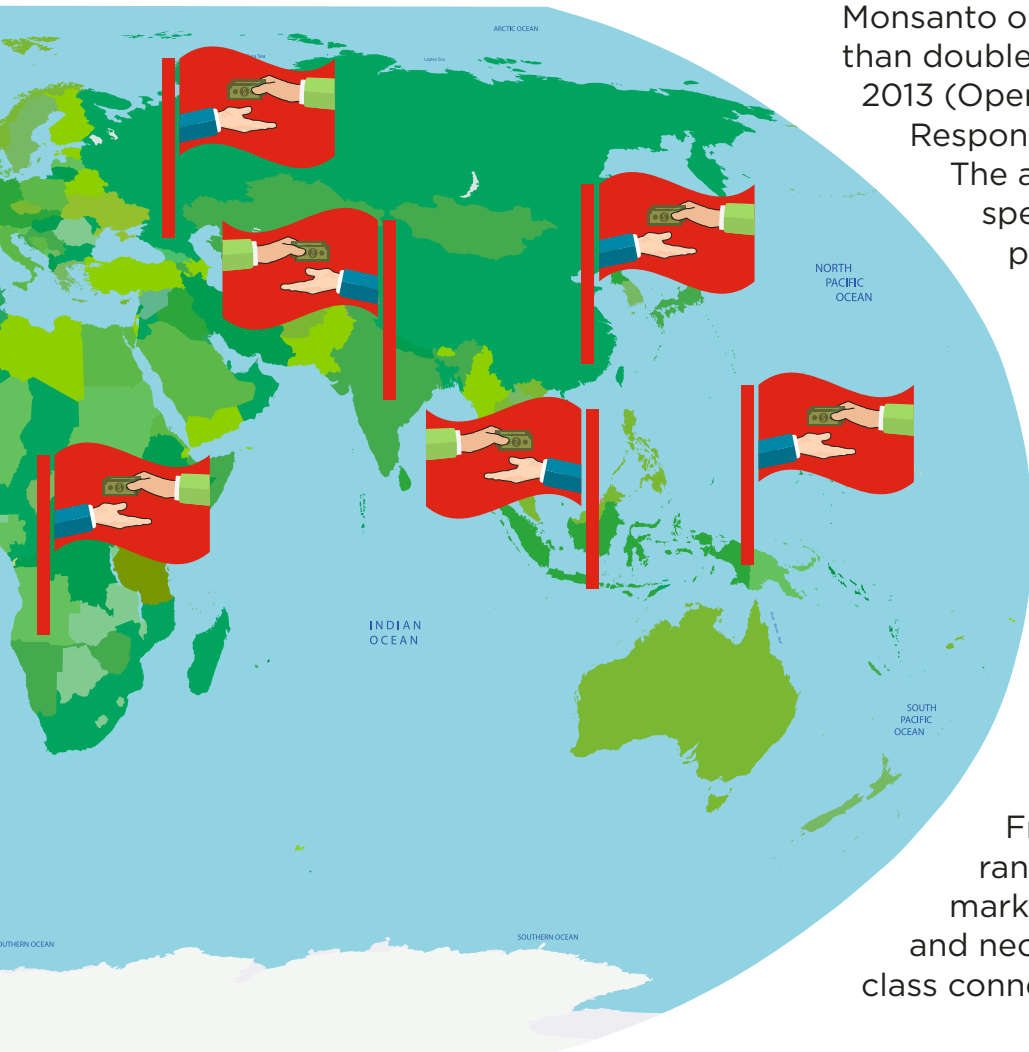
In a survey by Transparency International, over 54 percent of India's residents claimed to have paid a bribe in 2013 alone (Hardoon and Heinrich, 2013). Lack of accountability has led to corporate indecision and incompetency in often vital construction and development projects, slowing India's private sector and stunting GDP growth to 5 percent in 2013 (The Economist, 2014). Government corruption is normalized and propagated through a persistent lack of reform, and as a result, paying off government officials becomes routine procedure.



In the 2014 Sochi Winter Games, the largest contracts often went to Putin's childhood friends

Cronyism took another heavy toll in the 2014 Sochi Winter Games, with the massive US\$50 billion price tag dwarfing Vancouver's mere \$7 billion (Murray, 2014). As much as one-third of the sum was lost to bureaucracy; the largest contracts often went to Putin's childhood friends, like former judo partner Arkady Rotenberg, now a construction mogul (Murray, 2014).

Financial rewards from holding political office create a positive feedback loop, wherein power is followed closely by money, and money by power. Approximately 90 percent of the richest 1000 individuals in China identified by the Hurun Report in 2011 were officials or members of the communist party (Lee, 2014), and in 2011, the *Harvard Business Review* found that worker deaths from unsafe workplace conditions were over 10 times higher in "connected" companies, where at least one executive member had previously held a high-level



Monsanto on lobbying has more than doubled between 2006 and 2013 (OpenSecrets.org, Center for Responsive Politics (2014a).

The agricultural superpower spent \$654,000 in political contributions to Republicans and Democrats in 2012 alone (OpenSecrets.org, Center for Responsive Politics (2014b). Monsanto's lobbying has been costly, but at the end of the day Monsanto leaves courtrooms happy, trapping low-scale farmers in a net of patented GMO seeds.

Friends in high political ranks have disrupted the free market, creating inefficiencies and necessitating political and class connections.

post (Fisman and Wang, 2014). "Connections" allow companies to circumvent health and safety regulations at the cost of employee and customer welfare. Systems characterized by decision-making power concentrated in a group of elites are prone to corruption, manifesting in poorly maintained yet expensive infrastructure that hinders development.

Firms directly pushing for favourable legislation are not unheard of in the developed world, either. Money spent by the biotechnology firm

Money spent by the biotechnology firm Monsanto on lobbying has more than doubled between 2006 and 2013

Comedy of implicit errors

In 2013, Microsoft, along with some 16 other firms in the FairSearch coalition, accused Google of unjustly pushing its services through the Android mobile device platform (BBC News, April 9, 2013). FairSearch, which includes Google rivals from Expedia to Nokia, is taking on a course of action that benefits itself. Unlike in explicit cronyism, FairSearch

was not actively pushing for new bills to be passed or for new subsidy checks to be written. FairSearch was making the most of established social institutions; in other words, when firms are not actively erecting barriers to entry or lobbying for their removal, they are manipulating their environment. Echoed in ongoing Apple vs. Samsung patent feuds, instead of innovating, big businesses are engaging in a war of legal suits (Newman, 2014).

Likewise, the 1800s marked a period of massive subsidies for a handful of steamboat operators. Large firms continued using wooden hulls due to high iron costs, leaving smaller unsubsidized firms afraid to move forward. Cornelius Vanderbilt was the first to switch to iron and was so successful that competitors paid him 75 percent of their annual subsidy to not run his ships in their waters; only after the subsidy expired did iron



hulls take off (Weingarten, 2014). When dominant firms are protected, they are complacent, and competitors are unable to innovate. The result: poor quality and higher prices for the consumer.

When dominant firms are protected, they are complacent, and competitors are unable to innovate

In China, and in many developing countries, vague and lax legislation and enforcement leave the door open for corruption and skewed interpretations and applications of law. Apart from granting firms the ability to exploit resources, this social structure inherently promotes collusive behaviour between firms and high-ranking officials, lest firms wish to find themselves suddenly punished under a law never previously enforced (Kumar, 2010: 77). Businesses' behaviours reflect legislations and interventions in what should be a free market.

In India, the government's decision to create "mandis," or marketplaces where prices are determined through auctions to protect farmers from moneylenders and traders, shows how problematic intervention can prove. In these mandis, traders need licenses to function, generating revenue through farmer and retailer commission. Because of an immature enforcement system, auctions have not been held regularly, nor has tax from

transactions been used in developing mandi infrastructure (Chand, 2012: 54). The government's intervention led to further exploitation of farmers by middlemen.

In Malaysia, politically connected firms were found to have greater profit margins than unconnected rivals, despite lower returns on assets

In reacting to governments and social institutions that prevent markets from clearing, firms are now highly incentivized to pursue rent-seeking behaviour rather than innovate, resulting in loss of social welfare due to productive inefficiencies and the perpetuation of wealth and power concentration in a social elite class.

Much ado about institutions

All being said, the focus of reform and debate should not be criticism of business leaders. Big business isn't evil: in cases like TransCanada Rail where high infrastructure costs exist, it might be more efficient for one firm to supply to an entire market. Likewise, larger firms can attain scale economies, enhancing profits and thus the capacity to innovate. In practice, an uncompetitive firm relying solely on cronyism will not succeed for long. Innovation should be celebrated, and business leaders like Bill Gates and Steve Jobs who are contributing both domestically and globally should be recognized. What needs to go is government

intervention in what should be a free market.

With cronyism proliferating, consumers are unable to satisfy their own needs and wants, leading to the rise of parallel markets. Following the implementation of the medallion regulation system for taxi cabs in early 20th Century New York, the high costs of taxi leasing cut into the income of cab drivers and raised prices for consumers. The result? Underground economies in underserved areas (VanDoren, 2014). Under-the-table agreements favour those who are able to pay, ignoring those who aren't.

When the government picks winners and losers, disparity is perpetuated. In Malaysia, politically connected firms were found to have greater profit margins than unconnected rivals, despite lower returns on assets (Johnson and Mitton, 2003). Power, wealth, and influence is concentrated more and more within an upper class. The middle and lower classes are disenfranchised, having less opportunity and willingness to participate in economic activity, thus contracting output and productivity in the long run.

Positive means to an end

Further government regulations cannot resolve crony capitalism. In a modern context, businesses facing cronyism are conditioned to curry favours and manipulate their environment, not necessarily operating efficiently, but making use of available resources. From Putin's Sochi to the failed Kyoto Protocol,

the “government knows best” approach is clearly unreasonable and ineffective at best. In India, government spending on the provision of basic humanitarian services rose 11% faster than GDP in real terms between 2005 and 2012; half of the sum did not translate to improved living conditions. It was lost to inefficiency and corruption (Gupta et al., 2014: 5).

When dealing with implicit cronyism, the key is to liberate both markets and trade

One could look to Hong Kong as a beacon as it works to curb explicit cronyism and corruption. Hong Kong established the Independent Commission Against Corruption (ICAC) in 1974 with power to make arrests and prosecutions in conjunction with the Department of Justice, apprehending 245 individuals in 2012 alone. The ICAC also protects whistleblowers by providing them with new identities and relocating them. Through community outreach programs like exhibitions and e-learning workshops, Hong Kong has established a culture of integrity in both the private and public sectors (Gupta et al., 2014: 119).

When dealing with implicit cronyism, the key is to liberate both markets and trade. In doing so, firms can seek to maximize efficiency rather than connections, leading to more optimal allocation of resources and a society better integrated across all social strata. Governments have

a responsibility to protect taxpayers and citizens, not through more regulation, but through pro-market reforms.

It’s not the “capitalism” that makes “crony capitalism” an issue—it’s the “crony” part. 



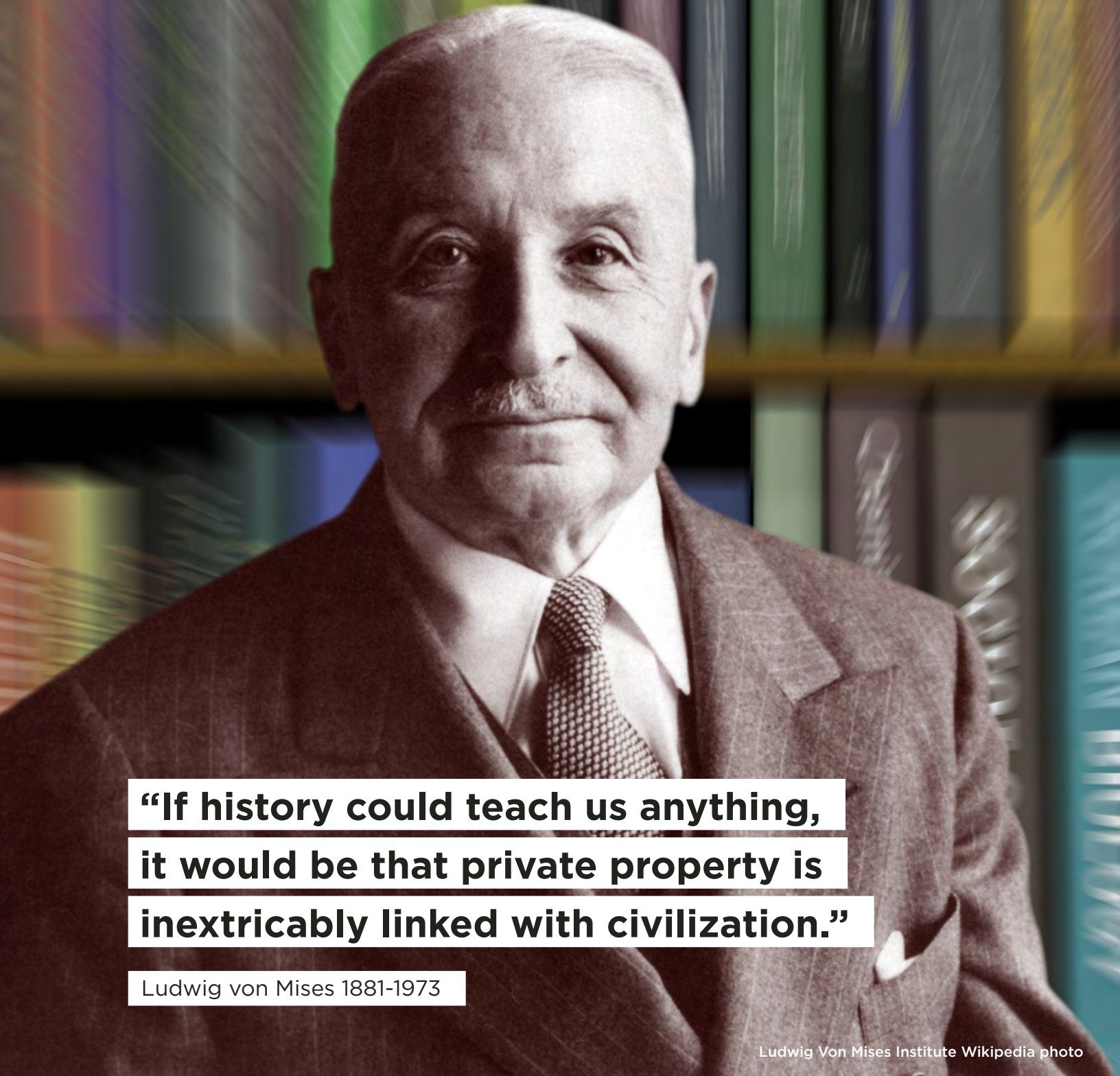
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**QUOTE
WALL**



**“If history could teach us anything,
it would be that private property is
inextricably linked with civilization.”**

Ludwig von Mises 1881-1973

Ludwig Von Mises Institute Wikipedia photo



WAITING YOUR TURN, MEDICAL WAIT TIMES IN CANADA 2014

Watch our video on wait times for medically necessary health care, based on an annual survey of physicians practising in 12 specialties in each province.

**THIS ARTICLE WAS PUBLISHED IN
THE VANCOUVER SUN ON JANUARY 6, 2015**



DO WE NEED GOVERNMENTS TO MEDDLE WITH CEO PAY LEVELS?

Charles Lammam

A number of pundits and activists regularly claim CEOs are grossly overpaid compared to average workers. Their solution: raise taxes or impose a government mandate such as limiting CEO pay to some arbitrary ratio relative to the lowest paid worker.

A recent report is the latest to suggest CEO pay is too high because the top 100 Canadian CEOs in 2013 earned an average total compensation of \$9.2 million or 195 times the average worker's pay. Such a comparison is deeply flawed and only fuels alarmist views about income inequality.

For starters, the comparison breaks a basic rule of statistics by comparing apples to oranges, using a definition of CEO pay that is much more wide-ranging than that used for average workers.

Specifically, the compensation figure for CEOs includes not just base salaries but all forms of compensation such as bonuses, company shares, stock options, "perks," and pensions. Meanwhile, the pay of average workers only includes their salaries—not pensions and other benefits. So right from the start, the so-called "pay gap" between workers

and senior management is exaggerated.

The top 100 CEOs are not a representative sample of Canadian corporate leadership; they are the top people—the superstars with unique talents and qualities in high demand.

Another glaring issue with the comparison: the top 100 CEOs are not a representative sample of Canadian corporate leadership. These are not your average corporate leaders; they are the top people—the superstars with unique talents and qualities in high demand. Presenting their compensation as being typical of CEOs is like saying Sidney Crosby's salary (\$12 million) is representative of the average NHL player's salary (\$2.4 million).

An ideal comparison would compare the average Canadian CEO's total compensation to the average worker's total compensation. Unfortunately, there is no such readily available data. But data from Statistics Canada's National Household Survey, though limited, allows for a more apples to apples comparison.

The data cover a narrow measure of compensation: wages and salaries. And the data are for a broad occupational group: senior management (which includes more than just CEOs—for instance, senior government managers and officials fall into this group).

In 2010, the latest year of available data, the wages and salaries of the average senior manager was \$142,434. That is 3.4 times the wages and salaries of the average worker (\$42,445)—a far cry from the “195 times” figure cited above.

In 2010, judges were the highest paid, with average wages and salaries of \$199,756 or 40.2 per cent more than the average senior manager (\$142,434).

Digging a little deeper into the data reveals the average senior manager is not even the highest paid occupation (based on wages and salaries). In 2010, judges were the highest paid, with average wages and salaries of \$199,756 or 40.2 per cent more than the average senior manager (\$142,434). The average petroleum engineer (\$154,249) also made more than the average senior manager.

The story is the same if we consider the median (which mitigates the effect of outliers like extremely high or low wages and salaries) rather than the average. In 2010, the median senior manager earned \$86,824 in wages and salaries or 2.6 times the median worker (\$33,094).

Still, the total compensation of heads of large corporations is sometimes in the eight-figure range so surely some of that money could have gone to pay a lot higher wages for other workers instead? But this assertion does not withstand scrutiny.

Take Gordon Nixon, the former CEO of the Royal Bank of Canada (RBC), as an example. At \$14 million, Mr. Nixon was the highest paid Canadian bank CEO in 2013. In the same year, RBC had about 74,000 full-time equivalent employees. If Mr. Nixon had taken a pay cut of 20 per cent and distributed it evenly among RBC’s full-time employees, it would have increased their hourly wage by only two cents.

Even if Mr. Nixon had given up his entire compensation, it would have translated into a mere 10 cents more per hour for RBC’s employees. Clearly, Mr. Nixon’s compensation package was not preventing RBC workers from enjoying dramatically higher wages.

The point is not that CEOs deserve more or less pay relative to average workers. The compensation of senior managers is a matter for owners to fret about. Decisions about CEO pay are not for governments to meddle with and they should not be made on faulty and misleading statistics. ©



Charles Lamman is Associate Director of Tax and Fiscal Policy at the Fraser Institute.

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THE APPEAL—AND FOLLY— OF A MINIMUM WAGE

Matthew Lau

Matt Jiggins Flickr photo



This is an election year and the New Democratic Party of Canada will include as part of its platform a federal minimum wage, which the party says will increase to \$15/hour within its first term in government if elected (New Democratic Party of Canada, 2014). This policy will undoubtedly be backed by numerous students' unions in Canada. Over the past two years, students' unions have poured significant time and resources into a campaign organized by unions and activists to lobby the Ontario Government to increase the minimum wage.

Over the past two years, students' unions have poured significant time and resources into a campaign to lobby the Ontario Government to increase the minimum wage.

In November 2013, the Canadian Federation of Students–Ontario, an organization composed of 38 students' unions and more than 300,000 students, called for an immediate minimum wage increase to \$14. The CFS-Ontario presented two primary arguments in favour of a minimum wage hike. Firstly, it argued that an increased minimum wage “should help ensure that students can afford to pay for tuition fees, books, supplies, and living expenses,” as many students work to put themselves through university (Canadian Federation of Students–Ontario, 2013a). Minimum wage hikes would help students, the CFS-Ontario argued, because 60 percent of minimum wage workers are youth

under the age of 25 and many of them attend school. The second argument the CFS-Ontario gave for an increased minimum wage was that a hike to \$14 would put a full-time worker earning the minimum wage 10% above the poverty line.

Experience has shown that large jumps in the minimum wage tend to hurt the very people they are supposed to help

Unfortunately, the CFS-Ontario's analysis was devoid of any behavioural changes that would arise as a result of a minimum wage hike. The Canadian Federation of Independent Business points out that "experience has shown that large jumps in the minimum wage tend to hurt the very people they are supposed to help: low-skilled and low-income Canadians," (Braun-Pollon, DeMarco, and Wong, 2011). Indeed, if the minimum wage rises above an employee's capacity to produce, "employers adjust their affairs accordingly. Employers not only respond by decreasing the number of jobs, but also by reducing the hours employees work, cutting non-wage benefits like on-the-job training... and/or finding ways to operate with fewer workers and more automation" (Lammam and MacIntyre, 2013).

The job losses and reduction in future job growth from even a small minimum wage increase are not trivial. The CFIB estimates that increasing the minimum wage in each province by 10% would result in between 92,300 and 321,300 job losses in Canada (Braun-

Pollon, DeMarco, and Wong, 2011). An American study published by the National Bureau of Economic Research in 2013, and cited by Charles Lammam and Hugh MacIntyre in a 2013 Fraser Forum article, "found that a 10% increase in the minimum wage led to about a one-quarter reduction in the rate of net job growth" (Lammam & MacIntyre, 2013).

Furthermore, another paper from the National Bureau of Economic Research that examined close to 100 studies on the minimum wage concluded that that a "sizable majority of the studies" indicated that minimum wages had a negative effect on employment and that there were "very few—if any—studies that provide convincing evidence of positive employment effects of minimum wages" (Neumark and Wascher, 2007). It is clear that the evidence overwhelmingly disproves the Canadian Federation of Students' claim that increasing the minimum wage creates jobs (Canadian Federation of Students, 2014).

There are very few—if any—studies that provide convincing evidence of positive employment effects of minimum wages

The damaging effects of minimum wage hikes on employment prospects disproportionately affect students and youth who, as previously stated, hold the majority of minimum wage positions. Canadian studies estimate that "a 10 percent increase in the

A national minimum wage of \$15, which represents a 36 to 50 percent increase depending on the province, would result in significant employment reduction among youth and students

minimum wage is likely to decrease employment by an average of three to six percent for young workers (aged 15 to 24). For young workers most directly affected—those earning between the current minimum wage and the proposed minimum wage—the impact is more acute, with employment losses of up to 20 percent” (Veldhuis and Karabegovic). The three to six percent reduction in employment among young workers estimated by the Canadian studies is “consistent with that from most other industrialized countries when comparable methodologies are used” (Gunderson, 2008).

If such substantial job losses are expected as a result of a 10% minimum wage hike, it is easily imaginable that a national minimum wage of \$15 (as proposed by the NDP), which represents a 36 to 50 percent increase depending on the province, would result in significant employment reduction among youth and students. Furthermore, contrary to popular belief, the minimum wage hike would likely not improve the standard of living for poor households. Only 17.1 percent of low-income earners belong to a poor household, and only 23.2 percent of poor households contain a low-

income earner (Mascella, Teja, and Thompson, 2009).

Lastly, any plan to implement a national minimum wage should be rejected because it would do away with Canada’s current provincial minimum wage laws, which are likely less damaging because they allow provinces to take into account regional economic factors when setting a minimum wage policy.

In sum, while a national minimum wage of \$15 may sound appealing to students who are looking for better-paying jobs or who care about poverty alleviation, such a plan should not be supported due to the damaging effects it would have on youth employment and because minimum wage hikes do not generally benefit low-income households. Students’ unions, which have in the past poured large amounts of financial and other resources into election campaigns and into campaigns to hike the minimum wage (Canadian Federation of Students-Ontario, 2013b), should not support any plans by any political party to hike the minimum wage. Doing so would only be a waste of students’ money and would damage the employment prospects of the students the union is supposed to represent. ©



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Fraser Institute researcher-recommended books
on free market policies and economics

THINK LIKE A FREAK

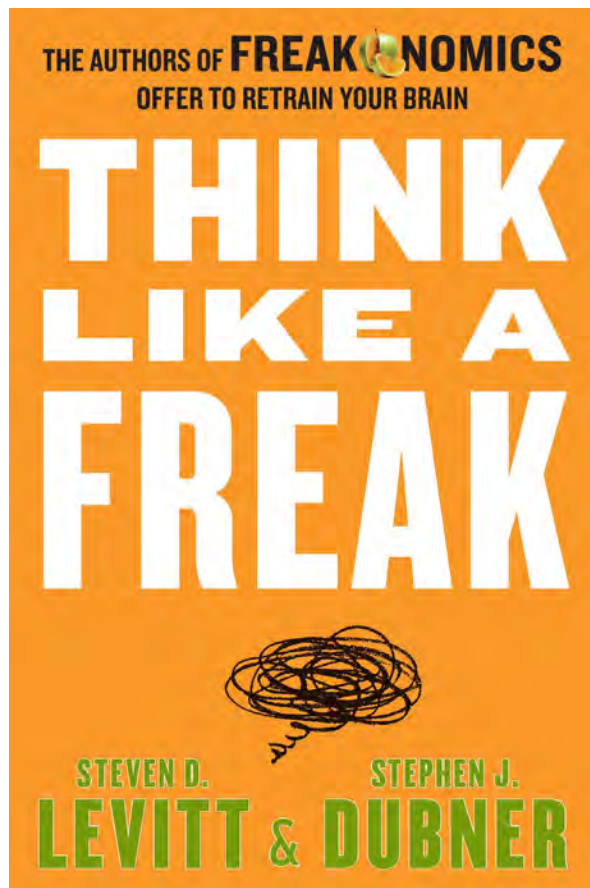
STEVEN D. LEVITT AND STEPHEN J. DUBNER

The bestselling book *Freakonomics* changed the way readers saw the world: a revelatory approach to everyday problems, and a straight-talking examination of conventional beliefs. Now, co-authors Steven D. Levitt (Professor of Economics at the University of Chicago) and journalist Stephen J. Dubner continue with their quest to get people to think in new ways in their latest book about decisions and problem solving. Using storytelling and their trademark quirky analysis, they take us inside their minds to show us how to retrain our brains to look at the world in a different way: in their words—to “think like a Freak.”

The authors are enthused with a sense of curiosity and an almost revolutionary call to action

The nine fast-paced chapters are full of nuggets of useful advice threaded together with catchy stories. They contain guidance such as: ignore conventional wisdom; focus on data; test theories with experiments; and don't be afraid to say, “I don't know.” The authors offer a blueprint for a new way to solve problems; they are enthused with a sense of curiosity and an almost revolutionary call to action. Most people, they argue, “seek out evidence that confirms what they already think,” so they urge us to consider evidence that may seem obvious, counterintuitive, or even childish. (Children, they assert, are much more likely than adults to focus on small, solvable problems, rather than complex issues.)


Levitt and Dubner include some interesting recent research, ranging from the secrets of a Japanese hot-dog-eating champion, to the reason an Australian



doctor swallowed a batch of dangerous stomach bacteria, to why Nigerian e-mail scammers make a point of saying they're from Nigeria. The Nigerian email scam story is particularly telling. Most people have received one of these emails at some point: a large sum of money needs to be transferred out of Nigeria, and the recipient will get a large portion of it if they supply their bank details. The book details why scammers still insist on specifying Nigeria in their correspondence, even though the mere mention of the country is enough to signal to (almost) everyone that the e-mail they have just received is a con. Sending out millions of emails has minimal financial cost, so having millions of people ignore them doesn't really matter. What would cost both time and money would be to set up a fake transfer with people who realize halfway through that

they are being tricked and call off the transaction. By choosing Nigeria as the source country, the scammers are adding an efficient testing device for naiveté into their email blast. Anyone who responds has clearly signaled that they are completely unaware of this email scam.

Their research ranges from the secrets of a Japanese hot-dog-eating champion, to why Nigerian e-mail scammers make a point of saying they're from Nigeria.




Think Like a Freak is the third book in the Freakonomics series—a new compendium of arguments that are upbeat and nifty, categorized under the guise of “self-help.” Thinking “like a Freak” means being willing to think creatively, and while the problem-solving advice the authors include is fairly routine, Levitt and Dubner draw you in with their amusing and revelatory stories. Their mission—to help us think in different ways and enable us to see the world like they do—certainly makes for an enjoyable read. 



INFOGRAPHIC



1987

The last time Canada fundamentally reformed the personal income tax system, Reagan was  president, Gretzky  was an oiler and parachute  pants were cool.



Let's Create



THE MYTH OF GOVERNMENT JOB CREATION

Brennan Sorge,
Regular High School Contributor

When the government promises to “stimulate” the economy in order to create jobs through government spending, can it deliver? I argue that it cannot, simply due to the reality of the way government funds must be raised, which includes taxes on privately employed citizens and private enterprises that pay for all government spending, including government jobs or employees. The taxes paid by public employees do not raise government revenue per se, but rather reduce government costs, including the government employee’s wage. This is because the government is taxing the very wages that it is paying.

In other words, the government uses funds that are not raised through the private production and sale of

goods or services. Governments rarely create an asset which is to be sold in order to raise revenue, and are, in theory, primarily tasked with supplying necessary services that cannot be provided and financed privately. This includes, for example, a functional military to maintain national security. In some cases the government is better placed to provide certain services than the private sector. But in the framework of “government job creation”, government suffers from both bureaucratic displacement (when unnecessary bureaucracy grows over time, and decreases the efficiency of the affected institution), and the fact that it is moving resources from where the market has determined them to be most efficient, to where the government has decided they would be better

used. Government suffers most from bureaucratic displacement as government programs are not held to the same income constraints as private organizations. Government programs can afford to be inefficient as they are publicly funded and face no competition. Because government raises revenue by taking money out of the private economy, it necessarily imposes a tax cost on the very people that will also generate future government revenue.

By turning a potential private sector employee into a public one, the government has imposed a cost on itself (the wage it pays), while simultaneously eliminating the potential additional income of a private taxpayer.



As government job creation imposes costs on the private economy, these costs often take the form of lost jobs in the private sector. If, in creating government jobs, private jobs are lost, then “government job creation” is really just a transfer of jobs from the private to the public sector. Here is the sticking point: by turning a potential private employee into a public one, the government has imposed a cost on itself (the wage it pays), while simultaneously eliminating the potential additional income of a private taxpayer.

The issue is not just about losing existing jobs; it is also about not having created new jobs where the market has determined them to be most efficient.

This kind of approach to job creation is damaging to economic growth, damaging to taxpayers, and even damaging to government revenue. Indeed, when government increases the size of the public workforce, some private sector jobs that otherwise may have been created will not be created. The issue is not just about losing existing jobs, which is bad enough. It is also about not having created new jobs where the market has determined them to be most efficient. We cannot know what jobs, innovations, and businesses will not be created because of this distortion in the private market.

In addition, we are often told that this approach is to be temporary and is intended to relieve the effects of a

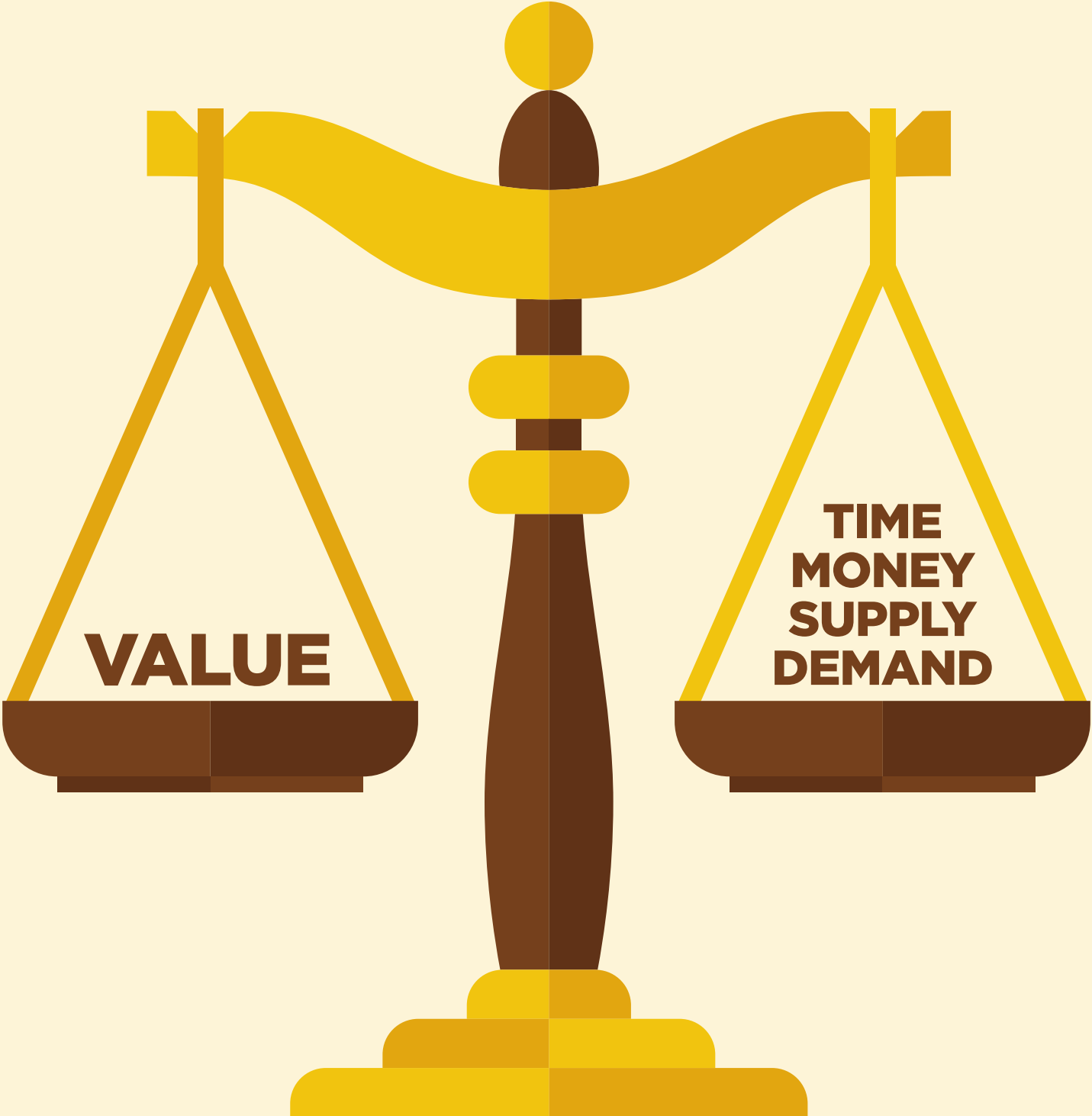
recession. It is worth remembering Milton Friedman’s words: “Nothing is so permanent as a temporary government program.” But even if the program is truly temporary, there would be a cost over and above that of bureaucratic displacement and government inefficiency, as the new government job may now have to be financed through debt. This spending would result in a long-term cost for government, to be paid over time and into the future. Such a situation makes it even harder for the economy to grow, as future growth has been spent in an attempt to avert present short-term pain. It is essential that we not spend the prosperity of the future to dull the economic pains of the present. After all, recessions happen because parts of the economy need to restructure, and that process of restructuring is not something we should spend our future growth hindering. 



Brennan Sorge is a grade 10 student at the Discovery Centre for Balanced Education in Sun Peaks. Having taken an interest in politics, and economic policy, he hopes to earn a degree in economics as well as law, and then continue into the political arena



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VALUE

CAN IT BE MEASURED?

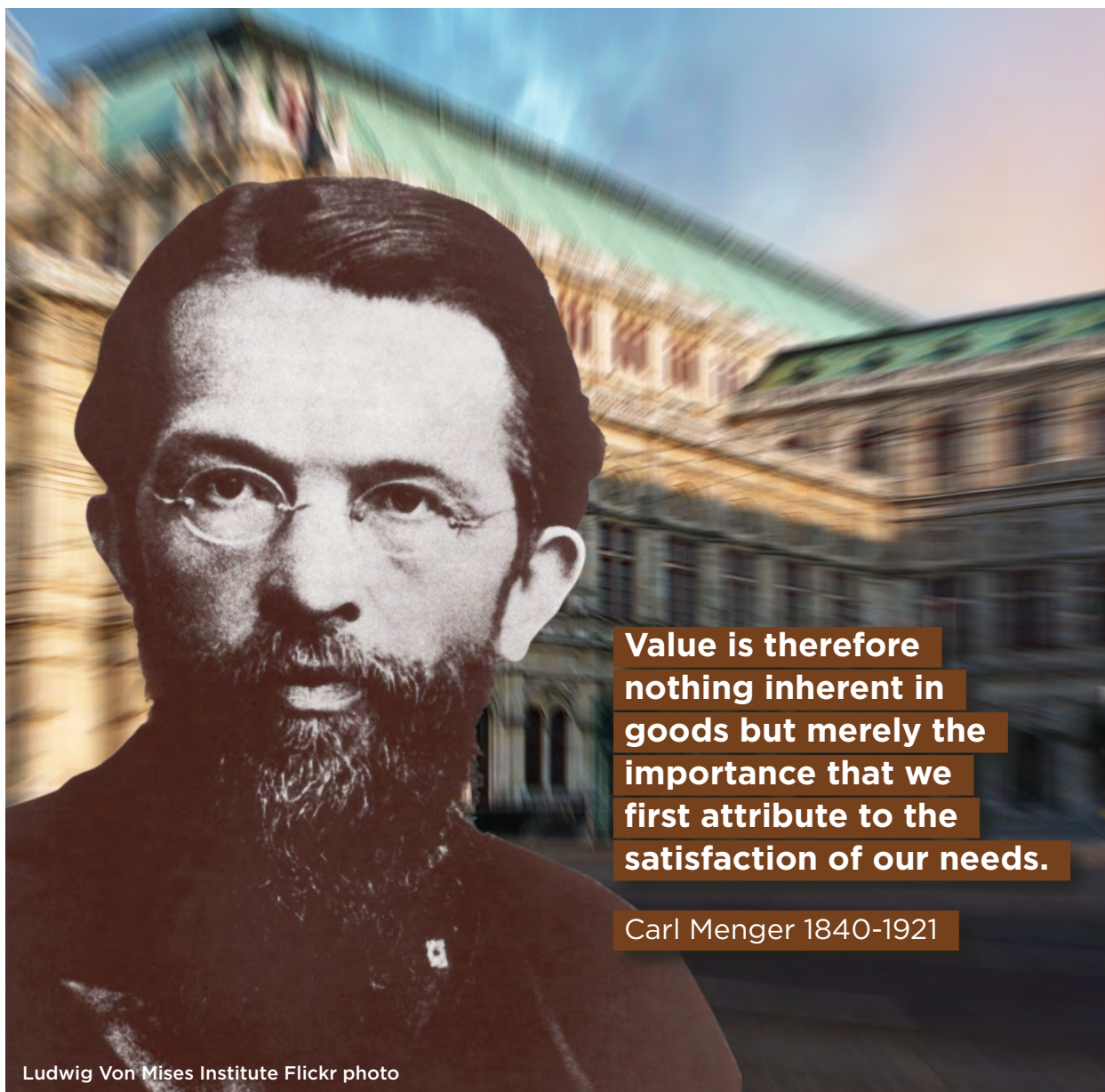
Danny LeRoy

Perhaps no other economic concept has spawned and enabled as many intellectual hobgoblins that befuddle clear thinking as that of value. The source of this confusion is the mistaken notion that the value of any good or service is a function of its production cost.

Classical economists believed that cost determined value and that value was something objective and measurable

Classical economists, such as Adam Smith, David Ricardo, and John Stuart Mill, were each confounded by the problem of value. They subscribed to the fallacious

idea that value was embodied in products in proportion to the amount of labour that went into their creation. In other words, they believed that cost determined value and that value was something objective and measurable. Inescapable paradoxes immediately arose from the practical application of this theory of value. For example, how could certain raw materials like exotic hardwood or uncut gems fetch higher prices than products that required hundreds of man hours to produce, such as ornate furniture or finely crafted telescopes? How could an essential good, such as water, have a lower price than a luxury product, such as diamonds? In addition to failing to provide satisfactory insight into these



Value is therefore nothing inherent in goods but merely the importance that we first attribute to the satisfaction of our needs.

Carl Menger 1840-1921

Ludwig Von Mises Institute Flickr photo

and similar questions, the labour theory of value could not explain fluctuating values for different kinds of labour, nor could it account for why found goods could be more valuable than extracted goods.

In 1871, Carl Menger brilliantly and completely resolved the conundrum over value by combining the novel concepts of marginalism and

subjectivism. Marginalism refers to the way individuals evaluate certain things depending upon the quantity available and the quantity consumed. If you were thirsty, you would, for example, pay more for your first glass of lemonade than for the second, third, or tenth glass. After the tenth glass, there may be absolutely no marginal value to lemonade at all (at least as far as

you are concerned). The marginal value of the lemonade decreases with each glass consumed. Subjectivism refers to the fact that things are inescapably appreciated (and valued) according to a private set of priorities, tastes, and preferences. Some people pay vast sums for old comic books whereas others could not be convinced to pay a nickel for even one comic book. This largely comes down to individual—hence subjective—preferences.

If you were thirsty, you would pay more for your first glass of lemonade than for the second, third, or tenth glass

While the medieval scholars and French economists of the 18th and 19th century implicitly used a marginalist and subjective theory of value, Menger formalized this combination (together, but independently with Stanley Jevons and Léon Walras) and in doing so contributed to one of the greatest discoveries in economic science. Menger revealed the precise nature of economic value and rooted economics firmly in the real-world actions of individual human beings.

Menger's penetrating insight was that value is not inherent in goods or services. Instead, goods or services take on significance for individuals, either as a way to directly satisfy a need or as a means to satisfy a need through exchange. It is for this reason that a good can

have great value to one individual, little value to another, and no value at all to a third, depending on each individual's requirements and the good's availability. Thus, both the nature and the measure of value are entirely subjective. Goods or services always have some kind of value to individuals—at least to economizing individuals who are sensitive to scarcity and prices—and their marginal value can only be determined by those individuals. In other words, value is in the eye of the beholder.

Since value is completely subjective, it cannot be quantified or measured. There are no cardinal units of value that enable it to be added, subtracted, multiplied, or divided across individuals. Furthermore, individual valuations are not constant; they are always changing. Value is something that each individual weighs on a purely private set of scales. When determining value, an individual takes into account a vast range of considerations, many of which are peculiar to him alone and may be so deeply subjective that they could not be described to another person.

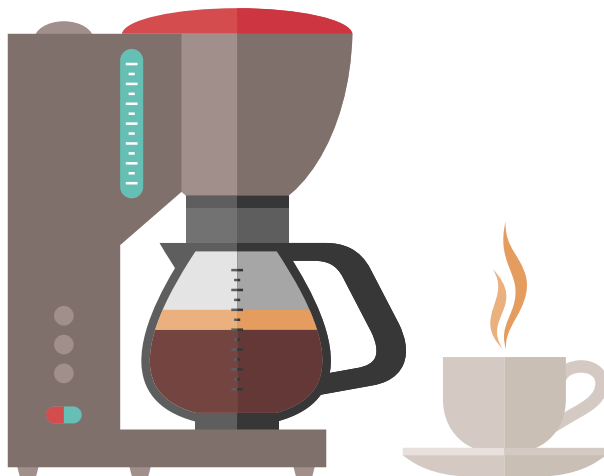
Goods or services take on significance for individuals, either as a way to directly satisfy a need or as a means to satisfy a need through exchange

The expression of subjective valuations is most clearly seen through interpersonal exchange. Every time a person decides to

buy something, he or she gives up something they value less (a specific amount of money) in exchange for something they value more (a specific quantity of a specific good or service). The same is true for the counterparty to the transaction, the seller. He or she gives up something they value less (a specific quantity of a specific good or service) in exchange for something they value more (a specific amount of money). The resulting price may be public knowledge, but the value to each individual is known only to them and can be known only by them.

When determining value, an individual takes into account a vast range of considerations, many of which are peculiar to him alone

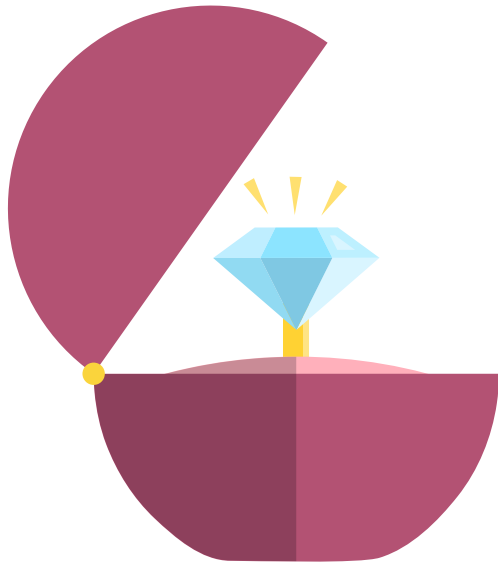
Thus, when I pay \$1.64 in exchange for one large coffee at a particular place and time, the value of my newly acquired coffee is known




only by me. By virtue of Menger's contribution, it is first and foremost evident that in this and in every other unhampered interpersonal exchange, value never equals price. Second, my personal (and marginal) valuation of a cup of coffee changes over time with each mouthful, as the coffee cools, and in concert with my perception of the external world which influences my enjoyment of that beverage. For instance, my valuation of a cup of coffee on a given day is certainly much higher after a poor sleep the night before.

My valuation of a cup of coffee on a given day is certainly much higher after a poor sleep the night before

The subjective valuation of consumer goods and services ultimately determines the valuation of all factors of production, including the inputs required to produce goods and services. Each unit of each input at every stage of production is valued by entrepreneurs according to the estimated value of the consumer goods they might produce. It is true that many goods or services requiring high-priced inputs will themselves command a high price. But that is because entrepreneurs will not use expensive inputs in the creation of these goods or services unless consumers are willing to pay high prices. It is not because diamonds are expensive that diamond rings are expensive; it is



because people value diamond rings highly that diamonds are expensive.

Although Menger provided a correct theory of value in 1871, ancient errors clearly die very hard. Fallacious and erroneous conceptions of value inevitably misdirect contemporary discussions of economic issues. The resulting problems would be far less widespread if valuation was not so central to economic decision making. 

SUGGESTIONS FOR FURTHER READING

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**HOT
TOPICS**



A LOW DOLLAR AND CHEAP OIL DIDN'T RESCUE ONTARIO AND QUEBEC BEFORE

Mark Milke

One of the more persistent myths about prosperity is that it results purely from luck. Often, commentators credit the mere presence of oil, gas, potash and other natural resources for Western Canada's recent (and presently fading) boom in investment, jobs and government revenues.

But Nigeria, South Africa, and Venezuela all have natural resources in abundance. Yet on many prosperity measures from per person GDP to longevity, they lag far behind Hong Kong and Singapore which possess no oil, gas or mineral deposits.

Ontario and Quebec policy-makers might be tempted to believe that a lower dollar will now magically transform Central Canadian economies.

I note this enduring myth because Ontario and Quebec policy-makers might be tempted to believe a similar fairy tale: that a lower dollar will now magically transform Central Canadian economies.

A lower dollar might temporarily help a few businesses do a bit better; but the reason for a particular jurisdiction's failure or success is more prosaic—it depends on getting the basics right, everything from the security of property rights and independent courts to tax levels and sensible (as opposed to burdensome) regulation.

At the sub-national level, a province needs smart policy on labour and land regulation. It also requires moderate tax levels.

To understand why Ontario and Quebec are not poised to automatically replace the West as the economic engines of Canada, consider where oil and the dollar have been, and past trends.

The reason for a particular jurisdiction's failure or success depends on getting the basics right, everything from the security of property rights and independent courts to tax levels and sensible regulation.

Over the past several decades, the monthly average per barrel oil price ranged from \$11.35 (US) in December 1998 to \$133.88 (US) in June 2008. The dollar was as low as 62 American cents (January 2002) and as high as \$1.10 (US) in November 2007.

So how has Central Canada fared during high dollar, low dollar and “yo-yo” oil prices over time? Let’s start with private sector investment.

From 1982 to 2013, the average annual private sector investment

(per worker) in Alberta was \$45,842 followed by Saskatchewan (\$35,458), British Columbia (\$24,486), Ontario (\$19,850) and Quebec (\$18,271).

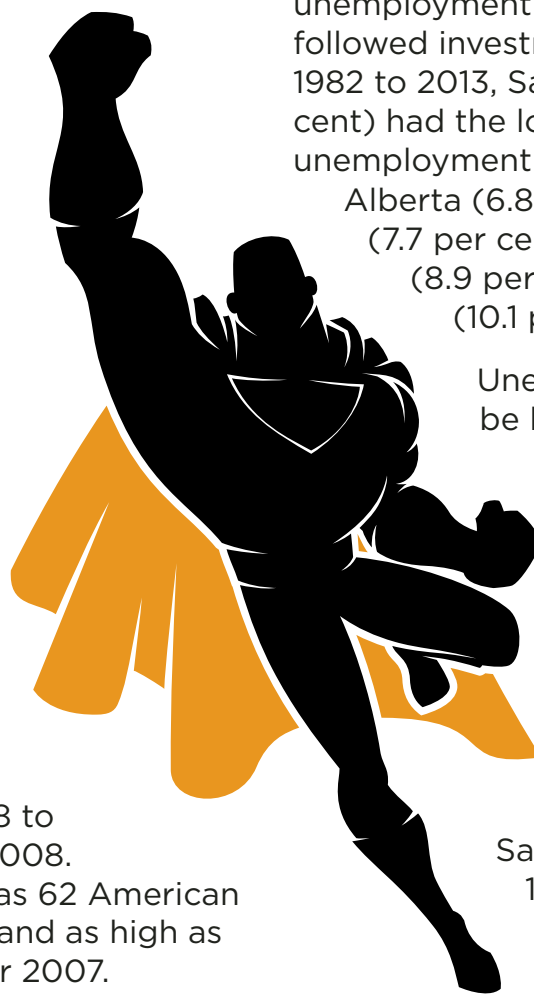
By a wide margin, the West saw more investment (per worker) even when oil and natural gas and other resource prices were low.

Private sector investment dollars are a “futures market” indicating where jobs will be created. Not surprisingly, unemployment rates have mostly followed investment flows. From 1982 to 2013, Saskatchewan (6.2 per cent) had the lowest average annual unemployment rate, followed by Alberta (6.8 per cent), Ontario (7.7 per cent), British Columbia (8.9 per cent) and Quebec (10.1 per cent).

Unemployment rates can be lower if a province experiences a substantial outflow of people, especially among those of (mostly) working age. That was Saskatchewan until recently. For those between ages 15 and 64, Saskatchewan lost 115,245 people (from 1982 to 2014) on a net basis.

But here’s where the data—and the caveat for Ontario and Quebec—comes into play.

For Alberta, the worst period for interprovincial migration was



between 1982 and 1989 when 81,134 people aged 15 to 64 left the province.

After that, other than a small loss in the mid-1990s and a blip of a decline in the last recession, Alberta has gained people. In total, even with the steep 1980s-era losses, 339,381 people moved from other provinces to Alberta since 1982.

In Ontario and Quebec, future success will depend on the correction of poor policies that for years have hindered greater prosperity in those two provinces.


In contrast, while Ontario gained 53,083 working-age folks between 1982 and 2014, it hasn't seen net positive migration numbers since 2003, and has been losing people ever since. Meanwhile Quebec lost people in every single year since 1982, or 237,593 in total.

B.C. has a mixed record in the interprovincial migration sweepstakes. It lost some people in the early 1980s and saw significant out-migration between 1998 and 2003, but has mostly gained working-age people—an extra 257,949 since 1982.

In short, despite past periods of low oil prices and a cheap Canadian dollar, since 1982 Ontario and Quebec have never overtaken Alberta and Saskatchewan in per worker private sector investment. And migration and unemployment

rates have generally been healthier in the West than in Central Canada.

Which means there's something amiss in Ontario and Quebec, which bargain-basement oil prices and a low dollar won't solve: High marginal personal tax rates, inflexible labour legislation, unnecessary regulatory hurdles and botched electricity policy (in Ontario, in particular).

In Ontario and Quebec, future success will depend on the correction of poor policies that for years have hindered greater prosperity in those two provinces. That will require policy-makers to eschew magic bullet myths—such as how a low dollar will rescue Central Canada. 



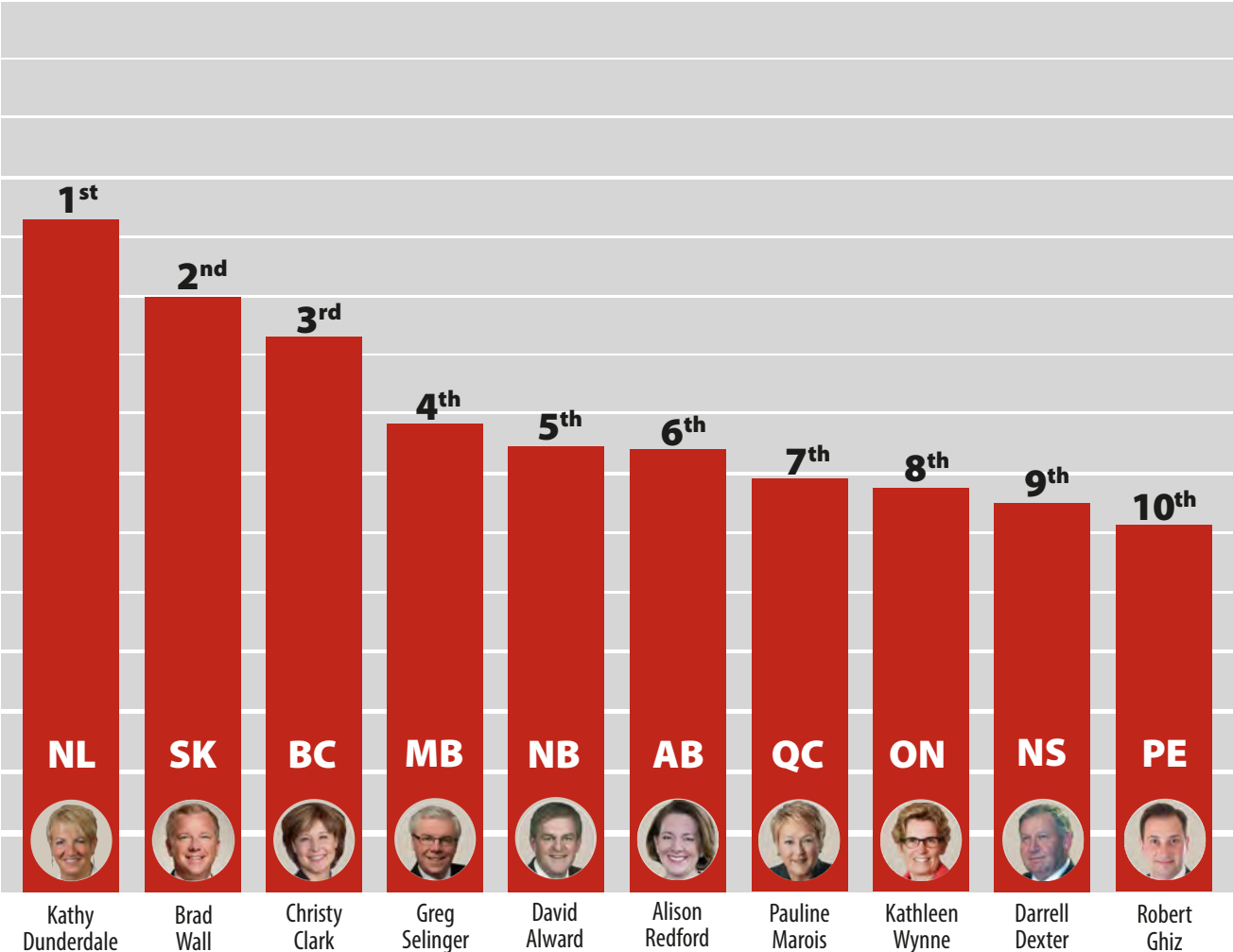
Mark Milke is a Senior Fellow at the Fraser Institute.

MEASURING THE FISCAL PERFORMANCE OF CANADA'S PREMIERS, 2015

Charles Lammam, Milagros Palacios, and Feixue Ren

Measuring the Fiscal Performance of Canada's Premiers, 2015 measures the relative fiscal performance of 10 Canadian premiers (five current and

five former), up to the 2013/14 fiscal year for three components of fiscal policy: government spending, taxes, and deficits and debt.




Overall, the premiers ranked (of 10) and scored (of 100), as follows:

- 1st Kathy Dunderdale (former premier), NL (84.6)**
- 2nd Brad Wall, SK (71.5)**
- 3rd Christy Clark, BC (64.8)**
- 4th Greg Selinger, MB (49.9)**
- 5th David Alward (former premier), NB (46.0)**
- 6th Alison Redford (former premier), AB (45.9)**
- 7th Pauline Marois (former premier), QC (40.8)**
- 8th Kathleen Wynne, ON (39.5)**
- 9th Darrell Dexter (former premier), NS (36.9)**
- 10th Robert Ghiz, PE (33.2).**

On the government spending component, Dunderdale took top position (scoring 98.5), followed by Alward (77.7) and Clark (64.3). The remaining premiers scored below 50: Selinger (41.9), Wall (35.7), Wynne (26.8), Dexter (20.8), Marois (12.4), Redford (8.8), and Ghiz (7.8).

On the taxes component, Redford led the premiers (scoring 90.0). Premiers from Canada's most populous provinces, Wynne (63.5) and Marois (55.7), ranked 5th and 7th, respectively. Alward ranked last (27.3).

On the deficits and debt component, Wall topped the list (scoring 100). Dunderdale came second (91.1), followed by Clark (74.2) and Marois (54.2). The remaining premiers scored below 50: Dexter (49.0), Ghiz (44.2), Selinger (41.7), Redford (38.7), Alward (32.9), and Wynne (28.1). 



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