RAQUEL BERNAL
UGO PANIZZA
RODRIGO SOARES
ROBERTO RIGOBÓN

Editors' Summary

This volume of *Economía* consists of four papers. The first paper, by Nick Barr and Peter Diamond, discusses the lessons from economic theory for the design of pension funds. This article is based on a book written by the same authors, and according to Diamond, this is perhaps the last paper they will write on pension funds. We are honored and ecstatic that they decided to publish this piece in *Economía.* From pension design, we move to the current subprime crisis. The second paper, "Containing Systemic Risk: Paradigm-Based Perspectives on Regulatory Reform" by Augusto de la Torre and Alain Ize, offers new institutions for dealing with the global financial crises. The third paper, "Labor Market Rigidities and Informality in Colombia" by Camilo Mondragón-Vélez, Ximena Peña, and Daniel Wills, studies how labor market rigidities such as minimum wage regulations affect the size of the informal sector. The paper finds that labor market rigidities tend to increase informality, and it has a larger impact on unskilled workers than on skilled workers. Finally, the fourth paper studies the impact of central bank communications on the performance of the economy. The paper, "Communicational Bias in Monetary Policy: Can Words Forecast Deeds?" by Pablo Pincheira and Mauricio Calani, studies how central bank communications actually predict the path of future monetary policy.

In 2008 Nicholas Barr and Peter Diamond published a book entitled *Reforming Pensions: Principles and Policy Choices.* From that extensive research and experience, they decided to summarize the main policy lessons for designing pensions for Latin America. The key lessons that arise from the theory are the following: First, pension systems have multiple objectives. Although this might sound trivial, it is rarely recognized when a pension system is to be designed. Second, different pension designs have very different risk-sharing implications for the participants. Some systems put more of the burden on the individuals, others on the government, others on the young, and so forth. Third, there is no single pension system that is the best for all countries, at all times. Again, this might sound trivial, but few bureaucrats have ever even considered the possibility that their country's pension system might not be the perfect one. Fourth, because of the existence of clear market failures, a pension system should be designed in the context of the second-best option. Finally, and almost a corollary of the previous four, moving to a funded system might not be appropriate given the specific conditions in which the system operates. After summarizing the lessons, the paper explores the policy implications for high- and middle-income countries. The paper reduces the complexity of all possible choices to a smaller set, concentrating on those aspects of the design that are particularly relevant.

Augusto de la Torre and Alain Ize discuss the possible institutional arrangements needed in international financial markets to deal with the global crisis caused by the subprime collapse. The paper starts by considering the four possible financial paradigms that govern banking and financial regulation: costly enforcement, collective action, asymmetric information, and collective cognition. Each of these paradigms has an associated market failure, such as rational bubbles, coordination failures, moral hazard, and cascades, respectively. After discussing the framework for analyzing the problem of regulation, in which all paradigms need to be contemplated, the authors proceed to their recommendations for improving the current regulatory environment.

Camilo Mondragón-Vélez, Ximena Peña, and Daniel Wills study the evolution of labor market informality in Colombia between 1984 and 2006. This period is particularly interesting because it has booms and recessions, as well as changes in labor market regulation. In particular, there are significant changes in nonwage costs and minimum wages. The authors use the time heterogeneity in these variables to disentangle their effects. As expected, they find that when there are high nonwage costs and high minimum wages, "the formal sector must adjust to the economic cycle through quantities rather than wages, cutting back on mostly low-skilled jobs." This also implies a decrease in wages in the informal sector. In their regressions, it is clear that the informal sector suffers as much as the formal sector—in other words, the supposedly second-order effects on the secondary market of tighter labor regulation in the formal sector are actually first-order effects. The paper does not directly discuss welfare implications, but rather focuses on the negative effects of labor market rigidities.

One of the most interesting findings in the paper are the results presented in table 5, which reports the transition probabilities controlling for skill level. These coefficients (and their significance) show an extraordinary pattern: they highlight the tremendously negative impact these types of interventions have on the most vulnerable groups in society. For instance, the impact of minimum wages on the transition probabilities from formal to informal are not only statistically different from zero, but one is positive and the other negative! The same pattern is found for unemployment spells and for nonwage costs and the transition from informal to formal. In other words, the most vulnerable groups become even more vulnerable and more likely to move to informality, while skilled workers see their position strengthen. This paper should be one of the starting points of labor market reforms in Colombia, as it provides an additional piece of information by looking at the distributional effect of such rigidities.

In the fourth paper, Pablo Pincheira and Mauricio Calani evaluate one of the most obvious questions about the communications issued by inflation-targeting central banks: when the central bank promises a tightening (loosening), do they actually tighten (loosen)? In other words, does the central bank actually do what it said it would do? Their purpose is to evaluate the monetary policy forecast generated by different models and compare it to the stance announced by the central bank. They show that in the case of Chile, the Central Bank follows a monetary policy path that is consistent with the Board's announcement and not necessarily consistent with the model predictions. They use two different models to evaluate the robustness of their results.

The exercise is simple, but novel. They use different models to produce interest rate forecasts and then compare the accuracy of the forecasts with the Central Bank of Chile's promised interest rate path. They show that the Central Bank's announcement contains information beyond what is contained in the models—and hence beyond the current macroeconomic data. They also show that interest rate forecasts can be improved by using the communicational bias, suggesting that the information contained in the Central Bank's announcement is orthogonal to the information in the market. Finally, the paper finds that the predictive power of the monetary policy stance is highest at long-run horizons. In other words, the communicational bias does not outperform the models one month ahead, but it has a much better performance when horizons are extended to six months or more.

Economía is the result of a collaborative effort, and as usual, thanks are due to many people who made that process successful. Associate editors worked hard to guide papers to publication, members of the panel contributed valuable insights and spirited discussions, and *Economía* staff, in particular Roberto Bernal, helped put it all together. Without his steady and abundant effort, this volume would not have come to fruition. These papers were presented at two of our meetings. Two of the articles were presented during the annual LACEA 2009 conference, which took place at the Universidad Torcuato Di Tella in Buenos Aires, while the others were presented during our 2010 spring conference, which was held at the Inter-American Development Bank (IDB) in Washington D.C. We thank Torcuato Di Tella and the IDB for their extraordinary support.