

REVIEWS

The Economic Consequences of Rolling Back the Welfare State. By ATKINSON (A. B.). (Cambridge, Mass. and London: MIT Press, 1999. Pp. xii+216. £15.50 hardback. ISBN 0 262 01171 9.)

This book, originally given as the Munich lectures, dissects the argument that welfare state spending is unsustainably high. The intention is ‘to make readers think again about issues they may regard as settled, rather than to give definitive answers’ (page xi). The book is much more than a new edition of Atkinson’s 1987 *Handbook of Public Economics* survey: it is rich in theory and includes a significant, and greatly welcome, political economy dimension. The major focus is income transfers, primarily unemployment compensation and aspects of pension finance.

Chapter 1 is largely taken up with a critique of the way many economists approach the welfare state: a tendency to look at its costs without considering its benefits; a concentration on poverty relief, ignoring other major purposes; a tendency to ignore institutional structure; and a simplistic approach to political economy. These themes recur throughout the book.

Chapter 2 considers the relationship between welfare state spending and economic performance. Its main message is that the relationship is not automatically one way, and hence that there is not *necessarily* a trade-off: ‘the existence of a social safety net may encourage the risk-taking necessary to engage in the inventive activity that leads to new ideas and new techniques of production’ (page 31).

Chapter 3 discusses unemployment in the context of an equilibrium model of the labour market. This approach, however, ignores important institutional detail. Chapter 4 rectifies this omission, and goes on to discuss the effects of unemployment benefit in a segmented labour market. The conclusion, depending on institutional features and the nature of segmentation, is that less generous benefits may increase or decrease employment. Again, the relationship is not necessarily one way.

Chapter 5 considers the political economy of social security, discussing reasons why people might support the welfare state and also, and importantly, the dynamics of that support.

Chapter 6 discusses the impact of pensions on output growth in terms of simple growth theory, a key feature of which is the assumption that savings automatically translate into productive investment. Chapter 7 draws on models of corporate behaviour to relax this assumption, and finds that a move from pay-as-you-go finance to funding may not increase growth rates. ‘If increased ownership of shares by private pension funds leads to increased monitoring,

and the interests of private pension funds are more in maximising share values than in long-term growth, then the switch from state to private pensins may *lower* the growth rate' (page 182, emphasis added).

One of the book's great strengths is its theoretical anchor, drawing on consumer theory, the theory of the firm, growth theory, and recent developments in macroeconomics. The analysis of pensions includes a marriage of endogenous growth theory with the theory of the growth of the firm. The book provides insights into big issues and, as one would expect from an Atkinson volume, provides compendious coverage of the relevant literature.

At risk of oversimplifying the author's wide-ranging analysis, Atkinson points us to four central conclusions. First, richer theory leads to a more complex range of outcomes than the simple unsustainability/roll back argument suggests. Second, benefits matter as well as costs.

'The emphasis by economists on the negative economic effects of the welfare state can be attributed to the theoretical framework adopted . . . , which remains rooted in a model of perfectly competitive and perfectly clearing markets. [*This*] *theoretical framework incorporates none of the contingencies for which the welfare state exists . . .* The whole purpose of welfare state provision is missing from the theoretical model' (page 8, emphasis added).

Third, institutions – including country differences – matter. Another great strength of Atkinson's analysis is that it not only avoids one-size-fits all prescriptions but explains why this is a fruitless – and potentially harmful – approach. Fourth, politics matters. Alongside other aspects of political support for the welfare state, Atkinson brings out the role of economists.

'The dynamics of the welfare state may have been fundamentally changed by the alarms raised about the feasibility of its continuance. Calls by economists for rolling back the welfare state are themselves part of the political process; we have not just endogenous politicians but also endogenous economists, whose behavior has to be explained' (page 187).

During my time at the World Bank I saw the influence which – for good or ill – economists can have. To argue that we are simply technicians offering dispassionate advice to politicians, and that it is politicians, not technical advisers, who are responsible for policy decisions is naive and potentially cowardly. It is perhaps no accident that the preceding quote is the book's closing passage.

This is a marvellous book – theoretically sophisticated but readable, rigorous but accessible to readers with a limited technical background, fair-minded but never sitting on the fence. A must for anyone with even a peripheral interest in the welfare state.

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Generational Accounting around the World. Edited by AUERBACH (ALAN J.), KOTLIKOFF (LAURENCE J.) and LEIBFRITZ (WILLI). (Chicago and London: University of Chicago Press, 1999. Pp. x+534. £57.50 hardback, US \$72.00 hardback. ISBN 0 226 03213 2.)

As suggested by the title, this book is about generational accounts in numerous countries across five continents. Generational accounting imputes expected lifetime net tax burdens for each generation. Generational accounting is certainly not new to this book, but it is a relatively recent idea. Auerbach et al. (1991) and Kotlikoff (1992) first calculated expected lifetime fiscal burdens across generations, although the idea of intergenerational fiscal imbalance has been around for much longer. In fact, Kotlikoff and various co-authors have been harping on intergenerational fiscal imbalance and the inadequacy of traditional deficit accounting in various mediums at least since Kotlikoff (1984). But when there is something as important as the fiscal difficulties looming in the coming decades, a little harping is very good thing. The authors do not overstate the case when they contend that '[t]he tremendous size of this fiscal liability, its dire implications for our children, and its independence from the traditional deficit is leading economists, government officials, and the press to search for a meaningful measure of our fiscal future' (page 2), which, of course, is what generational accounting is all about.

This book is a natural and useful extension of the earlier work on generational accounting. It compiles comparable generational accounts for seventeen countries (Argentina, Australia, Belgium, Brazil, Canada, Denmark, France, Germany, Italy, Japan, the Netherlands, New Zealand, Norway, Portugal, Sweden, Thailand, and the United States). Not surprisingly, substantial differences are found in the generational accounts across this diverse set of countries. The similarities found in these accounts, however, are striking.

For instance, in every country except for Thailand those over the age of 65 (in 1995) have a negative lifetime net tax burden (i.e., their transfer receipts exceed their tax payments), while those under the age of 50 have a positive lifetime net tax burden. In other words, with one exception, every country has seen an intergenerational redistribution from the relatively young to the relatively old. And this intergenerational redistribution is huge. For example, the estimated difference in lifetime net tax burdens of typical 25 and 70 year old Americans is \$277,300!

Another alarming finding in the generational accounts is that current (1995) fiscal policies are not sustainable in 13 of the 17 countries. Moreover, the expected fiscal imbalances in these 13 countries are large. Surprisingly, the largest imbalance is in Japan, followed by Germany, Italy, France, and the Netherlands. Moreover, these expected fiscal imbalances are not revealed by traditional debt measures. Most of the previous concern over intergenerational fiscal imbalance has examined the US situation. This book, however, reveals that the US position is not unusual. Compared to the other 16 countries, the American situation is near the median in terms of both intergenerational redistribution and fiscal unsustainability. This book also identifies the usual

culprit of the intergenerational fiscal imbalance: demographic change coupled with unfunded public pensions and public spending on health care. Slowing fertility rates are causing populations to age, and this has by far the largest single impact on the intergenerational fiscal imbalance in most of the countries in question.

The contents of the book are: a short introduction, three methodology chapters, chapters for each of the 17 countries, and a chapter summarising and comparing these 17 chapters. The material in the methodology chapters has been published previously (two are reprinted papers, and one is drawn from an earlier book chapter), but it helps to make the book self-contained. Each of the country chapters contains a detailed analysis of each country's recent fiscal policies, as well as its generational accounts, sensitivity analysis, and so forth. The varied experiences of these countries make these chapters an interesting read. For example, the German case is complicated by the costs of reunification. The Norwegian case is unique because of its large government revenues from depletable natural resources.

Naturally there are numerous debatable assumptions involved in calculating generational accounts such as the choice of discount rate, tax incidence, etc. Indeed, there are several lengthy critiques of generational accounting [Cutler (1993), Haveman (1994), Diamond (1996), and Buiters (1997)]. It is clear, however, that generational accounting is an important step in the right direction in evaluating fiscal balance. And this book is another useful step along this path. The book's jacket claims that it is 'a consummate resource for economists, political scientists, and policymakers concerned with fiscal health and responsibility.' My hope is that accountants will be added to this list someday. Generational accounting strikes me as a quintessential accounting exercise. It provides useful information for evaluating situations and making decisions. Perhaps one of the subtle contributions of generational accounting will be to push accounting research towards a more theory-based methodology.

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Privatizing Social Security. Edited by FELDSTEIN (MARTIN). (Chicago and London: University of Chicago Press, 1998. Pp. x+471. £47.95 hardback, US \$60.00 hardback. ISBN 0 226 24101 7.)

This important book examines the potential benefits for the United States of transforming its partially funded public pension scheme into individual retirement saving plans managed by private providers. The book divides into two parts. The first part studies other countries' experiences with they type of pension reform. There are chapters on pension reform in Chile, Australia, the United Kingdom, Mexico, and Argentina. The second part addresses issues of specific concern to pension reform in the United States. It includes three chapters simulating the impact of pension reform and the transition path, alongside two chapters discussing the issues of financial investment and administrative costs. The book is the outcome of a Conference held at Cambridge, Massachussets in August 1996, and both discussant's comments and a summary of the general discussion are included for each of the chapters.

In common with other countries in the developed and developing world, the United States has a public, partially funded, pay-as-you-go pension program, providing retirement, disability, and survivor benefits. Population ageing is expected to place considerable pressure on these programs, leading to rising tax rates and/or benefit reductions. Against this background, the reform of public pension programs has become an important policy issue. Discussion has centred on whether individual retirement saving accounts held with private pension fund managers are a better model for pension provision. The introductory chapter by Martin Feldstein makes a strong case for reform. He argues that payroll taxes needed to finance social security produce large distortions in the labour market, and that social security displaces private saving. Estimates of the impact of population ageing suggest the payroll tax rate needed to finance social security expenditures in the United States over the next fifty years could rise to between 18 and 23%. He concludes that the gains from replacing the public pension program with individual retirement saving accounts could be as high as 2.4% of GDP.

The chapters in the first part provide case studies of pension reform introducing individual retirement accounts. It is not surprising that three of the five case studies are from Latin America as pension reform of the type explored in the book has been extensively tested in the region. Chile replaced its social insurance pension programs with individual retirement saving accounts in 1981, rapidly becoming a paradigm for other Latin American countries. Argentina reformed its pension programs in 1994, but in contrast to Chile, the reformed pension system includes a basic public pension with a choice of either a public defined benefit program, or a private defined contribution program, as the second pillar. Mexico's reform was implemented in 1997. The Australian experience is unique in that individual retirement accounts developed from collective bargaining in the mid 1980s and have evolved into a distinctive pension program. In the United Kingdom, the 1988 reform of social security allowed employees to opt out from the public second

pillar pension scheme into individual retirement saving accounts leading to a rapid growth in this type of pension plan. These chapters provide excellent in-depth studies of pension reform in the selected countries and conclude that the balance is generally a positive one.

The five chapters included in the second part focus on the likely impact of replacing the public unfunded pension program in the United States with individual retirement saving accounts. Feldstein and Samwick simulate alternative transition paths and the impact of reform on cohorts. Kotlikoff uses an overlapping generations model to assess the impact of the introduction of a voluntary individual retirement saving accounts, while their impact on retirement behaviour is examined in a chapter by Gustman and Steimeier. Poterba and Wise concentrate on likely investment choices, while Mitchell considers the impact on administrative costs based on a careful examination of social security and pension scheme administrative costs in the United States and other countries. Overall the chapters conclude there are potential gains in the proposed pension reform.

The book makes an important contribution to the current global debate on pension reform and deserves a wide readership. There is much to be learned from the chapters in this book, both in terms of the experiences of pension reform, and in the methods needed to investigate them. The title of the book is not, however, very helpful. The editor argues that the essence of social security privatisation lies in the transfer to individuals of control over the investment of their pension contributions. This feature is largely absent from the country studies of pension reform in the book, and there is much evidence emerging from these studies suggesting that a successful introduction of individual retirement saving accounts requires considerable government and public sector support.

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The State of Working Britain. Edited by GREGG (PAUL) and WADSWORTH (JONATHAN). (Manchester: Manchester University Press, 1999. Pp. xvii+285. £45.00 hardback, £14.99 paperback. ISBN 0 7190 5646 2, 0 7190 5647 0.)

The State of Working Britain is likely to be an often up-dated standard work on recent developments in the British labour market. It meets a major need: the provision of up-to-date labour market analysis firmly based on the best available statistics. It provides a valuable variant on the earlier *The State of Working America*, published by the Economic Institute in Washington.

Several essays bring out the increasingly relative weaker position of men, especially over 50, and the stronger position of women, notably those with children, in the labour market. Paul Gregg and Jeremy Wadsworth on 'Economic inactivity' argue that the substantial rise in male inactivity (from 400,000 to 2.3 million non-student males of working age) over twenty years was

not principally due to early retirement, as is often thought. They find that the higher the unemployment rate, the higher the male inactivity rate, with the least skilled worst affected.

This collection of essays also reinforces the importance of legislation in improving the position of women in the labour market. The gender gap in employment rates fell from 33 to 12% in 1975–8. Tanvai Desai, Paul Gregg, Julian Steer, and Jonathan Wadsworth in 'Gender and the labour market' point to the increased number of women with young children in full time work as the main beneficiaries with nearly two-thirds returning to the same employer after child-birth. The Maternity Rights legislation of 1978, reinforced by that of 1993, enabled this to happen in Britain, as has occurred in other countries with similar legislation. They also point to a closing of the gender pay gap from the early 1970s, assisted partly by the Equal Pay Acts of 1975 and 1983 as well as by better rewards for education, training, and experience. The authors rightly predicted that women in part-time jobs would be major beneficiaries of the statutory minimum wage.

Steven Machin, in his analysis of 'Wage inequality in the 1970s, 1980s, and 1990s', shows that wage inequality rose faster in Britain than in most other countries from the late 1970s, with the most rapid growth in the Thatcher years. His essay supports the view that the more technologically advanced industries require more skilled labour and that in spite of a greater supply there has not been a fall in relative wages. He finds little evidence of a link between rising import competition from developing countries and rising labour market inequality. He is more impressed by the likelihood that part of the rise in wage inequality is due to the weakening strength of the trade unions.

Simon Bargess and Carol Propper in 'Poverty in Britain' provide details of the rapid rise in numbers of people in poverty (according to various definitions) between 1979 and the mid 1990s. They find that the greatest rise in poverty has come in households with children. Whereas in 1979 one in twelve children lived in poor households, by the mid 1990s this had risen to one in three.

In analysing 'Wage mobility in Great Britain' Richard Dickens dismisses notions that those receiving low pay are likely to move on to better pay. He finds that more are likely to be in a low pay-no pay cycle. This is confirmed by Mark Stewart in 'Low Pay in Britain', where he also finds that the longer someone is unemployed the less likely they are to move out of low pay.

The State of Working Britain is a very welcome addition to the literature. A future edition would be strengthened by an analysis of the role of the trade unions in the labour market. The British trade unions were weakened in the 1980s and 1990s, but even in 1997 remained a more substantial presence than in several other OECD countries. The book would also be much enhanced by more – and also more systematic – comparisons with other OECD countries. In the first edition, Susan Harkness' contribution, 'Working 9 to 5', and Stephen Machin's on wage inequality, make some valuable use of comparative data. Notwithstanding the major problems of using statistics from several

countries, such a dimension should be a norm for many essays in a future edition.

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Unequal Pay for Women and Men: Evidence from the British Birth Cohort Studies.

By JOSHI (HEATHER) and PACI (PIRELLA). (Cambridge, Mass. and London: MIT Press, 1998. Pp. xvii+181. £19.95 hardback. ISBN 0 262 10068 1.)

This book provides contemporary evidence about gender pay differentials in Britain, using evidence from two large and detailed longitudinal data sets, the National Child Development Survey, NCDS (a cohort born in 1958) and the Medical Research Council National Survey of Health and Development (a cohort born in 1946). The timing of the surveys enables the authors to both compare gender pay differentials at particular points in time, and to analyse the extent to which they have changed over time. This enables them to evaluate the effectiveness of British equal pay legislation in the 1970s. They are amongst the first to exploit the 5th wave of the NCDS (from 1991) for this purpose.

The book is interesting and well written; several chapters are co-written with Jane Waldfogel and Gerry Makepeace. The book starts with a general discussion of discrimination, in particular the circumstances under which unequal pay may be indicative of discrimination. The Blinder-Oaxaca decomposition technique, which distinguishes between unequal characteristics and unequal treatment of the same characteristics, is first described. This technique, which is used extensively throughout the book, assumes that human capital characteristics are exogenous. In my view, the problems this causes are not highlighted sufficiently in the text. For example, fewer women may choose to accumulate human capital if they anticipate adverse discrimination; but this will then spuriously show up as 'non-discrimination' according to the decomposition. Ideally, future work should construct a full model of endogenous human capital accumulation in which this additional effect of discrimination can be identified.

The authors do not attempt a theoretical treatment; rather, theirs is a purely empirical study. After describing the data sets, they adopt a sequential approach to uncovering the possible causes of unequal pay. Chapter 4 deals with human capital characteristics. It is found that a narrowing of human capital differences between genders is responsible for much of the decline in the gender pay gap. Chapter 5 then considers whether different job characteristics also help explain the pay differential. A rich variety of job-related variables augment the human capital variables, a key strength of the data sets. The authors are most successful in accounting for the differential wage rates of part-time versus full-time women, but less so for full-time men versus full-time women. I think the former is worthy of remark, since it points to a role for

omitted variables (rather than discrimination) in explaining unequal pay. Presumably the same caveat applies to the analysis of the full-time gender differential. It is to the authors' credit that they recognise this possibility, and also that discrimination may push the other way via women bunching into low paid occupations. Again, it would seem that there is, at least in principle, scope for theoretical work to pin down this type of effect.

A particularly interesting finding appears in the penultimate chapter, which asks whether family responsibilities help explain women's low pay. It is commonly thought that low female part-time pay is caused by a high concentration of mothers in this sector. Yet the authors argue that reverse causality appears to exist: mothers tend to be poorly paid *because* they are part-timers. The final chapter concludes with an overview of the findings and policy implications. Concerning the findings, women in a given occupation are still, all other observable factors held constant, paid 12% less than men if full-time, and 19% less if part-time. Moreover, there has been only a limited reduction in unequal pay over time, of around 9% for women in their early thirties between 1978 and 1991. Regarding the policy implications, the authors lament the de-regulation of the labour markets in the 1980s as weakening the channels through which anti-discrimination policies can operate. Their favoured policy instruments are a national minimum wage (which has of course since been re-introduced), job training for women, paternity leave, better child care, and raising awareness of the 'gender agenda'. Monopsony is used as a counter-argument to the notion that a minimum wage could actually harm those it is intended to help; it is also referred to elsewhere in the book. Apart from the extreme nature of this market structure, there seems to be a problem in the argument. If labour and product markets have become more competitive as a consequence of de-regulation, then it should be easier for new entrants to compete away monopsony profits, so destroying monopsonies.

Overall the book is an example of good, objective, and careful scholarship. It provides a thorough treatment of gender discrimination in Britain that will appeal to labour economists in all countries. It can be warmly recommended to anyone interested in labour market discrimination.

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Legalizing Gender Inequality: Courts, Markets, and Unequal Pay for Women in America. By NELSON (ROBERT L.) and BRIDGES (WILLIAM P.). (Cambridge and New York: Cambridge University Press, 1999. Pp. xvi+393. £40.00 hardback, US \$59.95 hardback, £14.95 paperback, US \$19.95 paperback. ISBN 0 521 62169 0, 0 521 62750 8.)

In 1981 the Supreme Court opened the door to comparable worth claims, in the *Gunther* case, by enabling plaintiffs to use job evaluation results to demonstrate sex-based pay discrimination. For the first time valid comparisons could be made across organisations and lower earnings as a consequence of female

crowding were not regarded as a legitimate form of pay differentiation. However, in 1985 this result was overturned in *AFSCME v State of Washington*, when Judge Kennedy pronounced that 'neither law nor logic deems the free market a suspect enterprise. Title VII does not obligate [the State of Washington] to eliminate an economic inequality it did not create.' The authors, both sociologists, see this episode as reflecting an ideological bias in favour of the market by the Courts and a belief in the power of market forces in the labour market which is not justified by available evidence.

A large part of the book is based on re-analysis of four decided legal cases of discrimination – two in the public and two in the private sector. The authors recognise that this is a weak basis on which to formulate general theories, but believe that the depth of their analysis more than compensates for this. The re-analysis consists of examination of legal documents, an element of regression analysis, and interviews with key participants.

In the first case *Christensen v State of Iowa* a class action suit was brought against a university which paid (predominantly male) physical plant workers more than female clerks, despite an equal ranking based on job evaluation on the grounds that this reflected local labour market realities. The authors argue that the market issue was not subject to close analysis in the course of the litigation. In fact, there was no evidence of plant workers being in short supply in the local labour market. Rather, they conclude, wage policies reflected the superior political position of male relative to female workers within the university. However, an alternative interpretation is that males were more wage-orientated than women, engaging in collective action on this issue, while the female clerks were content simply to participate in committee meetings with university officials on matters relating to minor working conditions, suggestive of gender supply side or taste differences.

In the second public sector case, *AFSCME v State of Washington*, salaries in predominantly male jobs were 50% higher than in those predominantly female. It appeared that personnel staff attempted to accommodate pressures from various constituents by operating the wage survey, on which rates were based, in a flexible manner, so that in the words of the authors the system was 'shot through with subjectivity, arbitrariness, and interest group politics, virtually from beginning to end.' People working in mixed or female jobs appeared to be disadvantaged not so much from overt discrimination as from neglect, in so far as agency and union staff rarely filed claims on their behalf.

In the first private sector case, *EEOC v Sears, Roebuck and Co.*, the focus of the pay claim was a set of 51 checklist jobs used as the basis for pay comparison. In the authors' pay regressions the coefficient on sex was almost always negative and frequently significant. The compensation system had veered out of control with regard to the market wage rates in other large enterprises to such a degree that a centralised job evaluation system was introduced in 1976, which severely constrained the discretion to set wages on the part of store managers. Thereafter both the gender pay gap and job segregation diminished. The authors suggest that Sears' court victory in this case owed much to the failure of the plaintiffs to produce in court individual workers subject to discrimina-

tion, though it appeared also that one reason for the lower pay of women was a reluctance on their part to move geographically, thereby obtaining relocation allowances to the same degree as men.

In the final case, *Glass v Coastal Bank*, testimony by individual employees was key to the Court's judgement in favour of the plaintiffs. The bank had adopted traditional values to the extent that until 1975 it had maintained separate training programmes for men and women, excluded women from some departments, and placed female graduates routinely in secretarial and clerical posts. The incorporation of a percent female variable in a random effects wage model had a large and significantly negative effect for non-officers (but not so for officers) and this was to be explained by the lack of power of women in the politics of the organisation.

The central thesis of the authors, based on the (partial) evidence from their four case studies, is that gender-based pay inequality is largely the product of organisational forces within well-developed internal labour markets subject to male domination. Organisations only loosely follow the market, as indicated by the fact that only a small proportion of jobs are compared externally, salary survey methods are arbitrary, job comparisons are non-systematic, traditional differentials are maintained, and managerial discretion in pay-setting is common. Explanations based on efficiency wage models are also largely dismissed and comparable worth too is rejected. Recommendations include purging job evaluation of its inherent male biases; a movement away from establishing invidious intent on the part of employers in legal cases towards a need to justify wage differentials unexplained by genuine market or efficiency considerations; and mandatory pay equity studies or audits, as practised in Ontario.

To this reviewer there is not much that is as novel as the authors imply in all of this. Using partial data from just four organisations is hardly a strong refutation of the ubiquity of market forces. Nor should market forces, efficiency wages, job evaluation, and internal organisational issues be regarded as independent of one another. As Killingsworth (1990) has noted, in the absence of wage change models one cannot reject the hypothesis that the female intensity of jobs is a proxy for unmeasured skill and taste differences among workers, as confirmed by MacPherson and Hirsch (1995) using large data sets with panel elements over the period 1983 to 1993. One indication that internal organisational factors are not totally dominant is found in the fact that for both men and women, and including inter as well as intra-firm effects, earnings tend to be only 7% lower in typically female than in typically male occupations. Nor should it be automatically assumed that job evaluation systematically undervalues the work of women. A study of Iowa State government jobs (Chen et al, 1999), for instance, found that measurement errors in the job-evaluated scheme exaggerated the implied amount of discrimination against predominantly female jobs by 34 to 44%. What the book suggests is that much more research is required before the precise role of market forces, efficiency effects, and organisational factors on the gender wage gap can be established.

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Low-Wage Employment in Europe. Edited by BAZEN (STEPHEN), GREGORY (MARY) and SALVERDA (WIEMER). (Aldershot and Lyme, NH: Edward Elgar, 1998. Pp. xiii+200. £49.95 hardback. ISBN 1 85898 932 9.)

Low-Wage Employment in Europe examines the impact of low-wage employment in different countries in Europe. This is the most recent in a series of books to come out of the European Low-Wage Employment Research (LoWER) Network. As with the previous book, *Low Pay and Earnings Mobility in Europe*, the central questions are explored in a collection of empirical papers that compare and contrast the structure and outcomes of a number of European labour markets in terms of employment, institutions, wages, and poverty.

The book is split into three parts. The first includes three chapters providing international comparisons covering low-wage employment and poverty. The second includes three individual country experiences of low-wage employment, earnings, and poverty in Ireland, Germany, and Spain. The final part includes two chapters on youth workers and low-wage employment/mobility in France and the Netherlands. A detailed examination of each chapter is beyond the scope of this review so I have focussed on one or two papers from each section.

In part one, Bazen, Gregory and Salverda compare and contrast the low-wage employment experiences in the United Kingdom, France, and the Netherlands. Although the data sets analysed exclude (as the authors clearly note) two important sections of the low-wage population (part-time and very young workers) the figures still show the distinct low-wage employment experiences of each country since 1976 to the early 1990s. The different policy stances taken in relation to minimum wages have clearly had an important impact on the incidence of low-wage employment over time. For example, in France the percentage low-paid fell from 17% to 14% over this period while the minimum wage has been uprated through indexing since 1970 as well as benefiting from discretionary increases by successive governments. In the chapter by Marx and Verbist a cross-country comparison of poverty and low-wage employment is presented. The link between low-wage employment and household poverty is not found to be overwhelming. 'Poverty in work' tends to be determined by whether the low-wage worker is the main 'bread-winner' or not. Two earner households tend to avoid poverty, the main exception to this is the United States where almost 8% of these couples live in poverty.

In part two, Nolan investigates the links between trends in the earnings distribution, low pay, and household poverty in Ireland, one of the OECD countries with the highest levels of low-wage employment. Between 1987–1994

the earnings distribution widened consistently – the top decile rising from 196% to 224% of the median – and the percentage of full-time employees earning less than two thirds of the median wage increased slightly from 21% to 23%. Only a small percentage of the low-paid are found in poverty households – in 1994 only 5.5% are below 50% of mean income. In the chapter by Dolada, Felgueroso, and Jimeno the effects of minimum wages in Spain are presented. Spain is a particularly interesting country as it has an unemployment rate of 20%, the highest in the OECD. The numbers of individuals directly affected by the minimum wage is quite low as 85% of wage earners are covered by collective agreements. However, minimum wage increases for youths in 1990 are found to have a negative impact on the employment of workers aged 16–19 but a positive impact for 20–24 year olds, suggesting substitution of adult workers for youths.

In the final section Balsan, Hanchane, and Werquin provide an interesting analysis of wage mobility and earnings profiles of low-skilled youths in France using a six-year panel. Finding that youth schemes (for school leavers exiting school without a baccalaureate) improve the probability of getting a job but not higher wages. This is an important result, as high youth unemployment is a feature of many European labour markets and particularly relevant to the United Kingdom after the introduction of the ‘New Deal’ (initially for the under 25s).

To summarise, minimum wage policies provide some protection for low-paid workers but to reduce low-wage employment requires regular uprating over time. Secondly that relatively inflexible labour markets still have low-wage employment and finally, that the eradication of poverty requires more than just a minimum wage, as large numbers of households in poverty have no earners. The main criticism of the book that I would make is not so much based on what is included but rather what is not. The cover summary and introductory chapter make much of the question ‘does low-wage employment reduce unemployment’, however nowhere in the book is this question comprehensively addressed. Even so, this book provides a useful and timely contribution to the debate on low-wage employment. Particularly so for the United Kingdom as we approach the first anniversary of the National Minimum Wage and the imminent debate on uprating. This book would be a useful source of information for many Economists in policy and academic environments interested in this and other low-wage employment issues.

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Reference

Asplund, R., Sloane, P. and Theodossiou, I. (eds.) (1998) *Low Pay and Earnings Mobility in Europe*, Cheltenham: Edward Elgar.

Global Labour Flexibility: Seeking Distributive Justice. By STANDING (GUY). (London and Basingstoke: Macmillan, 1999. Pp. xv+441. £42.50 hardback, £19.50 paperback. ISBN 0 333 77314 4, 0 333 77652 6.)

The author's declared aim was to develop a work-based strategy for distributive justice, and I plunged in with considerable anticipation. What I think he has ended up with is a civilised approach to many of the major economic and social issues of the 20th century. It is clear what he wants to see in the 21st century but it is not clear how he envisages getting there. However he does provide a great deal of material which has to be taken account of in developing alternative developmental strategies to take us through into a future which is a happier place for more than simply the tiny advantaged minority.

The book begins with conceptual issues in the area of labour and work before going on to the growth of flexibility and insecurity and thence to policy. The conceptual issues in this area of economic analysis are very important and the author does a good job (?) in covering the complexities in a systematic and accessible way, but what is offered is an interesting collage of pretty well known conceptual issues. The concerns are long-standing ones and no particularly new insight or analysis is achieved. I found it disappointing that he ends up the conceptual chapter with 'the essential fuzziness of the notion of the labour market', (page 30). Whilst I can see what he means, what we need is a firmer platform for the way forward. Nevertheless I do find his discussion of the growth of flexibility and insecurity quite compelling.

He divides the post-war era in the United States and Western Europe between an earlier period of statutory regulation (up to 1975) and a later one of market regulation. He does not care for the Golden Age description of the earlier period, seeing it as a period of tension and distributional conflict. For the later period he demonstrates how the neo-liberals captured the language and complains about the 'visionless defensiveness of those opposing the neo-liberal onslaught,' (page 59) both points well-taken I thought. On flexibility he poses the obvious but crucial paradox for its advocates: why was unemployment so much higher at the end of a prolonged period of growing flexibility if increased flexibility was supposed to lower it?

Just as the treatment of flexibility provides an excellent compendium of knowledge for those seeking to understand the current reality, so does his treatment of rising insecurity in its many dimensions. He makes an important first point on what has been regarded as full employment – again obvious but of great significance: he sees full employment as never having existed, except for males! Thus there can be no return to it, even in Sweden. He proceeds to analyse unemployment experiences by estimating a variety of simple regressions for a wide cross-section of countries, with some interesting and revealing results, relating, for example, to the relationship between jobs growth and deflation in a globalising world. A wealth of information on a current reality – and a comment on it culled from the *International Herald Tribune*: 'Bargaining now is impossible for any task that can be exported. This now is universally true'. The sort of comment that stops you in your tracks, even if you see it as too stark.

Finally, the author turns to policy matters. He is generally disparaging of labourist options (minimum wages, labour subsidies, tax credits), seeing them as not appropriate to the flexible labour markets now prevailing, but retains most of his vitriol for workfare – ‘it is judgmental, it is paternalistic, it erodes real freedom; it is socially divisive, and it may block forms of social and economic participation, such as voluntary community service’ (page 333). He does not like it – and for good reason! Yet the argument all around us is that welfare has to be rolled back – it cannot be afforded, despite the same people often claiming that wealth is being created at an historically fast pace. One might ask, as Robert Reich did about the United States the other day, why is it that the wealthiest country in the world cannot provide access to health care to more than 40% of its population? Policy-makers have rarely been so deferential to the rich in recent history. Of course, one of the reasons they cosset them is because, as well as being rich, they are the ones who are driving the global system. To counter this situation we have to work for a redistribution of power – but how will this be achieved? The author observes, on the last page that ‘The forward march is usually resumed when the losers remember their history and find their voice’. Yes, and this process can be helped by people in the profession writing books like Guy Standing has, but perhaps going a little further in beginning the design of a way forward which is more hopeful for more people.

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Global Transformations: Politics, Economics and Culture. By HELD (DAVID), MCGREW (ANTHONY), GOLDBLATT (DAVID) et al. (Oxford: Polity Press, 1999. Pp. xxiii+515. £59.50 hardback, £16.99 paperback. ISBN 0 7456 1498 1, 0 7456 1499 X.)

The stated aim of this volume is to ‘investigate the extent to which regionalisation and globalisation are transforming the nature of world order and the position of national sovereignty and autonomy within it’ (page xix). The discussion proceeds in terms of a series of ‘case studies’, each focused on a particular aspect of global transformation. Issues examined cover, in order, organised violence, trade and global production, global finance, corporate power and global production networks, migration, cultural globalisation, and globalisation and the environment. There are introductory and concluding chapters. Each of the case studies or issue chapters offers a historical review of the aspect of globalisation under discussion and then proceeds to evaluate contemporary developments and their effects.

Important twin objectives of the volume are to provide an analytical basis for the study of globalisation and to place contemporary developments into historical perspective. The authors take the literature on globalisation to task for having no cogent theory and providing no coherent historical narrative. They intend to provide ‘a distinctive account of globalisation which is both

historically grounded and informed by a rigorous analytical framework' (page 1). The introductory chapter sets out a logical framework, made up of a series of definitions and a conceptual structure. This is a useful exercise and will help many readers to think more coherently about the issue. It is, however, not a 'rigorous analytical framework'.

Globalisation is described in the introduction as 'the widening, deepening and speeding up of world-wide interconnectedness' (page 2). It is the 'intensification of global connectedness' that is important here and this core idea is then defined in terms of a series of concepts and logical categories, designed to provide the analytical framework for the case studies that follow. The major ordering principles include the extensity of global networks, the intensity of global interconnectedness, the velocity of global flows, and the impact propensity of global interconnectedness. In order to place the discussion within the context of the ongoing debate on globalisation, the approaches of three major schools of thought – hyperglobal, sceptic, and transformational – are compared and contrasted.

In each of the issue chapters, the modern variant of globalisation is compared with earlier episodes in order to determine what it is that is new and different about the contemporary phenomenon. The three other epochs come under the heading of premodern, early modern, and modern. This is a very useful comparison. It helps to remind the reader that globalisation and its challenges are not a new phenomenon and it lays bare the essential differences between past and present episodes.

Among the volume 'strengths' is the focus on sorting, categorising, and organising a wealth of material in terms of a relatively parsimonious selection of criteria. This feature is especially evident in the summary tables and grids which accompany the discussion. The stress is on inclusiveness, on ensuring that important or potentially important considerations are not left out. The case-study chapters make informative reading on their own, as well as in the context of understanding globalisation. A reader interested in the spread of global production networks, for example, will find much useful information in chapter 5, regardless of whether he cares about globalisation or not.

While the authors succeed in amassing a great deal of important information, they do not consistently provide the reader with help in evaluating the relative importance of the many forces that are at work in the process of globalisation.

A concluding chapter, however, attempts to bring the findings together, focusing first on the differences between earlier and contemporary phases of globalisation and then on the implications of the latter for the future of the nation state. A related question deals with the extent to which the process of globalisation may be subject to 'civilising' and 'democratising' influences.

As noted, a strength of this effort is in categorisation and ordering of information. Ideas, arguments, and insights from a great diversity of sources are brought together and presented in an organised and easily digestible fashion. The many tables and grids are very well done. The individual chapters provide valuable overviews and assessments of the issues they cover, be it trade,

the history of warfare, global finance, or global migration. The reader interested in probing beyond description and categorisation, however, is less likely to be satisfied.

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Labour Standards and International Competitiveness: A Comparative Analysis of Developing and Industrialized Countries. By RAYNAULD (ANDRE) and VIDAL (JEAN-PIERRE). (Aldershot and Lyme, NH: Edward Elgar, 1998. Pp. ix+117. £39.95 hardback. ISBN 1 85898 949 3.)

This is a short book about a hot topic: the relationship between labour rights and competitiveness. The World Trade Organisation's chaotic meeting in Seattle in December 1999 brought back into the spotlight the question of whether multilateral trade agreements should be conditional upon the respect of fundamental labour rights. As noted by Raynault and Vidal in their introduction, the lack of stringent labour standards in developing countries is seen in many industrialised countries as a source of unfair competition. Most developing countries, on the other hand, view the linkage between trade and labour rights as a threat to their exports. The aim of the book is to determine whether labour standards really have an impact upon the competitiveness of firms. According to Raynault and Vidal the answer is an unambiguous 'no', but their analysis in support of this answer is less than convincing.

The book is split into three parts. The first chapter is a brief but useful review of the history and politics of labour standards. The second chapter provides a theoretical analysis of the benefits and costs of labour standards as well as of the links between labour compensation and competitiveness. The final chapter presents some empirical evidence.

An important argument in the book's second chapter is that since theory indicates that compensation must always be equal to labour's marginal productivity, the cost of standards must ultimately be shifted onto workers through lower wages. Thus, according to Raynault and Vidal, there is no reason to fear that labour standards will result in unemployment or in a loss of competitiveness (page 32). This argument is reinforced in a small model in which only one good is traded in world markets and in which labour costs and productivity are both ten times higher in industrialised than in developing countries. This model is intended to show that 'a country where wages and productivity are lower than elsewhere has no comparative advantage' (page 42).

Both labour economists and trade economists are likely to raise their eyebrows. The relationship between compensation and productivity does not necessarily imply that labour standards have no impact upon labour costs. In principle, any exogenous increase in labour costs could cause a corresponding increase in marginal productivity by inducing firms to reduce employment. Thus, whether labour standards lead to lower wages or higher labour costs – or both – is an issue that requires empirical scrutiny. Moreover, the evidence

now available suggests that the cost of standards is not always fully compensated through lower wages. MacIsaac and Rama (1997), for example, find that in Ecuador only part of the costs of centrally mandated benefits are shifted onto workers. There is also a large literature showing that collective bargaining can lead to a substantial wage gap between union members and other workers (see, for example, Filer et al. 1996).

In addition, Raynauld and Vidal's model neglects standard trade theory, most obviously because any analysis of trade must involve at least two goods, without which international exchange and comparative advantage simply cannot be considered. The book's lack of reference to existing trade theory also undermines the credibility of the statement, apparently based on the book's model, that 'since marginal output of a given factor is generally not the same in developed and in developing countries, the view that the factor-price equalisation theorem predicts a collapse of compensation in developed countries is mistaken' (pages 44–45).

The empirical section of the book finds, like most studies on the same subject, that high labour standards have no significant impact on countries' shares of world exports, foreign investment, or unit labour costs. Raynauld and Vidal divide their data set into two groups: on the one hand the twenty countries with high labour standards and, on the other hand, all the other countries, with lower standards, for which data are available. The authors then look at the percentages of high and low standards countries whose exports, investment, and so on have changed in either direction over the periods 1970–1993 and 1980–1993. They find that, on average, countries with low standards did not perform better than those with high standards. But here again, the findings are questionable, mostly because the chosen indicator of labour standards is the human development index (computed by UNDP in its yearly Human Development Report). This index – constructed from data on life expectancy, GDP per capita, literacy rates, and combined school enrolment ratios – has little to do with labour standards as usually discussed.

On the whole, therefore, the book – despite some interesting sections – contributes little to the deepening of our understanding of the links between competitiveness and labour standards. The issue of how some nations' weak labour rights impact upon countries with better standards remains open to research.

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Globalization and History: The Evolution of a Nineteenth-Century Atlantic Economy.
By O'ROURKE (KEVIN H.) and WILLIAMSON (JEFFREY G.). (Cambridge, Mass. and London: MIT Press, 1999. Pp. xii+343. £31.50 hardback. ISBN 0 262 15049 2.)

This ambitious volume not only aims to explain why some countries in the later 19th century Atlantic economy converged with the leader and why others did not. It also draws conclusions for the contemporary world economy and, in particular, for the North-South debate on trade and inequality. Much of the convergence literature has been concerned with processes generated by closed neoclassical or endogenous growth models. By contrast Jeffrey Williamson and Kevin O'Rourke focus on 'Hecksher-Ohlin forces'; the international movement of capital, labour, and goods, and the convergence of factor and product prices. Underpinning the modelling is a substantial earlier international data construction exercise for the real wages of urban unskilled workers.

If 'Hecksher-Ohlin forces' or 'globalization', rather than closed economy neoclassical growth, was driving world development, we would expect to find stronger convergence of wages than GDP per head. As international freight costs declined between 1870 and 1914 rural rents in Britain fell substantially, while wages indeed rose by more than GDP per head. Owners of British land were unable to prevent trade redistributing their income, as land-intensive goods were imported from the 'New World' (or 'neo-Europe'). On continental Europe, where political power and property were arranged differently, anti-trade reactions were more common. Rural rents were not allowed to collapse so far.

At the prospect of higher wages, European workers uprooted themselves to build new lives in land-abundant economies. Such factor mobility, a more direct equilibrating process, was also necessarily more powerful than moving products. Symmetrically with the European trade backlash, but later in timing, were the immigration restrictions in neo-Europe on behalf of domestic wage earners.

O'Rourke and Williamson elaborate, test, and quantify this story. They adopt two broad approaches to impact estimation. The first is investigation of shocks (such as falling transport costs and tariffs) to sector-specific-factors CGE models. In these, labour is mobile between sectors, but land is specific to agriculture and capital to industry. The second approach entails parameter estimation by regression models. Some of these are Barro-type conditional convergence regressions, usually with wage changes as dependent variable, instead of the more conventional GDP/GNP per head. Models include explanations for wage-rental ratios and regressions that explain inequality movements measured by the rate of change of unskilled wages relative to GDP per head. Finally there are the policy regressions, with a categorical dependent variable for the intensity of immigration restrictions.

The results show that after 1870 migration mattered a great deal where it happened, in Ireland and Italy. The absence of migration from Iberia accounted for some lack of wage convergence. But it is a rather special notion

of convergence that turns on people leaving an economy to raise the living standards of those remaining. Education (schooling) encouraged convergence in some countries but not in others; lack of it may explain a substantial component of Iberia's lag. International capital flows slightly increased equality, especially Scandinavia's catching up Britain. Trade effects were usually modest, thanks in part to tariff protection feedback. Cheap New World grain lowered real wages in France by reducing demand for agricultural labour in the large agricultural sector, but tariffs limited the impact. Without protection, trade increased the Irish-American wage gap. Trade and capital flows were often complements, as were trade and migration. Rising inequality in land-rich 'neo-Europe' ceased when migration was choked off by restrictions, and inequality appears as a significant predictor of restrictive immigration policy. The present day analogy is skill-abundance in the 'North', in comparison with land-abundance then. If history repeats itself, policy will become increasingly restrictive.

This is unquestionably a remarkable work of analysis that also synthesises a vast range of data and literature. Inevitably some of the data summaries will be at too high a level of abstraction for a few readers. For example, they might want to know what underlies the Australian immigration policy index fluctuation, around the time of the introduction of the literacy test, that is so briefly discussed (page 187). Some find interpretations of CGE models congenial; others are uncomfortable at being presented with a 'black box' and wonder about sensitivity to alternative plausible structures. However most will appreciate the lucid exposition.

Much of the analysis is concerned with growth rates, presumably to connect with the convergence literature. But some of the econometric evidence suggests levels are more appropriate. Moreover, differencing levels series with measurement errors may well increase the error proportion in the new growth series. A compelling reason for considering levels of wages or GNP per head is that welfare is ultimately about levels of living standards, rather than their growth.

In summary table 14.4 (page 281), O'Rourke and Williamson explain the (wage) convergence that did occur. It would be valuable as well to summarise forces making for the absence of convergence of various economies – the impacts on wage and income gaps of plausible counterfactual conditions. Readers will also want to know what other elements might have influenced convergence or divergence. The authors note they have not considered technology transfer, but other omissions, discussed in the historical literature, include natural resource endowments, such as coal deposits and climate.

These remarks are however merely to place the study in a wider context. All those concerned with building and maintaining an open, liberal world economy certainly should consider the lessons of this book.

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Globalization and Labor. Edited by SIEBERT (HORST). (Bremen: Institute for World Economics, 1999. Pp. viii+320. ISBN 3 16 147183 0.)

This is the latest of several good conference volumes over the past couple of years which are concerned with the impact of globalisation (reduced barriers to international flows of goods, capital, and knowledge) on national labour markets. The papers cover a broad range of issues and their authors include some prominent contributors to what has become a large and lively debate – Bhagwati, Leamer, Markusen, and Slaughter. Economists who have not followed the debate would benefit from reading most of this book. By contrast, those who are familiar with the debate should read it more selectively, since there is quite a lot of recapitulation of material that has appeared elsewhere. Even for the latter group of readers, however, the book is well worth getting, since it contains some high-quality value added.

The star of the show is a brilliant and profound (albeit long) paper by Richard Baldwin and Philippe Martin, which the editor has rightly placed first in the volume. It compares the globalisation experience of the late 20th century with that of the late 19th century, placing both phases in the even longer-term context of the industrial revolution which began in the 18th century. The key question is why, in the 19th century, globalisation industrialised the North and deindustrialised the South (in 1750, three-quarters of the world's manufactures were produced in countries which are now classed as developing), whereas in the late 20th century it did the opposite – deindustrialising the North and industrialising large parts of the South.

The answer which Baldwin and Martin suggest, based on the theories of Romer and Krugman and on an impressive variety of empirical evidence, is that in the 19th century transport costs fell faster than communication costs (causing agglomeration of production and innovation in the North), whereas in the late 20th century the cost of transporting goods was approaching a lower asymptote but the cost of communication continued to plummet, permitting industrial technologies and hence production to be transferred easily and quickly to the South. I find this answer compelling, although I think that cheaper and quicker business travel (falls in the cost of transporting people, as opposed to goods) was just as important as falls in the cost of communication in facilitating the transfer of industrial production to the South.

The next nugget is a concise and thoughtful survey by Tamim Bayoumi of recent work on international capital mobility, focused on the conflict of evidence between studies of interest rates, which suggest a lot of mobility, and studies of saving, investment, and consumption, which suggest much less mobility. He assesses critically both sets of evidence, but in the end rejects neither of them, suggesting persuasively that they can be reconciled by recognising that short-term capital is far more mobile internationally than long-term capital.

A similarly concise review by James Markusen of the main findings of his recent influential work on multinational firms, based on the 'knowledge-capital' model, is followed by some polite but devastating comments by

Dietmar Harhoff, who observes that the key assumptions of this model are contradicted by much empirical evidence. Most R&D does not appear to be a fixed cost of developing new products or processes which has to be spread over a large volume of output. The transfer of knowledge from one part of a multinational firm to another is by no means costless – it may be as expensive as the initial development of the knowledge. And R&D is increasingly carried out in the overseas subsidiaries of multinational firms.

Edward Leamer's chapter on the effects of trade on wage inequality contains much that will be familiar to those who know his earlier work in this area (and is as ever distinguished by its wit as well as its intellectual rigour), but it breaks important new ground in two respects. One is to analyse the effects of distance and differences in location. The other is to look more closely at the situation of countries which, in a trading equilibrium, are specialised rather than diversified producers and whose wages are therefore not simply dictated by world prices but dependent also on domestic factor supply and demand. By contrast, the chapter by Jonathan Haskel and Matthew Slaughter, analysing the effects of technical progress on wage inequality (with particular emphasis on the importance of sectoral, as opposed to factoral, bias) remains firmly set in the diversified or 'one-cone' version of Heckscher-Ohlin theory.

These chapters could be read in a morning. But if you have the afternoon to spare, there are other stimulating bits, ranging from Michael Burda and Barbara Dluhosch's theoretical model of how North-North (and not just North-South) outsourcing might affect wage inequality to Deepak Lal's historical account of how two Popes named Gregory transformed the course of Western economic development.

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Democratic Choice and Taxation: A Theoretical and Empirical Analysis. By HETTICH (WALTER) and WINER (STANLEY L.). (Cambridge and New York: Cambridge University Press, 1999. Pp. xi+331. £35.00 hardback, US \$59.95 hardback. ISBN 0 521 62291 3.)

Hettich and Winer's monograph is a synthesis and extension of work that they have been involved in and which has mostly appeared in journals. However it is not simply a collection of papers but is an ambitious book both in terms of the issues considered and particularly, at least to this reviewer, the range of techniques used. Theory, micro and macroeconometrics, and simulation are all used here mostly to good effect. So there is something in here for everyone although aficionados of some of those methods may not be over-awed by the level of sophistication.

The monograph is about the *public choice* approach to tax policy: how tax structure is determined by, or interacts with, political constraints on policy makers. It does not deal with the big questions favoured by the *political economy* approach. By tax structure one means not just the size of the government

budget but the complexity of the tax system, the number of tax bands, the relative use of different tax bases, special provisions, and so on. The authors set out their stall at the beginning by outlining no less than six possible theoretical frameworks: median voter models, structure induced equilibrium, probabilistic voting, the 'Leviathan' or budget maximising bureaucrat, cooperative game theory, and representative voter models. To choose between these approaches the authors suggest four stylised facts that a model must explain, notably the absence of vote cycling and the multi dimensionality of both the tax system and tax policy. They conclude that probabilistic voting (politicians choose their policies to maximise the expected vote) is the best bet.

The opening chapters provide a series of theoretical models of equilibrium tax structure. Starting from a situation with heterogeneous individuals who politicians would like to tax separately they ask why individuals are invariably grouped in tax bands. The answer of course is administration costs. In a chapter (co-authored with George Warskett) they extend the framework to allow for self-selection by individuals with different abilities so a 'single crossing' property is invoked. They develop a model in which voters are grouped in tax bands within which the variance of their 'ideal' tax rates is minimised and between which the variance is maximised. While the result is hardly earth shattering it is useful to see this formally modeled. They also outline an existing result central to their approach which they call a Representation Theorem namely that equilibrium in the vote maximisation model corresponds to a Nash equilibrium to a particular game.

The most interesting part of the book comes in chapter 7: 'Tax Policy in a Computable Model of Economic and Political Equilibrium'. Based on work with Tom Rutherford, they link their probabilistic voting model with a CGE model, the well-known GEMTAP model of US fiscal policy. Households are aggregated based on income levels and the relative shares of capital income to allow the creation of interest groups. Such a model allows them to ask several interesting questions. Having calibrated the political support function implied by the Representation theorem, counterfactual simulations allow them to distinguish between political and economic determinants of the changes to fiscal policy between 1973 and 1983. They also simulate the implications for policy if political influence was more equally distributed. While CGE models are not to everyone's taste and the research literature often inaccessible to outsiders this approach is fascinating and deserves wider currency. One can think of many policy issues with thorny re-distributive trade-offs (such as the debate regarding US immigration policy exemplified by Borjas (1999)) that would benefit from formal general equilibrium analysis.

The final section contains econometric investigations of tax structure. The first is micro-econometric, based on state level data attempting to explain why different states differ in their reliance on income tax and the use of special provisions. The second exercise analyses the evolution of the Canadian tax revenue system between 1871 and 1913. This section is probably the weakest part of the book perhaps because the data available require extensive use of

proxies and it is unclear whether one can really test rigorously models of interest. That said, it is certainly worth trying and the authors are admirably up front about what they are doing.

It is difficult to summarise a book as varied as this. It is a significant addition to the literature on the formation of tax policy with many interesting insights although those wishing to get acquainted with the literature should probably start elsewhere.

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Reference

George, J. Borjas (1999) *Heaven's Door: Immigration Policy and the American Economy*, Princeton, NJ: Princeton University Press.

Market Failure, Government Failure, Leadership and Public Policy. By WALLIS (JOE) and DOLLERY (BRIAN). (London and Basingstoke: Macmillan, 1999. Pp. xv+214. £45.00 hardback. ISBN 0 333 73423 8.)

This book addresses the issue of the changing nature and role of the state in advanced economies. It then proceeds to provide a critique of the various theories that have been advanced to justify the existence of state intervention in its various forms. The authors propose a radical approach to public policy based on an economic theory of leadership. Two critical elements of leadership are identified; first, policy entrepreneurs and policy networks, which permit the reform of public sector management. Second, the relationship between leadership and hope whereby the policy-making processes not only adapt quickly to changing relationships but actively drive these changes.

Underpinning the book is an increasing recognition that policy issues are interdisciplinary and that the subject-specific approach adopted by, for example, economists, political scientists, and public administrators has become less and less able to provide a satisfactory analysis of the policy process. The authors provide an interesting critique of a spectrum of thinking and draw heavily on the experience of New Zealand to support their arguments.

The book consists of nine chapters and falls into two distinct parts. The first part, consisting of chapters 2, 3, and 4, covers the theoretical paradigms within which the role of the state is analysed. Chapter 2 covers the area of market failure and concludes that the approach is flawed because it assumes that government intervention can solve problems such as allocative inefficiency or of a lack of equity associated with the market mechanism. The argument is extended in chapter 3 which presents a number of theories of government failure. These are presented as responses to the unease associated with the markets failure justification for government action. However, it is argued that the government failure model does not represent a real alternative to the markets failure model because both depend on the acceptance that the market and the government are alternative mechanisms for solving social and eco-

conomic problems. The key omission from both models is the lack of treatment of social forces such as leadership. Chapter 4 deals with the 'new public management' which is an amalgamation of the new institutional economics and generic managerialism. New Public Management represents the theoretical paradigm which the authors believe offers important insights into explaining the changes experienced within the public sectors of a number of advanced economies. The chapters therefore present a useful overview of a number of important and influential theories that play central roles in theoretical and applied economic analysis.

The second, more substantive, part consists of chapters 5–9 in which public policy paradigms are discussed with particular reference to theory of leadership. In chapter 5, they argue that the theories mentioned above have been unable to explain changes such as privatisation, commercialisation, and liberalisation that have occurred in the provision of public services over the last twenty years. New Zealand's recent reforms are used to illustrate how these problems have been dealt with. It is argued that the significant changes in policy, referred to as 'paradigmatic policy change', and the opportunities for policy leadership provide the framework for explaining the new public sector attitude. Chapter 6 introduces the concept of leadership and argues that economists have been constrained from developing economic theories of leadership because models predominantly use concepts such as rationality. If theories could be proposed that include 'the expressive dimension of human behaviour', this would permit the development of models which could deal with leadership and therefore explain the changes that have taken place within the public sector.

Chapter 7 is an important one in which the authors develop a theory of leadership that concentrates on a key element of leadership, namely hope. It is hope that enables leadership networks to be built up. The network, and therefore a wider commitment to the aims of the leader, will expand as new members are recruited. The network ensures that changes are carried through and that reactionary forces overcome. Chapter 8 deals with the debates surrounding the introduction of paradigmatic policy changes and concludes that an appreciation of the way rival leadership networks operate may result in a greater understanding of the way in which public policy and the public interest interact. Finally, chapter 9 draws together the different strands of the book.

There are a number of comments to be made in relation to the leadership model discussed in the book. First, in terms of the outcomes of the new public policy paradigm, it is still a moot point as to whether or not the changes have actually improved the delivery of government services. For example, cost cutting associated with contracting out and privatisation has not necessarily provided better refuse services or a better rail service. Second, has leadership not existed before? The model does not explain why some leaders are successful in instituting significant change while others are not. Is change the measure of success? Third, it is not clear why the participants in the policy

changes should not be driven by self-interest. If they are, how does the model incorporate this?

True to its interdisciplinary thesis, the book provides an interesting mix of economic and political theory against which a theory of public policy may be constructed. As such it is an interesting and thought-provoking book which makes a valuable contribution to the public policy debate.

CHARLIE WEIR

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The Politics and Economics of Power. Edited by BOWLES (SAMUEL), FRANZINI (MAURIZIO) and PAGANO (UGO). (London and New York: Routledge, 1999. Pp. vi+308. £55.00 hardback. ISBN 0 415 18542 4.)

This edited collection of papers – authored by distinguished economists and political scientists – examines the relationship between politics and economics with particular reference to the analysis of power relations. The editors argue – in my view, correctly – that the analysis of power relations is important for understanding concepts like the ‘contested nature’ of market exchanges. With this in mind, the general thrust of the papers is to offer an economic perspective on political relations. The book is organised in three sections: politics and power in economic organisations; the economic analysis of political organisations; and politics, economics, and social change. Space precludes a discussion of every chapter in the book and so this review focuses on a few that captured my attention. A different reviewer would, no doubt, have chosen differently.

In the first part, I was struck by two chapters. In their chapter, ‘Power in competitive exchange’, Bowles and Gintis argue that even in the competitive equilibrium of post-Walrasian microeconomic theory, a market economy sustains a system of power relations. They do so by relaxing what they regard as one of the most implausible assumptions of the model namely that exchanges between parties can be enforced by the judicial system at no cost to the exchanging parties. In their contribution, Milgrom and Roberts examine the internal politics of the firm and the influence of power relations within the firm upon its economic outcomes. They argue that decision making in firms affects the distribution of rents within a firm and this generates intra-firm political activity to capture such rents. Consequently, outcomes with respect to price and output may be the result of a richer interplay of forces than suggested by the clinical maximising of profits that is assumed to occur under traditional microeconomic theory.

In the second part, Breton in his chapter ‘Modeling politics as a competitive endeavour’ surveys five models of government and four concepts of efficiency and selects a model of government and a concept of efficiency that would be most consistent with a neo-Madisonian theory of democracy. The former is composed of a multiplicity of autonomous and quasi-autonomous centres of power which are capable of checking each other; as regards the latter, the Wicksell–Lindahl conception – which says that efficiency will be greater the

closer the behavioural connection between expenditure and revenue decisions – is recommended. Galeotti in ‘Political parties and democracy’ interprets political parties as a ‘quasi-pledge’ that maintains a degree of consistency between the expectations that citizens and elected representatives hold about each others behaviour. Two types of exchanges characterise the political-economic system: vertical exchanges between citizens and representatives cement and strengthen the democratic relationship; on the other hand, horizontal exchanges between representatives occur whenever voter pressure is perceived as weak. Different combinations of vertical-horizontal exchanges will result in different types of parties: grass-root parties, with a weak organisation, would be the result of an abundance of vertical exchanges, while leader dominated parties, with a strong organisation would follow from horizontal exchanges. In his chapter, Wittman argues that the key to understanding democratic institutional design is to realise that competitive forces in democracies tend to minimise transaction costs: the interesting question is how the system is designed to control agency problems.

In the final part, Wintrobe uses simple tools of economic analysis to understand ethnicity, ethnic conflict, and nationalism and their role in destabilising the Weimar regime. The critical assumption here – which is also the theme of the earlier chapter by Bowles and Gintis – is that property rights, particularly in the political and social sphere, are not costlessly enforceable. Consequently, a cost-effective way of making exchanges is to invest in ‘ethnic capital’ and to use race and blood to determine network membership.

In summary, the chapters in this book coalesce to form a coherent whole. The central theme of power relations and the importance of such relations in understanding market exchanges is pursued in a variety of contexts and through chapters that are, in the main, interesting and informative. To anyone who is interested in a richer view of economics than is provided by the standard diet of the atomistic, optimising economic agent, and welcomes a perspective that places economics in its wider context of a social science, this book will provide an invaluable read.

VANI BOROAH

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Encyclopedia of Political Economy: Volume 1 – A–K: Volume 2 – L–Z. Edited by O’HARA (PHILLIP ANTHONY). (London and New York: Routledge, 1999. Pp. xxxiv+1934. £160.00 hardback. ISBN 0 415 15426 X.)

This two-volume Encyclopedia of Political Economy (EPE) is concerned largely with ideas in economics that lie within the area of political economy. The entries in this encyclopedia are indexed in a continuous A-Z format though, conceptually, its entries may be grouped into three main types: (a) concepts, principles, theories, or problems: for example, path dependency, poverty, inflation; (b) general fields of political economy such as money, credit and

finance, or regional economic integration in the world economy; (c) major figures of political economy – Marx, Veblen, Keynes etc.

Political economy is defined in the forward to the volumes by juxtaposing it with ‘contemporary’ economics. The latter emphasises economic agents acting rationally and individualistically, without reference to society, polity, or history. By contrast, Lavoie and Pressman – the authors of the forward – claim that political economy reaches parts of economic behaviour that remain – and are destined to remain – untouched by contemporary economics. In broad terms, this territory embraces questions of how human behaviour is influenced by society and how individual economic pursuits may lead to sub-optimal outcomes. The editor of the volumes – Phillip O’Hara – in his preface is more specific. He sees political economy as addressing the central issues of the day which, in the 1990s, were *inter alia*: (i) the relationship between economic growth, institutional change, and unemployment; (ii) the link between growth, development, and sustainable development; (iii) the balance of payments constraint and political forces operating in the global economy; and (iv) the distribution of income, wealth, and power on the basis of nation, class, gender, and race. The stated aim of the Encyclopedia is to ‘link these and other issues to concepts, theories, real world processes and policies.’

In order to test the validity of this claim I looked up ‘poverty’ – for no better reasons than that, firstly, it happens to be an area that interests me and that secondly, poverty-related issues are central to political economy. There were two entries under this topic: (a) poverty, absolute, and relative; and (b) poverty, definition, and measurement. Entry (a) contained just one reference – to Mollie Orshansky who developed the US poverty line – and was oblivious to, for example, the (rather animated) absolutist-relativist debate between Amartya Sen and Peter Townsend. Entry (b) ignored measurement issues – Sen’s axiomatic approach, the drawbacks of conventional measures, what is a ‘good’ poverty measure – and instead retraced much of the ground already covered by entry (a). As a check, I looked up ‘poverty’ in the *New Palgrave*. This entry, written in 1987, was much more comprehensive covering both practical and conceptual issues. However, the poverty entry in the EPE also referred me to the ‘feminisation of poverty’. This was altogether much more satisfactory. A tightly written piece, in addition to having the advantage of covering an aspect of poverty neglected by the *New Palgrave*, provided an excellent overview of gender-related issues in poverty.

This led me to muse whether the value-added of this Encyclopedia might not lie in the fact that it covered precisely those minority interest areas which more mainstream Encyclopedias neglected. For example, racism gets an institutionally richer treatment in the EPE than the relatively more academic entry under ‘Race and Economics’ in the *New Palgrave*. Military expenditure in developing countries is discussed in some detail as are: debt crises in the third world; Gandhian Political Economy; gender issues in economics; health and safety in the workplace; Islamic political economy; North-South trade models; slavery; multinational corporations and their role in development. An entry that particularly impressed me was ‘international political economy: major

contemporary themes'. This entry *inter alia* covered issues relating to governance, globalisation, the East Asian miracle. These collectively constitute the life-blood of contemporary economic concerns and it is extremely useful to find within a single book a discussion of the major points that define these issues. I would make a similar observation about the entry on 'work, labour and production: major contemporary themes'.

If this conjecture is correct then therein lies the value of these volumes. An academic treatment of mainstream topics is perhaps better obtained from sources like the *New Palgrave*. But where the Encyclopedia of Political Economy comes into its own is in an institutionally-rich treatment of topics that lie off the highway of conventional economics. To the growing number of persons who are interested in the broader context of economics, these volumes are to be highly recommended.

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The Economics of Regional Trading Arrangements. By POMFRET (RICHARD). (Oxford and New York: Clarendon Press, 1997. Pp. xiv+440 £48.00 hardback. ISBN 0 19 823335 3.)

The Regionalization of the World Economy. Edited by FRANKEL (JEFFREY A.). (Chicago and London: University of Chicago Press, 1997. Pp. ix+285. £34.50 hardback, US \$43.00 hardback. ISBN 0 226 25995 1.)

Market Integration, Regionalism and the Global Economy. Edited by BALDWIN (RICHARD), COHEN (DANIEL), SAPIR (ANDRE) et al. (Cambridge and New York: Cambridge University Press, 1999. Pp. xix+344 £45.00 hardback, US \$74.95 hardback, £16.95 paperback, US \$27.95 paperback. ISBN 0 521 64181 0, 0 521 64589 1.)

There is an apparent paradox between the spread of regionalism and the negative attitude of both economic theory and world trade law towards discriminatory trading arrangements under which up to 60% of world trade currently takes place. Today's regionalism is often qualitatively different from earlier initiatives: deep integration going well beyond trade is increasingly an element; the context – for developing countries – is more outward-looking; and important schemes – like NAFTA – incorporate both advanced and developing countries. The intensified spread of regionalism during the past decade has prompted a flood of studies re-evaluating its implications in that context for both participants and the multilateral system. These books are notable examples.

Pomfret's study is one of the best available surveys of the varied issues that regionalism presents in its specifically trading aspects. A historical survey of discriminatory trading arrangements in the world economy (one-third of the book) is followed by a succinct second part – about 80 pages – that reviews successively: mainstream theory and leading extensions; aspects of the new regionalism involving policy integration; and the recently revisited geographi-

cal issues of location. A still more succinct third section reviews empirical studies – mainly of blocs such as the EU and NAFTA. The concluding fourth part discusses the political economy of regionalism.

Pomfret is centrally concerned by the paradox noted above. But the contrived paradox arises only in the context of a narrow model that excludes many crucial factors, including transactions costs, uncertainty, and – with deep integration – the absence in other spheres of policy of an equivalent to the WTO to provide a commitment mechanism. Pomfret's own initial resolution mainly appeals to terms of trade effects (rather than to Wonnacott wedges), and to internal distributional impacts which lead finally into his illuminating political economy survey in part four. Although his starting point is Cooper and Massell's stance that customs unions can never be justified on economic grounds, he ignores their modification of their initial stance which essentially appeals to a public goods justification. That and other modifications may not affect the presumption that trade discrimination *per se* is inferior to non-discriminatory trade liberalisation in terms of global resource allocation, but it remains to be demonstrated that there is a similar presumption that regionalism cannot be justified on economic grounds – unless beneficial deep integration measures could be pursued independently of trade discrimination underpinnings.

Pomfret's review of mainstream theory and its leading extensions is a model of penetration and clarity. He also provides an excellent brief discussion of certain aspects of deep integration, notably competition policy, foreign investment, and money. The big omission is of fiscal issues where there is a vast literature to which there is hardly any reference. Yet fiscality is central. The benefits of deep integration in fiscal affairs have been estimated to be considerable. Also fiscal arrangements may be crucial to feasibility. Pomfret underlines the point that with preference diversity the real issue concerns the desirable extent of integration. The trade-off amongst alternative economic objectives is also relevant.

Because the theoretical results of discrimination are ambiguous, its actual trade effects are crucial for an evaluation of regionalism. The NBER report edited by Frankel which contains papers originally presented in 1995, focusses on the trade and welfare effects of existing arrangements. An early approach – due to Tinbergen and recently resuscitated – utilises the gravity equation to determine the counterfactual. That relates trade between two countries positively to their size and negatively to transactions costs, taken as a function of distance between them. This book's distinctive feature is that half of its eight substantive chapters focus on the gravity approach, extended in the empirical studies by introducing dummy variables for the presence of RTAs in order to test for the effects of regional arrangements. Although the approach fits the data well, it often prompts unease because of its perceived lack of adequate theoretical foundations. Deardorff's opening chapter will reassure some sceptics through its elegant demonstration that gravity is consistent with a large class of models. The empirical results obtained in the chapters by Frankel and Wei and by Frankel, Stein, and Wei, also lend some credence to the use of the

gravity approach for interpreting the impact of RTAs. However, Eichengreen and Irwin challenge it, arguing that both theory and evidence suggest that it neglects the role of hysteresis. It would be unwise to rely exclusively on the gravity model for evaluating the extent to which the influences of geography rather than regional arrangements determine trading patterns. One alternative approach is presented by Engel and Rogers who utilise observations of deviations from the law of one price to evaluate the effects of RTAs. Other more mainstream methods are well surveyed in Pomfret's book. There are many other challenging contributions in this volume, some already familiar from other sources, but its extended application of gravity analysis constitutes its particular interest.

The chapters in the book edited by Richard Baldwin *et al* are drawn from the final conference of the CEPR's eponymous programme of research that was held in Spain in 1996. Part One contains contributions that analyse regional integration in a global context. Three are central. Winters provides a masterly survey of recent theoretical and empirical literature that seeks to illuminate the question of whether regional trading arrangements are building blocks or stumbling blocks for multilateral liberalisation. The theoretical literature on this second-best issue is predictably inconclusive. Winters emphasises that the evidence he considers is equally ambiguous. Bagwell and Staiger mainly review and consolidate their own well-known work in this vein. They conclude that if WTO rules enable countries to reach their own efficiency frontiers (by completely internalising terms of trade effects), regional agreements have nothing to contribute. If not, or if there are enforcement problems, the efficiency of the multilateral system may be enhanced by RTAs. Helpman's succeeding chapter provides a very accessible survey and synthesis of different approaches to the political economy of trade policy that relates them to each other and also comments on the tariff formulae they point to. Oddly, Winters's brief discussion of such models offers in some respects more inclusive and up-to-date references. Part Two examines issues arising within regional groupings, notably those associated with a common currency, (Bayoumi and Eichengreen), labour migration (Faini), industrial specialisation (Venables), and convergence (Bertola). The two chapters with a strong empirical bias – those on currency and migration – focus on Europe. The book's strong claim to attention rests on the invaluable surveys it provides of empirical and, in particular, of theoretical literature in several key areas. Useful pointers to research strategy and agendas also emerge.

If a common message emerges from these books, it is the equivocal one that RIAs may or may not foster benefits to members or global integration or regional or global convergence, although there are some weak grounds for optimism. The key, according to the oracular summing-up in one, is simply good economic policy based on sound economic analysis. Any more specific policy guide-lines that might facilitate beneficial outcomes are scanty. At the global level, might reform of the WTO treatment of RIAs help? Perhaps the best hope there may be to try to improve the disciplines of Article XXIV of the GATT on coverage and depth of liberalisation and its equivalent for services,

and to seek to enforce these rigorously in the work of the Committee on Regional Trading Agreements.

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The Road to European Monetary Union. By SZÁSZ (ANDRE). (London and Basingstoke: Macmillan, 1999. Pp. xiii+258. £45.00 hardback. ISBN 0 333 74973 1.)

Szász makes it abundantly clear from the outset that European union in general, and European monetary integration in particular, were determined by political, not economic, considerations. 'Political motives dominated European integration from the start' is the opening sentence of his main text, (page 1). Moreover, political relationships between the two main players, France and Germany, are crucial. Thus, 'writing about European monetary integration means writing about French–German relations Both are convinced that good relations between them are crucial for stability in Europe. Both believe that these relations have to be part of a European framework. In order to be acceptable to France, this framework has to contain monetary arrangements, as it is in the monetary domain that Germany has become increasingly powerful since the late 1960s,' (Introduction, page xii).

With Germany having become so strong economically and monetarily, France was forced into the comparatively ignominious position of having to devalue regularly against the Dm, or to adjust domestic policy in line with autonomous Bundesbank monetary decisions. France wanted more 'symmetric' adjustments between the stronger and weaker currencies, and, failing that, since Germany and the Bundesbank refused to compromise on the maintenance of price stability and monetary control, France wanted at least a share in operating the monetary levers, which translated into the pursuit of European monetary integration.

Since France was the 'demandeur', to use Szász' phrase, the momentum towards European monetary integration speeded up whenever Germany wanted something in return. During these years this exchange involved French support, or at least acquiescence, for German policy shifts towards Eastern Europe, for example Brandt's 'Ostpolitik' in 1969, leading to the Hague summit (December 1969) and the Werner Report of 1970 (chapters 3 and 4), and German reunification in 1989 leading on to the Maastricht Treaty (chapters 15 and 16). The other main occasion when Germany wanted support from France was in 1978, when Schmidt felt that the USA under Carter was so unreliable that closer European relationships were essential (chapter 7), which heralded the EMS.

The author maintains, correctly in my view, that EMS/EMU is essentially about Franco/German relationships. The United Kingdom makes discordant noises off, and has several sections and one chapter to its travails. Everyone else is a bit player, with few mentions of Italy and Spain, and none of the

countries such as Austria, Portugal, and Greece. The only Scandinavian country to get a mention is Denmark, and then only because it surprised everyone by voting 'no' in its Maastricht ratification referendum (chapter 18). The Netherlands own main role, according to the author, was to be Germany's main steadfast ally, so that Germany was not so isolated (as by contrast was the United Kingdom); Szász makes it plain that the Nederlandsche Bank acted as the North-West branch of the Bundesbank (chapter 21).

The book is entirely about the politics of monetary integration. As an Executive Director of the Nederlandsche Bank and member of the European Community's Monetary Committee, Szász was a well-placed observer. From my own viewpoint his political analysis is, throughout, correct and astute, and I learnt several new points. In particular, I had believed that the EMS was largely imposed on an unwilling Bundesbank by the political diktat of the Schmidt/Giscard (Bremen) summit. Instead Szász records (chapter 7) that Schmidt had been initially willing to accept a much more, 'symmetrical', French-inspired mechanism, but that the Bundesbank forced him back onto a system that closely resembled the prior 'Snake'; so the actual EMS was much closer to Bundesbank wishes than it might have been.

This reflects one of the Szász's main themes, that European structural monetary decisions have involved a two-tier decision making process (see Section 22.3). The primary initiative comes from the Heads of State (of Germany and France). They initiate and set the direction, but carefully refrain from entering into specifics. Indeed 'Heads of State or Governments were sometimes only vaguely aware of the implications of their intentions and, once these became clearer, were not really willing or able to accept them, ...', (page 221). So then it becomes the turn of the second tier, of monetary experts, especially Central Bank Governors and senior officials in Ministries of Finance and Central Banks.

The political appreciation and insights in this book are first-class; by contrast the economics are simply non-existent, despite Szász being an economist by training. There is no mention whatsoever of such concepts as optimal currency areas, asymmetric shocks, Phillips curves, or NAIRU. There is considerable discussion of the fiscal criteria for EMU, (chapter 17), since these formed part of the political scene, but there was, for example, no mention of the concept of a 'cyclically-adjusted' deficit. There was no discussion of the role that might need to be played by labour market flexibility in a single currency area, despite the recognised fact, (page 140), that failure in this respect had soured German reunification.

Presumably Szász might respond that, first, he was not trying to write an economics book and, second, that the influence of economics in general, and academic economy theory in particular, on the road to EMU has been minimal. Perhaps, but it all leaves the impression, as indeed does the author, that the foundations of EMU are somewhat precarious. Start with the paradox that a supranational mechanism has been established on the basis of essentially national horse-trading. Go on with the dilemma that 'Germany and France agree that EMU has to be part of a wider process of European integration, but

they do not agree either on its substance or form', (page 227). Continue with the comment that many governments 'are committed to what is a major change affecting all citizens without real backing from a large part of the public.' Moreover quite how the adjustment mechanism will work, in the face of asymmetric shocks, remains to be seen. The next decade will continue to be an exciting period for monetary economics, even if political considerations remain the main driving force.

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Living with the European Union: The Northern Ireland Experience. Edited by KENNEDY (DENNIS). (London and Basingstoke: Macmillan, 1999. Pp. x+207. £45.00 hardback. ISBN 0 333 75380 1.)

This collection of nine essays considers the impact of European Union membership on the political, economic, and social life of the province – or as is emphasised – the region of Northern Ireland. The approach is broadly interdisciplinary, with specialist essays on economic, regional, and environmental policies as well as on public opinion and the province's political divisions.

In the introduction Kennedy suggests that EU membership has, in the last twenty-five years, made very little difference outside the realms of agriculture and, to a decreasing extent, external trade. In examining this hypothesis from an economic perspective, Gudgin argues that Northern Ireland has consistently failed either to attract inward investment from other European Member States, or to utilise EU structural funds to the fullest. The stark contrast with circumstances in the Republic of Ireland is duly noted.

Christiansen is more positive in his assessment of the impact of the EU on Northern Ireland as a region. Drawing on a comprehensive survey of the regionalisation of Europe, he concludes that regions have been forced to compete with one another for the gains of economic integration. While Northern Ireland may not always have been on the winning side, the process has, nevertheless given a new and welcome impetus to the province's regional authorities.

Membership of the EU has, Kennedy argues, had a rather mixed effect on political divisions within the province. By challenging the very concept of national identity, European integration has changed the approach of many parties in Northern Ireland to the contentious issue of nationalism. The European Union has, however, had very little bearing on political negotiations. In one sense, such influence is outside the scope of the treaties. In another, neither the British nor the Irish governments, on one hand, nor their Continental peers, on the other, ever sought to make Northern Ireland's political problems a matter for Europe.

Why then has the EU benefited some regions but not Northern Ireland? Over the course of the nine essays three main answers are considered. First,

decisions regarding the EU have generally been taken in London for the United Kingdom as a whole. In consequence, the specific needs of the province have often been watered down with those of Scotland, Wales, and England. Second, the UK's rather troublesome relationship with the revenue side of the EU budget has contributed to the under-utilisation of its share of the expenditure side. Thirdly, in an excellent essay on public opinion, Smith notes that European Integration, means different things to different sides of the Community. Unionist concerns about the implications of deeper integration for their own autonomy have, in certain cases, prevented a widespread support for the EU and its policies.

As a retrospective analysis of Northern Ireland's experiences in the EU, this volume largely succeeds in its objectives, and indeed its interdisciplinary approach must be commended. Given current regime changes in the province, however, retrospection may prove an unreliable indicator of future trends. Scant attention is paid to the potential role for Northern Ireland's new political institutions at the European level. No mention is made of the economic implications of the island of Ireland being both inside and outside the euro-zone, while the effect of political stability on the economy's capacity to attract inward investment is largely ignored. Since such issues will occupy Northern Ireland's future, the shelf-life of this volume may be shorter than its author intended.

DERMOT HODSON

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European Monetary Integration: 1958–2002. By APEL (EMMANUEL). (London and New York: Routledge, 1998. Pp. xiii+222 £15.99 paperback. ISBN 0 415 11432 2, 0 415 11433 0.)

A Concise History of European Monetary Integration: From EPU to EMU. By UNGERER (HORST). (New York: Quorum Books, 1997. Pp. xii+338. £55.50 hardback. ISBN 0 89930 981 X.)

Much of the economic debate in the 1990s has been focused on the process of integration within the EU. Did this process progress successfully? For instance, was the implementation of the EMU, with its Maastricht convergence criteria, which were primarily concerned only with monetary convergence, especially with regard to the prime goal of achieving a low and stable level of inflation, really what Europe needed? What about the level of economic growth and the battle against European mass unemployment? Ought not the treaty about EMU to specify convergence criteria concerning these matters? Perhaps one is right in assessing that the people of Europe politically see an economic unification as the ultimate goal of the European process of integration but this does not mean that one should be careless about how the institutional set up is to be constructed.

However, to understand the development of the process of European integration correctly, one has to see it in a broader perspective and not just focus on the

economic aspects. Integration is a very time-consuming process, which involves economic, political, and historical elements. Any evaluation, therefore, has to take all three of these into account. This is exactly what both Horst Ungerer and Emmanuel Apel are trying to do in their books. Ungerer with a clear explicit historical dimension in his precise and very well written book about the long period of transformation from a European Payments' Union in 1950 to the establishment of the Economic and Monetary Union from 1 January 1999. It is an illuminating story that he tells with great personal excitement in 24 brief chapters. Apel on the other hand gives a more traditional textbook-like presentation, comprising an introduction and five chapters, with the main emphasis on the Maastricht treaty and the making of the EMU. With these two rather different approaches they both succeed fairly well.

As a more traditional textbook, addressed to undergraduates, Apel's presentation is, of course, more explicitly and directly linked to economic theory although virtually without any use of formalism, whereas Ungerer more implicitly makes use of a distinct analytic economic reasoning in most of his chapters (e.g chapter 21 where the economic benefits and costs of the EMU are discussed). At the same time it seems as if Apel has written his book with a more critical view towards how the European monetary integration took place than seems to be the case with Ungerer. As an example of this, one reads in the preface of his book, briefly discussing the very crucial role of France and Germany in determining the actual development of the process of integration, that 'the simultaneous pursuit of a monetary union ... is not necessarily "optimal" and is sometimes viewed as sheer economic folly, driven more by political arguments than by clear and convincing economic arguments'.

By reading either one of these two books we are constantly reminded of this fact. Since the European Coal and Steel Union was established in 1952, it has always been a characteristic of how the European Community actually worked. The road towards a perfect economic union has not been without various economic, as well as perhaps more importantly political, problems and obstacles. At times, the process of integration in Europe has even been set back deliberately because of a fundamental disagreement among the leaders of the member states, though only temporarily, of course, as history has shown us. From the very beginning of this process, a French–German co-operation, as Ungerer so rightfully points out, was the most crucial element in achieving a successful European integration. And that is of course exactly why 'the partnership between France and Germany has set the pace of European integration and determined, to a large degree, its achievements as well as its failures', (page 35).

Today the Economic and Monetary Union is a reality. It is, perhaps, questionable whether the Union is going to be prosperous enough in making all of its objectives come through politically as well as economically. Looking at the historical evidence concerning international economic co-operation, especially, with regard to achieving and maintaining stable exchange rates in the 20th century starting with the regime of the Gold Standard and onwards, perhaps the lesson history has told us has been a rather pessimistic one.

Namely what Ungerer calls the basic challenge is at the very best a difficult, if not an impossible, one to meet successfully. Is it at all possible in the longer run to fulfil the wishes of the politicians in making a regime of stable and even ultimately irrevocably fixed exchange rates with an institutional set up such as that of the EMU, where important aspects of economic policy – especially fiscal policy – will still be governed under the sovereignty of individual countries? Especially, if one bears in mind that the Union in question probably does not, to a satisfactory extent, fulfil the criteria that are necessary to be defined as an optimal currency area. Criteria that naturally would be even harder to meet successfully in the case of a further enlarged EMU.

Whether true or not, the Economic and Monetary Union will most certainly gain further importance in the years to come. In setting the political agenda, the way in which political decisions are made and implemented will determine the content of these decisions. Such an experiment will also inevitably be influencing the way economists and others think about how to pursue and obtain, in the most prudent manner, a macroeconomic situation with internal as well as external equilibrium within the Union's regions and its member countries. As a guide to this, books like the ones of Ungerer and Apel would come in handy in sharpening the eyes of the observer (and the evaluator) of the European process of integration. One might actually learn from history.

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Monetary Policy and Inflation in Spain. Edited by MALO DE MOLINA (JOSE LUIS), VINALS (JOSE) and GUTIERREZ (FERNANDO). (London and Basingstoke: Macmillan, 1998. Pp. xviii+601. £75.00 hardback. ISBN 0 333 71788 0.)

Both the environment and the conduct of Spanish monetary policy have undergone substantial changes over the last 25 years, with the opening up and liberalisation of what had been (financially, in particular) a relatively closed economy and the evolution of monetary strategy from monetary targeting through exchange rate pegging to direct inflation targeting (and now, of course, to EMU). This weighty volume (which seems to have been put to bed in mid-1996) starts with an editorial introduction by Malo de Molina and a useful background paper on monetary policy and inflation by Viñals. It contains material of three different kinds: papers where outsiders discuss general issues in which the Spanish dimension is limited, papers where the monetary policy strategies of the Banco de España are presented and justified, and papers that deal in much more detail with aspects of Spanish monetary policy and the environment within which it operates.

In the first category Alvaro Almeida and Charles Goodhart examine the effect of inflation targeting on the behaviour of the central banks that operate this strategy, covering the way monetary policy is carried out, the forecasting and controllability of inflation, and the credibility of the inflation targets.

Using data up to early 1996 they find little effects of inflation targeting in the countries that adopted it (Australia, Canada, Finland, New Zealand, Spain, Sweden, and the United Kingdom) except for a substantial increase in openness and communication by the central bank. With the benefit of hindsight (and the 1997 changes in the United Kingdom), the reader might wish that they had said more about central bank independence, but in general their paper is careful, comprehensive, and judicious, a model for evaluations of monetary policy regime changes.

Matthew Canzoneri and Behzad Diba provide a lucid introduction to work on price determination which focuses on the intertemporal government budget constraint, and use it to provide a novel and interesting justification for the Maastricht Treaty (and Stability Pact) budget deficit limit of 3% of GDP. On this analysis some limit of that kind is essential to ensure that primary surpluses tend to rise whenever government debt grows too quickly. In such a 'monetary-dominant' regime conventional views on price determination hold, whereas in a 'fiscal-dominant' regime where primary surpluses do not respond in this way to government debt the price level is determined by the needs of fiscal solvency: it rises to bring the real value of the stock of debt into line with the present value of future surpluses.

Trends in Spanish monetary policy are presented in papers by Juan Ayuso and José Luis Escrivá, and by Gutiérrez. The former details the evolution of policy by stages, from the development and implementation of monetary targeting (1973–83) through the increasing role of the exchange rate (1984–9) to exchange rate pegging within the ERM from mid-1989 and the crises of 1992–3. The latter discusses the move to inflation targeting after the legal changes of 1994 which conferred a large measure of independence and a mandate for price stability on the Banco. These two papers are usefully supplemented by the contribution of Juan Luis Vega on the long run demand function for ALP (liquid assets held by the private sector, a broader aggregate which replaced M3 as the target aggregate in 1984). ALP had become increasingly unstable and difficult to target in the early 1990s, though it proved possible to rescue the long run function by including foreign interest rates. However, the evidence of past instabilities, the dependence of the function on variables outside the central bank's control, and the assumed likelihood of further instability in the future all contributed – together with the change in the Banco's status and mandate – to the decision to replace the ALP target with a direct inflation target (but to retain a reference value for ALP as a privileged leading indicator of inflation).

The book also contains another ten papers which focus on more detailed aspects of the Spanish monetary environment and strategy. Five papers cover aspects of the forecasting of inflation, from direct measures and indicators through monetary and credit aggregates and the yield curve to a BVAR forecasting model. One paper discusses the 'instrumentation' of monetary policy (reserve requirements, open market operations, etc). And four examine aspects of the monetary transmission mechanism, including the operation of the banking system, interest rate effects on consumption and investment, the

nature and impact of the financial position of different sectors, and an overall structural model. While the details of these chapters may have a more limited appeal, they mostly contain general introductions which are often (e.g. in the cases of the BVAR model, the instrumentation chapter and the banking system chapter) very useful.

Overall this is an excellent volume for those who wish to inform themselves about Spanish monetary policy (pre-EMU), and a showcase for the Banco de Espana's Research Department, which comes across as intelligent, up to date, and creative. But it also contains a considerable amount of more widely relevant material, and can be strongly recommended for library purchase.

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The Current State of Macroeconomics: Leading Thinkers in Conversation. By IBANEZ (CARLOS USABIAGA). (London and Basingstoke: Macmillan, 1999. Pp. x+372. £60.00 hardback. ISBN 0 333 72532 8.)

Conversations with Leading Economists: Interpreting Modern Macroeconomics. By SNOWDON (BRIAN) and VANE (HOWARD R.). (Aldershot and Lyme, NH: Edward Elgar, 1999. Pp. xi+370 £65.00 hardback. ISBN 1 85898 942 6.)

For simplicity these two volumes will be respectively called here 'the Spanish book' and the 'English book'. They publish interviews with, in total, thirty economists about the current state of macroeconomics, respectively eighteen and fourteen with only two appearing in both books (Alesina and Lucas). On this ground the books are complementary. The selections differ partly because of age and location of the interviewees, more significantly because of the nature of their contributions to macroeconomics. The fact reveals, however, that the position of leader is contested in the discipline.

The Spanish author interviewed mostly economists who entered the profession between 1965 and 1985 (14); only three were younger (Alesina, Marcet, Quah) and one older (Eisner). This may explain why just one Nobel prize winner was selected, whereas the English book has four more (Friedman, Modigliani, Solow, Tobin). With Blaug and Clower as well, the latter book has more seniors than middle-aged (Blanchard, Colander, Lucas, Prescott, Taylor) or juniors (Alesina, Mankiw, P. Romer). The English authors have a definite transatlantic preference since all their interviews but one were with people working in the United States (Blaug being selected because of his 'extensive knowledge of the history of economic thought and interest in methodology'). But balance is restored thanks to the Spanish book in which economists working in the United Kingdom have a substantial representation (Bean, Chick, Goodhart, Nickell, Pissarides, Quah, Snower). The rest of the world has to be satisfied with Cukierman, (Israel), Mancet (Spain) and Wyplosz (Switzerland now, France earlier).

The English book has a definite bias in favour of theory oriented towards

modelling and in favour of methodology, empirical macroeconomics being neglected when it is not associated with dominant theoretical views (readers might dispute this last statement as applying to the interviews with Blanchard, Friedman, Mankiw, Modigliani, Solow, Taylor, and even Tobin). In contrast, pure theorists have relatively little room in the Spanish book (Azariadis, Lucas), unless we add economists who were associated with new classical macroeconomics but with a more empirical inclination than the others (Chistiano, Eichenbaum, Marcet, Sargent, but not Prescott). Concerns with empirical knowledge and policy analysis is otherwise dominant (Alesina, Bean, Cukierman, Eisner, Goodhart, Gordon, Nickell, Pissarides, Snower, Wyplosz). The methodological insights of Victoria Chick echoes, however, those of Blaug, Clower, and Colander in the English book.

What should readers expect to learn from these two books? The answer is to be found in the interview with Mark Blaug: 'If the only economics you ever read is interviews with economists then it is not the way to learn about the subject. It is however a terrific way of sparking interest in reading more and also thinking about the personality of the economists concerned' (page 316 in the English book). The full text of the answer makes it clear that 'reading more' in the second sentence means reading 'the articles that the economists talk about', not reading more interviews. Also, 'the more you know about economics the more fascinating such conversations become'. So, the books are not to be recommended to undergraduates, who are already too much exposed to the personalisation of approaches to the study of macroeconomic phenomena. This being said, the books are quite good because the authors carefully prepared the questions they were going to pose.

Since their book is addressed to those who are already familiar with macroeconomics, we may wonder why Snowdon and Vane publish ninety pages of their own on 'Interpreting modern macroeconomics: from Tobin to Romer' (Tobin was the first to be interviewed, in February 1993, and Romer the last in January 1998). They write in the preface: 'In order to help place the interviews in context, in the opening chapter we provide a *brief* overview of the major developments which have taken place in modern macroeconomics since the Great Depression'. This reviewer doubts whether many users of the book will benefit from the overview, which, moreover, is not well balanced.

There is a lot to learn in these two books about the personalities and beliefs of the interviewed economists. Take for instance Robert Lucas in the English book (the interview in the Spanish book has only 5 pages, as against 25 for Christiano or Quah). Interviewed at the age of sixty, Lucas denies having created a separate school of thought (page 152). He rather modestly admits: 'My influence has been very much . . . inside the profession and for that matter on a technical subset of the profession' (page 164). 'People have gotten tired of [the Lucas critique] and I think that is fair enough'. He answers 'No' to 'Is it critical for macroeconomic models to have neoclassical choice theoretic microfoundations?' (page 159) and yes to 'Do you think that . . . rigidities have a considerable real impact in the economy?' (page 181 in the Spanish book). He admits that his paper with Sargent in 1978 contained rhetorical statements,

but explains that, being in the Boston enemy camp, they wanted strongly to state their difference (page 155). He associated himself with Friedman and Tobin in thinking that growth is explained by the supply side and fluctuations by monetary shocks (page 156). He, however, seems to stand firm on the position that it makes no sense to discuss a theoretical idea without a precise model.

Such a moderate vision of the contributions brought by classical macroeconomics differs from the one conveyed by many teachers of economics all around the world. Even from 'leading thinkers' we can read answers such as the following: 'Is it possible today to differentiate between micro and macroeconomics? No. And that's a good thing. That was the whole plan and it succeeded' (Eichenbaum, page 130 of the Spanish book). Christiano is more fortunate in his answer to the same question: 'To me, the word macroeconomics refers to a set of questions. For example: Why . . . business fluctuations? What should be done about them? This is what differentiates macroeconomics from microeconomics' (page 91). However, he goes on: 'Now, the distinction in conceptual frameworks (between macro and microeconomics) has largely disappeared, in favour of the microeconomic tradition'. Is the framework offered by this tradition best appropriate for the study of macroeconomic issues? That is the question. This reviewer would have much more to add to the exchange, starting with the positions taken on the same issue by other interviewees.

On this particular question we realise that books of conversations may be used for a third purpose, besides knowing the personality of some economists or becoming interested in reading more. It may be a source for finding out what the profession in its diversity thinks, and how it views the current state of its discipline or the challenges facing it. I am sure these two books will be used in the future for that purpose. But then a detailed and conveniently organised subject index will be wanted, because interesting statements arrive during a conversation and not always where they are expected. In this respect the English book is deficient: its index covers hardly more than one page. The index of the Spanish book, which covers 21 pages for both authors and subjects, is more useful but it is organised in a strange and inconvenient way.

The Spanish index may reveal how narrow and scholastic macroeconomics has become during the last decades in some quarters and how major difficulties of the discipline tend to be ignored. For instance the index contains many references to rational expectations, real business cycles or new Keynesianism, but few to theories which could not be linked to such dominant categories. The index has one reference for adjustment costs, no entry for irreversibility or persistence, but three references to multiple equilibria. Many references are given to money, monetarism, and monetary policy but just two to credit. No entry appears for firm, enterprise, corporation, or profit, which might well reveal the fact that such concepts are progressively evading macroeconomic thinking. In a book that gives so much attention to the micro-macro distinction, the importance and difficulty of realistic aggregations are mentioned,

incidentally, in just one interview (Snower, pages 262–3, 265); the word aggregation is ignored in the index.

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A Critical Essay on Modern Macroeconomic Theory. By HAHN (FRANK) and SOLOW (ROBERT). (Oxford and Cambridge, MA: Blackwell, 1998. Pp. viii+158. £45.00 hardback. ISBN 0 631 13483 2, 0 631 20989 1.)

Macroeconomics is a hard subject. One of the reasons why it is so hard stems from the tension between two objectives: the need to offer policy guidance about economic aggregates (unemployment, inflation, growth, etc), and the desire to provide theoretical underpinnings in support of the policy recommendations. Given the prevailing reductionist orthodoxy that demands micro foundations for macroeconomics combined with the feasibility of explicit aggregation for only the simplest of micro-theories, the construction of macro theories is fraught with difficulties. A common approach is to acknowledge the difficulties, then to propose some fairly simple hypotheses about individual behaviour, thus allowing predictions about the relationships among economic aggregates to be obtained (often with tenuous standards of rigour – see, for example, Kirman, 1992). If the predictions accord, approximately at least, with empirical experience, they can then be invoked as the basis for policy pronouncements.

Hahn and Solow (HS) take issue not with the approach *per se* but with a particular set of hypotheses, namely that associated with the new classical macroeconomics. Not for them a methodology that is prepared to rely on arguably implausible assumptions so long as tests of the predictions find empirical support. Rather, HS develop the implications of what seem to them more realistic hypotheses about the behaviour of households and firms. HS begin their assault (chapter 2) from within, retaining the cornerstone new classical assumptions of perfect competition, and price and wage flexibility. Here an overlapping generations model together with a ‘Clower constraint’ (to ensure a positive demand for money) form the basis for macro dynamics. Although, by assumption, markets clear at each instant, HS demonstrate that the evolution of this economy is such that a case can be made for interventionist monetary and fiscal policy to stabilise potentially pathological dynamics.

In pursuing their attack, HS aim more directly at the new classical assumptions by allowing for sluggish wage adjustments (chapter 3), by introducing imperfect competition and increasing returns to scale (chapter 4), and by exploring in greater depth wage-setting models that are compatible with persistent unemployment (chapter 5). Chapter 6 weaves together ideas introduced in the previous chapters by setting out a macro model that allows multiple equilibria, a positive relationship between employment and the real wage rate, employment and output fluctuations, and, once again, scope for stabilising policy interventions.

Chapter 7 concludes with the authors' reflections on macroeconomics largely, though not entirely, informed by the analysis of earlier chapters. Here the reader is treated to a commentary that ranges widely over the problems of macro modelling and the opportunities for advances in the subject. Their emphasis on the possibility of several equilibrium levels of unemployment – a hobbyhorse, they admit – is, in a sense, a call for modesty in macroeconomic theory: there is a limit to how much any model can explain without a knowledge of the economy's immediate history, its initial conditions. That HS end with remarks on economic policy comes as no surprise; neither does their sympathetic stance towards active government intervention.

At every turn in this short book HS are at pains to remind the reader that their goal is one of criticism, to discomfort the adherents of contemporary macroeconomic wisdom. Models are constructed as devices to undermine new classicism not to replace it and the authors frequently issue cautions to the effect that they are not (necessarily) advocating that any of the models they study should be regarded as providing the way forward in macroeconomics. As they point out early on: 'It is all a matter of choosing interesting and plausible micro foundations. There is plenty of room for maneuver.' Many of their 'interesting and plausible micro foundations' are Keynesian in flavour, though they would surely eschew infantile Keynesianism (that macroeconomic theories should be based on the divination of what Keynes really thought or meant). Prototypical models of the sort HS present ably serve their avowed nihilistic purpose. More constructively, their model-building exercises can be interpreted as an extended argument for the sorts of models of which they approve. The authors are careful not to commit themselves and could claim – with a measure of justice – that their purpose does not require this. Even so, it is disappointing that two such eminent scholars decline to take a more definite stand about precisely which model(s) they would propose to displace new classicism.

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Kirman, A. P. (1992) 'Whom or What does the Representative Individual Represent?' *Journal of Economic Perspectives* vol. 6, pp. 117–136.

Political Economy of Money and Finance. By ITOH (MAKOTO) and LAPAVITSAS (COSTAS). (London and Basingstoke: Macmillan, 1998. Pp. xviii+301. £55.00 hardback, £18.99 paperback. ISBN 0 333 66521 X, 0 333 66522 8.)

This is an important book coming from the pen of one of the most eminent Marxist economists in Japan, Makoto Itoh (with Costas Lapavitsas) dealing with a much ignored issue of money and finance from a Marxist perspective. It is also a timely book in the wake of the Asian, Latin American, and Russian

financial crisis of the last few years (although regrettably the book does not discuss the latter). It is so rich in detail and analysis that a short review cannot do it justice. It should be of interest to academics interested in the history of economic thought, financial economics, and Marxist economics. It may be used as a useful supplementary textbook in teaching any of the above areas.

As I have demonstrated elsewhere (Shamsavari 1991, chap. 10) the circuit of money capital for Marx was the most significant of all the circuits of industrial capital as it reveals the essence of the capitalist system, i.e. money that makes more money. In another work I have discussed the significance of money and finance in Marx's theory of capitalist development (Shamsavari, 1986). The question as to why it has taken such a long time for Marxist economists to deal with the issue is beyond the confines of this review. Let us hope that the publication of this book opens the way for a better understanding of the role of finance in capitalist as well as socialist development. The book not only reviews the theories of money and finance from classical economists through Marx to Keynes, it also addresses in detail institutional issues such as the emergence of joint-stock companies and central banking. Furthermore, it discusses the post World War II problems of world economy. I find the discussion particularly illuminating when it comes to the rise and fall of Bretton-Woods system. There were a number of factors in this period that led to high rates of growth of world output and even higher rates of export growth. Thus world economy was growing faster than individual economies. These factors include low commodity prices, technological change and abundant supply of labour power. It is not surprising that Keynesian policies worked very well in this era.

Although the book does not discuss recent global financial crises it anticipates them in its theoretical development (see page 202, where the authors argue in favour of a world central bank, an idea that can be traced to Keynes's vision for what became to be the IMF in the Bretton-Woods Conference of 1944). The problem of hoarding money leading to the Keynesian liquidity trap can be traced to Marx's view of the role of monetary exchange in creating economic crisis: the seller is under no obligation to buy unlike in barter where the acts of buying and selling are simultaneous. This important point, however, is not made explicitly in the book. This is unfortunate as I believe it is the cornerstone of Marx's monetary theory, which can be developed to explain the nature of financial crises under capitalism.

I wish to offer two main criticisms of this otherwise excellent work: (1) It does not deal with financial globalisation and the pressure of financial liberalisation on developing countries. It also bypasses the important issue of the role of informal and formal finance in the development of these countries. (2) The most disappointing part of the book is chapter 11: Money and Credit in a Socialist Economy. I believe the authors, although open to the possibility of the existence of money and credit in a socialist economy, are too much influenced by the Marxist tradition that envisages a socialist economy, particularly in its higher stage of development (communism), without value relations, i.e. commodity production, money and exchange-value. Although Marx him-

self encouraged this view, it is clear that he was wrong. It is impossible to abolish capitalist social forms, such as value as long as the production of goods and services continue to be organised on an independent/individual basis. 'The free association of producers' envisaged by Marx is based on meeting basic needs (such as food and shelter) and that is why it works well in war-time economies. Although I do not advocate socialist 'consumerism', it is clear that consumer needs have become more diverse and sophisticated with the rise of per capita incomes in capitalist countries. A socialist economy will only undermine itself if it does not adequately address this issue which is inseparable from value relations.

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The General Theory of Transformational Growth: Keynes after Sraffa. By NELL (EDWARD J.). (Cambridge and New York: Cambridge University Press, 1998. Pp. xxviii+784. £90.00 hardback, US \$135.00 hardback. ISBN 0 521 59006 X.)

Someone who should have known better once declared that 'There is no such thing as society; there are only individuals'. Ed Nell takes issue with this, demonstrating that to understand the processes behind economic growth, innovation, and enterprise requires an analysis of institutional and societal factors. It is thus rather ironic that Mrs Thatcher, the source of the 'no such thing as society' claim, has since endowed a Chair in Enterprise Studies when such studies clearly demonstrate the importance of society itself for fostering and sustaining enterprise.

In this impressive volume Nell has set himself the task of explaining the sources of economic growth. His starting point is to analyse the nature of economic growth itself. This demonstrates two things. Firstly, economic growth has changed drastically over time, both in rate and nature. Secondly, economic growth is inextricably linked to structural change in the economy and to innovation. Economic growth is clearly *not* a linear or equilibrium process, and to try to model it as such is doomed to failure, or at least to being irrelevant. (The caveat is important, since despite its irrelevance, the failure of growth theory has not been generally acknowledged).

To make his point, that to analyse growth we should start from an analysis of the sort of continual economic transformations which constitute the process of growth, Nell refers to 'transformational growth'.

Once it is accepted that innovation and structural change play key roles, the dangers of modelling growth as an equilibrium process, and of imagining that

the market simply allocates resources, should be clear. Nell argues that equilibrium may be a useful analytical tool if taken in moderation, but that it hardly represents the force behind innovation and creative destruction. Equilibrium theory fails to explain the behaviour of business and the actual working of markets. A more fruitful course, Nell argues, is to abandon the view that markets allocate resources through optimising and market-clearing adjustments in favour of seeing markets as forcing development through a competitive struggle that creates incentives to innovate.

Nell looks at the very different sorts of economy that have existed over the past hundred years or so, and the very different ways in which pricing, output decisions, innovation, and growth have operated. He contrasts 20th Century mass production economies with the previous craft production economies. These economies operated quite differently. So any attempt to present a general theory of economic growth – that might be able to be of use in analysing the economy of the future, as well as of the past and present – needs to be relevant to these different types of economies.

Measured against these requirements, mainstream theory fails. However, Nell is most definitely not arguing against the use of theory, in favour of some sort of descriptive institutionalism. On the contrary, he argues that we need to develop better theory. He presents this book as an attempt to contribute to this process, and in this it succeeds admirably. Anyone who wants to undertake serious academic work on issues of economic growth should certainly consult this book. It will also prove an extremely useful text for postgraduate and doctoral students. It not only discusses the theory and practice of economic growth, it also includes detailed and useful discussions of the proper use of theory itself, and of research and research methods, including for example the best combination of case study and statistical work in developing and testing theoretical propositions.

Nell starts from the classical economists and move on to an analysis of how Keynes's contributions can be best incorporated and how the resulting theory can be best developed. In doing so he discusses the contributions of others, including an analysis of neo-Ricardian and post-Keynesian economics. He also comments on the contributions from the new growth theory and the New Keynesian economics. On how markets actually work in practice, he describes the importance of innovation in which firms play an active role rather than being simply price takers, an analysis which is certainly confirmed by studying the actual behaviour of innovative firms which includes co-operation as well as competition (Kitson and Michie, 2000). On the non-linear nature of growth, he describes in detail the patterns of wages, prices, and profits over the business cycle, and how these patterns have altered over time. On the role of innovation he contrasts the early writings of Schumpeter on the role of entrepreneurs with the later writings on the importance of large firms with R&D labs, citing Malerba and Orsenigo's paper on this. (Sadly this paper is omitted from the book's bibliography; for the source see below).

This is an important and useful book that should certainly be consulted by anyone with an interest in entrepreneurship, innovation, and economic growth.

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The Economics of Increasing Returns. Edited by HEAL (GEOFFREY). (Aldershot and Lyme, NH: Edward Elgar, 1999. Pp. xxvii+598. £140.00 hardback. ISBN 1 85898 160 3.)

This volume in the series 'The International Library of Critical Writings in Economics', is an essential reference source for researchers, containing a selection of most important and pioneering articles written by the most outstanding experts in the field. The notion of increasing returns has had a long but uneasy presence in economic analysis. Since Adam Smith increasing returns have been emphasised to explain both specialisation and economic growth, but the two phenomena he grouped together, that is, the gains from specialisation and the efficiency of the invisible hand, are inconsistent. Indeed, a competitive system and a cost-of-production theory of value cannot be made rigorous except by assuming constant returns. Economists then followed the competitive assumptions and quietly dropped Smith's statement that the division of labour is limited by the extent of the market, since the division of labour leads to specialisation and, consequently, greater productivity. This is a remarkably modern issue, stressing the conflict between technology efficiency, coming from scale and from the novel and far-reaching concept of externalities, and economic and organisational efficiency, coming from competition and information transmission.

A key obstacle for economics in dealing with increasing returns has been the indeterminacy introduced by the possibility of multiple equilibria. Another obstacle is the fact that with increasing returns we cannot rely on the market mechanism, as a competitive market may lack equilibrium. Recognising increasing returns affects the possibility of market equilibrium, causes economies to lock-in to inefficient technologies, produces historical dependence and asymmetry, can generate hard problems for regulators, planning policies, and international trade.

The papers in this collection largely deal with allocation problems under increasing returns. Some of them take a history-dependent, dynamic approach (Parts II and IV): the papers by Arthur (chapter 25) and David (chapter 23) are an important part of the recent movement toward using positive feedback mechanisms to explain the evolution of economic systems. There are also other approaches: the imperfect-competition, static approach, which is prominent in international trade theory, pioneered by Krugman (chapter 33) and others (Part VI), and in the study of product differentiation, pioneered by Dixit, Stiglitz, and Spence (Part III); the deterministic-dynamic approach of

Romer (chapter 32) and others (Part V), who have explored endogenous growth powered by increasing returns mechanisms.

The papers in Part I contain basic results about resource allocation and economic efficiency under increasing returns. Part I, A follows a non-market approach. Heal (chapter 2) proposes a dual to the market mechanism, with a central agency that sends out quantity signals to non-price takers firms and receives back marginal value products, acting as shadow prices. Such a non-market mechanism leads to an efficient allocation of resources, although at quite a high cost in terms of centralisation of information. Cremer (chapter 6) describes a decentralised planning procedure which converges to a global optimum, whether or not the production possibility sets of the firms are convex, and shows a relevant point: good performance with increasing returns requires the exchange of more information than in a competitive market.

The papers in Part I, B deal with general equilibrium; they all constitute fundamental contributions in the literature. Guesnerie (chapter 8) and Brown and Heal (chapter 9) show that the usual formulation of the doctrine of 'marginal cost pricing' for achieving Pareto optimal states in a non-convex decentralised economy has an unsatisfactory logical basis. Actually, an economy may have many marginal cost pricing equilibria, all of which are Pareto inefficient. Even worse, Beato and Mas-Colell (chapter 10) show that there may be non-convex economies where all marginal cost pricing equilibria are not only Pareto inefficient, but also production inefficient, and therefore are inefficient in the aggregate. A way out in order to reach efficiency with increasing returns has been formalised by Edlin, Epelbaum, and Heller (chapter 13): price discrimination rules out inefficient equilibria of the type illustrated above, although it requires more information about individual preferences. The intuition that an efficient equilibrium can be supported by some form of price discrimination is clearly captured by the seminal contributions by Dixit and Stiglitz (chapter 20) and Spence (chapter 22), which focus on the optimal degree of product variety in the context of fixed costs and imperfect competition.

One outstanding feature of the literature on increasing returns is its dynamic nature. Learning-by-doing and learning-by-using play an essential role in competing technologies as opposed to static examples of returns to scale. At the macro level, increasing returns may have destabilising effects, giving rise to patterns of cumulative causation, persistence of disequilibrium, economies stuck at inflation or unemployment, which are dealt with in Part II.

Certainly, it is a benefit to economists to have all these path-breaking papers from widely scattered sources brought together conveniently. Such papers represent the progress of research, which already looks impressive. The volume will be an important stimulus to further research as well.

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Foundations of Complex-system Theories: In Economics, Evolutionary Biology, and Statistical Physics. By AUYANG (SUNNY Y.). (Cambridge and New York: Cambridge University Press, 1998. Pp. xii+404. £50.00 hardback, US \$64.95 hardback. ISBN 0 521 62167 4.)

Over the recent years the field of complex systems theory has mushroomed. There has been an explosion of research activity within the general area of non-linear sciences, including chaos theory, interacting particle systems, cellular automata theory, simulated annealing learning models, and stochastic processes. Order, disorder, self-organisation, synergetics are now notions which constitute parts of the knowledge which is increasingly being transferred from one discipline to another – from physics, chemistry, computer science, mathematics, to biology, psychology, and economics.

This book provides a non-technical introduction to the way we understand complexity and compares key notions and general methods of complexity in statistical physics, evolutionary biology, and economics. It begins with a description of what constitutes a complex system. Complexity is a notion used to describe ‘self-organised systems that have many components . . ., exhibit many structures in various scales, undergo many processes in various rates, and have the capabilities to change abruptly and adapt to external environments’ (page 13). The subject matters of economics, evolutionary biology, and statistical physics are all complex systems made up of many interacting constituents: there are ‘national economies made up of millions of consumers and producers bargaining and trading; evolving species comprising billions of organisms competing for resources; solids constituted by septillions of electrons and ions attracting and repelling each other’ (page 3). The main concern of the book is to understand how scientific theories do handle large-scale composition, in which a system and its constituents are entities of different scale and are characterised in diverse forms. Indeed, composition includes structures and is not merely aggregation. Variety and diversity characterise the structures of large and composite systems. Variety explodes, as the number of possible combinations of building blocks increases exponentially with the number of blocks; moreover, the relations among the constituents are the major source of complexity in many-body systems and thus of the difficulty in understanding them. As a consequence, it is argued that the deductive method suitable for small systems does not go far: the book shows that as the size of the system increases, the analysis of individual constituents quickly becomes impractical and uninteresting, and does not suffice to describe the characters of the system as a whole. Put in another way, microreductionism and methodological individualism are no longer the correct approaches for the study of complex systems.

Actually, the book becomes of great interest to philosophers engaged in scientific methodology and the approach which is proposed here is the ‘synthetic microanalytic’ one, emphasising the analysis of wholes instead of combination of parts. In this approach, ‘a synthetic framework is posited in which microanalysis is directed so that the constituents are acknowledged as

parts of a whole and their relations grasped as the structure of the composite system. We delineate a composite system, raise questions in macroconcepts that capture its salient features concisely, microanalyse it into constituents, and reach down to seek the constituent behaviours and mechanisms that answer system questions' (page 57).

The book provides abundant examples of the interaction between micro-explanations and macroexplanations for the understanding of many-body systems. Unfortunately, most of these examples, being presented in a non-analytical way, remain a little superficial. Also the link between the three different disciplines would require more deepening, in order to be able to transform a few insights into rigorous modelling and prospective applications.

The book examines a range of important concepts like 'situated individuals', composite systems and collective phenomena in physics, biology, and economics. Because of the complexity of large scale organisation, we are usually unable to predict emergent characters on the basis of the information of their constituents. Such 'emergence' has long been recognised in condensed matter physics, where ordered systems such as crystals or ferromagnets display collective behaviour that cannot be understood in terms of individual atoms considered separately. In economic systems it is important to evaluate which structure emerges from individual choices and decentralised decision-making in 'network' contexts, and how they operate in propagating the influence of historical events. The idea of 'emergence' is investigated by a discussion of the following three mathematical theories that find extensive application in the above-mentioned sciences: deterministic dynamics, stochastic processes and the ergodic theory connecting the two, and hence offering the appropriate context to analyse randomness and complexity.

In short, the book seems to capture the unique fascination of an interdisciplinary approach. Closer acquaintance, however, dispels this first impression. It contains too sweeping a survey from the point of view of the area it embraces, including very diverse topics, which are naturally less sophisticated than the scholars would expect. It succeeds in conveying to us, if only vaguely, something of the interdisciplinary approach, although its ambitious goal proves not to be feasible within the compass of a single book.

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Positive Feedback Economies. By AGLIARDI (ELETTRA). (London and Basingstoke: Macmillan, 1998. Pp. ix+154. £45.00 hardback. ISBN 0 333 62128 X.)

This book is claimed by its author to be a theoretical study of the economic system as a complex dynamic process of the self-reinforcing type, that is, processes with local positive feedbacks, which are characterised by a multiplicity of asymptotic states or possible equilibrium outcomes. This framework, usually nonlinear in form involves path-dependence or history-dependence in

the sense that interactions among economic agents and their mode of learning about the environment, which determines the multiple equilibrium outcomes are themselves determined by the particular path followed in the economy.

Self-reinforcement concepts have featured in different areas of economics under different names, such as increasing returns, cumulative causation, and dynamic economies of scale. For example, Kaldor regarded cumulative causation as important in explaining the different time paths of development in different countries. More recently, the endogenous growth theorists have stressed very strongly the dynamic economies of scale that arise from learning, and the process of innovation and the creation of knowledge that generates cumulative causation. This causation sometimes involves irreversibilities in economic activity and the possibility that small changes in such activity may result in large changes in the original trajectory of the overall economy.

The book consists of six parts. The first two chapters provide a mathematical description of complex economic dynamics and their essential features such as the different self-reinforcing mechanisms, random economies with many interacting agents, bifurcations and catastrophic behaviour and the role of path dependence. The next two chapters analyse in some detail the various externalities and sources of discontinuity in information networks for dynamic economic systems. The last two chapters discuss the role of random events and shocks in the technology and innovation process: its creation, competition, externalities, and evolution, where there may persist various sources of instability and chaos.

The book makes a significant contribution to our understanding of the nonlinear dynamic phenomena in modern economic theory that arise from the self-reinforcing and adaptive mechanisms in dynamic economics leading to chaotic phenomena and stochastic instability. The contribution has been significant in two areas of mathematical economics in particular. One is the dynamic externality effect by which the agents have to choose the equilibrium adoption path, which is characterised by intrinsic uncertainty. This aspect is all the more important for the modern technology-intensive industries and the internet framework. The second is the long-time behaviour of the markets, especially the innovation and knowledge market which is modelled here by a nonlinear Markov process with the possibility of switching from one state to another. The equilibrium specification in such markets is significantly constrained by several stochastic forces which may disturb the process of convergence to steady states.

Two brief comments about the book's contributions are in order. One is that it stays away from the host of empirical applications of some of the basic concepts of nonlinear economic dynamics such as chaos, co-integration processes, and asymmetry in random behaviour discussed in modern economic literature. Second, dynamic evolutionary games and the various generalisations of the evolutionary stable strategies under uncertain environment could be well integrated in the mathematical framework of the book. One may hope that the author will extend the contribution along these new lines in near future.

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Value, Distribution and Capital: Essays in Honour of Pierangelo Garegnani.
Edited by MONGIOVI (GARY) and PETRI (FABIO). (London and New York: Routledge, 1999. Pp. xi+364. £70.00 hardback. ISBN 0 415 14277 6.)

This volume contains a collection of essays that were presented to Pierangelo Garegnani on the occasion of his 65th birthday. As one of the editors, Gary Mongiovi, points out in his introduction, the sixteen contributions collected in this book cover quite well Garegnani's main fields of interest: the Sraffa-based critique of neoclassical theory, the reconstruction of the classical approach to economic theory and its relation to the marginalist approach, and the further elaboration of the surplus approach. As befits a *Festschrift*, the book also carries a full bibliography of Pierangelo Garegnani's writings. His list of publications, while not excessively long, includes a number of highly influential papers (often not excessively short), and his contributions can certainly be expected to have a lasting impact on the development of economic theory.

The book opens with three essays in which the authors pursue, from different angles, a common theme, namely to assess the meaning and significance of temporary and intertemporal general equilibria. Fabio Petri's reply to Hahn's 1982 article is an attempt to overcome the grave difficulties of communication which have marred the debate on capital theory by formulating the criticisms in a way that makes them easier to grasp for neoclassically-trained economists. Roberto Ciccone investigates the intended empirical content of temporary and intertemporal general equilibrium prices, and John Eatwell and Murray Milgate argue that the original meaning of competition has been corrupted in neoclassical theory, thus making it impossible to conceive of an intertemporal equilibrium as a centre of gravitation. Significantly, Paul A. Samuelson in his rather idiosyncratic defence of neoclassical capital theory does not invoke temporary or intertemporal general equilibrium theory, but rather argues in terms of comparisons of long-period positions, which he interprets as steady states.

A large set of papers is devoted to the reconstruction of the classical approach and its submergence in the wake of the 'marginalist revolution'. Tony Aspromourgos and Peter Groenewegen explore the notion of the subsistence wage in pre-Smithian writers, Fernando Vianello offers some clarifying observations on Adam Smith's distinction between gross and net revenue, and Antonella Stirati re-addresses the contentious issue of the existence of wage fund reasoning in Ricardo's *Principles*. Alessandro Roncaglia explores the connections between utilitarianism and marginal utility theory, Bertram Schefold reflects on the usefulness of the concept of use value, and Heinz D. Kurz reconstructs the role of the classical theory of rent in the development of marginal productivity theory, focusing on the works of von Thünen and Hermann.

Contributions to the elaboration of the surplus approach come from Neri Salvadori, who shows that in fixed capital models with transferable machines with constant efficiency paths the complications of general joint production

systems can be avoided, and from Ian Steedman, who argues that the 'reduction to dated quantities of labour approach' is of wider applicability in its vertically-integrated form. Sergio Cesaratto stresses the continuity between the 'new' and the 'old' neoclassical growth theory. Picking out increasing returns and induced labour-augmenting inventions as the two main forces counteracting falling marginal productivity of capital in neoclassical growth models, he shows that both routes were already explored in the 1960s, long before the emergence of the so-called 'new' growth models, by authors such as Arrow, Frankel, and Phelps. Massimo Pivetti discusses the plausibility of employing the European Monetary Union as a disciplinary instrument for checking inflation and the government debt.

Two interesting papers on the monetary determination of income distribution come from Edward J. Nell and Carlo Panico. Nell addresses Garegnani's argument that the Cambridge equation entails a logical inconsistency, because the *actual* rate of accumulation cannot possibly determine the *normal* rate of profits. According to Nell, it is the normal growth of effective demand, rather than the accumulation rate, that should make an appearance in the Cambridge equation. On the other hand, he argues that the normal rate of profits cannot be taken to be determined by the money rate(s) of interest, because the latter is too volatile and unstable. Carlo Panico on the contrary argues that the two closures, which are generally considered alternatives, that is, the determination of the profit rate by the rate of accumulation or by the monetary interest rate, can be reconciled in a model with an unbalanced government budget, in which both the rate of accumulation and the nominal rate of interest on government bonds are taken as given.

This *Festschrift* volume is a fitting tribute to an impressive and determined scholar, a thorough and rigorous economic theorist with a profound knowledge of the history of economic analysis. Pierangelo Garegnani must surely have been delighted to be presented with this fine collection of essays. It is equally sure, however, that there is one thing that would have pleased him even more: if he had been given the opportunity to comment on some of those essays.

CHRISTIAN GEHRKE

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The Microdynamics of Technological Change. By ANTONELLI (CRISTIANO). (London and New York: Routledge, 1999. Pp. xvi+286. £60.00 hardback. ISBN 0 415 19052 5.)

The claim for this book is that it provides an original framework within which one can comprehend the structural change wrought by the advent in recent years of knowledge-based economies (KBES) and the economic effects of the emerging information and communication technologies. This framework is based on three bodies of knowledge: (1) the economics of path dependence and of historical time; (2) economic topology based on the methodology of

network analysis; and (3) the new economics of knowledge and the concepts of localised technological change and technological communication.

In an eloquent foreword J. S. Metcalfe embraces the view that the accumulation of intangible, intelligence-related assets is the key to the distribution of economic activity and the standard of living in these renaissance economies. He deplores the 'largely fragmented and partial' treatment of this new world by economists and other social scientists. Antonelli seeks to redress this neglect and move towards 'a more comprehensive understanding of modern capitalism and its intangible foundations'.

Antonelli has been a prolific presenter of conference papers and author of journal articles. Our immediate gain is that much widely scattered material is now synthesised and put between two covers.

Part I (The theory) deals with the three bodies of knowledge listed above and adds chapters on (a) localised technological change and Schumpeterian growth regimes and (b) economic topology. Part II (Applications) is a series of investigations into the telecommunications and business services sectors that have assumed great importance in KBEs.

As befits writing in the Marshallian and Schumpeterian tradition, there is a heavy emphasis on the historical dimension. It is therefore a little surprising that this approach does not carry over to the treatment of the history of ideas. Fritz Machlup, the pioneer of the study of KBEs, rates only one index entry and that for a view on intellectual property rights rather than for his successful 1962 encapsulation of the key characteristics of the KBE. Burton Klein does not get a guernsey. 'Arrovian' economics of knowledge is castigated, despite the superb sentence in *The Limits of Organization*:

'The theme to be presented is that the combination of uncertainty, indivisibility and capital intensity associated with information channels and their use imply (a) that the actual structure and behaviour of an organisation may depend heavily upon random events, in other words on history, and (b) the very pursuit of efficiency may lead to rigidity and unresponsiveness to further change' (page 49).

While information is undoubtedly more excludable than Arrow allowed, even in his seminal 1962 paper, so much loved by advocates of intellectual property rights and information as a public good, Arrow did include a lengthy catalogue of qualifications that fit nicely into the disequilibria at the heart of Antonelli's writing.

The discussion of economic topology may well prove the most interesting part of this book. This is directed to 'the quality of connectivity among agents, their receptivity to external information, their density in multidimensional spaces, and the extent of external pressures' (page 4). These agents remain rather mysterious entities. Whether they be individuals or firms, it will likely be found necessary to probe much further into their thoughts or within their boundaries than this borrowed methodology of spatial stochastic interactions seems to contemplate. Microeconomics has always been reluctant to get involved with matters of internal organisation; but 'the state of readiness' of

the decision-maker or firm would seem directly relevant to both receptivity and connectivity.

This has a bearing on the conclusions reached about the role of new information and communication technologies. Antonelli argues that these technologies intensify 'the connectivity and receptivity of firms perceived as learning agents' (page 5), 'fuelling the growth of a market for knowledge-intensive business services' (page 177). It remains unclear whether such intensification is a recipe for success or may merely quicken the march to organisational obsolescence implicit in Arrow's reasoning.

But a good book opens doors and we should be grateful to Antonelli for a stimulating contribution that has far-reaching implications for economic theory and policy and for the distorted images of the economy provided by official statistics.

DON LAMBERTON

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The Economics of Knowledge Production: Funding and the Structure of University Research. By GEUNA (ALDO). (Aldershot and Lyme, NH: Edward Elgar, 1999. Pp. xix+205. £49.95 hardback. ISBN 1 84064 028 6.)

In modern societies, universities are institutions which teach at various levels, producing graduates with first degrees or higher degrees, the latter being either coursework-based (most masters level degrees) or research based (the PhD and equivalents). Universities also engage in research. On the one hand, this gives rise to a whole range of forms of research 'output' such as research papers, books, conference presentations, and the like; on the other, it links universities into a network of other institutions concerned with research – from private sector companies, through government departments and the research councils (in the UK, at least), to international institutions such as the European Commission.

Surprisingly, economists have paid relatively little attention to the economics of universities and even less, within that broader theme, to the economics of university research. Yet in recent decades many developed countries have witnessed a huge expansion in their university systems as governments have sought to encourage higher participation in higher education, and this expansion has been accompanied by increasing reluctance by the public sector to provide full funding on the same scale as in the past. In some countries, such as the UK, one consequence has been the introduction of new modes of student finance. But everywhere, the increasing financial pressure faced by institutions has also had an impact on the funding of research. From the standpoint of a professional economist there are two types of question that might then be posed of the university system. One type is essentially *positive*, simply asking how universities are likely to behave in the environment in which they operate – how much research they will do, what sorts of research, in what ways different institutions might specialise, etc. The second type of question is

more *normative*, asking what is the most desirable organisation of research from a social point of view, and what this would imply for the most appropriate structure of university system.

In this context, the present book is an immensely valuable addition to the literature, focusing mostly on the more positive aspects of the above issues. Geuna's book is organised as follows. After a short introduction, the subsequent eight chapters fall into four parts. Part I, on theory and history, includes a thought provoking chapter on the economics of university research behaviour and then one giving an evolutionary account of European universities. Part II uses the framework established in Part I to explore issues to do with the allocation of funds and university research. It does so through one chapter on European universities and another on British universities in which research assessment exercises and the mix of research funding through funding councils and the research councils are studied. Part III moves to the multi-national level by investigating EU funding of university research. This has occurred through many different EU programmes, but the book wisely focuses on specific examples to illustrate its argument. Thus chapter 6 examines university participation in Community framework programmes and chapter 7 looks at EU and national university research funding through the example of the BRITE-EURAM programme. Chapter 8, the only chapter of Part IV, draws key conclusions from earlier chapters.

The book focuses on EU universities in the early 1990s. Its overall aim (page 6) is 'to investigate the unintended consequences of the changes in the rationale for resource allocation to universities'. By this, it refers to the tightening financial situation facing EU universities, the spread of performance indicators, and the increasingly competitive approach to allocating resources for research. The point is that while there are clear rationales for all these new features of our university systems, they have all sorts of side effects that were not anticipated at the start – these are the unintended consequences. Naturally, they may or may not be desirable in terms of any given normative conception of the university system.

The conceptual framework of the book, sketched in chapter 2, is reluctant to adopt a utility maximising model of the university, but adopts an industrial-economics perspective taking account of the regulatory framework and market conditions, together with relevant incentives and constraints. Exploring the effects of an increasingly competitive allocation of funding for research, four types of unintended consequence are highlighted in the book: increased concentration of resources; disproportionate incentives for short-term, foreseeable research; conflicting incentive structures; and exacerbation of cumulative and self-reinforcing phenomena. The net effect is an increasing polarisation of university systems in EU countries – with a few dynamic, research-oriented institutions, and many others, mainly teaching-oriented. Reductions in government research funding have already pushed many institutions towards an increasing dependence on industrial/consultancy income – often with clear reductions in research publications, and a focus on knowledge

that does not lay a foundation for future advances. Effectively, universities end up subsidising short term industrial goals.

In order to design a good system of funding research, therefore, the book concludes (page 173) that there is a need for balance between competitive allocation (good for efficiency), and non-competitive allocation (to support long-term societal objectives) of research funding. Reflecting the limited research undertaken to date, the book also recommends further research in two areas: (a) study of the operation of the university as an economic and social institution; and (b) study of the modes of collaboration between universities and industry in order to learn about social returns, and relevant trade offs, and so on.

Overall, this book was a delight to read. It both enlightens the reader and raises lots of interesting questions suggesting further research around the main themes. It should be read both by academics like myself, 'inside the system', and by policy-makers, and officials who influence the functioning of universities without themselves being insiders. As usual, better policy towards the universities is likely to arise from a better understanding of how the system – specifically in regard to research – functions, and this book makes an excellent start in that direction.

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Knowledge, Institutions and Evolution in Economics. By LOASBY (BRIAN J.). (London and New York: Routledge, 1999. Pp. xv+168. £50.00 hardback. ISBN 0 415 20537 9.)

This short book, based on Brian Loasby's 1996 lectures to the Graz Schumpeter Society represents a clear and handy summary of the thinking of one of the most important and sophisticated critics of mainstream economics. It is not too far off the mark to say that, in many ways, Loasby is the contemporary heir to George Shackle's critique of economic doctrines. Although Loasby's thinking is distinctive and the Shacklian influence is only one among many, there is a shared insistence on beginning with an understanding of human activities that goes significantly beyond the optimisation paradigm, and, therefore, a shared scepticism towards a mainstream economics (or, what Loasby calls 'North-American economics') that has little or no room for processes.

The familiar charge against Shackle was that of 'nihilism': if taken seriously, Shackle's stress on imagination, novelty, and the kaleidic nature of human interaction would mean a farewell to most of economics. Loasby, too, stresses these features of decision-making and interaction, but whereas there may have been some truth to the nihilism charge in the case of Shackle, this charge certainly cannot be directed against Loasby's thinking. Indeed, much of his work may be described as an attempt to identify the *constructive*, but deeply unconventional, implications of a starting point that is at least partly Shacklian in the stress placed on creativity and the aggregate consequences of changing

knowledge. In Loasby's view, such a starting point provides ample room for an understanding of processes – some of which are described as being evolutionary and all of which involve changing knowledge – and institutions, which aid coordination, not just because they embody incentives but also (and perhaps even more) because they structure human cognition. To use his own phrase, it allows us to develop and organise knowledge about how agents develop and organise knowledge, which is '... the fundamental question facing anyone who wishes to understand economic systems' (page 8).

The present book may be read as one sustained attempt to identify and describe these implications. Apart from that, it is hard to precisely characterise the book. It is not economic theory, at least in the contemporary understanding of that term. But neither is it economic methodology or doctrinal history. It is a blend of all of this, and at the same a sort of ongoing dialogue with Loasby's heroes and main sources of inspiration, namely Adam Smith, Alfred Marshall, Friedrich Hayek, Ronald Coase, Edith Penrose, and George Richardson. The book appropriately begins with a chapter on 'the problem of knowledge', which identifies six main obstacles to complete knowledge, namely the Humean problem of the insufficiency of induction, complexity, the limits of human cognition, exogenous change, the interdependence of individual initiatives, and conflicting ideas and purposes. This provides a direct link to both evolutionary processes (chapter 2) and institutions (chapter 3), which represent both sources of, and constraints on, changing knowledge. The focus is then narrowed somewhat, as the overall knowledge-based and cognitive perspective is applied in succeeding chapters to the notion of capabilities, issues in transaction cost economics, the nature of the firm and of markets, before the discussion in the final chapter (8) returns to a more overall level, connecting the growth of knowledge with the division of labour.

Loasby's mode of discourse is very much centered on the discovery and teasing out of multiple analogies; he is taken up with the discovery of connecting principles and ideas. Sometimes these analogies are not sufficiently substantiated and it is not always clear what comes out of them; Loasby often seems content simply with noting analogies, leaving the elaboration to the reader. An example may be the association of Penrose's theory of the firm with Austrian capital theory (page 92). Because such analogies are left undeveloped, the reader is easily left wondering what is actually added by making the analogy. However, the present book is a relatively brief statement, and undeveloped analogies and suggestions are, therefore, not only to be expected, but should be taken as invitations to develop them further. Those who wish to see how Loasbian themes have inspired other writers may also consult the volumes recently published in honour of Brian Loasby (Dow and Earl, 1999*a*, *b*). In sum, I highly recommend this book as a compact statement of the thought of a very original and creative thinker.

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Investment Intelligence from Insider Trading. By SEYHUN (H. NEJAT). (Cambridge, Mass. and London: MIT Press, 1999. Pp. xxxvii+402. £23.95 hardback. ISBN 0 262 19411 2.)

This book provides an excellent, highly readable, and useful analysis of the informational content available to an outsider wishing to follow the share-picking strategies of an insider. The term *insider trading* is referred to by Seyhun as the legal share transactions of the officers, directors, and large shareholders of a firm. Many investors believe that corporate insiders, informed about their firms' prospects, buy and sell their own firm's shares at favourable times, reaping significant profits. Given the extra costs and risks of an active trading strategy, the key question Seyhun attempts to answer is whether publicly available insider trading information can help investors outperform a simple passive index fund. Seyhun bases his findings on a data set of over one million transactions, capturing information on all reported insider trading in all publicly held US firms over a twenty-one year period spanning 1975–95.

Seyhun shows how investors can use insider information to their advantage, providing compelling evidence from numerous articles, many of which are published in respected finance journals. He documents the magnitude and duration of the share price movements following insider trading, determinants of insiders' profits, and the risks associated with imitating insider trading.

Additionally, Seyhun provides an interesting chapter on the stock market crash of October 1987, where he cites various hypotheses for the crash, and examines insider trading around the crash. Seyhun also devotes a couple of chapters to insider trading in firms which are subsequently involved in take-over, either as targets or bidders. He reports that it is generally quite difficult to use insider-trading information to outperform other market participants around corporate takeovers.

The author also considers the likely performance of individual firms and of the overall stock market, and compares the value of what one can learn from insider trading with commonly used measures of value such as price-earnings ratio, book-to-market ratio, and dividend yield.

The final chapter of the book is devoted to the question of whether it is possible for investors to mimic insiders and make profits in practice, the magnitude of the profits, and whether the risk-reward profile is attractive. In his final analysis, Seyhun concludes by noting that investors can potentially generate appropriate profits after the reporting of insider trades, despite the given delays in reporting and publication of insiders' information, transaction costs, and some risks associated with imitating a small number of transactions.

Nevertheless, he adds the caveat that outside investors need to limit the size of the bets they make, diversify their bets across a large number of mimicking transactions, and monitor their performance.

This book has a helpful format, with chapters being well structured, often including useful graphs and tables, and each chapter includes a 'conclusions and investment implications' section. Further, the extensive use of footnotes provides detail for the interested reader, whilst maintaining the thread within the main body of the book. For researchers interested in insider trading, Seyhun provides a comprehensive list of up to date references, which back up many of his findings.

In summary, this is an exceptionally well written book, which is accessible to both the general reader who has an interest in investing, and also to academics engaged in, or wanting to pursue research in insider trading. The layout of the book is extremely clear, with the chapters being structured in a well thought-out manner, making it very readable. Seyhun should be congratulated on producing such a well-written and readable book on the subject of insider trading. His book should be of interest and value to both investors and researchers.

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Economic Games and Strategic Behaviour: Theory and Application. By STAHLER (FRANK). (Aldershot and Lyme, NH: Edward Elgar, 1998. Pp. xii+259. £55.00 hardback. ISBN 1 85898 905 1.)

This book is concerned with the general problem of two agents who are to play an infinitely-repeated game and first bargain over which equilibrium they should play. The point of view adopted is that they must agree on a self-enforcing contract, where 'self-enforcing' is interpreted as 'weakly renegotiation-proof' as defined by Farrell and Maskin. The contract which they choose is arrived at by a process of Rubinstein alternating-offers bargaining. Whereas most of the literature on renegotiation-proof equilibria of repeated games is concerned with the case of very patient players, this book is concerned mainly with analysing how the solution varies as the discount factors vary.

There are three classes of stage game considered, each of which has continuous strategy spaces and a unique Nash equilibrium. In the first of these, each player chooses an effort level; the benefit each player gets is linear in the sum of efforts and the cost is quadratic in own effort. The second is the same as above but with money transfers and quasi-linear utility in money. The third is a buyer-seller game in which the seller chooses how much to produce and the buyer simultaneously chooses how much to pay. There is also some discussion of applications to duopoly, an international environmental policy game, and a trade policy game.

The essence of the problem is that, as the discount factors change, the Rubinstein bargaining solution for a given utility possibility set changes but the

set of weakly renegotiation-proof equilibria (i.e. the utility possibility set) changes too. The main qualitative results of the analysis are that the two parties may, for some discount factors, negotiate a Pareto-inefficient equilibrium and that, even if one party has all the bargaining power, by virtue of being very patient, he or she will not necessarily hold the other player to the reservation payoff. The reason, in both cases, is that each player has to have a certain minimum payoff in equilibrium in order to have no incentive to break the contract.

The problem studied here is in principle interesting but the execution is fairly unsatisfactory. The author says at the outset that 'results will not be given in the form of propositions and proofs. Balancing rigidity and readability, the book will bias presentation in favour of readability and economic understanding.' Unfortunately, however, most of the book is very heavy going and substantial parts of it are in my opinion almost unreadable. There is a standard way of presenting game theory and this book, which departs from it, shows very clearly how essential it is. It involves precise definitions of assumptions, of equilibrium concepts, of the strategies involved in a particular equilibrium, etc., as well as precise and clear statements of results. This book is an object lesson in how the lack of these elementary disciplines can become extremely tiresome. Part of the problem is the turgid writing style, which may be due to poor translation from the German.

Furthermore, the results are in some respects dubious. For example, all of the discussion in the book concerns one particular class of equilibria: those in which, after a deviation, the deviator plays, for one or more periods, the same action as he would take in the 'normal' phase while the other player plays his best response to this. But there are presumably many other possible ways of punishing the deviator while preserving the weakly renegotiation-proof property. Why are they ruled out? There is no discussion of this, nor any attempt to characterise the set of weakly renegotiation-proof payoffs. For a second example, the author claims that strategic bargaining rules out the possibility of a non-stationary equilibrium even though a stationary equilibrium may be inefficient if the two players' discount factors differ. The reason is given as follows. 'After the first period's policy has been realised, however, the situation is the same as before the first period (i.e. before the bargaining phase). If the situation is the same as before, why should agent i now keep his/her promises which were made in the first bargaining procedure?' In other words, if the continuation equilibrium did not reflect the relative bargaining strengths, there would be more bargaining, resulting in a shift in payoff from the weaker to the stronger bargainer. This is unconvincing. The situation is not the same as before the first period because an agreement to play a particular infinite-horizon equilibrium has been struck since then. The assumption implicitly made in the book is that if the agreement is self-enforcing then each believes the other will stick to it. Agent i therefore should keep his/her promises for the simple reason that to do so is an optimal response.

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Unit Roots Cointegration and Structural Change. By MADDALA (G. S.) and KIM (IN-MOO). (Cambridge and New York: Cambridge University Press, 1999. Pp. xviii+505. £42.50 hardback, £15.95 paperback. ISBN 0 521 58257 1, 0 521 58782 4.)

One of the major advances in econometrics during the past fifteen years is the development of an appropriate statistical theory that enables one to analyse non-stationary time series processes empirically. Non-stationarity is a feature which by now is considered a predominant empirical regularity of most economic time series and hence a proper framework for analysis is naturally called for. This monograph provides a very comprehensive and useful review of contributions to the voluminous literature characterising this area, and hence it may be useful for researchers and graduate students who would like a quick guide to references in the field. The book is partitioned into four main parts each containing a number of sub-chapters. Part I introduces some basic concepts in time series econometrics which become useful in the subsequent presentation. Part II reviews topics in testing for unit roots and with focus on estimation and inference in cointegrated systems whilst part III presents numerous extensions to and special cases of the basic models outlined in part II. Finally, part IV addresses models with structural change both as a likely alternative to unit root processes, but also as separate classes of models such as switching regime models and structural time series models.

The basic material introduced in part I includes standard stochastic process theory and concepts in Box-Jenkins (ARIMA) time series modelling. Also the fundamental definitions of integration and cointegration and some of the implied properties are given. Part II starts by discussing more thoroughly unit root processes and their limiting behaviour and in so doing presents the necessary theory for Wiener processes and the functional central limit theorem. However, although the listing of limiting results is useful, the presentation given is not very formal. Although the required results for deriving e.g. the Dickey-Fuller and other unit-root distributions are provided, the material covered and the overall analysis is not sufficiently rigorous for students to use the book as a text of reference for deriving their own results. Even though it is naturally of interest to have some idea of the asymptotics related to unit root processes, limiting distributions are only very sparsely presented in the rest of the book and when it is actually done there is no clear pattern in which results are being presented. In addition to the Dickey-Fuller class of tests and their semi-parametric counterparts, an overwhelming list of other parametric and semi-parametric unit root tests are presented including tests where stationarity is taken as the null. Many of the practical problems implied by undertaking unit root tests are carefully described as well. However, one might wonder why such a variety of tests is presented, given that only a very few of them are in actual use and several of them are known to have rather bad properties. To quote the authors: 'We discuss several [...] unit root tests – many of which we do not recommend, but they are all discussed for the sake of completeness and also because they are often used' (page 145). It would have been much

more constructive to undertake a comparative presentation of the most common tests and those where some optimality criteria are known to be (almost) satisfied. The authors are correct that no uniformly most powerful test for the unit root hypothesis exists, but point optimal tests are available, (see Elliott, Rothenberg, and Stock, *Econometrica*, 1996), and the power functions of existing tests could be naturally compared to the power envelope suggested in the Elliott et al. paper. Actually, Maddala and Kim do discuss separate Monte Carlo results available in the literature for the various tests and they also suggest which tests to prefer in practice, but given the fact that so many tests are presented a more comprehensive comparative treatment would have been desirable.

A section is devoted to describing unit roots in panel data. At the time the book was written rather few results were available but indeed this is an area where a lot of new papers and results are presently being developed and in this sense the inclusion in the monograph indicates the authors foresightfulness although their list of references is already slightly outdated. Also extensions of univariate models in a number of other directions are given in part III and include topics such as the Bayesian approach to unit roots testing, fractional unit roots, bootstrapping, $I(2)$ series, and seasonality. These are all interesting and relevant extensions and there is now an increasing number of applications where these generalisations are addressed.

The review on cointegration is also given in part II with appropriate extensions in part III. Many of my comments on univariate models equally apply to the presentation of multivariate models and cointegration. It is my belief that too many estimation and testing approaches are presented, given that only a few are in actual use and others like the Engle-Granger 2-step procedure, say, appears to be inappropriate for practical applications. However, for pedagogical reasons and to present some intuition, the EG procedure may still be worth presenting. The finite sample properties of the various procedures are compared by reference to Monte Carlo papers one-by-one rather than trying to collect these results in a more unifying way. The survey given is rather broad; surprisingly a few important references seem to be missing. For instance, in discussing the Fully-modified OLS procedure of Phillips and Hansen (1990, *Review of Economic Studies*) the equivalent procedure of Park (1994, *Econometrica*) is left out although it is probably easier to implement in practice.

The Johansen approach to estimating cointegrated systems seems dominant in the applied literature and hence is given a very detailed description. An important problem in implementing this procedure concerns the identification of the single cointegrating relations. As in the present text, this problem is often exaggerated given that in fact identification of the long run and the short run structure can be checked separately in a way similar to the suggestions of the Cowles foundation structural approach. Hence, the identification problem is really simpler than is frequently believed. One thing that really seems to be missing from the discussion of the Johansen VAR procedure is a proper description of the meaning of deterministic components. The authors

rightly argue that the problem is much like the problem of whether to include or exclude a trend, say, in a Dickey-Fuller regression. Notwithstanding, in a system of equations a complete characterisation of the property that a constant, for instance, can act as a constant in certain directions and as a trend in other directions, would have been useful. Also, the VAR model could have been used as a convenient framework for highlighting the relationship between cointegrating relations and the common stochastic trends driving a multivariable system. These quantities are intimately related and helps our understanding of the dynamics of cointegrated systems; this important link seems less well explained at a rigorous level.

Generally, cointegration methods have been shown to be rather sensitive to pretesting for unit roots as well as the invalid imposition of exact unit roots, c.f. Elliott (1999, *Econometrica*). This is clearly a practical problem as stressed by the authors of the monograph, however, unfortunately there seems to be very few attempts to react to this criticism in applied work.

The final part, part IV, addresses structural change in univariate series as well as in economic relations. Whilst the literature is clearly dominated by contributions focussing on the discrimination between unit root processes and processes with a known or an unknown trend or mean break there are rather few results on the implications of breaks in multivariate models. An adequate account of the implications of breaks for multivariate time series modelling would have been desirable, but perhaps this is merely reflecting the state of both the theoretical and the empirical literature. A chapter focusses on different types of outlier in univariate time series. Outliers may take many different forms with rather different implications. For instance, innovation outliers have the property that it may become hard to discriminate between stationary models with shifts and stochastic trend models. On the other hand, additive outliers produce models with contaminated errors acting as measurement errors which will affect the size of unit root tests. Hence the latter class of outliers merely deals with the general robustness of unit root tests rather than with structural change issues. The last topic covered in the monograph concerns Markov switching models, structural time series models and time-varying parameter models. Some of these models can be handled in state space form and can be estimated by the Kalman Filter; hence these sub-topics are explained. It is nice with a text covering these different topics; still, it is less clear how this relates to the rest of the book. Structural time series models may be considered a convenient alternative to standard unit root models but whether the presentation should be under the general heading of *structural breaks* is less obvious.

The Maddala-Kim monograph is useful for graduate students and other readers who want a comprehensive review of the unit root, cointegration, and structural break literature without wanting to go into the every detail. There has certainly been a need for such a text in the literature. The coverage of topics is indeed broad, and in this sense the book serves one of its purposes, that is, to bring together the different stands of research in the area. One might wonder whether a more selective exposition would have been preferable

because there are a lot of contributions in the literature which have had very little impact. Finally, I agree with the author's view on the future research, namely that what we do not need is yet another unit root test using the Nelson-Plosser data as a guinea pig.

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Handbook of Applied Econometrics: Volume I: Macroeconomics. Edited by PESARAN (M. HASHEM) and WICKENS (MICHAEL R.). (Oxford and Cambridge, MA: Blackwell, 1999. Pp. x+482 £18.99 paperback. ISBN 1 55786 208 7, 0 631 21558 1.)

Handbook of Applied Econometrics: Volume II: Microeconomics. Edited by PESARAN (M. HASHEM) and SCHMIDT (PETER). (Oxford and Cambridge, MA: Blackwell, 1998. Pp. viii+453. £85.00 hardback. ISBN 1 55786 209 5.)

These two volumes of the *Handbook of Applied Econometrics* were first published in hardback in 1995 (*Volume I*) and in 1997 (*Volume II*), and represent the first two contributions 'in a regular series of handbooks surveying the latest developments in applied econometrics' (*Volume I*, page 1). Paperback versions of each volume were subsequently published in 1999. As a result, the time that has elapsed since first publication, combined with the inevitable delays between writing an article and seeing it in print, mean that the contents of the two volumes can no longer (at the time of writing, January 2000) be considered as new. But, nevertheless, the two volumes still contain much that is of relevance to empirical modelling in economics.

The first volume has as its broad theme topics in macroeconomics. It is not possible to do justice to all the chapters in a review of this length, but it is nevertheless worth conveying to the reader the contents of the chapters at the very least. The first of the nine chapters, by Agustin Maravall, is concerned with unobserved components models. Such models typically decompose a time series into its trend, seasonal, and cyclical components, and enable those aspects of a series about which economic theory has little to say (e.g. the seasonal component) to be adequately modelled while incorporating economic theory where it is most relevant. A notable area of application in macroeconomics lies in real business cycle theory. Vector autoregressive (VAR) models are the subject of the chapter by Fabio Canova. VAR models lie at the heart of much of the recent cointegration literature, and such issues are discussed alongside more traditional topics such as identification and forecasting. Multivariate rational expectations models are dealt with by Michael Binder and Hashem Pesaran. This chapter provides a review of existing methods of solving and estimating such models, as well as providing new methods that also allow for the inclusion of nonstationarities into the set-up. In chapter 4, Kenneth West examines inventory models and Euler equations from the perspective of a rational expectations version of a linear quadratic model, and

focuses particularly on the comparison between full and limited information estimation methods.

One of the most widely investigated topics in macroeconomics is the consumption function, and the volume would not be complete without a chapter on this topic. John Muellbauer and Ralph Lattimore are the authors and provide a very extensive review, incorporating topics such as expectations, credit rationing, savings and leisure, assets, and the excess smoothness debate. A consumption function of some description is usually at the heart of most macroeconometric models, and it is large-scale macroeconometric modelling that is the subject of chapter 6 by Kenneth Wallis. The particular issues treated in the context of large-scale models are forecasting, rational expectations, and stochastic simulation. On a related theme, K. Kim and A. R. Pagan examine calibrated models, and focus their contribution around the comparison between the calibration approach and the systems of equations approach to the analysis of aggregate behaviour. Guy Laroque and Bernard Salanié's chapter is concerned with disequilibrium models, and provides a review of techniques in this area, while tests of financial market efficiency are the concern of Tim Bollerslev and Robert Hodrick. This final chapter is probably the most empirically oriented in the entire volume, and the blend of theory and application works extremely well. Because empirical modelling always has to confront the theory with the available data, however imperfect they may be, it is pleasing to see that most of the chapters include empirical illustrations of the methods, either from other studies or carried out specially for this volume. Such applications are essential for a venture of this kind, and the editors are to be commended for ensuring that empirical results are brought to the fore.

The second of the two volumes concentrates on various topics in microeconomics. Chapter 1 is an editors' introduction, while chapter 2, by David Good, Ishaq Nadiri, and Robin Sickles, provides a comprehensive review of index number and factor demand approaches to the estimation of productivity. The estimation of frontier production functions is surveyed by William Greene, and contains an extensive application using US airline data. The fourth chapter, by Arthur Lewbel, is concerned with consumer demand systems and household equivalence scales. This is a large literature to attempt to survey, and Lewbel successfully focuses on 'the numerous practical problems that arise in empirical demand system estimation' (*Volume II*, page 167). In the next chapter, Esfandiar Maasoumi's subject is empirical analyses of inequality and welfare. At the heart of this literature is the desire to compare different income distributions, and a review of the issues involved is provided along with the relevant statistical techniques that are used to estimate measures of inequality. In chapter 6, Robert Miller surveys the literature on estimating models of dynamic optimisation using microeconomic data, dealing along the way with the associated topics of model building, identification, and statistical inference. This leads on in the next chapter to the estimation of parametric and semiparametric search and duration models, an area about which George Neumann provides a very readable survey. Quasi-likelihood methods for count data are the subject of chapter 8 by Jeffrey Wooldridge, with most of the focus

allocated to univariate methods appropriate for cross-section data. The final chapter in the volume, by Klaus Zimmermann, deals with the analysis of business surveys, providing a review of the statistical methods that are of use in this field, along with some examples of the areas in which business surveys have been investigated. Although some of the chapters in this volume contain empirical applications, they appear to be less extensive on the whole than in *Volume I*, but are nonetheless welcome.

Any collection of articles has to be selective to a greater or lesser degree, and the editors of these two volumes are well aware of the topics that they have omitted. For example, they acknowledge the omission of 'recent developments in growth theory, international trade and finance, and nonlinear dynamic modeling' (*Volume I*, page 10), all of which would have been worthy candidates for inclusion in the macroeconomics volume. It is possible that such omissions will provide an incentive to produce subsequent volumes in the years ahead to keep abreast of developments in applied econometric practice.

According to the editors of *Volume I*, 'the emphasis of the series will be on rigorous applications of econometric and statistical methods to economic problems, and the methodological issues that arise from such applications, not on contributions of econometric and statistical theory' (*Volume I*, page 1). There is certainly a need for collections of articles that provide an overview of 'best' practice in empirical investigations in economics, but to remain relevant and topical the series needs to be updated and/or added to on a regular basis. These two volumes provide a fine start to such a series. Let us hope there are more contributions to come in the future.

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Econometrics and Economic Theory in the 20th Century: The Ragnar Frisch Centennial Symposium. Edited by STRØM (STEINAR). (Cambridge and New York: Cambridge University Press, 1999. Pp. xiv+629. £60.00 hardback, US \$90.00 hardback, £24.95 paperback, US \$39.95 paperback. ISBN 0 521 63323 0, 0 521 63365 6.)

Quantitative economics has come a long way since Ragnar Frisch embarked upon his career in the 1920s. The best of the papers collected here reveal just how far. Frisch's contributions to the subject are well known from his role in establishing the Econometric Society, his service for more than two decades as the founding editor of *Econometrica* and, not least, his own innovative research. Less widely known, outside Norway, are his contributions to the University of Oslo and to Norwegian economic planning. All these aspects of his career are documented in the first three chapters of this volume, produced to mark the centenary of Frisch's birth in 1895.

In the third of the introductory chapters, J. S. Chipman offers a characteristically elegant overview of Frisch's contributions to economics and econometrics. This fine paper provides the context for the subsequent chapters by

identifying the main topics of interest to Frisch and – most helpfully – by expressing his ideas in a form comprehensible to modern readers. With this aid, it is easy to appreciate how much the subject has advanced in the last half-century, and even more to admire the talents of those who pioneered ideas and techniques that are now taken for granted.

Most of the remaining sixteen chapters present original research, some of which follow directly in the tradition of Frisch himself. The papers are grouped into six parts: utility measurement, production theory, microeconomic policy, econometric methods, macrodynamics, and macroeconomic planning. Four of the six chapters in the last two parts are devoted to reflections on, and interpretations of, Frisch's work. Although most of the rest pay the customary respects, they stand on their own merits as substantive contributions with limited direct descent from those of Frisch himself.

The picture that emerges is of a subject infused with high professional standards, especially of technical rigour. Many of the questions (e.g. measurement of consumer surplus, estimation of elasticities, evaluation of government policies) would have been familiar to Frisch even early in his career. But by the late 20th century, the authors show how it is possible to address the questions with more precision, with greater generality, and with a clearer understanding of the limitations of the solutions than could have been possible in earlier times. If the underlying models – for instance, of household demand – have not changed much, their empirical implementation has surely advanced with the application of a rich array of tools for estimation, both parametric and non-parametric, and for the empirical evaluation of policy. The papers by Hausman and Newey (chapter 4), Blundell (chapter 5), and Heckman and Smith (chapter 8) provide particularly impressive testimony to the progress accomplished on these fronts.

Similarly for production theory, with respect to which Griliches and Mairesse (chapter 6) explore the pitfalls and resolve some of the problems in estimating the parameters of Cobb-Douglas production functions. Not that the econometric techniques themselves have reached a plateau, as the papers by Pesaran and Shin (chapter 11) and Johansen (chapter 13) demonstrate in their research on methods for analysing non-stationary time series.

To the extent that this book is representative of current research, it is the formal analysis of techniques to which the most efforts have been dedicated. The development of new and empirically applicable theories receives rather less attention. Or, perhaps, instead it is that the efforts made have yielded only modest progress. This appears to be especially true in macrodynamics, at least with respect to the papers reproduced here. The last of the areas identified directly with Frisch – macroeconomic planning – has become unfashionable in recent years, as evidenced by the evaporation of the early optimism present in the 1940s and 1950s. Although the final three chapters of the volume use Frisch's ideas as vehicles for spirited arguments advocating planning, as an area of research it seems to be dormant, at least in contrast with the more technically oriented subjects of microeconomics and econometrics.

While this volume is testimony both to the enduring legacy of Ragnar Frisch

and to advances in economics, it also provides another reminder about the increasingly specialised nature of the subject. For, despite its merits – or, maybe, because of them – each reader is likely to find something of interest in only a limited portion of the book.

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Economic Development in Palanpur Over Five Decades. Edited by LANJOUW (PETER) and STERN (NICHOLAS). (Oxford and New York: Clarendon Press, 1998. Pp. xxviii+640. £70.00 hardback. ISBN 0 19 828832 8.)

The village of Palanpur, in western Uttar Pradesh, in northern India, has been subject to quite remarkable examination by economists since the 1950s. It is scrutiny that has been intensive and sustained. There can be little about it, of any conceivable interest to economists, that remains unknown. Palanpur is, in this respect, unique. It is most unusual for economists to study villages over long periods of time.

The searching investigation began in 1957–8, when Palanpur was studied by the Agricultural Economics Research Centre (AERC) of the University of Delhi. It was further studied by the AERC in 1962–3. Palanpur was subsequently chosen by Christopher Bliss and Nicholas Stern for fieldwork in 1974–5, after discussion with AERC staff. Bliss and Stern's work resulted in what is now, in development economics, a celebrated book, *Palanpur: The Economy of an Indian Village* (Oxford: Oxford University Press, 1982). Since 1974–5 there have been two further periods of fieldwork, one in 1983–4 and the second in 1993, on the initiative of Jean Dreze and Nicholas Stern, with Dreze the driving force behind the field investigations. Those five household surveys have yielded data of very high quality. Several articles on Palanpur have been published and at least two doctoral theses completed. The present edited volume is the most recent outcome. In it a comprehensive analysis of economic change in Palanpur between 1957 and 1993 is provided.

There are, in India, 500,000 villages. Quite what the villagers of this particular one have made of all this attention (there were 762 of them in 1974 and 1,133 in 1993) is not clear. It is said that, in the late 1970s, villagers of West Bengal, if approached by people with questionnaires, would enquire, before answering, if their interrogators were Marxists or neo-classicals. If it did not occur to the inhabitants of Palanpur to ask such a question, they are likely, nevertheless, now, if exposure to their investigators has had any influence, to be more neo-classical than Marxist in their orientation. They may, even, have imbibed the rudiments of, say, Marshall's and Cheung's theories of sharecropping, or the theory of 'efficiency wages'; and something, perhaps, of the principles of regression analysis. They are unlikely, however, if they have absorbed the views represented in this volume, to be convinced of the usefulness of class, in relation to processes of change. Class is robustly dismissed in the present volume. One wonders what they might think of all this

in relation to their own condition, if the relevant, and conflicting, hypotheses were put to them clearly and dispassionately. Probably we will never know. During my own stay at the AERC at Delhi, in 1964–5, the authors of one AERC village report told of taking back their report and showing it to the villagers. One of the villagers examined its outward appearance with interest and said: ‘Yes. It is very impressive. But what good will it do us?’.

Whatever good the present volume might do the villagers of Palanpur, most certainly the contributors have produced a wealth of data and papers of high quality. Apart from the two editors, Peter Lanjouw and Nicholas Stern, the contributors are Christopher Bliss, Jean Dreze, Joceyln Kynch, Anindita Mukherjee, and Naresh Sharma. They have written, sometimes individually and sometimes in various combinations, very detailed chapters, containing a battery of most valuable tables, on ‘Palanpur: Population, Society and Economy’, ‘Economic Development in Palanpur, 1957–93’. ‘Population Growth, Employment Expansion and Technological Change’, ‘Poverty’, ‘Inequality’, ‘Nutrition’, ‘Labour’, ‘Tenancy’ and ‘Credit’.

Their concern is with the nature of economic and social change in Palanpur, the outcome of that change, and its determinants. They argue that the three basic forces determining change have been population growth, the introduction of new methods and the associated intensification of agriculture, and growth of the outside economy. They are particularly concerned with ‘living standards and their distribution’ in Palanpur. All of this is conveyed vividly, clearly, and rigorously.

In the Preface, Stern observes that while in the earlier Bliss-Stern volume they were largely concerned with the ‘formal testing of particular economic theories’, here, while staying within the bounds of ‘modern economics’ and approaching the study ‘from the perspective of economic analysis’, they have located it within the context of ‘the social structure, mores, and politics of the village’. Certainly, here the study comes alive in a way that the 1982 book did not, and one gains a vibrant sense of the forces of change and the impact these have had upon the lives of the villagers.

It is at once analytically powerful, empirically rich, and full of important new insights. The contributors have placed all social scientists, and not only economists, who study agriculture in poor countries, seriously in their debt. The book is a major achievement.

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Fathers, Sons, and Daughters: Industrial Entrepreneurs During India’s Liberalization. By NAFZIGER (E. WAYNE). (Greenwich, CT and London: Jai Press Inc., 1998. Pp. xiii+140. US \$78.50 hardback. ISBN 0 7623 0440 5.)

In writing this short book of 140 pages (of which 27 comprise an appendix, index, and bibliography) E. Wayne Nafziger fills seven chapters, three of which

are under ten pages each. This level of brevity has robbed the author of any opportunity to live up to the ambitious sounding title of his project. To this reviewer the title suggests the book's canvas to be a more detailed intergenerational study of private industrial development within India as a whole. This is not what this book delivers.

This study is an attempt at explaining some socioeconomic and other factors responsible for firm *and* entrepreneur survival in the coastal city of Visakhapatnam, within India's central-eastern state of Andhra Pradesh during the 23–24 year period between 1970–1 and 1993. In this context discussion of the role of the entrepreneurs' so-called human capital in perpetuating their businesses over time provides some useful insights. One interesting point is that more education is not necessarily associated with better success for the entrepreneurs in question. More education raises the opportunity cost of all other endeavours and therefore, in a relative sense, downgrades its value to immediate entrepreneurial interests.

As a precursor to all of this, Nafziger presents, in his first chapter, a lengthy account of theoretical perceptions of entrepreneurial activity in general. This discussion seems a little laborious and misplaced for what is basically an empirical investigation. This is not to say that the analysis is devoid of any originality or even some elegance. For example, discussion of Adam Smith's contributions (notwithstanding Nafziger's categorisation of him as an *English* Classical economist) is very readable. His account of the positions taken by relatively more recent writers such as Maurice Dobb, Leon Walras, Joseph Schumpeter, and Frank Knight, amongst others, is no less interesting but, in this reviewer's opinion, still without enough and appropriate context.

Nafziger's main interest is to unearth the characteristics typical of his group of surviving firms and entrepreneurs. The sample of 55 interviewees in 1970–1 (representing industrial firms registered with the Industries Department as employing five or more people) had all established their businesses between 1958 and 1970. Due to a perfectly legitimate set of reasons (for example, non-cooperation by one entrepreneur/firm, missing data for four others, etc.), discussion of the econometric results, from chapter V onwards, relies on a sample of just fifty interviewees. One source of potential confusion remains. Much of the earlier discussion relying on more descriptive statistical data (for example, that involves Tables II.1, II.6, and II.12 in chapter II) uses the full sample of 54 interviewees (that is, the original 55 less the one case of non-cooperation). This suggests some selective use of available data, which need not in itself be damaging to any interpretation of the overall results, as long as the reader is given the necessary cautions. It goes without saying that even casual omissions of statements of intent on how information will be used, as in the previous example, can detract from a study's authority. Another example of an apparent oversight is Nafziger's well-intentioned claim (mentioned early in the first chapter) to be using pseudonyms for his sample of interviewees. The discussion in chapter VI seems to contravene this pledge more than once. However, the detailed questionnaire appearing in the appendix testifies to the care intended with the procedural and methodo-

logical aspects of the study, even though these may have been occasionally compromised.

By the time the re-visit occurred in 1993, only 22 of the original cohort of firms had managed to survive. Of these, 20 continued to be in the hands of either the entrepreneurs first interviewed by Nafziger in 1970–1, or members of their immediate family (including a couple of grandchildren). This reviewer would have benefited from greater detail (over and beyond the econometric analysis presented in later chapters) on the changing fortunes of the 28 firms that failed to survive.

Chapter III, with less than nine pages, is devoted to a discussion of what is known as achievement motivation training (or AMT) within its Indian (or rather, Andhra Pradeshian) context. Nafziger's discussion of this appears to be motivated by a mid-1960s government initiative to expose some of Andhra Pradesh's business community to the benefits of AMT. Thankfully Nafziger's recognition of the incompatibility of AMT with Indian settings leads to his rejection of it as a topic for further discussion.

Chapter IV focuses on the historical context of the licensing regime from independence through to the mid-1980s. The purpose is to summarise the key events and to provide a background to how the entrepreneurs and their firms progressed throughout the period under study. However, given that few, if any, new insights are provided in this summary the devotion of a chapter to the topic – albeit a short one – seems a little unnecessary. An alternative approach to writing this chapter might have been an attempt to systematically track firm and/or entrepreneur-related changes over the 23–24 year period. However, given the resources required it is understandable why Nafziger did not proceed in this manner. But that is what is needed for such a study to be, in a sense, intergenerational.

Chapter V sees Nafziger return to his main empirical theme of identifying the distinguishing characteristics of surviving entrepreneurs and their firms. This chapter, despite being very brief, forms the core of the book. As a particularly well written chapter it enables the author to claw back much lost credence for what is undoubtedly an important area of research.

In chapter VI Nafziger presents further discussion of the Schumpeterian views on the entrepreneur and supplements this with OLS and probit estimates of the main features of surviving firms. He also provides a listing of problems associated with government control of industrial and commercial activity. This chapter appears somewhat disjointed and again lacks contextual detail: a problem that would have been avoided had its main elements simply been integrated into chapters IV and V. Nevertheless, Nafziger's somewhat anecdotal description of the consequences of liberalisation on India's entrepreneurs is highly readable. In fact, this is the book's major strength: presenting a lucid description of an event or two and inviting the reader to reflect on the general message implied, or leading to, the events themselves.

Chapter VII sums up the findings and speculates about the applicability of the study to the rest of India and elsewhere. Perhaps not surprisingly a wider applicability (beyond Visakhapatnam and Andhra Pradesh) is claimed. How-

ever, given what has come before I would maintain that this generality of application is based on an unacceptable level of extrapolative reasoning.

This short book confirms that even respected scholars can occasionally make weak contributions in their field.

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Economic Transition in Hungary and East Germany: Gradualism and Shock Therapy in Catch-up Development. By STEPHAN (JOHANNES). (London and Basingstoke: Macmillan, 1999. Pp. xv+293. £50.00 hardback. ISBN 0 333 75143 4.)

The book provides a comprehensive analysis of the two transition paths based on well selected statistical sources and careful reading of the relevant literature. Chapter 1 highlights the contrasts between experiences of the two post-communist economies. The next three chapters present the East German path as an extreme case of shock therapy. Employed to this end are: descriptions of communist legacy, privatisation strategy executed by *Treuhandanstalt*, and monetary union with West Germany which led to a high level of real wages relative to that of labour productivity. The Hungarian part of the book is twice as long. Chapters 5 and 6 deal with the issues of institution building in the financial sector and creation of an appropriate framework for macroeconomic stabilisation policies. These issues were resolved instantly for East Germany in the wake of monetary union. Chapter 7 investigates the role of foreign trade in the Hungarian development strategy. In the following chapter the restrictive macroeconomic policies applied in March 1995 are evaluated. Chapter 9 concludes. The East German case is labelled as that of premature integration. Consequently it is not surprising to learn that ‘... only after the process of economic restructuring and catch-up in terms of productivity is more or less completed can full EU membership be to Hungary’s advantage’. The present reviewer finds the book’s argument controversial. What follows will be polemical in character.

To what extent does the Hungarian transition path bear the hallmarks of gradualism? If the key steps in the transition are thought to be price and foreign trade liberalisation then the answer must be, only to a small extent. True, it is claimed that under the NEM a substantial measure of liberalisation was achieved. However a number of economists see this claim as empty and maintain that an informal and highly complex system of rationing was maintained (Nagy, 1994, pages 2–3). If so we have to accept that it took only two years to decontrol prices and imports. This is a short period by the standards of other liberalisation programmes implemented over the last few decades. The speed of transition can also be measured by the pace at which budget constraints are hardened. In Hungary the rate of decline of soft bank lending determined this. By mid-1990s this lending ceased to be a major problem. It can be argued that budget constraints were soft for a similar period

in East Germany due to subsidies and credit guarantees disbursed by the *Treuhandanstalt*. Thus it would be more apposite to contrast East German and Hungarian experience in reference to the level of the real exchange rate rather than to the degree of gradualism.

In what sense can East German integration with the West be seen as premature? By 1997, according to the author's own calculation, East Germany achieved just over 90% of its 1989 GDP level, a figure that is very close to the corresponding figure for Hungary. Had the Ostmark been retained as a separate currency would East Germany have had performed better than Hungary? The high real wage is seen as a device that will prevent establishment of a German *Mezzogiorno* in the East (page 83). If so, why is a substantial investment flowing into the East not producing strong gains in labour productivity? Klodt (1999) points out that the federal government subsidises investment in the East via tax credits and depreciation allowances to the tune of 60 billion DM a year. The envisaged causality is that high wages require high labour productivity, which in turn is achieved by high capital intensity. Unfortunately it is not the case that East German industries that are more capital intensive than their West German counterparts are also characterised by higher labour productivity.

The book identifies export surpluses, currency undervaluation, and monetary stabilisation as the three major preconditions for successful catch-up development. There is obviously a problem of exact definitions of these terms and their inter-relatedness. The association of the post-1995 resumption of growth in Hungary with a stable real exchange rate can be seen as a vindication of the second precondition. More generally, few would disagree with the wisdom of avoiding a Mexican-style financial crisis. However if the first precondition is interpreted as advocacy of export-led growth a dissent becomes legitimate. Why should current account deficit not be financed by net inflow of foreign capital, particularly FDI, over a prolonged period? After all Spanish and Portuguese catch-up development has been associated with such financing. Much is made of the danger of economic peripheralisation. It arises because the pattern of 'absolute disadvantages' may prevent making use of comparative advantages (page 196). The origin of the first concept is traced to the 1837 analysis of Friedrich List. It is further argued that foreign trade policies and import protection are necessary to achieve a shift towards higher value added and higher capital intensity output. As it happens a number of favourable trends have emerged in the Hungarian exports, which cannot be traced to consciously executed sectoral industrial policies. Carlin and Landesmann (1997) provide evidence that the share of R&D and skill intensive exports in total exports of the Visegrad countries increased considerably over the period 1989–1995. The improvement was particularly marked in Hungary. Since 1996 there has been a remarkable acceleration in the growth of Hungarian exports. Is not the causal factor behind this trade liberalisation itself?

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The Political Economy of Japanese Financial Markets: Myths versus Reality. By BEASON (DICK) and JAMES (JASON). (London and Basingstoke: Macmillan, 1999. Pp. xvi+304. £55.00 hardback. ISBN 0 333 57933 X.)

Japan's experience in the 1980s and 1990s provides an interesting example of what can happen when asset valuations rise rapidly and then suddenly collapse. Ten years ago the Japanese stock and real estate markets had reached unprecedented highs. These valuations were widely believed to be justified by the tremendous success of the Japanese economy and effectiveness of Japanese management techniques. The significant increase in interest rates initiated by the Bank of Japan at the start of 1990 precipitated a dramatic collapse in asset prices. A decade later the Japanese economy has still not fully recovered.

This book by Dick Beason and Jason James provides a timely analysis of the Japanese financial system from both an economic and a political viewpoint. The authors start with an historical analysis of the development of the banking system and financial markets from the time of the Meiji Restoration until the mid-1970s. They then consider the liberalisation and easing of regulations that occurred as the Japanese economy became more globally integrated. The main part of the book is concerned with the collapse of asset prices and the subsequent evolution of the Japanese financial system in the 1990s and the role of the political system in determining this.

The authors are clearly very knowledgeable about Japan and provide an excellent account of the current operation for the Japanese financial system. Chapter 6 on private sector financial institutions and chapter 8 on public sector financial institutions are superb. They explain how the Japanese financial system functions and the ways in which it differs from the other financial systems. One important aspect of this is the size of public sector financial institutions. The Postal Savings, the Public Pensions, and Postal Insurance had assets of ¥223 trillion, ¥119 trillion, and ¥96 trillion as of 1996, respectively. The vast size of these funds and the fact that they are ultimately subject to political control means that the government can intervene to support financial markets in a way that is simply not possible in most economies. The discussion of the political aspects of the system is less satisfactory, perhaps inevitably so. Given the rapid turnover of senior Japanese politicians, the detailed discussion of their positions on various issues will soon become outdated.

The authors are not afraid to take positions on what caused the rapid run-up in asset prices and their subsequent collapse. Their basic thesis is that Japanese corporate governance operates through the main bank system. Extensive cross-holdings of shares by banks and non-financial firms means that an Anglo-Saxon market for corporate control cannot operate. Although the main bank

system provides an oversight mechanism for monitoring firms, the authors suggest that it has the disadvantage of providing excessive incentives for borrowers to invest because this generates income for the banks. The rapid growth that such over-investment in the 1980s led to prompted unrealistic growth expectations. This, together with the low interest rates of that period, resulted in very high asset prices. The raising of interest rates and the Gulf War in 1990 changed expectations and this caused the crash. The authors use this interpretation of events to argue that there was not a 'speculative bubble' in Japan. They take a number of other what might be termed moderate positions. For example, they point out that by several measures such as the extent of non-performing loans the magnitude of the banking crisis was similar to that in the United States in the late 1980s.

It would have been interesting to hear the authors' views on the relationship between the financial system and real economic activity. Although in many ways such as unemployment the crisis has been moderate, it could be argued that the full aftermath has yet to be felt. In particular the large deficit the government has run in recent years in an attempt to improve the economic situation and the resulting accumulation of debt pose a significant problem for the future. This is especially true given the aging of the population and the large burden this will place on the working population in the coming years. There is also the issue of whether more rapid intervention in the financial system by the government, such as that undertaken by Scandinavian governments in the late 1980s and early 1990s in the face of similar crises, could have led to faster recovery.

The conclusion of the book is that while the effects of the Japanese crisis were damaging it was not the end of the world. This conclusion may be comforting to those observers of the current US situation who fear that something similar to what happened in Japan in 1990 is just around the corner.

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South Asian Economic Development: Transformation, Opportunities and Challenges.

By HOSSAIN (MOAZZEM), ISLAM (IYANATUL) and KIBRIA (REZA). (London and New York: Routledge, 1999. Pp. xiv+272 £19.99 paperback. ISBN 0 415 12887 2, 0 415 12288 0.)

Myths and Realities of the East Asian Model of Development: Lessons for India. By VINANCHIARACHI (JEBAMALAI). (Chennai: Centre for Research on the New International Economic Order, 1999. Pp. Xix+150. Rs. 175 paperback.)

The Economies of Southeast Asia: The Growth and Development of ASEAN Economies. By TONGZON (JOSE L.). (Aldershot and Lyme, NH: Edward Elgar, 1998. Pp. xv+251. £59.95 hardback. ISBN 1 85898 264 2.)

It is hard now to remember that in the 1950s and 1960s South Asian countries appeared to have much brighter economic prospects than those of East Asia.

In 1960 Pakistan and Sri Lanka both had higher *per capita* GDP in PPP terms than Korea, and India was not far behind. South Asian countries had inherited from the British a tradition of 'fiscal conservatism' and a modern civil service, while India had had a century-long history of industrialisation. In 1913 20% of India's exports were of manufacturers. Hossain, Islam, and Kibria's book attempts to explain why India, Pakistan, Bangladesh, and Sri Lanka's achievements have failed to live up to their promise. Using comparative material from East and South East Asia, the authors seek to identify policies which would improve South Asia's economic performance, and to evaluate their economic reform programmes of the 1990s.

Hossain *et al.* attribute the failures of performance in the 1970s and 1980s largely to inward looking development policies, excessive government intervention in the economy, macroeconomic mismanagement, and an anti-business mindset on the part of the civil service, particularly in India. Whilst all these undoubtedly contributed, the authors make no attempt to explain things in terms other than of policy failure. They do not try to integrate into their economic analysis those social and political factors which retard economic growth, in the way, for example, that Platteau and Hayami (1998) have done for African development. Institutions are certainly mentioned, but they remain peripheral (with the partial exception of the final chapter, on policy). In this sense, the book does not achieve fully its stated aims. The penultimate chapter, on lessons from East Asia, is a neat summary and analysis of the Asian crisis. However, it is weak on the lessons to draw for South Asia. The final chapter on policy suggests mechanisms to lock South Asian governments into good governance, such as the use of laws against deficit financing, but mainly the authors propose rather standard policies, including continuing outward trade orientation and shifting the 'non-core' functions of government to the private sector.

Nevertheless, Hossein *et al.* do succeed in providing a useful and well-written overview of recent developments in South Asia. The chapter on the financial sector shows how South Asia has tended to follow the rest of Asia in liberalising its financial sector before putting effective regulatory mechanisms into place. Financial crisis, the authors hint, was largely avoided by the fact that the liberalised financial institutions were often still state-controlled, so the public assumed they would not be allowed to fail. The chapter on trade traces the rapid growth in the South Asian region's exports in the 1990s, following some degree of economic reform. However, intra-South Asian trade remains low by the standards of the rest of Asia. What is striking is the extent of the task ahead. Despite the rapid export growth in manufacturers and (in India's case) services, and despite the widespread adoption of green revolution technologies in agriculture, real incomes remain low. Some 40% of South Asia's population still suffers food poverty with a diet of inadequate calorific intake.

Jebamalai Vinanchiarachi explores the East Asian experience in order to draw lessons for Indian development policy. This interesting research was originally conducted for a doctoral thesis in the 1980s; it has been issued as a book, with some limited updating, in view of its relevance to lessons India

might draw from the 1997 Asian crisis. The central argument, from the perspective of the mid-1980s, is that it would have been difficult and unwise for India to have attempted to replicate in a thorough-going fashion the export-oriented pattern of development of Korea and Taiwan. India would have been starting from a far deeper pattern of import substitution than they, with protected domestic production of a wide range of capital goods and intermediate products. This pattern would have been threatened by the import-intensive way in which Taiwan and Korea expanded their capital-intensive exports. India, the author feels, also lacks the institutional and economic flexibility which enabled Korea and Taiwan continually to change their mix of export products and to withstand large fluctuations in demand in the US and Japanese markets, on which they were heavily dependent. Much of the book is taken up with a highly disaggregated investigation of precisely how dependent Taiwan and Korea were on external sources of demand, technology, and finance, and his warnings of a decade ago about financial vulnerability seem prescient in the light of the events of the Asian crisis. In a newly written concluding chapter, the author admits that Korea may well be able to recover from the crisis (and Taiwan was much less affected anyway). However, he feels that the trauma of 1997 shows the weaknesses of 'export overload', especially in the Korean case, where policy makers ignored structural weaknesses in the domestic economy. This book clearly is intended primarily for Indian readers. It would be good to see Vinanchiarachi produce a more generally available and thoroughly updated book, to include comparison with China as well as Korea, and to evaluate India's recent moves towards a more outward-oriented development path.

The members of ASEAN, the Association of South East Asian Nations, of course were also badly affected by the Asian crisis. Unfortunately, Tongzhon's volume has been too long in press for it to take account of the crisis, and his introductory overview contains a statement that the dynamism of ASEAN countries is expected to continue into the rest of the 1990s! Although he is hardly alone in failing to have predicted the crisis, the book's continual stress on economic success to the neglect of underlying problems obviously now detracts from its usefulness. For example, and with hindsight, the comments (pages 150 and 154) on the stability of the ASEAN countries' – especially Thailand's – financial system are embarrassingly complacent. That said, the book does give a wide-ranging and thorough account of events in South East Asia up to the mid-1990s. It manages to combine helpful institutional detail, for example on the ASEAN free trade area (AFTA), with a generally sensible economic commentary. It notes that AFTA could have various potentially negative effects, such as the enhancement of the market power of foreign companies, to set off against the benefits of enhanced competitiveness and greater attractiveness to foreign investors. The book will be valuable as a reference on South East Asia, especially when the publishers produce a revised edition.

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Reference

Platteau, Jean-Philippe, and Hayami, Yujiro (1998), 'Resource endowments and agricultural development: Africa vs Asia', in *The Institutional Foundations of East Asian Economic Development*, (ed Yujiro Hayami and Masahiko Aoki), London: Macmillan, pp. 357–410.

Birth of the Multinational: 2000 Years of Ancient Business History – From Ashur to Augustus. By MOORE (KARL) and LEWIS (DAVID). (Copenhagen: Copenhagen Business School Press, 1999. Pp. 341. £29.00 hardback, US \$48.00 hardback. ISBN 87 16 13468 0.)

This book represents an interesting project. It was apparently conceived as an historical investigation of ancient boundary-crossing commerce in order to provide insight into the institutional elements of the modern global economy. Attention is focussed on four commercial epochs: the Assyrian aggressive military expansion with its accompanying administered trade, the far-flung Phoenician commercial dominance of the Mediterranean based on exported products and the 'carrying trade', Greek 'free market trade', and Roman 'legionary capitalism'. The exposition is based upon extensive research into the recent academic literature reporting on archaeological and historical discoveries.

The moving spirit of the project is most effectively developed in the chapters on the Phoenician–Levantine and Carthaganean commercial expansions built on an institutional structure vaguely compared with developments in Japan. The descriptive exposition is interesting and well documented, but the analytical and theoretical burden of the book leaves much to be desired.

The methodology espoused by the authors is the 'eclectic paradigm' attributed to John Dunning, a leading business historian. This approach accepts a broad array of economic institutions from various cultures as viable functioning elements in modern global economics. Carrying this banner, the authors plunge into ancient economic history. This comparative historical institutionalism is a laudable venture and I applaud their commitment to interdisciplinary synthesis. One gets the feeling, however, that the Phoenician example stimulated interest in the project and the Assyrian, Greek, and Roman elaborations were secondary. Theoretically, Morris Silver's work, *Economic Structures of Antiquity* (1995) is cited, but his basic thesis was not elaborated. Silver's contention is that natural market forces could not assert themselves because of limits on transportation and political inhibitions, so supplementary economic institutions evolved to support economic activity. This analysis is in the tradition of the 'new institutionalism' and Coase's explanation of the vertically integrated firm.

For the economist and economic historian, the absence of any definition of 'capitalism' or 'nation' leads to a theoretical problem since any suggestion of commercial exchange is labeled capitalism and the Egyptian economy is completely passed over – dismissed as 'socialist'. Nationhood as a reference base for multinationals may have some resemblances to an ancient city state and the 'eclectic paradigm' offers a wide embrace, but broader research would

have brought home some fundamental considerations important to preindustrial economics. Fernand Braudel's classic on the development of capitalism, not cited, extensively documents the consensus that up to the 18th century, 80% or more of the population was committed to agriculture supporting the military, administrative, religious, and commercial superstructures of society. In an effort to document the emergence of a dominant 'free market economy' in the Athenian state, the authors (page 168, n. 118) cite V. D. Hanson's book, *The Other Greeks: The Family Farm and the Agrarian Roots of Western Civilization* (1995) page 361. What Hanson actually says is that the ideological status of the small farmer-citizen-soldier (hoplite) was eroding with the democratic inclusion of the landless, but booty from military ventures added greatly to the capital assets in agriculture and class status continued to be associated with landholding and productive agriculture (pp. 375–77). This was also true of Roman times. The Greek economy would be better characterised as a mixture of military enterprise, municipal regulation, and private and franchised trade with a large agricultural base. Xenophon's policy tract, *Ways and Means*, deals with the problems of the Athenian economy and would have added perspective. It is surprising that the authors did not consult M. I. Finley's *The Ancient Economy* (2nd ed. 1985). Further insight could have been drawn from Lawrence Krader's book, *The Asiatic Mode of Production* (1975) that surveys a wide range of literature analysing the productive rather than the commercial structure of antiquity with heavy emphasis on its agrarian foundations. J. A. Savloff and C. C. Lamberg-Karlovsky's edited collection, *Ancient Civilization and Trade* (1975) would have offered some theoretical considerations and of course, we miss the classic, Karl Polanyi, *et al. Trade and Market in the Early Empires: Economies in History and Theory* (1957). A broader and more eclectic perspective could have been gained by consulting P. D. Curtin's *Cross-Cultural Trade in World History* (1984) that has a parallel thesis and, in addition, covers 'tribute trade' in China where extorted tribute was tempered by large or even equivalent return gifts – shades of development aid in an age of imperialism. A somewhat different and provocative orientation could have been gained from A. G. Frank and B. K. Gill's edited collection, *The World System: Five Hundred Years or Five Thousand?* (1996).

Our concern is that more interdisciplinary synthesis and breadth of comparative perspective – an eclectic paradigm – is highly desirable and should be encouraged. I have a sense that the caveats are twofold. First, the temptation to rely on computer research can lead to a false sense of scholarship, missing important works that are 'old' or strangely titled. Second, there is no substitute for authors and publishers having their offerings refereed by competent scholars in all the relevant special fields. Granted, this frequently leads to encounters with 'turf defending' pedantic specialists who resent trespassers but erudite interdisciplinarians can still be found. We are aware that an educationally stimulating and broadening impulse can very easily get dragged down into a morass of detailed academic quibbles, but, at the same time, we do not wish to lose the benefits of accumulated recorded wisdom. We will laud the authors' vision and effort

while deploring the shortcomings of the institutional structures for research and prepublication criticism.

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John Ruskin's Political Economy. By HENDERSON (WILLIE). (London and New York: Routledge, 1999. Pp. xv+200. £55.00 hardback. ISBN 0 415 20067 9.)

It is a conventional opening gambit for historians of economic thought to stress the timely nature of the exercises in historical retrieval upon which they are engaged. Yet in the case of Ruskin such a claim is unquestionably warranted. As contemporary economists increasingly emphasise the importance of trust, duty, responsibility, commitment, and the non-contractual elements of economic relationships in the construction of success, there is a concomitant recognition of the importance of the socially-embedded nature of economic activity and, once that is accepted, Ruskin can be moved centre stage. One might also add, after the orgiastic indulgence in individual and collective consumption which marked the transition to Y2K, that Ruskinian strictures on an unreflective, unbridled, and unethical consumerism seem peculiarly pertinent.

For Henderson the contemporary imperative to reappraise Ruskin's contribution to the development of economic ideas derives from the 'Hegelian synthesis inaugurated by New Labour' of 'Thatcherite market-led solutions' with, one assumes, the remnants of a democratic socialist political economy. And, while one might demur at such claims, he does furnish in a series of interrelated essays a re-evaluation of Ruskin's economic and social criticism which is profoundly suggestive of the continuing critical and prescriptive relevance of what Ruskin has to offer.

This re-evaluation has four main components. First there is an exposition of Ruskin's ethically-informed political economy, effected through a consideration of his critical treatment of economic harmony, economic agency, natural law, and distribution, as these concepts were amplified and deployed by classical political economists. Secondly, there is a discussion of the classical philosophical roots of some of the methodological and prescriptive positions which Ruskin took up in his economic writing. Specifically Henderson seeks to show the influence of Xenophon's *Oeconomicus* with respect to Ruskin's use of the concept of the household, both as the basis of his critique of a market economy and as an alternative mode of organising economic activity. Here Henderson stresses too the importance of Plato's *Laws* and *Republic* as regards Ruskin's belief in a rational, paternalistic, ordering of economic life. Thirdly Henderson uses the text of Mill's *Principles*, Ruskin's marginalia on his copy of the second edition of the work and *Unto this Last*, 'to arrive at an understanding of Ruskin's reading [of Mill's work] that is richer than [existing] interpretations'. Finally, in two concluding chapters, there is an elucidation of

the lasting impact of Ruskin on professional economics by a discussion of elements of the work of William Smart, J. B. Clark, and Alfred Marshall.

The determined rhetorical turn of Henderson's exegesis of the primary texts does yield some interpretative dividends and, more generally, the volume undoubtedly adds to our understanding of Ruskin's economic writing and the part it played in his corruscating critique of late Victorian society. Yet in his discussion of both the origin and impact of Ruskinian political economy, it is not always apparent when Henderson is arguing the case for an influential filtration of ideas, when he is in the business of simply highlighting illuminating theoretical and conceptual parallels and when he wishes the reader to understand that the latter should be taken to imply the former. If, for example, the aim of the chapter on Xenophon 'is, primarily, that of establishing textual and conceptual links between Greek economic and social thinking and Ruskin's views on political economy', then it is necessary to establish just what the nature and status of those links are. Allusion to parallels, in this regard, is not really helpful.

This problem with establishing the nature and extent of filtration and influence becomes even more acute when Henderson moves on to consider the Ruskinian legacy for professional economics. Thus the fact that Ruskin is only mentioned once in J. B. Clark's *Philosophy of wealth* is not deemed 'reason enough to suppose ... that there is not more to his influence'; Clark was, Henderson reminds us, usually remiss in acknowledging the work of others. 'Ruskin's invisible textual presence' can still be identified in the big methodological issues which Clark explores. But, as Henderson himself recognises, it is clear that many of these were integral to the late 19th century *Methodenstreit* generated by the German Historical School, which certainly engaged the young J. B. Clark's attention. Again one is left wondering as to the source, nature, and direction of intellectual influences.

With Marshall the one text considered is his lecture on 'The social possibilities of economic chivalry'. Here again there is no mention of Ruskin but we are to impute influence from the Ruskinian nature of its rhetoric and the discursive themes which Marshall pursued. Of course William Morris *is* cited but given that Henderson sees him only as Ruskin in socialist mufti the argument for influence is saved. Here, and elsewhere in Henderson's discussion of the Ruskinian legacy, the reader is sometimes distracted by the shuffling of angels as they are mustered to pirouette on pinheads.

Of course the problem with Clark and Marshall is also that the texts chosen are at odds with, or at least in no way representative of, the totality of their economic opera. Indeed these authors' respective contributions to the evolution of economics were markedly inimical to Ruskin's view of what economics should be and what it should become. In this and other respects one can only agree with the author that the decision to consider the work of Clark and Marshall to establish the positive Ruskinian legacy for economics is 'perhaps a surprising one'.

It is all the more surprising as, in terms of impact and influence, the really interesting tale to tell is that which involves the heterodox political economies

of Morris, Blatchford and Hobson, Penty, Tawney and Cole, Schumacher, Illich, and Roszack. It is in the work of these writers that one finds a profound Ruskinian methodological challenge to mainstream economics; it is in their political economies that the most potent elements of the Ruskinian assault on late Victorian capitalism are replicated and revised; it is in the economic literature they produced that the critical relevance of Ruskinian thinking to 20th century capitalism is established and it is they who give real substance to Henderson's final claim that Ruskin's writing *still* has the 'power to surprise and subvert'.

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Max Weber and the Idea of Economic Sociology. By SWEDBERG (RICHARD). (Princeton, NJ: Princeton University Press, 1998. Pp. x+315. £19.95 hardback, US \$29.95 hardback. ISBN 0 691 02949 0.)

It is commonly held that Max Weber, although he held chairs for National Economics from 1894 to 1899 at Freiburg and Heidelberg, and although economic issues play a crucial role in his sociological work, was never an economist in his own right. However great his influence on the social sciences in general, and the new field of sociology, his economic theories have never been given proper attention by economists, ever since the demise of the traditional Historical School. This book attempts to demonstrate that this assumption is misleading. Rather, as Swedberg contends, Weber was deeply involved in developing a fullscale project of an 'Economic Sociology', or, as Weber himself put it, taking up a concept by Dreitzel, of 'Sozialökonomik', and that it would be worthwhile indeed even for present-day economists to acquire a greater degree of familiarity with Weber's relevant texts, rather than being content with analysing the famous essay on 'The Protestant Ethic and the Spirit of Capitalism' that indeed represents only a small segment of his writings on economic matters. However, Swedberg's reasoning is slightly impaired by the fact that he relies almost exclusively on the English translations of Weber's works which in part already represent a bias against taking economic arguments fully into account; at times the reader is puzzled by the somewhat arbitrary translations of key terms which admittedly abound in the available translations. Besides, the edition of Weber's lectures on 'General Economic History' in Munich in 1919/20 which was based in part on his notes, and in a large part on scripts by students (both lost to us) must be considered rather unreliable, and it ought not to be used under key points interpreting his ideas.

This being said, Swedberg's undertaking is in many ways admirable. It goes without saying that the concept of a capitalist economy presented in the essays on Protestantisms is but a segment of a far wider and far richer picture of capitalism as an economic system developed in Weber's later writings, notably in the so-called first (that is in fact the latest) section of 'Economy and Society'.

With good reason Swedberg proceeds from Chapter 2 of *Wirtschaft und Gesellschaft*, one of the texts which Weber wrote in 1920 only shortly before his death, which can be considered his final word on these issues, in reconstructing a diversified model of different types of economic systems, extending from the household economy to the modern purpose-rational capitalist market economy. Swedberg attempts to clarify Weber's typology of various modes of capitalism by distinguishing between three basic types of capitalism, rational capitalism, political capitalism, and traditional commercial capitalism; this endeavour is welcome in as much as the richness and diversity of Weber's thought is elaborated in this way to the full. However, it may be argued that in principle Weber's ideal types of the various variants of 'Verkehrswirtschaft', that is to say an economy exchanging goods in a market place, are even more differentiated than Swedberg would have it. Besides, as Swedberg himself notes, the rationality of modern capitalism is of a double-edged nature, and to some degree this presentation of his concept of capitalism simplifies the problems. Swedberg emphasises that Weber's theory of political domination does in fact fully take into account the economic ramifications of the different types of domination; indeed one of the main thrusts of Weber's reasoning was to clarify the consequences of particular forms of domination for the economy. Neither in this field, nor anywhere else, is the economic dimension lacking. Perhaps one will take exception to the interpretation of Weber's concept of non-legitimate domination which is erroneously equated with democratic rule (page 72f.); rather his typology is constructed in such a way that there cannot be a type of non-legitimate rule, but only a variety of types of domination based on different grounds of legitimacy.

The third area that Swedberg analyses in depth is the interrelationship between religion and economics, on the basis of Weber's imposing treatises on the sociology of world religions. He points out that here Weber extended the notion of Economic Ethics far beyond the narrow conception in the essay on protestantism and the rise of capitalism, in as much as Weber now describes a far wider range of components of economic ethics in a given society, religion being just one of them.

On the whole, Swedberg's endeavour to present Weber's thoughts on economic sociology in a systematic form and to confront them with the position of contemporary economists is most fruitful, even though Weber's most sophisticated reasoning is at times presented in a somewhat simplified fashion that is more orderly and more systematic than the original. It provides lucid insights into key issues of Weber's sociological work. Swedberg attempts to further strengthen his argument by a careful analysis of Weber's earlier work, in particular the so-called *Grundriß der Sozialökonomik* which show more clearly that Weber's *Sozialökonomik* intended to encompass contemporary economics in the German-speaking world in its entirety, though with a strong impact upon the social dimension. The purely theoretical aspects of economics were left aside, not because Weber showed no interest in them, but because he wanted to concentrate upon the cultural impact of economic systems, in particular the impact of economic conditions upon culture. Weber was a

strong adherent of the theory of marginal utility (a point somewhat underrated by Swedberg), but at the same time he emphasised that scarcity' being the key notion of marginal utility is largely determined by cultural and historical factors rather than being given. Swedberg's account of 'the evolution of Weber's thought' which he modestly published in an appendix only is very informative, and would deserve a fuller elaboration. All in all, this book, even though some of Swedberg's theses are arguable, must be considered a major contribution to the ongoing debate on Max Weber. Perhaps economists would be well advised to have a new look at Weber's sociology and its economic aspects.

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