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Editors' Summary

Chile's economic performance over the last two decades is one of the few success stories in Latin America during this period. The country's per capita gross domestic product (GDP) grew at an average rate of 4.3 percent a year, and the fraction of the population living under the poverty line decreased from 45.1 to 13.7 percent. The contrast with other countries in the region is stark. For example, Brazil's per capita income, corrected for purchasing power parity (PPP), was 45 percent higher than Chile's in 1985, but it lagged by 30 percent two decades later. These trends have motivated the search for the determinants of the Chilean success story. Early and deep reforms following the prescriptions that eventually became known as the Washington Consensus are one line of explanation. The way in which Chile deviated from this blueprint is another factor.

In "Taxes and Growth in a Financially Underdeveloped Country: Evidence from the Chilean Investment Boom," Chang-Tai Hsieh and Jonathan Parker put forward a provocative thesis that goes beyond the standard explanations for Chile's performance. They argue that a reduction of the tax rate on retained profits from 50 to 10 percent in 1984 explains the investment boom underlying the so-called Chilean growth miracle. A central argument of their thesis is that taxation of retained profits is particularly distortionary in an economy with good growth prospects and poorly developed financial markets—as Chile arguably was after liberalizing the economy in the late 1970s and suffering the banking crisis of 1982—because it primarily reduces the investment of financially constrained firms. Consistent with this theory, they find a large increase in aggregate investment after the reform, which was entirely funded by an increase in retained profits.

Hsieh and Parker's thesis has its caveats, and both discussants do a good job of pointing them out. Yet sometime in the future, when the dust has settled and a synthesis emerges, their thesis is likely to represent a significant part of the explanation for Chile's success story.

Inequality is often cited as a possible explanation for Latin America's lackluster economic performance. Some of the mechanisms through which inequality may hinder growth relate to unequal opportunities and lack of economic mobility. In "Social Mobility and Preferences for Redistribution in Latin America," Alejandro Gaviria uses Latinobarómetro data to explore the relationship between intergenerational mobility and political attitudes in seventeen countries in Latin America. While it has long been known that inequality (say, in educational attainment) is higher in Latin America than in the United States, this paper presents the first multi-country study of differences in educational mobility. The news is not good: in addition to being considerably more unequal, Latin American countries tend to display lower levels of mobility across generations than do developed countries.

Does this matter for the outcome of the political process in Latin America? Using Latinobarómetro data on political attitudes, Gaviria finds that demands for redistribution are relatively high in Latin America. Preferences for redistribution are (negatively) correlated with socioeconomic status, more strongly than in other regions, suggesting that the Meltzer-Richards paradigm (that the poorer the median voter, the more redistribution he or she will demand) seems to apply to the region. But one's present position in the distribution is not all that matters: those who are most optimistic about mobility seem to demand less redistribution, as predicted by the hypothesis on prospects for upward mobility. Finally, people's own views of the causes of inequality also matter. Those who feel that poverty is caused by external circumstances, rather than lack of effort, or that hard work does not guarantee success, are more likely to favor an active redistribution policy than those who hold the opposite views. Sadly, a majority of Latin Americans believe that opportunities are not equal for all, that poverty is due to external circumstances, and that hard work is no guarantee of success. This probably reflects their own experiences of limited mobility, and it probably also helps shape their political demands for the role of the state. If the recent literature on the role of beliefs in shaping different politico-economic equilibria is right, then Gaviria's analysis of these correlations would suggest that Latin America might end up trapped in an equilibrium characterized by high redistribution, low effort, and a low belief in effort.

Taxes on retained profits and limited mobility are two nonstandard explanations for economic performance. Country size is another. In "Regional Integration: What Is in It for CARICOM?" Mauricio Mesquita Moreira and Eduardo Mendoza address an old concern in the Caribbean region—namely, whether the small size of the countries has implications for their development prospects. Regional integration has often been proposed as a solution for the problems of small countries, and it has been part of the Caribbean policy agenda for many decades. The authors explore this issue from many perspectives, beginning with whether size is truly a liability. Given the possibility of trade, a small country can achieve relevant economies of scale by specializing in a few sectors while importing other goods. In this way, being small may not be so costly in a globalized world where transportation costs and other trade barriers have fallen substantially. The authors review and extend some recent empirical research to show that the small Caribbean countries do not seem to be paying a significant price for their size. These considerations may explain why the Caribbean Community and Common Market (CARICOM) appears to have generated few benefits and significant costs. Additional factors include the slow implementation of the agreement in the early decades, the undeniable fact that the CARICOM members have very similar factor endowments, and the small size of the whole region.

The limitations of regional integration pose a particular challenge in light of the erosion of unilateral preferences for CARICOM exports to world markets and the growing global competition for aid and foreign direct investment. What, then, can be gained from regional integration? The authors convincingly argue that trade can alleviate the possible disadvantages associated with size for certain nontradable sectors, such as infrastructure, health, education, and other areas for which the minimum efficient scale surpasses most Caribbean countries. Although some efforts are under way in this direction, the paper concludes with a call for the region to take this much more seriously.

Weak governance is yet another possible explanation for poor economic performance in some Latin American countries. A prominent factor in this regard is capture of the political agenda by interest groups. Electoral campaign finance legislation is often discussed as a deterrent for this problem. Limiting contributions by interest groups or individuals, making political funding more transparent, and introducing state financing for political campaigns are among the central elements considered in such legislation.

In "Electoral Campaign Financing: The Role of Public Contributions and Party Ideology" Adriana Cuoco Portugal and Maurício Bugarin begin by reviewing the plethora of electoral campaign finance legislation and reform, both in Latin America and elsewhere. They also provide detailed evidence on how illicit political financing has ignited many crises in the region. The core of the paper develops a model to analyze the effects of public financing of electoral campaigns on policies announced by ideologically oriented parties, subject to pre-electoral lobbying. Parties' ideologies lead politicians to announce divergent platforms, even though this means losing some votes. Divergent platforms, in turn, make lobbies actually contribute to parties' electoral campaigns. The announced platforms are biased in favor of the parties' ideology and the interest groups' preferred policies. Finally, increasing public financing of electoral campaigns may generate unequal electoral competition and may significantly raise the chances of one party's becoming hegemonic, wiping out party competition in the long run.

The last paper in this issue examines the effects of Mexican interstate (internal) migration and international return migration (Mexican workers who return to Mexico after working abroad) on wages and employment in the *maquiladora* industry in Mexico. One motivation behind Scott Atkinson and Marilyn Ibarra's article, entitled "The Effect of Mexican Workforce Migration on the Mexican *Maquiladora* Labor Market," is the relocation of a number of firms in recent years from Mexico to China in search of lower labor costs.

Interstate or return migration in pursuit of employment in Mexican manufacturing assembly plants can either reduce or increase the market wage for unskilled and skilled workers, depending on whether it expands or contracts the supply of available labor. Migration can also shift labor demand to the right. This could reflect an increase in productivity if migrants are more skilled than local workers or an increase in the demand for goods produced by the migrants. The share of migrant workers is quite significant. Approximately 7.5 percent of the total number of workers are interstate migrants, while 5 percent are return immigrants.

The paper estimates cost and demand functions for Mexican skilled and unskilled labor in the textile *maquiladora* industry in twenty Mexican states for 1998–2001. The study concludes that the demand for labor is sensitive to costs, but more so for skilled than unskilled labor. Separately, the authors use the 2000 Mexican census to estimate the effect of return and interstate migration on the equilibrium wage in the manufacturing industry labor market. They find that interstate migration has a negative effect on wages, while international return migration has a modest positive effect. They then use a combination of these two models to compute the effects of both types of migration on the wages and employment of skilled and unskilled workers in the textile *maquiladora* industry, concluding that interstate migration has led to a reduction in wages and increased employment in this sector in a number of Mexican states.

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