

strong link between the two. Hence, he concludes that the reason for the weakness of the statistical link is not the unimportance of institutional factors but the difficulty of quantifying them.

Freytag's emphasis on the importance of the institutional milieu as a determinant of the success of monetary reform is intuitively appealing. For example, if the public is not willing to accept the short-term costs of disinflation or the government violates the Tinbergen Rule by trying to use monetary policy to achieve more than one goal, the most well-intended reform is likely to fail. In addition, the author's case studies, covering the experiences of Germany (1923–1924 and 1948), Argentina (1985 and 1991), Estonia (1992), Hungary (1924), Israel (1985), Lithuania (1984), Poland (1995), Paraguay (1943–1944), Greece (1944), and Brazil (1986), demonstrate the relationship between the extent to which the countries' institutions were conducive to reform and the degree of success of the reforms these countries undertook. The failure of many stabilization programs prescribed by the International Monetary Fund because governments were unwilling or institutionally unable to implement the programs or populations were not prepared to accept the economic sacrifices the Fund programs entailed, further buttresses Freytag's point. Absent an appropriate institutional framework, monetary reforms are unlikely to succeed. While the author confines his analysis to the relationship between the institutional framework of an economy and the chances of successful monetary reform, the experience of the Eastern European countries and the Former Soviet Union since 1990 shows that the principle Freytag enunciates applies more-broadly. The economies that have performed most successfully in the wake of the discrediting of central planning are those that put in place economic, social, legal, and political institutions that respected and enforced "rules of the game" that preclude gangster capitalism and the attaining of monopoly power by powerful politicians or their cronies. The institutional framework in which an economy functions matters. *Success and Failure in Monetary Reform* is a volume that should be read by policy analysts and policymakers who are considering reforms in any segment of a country's economy.

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de Matos, J. A.: *Theoretical Foundations of Corporate Finance*. XVII, 302 pp.  
Princeton University Press, Princeton, New Jersey. 2001. Hardcover \$ 39.95.

Although there is a plethora of books on corporate finance at the undergraduate and MBA levels there are very few at a higher level. This book is a

welcome addition. It provides an account at a fairly advanced level of theories that were mostly developed in the 1980's and 1990's. There are also short passages on empirical contributions where relevant. It is intended for Ph. D. or advanced undergraduate students interested in understanding the models that underlie this subject.

The book is divided into four parts. The first considers the foundations of finance. It covers valuation under certainty and uncertainty in single and multiperiod economies. The Modigliani and Miller propositions and the role of personal and corporate taxes are also laid out here. As is well known, this framework does not provide a very convincing account of what is observed in practice. This sets the stage for more modern approaches based on agency theory and asymmetric information that are considered in the second part. The initial focus is on the implications of such imperfections for the choice between debt, equity and other types of security and for payout policy. The role of financial contracting in determining the allocation of control and the design of securities is another focus. The third part of the book is concerned with capital restructuring. This involves the initial decision to go public, the decision to return to being private and mergers and acquisitions. The final part consists of appendices that provide a brief introduction to the optimization principles and game theory that are used to develop the theories in the book.

The pedagogical approach taken is to choose a number of key papers for each topic and outline the basic models in these. There is some attempt to provide a common framework. This is more successful in some places than in others. For example, the first two chapters that develop foundations do a good job of this. Some of the later ones are a sequence of fairly unrelated models. The accounts of the empirical literatures are brief but useful.

Writing a book such as this is a long, drawn out task. An interesting comparison is how a book such as this would look if somebody was to start writing it today. Law and finance would probably play an important part (e.g., La Porta et al., 1998; Rajan and Zingales, 2003; Stulz and Williamson, 2002). Recent developments in corporate governance (e.g., Allen and Gale, 2000; Vives, 2000), might also be significant. Although there is a long history of behavioral corporate finance dating back at least to Shefrin and Statman (1984), this field is currently in the process of rapid expansion (e.g., Gervais and O'Dean, 2001; Malmendier and Tate, 2001). It would merit serious attention.

The other striking aspect of the book is the stark difference between it and standard undergraduate and MBA corporate finance books such as Brealey and Myers (2002), and Ross, Westerfield and Jaffe (1999). There is no emphasis at all here on so many things that are crucial for practical corporate finance, such as the basic elements of capital budgeting like forecasting cash

flows and deriving discount rates. This is not meant as a criticism of the book, it is simply a reflection of the field. However, it does point to the importance of returning to basics in corporate finance research.

Overall the book is a very useful addition to the literature. The exercises that are given throughout are a crucial learning tool. The fact that comprehensive solutions are provided will be welcome news to professors and students alike. The book will be seen on the shelves of serious scholars in corporate finance.

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