toward debate over particular industries' levels of protection.

Hiscox devotes relatively little attention to broad institutional changes, such as creation of the General Agreement on Tariffs and Trade. These changes might help explain, for example, why his empirical model performs less well for 1945–1962 (pp. 153–4, 163). Along the same lines, countries experienced significant changes both in the structure of their protection-granting procedures and laws (e.g., across-the-board protection versus special administrative protection such as antidumping and countervailing duties) and in the extent to which economic policies took the form of laissez-faire versus a managed economy with sector-specific targets.

Perhaps most important, *international* factor mobility—both labor and capital—varied dramatically over the period in question. Broadly speaking, international integration rose until World War I, declined, and then increased post-World War II. International factor mobility clearly cannot be assumed exogenous with regard to either trade policy or domestic political processes. Therefore, one wonders both about the implications for Hiscox's measures of inter-industry mobility and about any connection between the World War I break in *international* factor mobility and Hiscox's turning points in *inter-industry* factor mobility (p. 163).

Hiscox proves that, after 60 years, the Stolper-Samuelson Theorem continues to provide a robust framework for analyzing the complicated domestic politics of trade policy. Readers who want to know more about these issues from an applied perspective definitely should read *International Trade & Political Conflict*; but start with Kevin O'Rourke and Jeffrey Williamson's *Globalization and History: The Evolution of a Nineteenth-century Atlantic Economy* (Cambridge, Mass.: MIT Press, 1999).

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G Financial Economics

Financial Liberalization: How Far, How Fast? Edited by Gerard Caprio, Patrick Honohan, and Joseph E. Stiglitz. Cambridge, New York and Melbourne: Cambridge University Press, 2001. Pp. ix, 308. $50.00. ISBN 0–521–80369–1.
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Recent economic crises in emerging markets have led to widespread questioning of the benefits of financial liberalization. This book examines its merits in light of these events and asks how far and how fast liberalization should proceed. It starts with the premise that market pressures compel the abandonment of repressive financial regimes, sooner or later, either because controls are ineffective or too costly in terms of side effects. However, when information is asymmetric and competition inadequate, governments must think carefully about the design of policy reforms in order to dampen financial instability. The general message is that overly rapid financial liberalization, inadequately suited to a country's institutional circumstances, can do more harm than good and that premature capital account liberalization poses particularly large risks.

The book consists of ten chapters written by World Bank staff and other contributors and presented at a workshop in March 1999. The introductory chapter by the co-editors provides an excellent overview of the issues and content of the volume. It describes the rationale and costs of financial repression as well as the possible effects of financial liberalization on bank behavior and credit allocation. Honohan and Stiglitz, in the book's second chapter, argue that for countries accustomed to direct government control of banks the switch to indirect prudential regulations based on risk-based capital standards or best practice accounting practices may be ineffective and even destabilizing because of agency problems associated with asymmetric information. Conservative banks can suddenly become gamblers in the wake of large losses to their portfolio and franchise value. In response to this problem, they advocate a more "robust and nuanced" approach to financial liberalization that eliminates the worst distortions but restrains risk-taking activities by some combination of restrictions on entry, asset and liability composition, and deposit rate ceilings.

Honohan presents cross-country evidence that financial liberalization in emerging markets has indeed increased the level and volatility of interest rates. However, bank spreads have not declined, reflecting both continued market power and the higher risks of lending. He also presents a methodology for dating the de facto liberalization of interest rates through changes in the short run dynamic behavior of domestic interest rates and response to world interest rates. Asli Demirgüç-Kunt and Enrica Detragiache show that liberalized financial systems are more prone to banking crises, but less so when the rule of law and contract enforcement are strong. They provide suggestive evidence that liberalization lowers the franchise value of banks and encourages risk-taking behavior. They also find that financial liberalization has a net positive effect on economic growth, particularly in countries with initially repressive regimes (proxied by the presence of negative real interest rates), even if banking crises occur; the net benefits are less clear for countries with less repressive regimes.

The six remaining papers describe the liberalization experiences of selected countries. These country case studies are a mixed bag. The empirical analysis generally consists of tables and plots of descriptive statistics without much formal hypothesis testing. Nevertheless, they offer individual country details that may be of value to many readers.

Charles Wyplosz examines the financial restrictions and liberalization process in postwar Belgium, France, and Italy, which operated with relatively repressed financial systems even into the 1980s and were among the last European countries to remove capital controls on outflows. He interprets this experience as supportive of the view that domestic financial liberalization should be gradual, and that it should precede capital account liberalization. A contrasting case is offered by Korea, where Yoon Je Cho argues that poorly phased liberalization contributed to the country's 1997–98 financial crisis. In particular, mismatches between liberalizing short-term and long-term credit markets, bank and nonbank financial intermediaries, and between short-term and long-term capital flows weakened the financial system and contributed to the severity of the crisis.

Fernando Montes-Negret and Luis Landa analyze how interest rate spreads in Mexico fell with liberalization. However, the combination of macroeconomic instability and poor financial infrastructure lead to bank insolvencies and limited the extent of financial deepening. Fabrizio Coricelli contrasts the relatively successful reforms of advanced Eastern and Central European transition countries with the less successful experience of Russia and other former members of the Soviet Union. He attributes this difference to the more rapid financial liberalization process undertaken in the latter, where ongoing fiscal deficits and absence of contract enforcement led to demonetization of some economic sectors. James Hanson compares the rapid liberalization process in Indonesia with the more gradual approach of India. Ifran Aleem and Louis Kasekende discuss how Uganda's program of financial system liberalization widened bank interest rate spreads and lead to an increase of bad loans due to the adverse selection of borrowers willing to pay high borrowing rates.

All in all, the book makes an important contribution to discussions about the appropriate extent of financial sector reforms. Slowing down the pace of liberalization and avoiding a one-size-fits-all approach, as the book advocates, may indeed lessen the likelihood of crises and lower the costs of liberalization. However, there are some areas that remain insufficiently addressed. For one, it is unclear how much the banking crises that are associated with liberalization are due to the improper design of liberalization programs themselves as opposed to macroeconomic policy mistakes, such as overvalued exchange rates and implicit or explicit fiscal deficits. In addition, the focus of the book is almost all on the liberalization of controls on bank activity. This focus is justified to the extent that banks serve as the main intermediaries in the financial markets of most developing countries. Yet it would have been useful to know more about the relative development of bond and equity markets. Arguably a liberalization process providing a more diversified mix of channels for transferring funds from savers to borrowers might have resulted in more successful experiences. Lastly, the book highlights the importance of prerequisites for successful liberalization programs, such as the rule of law, contract enforcement, and improved prudential supervision. But how long can a country wait to attain these prerequisites to reduce risks to some acceptable level? On this there is no clear answer. Given the track record of financial repression, financial liberalization, sooner rather than later, still appears to dominate the alternative.

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I Health, Education, and Welfare

Human Well-Being and the Natural Environment. By Partha Dasgupta. Oxford and New York: