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Economics Outside the Classroom

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of intervening variables. Concerning young motherhood, these intervening variables could take the form of decisions such as early marriage or low educational attainment that in turn influence the standard of living. According to Seeborg, "if you don't look at indirect effects, then you truly don't know the impact of background decisions on the future standard of living."

In a current research effort, Seeborg is examining young immigrants brought by their parents to the United States to find out how important "ethnic capital" is on their eventual economic success. Seeborg defines ethnic capital as the "overall level of human capital that various ethnic groups in the United States achieve." As members in the sample completed part of their schooling abroad and part of it here, the study seeks to evaluate the influence that the ethnic group that the immigrant joins in the U.S. has on future educational attainment. Seeborg hypothesizes that the greater the ethnic capital of the group is, the greater the economic performance of the respondent (immigrant) will be. Although he admits the study still needs a lot of work, Seeborg's initial results show that even after controlling for age, experience, and language skills, ethnic capital proves to be crucial to the success of the young immigrant. "There seems to be an external effect that comes from members of the group . . . the cultural emphasis on education, independent of other choices, is very important."

In another project, not related to the NLSY, Seeborg is working in accord with two other professors to study the importance of the emerging "floating population" in China. Seeborg states that, "as markets become freer, it is easier for people to move from rural into urban areas . . . and to work under contracts with firms." Estimating the floating population at 100 million people currently, Seeborg is researching what institutional changes have caused the emergence of this population and what implications it has for the rapidly changing Chinese economy.

Although Seeborg remarks he still has quite a bit of work to do on some projects, new possibilities for research continuously present themselves. Nonetheless, the Economics department of IWU was pleased to see him back in the fall of 1996.

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I. INTRODUCTION

Each year, Illinois Wesleyan's Economics Society, in conjunction with its faculty, brings special guests to campus to address practical applications of economics. The Economics Department recognizes the need to relate classroom material to every-day activities in business and government. This fall, some of the distinguished guests included Dr. David Vance, chief economist for Caterpillar, Illinois State Representative Bill Brady, and Bloomington Alderman Mike Matejka.

II. CORPORATE USE OF ECONOMIC FORECASTING & A LOOK AT THE CPI

With an undergraduate degree in political science from MIT and a Ph.D. from Notre Dame in economics, David Vance is the chief economist for Caterpillar's Business Intelligence Group, an internal consulting firm which renders marketing research, competitive analysis, and business information services. Caterpillar is a multinational corporation (MNC) specializing in the production of earth-moving machinery and employing around 54,000 people, with revenues of $16 billion in 1995 and profits around $1 billion. In 1995, 52% of Caterpillar's sales occurred outside the United States, and Caterpillar has marketing organizations in virtually every country in the world.

The most intriguing aspect of Dr. Vance's talk was his denunciation of the current system of calculating the Consumer Price Index (CPI). He contended that the CPI overstates the rate of inflation by up to 2%, which a congressional advisory panel validated on December 4, 1996[1]. This holds massive implications for our economy. Because the CPI is used to determine social security benefits, government pensions, cost-of-living raises, and welfare eligibility, an artificially inflated CPI translates into a perennial stimulation of aggregate demand. This, in turn, precipitates demand-pull inflation year after year. As a result, the Federal Reserve would attempt to fight inflation that does not exist. The coexistence of expansionary fiscal policy with contractionary monetary policy--both being unwarranted--would artificially force up interest rates while leaving aggregate income and output steady, rechanneling expenditures from investment to consumption. This situation does not bode well for the future.

III. THE PRE-ELECTION POLICY DEBATE: THE REPUBLICAN PROPOSAL

Bill Brady, a Republican Representative, in the State legislature, commenced the second session of the year, the election policy debate, by setting out how the Dole / Kemp economic plan would resolve what he feels is the most important economic and political issue--the national debt. Brady explained how each newborn child is born carrying $20,000 dollars in national debt. For the past three years under the stewardship of President Clinton, the economy has grown at an "anemic" 2.4% per year, a whole percent lower than the average recovery rate since World War II. According to Brady, this has led to falling income, shrinking wages, increased poverty, and a historically high number of bankruptcies. He rationalized Dole's plans to cut taxes, balance the budget, provide state tax relief--all of which are targeted to achieve a 3.5% growth rate per year, which would double median family income if maintained for a generation.

The major issue of the campaign was the 15 percent, across-the-board tax cut. Brady's argument that the cut would spur economic growth stems from Reagan's idea of supply-side economics. They claim that creating incentives for individuals and firms to increase productivity will shift the aggregate supply curve out, having an indirect effect on increasing aggregate demand. At this point in the dialogue, Mike Matejka, Bloomington Alderman and Editor of the *McLean / Livingston County Labor News*, jumped in and countered that as a result of the tax cut, there would need to be more local taxes to make up for federal program cuts. Furthermore, there would be job cuts, leading to crime and taxpayers paying even more. The wealthy are the real winners and there is no guarantee the U.S. would see increased investment because of foreign leakages. Brady responded that he has more faith in the American citizen. Perhaps Brady has a bit too much faith in his fellow Americans as well as too much optimism in supply-side economics.

Over six years, the Dole plan proposed cutting taxes by $548 billion, leading to a possible growth dividend of $147 billion[2]. Yet, his proposed spending cuts amount to approximately $217 billion. Thus, the national debt would grow by $184 billion. When the national debt increases, the government sells bonds. This increases competition for savings, raising interest rates. High interest rates lead to decreased borrowing for investment, including business fixed investment such as the machinery Caterpillar sells, residential investment, and inventories. These investment fluctuations correspond with a slow economy.

IV. AN INTERESTING COUNTER BY MIKE MATEJKA

Mr. Matejka kicked off his commentary on the national debt by asserting that the deficit is not always bad. This certainly perked all ears. He alleged that it depends on for what we are in debt--a basic the-ends-justify-the-means argument. Dole proposed cutting spending in areas such as student lunches and education subsidies--all justified reasons for going into debt in Matejka's eyes. On the other hand, he views national defense as a deficient excuse for debt. Basically, Matejka's underlying message was a defense of bureaucracy, remarking that it "reflects us and ensures safety."

Regarding government bureaucracy, we need to consider the government's very difficult job in balancing efficiency and equity in decision-making. Yes, perhaps the military reserves need not be as large. Yet, let us not forget that our national defense provides Americans with a sense of security, promoting trust in our government. People's perceptions are integral to how both an economy and a democracy work. From the banking industry to police enforcement, the American system is founded on faith and public opinion. On the other hand, a large bureaucracy casts shadows on transparency, such as the ready access to ascertain exactly where tax revenues are going. This weakens our trust in the government, whose stability is imperative to a healthy economy.

V. A CONTINUED CORPORATE PERSPECTIVE: THE ELECTION DEBATE

Though Dr. Vance was not present at the debate between Republican Bill Brady and Democrat Mike Matejka, one can imagine his response based on his presentation regarding the economic policy debate of the 1996 Presidential campaign. He first emphasized the reality that there would be very little impact on the economy if Clinton were re-elected (which, of course, he was). However, Vance was on campus in October and thus speculated on the effects if Dole did happen to win.

Vance's vantage point provided another dimension to the argument against the Republican plan. He pointed out cutting taxes raises disposable income and consumption, leading to a higher interest rate. The economy grows too fast, prices rise, and the Fed (or Alan Greenspan) will raise short-term interest rates. Because of the corresponding government budget deficit, the bond market will raise long-term interest rates. Therefore, cutting taxes will not foster growth because the Fed will stop it in order to fight inflation, the leading economic indicator they seem to monitor the most closely.

This analysis is important to Caterpillar, for interest rates directly affect a large capital based corporation such as Caterpillar. Capital goods companies suffer under higher interest rates. The cost of taking out a loan on capital goods goes up, making people less likely to invest[3]. Overall, whether one looks at the 15% tax cut from the angle that the Fed will not allow the economy to grow too quickly anyway or from the argument presented earlier--that it would lead to investment fluctuations and thus a slowed economy--Dole's tax plan appears to have been a political ploy and only that. He did not take into account the possibility that voters are forward-looking.

VI. CONCLUSION

Overall, from Dr. Vance to the Presidential campaign debate, the co-curricular opportunities offered this semester were informative, engaging, and worthwhile to any person--whether an economics major or not. There were also many other notable speakers who spoke on the banking industry, the insurance arena, and other topics relating to the discipline of economics. People often ask if a degree in economics is really practical. If you want an answer to this question first-hand, attend one of the Economic Society's events on Wednesday nights, where one learns just how important the understanding of all different aspects of economics truly is to the effective maintenance and improvement of this world.

FOOTNOTES

1. The panel determined the inflationary overstatement to be 1.1%.

2. Some leading economists have arrived at this figure.

3. Another way to look at this is that the opportunity cost of owning capital goes up, for the money spent on capital could be earning interest in a bank.