

The Big Job of Raising Little Kids

Inter-American Development Bank
Research Department

Volume 38
September–December 2015

In recent years, advocates of limited government in both the developed and developing worlds have gained significant traction, arguing that large bureaucracies feed inefficiency and corruption, stifle initiative, and interfere with personal privacy. Yet, there is at least one area (likely more), in which that passion for limited government may well be misplaced: the need to guarantee the successful development of children. In Latin America and the Caribbean, oversized governments have often throttled growth and development, but when it comes to raising little children, governments' limited involvement may be just as damaging.

Why should the government be involved in raising children, an area that by definition would seem to be a parental responsibility? To begin with, children have their own legal identities and interests—separate from their parents'—worthy of protection. The United Nations Convention on the Rights of the Child, signed by 194 nations, compels states to guarantee their well-being. They are individuals with legal rights and are equal before any law and policy.

Although most parents have their child's best interest at heart, this is not always the case. Consciously or not, parents don't always make the appropriate sacrifices for

Children are not raised by their parents alone—nor should they be.

their children. Families with limited resources face competing priorities, such as investing in the family business, buying clothes, or sending their child to school or a doctor. Putting a young son or daughter first in that context may involve forfeiting current needs for rewards whose full benefits will be reaped by the child only when he is an adult, whether in professional abilities or health. Unfortunately, some parents are neither patient nor altruistic enough to make those sacrifices.

Sometimes, parents simply lack the information needed to make the right decisions. They may fail to grasp the link between early childhood experiences and positive outcomes later in life. The importance of day care is a classic example. Children from low-income families randomly assigned in the 1970s to high-quality day care in North Carolina were less likely to drop out of high school and more likely to attend a four-year college at 21. But poor parents who aren't aware of day care's vital role may fail to take advantage of the opportunity, even when they have the interests of their child at heart.

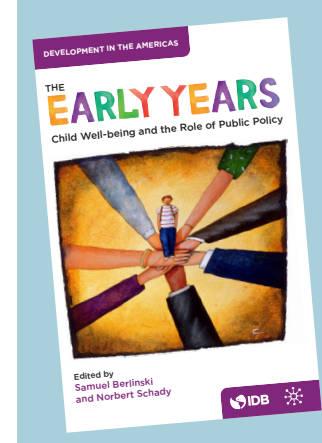
Money also weighs into parents' decisions. Even if they want the best for their children, parents don't always have the resources to invest in them. Consider medical

► [Continued on page 3](#)

IN THIS ISSUE

A Report Card on Early Childhood Development	2
Crumbs for Kids	4
Teachers Matter	5
The Beauty of a Bedtime Story	7
New Publications	8

NOW AVAILABLE



Order at Amazon.com

A Report Card on Early Childhood Development

Child well-being is multidimensional, comprising health, nutrition, cognitive, language, socioemotional, and motor development. These measures are important in their own right, and because of their implications for long-term productivity and growth in Latin America and the Caribbean.

How do Latin America and the Caribbean's young children fare? There is at least some cause for celebration. The region's progress in improving child health and nutrition has been nothing short of remarkable. Over the course of the past 50 years, most countries have reduced infant mortality by three-quarters or more. In both 1990 and 2010, roughly 10 million children were born in Latin America and the Caribbean. Of these 10 million children, 428,000 died before their first birthday in 1990, but only 149,000 died in 2010. In addition to these absolute declines, some countries have made dramatic improvements in relative terms as well. Compared to other countries with similar GDP per capita, they have gone from levels of infant mortality well above comparators to

levels significantly below. The rest of the health picture is similarly bright. Children and adults are growing taller and, in most cases, chronic malnutrition is down.

Of course, socioeconomic factors still make a difference. Table 1 summarizes differences in infant mortality for women of “high” education (complete secondary education or more) and “low” education (incomplete elementary education or less) for select Latin American countries with data. It shows that, in the Dominican Republic, children born to low-education mothers are four times as likely to die in their first year as those born to high-education mothers; in Bolivia and Colombia, children of low-education mothers are twice as likely to die in their first year.

Despite these socioeconomic gradients, overall the region's children enjoy relatively good health and nutrition. Unfortunately, the picture is less rosy when it comes to other aspects of child development. Deficits in language and cognition are notable, particularly among the poor, and are

reflected in poor school performance and test scores throughout children's educational careers. In a recent test of math among third graders in 14 countries in Latin America, 75% of children in the Dominican Republic could not solve simple addition or multiplication problems. Although the Dominican Republic ranks at the bottom in this test, even in Chile, the region's highest performer, 10% of children could not solve these problems. Not surprisingly, these dismal results among third graders are repeated among 15-year-olds on the international PISA exams. In turn, test scores are but a precursor of a lifetime of unfulfilled dreams for many of the region's children.

Every child deserves a chance to realize her dreams. Unfortunately, every child does not have that chance. And parents are not the only ones to blame. Governments also have a role to play in assuring that children have the opportunity to reach their potential. Some children are destined to swim upstream their entire lives because of the poor care they receive during their

► [Continued on page 3](#)

TABLE 1: Infant Mortality Rate by Mother's Education

Country	Incomplete primary or less	Completed secondary or more
Bolivia (2004)	50.5	23.5
Colombia (2006)	23.8	12.5
Dominican Republic (2003)	39.9	11.1
El Salvador (2004)	13.0	10.0
Honduras (2008)	16.8	11.2
Peru (2008)	16.8	12.8

Source: Demographic and Health Surveys (DHS), except for El Salvador. Encuesta Nacional de Salud Familiar (FESAL), 2008, for El Salvador.

Note: Restricted to mothers between 25 and 37 years of age at the time of birth; 5-year moving average; averages calculated for cells with at least 100 births.

A Report Card on Early Childhood Development ► from page 2

early years. Improving that level of care is where government can make a difference.

What can governments in Latin America and the Caribbean do to help their children thrive? To begin with, they can spend more on their youngest citizens. Spending on early childhood services and programs makes up less than 6% of total social spending in the region.

More importantly, however, governments must spend better. Building shiny new day care centers will do little to help children if the quality of services provided within them is not improved. Defining quality, however, is the hard part. It's not spanking new buildings, state-of-the-art computers, or high-tech teaching aids. Instead, quality

is as ethereal as a child's very dreams and aspirations. Research shows that at home, in day care centers, and in early schooling, quality is determined by the interactions of children with those who surround them. Neurological studies demonstrate how the connections young children establish with each other and with adults shape their brains in ways that have lifelong implications. When a caregiver is sensitive and responsive to children's wants and needs, they begin to blossom and grow. When a teacher or parent provides early stimulation and focused instruction, children learn.

What does this mean for public policy? It means less investment in infrastructure and more money for training, supervision, mentoring, and incentives for caregivers in the

gamut of childcare interventions—from parenting programs to day care facilities, to kindergarten classrooms. It demands a long-term vision and commitment that transcends political cycles. It requires institutionalizing a system that rewards creativity, innovation, and hard work among educators while weeding out ineffective and counterproductive teachers.

Governments in Latin America and the Caribbean get a passing grade when it comes to some basic indicators of child well-being, but remain well below the curve when it comes to other critical aspects of language and cognitive behavior. The task ahead is daunting, but given the stakes in terms of national growth and development, they cannot afford to fail. ■

The Big Job of Raising Little Kids

► from page 1

procedures. A child with cataracts may need an operation for his eyesight to develop normally. The operation could save the child from serious eyesight problems that would affect his well-being and productivity as an adult. To pay for such an operation, however, the child's parents need cash in hand or the ability to borrow it. Capital markets might not provide the parents with money today in exchange for some of the future returns from investing in the child.

From a governmental standpoint, the well-being of children affects not only them and their families but society as a whole. Children who flourish in the early years are more likely to become productive citizens

and contribute to a prosperous economy and participatory democracy. An investment in a child's well-being generates returns over the long term and affects the prosperity and viability of society well into the future.

Children are not raised by their parents alone—nor should they be. It is a far too important and difficult task to be placed solely on the shoulders of a mother and/or father. Relatives, other caregivers, teachers, and government also have a hand in molding the experiences children accumulate at home, in day care centers, at school, and in society at large. Improving those experiences will shape children's lives and the face of the societies they live in for years to come.

This issue of *IDEA* examines some of the issues surrounding early childhood development in Latin America and the Caribbean and the role of public policy in this important endeavor. It draws on the 2015 edition of the IDB's flagship series, *Development in the Americas*, entitled *The Early Years: Child Well-Being and the Role of Public Policy*. Edited by Samuel Berlinski and Norbert Schady, *The Early Years* makes a strong case for government intervention in what is instinctively a family affair. Child well-being matters for both ethical and economic reasons and public policy has a vital role to play in developing happy, healthy, and well-educated children who grow into socially and economically productive adults. ■

Crumbs for Kids

For every dollar spent on children aged 0 to 5, three dollars are spent on children aged 6 to 12 in Latin America and the Caribbean. Public spending on early childhood is not only low relative to investment in middle childhood, but also with respect to spending on all other age groups. The elderly, in particular, receive pensions and other transfers to help them confront the risks linked to old age. This is true even in countries with very different population profiles. For instance, Chile, Guatemala, and Peru all spend between seven and nine times as much on the elderly as on children aged 0 to 5, measured on a per capita basis. When it comes to dishing out the budgetary pie, young children receive little more than crumbs.

How does Latin America and the Caribbean compare to other regions when it comes to spending on early childhood? Not well. Countries in the region spend on average only

0.4% of GDP on their youngest children, about half the OECD average (see Figure 2). Some high-performing countries spend close to four times as much.

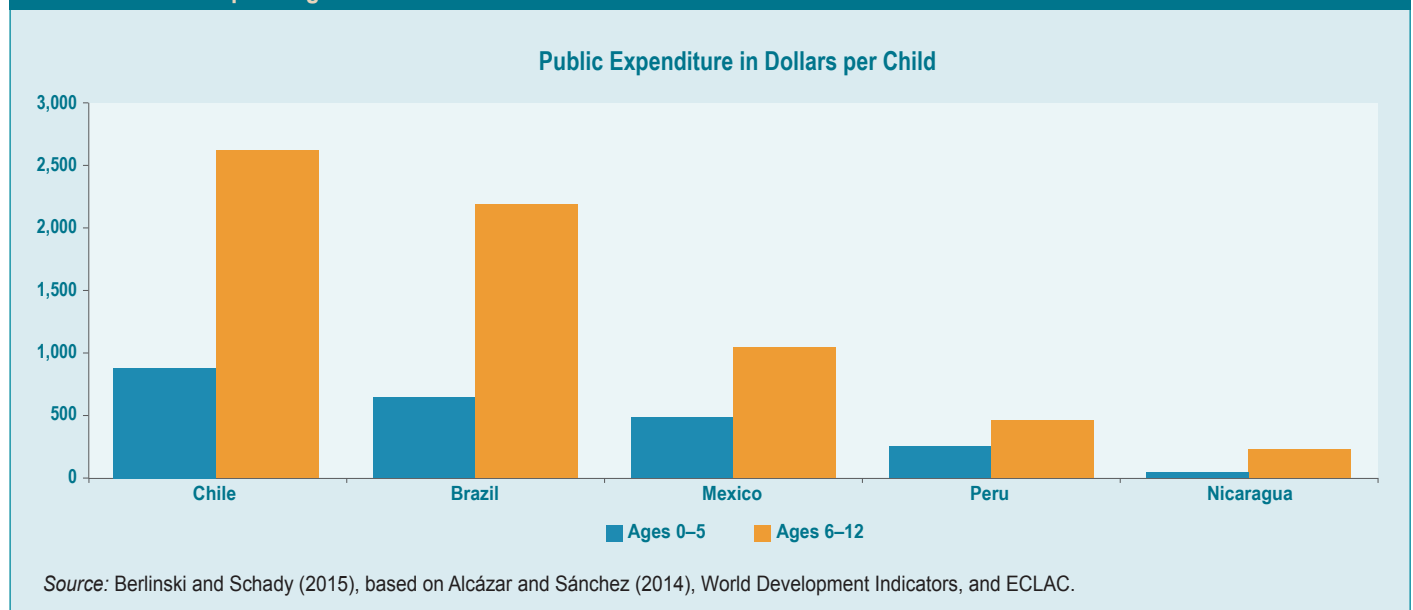
The good news is that, although government spending on early childhood is low in relative terms, it has been on the upswing over the past decade. For example, Chile, the Dominican Republic, and Guatemala have boosted spending between two and four times since 2000. Most countries have pumped more money into preschools and conditional cash transfer programs while day care and parenting programs have enjoyed more modest investment increases. This allocation is unfortunate as parenting programs, which receive the smallest allocation of overall budgets, have been shown to generate the greatest bang for the buck.

The region's generally tight-fisted handling of little children reflects

a poor investment decision. Spending on early childhood could be one of the best investments a government can make. To begin with, the earlier the government invests in a child, the longer the country has to reap the benefits. Moreover, the investments made on young children magnify the returns to investments made later in an individual's life. For instance, spending on university education or training for someone who benefited from investment in her early years will likely have a greater payoff than money spent on an individual who did not enjoy quality care early on. Finally, the benefits of early investments show up well into adulthood. A study from Jamaica revealed that children who benefited from a parenting intervention in the first two years of their lives and were followed twenty years later had higher IQs, earned 25% more, were less depressed, and were less likely to be

► *Continued on page 5*

FIGURE 1. Public Spending Is Skewed towards Older Children



Teachers Matter

School access is no longer a major challenge in most countries in Latin America and the Caribbean. What is a challenge is quality. The quality of education many children receive is poor, and does not prepare them well for schooling in later grades or for life generally. New schools, textbooks, and technology are not the answer. When it comes to school quality, teachers make the difference.

Numerous studies show that early education is part of a cumulative process that propels the development of cognitive and other abilities needed in later years. Argentina implemented a large expansion of preprimary education between 1993 and 1999.

It discovered that, as a result, beneficiaries performed significantly better on tests of mathematics and Spanish by the third grade. In Uruguay, children who had attended a preprimary institution were 27% more likely to be in school than their peers at age 15. Early education, it appears, is not only valuable in and of itself; it is the basis for later success.

Unfortunately, early education in Latin American and Caribbean nations is falling short. Moreover, the effects are long-lasting. They can be seen both in the floundering performances of secondary school students and in the often deficient cognitive skills of Latin American and Caribbean workers.

They contribute to the region's low economic growth rates.

Education coverage has improved dramatically. School attendance is nearly universal in the region for children between 6 and 9 years of age. Many countries have made a vigorous push to expand coverage at the preprimary level. And wealth is increasingly falling away as an obstacle. In the Dominican Republic, for example, the difference in the proportion of 5-year-olds attending school between the first and fifth wealth quintiles fell from 33 to 7 percentage points between 2000 and 2013. Chile and Panama also have reduced the wealth gap.

► *Continued on page 6*

Crumbs for Kids

► *from page 4*

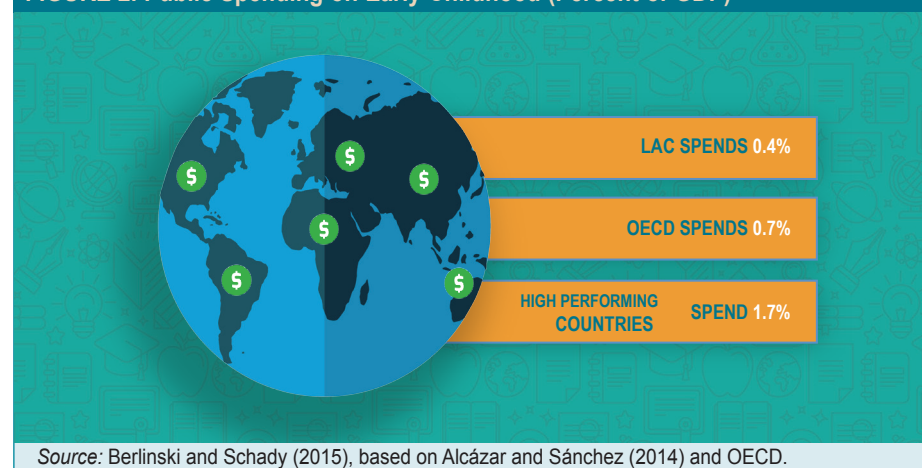
involved in criminal activities than children who did not benefit from the intervention.

Of course, more money is not the whole answer. Another major message of the book is that quantity cannot

substitute for quality when it comes to early childhood care. And quality is measured less in terms of bricks and mortar, and more in terms of the intangible benefits of the interactions between caregivers and children.

By shortchanging their youngest citizens, governments are missing an opportunity to impact not only the lives of their children but the well-being of their societies for decades to come. Happy, healthy, stimulated children grow up to be productive, participatory adults. And by targeting lower-income children, early childhood spending can be an effective redistributive tool that can reduce the intergenerational transmission of poverty and inequality. A nation's future is in the hands of its children. They need and deserve more than pennies to take on the task. ■

FIGURE 2. Public Spending on Early Childhood (Percent of GDP)



Teachers Matter

► from page 5

But if access to early education is on the upswing, its quality is not. A series of recent studies from around the region shows that young people in the classroom spend much of their time eating and in recess; that instruction is often dedicated to rote learning, and that students are rarely encouraged to develop creative or critical thinking through collaborative work in small groups.

Some education experts recommend structural changes. They talk of reducing class size, improving student-teacher ratios, and using better classroom materials and technology. Yet a large-scale review of educational interventions in more than 30 lower- and middle-income countries found that such innovations have little impact without a similar rise in the quality of teacher-student interactions.

What does that involve in practice? Effective teaching seems to occur

when teachers provide emotional support to their students, encouraging their interests and points of view. It happens when teachers maximize meaningful activities, rather than reacting to behavioral problems or letting students wander, and when they offer high levels of instructional support. That doesn't mean rote learning. It means stimulating critical thought and problem solving mixed with feedback that is deft and sharp.

A teacher's ability to interact with her students in those ways makes all the difference. A recent study of more than 200 schools in coastal Ecuador found that a child randomly assigned to a teacher at the 95th percentile in terms of possessing those qualities was at a considerable advantage. The child learned on average 0.18 standard deviations more than a child assigned to an average teacher. His abilities improved in a wide variety

of areas, including language, math, and executive function. And the improvements were generalized, with all children progressing by roughly the same amount, regardless of their baseline skills, their parents' level of education, or their family income. In fact, teachers can help eliminate the gap between children of mothers with widely varying educational levels. The children whose mothers were elementary school dropouts and were assigned to the "exceptional" teachers in the Ecuador study, rather than an average one, made up one-quarter of the gap relative to children whose mothers graduated from high school—in just one year!

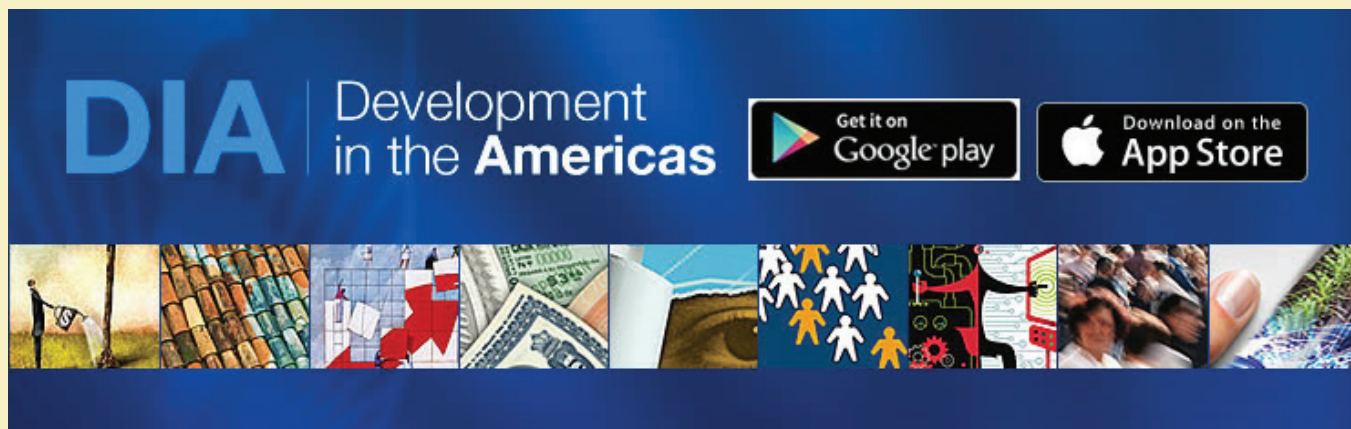
Studies in the United States have found similar results. In an op-ed in the *New York Times*, David Kirp notes that the difference between child outcomes from Pre-K education in

► Continued on page 7

Check out our new App!

Now available for **iPhone** and **Android**.

Presenting updated data and the main messages of every edition of the IDB's flagship series, Development in the Americas (DIA)



The Beauty of a Bedtime Story

Being able to read and write can impact people's lives on many levels. It can enable a person to read a sign on the street, enjoy reading a book, complete an education, land a job, earn an income to provide for his or her family, and contribute to society and a country's economic growth. And to think that it can all start with just a bedtime story, as opening a storybook can open up a whole world of possibilities for children, and have a huge impact on their development.

Reading a bedtime story can be one of the most rewarding experiences for parents, a time when they establish a deep connection with their children. During that very intimate moment, the child's whole world revolves around knowing what will happen next and the parent enjoys his or her undivided attention. As children quickly grow up to become teenagers, parents will cherish those memories for years to come.

For the child, this will mean much more than a childhood memory. By talking to children, playing with them,

reading or telling them stories—or not—parents and other family members determine how much stimulation young children receive. After all, the family is the single most important determinant of the well-being of children, and these choices have profound and long-lasting effects on their development.

Young children need a home environment that stimulates the development of language and cognition, in addition to having warm, nurturing, and stable interactions with their families. How can parents foster this development at home in the preschool years? Shared reading is a good example: parents and children share an age-appropriate book with parents promoting an active role of children in book-reading by asking them questions and providing feedback. There is encouraging evidence in the United States of the effect of this approach on the development of vocabulary of preschool and kindergarten children.

Young children need a home environment that stimulates the development of language and cognition.

In the developing world, however, the fact that many parents of poor children have limited skills (for example, those that are illiterate or have very little schooling) may present an important constraint. Indeed, in Latin America parents' literacy is an area in which the home environment can keep many children from reaching their full potential. Children of mothers with less education are much less likely to be read to than children of mothers with more education in all of the region's countries except Guyana, where very few children are read to, regardless of their mothers' education.

For children of school age, a number of programs have focused on increasing reading and literacy during summer holidays when children from low socioeconomic backgrounds tend to lose ground on literacy achievement, compared to their more affluent peers—a phenomenon that has been described as "Summer Loss." Researchers speculate that this setback is partly explained by lack of voluntary reading over the summer. There is encouraging evidence from U.S. studies that suggests that distributing books to children over the summer

► *Continued on page 12*

Teachers Matter

► *from page 6*

Boston and Tennessee is teacher quality. The lack of results in Tennessee can be traced to teachers who are essentially "left to their own devices" while Boston Pre-K teachers undergo extensive coaching and follow a creative, challenging curriculum.

The challenge is getting teachers up to speed. Personalized coaching for teachers is one option, especially if the training is hands-on, rather than theoretical. Monetary rewards for excellent

performance is another, while dismissal or early retirement of teachers that consistently underperform may be a necessity in many instances. There is no one-size-fits-all policy; nothing that works equally in all places. But given the benefits for children, for the adolescents and adults they will become, and for the countries they live in—desperately in need of critical, creative thinkers and problem solvers—the stakes could not be higher. ■

New Publications

Available in English only unless otherwise stated

WORKING PAPERS

Becerra, Óscar, Eduardo Cavallo, and Ilan Noy

The Mystery of Saving in Latin America (IDB-WP-615)

Using reduced-form regression models, this paper shows that average, predicted private-saving rates in Latin America and the Caribbean are significantly lower than in other regions, particularly Emerging Asia (about 4 percentage points of GDP on average). Predicted public-saving rates in Latin America and the Caribbean are also lower than in Emerging Asia, albeit by a smaller margin (1 percentage point of GDP on average). It is further shown that private-saving rates in Latin America and the Caribbean are below the region-specific prediction by approximately 1.5 percentage points of GDP, on average. Finally, we found that greater reliance on external savings does not fully close the negative estimated private-saving gap; it reduces the gap by less than 1 percentage point. We found no gap in public-saving rates, suggesting that the lower, predicted public-saving rate in Latin America and the Caribbean is accounted for by the known determinants of fiscal policy.

Cavallo, Eduardo, and Mathieu Pedemonte

What Is the Relationship between National Saving and Investment in Latin America and the Caribbean? (IDB-WP-617)

Using panel co-integration techniques and a comprehensive dataset from 1980 to 2013, this paper finds a positive, significant correlation between national saving and domestic investment rates in Latin America and the Caribbean. The estimated corre-

lation is approximately 0.39; in other words, for every percentage point of GDP increase in national saving, domestic investment increases by 0.39 percentage points on average. This result, however, is tempered by three nuances: i) the estimated correlation has been declining over time; ii) the regional average conceals intra-regional heterogeneity to a large degree; and iii) the estimated coefficient is greatest amongst the largest economies in the region. We conclude that low national saving rates remain a major constraint for capital accumulation in Latin America and the Caribbean.

Cerda, Rodrigo, Rodrigo Fuentes, Gonzalo García, and José Ignacio Llodrá

Understanding Domestic Savings in Chile (IDB-WP-626)

In this paper, we construct time-series data on savings by type of agent in Chile between 1960 and 2012. We find that the Chilean economy's average savings rate was 11 percentage points higher during the 1985–2012 period than during the 1960–84 period; growth in corporate savings was particularly pronounced. The evidence suggests that this increase was driven largely by the following measures: i) pension reform, which introduced mandatory savings and private sector management; ii) banking reform; iii) tax reform; iv) capital market reform; and v) privatizations.

Hallerberg, Mark, and Carlos Scartascini

Explaining Changes in Tax Burdens in Latin America: Does Politics Trump Economics? (IDB-WP-613)

This paper examines whether elections—which are generally held at

regular intervals—and banking crises explain the timing of tax reforms, and allocation of the additional tax burden. An original, fine-grained dataset of tax reforms facilitated our task of explaining the role of these two sources of variation. In particular, that the likelihood of reform is greater during banking crises. During election periods, raising taxes becomes highly unlikely, even if the government is facing financial problems. Interestingly, politics seems to trump economics: banking crises do not increase the chances of reforms being made during election periods. Moreover, the existence of an IMF program affects what tax instruments are chosen: countries subject to an IMF program increase value-added taxes, while countries not subject to an IMF program raise personal income taxes. Finally, the president's ideology does not explain who bears the additional tax burden.

Machado, Fabiana V.P., and Giselle Vesga

The Political Economy of Pension Reform: Public Opinion in Latin America and the Caribbean (IDB-WP-611)

Countries around the world are facing significant challenges to the sustainability of their pension systems. Changing existing policies, especially those of broad scope and financial magnitude, is a political challenge. It takes a combination of willingness, capacity, and sufficient political support to change the status quo and avoid costly reversals going forward. Using several waves of public opinion data in Latin America and the Caribbean, this paper endeavors to identify and analyze individual-level factors that are relevant to gauging political support for pension reform.

► *Continued on page 9*



New Publications

▶ from page 8

*Miller, Sebastián, and
Riley Wilson*

Parking Taxes as a Second Best Congestion Pricing Mechanism (IDB-WP-614)

Growing vehicle use and congestion externalities have led many to consider alternative congestion-pricing mechanisms, since road pricing often carries high infrastructure costs and faces public opposition. In this paper, we explore the role of parking taxes in reducing congestion by using as an example the progressive parking tax increase enacted in Chicago in January 2012. Using differences in vehicle use across income groups, we estimated that the parking tax increase of approximately \$2 a day led to a 4–6 percent reduction in total vehicle trips in high-income areas; we noticed the greatest impact on roads most heavily used by commuters. We also found corresponding increases in public transit use and a 3.1 percent aggregate reduction in vehicle trips. We concluded that, although parking taxes can help mitigate congestion externalities, they are only about half as effective as more efficient congestion tolls.

*Ortega, Daniel, and
Carlos Scartascini*

Don't Blame the Messenger: A Field Experiment on Delivery Methods for Increasing Tax Compliance (IDB-WP-627)

There is ample literature on the determinants of tax compliance. Several field experiments have evaluated the effect and comparative relevance of sending moral suasion and deterrent messages to delinquent taxpayers. The effect of various delivery mechanisms, however, has so far not been evaluated. In this study, we conducted a field experiment in Colombia that changes how the Na-

tional Tax Agency notifies taxpayers regarding income tax, value-added tax, and wealth taxes owed. More than 20,000 taxpayers were randomly assigned to a control group or to one of three delivery mechanisms (letter, e-mail, and in-person visits by a tax inspector). Results indicate large, highly significant effects, as well as considerable differences across delivery methods. An in-person visit by a tax inspector is more effective than a traditional letter or e-mail, which depend on delivery, although e-mails tend to reach their target more often. Gathering more complete taxpayer contact information can significantly boost collection of unpaid taxes.

Ronconi, Lucas

Enforcement and the Effective Regulation of Labor (IDB-WP-622)

This paper provides new measures of labor law enforcement around the world. The dataset I used shows that countries with more stringent *de jure* regulation tend to enforce less. While countries with civil-law legal systems tend to have more stringent *de jure* labor codes as predicted by legal origin theory, they enforce these codes less, suggesting that, in practice, legal origin theory is more nuanced. The paper further hypothesizes that in territories where Europeans pursued an extractive strategy, they created economies characterized by monopolies and exploitation of workers, which ultimately led to stringent labor laws—in an attempt to buy social peace. Those laws, however, in practice only applied to firms and sectors with high rents and workers capable of mobilizing. Finally, I show that territories with higher European settler mortality presently have more stringent *de jure* labor regulations, fewer labor inspections overall, and

greater gaps in the effective regulation of bigger firms.

*Székely, Miguel, Pamela Mendoza,
and Jonathan Karver*

Understanding Domestic Saving in Latin America and the Caribbean: The Case of Mexico (IDB-WP-606)

This study addresses why Mexico continues to experience below-average economic growth rates, despite having systematically higher domestic savings than other countries in the region. Using the wealth of relevant databases available for the country, we find that a possible explanation is that household savings make up the majority of domestic savings, and that the main instrument used for savings is durable goods; this implies that savings are not directly injected into the financial system to fuel productive investment. A synthetic panel constructed of household survey data reveals that household savings in Mexico show a clear upward trend in age, and have been growing across generations during the past 30 years. It is therefore probable that rates will increase in years to come. However, if those savings continue to elude the financial system, their influence on economic growth may remain limited.

TECHNICAL NOTES

*Bebczuk, Ricardo,
Leonardo Gasparini,
Julián Amendolaggin, and
Noelia Garbero*

Understanding the Determinants of Household Saving: Micro Evidence for Latin America (IDB-TN-843)

Using a broad dataset of official household surveys for 10 Latin Amer-

▶ Continued on page 10

New Publications

▶ from page 9

ican countries and 27 surveys covering selected years between the 1990s and 2010s, this paper investigates the main patterns and drivers of the household saving rate in Latin America. Almost half of all households reveal negative savings, which raises suspicions of income underreporting and/or consumption overreporting. The estimates highlight the overriding, positive role that income plays in shaping saving decisions. Government transfers, remittances, self-employment, capitalized pension systems, access to financial services, living in urban areas, and health and education expenses seem to diminish saving, whereas labor formality and homeownership increase saving. In terms of policy implications, the drivers identified are either beyond the realm of direct government intervention or may be modified only in the long term. Moreover, some of these policies entail significant policy trade-offs, as they may boost saving at the expense of other worthy policy goals.

OUTSIDE PUBLICATIONS

Avellán, Leopoldo, and Guillermo Vuletin. 2015.

Fiscal Procyclicality and Output Forecast Errors. *Journal of International Money and Finance*, Vol. 55. 193–204.

Government spending in the developing world has historically been procyclical. Traditional explanations consider that fiscal procyclicality is the deliberate result of political economy distortions and weak institutions. Two recent explanations have gained increasing support: (i) over-optimism in output forecasts as a cause of procyclicality; and (ii) real-time data, as opposed to ex-post data, as an explanation for policymakers' intended re-

sponses to output fluctuations, which in practice tend to deliver less procyclical intentions than reliance on ex-post data. This study revisits the implications of output forecast errors on fiscal procyclicality. Using output forecasts for 101 countries, the results showed that: (i) over-optimism is neither necessary nor sufficient to explain fiscal procyclicality; and (ii) there is no reason to accept the interpretation that forecast errors have "unfortunate" systematic effects on fiscal procyclicality. Traditional political economy arguments help explain how governments handle unanticipated output fluctuations.

Bassi, Marina, Matías Busso, and Juan Sebastián Muñoz. 2015.
Enrollment, Graduation, and Dropout Rates in Latin America: Is the Glass Half Empty or Half Full? *Economía —Journal of LACEA*, V16, N1.

This paper uses 113 household surveys from 18 Latin American countries to document patterns in secondary school graduation rates over the 1990–2010 period. It finds that enrollment and graduation rates increased dramatically during that period while dropout rates decreased, and provides two types of explanations for these patterns. Countries implemented changes on the supply side to increase access, by increasing the resources allocated to education and designing policies to help students stay in school. At the same time, economic incentives to stay in school changed, since returns to secondary education increased over the 1990s. Despite this progress, graduation rates are still low and remarkable gaps persist in educational outcomes in terms of gender, income quintiles, and regions within countries. In addition, wage returns have recently stagnated and the region shows low

quality of education, casting doubts on whether the positive trend is sustainable in the medium term.

Busso, M., J. Cristiá, and S. Humpage. 2015.
Did You Get Your Shots? Experimental Evidence on the Role of Reminders. *Journal of Health Economics* 44: 226–237.

Many families fail to vaccinate their children despite the supply of these services at no cost. This study tests whether personal reminders can increase demand for vaccination. A field experiment was conducted in rural Guatemala in which timely reminders were provided to families whose children were due for a vaccine. The six-month intervention increased the probability of vaccination completion by 2.2 percentage points among all children in treatment communities. Moreover, for children in treatment communities who were due to receive a vaccine, and whose parents were expected to be reminded about that due date, the probability of vaccination completion increased by 4.6 percentage points. The cost of an additional child with complete vaccination due to the intervention is estimated at about \$7.50.

Du Caju, Philip, Theodora Kosma, Martina Lawless, Julián Messina, and Tairi Rööm. 2015.

Why Firms Avoid Cutting Wages: Survey Evidence from European Firms. *Industrial and Labor Relations Review*, Vol. 68 No. 4: 862–888.

Firms very rarely cut nominal wages, even in the face of considerable negative economic shocks. This paper uses a unique survey of 14 European countries to ask firms directly about the incidence of wage cuts and to assess the relevance of a range of potential reasons for why the firms avoid

▶ Continued on page 11



New Publications

▶ from page 10

cutting wages. They examine how firm characteristics and collective bargaining institutions affect the relevance of each of the common explanations for the infrequency of wage cuts. Concerns about the retention of productive staff and a lowering of morale and effort were reported as key reasons for downward wage rigidity across all countries and firm types. Restrictions created by collective bargaining were found to be an important consideration for firms in Western European (EU-15) countries, but were one of the lowest-ranked obstacles in the new EU member-states in Central and Eastern Europe.

Fernández, Andrés, Alessandro Rebucci, and Martín Uribe. 2015. Are Capital Controls Countercyclical?, Journal of Monetary Economics 76. 1–14.

A growing literature advocates the use of countercyclical capital control policy; that is, the tightening of restrictions on net capital inflows during booms and their relaxation during recessions. This paper examines the behavior of capital controls in 78 countries over the 1995–2011 period. It finds that capital controls are remarkably acyclical. Booms and busts in aggregate activity are associated with virtually no movements in capital controls.

Fernández, Andrés, and César Tamayo. From Institutions to Financial Development and Growth: What Are the Links? Forthcoming in Journal of Economic Surveys. doi: 10.1111/joes.12132

This paper presents an integrated overview of the literature linking institutions, financial development, and economic growth. From the large body of research on institutional development, the paper first selects those contributions that make it pos-

sible to study the role of institutional arrangements in ameliorating/worsening the information frictions and transaction costs of financial markets. It then investigates the theoretical mechanisms by which these frictions affect economic growth and presents the stock of empirical evidence quantifying the impact of institutions on growth through financial development.

Frisancho, Verónica, and Kala Krishna. 2015. Affirmative Action in Higher Education in India: Targeting, Catch up, and Mismatch, Higher Education, 10.1007/s10734-015-9927-1. pp. 1–39.

Using detailed data on the 2008 graduating class from an elite engineering institution in India, we evaluate the impact of affirmative action policies in higher education by focusing on three issues: targeting, catch up, and mismatch. We find that admission preferences effectively target minority students who are poorer than average displaced nonminority students. Moreover, we find that minority students, especially those in more selective majors, fall behind their same-major peers in terms of grades as they progress through college. We also identify evidence in favor of the mismatch hypothesis: Once we control for selection into majors, minority students in more selective majors end up earning less than they would have had they chosen a less selective major.

Nirei, Makoto, Vladyslav Sushko, and Julián Caballero. 2015. Bank Capital Shock Propagation via Syndicated Interconnectedness. Computational Economics. pp. 1–30. DOI: 10.1007/s10614-015-9493-8

Loan syndication increases bank interconnectedness through co-lending relationships. This paper studies the financial stability implications of such dependency on syndicate partners in the presence of shocks to banks' capital. Model simulations show that such shocks can produce rare events in this market when banks have shared loan exposures while also relying on a common risk management tool, such as value-at-risk (VaR). This is because a withdrawal of a bank from a syndicate can cause ripple effects through the market, as the loan arranger scrambles to commit more of its own funds by also pulling back from other syndicates or has to dissolve the syndicate it had arranged. However, simulations also show that the core-periphery structure observed in the empirical network may reduce the probability of such contagion. In addition, simulations with tighter VaR constraints show banks taking on less risk ex-ante.

Riera-Crichton, Daniel, Carlos Végh, and Guillermo Vuletin. 2015. Procyclical and Countercyclical Fiscal Multipliers: Evidence from OECD Countries. Journal of International Money and Finance, Vol. 52. 15–31.

This paper argues that existing estimates of government spending multipliers in expansion and recession may yield biased results by ignoring whether government spending is increasing or decreasing. In OECD countries, the problem originates in the fact that, contrary to one's priors, government spending does not always go up in recessions (i.e., acting countercyclically). In almost as many cases, government spending actually goes down (i.e., acting procyclically). Since the economy does not respond symmetrically to government

▶ Continued on page 12

New Publications

spending increases or decreases, the “true” long-run multiplier for bad times (and government spending going up) turns out to be 2.3 compared to 1.3 if we just distinguish between recession and expansion. In extreme recessions, the long-run multiplier reaches 3.1.

Végh, Carlos, and Guillermo Vuletin. 2015. Unsticking the Flypaper Effect in an Uncertain World. Journal of Public Economics, Vol. 131, 142–155.

This paper provides a novel explanation for the flypaper effect based on insurance arguments. In the model, the flypaper effect arises due to the differential response of precautionary savings to private income or fiscal transfer shocks in an uncertain world with incomplete markets. The model generates two testable implications: (i) the flypaper effect is a decreasing function of the correlation between fiscal transfers and private income; and (ii) this relationship is stronger the higher the volatility of fiscal transfers and/or private income. An empirical analysis of Argentinian provinces for the 1963–2006

period finds strong support for the model’s implications.

Végh, Carlos, and Guillermo Vuletin. 2015. How Is Tax Policy Conducted over the Business Cycle? American Economic Journal: Economic Policy. Vol 7. 327–370.

It is well known that government spending has typically been procyclical in developing economies but acyclical or countercyclical in industrial countries. Little, if any, is known, however, about the cyclical behavior of tax rates (as opposed to tax revenues, which are endogenous to the business cycle and hence cannot shed light on the cyclicity of tax policy). This paper presents a novel dataset on tax rates for 62 countries for the 1960–2013 period that comprises corporate income, personal income, and value-added tax rates. It finds that, by and large, tax policy is acyclical in industrial countries but mostly procyclical in developing countries. Further, tax policy in countries with better institutions and/or more integrated with world capital markets tends to be less procyclical/more countercyclical.

This issue of *IDEA* was prepared by Rita Funaro and is based on the latest edition of the IDB’s flagship publication, Development in the Americas (DIA). This year’s DIA is entitled *The Early Years: Child Well-Being and the Role of Public Policy* and is edited by Samuel Berlinski and Norbert Schady.

José Juan Ruiz

Chief Economist and Manager (RES)

Rita Funaro

Managing Editor (RES)

IDEA (Ideas for Development in the Americas) is an economic and social policy newsletter published three times a year by the Research Department, Inter-American Development Bank. Comments are welcome and should be directed to *IDEA*’s managing editor, Rita Funaro, at ritaf@iadb.org.

To receive the newsletter electronically, please send your e-mail address to: research@iadb.org. Past issues of this newsletter are available on the Internet at: <http://www.iadb.org/idea>.

Copyright © 2015 Inter-American Development Bank. This work is licensed under a Creative Commons IGO 3.0 Attribution-NonCommercial-NoDerivatives (CC-IGO BY-NC-ND 3.0 IGO) license (<http://creativecommons.org/licenses/by-nc-nd/3.0/igo/legalcode>) and may be reproduced with attribution to the IDB and for any non-commercial purpose. No derivative work is allowed.

Any dispute related to the use of the works of the IDB that cannot be settled amicably shall be submitted to arbitration pursuant to the UNCITRAL rules. The use of the IDB’s name for any purpose other than for attribution, and the use of the IDB’s logo shall be subject to a separate written license agreement between the IDB and the user, and is not authorized as part of this CC-IGO license.

Note that the link provided above includes additional terms and conditions of the license.

The opinions expressed in this publication are those of the authors and do not necessarily reflect the views of the Inter-American Development Bank, its Board of Directors, or the countries they represent.



The Beauty of a Bedtime Story

► from page 7

and engaging parents and teachers in the process can produce gains in literacy.

Books are not the only way of affecting the interaction between caregivers and children. In fact, parenting programs designed to stimulate child cognition have been piloted in the

region with promising results. The biggest promise, but also the biggest uncertainty, surrounds programs that directly seek to improve parenting practices. Changing behaviors is hard. Changing behaviors about something as intimate and personal as child rearing is even harder. ■