

Technical journals, institutional working paper series and specialized Web sites publish a blizzard of economic research, most of which is read only by insiders. And often with good reason – one must be motivated to plow through, say, Mohamed A. Ismail and Tarek Ibrahim Eldomiati’s paper “Bayesian Identification of the Predictors for Capital Structure in Egypt,” in the *Journal of Applied Corporate Finance*. But some deserve a wider audience, and from time to time, the *Review* flags a few that worth a look by non-specialists. Check these out...

PARADISE LOST?

Back in the 1960s, long before Ronald Reagan was president and Adam Smith had been granted sainthood, Sweden was widely viewed as one of the world’s most successful economies. Not only were the Swedes rich, lavish social programs guaranteed every man, woman and child a comfortable place at the table. But in the 1970s, Sweden’s economy slipped, and the country’s high tax rates and tangle of regulations became a symbol of all that was wrong with the European welfare state.

Now it’s time for a little revisionism. According to Valerie Cerra and Sweta Chaman Saxena of the International Monetary Fund and the University of Pittsburgh respectively, commentators got the story all wrong. In their view, Sweden’s economic woes had little to do with the failings of the welfare state and much to do with the weakness of its financial system. [*IMF Working Paper WP/05/29, “Euro-sclerosis or Financial Collapse: Why Did Swedish Incomes Fall Behind?” February 2005. Download free from www.imf.org.*]

TOLD YOU SO

When the euro was launched in 1999, Martin Feldstein of Harvard and the National Bureau of Economic Research was one of the few high-profile economists to argue that Europe’s monetary union was built on a framework of contradictory policies that would lead to political and economic conflict.

Specifically, he noted that centralizing monetary policy while leaving fiscal policies in the hands of individual national governments would lead to chronic budget deficits, because each national government would bear only a small portion of the adverse consequences of its profligacy. Here, Feldstein (who is widely seen as a candidate to replace Alan Greenspan at the Fed) describes what came to pass – in particular, how the Eurozone countries have effectively abandoned rules designed to keep cyclical deficits in check, and how the system could be saved from itself. [*NBER Working Paper 11249, “The Euro and the Stability Pact,” March 2005. Download (\$5) from www.nber.org/papers/w11249.*]

MELTING POT OR MOSAIC (REDUX)

In 19th century America, ethnic immigrants largely lived among their own, in part because they were denied access to housing and jobs among the native-born. It's not surprising, then, that the gradual desegregation of immigrants in the first half of the 20th century was seen as a victory for tolerance and social mobility. What may surprise is that, in the past three decades, the pattern has again reversed; immigrants are more segregated, even as segregation based on race has declined. David Cutler (Harvard), Edward Glaeser (Harvard) and Jacob Vigdor (Duke) find the obvious explanation – that the new immigrants are poorer and thus face greater discrimination – is wrong. Rather, the phenomenon seems to follow from the rise of suburbs and the decline in public transportation, which have effectively forced young, poor immigrants to live in city centers. [*Harvard Institute of Economic Research Discussion Paper 2071, "Is the Melting Pot Still Hot?" May 2005. Download free from post.economics.harvard.edu/hier/2005papers/2005list.html.]*

DEMOCRACY'S GROWING PAINS

These days, hardly anyone has high expectations for young democracies – think Zimbabwe or Russia, or, for that matter, Iraq. But it isn't easy to pinpoint why democratic start-ups have such severe growing pains, in many cases even failing to deliver services – everything from education to garbage collection – as well as the autocracies they replace. Philip Keefer, an economist at the World Bank offers a somewhat surprising explanation: politicians in young democracies have little credibility from the get-go, and are thus forced to overpromise to selective interest groups at the expense of the general public in order to gain



and hold power. [*World Bank Policy Research Working Paper 3594, "Democratization and Clientelism: Why are young democracies badly governed?" May 2005. Download free from econ.worldbank.org.]*

CHARTER SCHOOL BLUES

To many disenchanted with the quality of public education, the answer lies in competition. And for many of them, the solution is charter schools – non-profits that run schools with public money and supervision. But, according to Eric Hanushek (Hoover), John Kain (University of Texas, Dallas), Steven Rivkin (Amherst) and Gregory Branch (University of Texas, Dallas), Texas' experiments with charter schools are not reassuring. Average charter school quality, measured in terms of reading and math achievement, is no better than that of public schools. Charter schools do offer the advantage that parents can vote with their feet, switching schools where they are not satisfied. But even here, there's a rub: the parents of poor children – the kids who need good schools the most – are less likely to leave bad schools. Other scholars, it should be noted, come to very different conclusions. [*NBER Working Paper 11252, "Charter School Quality and Parental Decision Making with School Choice" March 2005. Download (\$5) from www.nber.org/papers/W11252.]*

RESEARCH F.Y.I.

THE FREE LUNCH LIVES

Ever since the early 1980s, self-proclaimed “supply-siders” have argued that tax cuts pay for themselves by stimulating investment, innovation and growth. But, like the huge tax cuts of the Reagan administration, the huge tax cuts of the Bush administration have led to substantial increases in federal deficits. And the fact that supply-siders seem to pay too little attention to the structure of tax incentives, and too much to the distribution of the benefits, has led cynics to view the whole idea as a cover for feathering the nests of the wealthy.

In fact, Greg Mankiw (the former Bush economic adviser) and Matthew Weinzierl (Harvard) make a pretty good case that half the initial revenue losses from taxes on capital income are recouped through economic growth and subsequent expansion of the tax base. [*Harvard Institute of Economic Research Discussion Paper 2057, “Dynamic Scoring: A Back of the Envelope Guide,” January 2005. Download free from post.economics.harvard.edu/hier/2005papers/2005list.html.*]

PAY ME NOW, OR ...

The United States is the last major market for pharmaceuticals without price controls, which explains why most drugs cost more in the United States than in other rich countries. Not fair, you say? Maybe not. But the long-term consequences of bringing U.S. prices in line with prices in Europe and Canada by means of regulation would be highly problematic, argue Thomas Abbott (Merck Pharmaceuticals) and John Vernon (University of Connecticut).

They estimate that cutting the prices of

prescription drugs in the United States by an average of 40 to 50 percent would reduce the number of new compounds brought to the first stage of testing for safety and efficiency by 30 to 60 percent. Which makes one wonder why the United States is so reluctant to ask the Europeans to chip in more for R&D. [*NBER Working Paper 11114, “The Cost of U.S. Pharmaceutical Price Reductions,” February 2005. Download (\$5) from www.nber.org/papers/W11114.*]

HE HAD A DREAM

Given the perspective of a half-century, some historians now argue that the impact of the Supreme Court’s landmark *Brown v. Board of Education* ruling was largely symbolic – that under legal pressure, segregated public school districts had already narrowed the quality differences between black and white education. Orley Ashenfelter (Princeton), William Collins (Vanderbilt) and Albert Yoon (Northwestern) confirm that segregated black education was, indeed, getting better before the ruling; their statistical analysis suggests that the wage gap linked to class size and longer school years fell significantly.

But they also found that Southern black males who went to school just after the effective end of segregation had higher incomes as adults than their counterparts who went to school just before desegregation. One interpretation is that the court was right – that separate education was inherently unequal, even if spending was equal. Symbols, it seems, do matter. [*Princeton Industrial Relations Section Working Papers, “Evaluating the Role of Brown v. Board of Education in School Equalization, Desegregation and the Income of African-Americans,” May 2005. Download free from www.irs.princeton.edu/wpframe.html.*]

— Peter Passell