

Catherine Caufield

Masters of Illusion

The World Bank and the Poverty of Nations

Henry Holt, New York, 1997, xii + 432 pp., \$27.50 (cloth).

H.N. Ray

The World Bank

A Third World View

Indus Publishing, New Delhi, 1996, 302 pp., Rs. 450 (cloth).

World Bank-bashing has become a major hobby. Interestingly, many of its best-known practitioners have been women: Teresa Hayter, Cheryl Payer, Frances Moore Lappé, Patricia Adams, Susan George, and now the environmental journalist Catherine Caufield. Perhaps the Bank's behavior, less like that of an exploitative colonial governor and more like that of an overly concerned Victorian governess, has provoked these critics. *Masters of Illusion*, the very well-written book by Catherine Caufield, ranges from a vivid description of the undoing of the Swedish match tycoon Ivar Kreuger, who killed himself in 1932, via a history of many of the errors of the World Bank, to the latest activities of its current and most glamorous President, James Wolfensohn.

The author's complaints are numerous. Many projects that were launched under the banner of helping the poor made the rich richer. The debt crisis was the result of greedy lenders lending to profligate borrowers. The Bank prefers authoritarian regimes to democracies. Among her principal charges against the Bank are its violations of the environment.

Environmental errors

Under the Narmada Valley Development Plan, the Indian government was going to build the Sardar Sarovar Dam across the Narmada River. Caufield writes that "it will also take the land of at least 320,000 people, many of whom are the indigenous or tribal people known in India as *adivasi*." (A more correct figure would be a maximum of 225,000 people.) An independent assessment of the project's environmental impact that was commissioned by the Bank in 1991 stated that silting and salinization were likely to occur, destroying one of India's most lucrative fishing grounds, and that only half the irrigation water promised would actually be delivered. It also noted that already-constructed parts of the project had become ideal breeding grounds for malarial mosquitoes. The Bank pulled out of the project in 1992.

Then there are the Bank's much criticized transmigration projects. The Indonesian one ignored the facts that soils on the outer islands were poor; that the islands were already populated by tribal people; and that large-scale land clearing would devastate the island's soils, water supply, and wildlife.

When discussing the dominance in the Bank's thinking of GNP and the neglect of the environment, Caufield quotes with approval a former Bank economist, Herman Daly: "It doesn't do you any good to have thousands of highly educated petroleum engineers if

you've run out of oil." But good technologists have in the past, and will in the future, come up with substitutes for oil, such as energy from the sun, the wind, the waves, or nuclear fusion. Human capital is substitutable for natural capital. The question that nobody has raised is whether the ultimate limit may not be time—for it takes time to be ever more highly educated, and to acquire, absorb, and apply the growing body of knowledge.

Debt service

Caufield writes that "the hundreds of billions of dollars developing countries borrow from abroad each year are more than canceled out by the hundreds of billions they send back each year in debt service." This statement indicates that she misunderstands the purpose of borrowing. It is sensible to borrow only if the returns on the loan (private and social) are higher than the interest paid, and developing countries' higher repayments are made from higher incomes and output than would otherwise have been possible. It is, however, true that transferring money across the foreign exchanges and raising public revenue to service foreign loans can present additional problems for some developing countries that a domestic borrower would not face.

She asks, "Does it make sense for a country to borrow money from abroad in order to fund its efforts to improve housing, education, health, or population control? Will such investments, however desirable, produce enough money . . . to repay their cost?" It is odd that neither the author nor the Bank ever questions the production of beer or automobiles or television sets on grounds of their productivity. Since they are consumption goods serving the "sovereign consumer," they don't need any further justification; they are the final purpose of production. But education and health, which are at least as important and valuable as beer and automobiles, always seem to need a justification on productivity grounds.

Closing the gap

She repeatedly says that the gap between rich and poor has widened. She writes that "the developing world is getting poorer and poorer in relation to the rich countries" and that "the gap between rich and poor continues to widen." Not so. It may be asked whether it would matter if the rich countries were to grow faster, as long as the poor countries enjoyed an adequate growth rate, particularly, but not only, if the higher growth rate of the rich were partly responsible for the moderate growth rate of the poor. But the relative gap between poor and rich countries did not widen (though the absolute gap must widen for a time if the initial difference is great). GDP growth rates per head during 1965–80 and 1980–93 were 4.6 percent and 4.0 percent, respectively, in the developing world, and 3.9 percent and 1.6 percent, respectively, in the developed world. East and Southeast Asia (excluding China) grew annually by 3.7 percent, and China by 5.7 percent, between 1965 and 1989. Although the 1980s were indeed a time of regress for Africa and Latin America, poverty was reduced in the large countries of East, South, and Southeast Asia. (In China, for example, income per head grew by nearly 8 percent a year during this period.) Average annual growth of income per head was higher between 1980 and 1989 than between 1965 and 1980: 3.2 percent compared with 2.4 percent. The

percentage of the world's population whose countries enjoyed a growth rate of more than 5 percent grew from 10.6 percent in the earlier period to 33.2 percent in the later one.

The World Bank is the best institution in the world in terms of the proportion of its loans that goes to the poorest countries, far better in this respect than many bilateral aid programs. The trouble during the 1980s was that there was polarization: the proportion of people whose countries experienced average annual growth rates below 1 percent also grew. In Latin America and the Caribbean, and particularly in Africa, many people suffered from declining incomes. But the majority saw their lot improve in terms of real income per head (which increased, on average, from \$950 in 1960 to \$2,170 in 1990), and even more people benefited from increased life expectancy, decreased infant mortality, and the wider availability and improved quality of education.

According to the United Nations Development Program's *Human Development Report* for 1993, life expectancy in low- and middle-income countries was 46 years in 1960, compared with 63 years in 1990; infant mortality was 149 per 1,000 live births compared with 71 per 1,000; and the adult literacy rate was 46 percent, compared with 65 percent.

Many of the highly successful countries received massive loans and credits from the World Bank. Caufield tells vivid stories of the disasters and failures of projects, but none of the many successes. She ends her book by quoting the well-known epigram that development is "a matter of poor people in rich countries giving money to rich people in poor countries."

An insider's view

H.N. Ray was an Executive Director of the World Bank from 1980 to 1985 and a member of the Indian civil service. Unlike Caufield, who is a journalist, he is an insider; and unlike Caufield's narrative, which is easily read, his style is somewhat ponderous. In contrast to the complete absence of analysis in Caufield's book, Ray's—though it devotes much space to description—provides arguments. Where Caufield asserts, Ray reasons. Both authors discuss the Sardar Sarovar project, but Ray states that "it is the poor masses in the developing countries who will suffer the most because of the Bank's withdrawal from these multi-purpose projects." He is against yielding to pressure from environmentalists, whose policies, he believes, would hurt the poor. Not only has the Bank, in his view, fully justified its existence and "been an unqualified success," but its capital should be substantially increased. Whenever he comes up against a conflict, his recommendation is for a "proper balance."

Decentralizing the Bank

It is, however, surprising that Ray, who endeavors to present a Third World view, does not discuss the need for the Bank to decentralize and to permit its resident missions, preferably reorganized at a subregional level, to have more influence. He endorses only a recommendation of the 1992 Wapenhans Report (an internal Bank study of project performance that was chaired by former Bank Vice President Willi Wapenhans) that greater use be made of the resident missions for supervising the implementation, and advising on modification, of projects. Nor does he mention the more controversial need, particularly in Africa, for the Bank to manage some of the projects it helps to finance rather than pulling out when construction is finished, which, in my view, is when the Bank's full commitment becomes most important.

The Bank is surely too centralized. Only one-tenth of the staff are now located in the low-income countries. When the Bank

talked in the past of decentralization, it meant decentralization of the organization in Washington. In contrast, the U.K. Commonwealth Development Corporation only began to be an effective development agency when, under Lord Reith, it decentralized its activities to regional (not national) offices, which produced proposals for projects and submitted them to headquarters in London. When agency staff members live in the recipient country, have daily contact with local people, and carry on a dialogue with policymakers, the decisions they make about projects are far more likely to reflect social and political, as well as economic and engineering, considerations. It can also help to reduce the acrimony so often created by the conditionality attached to loans. Fortunately, it seems that current Bank policy is to decentralize staff and to aim at a substantial increase in the proportion of those living and working in the field.

Project management

The other omission from Ray's book is more controversial. It applies mainly to the low-income countries of Africa. We know that there are now more foreign experts in Africa today than there were under colonialism. Yet their impact on self-reliant development is small, if not negative. Here again, the Bank should learn a lesson from the Commonwealth Development Corporation, which is unique in that it not only lends to finance a project but also manages it initially, with a mandate to train local people and hand it over to them when they are ready. A manager's commitment, after all, is much stronger than that of a detached advisor. The charge of neocolonialism may be raised against using such foreign managers, but a genuinely multilateral institution, with a staff that is trusted to have the interests of the host country at heart, can escape such suspicions.

Turning to the management of the Bank Group (including the International Finance Corporation and the Multilateral Investment Guarantee Agency) itself, there has long been a demand for greater openness and transparency, less secrecy, and more accountability. If the member governments were to demand these as conditions and were to ask for performance targets, they would only be practicing what the Bank and the Fund have told their borrowers for years: conditionality is good for you.

Paul Streeten

Kimberly Ann Elliott (editor)

Corruption and the Global Economy

Institute for International Economics, Washington, 1997, xiv + 244 pp., \$20 (paper).

Corruption is in vogue nowadays. So is its study, which, coupled with the many interpretations and disparate forms of malfeasance that corruption encompasses, has resulted in an explosion of writings, from many perspectives, on the topic.

Views of different analysts on the worth of various approaches to combating corruption vary widely. Many diverse views are



represented in this concise book, *Corruption and the Global Economy*, which is the outcome of a conference on corruption hosted by the Institute for International Finance in April 1996. Arguments are presented by theorists, economists, lawyers, and even an insightful detective (Jules Kroll).

Following the introduction is a beautifully written chapter by Patrick Glynn, Stephen J. Kobrin, and Moisés Naím on the globalization of corruption. The synthesis of the global initiatives to combat corruption it provides is helpful, although the number of references to this theme in subsequent chapters of the book seems excessive. The stories this chapter includes of corruption in industrial countries puts the potentially sensitive North-South issue in perspective. Its discussion of the pitfalls and opportunities brought about by the explosion of technological wizardry in international finance—permitting market participants to move millions with a single mouse click—is timely. And its account of the role of the former U.S. Secretary of State, Warren Christopher, in pushing for the OECD's criminalization of international bribery is revealing—not least by suggesting that, in a field populated by skeptics and pessimists, the resolve of one person can make a difference.

Another remarkable story is that of the OECD's Working Group on Bribery in International Commercial Transactions, chaired by the Swiss official Mark Pieth, and how, following a legislative review requested by this group, the U.K. government recently unearthed the long-forgotten 1906 Prevention of Corruption Act, one closely paralleling the much-touted American Foreign Corruption Act of 1977. This discovery challenged the notion that the OECD's push for criminalization was just a U.S. exercise in extraterritoriality.

More broadly, however, the fact that the chapter on globalization leads this collection raises a key question about the essence of the corruption challenge. Most of the book sees corruption as an international trade and investment problem, with cross-border bribery being a prime concern. In addition to the focus on international initiatives in the introduction and both the first and the concluding chapters, there are contributions by Mark Pieth tracing the OECD's efforts, by Fritz F. Heimann on initiatives by the International Chamber of Commerce and on corporate compliance programs, and by Alan Larson on the U.S.

perspective on international corruption. While each contribution has significant individual merit—and some make fascinating reading—as a whole they may suffer from a fallacy of composition. Indeed, two commentaries, provided by Dani Rodrik and Vito Tanzi, question the premise that corruption ought to be seen mainly through an international trade and investment lens, suggesting instead that corruption be addressed as a development challenge.

To be sure, the domestic and developmental aspects of corruption are not absent

“Ultimately, . . . inroads into corruption will have to be made within afflicted countries by their own leaders and people.”

in this book. It is refreshing to read the account of Uganda's then Inspector General, Augustine Ruzindana, of specific anticorruption initiatives (in which he had a leadership role). Admirably, he places these institutional actions in the much broader context of political, economic, and administrative reforms that are still ongoing in his country. The chapter by Susan Rose-Ackerman, a pioneer in the academic study of corruption, presents the incentives to engage in corruption and discusses corruption's economic consequences in an analytically rigorous fashion, while Paolo Mauro presents his empirical findings on the harm corruption does to development (see his article, “Corruption: Causes, Consequences, and Agenda for Further Research,” in this issue).

Michael Johnston focuses on the political sources and effects of different kinds of corruption and lucidly looks at the social and political imbalances that arise from different political typologies of corruption, distinguishing between political and economic opportunities, and emphasizing the role of elites in different societies. He suggests various strategies for dealing with corruption under different political regimes, including ways in which democratic reforms can have a positive influence.

The substantial concluding chapter by Elliott emphasizes the international policy aspects and provides a long list of recommendations, including exhortations to the international financial institutions to do

more. There is also a presentation of empirical correlates with corruption, which may have been included to compensate for the reticence of earlier chapters (Mauro's is one exception) to make systematic use of data.

Though it has both the strengths and the weaknesses common to edited collections of articles, this book is required reading for anyone interested in corruption. It covers most of the first-stage issues that have been raised in the new anticorruption era. The first stage, which encompassed consciousness raising and initial mobilization of international support and of civil

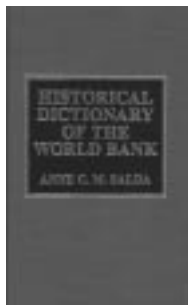
society, has been successful and is already giving way to the second stage—one of concerted action. Yet many political economy, institutional, and implementation issues still need to be addressed, and priority areas for further work need to be identified and followed up. Indeed, resolution of the more concrete second-stage issues will require innovative and analytically sound approaches incorporating

more extensive use of data, as well as developing conceptual frameworks within which to analyze corruption within specific countries and to design reform programs tailored to their needs. For instance, a more in-depth understanding of the politics of systemic corruption in particular countries is likely to lead to different (and at times counterintuitive) reform recommendations being made to them, compared with countries where corruption is widespread but not endemic.

The OECD's recent resolution encouraging criminalization of international bribery is a notable achievement, and undoubtedly its implementation by OECD member countries ought to be given high priority in the near future. Initiatives from international financial institutions will also be important. Ultimately, however, inroads into corruption will have to be made within afflicted countries by their own leaders and people. In most countries where the need to combat corruption is dire, the necessary work is either just getting started or has not yet begun.

Daniel Kaufmann





Anne C.M. Salda

Historical Dictionary of the World Bank

Scarecrow Press, Lanham, Maryland, xxiv + 281 pp., \$68 (cloth).

How is one to encapsulate, in 305 printed pages, fifty-plus years of the personal, political, institutional, and policy-making history of an organization as complex and diverse as the World Bank? Edward S. Mason and Robert E. Asher (*The World Bank Since Bretton Woods*, published by the Brookings Institution in 1973) needed 942 pages, and they covered only the first 25 years. The recent history by Devesh Kapur, John P. Lewis, and Richard Webb (*The World Bank: Its First Half Century*, published by Brookings in 1997) extends to almost 2,100 pages in two volumes and weighs in at seven and a half pounds.

The volume under review is clearly far more modest in its scope and ambition (and weight) than those, and is no less valuable for that. It deserves a permanent place in any World Bank briefcase. I wish it had been available to me during my career as the Bank's publisher, when I was from time to time called upon to address groups of various kinds about the growth and development of the institution. Thumbnail sketches of the Bank's country and sector policies, brief histories of country relations, and explanations of organizational and bureaucratic complexities and

affinities were at that time surprisingly hard to find. Anne Salda, who worked for more than twenty years in the joint World Bank-IMF library, has placed us in her debt by producing a clear and comprehensive reference work.

She begins with a useful chronology and a 23-page introduction that is a model of lucidity and compression. She covers the passing decades a page at a time and finds room for handy "speaker's notes" on the International Finance Corporation, International Development Association, International Center for Settlement of Investment Disputes, and Multilateral Investment Guarantee Agency. The dictionary proper begins with AIDS and ends with World Tables. In between are brief biographies of all nine presidents, discussions of sector policy (from agriculture to wildlife management), relevant United Nations agencies, and valiant attempts to explain such arcana as negative pledge clauses.

Nor does she avoid controversy. Entries on governance, the Narmada River project (listed under Sardar Sarovar), and Arun III (under World Bank Inspection Panel), for example, give judicious hints of some of the turmoil surrounding such issues and projects. But this is very much a librarian's book, drawn, as Mrs. Salda makes perfectly clear in the acknowledgments, largely from "official" sources. The bibliography occupies almost a fifth of the space, and one has to wonder whether it is really necessary, in this age of electronic retrieval, to list so many periodical articles, country studies, and discussion papers. The statistical appendix, confined as it is to subscriptions to the World Bank's capital stock, country

eligibility for borrowing, and lending totals by sector for 1994 and 1995, is of limited use.

The book is stronger on process than policy, on organization than analysis. President Barber Conable's 1987 reorganization, for example, is mentioned without a word about the reason for it—the refusal of the major shareholders to support the first budget Conable presented to the Executive Board. The Operations Evaluation Department's (OED) role and functions are admirably described, but there is no discussion of the trend of its findings over time. No link is shown between OED's findings and the growing emphasis, beginning with Lewis Preston's presidency, on implementation and effectiveness.

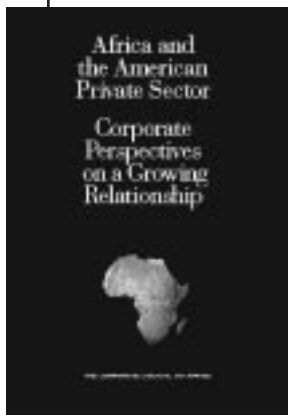
Aside from the nine presidents, personalities get short shrift. Lord Keynes is there, as one would expect, and Harry Dexter White, but the only officers of the Bank to be included are Aron Broches, Robert Garner, Eugene Rotberg, Ernest Stern, and Willi Wapenhans. The absence of an entry for Moeen Qureshi seems astonishing.

Lack of space cannot be adduced in mitigation. Books are customarily printed in multiples of 16 pages. Because this book's contents run to 305 pages, the publisher has left 15 blank pages at the end of the book—useful for making notes but not for much else.

While there are certainly elements of the book that might have been done better, it remains probably the most useful brief source on its subject, and that is a great deal to be thankful for.

James Feather

AFRICA AND THE AMERICAN PRIVATE SECTOR: CORPORATE PERSPECTIVES ON A GROWING RELATIONSHIP



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Ronald I. McKinnon and
Kenichi Ohno

Dollar and Yen

Resolving Economic Conflict between the United States and Japan

MIT Press, Cambridge,
Massachusetts, 1997,
x + 266 pp., \$39.50 (cloth).



much of the period. McKinnon and Ohno argue that the U.S. current account deficits are a reflection of that nation's propensity to invest more than it saves and are not very responsive to exchange rate changes. Chapter 7 is an incisive critique of the theoretical rationale and empirical estimates of the elasticities approach to the

trade balance, which the authors believe has been misapplied in the form of a proposition that currency depreciation, somehow engineered, can improve the trade balance.

Dollar and Yen's authors argue that the policy of what they call "the syndrome of the ever higher yen"—based on the elasticities approach—has trapped both countries in a distinctly suboptimal position. The authors maintain that, over time, the exchange rate reverts to its purchasing power parity (PPP) level. When the *nominal* exchange rate is used as a policy tool, the exchange rate forces national price levels to adjust in order to restore PPP. The U.S. economy, however, is still a relatively closed economy and, as such, U.S. prices are not very responsive to exchange rate changes. The Japanese economy, therefore, bears the brunt of relative price adjustment, imparting a deflationary bias to Japanese monetary policy. An issue that naturally arises in this context is why the Bank of Japan has validated this deflationary bias by tightening its policy stance. McKinnon and Ohno respond that the bank has done so to avoid the wrath of U.S. protectionists, although during episodes of particularly sharp yen appreciations, it has typically responded by easing.

The authors argue that the syndrome of the ever-higher yen and the associated deflationary bias of Japanese monetary policy have had several important implications. First, market participants—projecting that Japanese current account surpluses will persist into the future—have come to expect that U.S. pressure on the yen will periodically reappear and consequently incorporate these expectations into the term structure of interest rates. Thus, market expectations of this syndrome have caused U.S. long-term interest rates to exceed comparable Japanese rates by between 3 and 4 percentage points since the late 1970s. Second, the deflationary policy forced the Bank of Japan into unwanted deflation beginning in the mid-1980s.

McKinnon and Ohno link the Japanese downturns of 1985–86 and 1993–95 to their thesis that U.S. commercial policy exerted unwarranted pressures on the Bank of

Japan to maintain overly restrictive policy stances in 1985 and 1993. The asset bubble of 1986–87 represented the bank's overcompensation in the opposite direction in order to spring the economy loose from the earlier downturn. The collapse of the asset bubble, McKinnon and Ohno argue, contributed to the U.S. credit crunch and cyclical downturn of 1991–92.

In addition to asserting that managed exchange rates imparted a deflationary bias to Japanese monetary policy, McKinnon and Ohno ascribe the slowdown in world economic growth in the managed floating era, relative to that seen under the Bretton Woods regime, to what they perceive to be the excess volatility, misalignment, and long-term drift inherent in floating exchange rates. The solution they prescribe is the adoption of target zones (with ± 5 percent bands) for the U.S. dollar, the yen, and the deutsche mark (or the euro). Unlike John Williamson's target-zone proposal, which aims to stabilize real exchange rates through frequent adjustments of the nominal exchange rate, McKinnon and Ohno propose to permanently stabilize the nominal rate through sterilized intervention (with some adjustment of relative interest rates). The central rate would be based on the initial purchasing power parity that aligns wholesale price levels. McKinnon and Ohno recognize that a number of conditions, not the least of which is the absence of asymmetric business cycles, need to hold in order for their proposal to be successfully implemented. Chapter 11, written in early 1997, deals with the recent depreciation of the yen against the dollar and asks whether this marks a sustainable departure from the syndrome of the ever-higher yen. The authors think not, but subsequent events will shed much light on the matter of whether the conditions for their target-zone proposal are in place in today's highly integrated, but diverse world.

George S. Tavlak

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Hiroyuki Odagiri and Akira Goto

Technology and Industrial Development in Japan

Building Capabilities by Learning, Innovation, and Public Policy

Oxford University Press, 1996, xiii + 309 pp., \$75 (cloth).

Japan was the first non-Western economy to industrialize. The broad outlines of its remarkable transition from a poor agricultural society in the 1850s to a major industrial power by the 1970s are widely known. What has been less widely acknowledged, however, are the details of how Japan managed the transition. Hiroyuki Odagiri and Akira Goto's book admirably fills this gap in the literature.

The authors' main thesis is that Japan succeeded in developing because it was particularly adept at importing technology from abroad. Following its isolation during the Tokugawa shogunate period, and again after World War II, the country found itself behind the West in technology. By importing and adopting technology from the United States and Europe, Japan managed to achieve faster growth rates than were seen anywhere else.

Importing best practices is easier said than done. Odagiri and Goto argue that a

country must have the following four ingredients to effectively import foreign technology. First, it must have a deep pool of engineering talent. Second, funds must be available to send delegations of engineers and technicians overseas, hire foreign technical advisors, and license foreign-owned patents. Third, the country must have a group of entrepreneurs who can discover and take advantage of profit opportunities. Fourth, and most controversial, a company started with foreign technology should be given a reasonable chance of attaining a high level of profitability—usually by being granted a monopoly for one or more products.

Surprisingly, since Japan is often mentioned by other economic historians as a country where state-led development was important, Odagiri and Goto downplay the Japanese government's role in fostering the importation of technology. According to the authors, the following were the Japanese government's main contributions. First, it helped negotiate the terms of the technology importation with foreign companies. (The competition among Japanese firms to obtain technology was so intense that the royalty rates would otherwise have skyrocketed.) Second, it introduced preferential tax measures to encourage technological importation. Third, it restricted the market access of foreign companies by

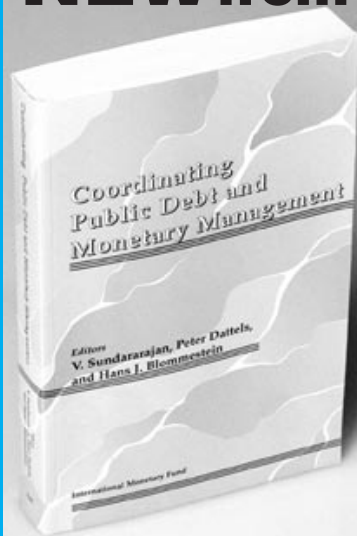
formal and informal means—a domestic firm with a license to use foreign technology therefore had little foreign competition and usually was able to earn high (monopoly) profits.

The authors devote six chapters to case studies of the following industries: textiles, iron and steel, electrical and communications equipment, automobiles, shipbuilding and aircraft, and pharmaceuticals. These chapters are the best part of the book. From them, we learn—for each industry—how the relevant technology was imported, adopted, and perfected. Except for aircraft and pharmaceuticals, Japan managed to improve upon the imported technology in all of these industries.

So much of the current writing about Japan starts with the close of World War II. It should not be forgotten, however, that Japan had already achieved rough technological parity with Western countries before the war began. This book provides the most detailed account and analysis of Japanese technological development in the century after the Meiji restoration of 1868. Learning about the technological development of Japan is important because it enables us to better understand not only that country's economic history but also how economic development takes place.

Robert Dekle

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Coordinating Public Debt and Monetary Management: Institutional and Operational Arrangements

Edited by V. Sundararajan, Peter Dattels, and Hans J. Blommestein

This book examines issues and practices in the coordination of monetary and public debt management, drawing on the experiences of both developed and developing economies. It emphasizes the importance of appropriate design and management of institutional and operating arrangements, particularly in economies liberalizing their financial systems.

US\$27.00. Available in English. (paper). ISBN 1-55775-555-8. xix + 419 pp. 1997.

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