

Understanding gasoline prices



**Hockey
economics**

by Tim Mak

**Free trade stops
at the border**

by Mark Milke

**Victims,
incarceration,
and justice**

by Hilary Furness

**Missing women
and economic
freedom**

by Alecs Dragne

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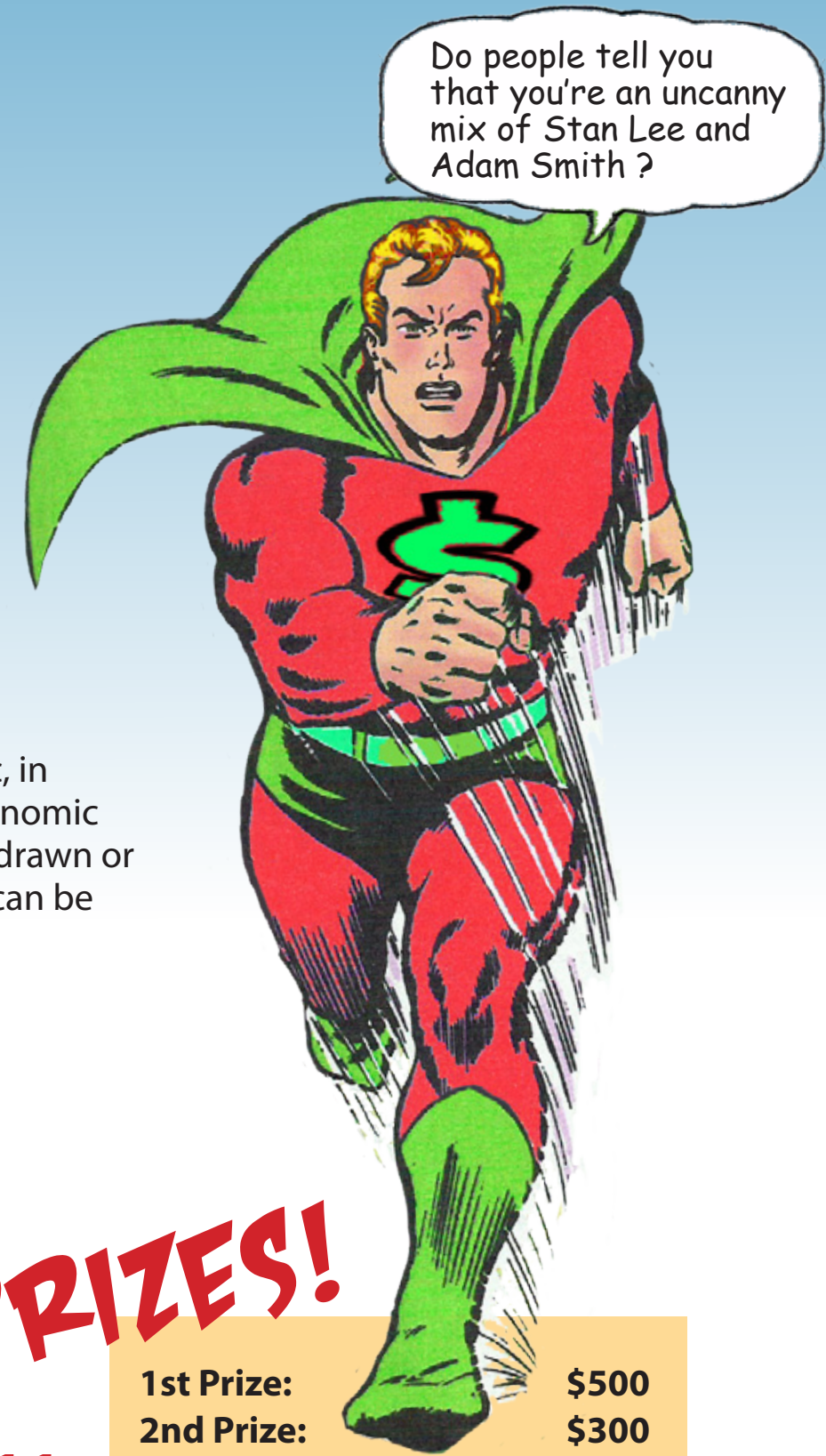
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Canadian student review

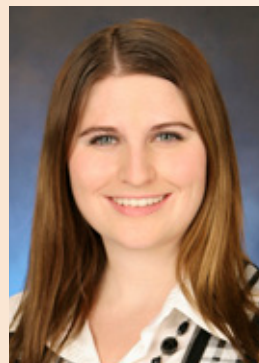
Welcome!

Dear Reader,

With the variety of topics in the
summer 2011 issue of *Canadian
Student Review*, it is easy to see
how economics and policy are
applied everywhere—they are not
just theories taught in the classroom. This issue raises lots
of important, practical questions for us. Summertime and
road trips usually go hand-in-hand, but with gas prices
skyrocketing, can you afford to drive anywhere this year?
As professional hockey returns to Winnipeg, what are the
economics behind the NHL and other sport franchises?
The Conservative government promised tough crime laws
as part of their election platform, but can and should they
follow through? Why are 100 million women missing in the
developing world? This issue also discusses immigration,
health care, and trade with the US.

Once you are finished reading the articles, I encourage you
to explore our website for upcoming fall programs, including
free student seminars and new internship positions.

Best,
Lindsay Mitchell
Editor, *Canadian Student Review*



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Hockey economics

How a freer market in hockey could lead to more Canadian teams

Tim Mak

The National Hockey League and local governments have adopted policies that create poor incentives that keep financially flailing teams from moving to more profitable areas. Changing some of these policies could lead to better outcomes for Canadian hockey fans.

Hockey's welfare statism: revenue sharing

Everyone loves "free" money, so what makes the wealthy owners of NHL teams an exception? In May 2011, Edmonton Oilers owner and billionaire Daryl Katz came to an arrangement that would have had the both the provincial and municipal government subsidize the

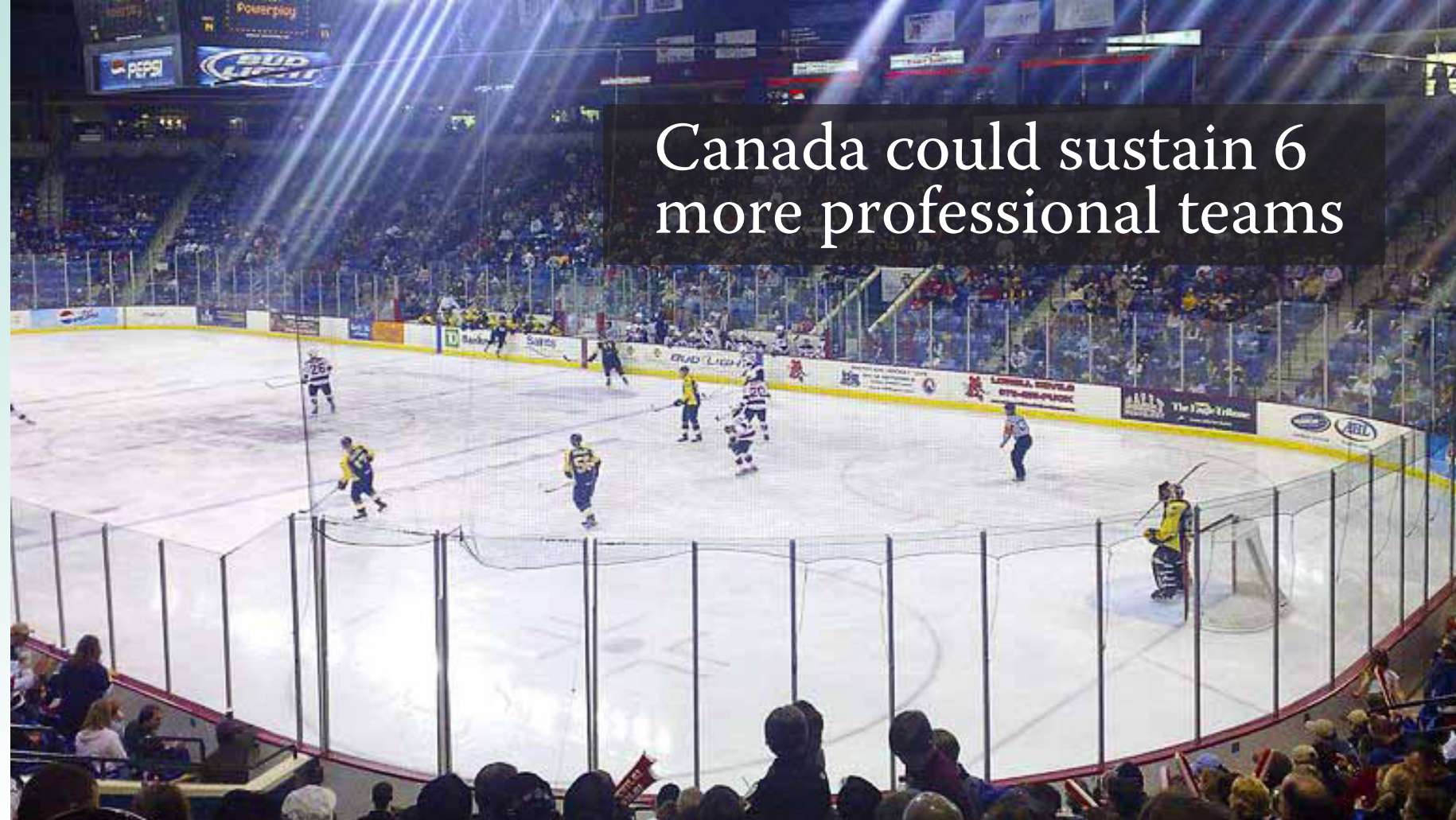
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building of a new downtown arena. As of the time of writing, the province has declined to take part (Salz, 2011); however, it illustrates how NHL teams often ask for subsidies for unprofitable activities.

Indeed, the National Hockey League has formalized internal subsidization programs that force more profitable teams to share revenue with less profitable teams. After a labour dispute which forced the cancellation of the 2004/05 NHL season, both team owners and the hockey players' association agreed upon a collective bargaining agreement in July 2005 (Jones, 2005).

This collective bargaining agreement established many of the policies that govern the financial rules of the National Hockey League. Among these rules was the commitment that the top ten best performing clubs would redistribute revenue to the bottom ten worst performing clubs. The amount to be redistributed was set to be 4.5% of total league revenues (Brinkman, 2006).

The exact technical details of where this revenue comes from is complicated and beyond the scope of this article, but to simplify, the money comes from a combination of centrally generated league revenue, "taxation" on the top ten revenue-earning teams, and a "tax" on NHL playoff revenues (Brinkman, 2006).



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NHL revenue sharing attempts to make floundering, unprofitable franchises more economically viable (Brinkman, 2006). By taking in revenues from profitable, successful teams, hockey franchises are more likely to survive in cities which would otherwise not be able to support them.

Imagine a parallel in real life—say, a convenience store that was consistently losing money, month after month. If some level of government stepped in to save the convenience store, it would have to do so with

money taken from more successful enterprises. On the other hand, if the unprofitable convenience store was not propped up, its private investors would eventually shut it down and invest their money elsewhere. Similarly, if not bailed out by revenue generated from successful teams, failing NHL franchises would face a greater incentive to relocate to markets where they could perform better economically.

There is a strong chance that those markets would be in Canada. In fact, a recent study by the Mowat Center suggests that if market

Governments often subsidize poorly performing teams by building stadiums



Canadian hockey teams are “taxed” to support flailing American hockey teams. Indeed, despite having only six teams, or one-fifth of the league’s total number of franchises, Canada generated one-third of the NHL’s revenue in the 2007/08 season. That same year, Canadian teams sent over \$41 million to struggling American teams (Gordon et al., 2008) —money that might have otherwise been spent on improving local arenas, signing better players, or providing a higher-quality hockey experience for Canadian hockey fans.

In short, ending the NHL’s policy of revenue sharing would create a freer market in North American professional hockey. This would in turn ease the “taxation” that Canadian teams disproportionately suffer under, and would create incentives for struggling American teams to move north for more profitable pastures.

Government subsidies

Internal wealth redistribution within the league is not the only type of wealth distribution related to hockey in the NHL. Often, governments will subsidize poorly-performing teams in order to keep them playing in their locality.

“These subsidies generally take the form of building a stadium...with taxpayer dollars, and then allowing the team to play there at very

forces were allowed to determine the location of NHL franchises, the demand for hockey in the Canadian market is such that the country could theoretically sustain twelve hockey teams—double the current number (Keller and McGuire, 2011).

Currently, revenue sharing disproportionately affects Canada, which, due to its passion for hockey, performs extremely well in earnings. A strong Canadian dollar has also boosted the bottom lines of Canadian teams, as salaries are paid in US dollars. But because of their successes,

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Canadian teams sent over \$41 million to struggling American teams

low rent, or no rent at all,” note Mowat Center co-authors Tony Keller and Neville McGuire in a recent study of Canadian hockey market potential (2011). The pair identify that “the most egregious recent case is that of the Phoenix Coyotes...the city of Glendale [Arizona] is still trying to borrow US\$100 million on behalf of the Coyotes as part of a plan to give the team’s intended buyer a subsidy greater [even] than the team purchase price” (2011).

Government favours are similar to internal league revenue sharing: when a local government subsidizes a hockey team, it creates disincentives for the team to move to a more genuinely profitable location, medium-sized American cities, or even perhaps a few Canadian cities (Keller and McGuire, 2011). As the Mowat Centre notes:

If the NHL were a free market, these Canadian sites would be first choices for team movement or expansion, and *not* treated as last resorts to be avoided at all costs. The economic case is clear. Canada can almost certainly support 12 NHL teams.

So why does Canada not have more than six NHL teams? The answer lies in the fact that the NHL is a monopoly (or more precisely a cartel), and not a free market. It artificially limits the supply of NHL teams, and controls where they play. The answer also lies in the fact that American local governments, responding to the



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cartel’s control over supply, have been willing to use taxpayer dollars to entice one of those scarce teams into locating to their city—something Canadian governments have not traditionally done.

At least when the National Hockey League redistributes money from one NHL team to another it mostly does so with its own money. When governments subsidize hockey teams, they do so with the money of their citizens—some of whom may not even like hockey and others who may even despise it!

Government expenditures that subsidize millionaire sports stars and billionaire sports teams do not compare well against other

things that the government could be doing. Further, subsidizing hockey is a particularly troubling matter because it is regressive—that is, it takes from the poor and gives to the rich. Indeed, hockey subsidies are “a regressive subsidy of the hobbies of the affluent,” opines writer Colby Cosh in *Macleans* (2007). This is because a tax base which is largely funded by middle income individuals is being doled out to players who are wealthy, and who would otherwise have to accept lower salaries if they were not being subsidized.

While this sort of regressive subsidization happens frequently in many major sports, hockey is perhaps the most egregious example of it. “The NHL fan base is the most affluent and

well educated of the four [major sports, among baseball, football and basketball],” points out writer David Markus in *Stanford Business Magazine* (2004). One study of NHL fans show that they are more likely to have college and graduate degrees than non-NHL fans, and are 64% more likely than non-NHL fans to earn an annual income of \$150,000 or more (Fetto, 2009).

Therefore, taxpayers would be better off if government subsidies for hockey ceased and the inequity now in place—transfers from the less well-off to the wealthier—would end, creating less strain on the local taxpayer, and a greater potential for new Canadian hockey franchises.

Conclusion

Both governments and the NHL currently provide incentives for otherwise-unprofitable hockey teams to stay where they are. If these incentives were removed, franchises would move to more profitable markets—and in select cases, even possibly to markets in Canada, though it is likely that NHL salary levels would have to moderate first.

Undoubtedly, there are other barriers not thoroughly explored in this article—barriers that could present additional impediments to the moving of additional hockey teams to profitable locations. For example, the NHL gives a great deal of leeway to franchises which do not want a hockey team moving into their area and

impinging on their local monopolies (Toronto owners opposing a theoretical franchise in Hamilton is one example).

But, by and large, the removal of revenue sharing in the NHL and government subsidies to franchise owners would at least remove the barriers to highly subsidized US teams moving to Canada.

The implication is clear: freer markets in hockey means a possibility of more NHL teams, some in Canada, and at the very least, an end to NHL dependence on taxpayers in the US and Canada.

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Free trade for consumers stops at the border

Mark Milke

Anyone over the age of 30 will remember how a trip to the United States was once a painful experience for one's wallet. Think back to how often the Canadian dollar was low relative to US currency. For much of the 1980s and 1990s, the Canadian buck often traded at a substantial discount to its American counterpart. The all-time low came in the new millennium. In early 2002, one Canadian dollar could buy just 62-and-a-half American cents.

Our currency has been better off as of late partly because of relatively more prudent federal budgets since the mid-1990s, though this

is only relative—budgets are still stuffed with unnecessary and wasteful spending. It also helps that Canada had no banking crisis, has better control of its debt, and has highly sought after natural resources. This is why the Loonie hit an all-time high in November 2007, at US \$1.10 (or now, as I write, about US \$1.04).

Cost-wise, shopping and vacationing in America is pleasant for Canadians, but the caveat is that such bliss only lasts until one returns to the border. Then, the long line up and eventual interrogation over how many bottles of beer and other purchases begins. Free trade at the macro-level between Canada and the United

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Consumers still get hassled on even the smallest purchases

States began officially in 1989, but 22 years later, consumers at the border still get hassled over even the smallest purchases.

For Canadians, any time we cross the 49th parallel and return within 24 hours, we can be charged for duties and taxes right away (the federal government has no exemption for short visits). That's unlike Americans who, in the first two days, can buy and bring back \$200 worth of Canadian goods before they must hand over their credit card to US customs. Over two days, the exemption is \$800.

It's a different border experience for us. Not only do Canadians get hit with duties and taxes on same-day trips, we're also subject to lower exemption limits on longer stints abroad. After one day, our "exemption" at the border is a mere \$50; between two and seven days, Canadians can bring back \$400 worth of goods before the customs cash register begins to ring.



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After one week, Canadians have a \$750 exemption on most goods. (The exception, as always, is for beer, wine, and spirits where different rules apply; Ottawa and the provinces insist on their pound of tax and duty flesh for anything beyond a few bottles of wine and slightly more beer).

Even American policy makers have noticed how badly Canadians are treated on these miserly exemptions. When I last wrote on this in January 2011, I suggested both the US and

Canadian governments stop hassling shoppers for total purchases of less than \$1,000. (It would be nice to have an unlimited exemption, but perhaps we should expect the government to start with baby steps.)

Moreover, that tax-and-duty free amount should apply regardless of the time spent abroad.

In a wonderful coincidence, someone down south was already thinking the same thing.

Border guards should concentrate on real threats



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According to reporter Bill Curry, and courtesy of a recent Access to Information request, two American politicians, Senator Kirsten Gillibrand and Congressman Bill Owens wrote federal Finance Minister Jim Flaherty last July. They also requested a \$1,000 exemption for consumers on both side of the border.

Gillibrand and Owens promise to press the US government to let visiting Americans buy \$1,000 worth of Canadian “stuff” duty- and tax-free if Ottawa does the same for Canadians.

But the hold-up is Flaherty, who resists, citing “competitiveness issues.”

That’s weak. Two decades after Ottawa and Washington signed a free trade agreement, it’s long overdue to bring consumers directly in on the deal. Ottawa can start by not engaging in penny-pinching border protectionism. Canadian retailers can and will survive and compete. Also, it’s not as if they didn’t benefit from American shoppers when the Canadian dollar was low.

It’s always a bad idea for governments to dampen trade by getting protectionist with consumers via pesky and chintzy border exemptions. It’s a tad ironic the best advocates for Canadian consumers are two American politicians and not Canada’s own federal finance minister. Conservatives in Ottawa preach competition and free trade around the world; they should step up to the policy plate at home and respond positively to the American overture.

There’s one last and not inconsequential angle to all this: border security. The point of border guards in 2011, on both sides of the 49th parallel, should be to focus on threats to both countries, and not on my 80-year-old mother’s minor purchases in Bellingham, Washington... or someone’s sixpack.

Published in the *Calgary Herald*, May 15, 2011.



Mark Milke is the director of Alberta Policy Studies at the Fraser Institute. He also manages the Fraser Institute’s Centre for the Study of Property Rights.



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Victims, incarceration, and justice

Disastrous
outcomes
with few
consequences

Hilary Furness

In 2006, armed with pepper spray, broken beer bottles, and an axe, a group of Canadian youth savagely beat a fellow teen named Michael Levy. The severity of the offence left the nineteen-year-old victim with a severed spine, permanently confined to a wheelchair (Ward, 2007; *Vancouver Province*, 2007). One year after the attack, three youths were found guilty of aggravated assault and a fourth was acquitted (Ward, 2007).

The first convicted youth received a sentence of two years less a day, and the second was given a twenty-month conditional sentence¹ (Ward, 2007). The judgments drove many to demand redress. The original sentences for these attackers were criticized as being too lenient and, in consideration of the permanent consequences, horribly unjust.

A swing in public policy

In 2006, Canadian policy leaders prioritized intolerance for crime. The enactment of rigorous crime prevention measures and hardened responses to misconduct were placed at the top of political platforms and revisions to the criminal code were proposed to provide police empowerment and toughen judges' verdicts.

Targeting wrongdoers doesn't help the victims

Suggestions were also made to enhance confidence in the enforcement of justice and personal well-being.

It was this heightened concern for security that initiated Canada's most recent anti-crime crusade. The objective was to respond more severely to crime, and the central approach was to incapacitate through incarceration. As many of the recommended policies were retributive in nature, they would respond to the offence, target the wrongdoer, mandate the use of custody, and extend time served.

Despite political backlash, within the last five years, justice officials have been directed to apply the following changes: limiting the credit for pre-trial jail time (which has been awarded routinely as two-for-one and thereby halving the actual time served); increasing mandatory sentence lengths for violent and organized criminals; abolishing sentence "discounts" for those who commit multiple homicides; and eliminating the Faint Hope Clause (which permitted murderers the opportunity to apply for early release) (Conservative Party, 2011).



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Calls for and against retribution

Many Canadians believe in the use of retribution through incarceration, and it is often the case that these individuals view penal responses as victims' rights; they are thus in favour of the new legislative changes. However, the call for severe reprimand is not always desired. One of the most notable grievances is that Canada is adopting the American mode of punitive policies. The critics argue that this model is extremely costly and is also a futile mode of justice.²

Who's right?

Incarceration does not mend

It is true that physical detainment denies one the ability to reoffend against the general public, as once incarcerated, the perpetrator can no longer victimize society. Thus, mandating compulsory imprisonment and extending sentence lengths ensures convicted felons can do no further criminal harm for longer periods of time.

However, incarceration is punishment (and hopefully deterrence), but not restoration. If the idea of justice is to reinstate what has been lost to the victim, one must query the degree to which sentence lengthening serves to repair. In this light, consider for a moment the outcome of the attack. How much would the victim's circumstance have changed if there had been harsher sentencing judgments?

As the nastiness of criminality so often results in long-term and irreparable harm, the argument in favour of victims' rights and service agencies becomes more powerful. What incarceration cannot provide is housing, information services, and health care to victims of crime. It does not counsel victims of violence, and it does not offer support to those sexually assaulted.³

Housing federal inmates costs \$323 a day

Incapacitation is costly

In 2008/09, of the 371,800 individuals who entered the Canadian correctional services,⁴ 88,747 (nearly 24%) were admitted to provincial or federal custody—a 1% increase from the previous year (Calverley, 2010). The total cost for all Canadian correctional departments was \$3.9 billion. Of that total, incarceration at the federal and provincial levels necessitated the majority of the spending; approximately 65% of federal and 79% of provincial correctional expenses were dedicated to prisons (Calverley, 2010).

During the same period, the daily cost of housing a federal and provincial inmate reached \$323 and \$162, respectively. According to these figures, to house an additional 50 federal inmates for a single year would cost taxpayers nearly \$6 million (Calverley, 2010). The price of a new prison is upwards of \$170 million, and the proposed expenditures on upgrading and building provincial prisons is \$2.72 billion (Mallea, 2010).

In 2008, there were 2,204,643 crimes known to police. Of that total, approximately 20%, or 443,608 of the offences, were violent (Dauvergne and Turner, 2010). Of these numbers, 612 people were murdered, 21,472 were sexually assaulted, and 239,432 were assaulted. In addition, there were 721 attempted murders

and 32,372 robberies (Dauvergne and Turner, 2010). Hence, there were plenty of victims of violence.

Unfortunately, recent statistics indicate that the total resources spent on formal victim repair remain appallingly low. In 2007/08 (the most recent years the data is made available) the cost was \$178.7 million—a mere fraction of the \$2.8 billion⁵ spent on prison operating expenses (Sauve, 2009; Calverley, 2010). In this regard, it is not surprising that the 2004 *General Social Survey on Victimization* reports that only 9% of those affected by acts of violence and 13% of those haunted by sexual assault receive accredited victim service support (Sauve, 2009).

A final call for support

The consequences of the assault mentioned above are tragic. The resulting physical damage and loss of freedom are not only grave, but everlasting. In consideration of the severity of the outcome, reprimanding the offenders may prevent further acts of misconduct, but is a shamefully inadequate response.

In the vast majority of criminal acts, two parties are involved. Yet, a disproportionate amount of money, time, and effort is spent on the offender while the victim is too often overlooked.





Policy amendments in favour of the intolerance for crime must also seek to mend the pain of those impacted. Otherwise, where exactly is the justice?

Notes

1 In Canada, a conditional sentence is a prison sentence of less than two years that can be served in the community instead, so long as a number of pre-conditions are met.

2 For examples of criticism, see MacQueen, 2010; Mallea, 2010; Galloway, 2011.

3 For more information on the types of support offered by victim services, see Sauve, 2009.

4 Canadian Corrections is a division of the Criminal Justice System and is composed of two principal sec-

tors: custodial reform and community services. The former division is most easily identified as legally sanctioned modes of institutional justice, such as imprisonment. The latter includes post-penal sentencing conditions such as probation (where the offender is granted partial communal access), or is pursued as an alternative to incarceration (conditional sentencing is a common example). Other divisions of Canadian corrections include statutory release and parole (Calverley, 2010).

5 This figure relates to 2008/09 not 2007/2008.

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Understanding gasoline prices

Mark McGinley

As gas prices continue their meteoric rise, more and more Canadians are left baffled as to why. In the last year alone, average Canadian retail gasoline prices have increased by over 30% and now hover around 130 cents per litre (c.p.l.) (Natural Resources Canada, 2011). With inflation for that same period amounting to 3.3% (Statistics Canada, 2011), questions abound regarding the underlying reasons for this dramatic increase. As bewilderment turns into suspicion, Canadians are searching for someone to blame for these outrageous prices. The usual suspects have

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been lined up and the traditional accusations levied: oil companies in collusion with one another, governments' insatiable appetite for taxation revenue, or the tried and true—yet unpalatable—argument of supply and demand. But what is really causing the marked increase in gas prices? This article seeks to demystify the various components of retail gasoline prices, and attempts to offer some explanations as to what is causing the volatility in the gasoline market. The first examination is of the smallest component of retail gas prices: marketing and distribution costs.

Marketing and distribution

Marketing and distribution costs include all of the costs associated with distribution of the gasoline to wholesalers and retailers, the costs of marketing the gasoline to consumers, and the profit margins for retailers and wholesalers. Much of the public ire has been directed towards retail stations, likely because they are the most obvious targets. Gas is one of, if not the only, commodity in the world where consumers can easily observe real-time prices from a moving vehicle. Given consumers' ease of observing gas prices among competi-

tors, and the extreme degree of correlation between prices set by competing stations, it is not surprising that Canadians see collusion in the marketplace. However, it is doubtful that collusion is the reason for the similarity in retail gas prices between competitors. The visibility of gas prices serves to make consumers highly price sensitive, and with the low switching costs incurred by changing from one station to another, they will take advantage of even small differences in price between competitors. This consumer price sensitivity forces competitors to match each other's prices to avoid losing market share, or risk entering a mutually detrimental price war. Hypothetically, even if collusion were to exist in the marketplace, the effect on prices would be minimal—marketing and distribution costs are by far the smallest

component of retail gas prices and accounted for roughly 7 c.p.l. of the total retail price of gas in Canada in 2010 (Natural Resources Canada, 2011).

Refining

Refining costs include all of the material, labour, and energy required to convert crude oil into gasoline as well as any profits made by the refiner.

Like marketing and distribution costs, refining is composed of a small portion of the retail cost of gasoline, averaging 15 c.p.l. across Canada (Natural Resources Canada, 2011). But could collusion among refiners artificially inflate the price of gas? It would seem that even if refineries were to collude in order to artificially inflate gas prices they would be unable to do so. Canada produces only 3% of the world's oil supply, which makes Canada's impact on world oil prices negligible (Natural Resources Canada, 2005). Interestingly, even Canada's largest integrated refiners (meaning refiners who both produce and refine oil) purchase more crude oil than they produce domestically, essentially making them price takers with no control over oil prices (Natural Resources Canada, 2011). Further, market collusion seems unlikely given the fact that there

are 16 refineries in Canada with 7 of them independently owned—making collusion difficult (Natural Resources Canada, 2005). Additionally, retail gas stations would also have the ability to import gas from US refineries, further reducing any potential effect of Canadian refiner collusion on retail gas prices.

Taxes

One of the largest components of retail gas prices is taxes. Gasoline is taxed at a minimum of two, and in some cases three, levels: federal, provincial, and municipal. Federally, there is a 10 c.p.l. excise tax, and, in all but the five provinces with harmonized sales tax (HST) (Newfoundland & Labrador, Nova Scotia, New Brunswick, Ontario, and British Columbia), an additional 5% goods and services tax (GST) (Natural Resources Canada, 2011). Provincial taxes include a provincial excise tax, and any applicable sales or carbon taxes. Provincial taxes account for anywhere from 16.5 c.p.l. in Newfoundland and Labrador to 9 c.p.l. in Alberta, and, on average, amount to approximately 13 c.p.l. of the total retail gas price (Natural Resources Canada, 2011). Overall, in 2010, federal and provincial taxes accounted for 34 c.p.l. at the pump (Natural Resources Canada, 2011). Only three municipalities charge a transportation tax (Vancouver, Montreal, and Victoria), amounting to an additional 4.8 c.p.l. (Natural Resources Canada, 2011).

In 2010, gas prices across Canada averaged out to 103.6 c.p.l. (Natural Resources Canada, 2011). Tallying up marketing and distribution costs, refining costs, and taxes, we have accounted for just over half of the retail price of gasoline. That leaves the remaining amount for the largest component of retail gas prices: crude oil.

Crude oil

Crude oil is by far the largest ingredient in gasoline, and correspondingly the largest component of retail gas prices (Pirog, 2008). Basically, the price of crude oil can be explained through two main mechanisms: supply versus demand and financial speculation. Where problems arise is in trying to determine and quantify the individual impact of these mechanisms on the price of oil.

Supply and demand should account for the vast majority of the price of oil, and should also explain oil's price volatility. However, upon closer inspection, it becomes clear that supply and demand alone is unable to provide a clear justification for the price of oil. Today, OPEC's spare production capacity sits at more than 3 billion barrels of oil per day (Davidson, 2008). To explain why OPEC doesn't just increase production to meet demand, the Qatari oil minister stated on May 2nd, 2008, that despite spare production capacity, "OPEC will not increase production of crude oil because what is

Supply and demand alone is unable to provide a clear justification for the price of oil



happening now is not an increase in oil demand, but heavy speculation on oil futures. That's what's making oil prices so high" (Davidson, 2008). Nor does the problem rest with US or Canadian refinery capacity, as utilization rates for refineries in Canada and the US sit at 73% and 79.8% respectively—well below the maximum utilization rate of 95%. In fact, such rates constitute the lowest utilization rates

seen in over a decade (Hall and Rankin, 2011; Natural Resources Canada, 2011). At a May 2011 US senate hearing on oil prices, flustered Exxon chief executive Rex Tillerson stated that current market fundamentals and production costs would set the price of oil in the \$60–\$70 per barrel range (Hall and Rankin, 2011), which is \$43 cheaper than the highs of \$113 per barrel reached on April 29th and May 2nd, 2011 (Hall and Rankin, 2011).

An overview of the crude oil futures market helps to explain this discrepancy. The crude oil futures market is composed of two main exchanges: the New York Mercantile Exchange (NYMEX) and the Intercontinental Exchange (ICE) based in London (Pirog, 2008). Both of these exchanges are regulated, and both are primarily financial in nature, meaning that no oil is actually traded. Instead, positions are settled in cash (Jickling and Cunningham, 2008). There are also over-the-counter (OTC) contracts, which consist of futures contracts drawn up between two parties outside of the exchanges. Since such contracts are intended to govern the relationship between two private parties, they are subjected to substantially fewer regulations than contracts exchanged on the NYMEX and the ICE.

Traditionally, futures contracts are entered into by two kinds of parties: a “hedging” party and a “speculating” party. The hedging party is seeking to lock in the price of a commodity it



will require in the future (thereby hedging its risk against future price increases), while the speculating party is seeking to profit by providing such security. Here is an example of how a futures contract operates: Air Canada (the

hedging party) notices that its current supply of jet fuel will run out in one year. Concerned that the price of jet fuel may increase in the interim, Air Canada decides to enter into a futures contract with a hedge fund (the specu-



What is the effect of speculation on gas prices?

lating party) whereby the hedge fund agrees to sell the company a specified quantity of jet fuel a year from now at a specified price—the “spot” price. At this point, Air Canada is happy because it knows exactly how much it will have to spend on jet fuel in the following year, allowing it to budget accordingly. The hedge fund is also happy because it has entered into a contract that could provide huge returns for little upfront capital. Once the year has passed, if the market price of jet fuel is more than the spot price, Air Canada will have profited because the hedge fund has to sell it the agreed amount of jet fuel at a price below market value. However, if the spot price is above the market price, the

hedge fund will have profited because Air Canada is obligated to buy the specified amount of jet fuel at a price above market value.

The market for futures contracts has expanded so that contracts are now also traded between speculators, with neither party seeking to hedge against the risk of an increase in price for the targeted commodity. In these situations neither party needs, nor wants, the underlying commodity, in this case oil. When the contract is set to expire, the losing party simply settles the amount it owes in cash. In the early 1990s, 70% of oil futures contracts were entered into by producers and consumers hedging their risk, while 30% of the contracts were entered into by speculators with no desire to actually sell or purchase oil; today, these numbers are reversed (Tankersley, 2008). According to Barclay’s Capital, commodity investments by “institutional” investors, e.g., hedge funds, investment banks, sovereign wealth funds, and pension funds with no interest in the underlying commodity, hit \$283 billion in 2010 (Sheppard, 2010).

Compounding the effect of these institutional investors on the oil futures market is a 10% margin requirement on futures contracts (Davidson, 2008). A margin requirement is the amount that regulators stipulate must be placed in an account to cover off any potential losses arising from the futures contract. A 10% margin requirement effectively allows a specu-

lator to place a billion-dollar bet with only \$100 million, giving the speculator more market influence than is actually warranted. This inflated level of influence on the part of speculators has historically contributed to the futures price of oil, which increased by 86% in 2008 while world demand for oil rose by only 2% (Davidson, 2008). This price escalation has led some, including Gorge Soros, one of the world’s most successful speculators, to believe that institutional investors are creating a commodities bubble akin to the housing or dotcom bubble that is driving up oil prices and, by extension, the cost of other commodities like basic food stuffs that are transported using fossil fuels (Jickling and Cunningham, 2008).

Theoretically, the futures market should not have any impact on the physical market for oil. Indeed, no physical oil is actually being traded, only shuffled around on paper. However, in the real world, the spot market, the market for the delivery of real crude oil, bases its prices off of the futures market (Pirog, 2008). In fact, data suggests that the difference in the price of oil between the spot and future markets never varies by more than a few cents (Pirog, 2008). Given this connection it is clear that financial speculation does play a role in the price of oil, though its exact contribution is difficult to quantify.

There continues to be significant debate around the effect of speculation on oil prices,

and there is little consensus as to the extent of the impact as measured in monetary terms. Conservative estimates range from \$10 to \$30 per barrel. However, even if speculation adds only \$10 to the price generated by simple supply and demand, oil producers would be earning an extra \$6 billion a week globally, or more than \$300 billion dollars a year (Sheppard, 2010).

Conclusion

As retail gas prices continue to climb Canadian consumers are left increasingly confused as to the reasons why. The components that contribute to the retail price of gas are highly obscure, and even when carefully examined, it is difficult to get an accurate picture of exactly how much each component is responsible for the stomach-turning number displayed at the pumps. However, if nothing else, understanding the major components of gasoline prices should help inform debate around gasoline pricing, and the role of speculation in the crude oil market.

While speculation in oil futures markets may be inflating prices, it also plays a critical role in providing liquidity in the market, allowing hedgers to easily enter into and exit out of futures contracts. Without a substantial amount of speculative volume in the oil futures market, hedgers may not be able to enter into contracts on favourable terms, thereby exposing their businesses to significant commodity price

risk. In this sense, speculation may be thought of as a double-edged sword: it allows hedgers to mitigate risk, which is good for business, but may affect prices, taking them out of the realm of simple supply and demand. Ultimately, whether the benefits of speculation outweigh the potential costs is a question that only the market can decide.

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ASK THE EXPERT



“Missing Women”

& Economic Freedom

Alecsandra Dragne

The disadvantaged social and economic positions held by women in many underdeveloped nations are some of the main issues that present a serious challenge to long-term economic development. Women are not only openly and directly discriminated against, but they are also indirectly affected by discrimination, in so far as they are presented with fewer opportunities than men in their social and economic interactions. This stark inequality presents a considerable barrier to economic development; however, it is an obstacle that can be eased considerably through the implementation of public policy promoting economic freedom.

Amartya Sen, Nobel Laureate in Economics, observed that a decade ago, the ratio of women to men was approximately 0.94 in Asia, Africa, and Latin America (Sen, 1990; Sen, 2003). This represents quite a low figure, particularly in comparison with

Officer

100 million women are “missing”

the ratio of around 1.05 for Europe and North America. From these ratios, Sen developed a rough estimate of the “missing women” in the developing world. By comparing the number of women that should have been born (if these under-developed regions had the same ratio as Europe and North America) with those who were actually born, Sen finds that there are more than 100 million “missing women” around the world. In other words, if “men and women [had] received similar care in health, medicine, and nutrition” these 100 million women would not be missing (Sen, 1990). Surprisingly, according to Sen’s calculations, it appears that Sub-Saharan Africa does not exhibit a skewed sex ratio at birth. However, he records 44 million women missing in China and 37 million missing in India overall. Sen points out that decade later, due to two opposing trends, the sex ratio has not changed.

Although the disadvantage that women experience in terms of mortality (particularly death at young ages) has declined, a new movement has taken hold, namely that of sex-specific abortions against girls. This practice has become quite widespread across many societies, due to the accessibility of new technologies that enable doctors to determine the sex of the fetus. Sen’s analysis is meaningful, as it quantifies the extreme inequality that has been

plaguing women in the developing world with long-lasting effects, particularly in India and China.

Economists Siwan Anderson and Debraj Ray built on Amartya Sen’s research to provide an analysis of the composition of the “missing women” by age and cause of death, thereby qualifying some of the earlier discoveries and shedding some more light on the sources of these “excess deaths” (2010). Similarly to Sen, Anderson and Ray compare the average death rates of women in developed countries to those in developing countries and categorize the “missing women” by age and disease. Their results are quite remarkable. Although previous research (including Sen’s) had emphasized excess female deaths at birth or at very young ages, Anderson and Ray’s analysis shows that the story is significantly more complex.

About 37–45% of the missing women in China occur at birth and in infancy—these are termed



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“prenatal factors” (Anderson and Ray, 2010). However, the situation is markedly more complex for India. The authors calculate that only 11% of missing women in India are due to prenatal factors, including sex-specific abortions against girls. In fact, the most prominent source of excess female deaths in India at *young ages* (between zero and four years) are infectious, respiratory and perinatal diseases, amounting to about 15% of the total, or 260,000 missing girls. Infectious diseases account for about half of these deaths. To put this number into perspective, maternal deaths in India, generally regarded as a significant issue, account for



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The causes of excess female deaths are diverse and complex

about 130,000 of the yearly excess female deaths. The largest number of excess female deaths in India, however, occurs at *older ages* mainly due to cardiovascular disease, a cause that far outweighs prenatal or maternal excess deaths. Essentially, this means that compared to developed countries, Indian women are affected by cardiovascular disease at a *closer rate* to men. In other words, the discrepancy between men and women in the rate of deaths resulting from cardiovascular disease is smaller in India than what is natural biologically. Another disquieting issue for India is death from “injuries”: for all ages, injuries (both unintentional accidents and intentional acts of violence) account for over 255,000 excess female deaths, far exceeding maternal mortality. In addition, about 30,000 women are missing from the 15–29 years category as a result of death from “intentional injuries” (Anderson and Ray, 2010).

Another surprising finding made by the authors is that the annual flow of missing women (as a proportion of the female population) in sub-Saharan Africa is quite large, adding up to roughly 1.53 million missing women in

2000 (Anderson and Ray, 2010). This may seem confusing, since the sex ratio at birth for sub-Saharan Africa is quite equal, at 1.03 (Anderson and Ray, 2010). However, we can reconcile Anderson and Ray’s findings with the parity sex ratio by emphasizing that none of the missing women are situated at birth. In other words, girls and boys are not treated differently at birth—the missing women are spread out over the age spectrum. In fact, as a fraction of the female population, the number of sub-Saharan missing women is *higher* than the Chinese and Indian populations. The biggest reason for missing women in Sub-Saharan Africa seems to be HIV/AIDS, by far (Anderson and Ray, 2010). The authors’ calculation yields over 600,000 annual excess female deaths from this disease; this is over a third of all missing women for the region. This finding is so striking because the death rate from the HIV/AIDS virus is 1.2 times higher for women than for men in Sub-Saharan Africa. Even more shocking is that in the rest of the world, HIV/AIDS death rates are *higher* for men than for women, even going up to a ratio of 4:1 in developed countries (Anderson and Ray, 2010). Although other causes, most notably maternal deaths, are also a significant cause of the missing women in Sub-Saharan Africa, it is imperative to emphasize that for whatever reason, there is an obvious bias against women in terms of HIV/AIDS deaths in this region.

In conclusion, Anderson and Ray’s findings show that the biggest fraction of missing

women come from disease-by-disease effects: “in India, the number is 1.64 million out of the aggregate estimate of 1.71 million, in sub-Saharan Africa 1.39 million out of a total of 1.53 million, and in China 1.59 million out of 1.73 million” (2010). The authors show that comparing aggregate sex ratios does not deliver the full story regarding missing women. By looking at distributions by age and disease, we can be closer to understanding whether direct gender discrimination or various other factors are responsible for the large number of missing women around the world.

These studies have established that there is indeed a significant problem of “missing women” and that the causes are quite diversified and complex. What can be done about it? Although there is an array of public policy tools that can be undertaken, economic freedom remains an essential mechanism that can help substantially redress the inequality between men and women. While it is by no means a complete solution, economic freedom can directly and indirectly empower women through a variety of mechanisms. First, nations that are more economically free perform substantially better than non-free countries in crucial indicators of well-being. Economically free countries exhibit a higher Gross Domestic Product (GDP) per capita and higher average incomes, better life expectancy and life satisfaction, less corrup-



Greater access to credit can empower women

tion, more secure political rights and civil freedoms, etc.¹ With a higher degree of economic freedom, developing countries are better poised to experience and maintain economic development.

How exactly can this process benefit women? Certainly, with economic development comes greater access to basic health provisions that decrease maternal mortality and the risk of disease in general, for both men and women.

In addition, greater economic freedom allows women to have greater access to education, a provision which increases their human capital and thus increases their employment opportunities and bargaining power in the household.

Finally, there is another formidable avenue through which women can be empowered: greater access to credit markets. Women in developing countries are denied an important source of income, because they cannot

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Bing Giang

Economic freedom brings health care, education, and employment opportunities to women

gain entrance to credit markets. This occurs because it is men who are generally the owners of property or wealth (due to cultural and traditional design). Such assets can be used as collateral, a necessary condition when borrowing. Economic freedom can profoundly empower women by giving them more access to credit markets, thus allowing them to borrow in order to pursue entrepreneurial activities. Such occupations give women opportunities to work outside the household and become more independent, both socially and financially. Economic freedom can simply help by developing proper functioning credit markets, which are non-existent or barely operational in many developing countries. In addition, governments can pursue microcredit finance schemes (such as the Grameen Bank) focused on lending to

women.² There seems to be evidence that even when the money borrowed by a wife is simply transferred to her husband, women still benefit in many ways, such as being subjected to less violence and gaining more self-respect (Kabeer, 2001). Therefore, greater access to credit can go a long way in changing attitudes towards women and giving them more alternatives to become meaningful economic and social participants of their societies.

The evidence suggests that the complexities surrounding the issue of “missing women” are extensive. There is no calculation that can fully account for the extent of discrimination against women and it is very difficult to separate direct discrimination from other contextual factors that may lead to excess female deaths. However, it is undeniable that the “excess deaths” of 100 million women have had and will continue to have a detrimental effect on the social, cultural, and economic fabric of the developing world if they are not addressed.

Notes

- 1 For more information, see the *Economic Freedom of the World: 2010 Annual Report*.
- 2 For more information on the Grameen Bank, see www.grameen-info.org.

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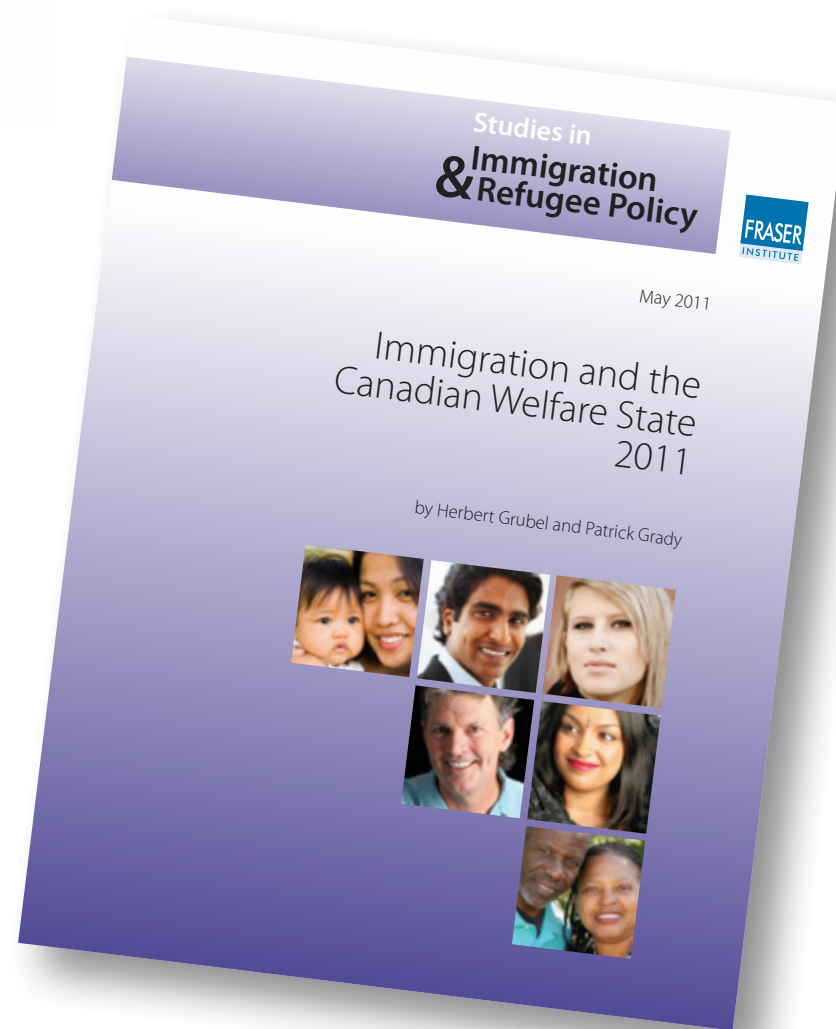


Immigration and the Canadian welfare state

A new report by the Fraser Institute recommends that Canada's immigrant selection process needs to be revamped to focus on admitting people with Canadian job offers and skills needed by employers.

"Recent immigrants earn incomes that are, on average, just 72% of those earned by other Canadians and pay only about one-half of the income taxes. At the same time, they absorb nearly the same value of government services and transfers as other Canadians. As a result of Canada's welfare-state policies, our progressive income taxes, and universal social programs, these immigrants impose a huge fiscal burden on Canadian taxpayers."

The Fraser Institute's Immigration study concludes that in the fiscal year 2005/06 the immigrants on average received an excess of \$6,051 in benefits over taxes paid. Depending



on assumptions about the number of recent immigrants in Canada, the fiscal burden in that year is estimated to be between \$23.6 billion and \$16.3 billion. These estimates are not changed by the consideration of other alleged benefits brought by immigrants.

[Read the complete report](#)

To understand health insurance performance, measure the right outcomes

Are Canadians getting good value for money from their health insurance system? This question is often discussed among health economists and policy makers. And while it's important to know whether citizens are getting the best "bang for their health buck," it's imperative that the appropriate outcomes are measured in order to accurately assess the economic performance of a health insurance system.

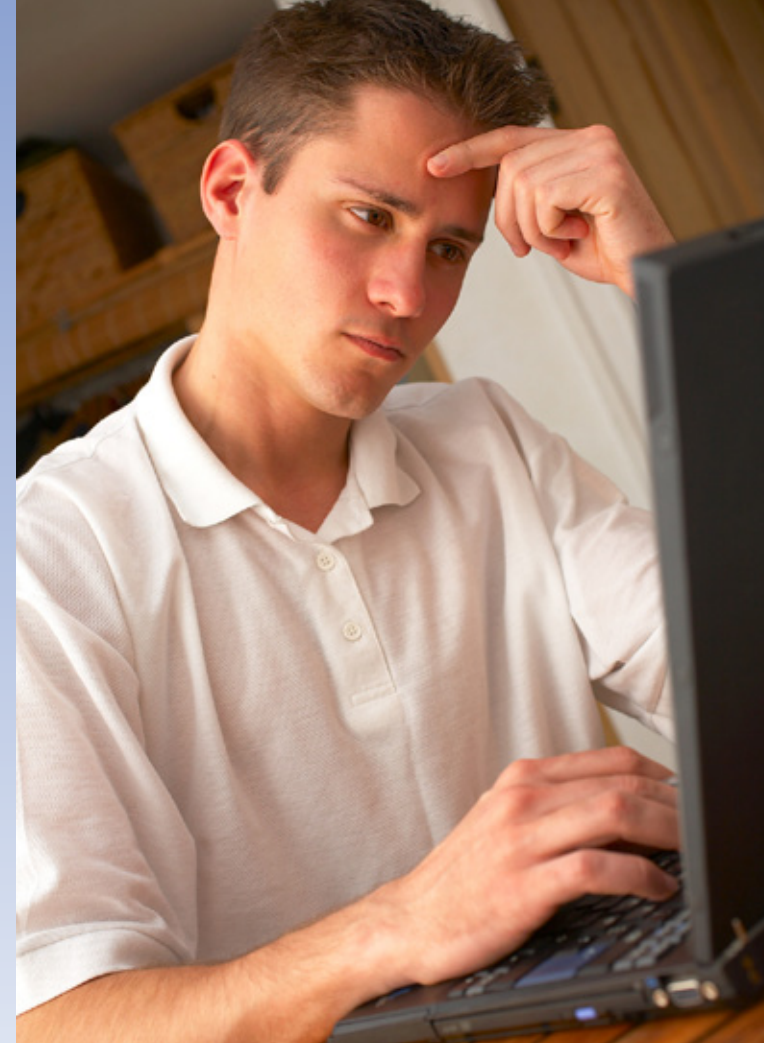
The best way to gauge whether citizens are getting value for the money spent through a health insurance system is to determine the availability of medical goods and services in relation to the associated level of national health spending. Unfortunately, some health researchers continue to measure broad population health statistics, which really doesn't tell us how well a health insurance system is performing.

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