*the old low price.* This indeed disappoints those who made their plans in error but it has not frustrated any present possibilities for mutually profitably exchange. Catallactic efficiency may well bring disappointment to those who have made entrepreneurial errors; but it never, insofar as it promotes entrepreneurial discovery, discoordinates (in the important sense here described).

The adjective "catallactic" is used by Cordato to remind us of Hayek's important distinction between "catallaxy" and "economy." By focussing on the coordination involved in catallactically efficient market processes, we can add emphasis to the goal of effectuating all opportunities for mutually gainful *exchange.* Emphasizing this goal will on the one hand draw attention to the genuine power and clarity of Cordato's catallactic efficiency criterion; on the other hand, such emphasis will discourage misinterpretation of the criterion as implying more than it can possibly deliver. This can only enhance the worth of Cordato's valuable contribution to Austrian economics.

Israel M. Kirzner
New York University

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## Combating Poverty: Innovative Social Reforms in Chile during the 1980s

Tarsicio Castaneda
San Francisco: ICS Press, 1992, 259 pp.

This book summarizes and analyzes the remarkable reforms of social welfare programs that occurred in Chile during the 1980s. The reforms covered are in the areas of education, health and nutrition, housing, social security, and interrelations between the central and local governments. While there is a considerable emphasis on reforms related to poverty alleviation, two of the areas—social security and intergovernmental relations—have rather little direct relevance to poverty. The social security reform gave some emphasis to the alleviation of poverty, but the social security system is primarily a middle-class issue or perquisite.

The author states (p. 13) that the social reforms were based on five common principles:

> First, the government should target subsidies to the poorest segment of the population rather than attempt to meet the basic needs of the entire population. . . . Second, social services should be

> provided by municipalities and the private sector, which are closer to the beneficiaries than is the central government. Third, financing for social services should be based on services provided rather than on historically based budget allocations. Fourth, subsidies should be given directly to beneficiaries rather than to providers. . . . Fifth, the public sector should undertake only those activities that are socially profitable and that no private-sector party is willing to provide.

These are principles or guidelines that can be recommended to any government that sincerely wishes to combat poverty or increase the effectiveness of governmental expenditures.

It is not possible in a review to summarize all the reforms and their effects. I shall instead try to discuss the nature of the education reforms, to present some information on the changes in health and nutrition, and, finally, to note the efficiency and distribution effects of the social security reforms.

The major components of the education reforms consisted of decentralizing the provision of public education to the municipalities, providing federal money to both municipal and private schools on the basis of the number of students rather than the historical allocation, and raising tuition at the university level while introducing loans for needy students. An important effect of these reforms was to increase the percentage of public funds spent on preschool and primary education from 38.6 percent of the total in 1974 to 57.4 percent in 1986 and to reduce the allocation to universities from 47.4 percent to 23.8 percent. The percent spent on secondary schools increased from 14.0 to 18.8 percent.

The overall effect of these changes on the distribution of education spending by income group was to increase the percentage spent for the benefit of the poorest 30 percent of the population from 28.6 percent in 1974 to 37.5 percent in 1986. The share going to the richest 40 percent declined from 47.3 percent in 1974 to 34.5 percent in 1986. The quality of primary education improved in terms of reduction of dropout rates and increase in promotion rates.

The reforms did not always work out as expected, however. A brief note on two glitches in university-financing reform may be of interest. The reform provided for per-student payments to be made for both public and private universities. One part of the formula was that payments were to be made for the 20,000 (out of 30,000) students who had the highest scores on the college entrance examination, while the other part was that the payment was differentiated by the field of study according to estimated costs of instruction—payments varied by a factor as much as 2.5 to 1.

The universities responded to these incentives. The older and more prestigious universities attracted the majority of the students with the highest scores and probably competed vigorously for them; consequently, a large share of this transfer went to the established institutions.

The differentiation of payment by field of study resulted in universities expanding enrollments in the fields that brought in the most money; some universities apparently opened up new fields of study or, perhaps, renamed some old ones. These two aspects of the reforms had to be dropped. The universities were paid for all students and the payment was the same for each field. You just cannot trust university administrators, or any other welfare recipient, not to take advantage of incentives that are offered.

In the health area, primarily through targeting expenditures and services, remarkable reductions in infant mortality were achieved between 1974 and 1986. Real expenditures for health care increased by about 50 percent between 1974 and 1982, but because of the budget difficulties in 1982, expenditures declined significantly. By 1986, real expenditures were only 20 percent above those of 1974. In 1975 the poorest rural region had an infant mortality rate of 93 per 1,000 births, nearly three times the rate of 34 for Santiago. By 1986 the infant mortality rate in the poor rural area was 25 while the rate in Santiago was 15. The infant-mortality rate for all of Latin America was 48 in 1986. There was evidence of a significant decline in child malnutrition. It is relevant to note that substantial improvements occurred in health and nutrition after 1982 even though it was not until 1988 that GNP per capita had returned to the 1981 level and that the real costs of medical services were contained.

The reform of social security accomplished several objectives. It permitted individuals to opt out of the public system and purchase annuity contracts with private funds. Participation is compulsory, with the individual required to contribute 10 percent of salary for retirement and 3.4 percent for disability and survivor's pension. In 1980 the payment by both employees and employers ranged from 32.5 to 41 percent of payroll. Clearly the new private system cost much less than the one it replaced. It is projected that the retirement system will provide a retirement income approximately equal to final pay before retirement.

The reforms had three other major effects. First, decisions on pension levels was taken out of the wage-negotiating process; it was easy to make large promises about pensions that would not be paid for some years. Second, the creation of private financial agencies helped to create a fluid capital market. Third, the rate of return on the pension funds has been far higher than the 2 percent the old system returned. A minimum pension at 85 percent of the minimum wage is guaranteed for those who have participated in the old and new systems for 20 years. That is about 40 percent of the average wage.

The municipal reform was an effort to move the decisions concerning many public services to the governmental unit closest to the people who use the services. In Chile, as in most other Latin American countries, there was heavy control over local services from the capital city.

I cannot say that I read every word in the book, but I read most of them and enjoyed doing so. I did not find General Pinochet's name anywhere. There is an occasional reference to the military government but this is as close an identification of the governmental authority as one gets. General Pinochet was responsible for many very bad things; it seems to me appropriate that he be recognized for the good things that would not have happened except for him.

D. Gale Johnson
University of Chicago

## The Economics of Prohibition

Mark Thornton
Salt Lake City: University of Utah Press, 1991, 153 pp.

Some of the strongest arguments against making drugs illegal come from economics. In arguing for legalizing drugs, I have often referred people to my article "A Humane Economist's Case for Drug Legalization" (Henderson 1991). But what has been needed is a *book* that pulls all these arguments together. The ideal book would, in a clear and compelling way, explain the economic effects of prohibition. (I use "prohibition" to refer to making any good illegal and "Prohibition" to refer to the Prohibition era early in this century.) Such a book would draw not just on recent evidence about illegal drugs, but also on the U.S. experience with Prohibition. The ideal book might also discuss the main economic literature on prohibition. *Undoing Drugs* by Daniel Benjamin and Roger Leroy Miller (1991) does some of this but not all; nor does it argue for legalization.

I had hoped that *The Economics of Prohibition*, by economist Mark Thornton, would be that ideal book. Almost all the elements are there: the economic analysis, the evidence from the Prohibition era, the discussion of the economics literature, and the case for making drugs legal. Unfortunately, one important element is missing. The book is badly written. The style is slow and boring; the reader often has trouble knowing where the author is going or even why some point is relevant; arguments and facts are presented incompletely.

Thornton shows how making a good illegal reduces the supply and therefore raises the price. One result, which is intended by prohibitionists, is that users of the good demand less of it. But Thornton, drawing on terminology from Austrian economist Israel Kirzner, points to four categories of unintended consequences of prohibition, all of which stem from interference with the free market's discovery process. Unfortunately, having laid out the four categories, Thornton does not do much with them.

On one unintended consequence of prohibition—drug potency—Thornton has a nice discussion. He shows, using standard economic analysis, that making drugs illegal causes the mix of drugs sold to be more potent. The idea, drawn from work by Armen Alchian and William Allen, and by Yoram Barzel, is that prohibition acts like a tax. If the