considerations should be brought into the picture in designing policy options. Finally, auxiliary mechanisms should be designed to determine the effectiveness of the policies that are put into place. Richardson also recommends that the U.S. government increase its role in providing export finance and encourages U.S. support for the development of human, physical, and technological capital that would raise the U.S. standard of living and ensure its position in future export markets.

This book represents one of the first attempts to assess the impact on the U.S. economy of policies to discourage certain U.S. exports. As with any first effort in a new line of inquiry, there are many things to criticize. Nonetheless, Richardson's study raises important questions and should lead to additional theoretical and empirical work on export policy. Whether Richardson's numbers are plausible or not, they are now in the public domain; because of that, they are important. The Clinton Administration has recently achieved several trade policy successes, including the passage of NAFTA and the completion of the Uruguay Round. It has sought public support for both of these efforts on the grounds that they will generate exports and job growth in leading sectors of the U.S economy. Richardson's study will undoubtedly be used as ammunition by those who view existing export restraints as futile or even counterproductive. This is good, because export policy has not been seriously rethought for several decades. With luck Richardson's study may also provide a stimulus to the government to streamline its antiquated export licensing program. That, in itself, would be an important and useful contribution.

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Alberto Giovannini, ed *Finance and Development: Issues and Experience* (Cambridge University Press, New York, 1993) pp. ix + 436, $49.50.

Finance and Development: Issues and Experience, edited by Alberto Giovannini, is a collection of nine papers with a helpful Introduction by Giovannini and a perceptive concluding Overview by Joseph Stiglitz. While all of the papers are related to finance and economic development, the volume is best viewed as a collection of individual papers rather than as a uniform and tightly coordinated treatment of finance and development. Instead, readers can pick and choose from the set of insightful papers.

Paul Krugman opens the book with a sobering message. In 'International Finance and Economic Development', he argues that despite current hopes that international capital market integration will spur economic development, there is little reason for optimism. Krugman shows that large capital flows from rich to poor countries did not happen in the past and contends that they will probably not happen now or in the future. Moreover, those capital flows that do find their way to developing countries will probably not affect growth much since the impact of capital on growth is small. Thus, Krugman concludes that international finance is unlikely to be a major engine of economic development.

Daniel Cohen's paper 'Convergence in the Closed and in the Open Economy' is a nice complement to Krugman's work. In contrast to Krugman, Cohen rigorously shows that there are plausible conditions under which enhanced access to international capital markets will dramatically boost the rate of physical capital accumulation and economic growth in poorer countries. Empirically, however, Cohen confirms Krugman's argument by finding that large debtors in the 1970s did not enjoy faster rates of capital accumulation than other developing countries. Those policy-makers and analysts who believe that international capital market integration can importantly spur economic development will have to confront Cohen's and Krugman's findings.

In 'Capital Market Imperfections and Regional Economic Development', Bruce Greenwald, Alec Levinson and Joseph Stiglitz extend the Stiglitz–Weiss model of credit rationing under asymmetric information to regional information-based capital market imperfections. They argue that local banks have better information about local borrowers than non-local banks, and banks therefore tend to invest locally. Thus, these regional information asymmetries reduce capital mobility. The authors note that if a negative shock hits a region, this will hurt bank balance sheets and induce a regional credit crunch, since regional information asymmetries will stymie cross-regional, private capital flows. This paper thus motivates a role for official interventions that help banks in depressed regions. Unfortunately, the paper does not specify why, when, or how governments will perform better than private capital markets at picking and funding good banks in depressed regions. Readers interested in this line of research should also see Boyd and Smith (*JME*, 1992).

In an important paper, Oren Sussman uses modern informational economics to examine the economic determinants of financial development. He develops a model with monopolistically competitive banks where bank market power is derived from informational advantages. As banks become more specialized at evaluating firms, intermediation costs fall. The model predicts that as the capital stock increases, the market for financial intermediation grows, which induces banks to enter and become more specialized, so that intermediation costs fall. The model also predicts that the share of the financial system in GNP will fall. Using a cross-section of countries, Sussman confirms one prediction: intermediation costs fall with economic development. However, he refutes his second theoretical prediction when he finds that the role of the financial system increases with economic development. Future research will have to reconcile these findings.

In an excellent and thorough paper that is bursting with interesting and provocative information, Ricardo Faini, Giampaolo Galli and Curzio Giannini evaluate finance and development in Southern Italy. Despite massive capital inflows and aid during the last few decades the ratio of GDP per capita in Southern Italy is about 57 percent that of rest of Italy, and total factor productivity is also considerably lower in Southern Italy. Analysts have advanced many explanations for this disparity: less well-developed infrastructure, worse labor market rigidities, more poorly defined and enforced property rights, and more distortionary policies. This paper focuses on the role of the financial sector in helping to explain differences in GDP per capita between Southern Italy and the rest of the country. The data suggest that (i) in contrast to elsewhere in Italy, Southern banks tend to be very small and serve distinct territories; (ii) bank operating costs as a share of total resources are 20 percent higher in the South; (iii) average loan quality is much worse in the South (14 percent bad loans, compared with 8 percent elsewhere in Italy; (iv) lending rates are about 2 percent higher in the South; and (v) profits are considerably lower in the South. The authors go on to argue that risk only explains about half of the interest rate differential. Moreover, they present evidence that (a) screening firms in the South is more difficult; (b) the informational advantages of local banks in the South restricts competition; and (c) the lower level of competition allows Southern banks to behave more monopolistically than elsewhere in Italy which keeps operating costs and interest rates relatively high. Thus, the authors conclude that differences between the financial systems of Southern and North-Central Italy help explain differences in the level of GDP per capita between the regions.

In 'Regional Imbalances and Government Compensatory Financial Flows: The Case of Spain', Juan Ramon Cuadrado, Guillermo de la Dehesa and Andres Precedo argue that regional policies in Spain have focused on compensating ex post income differentials. Consequently, these regional policies protected backward regions from increased competition and also reduced labor mobility to more prosperous regions. Thus, the authors contend that Spanish regional policies have helped exacerbate rather than mitigate the gap between rich and poor regions. Given some of the similarities between Spain and Italy, the book would have benefited from more comparisons between the study of Southern Italy and this paper on regional policies in Spain.

In 'The Role of Finance in Economic Development in South Korea and Taiwan', Yung Chul Park criticizes the view that financial liberalization boosts financial sector development and economic growth. Despite deregulation and technological innovations that greatly reduced the costs of collecting and processing information, Park could not identify significant changes in the provision of financial services by financial intermediaries. Moreover, Park argues that in Korea and Taiwan, financial development did not positively affect savings or the productivity of investment. Thus, Park is skeptical that financial liberalization and the building of a sound financial infrastructure will yield great returns. While an interesting discussion of Korea and Taiwan, the findings conflict with recent broad cross-country results (King and Levine, *QJE*, 1993) and detailed case studies (Caprio et al., *Financial Reform: Theory and Practice*, 1994); Park does not identify which characteristics of Korea and Taiwan produce these differences with other countries.

Ronald McKinnon explains why macroeconomic instability is almost endemic in the transitional socialist economies (TSEs) of both Asia and Europe in his paper 'Macroeconomic Control in Liberalizing Socialist Economies: Asia and European Parallels'. Using numerous country experiences, McKinnon contends that in rushing to dismantle the central planning apparatus and privatize state-owned enterprises, TSEs destroy the mechanisms for collecting taxes and maintaining monetary control. Under central planning, taxes are implicitly collected through the system of state-determined prices. As TSEs liberalize prices and decentralize decision-making, the tax system breaks down and enhances macroeconomic instability until a market-based tax system can be constructed. Similarly, under central planning, the financial system passively allocates credit in accordance with the government's plan and plays little role in exerting corporate governance and determining the allocation of savings. As TSEs disassemble the central planning apparatus prior to the construction of market-based financial intermediaries, another pillar that historically supported macroeconomic stability crumbles without being replaced with a market-based pillar. McKinnon suggest that countries should initially confine liberalized enterprises to self-finance and to non-bank capital market finance while maintaining tight control over bank credit to state enterprises. As the economy matures, bank lending can deliberately and carefully be extended to liberalized enterprises. Since the paper was written in 1991, it clearly establishes McKinnon's perceptiveness given subsequent developments in the former Soviet Republics during 1992–1994. However, countries did not follow his advice and cannot turn back the clock, leaving open the question of what to do now.

Philippe Aghion and Robin Burgess examine the role that international financial institutions, such as the European Bank for Reconstruction and Development, might usefully play in promoting economic development in Eastern Europe and the former Soviet Union. Their paper complements the macroeconomic focus of McKinnon by focusing on the microeconomics of privatization, restructuring, and foreign direct investment. Specifically, the authors examine the absence of market-based financial institutions, poor infrastructure, a dearth of a market for corporate control or of managements skills, and poorly defined property rights and argue that these market failures provide an economic rationale for intervention by multilateral institutions. Aghion and Burgess contend that the provision of financial resources is of secondary importance; instead, the critical value-added of an international development banks is to provide expert advice on privatization, restructuring, modernization, management training, and on forging links with foreign investors. While potentially true, the paper would benefit from a systematic assessment of whether multilateral institutions play these critical roles well.

As noted by the volume's editor, Alberto Giovannini, " . . . the papers in this volume offer a rather skeptical assessment of the role of financial markets in economic development" (p. 7). Although Robert King and I (*JME*, 1993) have argued the opposite, the collection of papers in *Finance and Development* offers a rich set of theoretical perspectives, country experiences, and empirical evidence such that financial and development economists will find much worthwhile information in this book.

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