REVIEW ESSAYS

IS THE DRIVE TOWARD FREE-MARKET GLOBALIZATION STALLING?

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THE ALLURE OF THE FOREIGN: IMPORTED GOODS IN POSTCOLONIAL LATIN AMERICA. Edited by Benjamin Orlove. (Ann Arbor: University of Michigan Press, 1997. Pp. 226. $42.50 cloth.)

DEVELOPING NATIONS AND THE POLITICS OF GLOBAL INTEGRATION. By Stephan Haggard. (Washington, D.C.: Brookings Institution, 1995. Pp. 178. $28.95 cloth, $10.95 paper.)

EXCHANGE RATE PARITY FOR TRADE AND DEVELOPMENT: THEORY, TESTS, AND CASE STUDIES. By Pan Yotopoulos. (New York: Cambridge University Press, 1996. Pp. 323. $54.95 cloth.)

GLOBAL CHANGE, REGIONAL RESPONSE: THE NEW INTERNATIONAL CONTEXT OF DEVELOPMENT. Edited by Barbara Stallings. (New York: Cambridge University Press, 1995. Pp. 410. $59.95 cloth, $17.95 paper.)

GLOBALIZATION, URBANIZATION, AND THE STATE: SELECTED STUDIES ON CONTEMPORARY LATIN AMERICA. Edited by Satya R. Pattnayak. (Lanham, Md.: University Press of America, 1996. Pp. 257. $52.00 cloth, $32.00 paper.)

LATIN AMERICA IN THE WORLD ECONOMY. Edited by Roberto Patricio Korzeniewicz and William C. Smith. (Westport, Conn.: Praeger, 1996. Pp. 280. $65.00 cloth, $24.95 paper.)

LATIN AMERICA'S NEW INSERTION IN THE WORLD ECONOMY. Edited by Ruud Buitelaar and Pitou Van Dijck. (London: Macmillan, 1996. Pp. 258. $65.00 cloth.)

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LESSONS IN ECONOMIC POLICY FOR EASTERN EUROPE FROM LATIN AMERICA. Edited by Gary McMahon. (New York: St. Martin's, 1996. Pp. 256. $59.95 cloth.)

MOBILE CAPITAL AND LATIN AMERICAN DEVELOPMENT. By James E. Mahon Jr. (University Park: Pennsylvania State University Press, 1996. Pp. 212. $45.00 cloth, $17.95 paper.)

REGIONALIZATION IN THE WORLD ECONOMY: NAFTA, THE AMERICAS, AND ASIA PACIFIC. Edited by Van R. Whiting Jr. (Delhi: Macmillan India, 1996. Pp. 310.)

THE TOBIN TAX: COPING WITH FINANCIAL VOLATILITY. Edited by Mahbub ul Haq, Inge Kaul, and Isabelle Grunberg. (New York: Oxford University Press, 1996. Pp. 318. $40.00 cloth, $21.00 paper.)

Globalization is a protean concept that encourages rhetorical excess regarding its speed and scope. Thus Gary Gereffi remarks in *Global Change, Regional Response*, "As almost every factor of production—money, technology, information, and goods—moves effortlessly across borders, the very idea of distinct U.S., German, or Japanese economies is virtually meaningless" (p. 101). But globalization also has identifiable economic and political dimensions that allow one to confront rhetorical excess with actual data on speed and direction and to uncover problematics embedded in the interactions of political, technological, and economic forces driving the process. Using Gereffi's exuberant comment as a taxonomic crutch, I will first show that globalization in the past quarter-century has accelerated in finance and in the spread of market-liberalizing policies but has decelerated along most other economic dimensions.

Economic and Policy Trends of the Past Quarter-Century

Let us turn first to money, which has unquestionably been flowing across borders at an accelerating pace following the breakup of the Bretton Woods system in the early 1970s. Foreign-currency trades per annum rose globally from U.S. $4.3 trillion (that is, thousand billions) in 1977 to U.S. $307.5 trillion in 1995 (Felix 1997–1998, t. 1). But money as a "factor of production" is a shaky metaphor. There is no stable covariance either in economic theory or in the real world between changes of the stock of money and the output of goods and services. The explosive growth of international currency flows during the past two decades scarcely diminished the close correlation between domestic savings and investment that prevailed within the countries belonging to the Organisation for Economic Cooperation and Development (OECD) in the 1960s (Feldstein 1994). Meanwhile, gross fixed-investment growth slowed substantially in all these countries after the 1960s (Felix 1997–1998, t. 5). Foreign direct investment has accelerated since the 1970s but chiefly to acquire privatized

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public assets and to carry out cross-border corporate mergers and takeovers in the first and third worlds. That is, the acceleration has mainly involved increased cross-border purchasing of existing productive capacity rather than increased construction of new capacity.

The notion of "effortless" cross-border movement of goods is harmless rhetorical overkill when referring to ongoing improvements in the speed and costs of moving goods. But it is totally misguided when referring to trends in the actual volume of internationally traded goods. In the past twenty-five years, the growth rates of both OECD and world export volumes have averaged well below those of the 1960s. The ratio of exports to gross domestic product (GDP) has risen since the 1960s, but that trend reflects economic involution as well as increased economic interdependence: output growth slackened more than export growth (Felix 1997–1998, tt. 3–4).

Have the rates of technological innovation and cross-border diffusion been accelerating? No reliable direct measures exist for answering these questions, but the indirect evidence is strongly negative. Labor and total factor-productivity growth of the OECD countries, globally the chief generators of technological innovation, have dropped far below their 1960s averages (Felix 1997–1998, t. 6). And the U.S.-led pressure to enforce its standards of intellectual property rights on third world countries by raising the price of technology transfers can hardly be accelerating the cross-border diffusion of technology.

In sum, the reality behind the perception that economic globalization has been accelerating is to be found not in performance but in policy and doctrine, where a sea change has indeed occurred since the 1960s. The change has moved from policies requiring an expansive economic role for the state, underpinned in capitalist countries by Keynesian doctrine and loosely coordinated by the Bretton Woods Accords, to a post-1960s global push to liberalize markets and expand their domain by diminishing the state's economic functions, for which doctrinal rationalization was supplied by Milton Friedman, Friedrich von Hayek, and their disciples.

The main objective of the Bretton Woods Accords was to restore multilateral trading, convertible exchange rates, and private-capital movements and to reduce tariffs and nontariff barriers. Implementation was to be constrained, however, by two key side conditions: the need to maintain stable exchange rates and full employment. Stable exchange rates required, according to Keynesian doctrine, controls over cross-border capital flows. Article 6, Section 3, of the International Monetary Fund's charter thus allows member countries to keep such controls and authorizes the IMF to cut off credit lines if used to finance capital flight.[1] To pro-

1. Section 3 waters down a tougher draft version initially approved by the British and U.S. delegations, which would have required member governments to collaborate in tracking down and repatriating flight capital. That requirement was deleted in the final version following heavy lobbying by Wall Street firms. For details, see Helleiner (1994).

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tect employment, members were also authorized to raise tariffs temporarily or to adjust their exchange rates semi-permanently when persistent external imbalances blocked the effort.

In response to decolonization and cold war competition, a third de facto qualification was added later. Newly industrializing countries could protect their economies from the full blast of international competition by delaying exchange-rate convertibility and trade liberalization until they had substantially reduced the gaps in labor, managerial, and technological skills, industrial experience, and other crucial determinants of economic growth separating them from their first world trading partners.

The change of doctrine and policy after the 1960s centered on rejecting all three side conditions. Doctrinally, they were denounced as sources of market distortions that retard economic growth. Attempts to stabilize nominal exchange rates exacerbated the volatility of real exchange rates, encouraging speculative inflows and capital flight. Liberating exchange markets and removing capital controls would, in contrast, allow fluctuating nominal rates to stabilize real exchange rates, curbing inducements to capital flight. Because the self-adjusting properties of markets allegedly ensure that full employment is a normal condition of free-market economies, active full-employment policies are otiose at best and detrimental at worst. In a world in which capital is allowed to move freely, developing countries need merely stabilize the price level, enforce property rights, and "get relative prices right" by liberating their goods and financial markets, and foreign capital and enterprise will flow in to fill development gaps.

Disconnects between Neoliberal Doctrine and Policies

The momentum of policy implementation lagged behind doctrine, reaching its apogee in the 1980s. Waylaid by political and economic realities, implementation also tended to be incomplete and doctrinally impure. This condition allowed defenders to blame implementation rather than doctrinal flaws for the poor results and to urge redoubling of effort rather than the reassessing of policy direction. But as poor results persist and now encompass rising exchange-rate volatility, misaligned real rates, an embarrassingly high incidence of systemic bank crises,[2] chronically high

2. An IMF study reported that 36 of its 181 members experienced one or more banking crises and 108 others had one or more periods of "significant banking problems" between 1980 and 1995. *Crises* are defined by the study as "cases where there were runs or other substantial portfolio shifts, collapses of financial firms, or massive government intervention." *Significant problems* refer to "extensive unsoundness short of a crisis" (Lindgren et al. 1996, 20). The Latin American–Caribbean region ranked above average: twenty countries had one or more banking crises or significant banking problems during 1980–1995, with Argentina, Bolivia, and Mexico suffering multiple occurrences. The OECD countries were also somewhat above the global average, three-quarters of them having crises or "significant banking

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unemployment, and rising inequality of income and wealth in both the first and third worlds, doctrinal purity itself is being adulterated with caveats that resemble the Bretton Woods side conditions.

The Tobin Tax: Coping with Financial Volatility, edited by Mahbub ul Haq, Inge Kaul, and Isabelle Grunberg, consists of essays exploring James Tobin's proposal to curb speculative short-term capital flows and reduce exchange-rate volatility by levying a globally uniform small tax on exchange transactions. The contributions focus mainly on first world problems with financial volatility. Most accept in whole or part the Bretton Woods theses that exchange-rate volatility deters international trade and that free-capital mobility destabilizes real as well as nominal exchange rates. The contributors diverge mainly over how to structure the tax and handle evasion problems as well as over the extent to which the tax could dampen exchange-rate volatility. This first comprehensive examination of the tax by prominent economists represents a sea change from the profession's reaction when Tobin, an unrepentant Keynesian, first advanced it in the 1970s. Then, in his words, "It fell like a rock."

Concern over rising financial volatility is also modifying the doctrinal backing for the neoliberal reforms that Washington-based international financial institutions (IFIs) have been vigorously urging on third world countries. The revisionism holds that thin financial markets, a structural feature of developing economies, require tighter financial controls than are needed by first world economies. This conclusion partially validates Bretton Woods's third side condition. For example, Sebastian Edwards's "Comments" in *Developing Nations and the Politics of Global Integration* holds up Chile as both an exemplar of neoliberalism and a model of how to reduce financial turbulence by controlling short-term capital flows.

Recent studies by IFI economists also underpin the revisionism. One study of a large sample of mainly third world countries found a strong positive correlation between the liberalization of domestic financial markets and the frequency of banking crises (see Kaminsky and Reinhart 1996). A second study concluded that imposing stringent capital-to-risk ratios on banks, which OECD bank regulators have been relying on to control bank failures, will not work in Latin America because concentration of wealth and income in few hands and thin equity markets make it easy to evade such controls by insider deals that distort the balance sheets of banks and their owners (Rojas-Suárez and Weisbrod 1996). The criticism that increasing reliance by central banks and the IFIs on expensive bank bailouts to stanch financial crises in first and third world countries encourages more risky financial behavior now shows up prominently in academic and semi-official conferences on financial globalization and its problems.[3]

problems" during 1980–1995 (Lindgren et al. 1996, t. 2). The global average, 73.5 percent, has since been raised by the current financial crises afflicting the ASEAN region and South Korea.

3. For a very recent example, see David Wessel, "Central Bankers and Economists Ponder

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Nevertheless, the United States, the G-7,[4] and the IMF all continue campaigning to remove the remaining controls on free capital mobility. The managing director of the IMF still wants to replace Article 6, Section 3 of the IMF's charter with the requirement that member countries make their currency freely convertible for capital as well as current-account transactions. Interviewed during the 1992 crisis in Europe's exchange-rate mechanism, a top official of the Bundesbank replied angrily to a question about the Tobin tax, "Oh, that again. It's the Loch Ness Monster popping up once more!" Interviewed on East Asia's current crisis, Lawrence Summers, U.S. Undersecretary of the Treasury, worried that it might set back the globalizing of capital's freedom to move.

This divergence between economists at the sherpa level and the policy setters of official financial institutions may reflect a normal lag between doctrinal reassessment and policy revision. More probably, it reflects the dominance of power over doctrine. As a Harvard economist, Summers had written articles dissecting financial-market misbehavior and promoting a tax on financial transactions to reduce asset price volatility. His epiphany on assuming a high U.S. Treasury position stems more likely from encountering political realities than from errors in his economic analysis.[5]

The eleven monographs and edited volumes under review here treat doctrine and policy selectively. Because the political, ideational, and economic forces shaping national economic policies and global economic integration operate along many dimensions, selectivity is unavoidable, although it also has its price. Neglected aspects of a complex process emerge after publication to confound generalizations. Too many of the studies under review ignore or underestimate the destabilizing potential inherent in free capital mobility or the point that it is a threat to first as well as third world economies.

On the Main Motives Impelling Market Liberalization and Integration in the Third World

To their supporters, trends toward market liberalization and integration have been motivated primarily by the realization in third world countries that free-market development strategies are inherently more effective than protectionist and statist ones (for an example, see Edwards's

Lessons of Thailand's Financial Crisis," *Wall Street Journal*, 2 Sept. 1997, p. A2. Wessel was reporting on a recent conference organized by the U.S. Federal Reserve, where the moral hazard problem was prominently discussed.

4. The G-7 is an official consulting group of major industrial economies consisting of Britain, Canada, France, Germany, Italy, Japan, and the United States.

5. For Lawrence Summers's academic views on financial-market misbehavior, see De Long et al. (1989). On the financial-transaction tax, see Summers and Summers (1989).

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"Comments" in *Developing Nations and the Politics of Global Integration*). This view, however, is contested by a number of the books and articles under review.

In *Developing Nations and the Politics of Global Integration*, Stephan Haggard argues that external extra-market pressure has been the dominant force, using the distinction between "shallow integration" and "deep integration" to elaborate on this point. Shallow integration refers to the "relaxation of border restrictions on trade and investment and the granting of national treatment for products and firms." Deep integration occurs when "numerous 'behind the border' policies—once deemed wholly domestic—become the subject of international negotiations" (p. 2).

Deep integration, Haggard contends, is mutually beneficial when negotiated among economies of similar levels of skills, technological prowess, and economic bargaining power because integration is then likely to be based on compromises over rules and enforcement mechanisms that accommodate equitably the differing national interests of the negotiating countries. Between developed and less-developed economies, however, the power relations are asymmetrical, and in Haggard's opinion, "there are both economic and political reasons to think that the deep integration agenda would be neither germane nor agreeable to developing countries. . . . In areas such as intellectual property, the environment, and labor standards, developing countries could suffer if harmonization occurred around the norms of developed countries, particularly if the convergence is enforced through sanctions" (p. 4).

Haggard contends that the "deep integration agenda" being pushed on developing countries is an extension of power (primarily by the United States) that reflects "growing corporate interest in exports and investment opportunities in the developing countries" that "resulted in U.S. trade policy shifting toward an emphasis on opening foreign markets. The threat of sanctions became an instrument not only for reducing traditional trade barriers but also for forcing broader regulatory changes favorable to American firms. . . . The willingness of developing countries to entertain the deep integration agenda can only be understood in light of powerful external economic and political constraints that operated on them during the 1980s" (p. 7). The debt crisis created strong incentives for policy changes to "regain access to foreign investment and borrowing." The international financial institutions were important instruments for effecting the policy change because the debt crisis greatly increased their financial clout over heavily indebted developing countries. The IFIs "widened dramatically" their conception of conditionality: "In effect, conditionality became a route to deeper integration" (p. 7).

Asian countries, less debt-ridden and less under the thumb of the IFIs than the Latin American countries, have therefore been liberalizing more slowly and selectively. Nevertheless, with unilateral resistance be-

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coming increasingly difficult, they are falling back on multilateral compacts as an additional defense. Haggard explains, "As trade grows, and the trade policies of the advanced industrial states become more erratic, the advanced developing countries have come to see GATT and the new WTO [World Trade Organization] as offering 'protection against protection.' The price to be paid . . . is an acceptance of the expanded policy agenda of the advanced industrial states, and of the United States in particular" (p. 111).

Haggard is especially caustic on NAFTA: "The lessons to be drawn from NAFTA . . . about the political economy of deep regional integration schemes are sobering. . . . The concessions made by Mexico to American demands were sweeping and revised upward at the last minute in order to secure support from opportunistic American legislators. NAFTA makes clear that regionalism does not obviate the basic dilemma of multilateralism and may even accentuate it. . . . [T]he weaker party to the regional agreement will also make the greater concessions and adjustments" (p. 113).

The essays brought together by Barbara Stallings in *Global Change, Regional Response: The New International Context of Development* agree with Haggard that the United States has been the main force pushing market liberalization and "deep integration" on the developing countries and that debt-ridden Latin American countries have been more submissive than Asian countries. The authors view hegemonic integration pressures more selectively than does Haggard, however. Developing countries geographically placed to integrate with Japan or the European Community (EC) are treated better than those in the U.S. orbit, according to Barbara Stallings and Wolfgang Streeck. They argue in "Capitalism in Conflict? The United States, Europe, and Japan in the Post–Cold War World" that Japanese communitarianism and continental Europe's social democracy assign a greater role to the state as allocator of resources and protector of distributional equity than does the individualism underpinning Anglo-Saxon capitalism. Japan and the EC countries will therefore continue to rely more than the Anglo-Saxons on government coordination of markets, finance, and risk-bearing in the international competition over market shares and will resist conforming to the Anglo-Saxon model. They will also remain more tolerant of developing countries in their orbit who pursue state-guided growth-with-equity policies, which Stallings and Streeck find more appropriate for developing economies than the neoliberalism favored by the United States. These analysts do not expect the hegemonic differences to produce semi-closed regional blocs, but they foresee regional ties strengthening, with developing country benefits accruing mainly to those tied to Japan or the EC.

The Stallings-Streeck position on regionalism is embellished by most of the other contributions to *Global Change, Regional Response*. Of these, Yun-han Chu's "The East Asian NICs: A State-led Path to the De-

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veloped World" stands out in its sophisticated, fact-filled analysis of the domestic and external political and economic factors shaping Korea's and Taiwan's largely successful implementation of dirigiste (state-led) development strategies. Also of interest to devotees of comparisons between Latin America and Asia is the prescient essay by Linda Lim, "Southeast Asia: Success through International Openness." Despite the rapid growth of the ASEAN countries (the Association of Southeast Asian Nations), Lim identifies two major flaws in their development approach: their investment in primary and secondary schooling is inadequate; and they rely excessively on technology, capital, and enterprise provided by multinational corporations (MNCs) and the network of agile family-run conglomerates of overseas Chinese dominating the non-MNC sectors of ASEAN commerce and industry. In recent years, these conglomerates have been moving their labor-intensive, low-tech operations to mainland China, slowing ASEAN export growth and requiring increased reliance on foreign borrowing to cover expanding current-account deficits.

Fred Halliday in "The Third World and the End of the Cold War" is the contrarian in *Global Change, Regional Response*, downplaying the importance of regional differences. The collapse of the Soviet Union, Halliday contends, has eliminated the space for autonomous statist development. The road is now clear for free-wheeling capitalism to complete the historic role assigned it by classical Marxism: that of transforming the world in its own image. Capitalism's longer-term prospects, however, will depend on whether globalized free-wheeling capitalism can diffuse prosperity and reduce the gap between richer and poorer states. The jury is still out on the answer.

Regionalization in the World Economy: NAFTA, the Americas, and Asia Pacific offers a more positive, if still mixed, assessment of the deep integration agenda of the United States. Some of the essays view regional trade and investment compacts as way stations on the road to full global integration, with NAFTA as a pacesetter. In "Regional Integration: The Relevance of NAFTA and APEC for India," Dae-Won Choi, S. W. R. Samarasinghe, and Van Whiting Jr. even advise India on how to join NAFTA, although they offer no evidence of Indian interest in doing so. Sidney Weintraub's "The Meaning of NAFTA Seen from the U.S." is more reserved. NAFTA is a promising first step but falls short of true integration. Weintraub recommends deepening integration among the three current members before "widening" the agreement by adding new Latin American members: "Deepening will require even more sharing of sovereignty, and this surely will increase Mexico's influence over American and Canadian discussions that affect Mexico" (pp. 86–87). He anticipates considerable U.S. and Canadian resistance to this idea, even if liberating intraregional migration (which Weintraub rules out as a certain nonstarter) were excluded from the agenda.

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Other contributions voice additional reservations about the gains in socioeconomic welfare from regional integration. Two view NAFTA's automotive regimen as an exclusionary instrument of Detroit in its rivalry with Japanese competitors. Ippei Yamazawa (in "Economic Integration in the Asia Pacific Region: A Japanese View") and Hadi Soesastro (in "APEC and the Asia Pacific: An ASEAN Perspective") report that Japan and the ASEAN members of APEC (the Asia Pacific Economic Cooperation Council) have been fending off suggestions from U.S. and Latin American members that APEC be converted from a loose consultative body into a regional free-trade agreement (FTA). Japan objects to giving up unconditional most-favored-nation treatment of its trading partners for the conditional most-favored-nation status that the FTA would require. The ASEANs, who have formed their own free-trade agreement, object because the "vast disparities in income, technology, and skill level among the APEC economies could lead to asymmetrical dependence, heightened tension, and North-South polarization within APEC" (Soesastro, pp. 257–58).

Nevertheless, the concluding essay by editor Van Whiting Jr., "Multiple Identities, Nested Sets, and Principles of Policy: Prospects for Regionalization in the World Economy," dismisses critics with an astonishing display of cheerleader rhetoric. These sentiments are built on a distinction between "old" and "new" regionalism and a misreading of key facts. According to Whiting,

> The old regionalism emphasized the political advantages of contiguous communities of states [with] similar cultures and similar *competing* endowments and levels of development. . . . The new regionalism emphasizes trade and investment communities based on economic advantages of contiguous markets augmented by the *de facto* communities of trading partners. Members of regions are more likely to have diverse and *complementary* endowments and levels of development. [Whiting's emphasis]
>
> The most notable outcome of this shift is that Latin America is no longer an economic community, though it subsists as a political and cultural community. In its place . . . , we observe North and South America nested within the Americas and, with the exception of Brazil, nested within Asia-Pacific. The diversity of the countries and cultures of Asia-Pacific contrasts with the relative homogeneity of earlier associations, from the European Community to the Andean Pact.
>
> The new regionalism holds the potential to benefit consumers as well as producers, the developing as well as the developed, the small as well as the big, the poor as well as the rich. (Pp. 286–87)

Latin America, of course, has never formed an economic community. Historically, the main economic links of Latino countries have been with Europe or the United States, not with each other. The EC is the only case thus far of successful deep integration, with Mercosur the most promising example to date of a Latin American subregional community in formation. Both are integration schemes between contiguous countries at similar levels of development, that is, examples of old regionalism. The ef-

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fusive welfare assessment of new regionalism calls to mind Anatole France's sardonic observation about equality before the law: "The Law in its majesty forbids the rich as well as the poor to steal bread and sleep under bridges."

Indeed, the deep-integration agenda of the United States does not conform well with the policy conclusions of Heckscher-Ohlin trade theory, the canonical theory central to neoliberal doctrine. According to this theory, when trading partners have equal access to a common set of technologies with minimal economies of scale and have similar labor quality, each country can maximize its welfare gains from trade by unilaterally liberalizing its markets for traded goods. Each country should welcome export subsidies by its trading partners as further improving its own terms of trade. The crucial assumptions rationalizing such advice are that full employment prevails and that market forces, assisted when needed by government policy, will ensure a broad sharing of adjustment costs and gains. Free-trade agreements may be desirable as barriers against dumping and other predatory tactics that raise adjustment costs, but unconditional most-favored-nation treatment of third parties should be part of all FTAs.

The U.S. agenda deviates from this policy line. It seeks FTAs that include members well below it in technological capability and labor and managerial skills. The United States wants members to abandon export subsidies and to alter policies, practices, and institutions, however longstanding, that hinder member firms from selling and investing freely in each other's markets. The U.S. agenda calls for MFN treatment to be made conditional on equivalent concessions from third parties. From the perspective of Heckscher-Ohlin theory, the national socioeconomic benefits become problematic even among countries at the same level of technology and human capital. Reciprocally lowering import duties would be welfare-enhancing, but retreating from unconditional MFN treatment of third parties would be welfare-reducing. Abandoning export subsidies would, by removing an allocative distortion, benefit the countries giving up the subsidies but would lower the terms of trade of partners who had not subsidized their exports. Promoting foreign investment is pointless because trade substitutes for factor movements, while including changes in domestic policies, practices, and institutions undermines the welfare exercise by upsetting the constancy of the institutional base on which Heckscher-Ohlin theory erects its apparatus for making judgments about welfare. This base is further undermined if the free-trade agreement brackets economies that differ greatly in technological capability and labor quality.

Abandoning the premise of full employment allows Keynesian theory to fill in part of the puzzle. When full employment is a goal rather than a premise, promoting a free-trade agreement that expands U.S. exports and removes export subsidies of trading partners is job-creating for the United States, if not for the trading partners. But Keynesian theory cannot

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fill in another part of the puzzle. If job creation is at issue, why would the U.S. agenda place such heavy stress on expanding foreign investment by U.S. firms?

Narrow interest politics is an inadequate explanation because freer access to investment opportunities abroad is intended for the full spectrum of U.S. firms. This intention gives a Marxist tinge to the assessment of welfare gains and losses, for the export of capital tends to raise its rate of return by enlarging the investment field and strengthening capital's bargaining power over labor. The welfare objective reduces from nation to class. But the U.S. economy remains wide open to foreign capital, which dilutes the Marxist tinge, unless one globalizes capital's community of interest, as Fred Halliday does in his essay.

The editors of *Latin America in the World Economy*, Roberto Korzeniewicz and William Smith, tackle this issue in their introductory chapter from a quasi-Marxist perspective, using Immanuel Wallerstein's world systems framework. The framework, however, postulates that capitalism, driven by the "logic of accumulation" (that is, reinvested profits) and by the "logic of rule" (that is, the need to control national economic policy and protect institutional rules of the game favorable to accumulation) has been a global phenomenon since the sixteenth century. Wallerstein's framework with its two "logics" may facilitate description of the changing forms of capitalism as it evolved in different times and places, but it is too amorphous for extracting causal generalizations. Thus the chapter has little to say on whether neoliberal restructuring in Latin America has been driven more by global or regional or domestic capitalist dynamics.

Mobile Capital and Latin American Development by James Mahon Jr., which deals with the political economy of capital flight, is meatier. Its basic thesis is that asset markets in Latin America are "virtual senates . . . where a narrow, internationally oriented elite of households and firms is 'represented' and wields a veto over economic policy," disciplining governments to protect asset prices and block populist reforms by threatening capital flight. Mahon asserts that the elite's "political power does not depend on conspiracy or even deliberation. . . . [I]t is based on the rule of one dollar equals one vote" (p. 23). The dominance, moreover, is largely impervious to formal democratizing of political institutions or to reforms requiring greater transparency of political and market transactions. In Mahon's view, "The main problem . . . is that where wealth is very highly concentrated, the very actors who constitute the market are those who enjoy lots of informal access to politicians and judges. If this is so, there would be little reason for such markets to demand that the state exercise power transparently and impersonally" (p. 158). This condition held during the eras of *crecimiento hacia afuera* and import-substitution industrialization (ISI). Reinvigorated by the post–Bretton Woods decontrol of financial markets and financial globalization, it is likely to prevail into the indefinite future.

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In elaborating his thesis, however, Mahon also finds it necessary to modify its starkness. A basic reason is that his estimates show capital flight to be a major and chronic feature in Argentina, Mexico, and Venezuela, somewhat less important in Brazil, and less severe in Chile and Colombia. Mahon's explanation of the variance is built around enduring interest-group divergences over exchange-rate and credit policies, in which populism is a participant as well as a threat.

Mineral and agricultural exporters favored cheap credit, an undervalued real exchange rate, and exchange-rate convertibility, which required periodic readjusting of the nominal exchange rate by devaluation. The ISI sector, protected by other means, favored cheap credit, an overvalued real exchange rate, and exchange controls rather than devaluation to handle exchange shortages. Its position was backed by unions and populist movements because that would keep down the relative prices of consumption goods. Finance capital favored a freely convertible and stable nominal exchange rate, with tight credit and high interest rates to stabilize the exchange rate. When the exporting sector was dominated by large private domestic and foreign firms, the ISI sector could elicit populist support against devaluation and tight credit, which encouraged finance capital and exporters to keep much of their portfolio abroad. Colombia was an exception because small farmers made up a large part of its coffee sector, which softened populist opposition to devaluation. Similarly, in the late 1960s, President Eduardo Frei softened populist resistance to devaluation and exchange-rate convertibility by semi-nationalizing Chile's Gran Minería. Efforts to increase taxes on the wealthy, promote unions, and tighten exchange controls also encouraged "international portfolio diversification" in Argentina, Mexico, and Venezuela. Mahon nonetheless disagrees with Sebastian Edwards's contention that populism has been the chief motivation for capital flight in Latin America. Pointing out that the massive capital flight of the early 1980s from Argentina, Brazil, and Chile occurred under the aegis of distinctly anti-populist authoritarian regimes, Mahon cites structural factors rather than fear of populism as the basic determinants of capital flight in Latin America.

Why has capital flight been more chronic and severe among the Latin American newly industrializing countries than among the Asian NICs? According to Mahon, two of the structural determinants in Latin America—asymmetry between thin and narrow financial markets at home and large, liquid financial markets abroad as well as volatile exports and terms of trade—have afflicted the East Asians equally. But two other determinants have not. Private wealth has been more cosmopolitan as well as more concentrated in Latin American NICs than in Asian NICs. In their avid pursuit of European and U.S. high-style consumption and high culture (see *The Allure of the Foreign*), Latin American elites also connected more with foreign high finance than did their Asian counterparts. Mahon

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explains, "People are not born comparing local interest rates to those of another continent. Arguably, this consideration will be made more widely . . . where history has formed more cosmopolitan tastes and culture among those who own most of the country" (p. 53).

Latin American elite cosmopolitanism has encouraged greater "international portfolio diversification," a more cautious attitude regarding placing funds in risky long-term home investment, and a weaker sense of community than that found among nationalistic East Asian counterparts. Mobile wealth has also enabled Latin America's wealthy to veto progressive taxes and limit outlays on basic and secondary education while extracting generous state bailouts when suffering financial stress. Mobile wealth has also enabled them to fend off proposals to repatriate their foreign assets as quid pro quo for socializing their foreign debts during the 1980s debt crisis or for easing the stress on the economy by suspending debt servicing, which they feared would endanger their access to foreign financial markets.

The position of international financial organizations, summarized by Edwards, blames ISI policies and populist demagoguery for the slower and more volatile economic growth of the Latin American NICs when compared with that of East Asians. The skittish behavior of Latin American capital is thus viewed as a defensive reaction to bad policy. Mahon, in contrast, makes adverse feedbacks from that behavior a prime initiating factor. The feedback was especially adverse during the 1980s debt crisis. Massive capital flight, plus financial bailouts that included ex post government guarantees of the foreign debts of private firms, produced mounting fiscal and monetary disorder that deepened and prolonged the drop in output and employment. Cowed by the hostility of domestic and foreign capital toward quid pro quos involving suspension of debt service or compulsory repatriation of foreign assets, Latin American governments saw as the alternative relieving the foreign-exchange bind by reaccessing foreign capital. Meeting IMF conditionality by adopting its panoply of neoliberal reforms was a prerequisite for the reaccessing. Mahon concludes that political scientists should not abandon dependency theory, which is needed to account for Latin America's abrupt economic-policy conversion.

Mahon interweaves the economics and politics with rich detail and subtlety in *Mobile Capital and Latin American Development*. Loose ends remain, many of which he recognizes. Some he does not, however, such as the point that the payoff to the first world from financial globalization has been more dubious than he implies. Regardless, this volume is a highly significant work.

The ambiguities regarding socioeconomic welfare found in neoliberal doctrine and the deep-integration agenda of the United States suggest two general observations. Uncritical support of the agenda by main-

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stream economists is merely a Pavlovian response to its free-trade label because their canonical trade theory is inadequate either to rationalize the intent of the agenda or to account for its results. Constructing an analytically and factually consistent explanation of the main motives promoting the spread of neoliberal policies and deep integration in the third world remains to be done.

Exchange Rate Parity for Trade and Development by Pan Yotopoulos represents a valuable contribution toward this goal. Combining price and expenditure data from the International Comparison Project (ICP) with statistics on direction of trade, Yotopoulos makes three major points analytically and econometrically. First, productivity differences between developed and developing countries are less for nontraded goods than for traded goods. Second, free-market forces produce nominal exchange rates in developing countries that persistently undervalue their real exchange rates, P^{nt}/P^{t}, where P^{nt} is the average price of non-internationally traded goods and P^{t} is the average price of internationally traded goods, biasing domestic investment toward internationally traded goods. Third, in his multiple regressions, only partial positive correlations of the growth rate of GDP per capita with P^{nt}/P^{t} and with the ratio of investment to GDP show up positively and robustly, that is, as invariant when combined in alternative combinations with other "growth variables." The correlations with "openness to trade" and other growth variables favored by neoliberal doctrine show up as statistically insignificant or not robust.

Raising the real exchange rate, P^{nt}/P^{t}, requires overvaluing the market exchange rate and containing the excess demand for foreign exchange by nonmarket rationing. Yotopoulos contends that a dirigiste development strategy in which such rationing forms part of a well-structured industrialization program with an appropriate sequencing of the industries to be nurtured has greater development potential than the export-led growth strategy favored by the international financial institutions.

The reason is that dependency theory's thesis that free-market forces bias relative prices against less-developed economies is supported by the ICP data.[6] But for the potential to be realized, Yotopoulos adds two other requirements: equitable land distribution early in the industrialization process to provide industry with a broad domestic market, and a capable government committed to the dirigiste program and its goals, which he dubs "good governance." In his view, both were present in abundance

6. De Long and Summers, using ICP data, have shown econometrically that the relative prices of equipment have tended to be higher, the lower the economy's output per worker. Poorer countries give up more consumption to acquire a capital good than wealthier ones. Concurrently, De Long and Summers find a strong positive relationship between the share of GDP invested in machinery and equipment combined and productivity growth. This result, they hypothesize, occurs because the learning-by-doing benefits are greater from growth led by capital goods than from growth led by exports (De Long and Summers 1991, 1993).

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in his successful cases—Japan, South Korea, and Taiwan—but were absent in the Philippines, his example of grand failure, and were deficient in Latin American efforts at import-substitution industrialization.

Yet making "good governance" more than an a posteriori rationalization is difficult, as neoliberal political theorists are discovering. Their contention had been that the greater the use of subsidies and controls, the greater the opportunities for rent seeking. Dirigiste strategies inexorably increase the frequency and scope of log rolling and corruption until government failures exceed the market failures that the strategies had sought to correct. But the recent experiences of Eastern Europe, India, and Latin America with privatization and deregulation demonstrate that the faster those processes, the greater also become the opportunities for corruption and rent seeking. Of fifty-two countries ranked in 1997 by Transparency International's Corruption Perception Index, several Latin American countries ranked in the top twenty: Bolivia (second), Colombia (third), Mexico (fifth), Venezuela (eighth), Argentina (tenth), and Brazil (sixteenth).[7] When the G-7 recently authorized the IMF to add good governance to its conditionality menu (IMF 1997), IMF operatives moved quickly to insist that Argentina increase taxes on profit and capital gains and curb tax evasion, to the consternation of the Carlos Menem administration.[8]

Consumer Behavior and Industrial and Urbanization Patterns

The difficulty of operationalizing "good governance" does not gainsay Yotopoulos's contention that postwar Japan, South Korea, and Taiwan sequenced their industrial promotion more sensibly than did their Latin American counterparts. The Asian countries gave priority to building up capital goods and capacity for industrial materials before promoting consumer durables, while the Latin Americans reversed the order.[9] Differences in corruption, leadership intelligence, and authoritarian control appear, prima facie, too minimal to account for the reversed sequencing.[10] Differences in consumer behavior are more promising, on a priori grounds and because testing is more tractable.

7. Transparency International is a German nongovernmental organization that constructs its index by sampling companies doing business in the fifty-two countries. The 1997 corruption scores of all the aforementioned Latino countries worsened over 1996, except for Venezuela. See "Measuring Corruption in the Region," *Latin American Weekly Report*, 5 Aug. 1997, p. 6.

8. See "Demand for Action Now on Corruption," *Latin American Weekly Report*, 19 Aug. 1997, p. 386.

9. On the contrast in sequencing, see also Wade (1990).

10. Recall that the bureaucratic-authoritarian model was developed by Guillermo O'Donnell to tie the outbreak of military regimes in Latin America to the need for authoritarian control of the "hard phase" of import-substitution industrialization (ISI). Hard-phase ISI in Latin America focused mainly on domesticating production of passenger cars and other consumer durables.

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The Allure of the Foreign, edited by Benjamin Orlove, explores interregional differences in nineteenth-century consumption patterns and constitutes a useful contribution to this line of analysis. The exploration is guided by the "well-established principle within anthropological studies of consumption [of] the near-universal tendency of humans to represent status differences by the ownership, use and display of goods" (Orlove, p. 116). The volume focuses on "status competition" between elites and arrivistes, viewed as a salient feature of stratified societies with some social mobility. The contributors find that the use of foreign goods to express status has differed in intensity among third world regions. In the Latin American desire for foreign goods "there was a fervor, approaching in some cases insatiability, which contrasts with the more limited appeal of exotic items which is noted in the broader comparative studies" (p. 18).

The sociology of consumption and the contrasting Asian and Latin American attitudes toward foreign-status goods highlighted in *The Allure of the Foreign* imply that because the status goods in nineteenth-century Asian countries were homegrown, status competition was serviced by larger and more decentralized skilled-craft sectors than in Latin American countries. The Asian adherence to homegrown status goods also meant that with the coming of twentieth-century "late industrialization," their displacement by imports and import substitutes of foreign consumer goods was relatively gradual. Favorable income elasticities of demand enabled major segments of the decentralized craft sector to accumulate capital and modernize their production processes. The counterpart to the slowly declining income elasticity of demand of the rising "middle classes" of Asia for traditional status goods was a lower import intensity of consumer demand than in Latin America. This feature gave dirigiste industrialization more freedom in Asia than in Latin America to expand the physical and human capital base prior to turning to production of consumer durables. While Japan in the 1950s was implementing its Okano Plan to expand capacity in steel, heavy chemicals, and shipbuilding by subsidizing domestic capital and enterprise, Brazil and other Latin American newly industrializing countries were implementing programs to develop a domestic passenger car industry by subsidizing the entry of foreign auto firms.[11]

Latin American small enterprise and the informal sector are treated in the books under review as urban phenomena. The scope of their interaction with the formal economy is a central issue, but linkages with traditional crafts and hinterland locales are passed over, presumably as unimportant. Inferentially, the urban focus highlights the contrast between the

11. This paragraph summarizes a thesis that I have elaborated with partial statistical support elsewhere, in hope that this time it might cease "falling like a rock" among development economists. See Felix (1989, 1983).

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evolution of small enterprise in Latin America and Asia, where rural linkages remain significant and help account for Asia's lower ratios of urbanization.

Alejandro Portes and Richard Schauffler take a different tack in their contribution to *Globalization, Urbanization, and the State*, edited by Satya Pattnayak. In "Competing Perspectives on the Latin American Informal Sector," Portes and Schauffler reject both the perspective of the International Labour Organization's Programa Regional de Empleo en America Latina (PREALC) and that of Hernando de Soto in *The Other Path* on Latin America's informal sector. In their place, Portes and Schauffler offer "structural articulation."

The PREALC thesis holds that the informal sector is primarily a reserve of impoverished surplus labor that swells when economic growth of the formal economy is too low to employ the growing supply of urban labor. From the structural articulation perspective, this view disregards the heterogeneity and dynamism of the informal sector. It grows pari passu with increase in formal employment because it provides assorted goods and services to firms and households of the formal-sector for which demand rises as formal-sector output and income rise. These include goods and services outsourced by formal-sector firms to small enterprises in the informal sector, low-price consumables that allow "working-class households to make ends meet within the constraint of paltry salaries," and menial services to affluent households. Central to the intersectoral articulation are the informal sector's "micro entrepreneurs," who earn on average double the formal-sector wage by employing informal-sector workers at half that wage. According to Portes and Schauffler, "the existence of an informal market represents a vast subsidy to formal capitalist enterprises. . . . [I]nformal enterprises undergird the profitability of their formal counterparts by allowing the latter to maintain wage levels below the cost of the basic needs if these had to be purchased through regulated channels" (pp. 164–65).

But is this a steady state dynamic? Table 7-1 of Portes and Schauffler's contribution reports that by 1990, Latin America's urban population had reached three-fourths of total population, overtaking the first world's ratio of urbanization. Because Latin American NICs are even more urbanized than the regional average, informal-sector recruitment must now be overwhelmingly intra-urban rather than rural to urban. With retreating back to the village no longer a serious option when formal-sector employment and real wages fall, the informal sector's labor supply should swell with laid-off formal-sector workers and first-time job seekers, intensifying the downward pressure on informal wages and micro-entrepreneurial income. Growth in formal employment has indeed slowed and informal-sector real income has fallen more than formal-sector wages in most of the Latin American NICs since 1980, while Table 7-3 shows that the ratio

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of informal to formal labor has risen since 1980 (actually since 1970). The structural-articulation model needs to allow urbanization trends to modify its linear dynamics and to incorporate as a later phase PREALC's contention that slower economic growth increases the informal sector and deepens poverty.

De Soto also stressed the dynamism of the informal sector, but his informal sector is adversarial rather than complementary to formal-sector enterprises. It consists of micro-entrepreneurs evading fees and regulations imposed to protect inefficient but politically powerful formal-sector firms. Abolishing the fees and regulations and letting informal micro-enterprises compete legally would elevate economic efficiency and invigorate economic growth. Portes and Schauffler dismiss this idea as romantic nonsense. The informal sector is not a Trojan horse. Many of its activities are initiated with the backing of formal-sector firms, and public regulation is essential for orderly market transacting. "Eliminating it through removal of state controls would not give rise to market-led development but to the disarticulation of orderly economic activity" (Portes and Schauffler, pp. 162–63).

Portes internationalizes his structural-articulation model in his contribution to *Latin America in the World Economy*, "Transnational Communities: Their Emergence and Significance in the Contemporary World System." "Capital is global, labor is local" has been the basis for a worldwide undermining of real wages and protective legislation, according to Portes. The gains from improvements in production and communication accrue to capital, while the third world laborers employed by first world firms get trapped in "Fordist" production lines, barren seedbeds for nourishing higher labor skills through on-the-job experience. Portes, however, perceives reactions arising that collectively may curb or reverse these globalization trends.

One is the push by first world unions and their political allies to incorporate fair labor standards in trade agreements. Portes views this aspect of "deep integration" more positively than does Haggard but doubts that developing countries will willingly hamper exporting by enforcing such standards. Also unlikely to have much effect would be disseminating to third world countries the Emilia-Romagna model of closely collaborating small firms producing high-quality exports to first world countries. In Portes's opinion, "Neither national laws nor cooperative efforts of small producers are enough by themselves to counterbalance that age-old tool of the moneyed class: complete mobility, which permits it to identify profitable options worldwide and seize them or buy out those initially profiting from them" (p. 155).

The best bet, Portes suggests, is embedded in the dialectic of capitalist expansion, which impels the first world to draw on an ever increasing volume of migrants for its labor while penetrating less-developed

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countries with the "productive investments and consumption standards of the advanced societies" (pp. 156–57). Clustered in ethnic ghettos, immigrants become sources of information to the village and family back home about prospective products for profitable marketing at home and abroad as well as suppliers of grubstake financing to start the enterprise. Portes conjectures,

> as the process continues, it may become a significant factor in modifying a strategy of capitalist accumulation based on wage differentials and information asymmetries between different regions of the world. The main reason . . . is that, unlike labor standards and flexible specialization, the emergence of transnational communities places everyday people on the same plane as the corporate actors who are engaged in global restructuring. The level of information and expertise thus acquired may partially neutralize the power of First World employers to simultaneously exploit Third World populations at home and their immigrants abroad. (Pp. 164–65)

Portes's tentativeness about the effectiveness of that process is warranted. The logic of capitalist expansion did not prevent nationalist political forces in the industrialized countries from closing off immigration from the poor countries during the interwar decades, an outcome suggesting that the current resurgence of anti-immigrant politics could again muddy up the capitalist dialectic. Nor need outsourcing to third world firms improve wages and working conditions for third world labor. First world firms marketing labor-intensive, low-tech products subcontract with Asian firms in large part because such firms drive Asian labor harder and at lower wages than first world firms find politic to attempt.

To be sure, benefits have also accrued for Asian development. Some overseas Chinese subcontractors come to broaden their product lines and engage in more sophisticated finance and marketing. But they are also footloose, as Thailand is discovering. The most successful East Asian economies used carrot-and-stick policies to redirect the foreign exchange from low-tech export activities to finance higher-tech industries that then took over industrial exporting when rising wages at home or cheaper labor abroad squeezed out lower-tech ones. These instances, however, are examples of industrial policy overriding the power of mobile capital.

In Latin America, labor-intensive industrial exporting through local subcontractors has been rare. Two case studies in *Latin America in the World Economy* document one alternative—indigenous firms initiating production and marketing.

Roberto Korzeniewicz describes in "Uncertainty, Innovation, and Global Competitiveness: The Brazilian Footwear Industry" the trajectory of a Latin American industry that for a time resembled the Emilia-Romagna model. Clustered in shoe districts in Southern Brazil, the shoe firms developed a strong cooperative tradition that his essay dubs *competitive collectivism*. They shared information on quality control, design, and

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productivity improvements via strong trade associations and took a live-and-let-live attitude toward market sharing. Aided by government fiscal and financial incentives, the industry moved into exporting on a large scale, becoming in the 1970s and 1980s a major world exporter of mid-to-high-priced women's shoes. But in the 1990s, trouble set in when the government, as part of its market liberalization strategy, abolished special incentives and shifted exchange-rate policy from timely devaluing in order to stabilize the real exchange rate to lagged devaluing in order to slow inflation, thus chronically overvaluing the exchange rate. In the severe squeeze on profits, competitive collectivism in the shoe industry gave way to fierce competition. Employment and real wages fell, smaller firms were wiped out along with the influence of the trade associations, and survivors began relocating to low-wage sites in northeastern Brazil.

In "The Cocaine Commodity Chain and Development Paths in Peru and Bolivia," Amy Bellone covers Latin America's outstanding case of an indigenously entrepreneured labor-intensive and low-tech industry that dominates the global market. She describes the stages from coca leaf to crack and presents expert guesstimates of the value added at each stage of production. Growing the leaf and converting it into paste, an activity concentrated in Bolivia and Peru, contributes about 0.2 percent to final value added, although in Bolivia that is remunerative enough to engage 10 percent of the economically active population. The conversion of paste to powder, chiefly a Colombian specialty, tacks on another 0.3 percent to final value added. Thus 99.5 percent of final value added comes from downstream activities: transporting to and distributing in the main markets—the United States and, more recently, Europe—and bribing politicians, police, and military to keep the routes open. Two lessons emerge. The industry's potential as a *pôle de croissance* for Andean development is nil, and eradicating production to destroy the drug trade is hopeless because the industry can easily raise payments to producers and officials as needed to maintain the flow.

Three essays in *Latin America's New Insertion in the World Economy*, edited by Ruud Buitelaar and Pitou Van Dijck, examine another alternative, that of exporting labor-intensive products from export-processing free zones (EPFZs). These contributions focus primarily on Central American experience with such zones. The exporting, they find, is being done almost entirely by foreign-owned firms that process mostly imported materials using imported equipment and local female labor, while host governments provide the infrastructure. Production is Fordist assembly-line, the export market is mostly the United States, and backward linkages with domestic suppliers have been meager. The authors' tentative judgments are that the jobs created have little potential for building human capital. The Costa Rican study also concludes that tax subsidies and infrastructure outlays per job created have been steep. Preferential tariffs

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under the U.S. Caribbean Basin Initiative were important in drawing foreign firms to the EPFZs.

On Mainstream Policy Heterodoxy in Latin America

In *Lessons in Economic Policy for Eastern Europe from Latin America,* edited by Gary McMahon, prominent Eastern European and Latin American economists assess the experiences of each region with privatization, monetary and fiscal reform, and trade liberalization. The premise of the volume is that the goal in both regions is to establish growing competitive capitalist economies with stable price levels, high employment, and an equitable distribution of income and wealth. The "lessons" from Latin America's experience are mainly negative: what to avoid. Eastern European economies should liberate goods and financial markets slowly, share adjustment burdens equitably, put off major privatizing until inflation is under control, reduce fiscal deficits by more efficient tax collecting, not by cutting back essential public expenditures, and so on.

Lessons in Economic Policy and *Latin America's New Insertion in the World Economy* share two features common to mainstream heterodoxy in Latin America. Their advocacy of a partial return to dirigiste policies is presented as merely a provisional slowdown on the road to ultimate liberalization, although neither the time frame nor the final state is spelled out. The liberalization trends in the first world are taken to be relatively problem-free and irreversible.

The first feature calls to mind the French adage, *Rien n'est plus permanent que le provisionnel* (Nothing is more permanent than the provisional). Beset by doctrinal flaws and disappointing results, liberalization in Latin America is being reduced to a politically correct umbrella covering a piecemeal retreat from the neoliberal agenda. This intellectual process is mirrored in the political arena. The precipitous drop in popular support for political parties implementing the neoliberal agenda is opening prospects for leftist parties to move out of the wilderness but is also motivating them to form coalitions with centrist parties and to incorporate neoliberal notions in their platforms in order to assuage business fears.

Is this development a reversal of Juan Perón's cynical adage, "One picks up the violin with the left hand and plays it with the right"? Two essays in *Globalization, Urbanization, and the State* tackle this question. James Petras's "The Transformation of Latin America: Free Markets, Democracy, and Other Myths" views as systemic the recent applications of the original Perón adage by Carlos Salinas de Gortari in Mexico, Carlos Menem in Argentina, Alberto Fujimori in Peru, and Andrés Pérez in Venezuela. Such post-election "betrayals" by the politically ambitious are inevitable when they become hemmed in by elite and foreign pressures. In contrast, Arthur Schmidt's "The Internationalization of the Economic Crisis in

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Mexico and Central America" gives more weight to circumstances than to moral flaws. This assessment seems apropos because changing circumstances have turned the tables on the neoliberal program. In the 1980s, proponents of that program neutralized popular opposition by blaming dirigiste policies of the past for the economic miseries of the present. In the 1990s, however, popular support is won by blaming neoliberalist policies of the past for the deepened miseries of the present. Even neoliberal officeholders may be shifting. *The Wall Street Journal*, editorializing on President Ernesto Zedillo's address to the newly elected Mexican Congress, voiced alarm: "He went out of his way to distance himself from market economics, saying that since the Mexican Revolution the state had a firm policy that provides for education, health, social security, basic nutrition, support for housing and basic services and job promotion. The bow to statism was dictated by the collapse of his support within the PRI, his alienating of the PAN, and his three-year-old agenda of blaming Mexico's economic crisis on his predecessor, Carlos Salinas de Gortari."[12]

Similarly, Mercosur has been careful to present the expansion of formal ties with its neighbors as complementing Washington's effort to create a hemispheric free-trade agreement by enlarging NAFTA, although strains are showing. Chile, anointed by Washington as the next addition to NAFTA, has cooled on the idea. "Mercosur is our FTA," Chile's foreign minister announced recently. Two reasons given are that NAFTA rules would require Chile to abandon controls over short-term capital and that the most-favored-nation terms of Chile's associate membership in Mercosur would require it to extend to Mercosur members without reciprocity any trade concessions that the country makes to its NAFTA partners.[13]

The retreat from neoliberalism is restrained, however, by the second main feature of Latin American mainstream heterodoxy: the belief that first world countries are free of the third world's problems with the globalizing of market liberalization of trade and finance. Fear of hostile reactions from the globalized financial markets to defections from neoliberal policies thus reinforces the fear of adverse reactions from domestic financial markets. Recently elected Mexico City Mayor Cuauhtémoc Cárdenas took time before the elections to make a visit of reassurance to Wall Street. Argentina's Frepaso-UCR alliance, riding high in the polls, has pledged not to touch the law that freezes the peso-dollar rate. The fear is real and extends to Mercosur, which would have difficulty surviving extended peso or cruzado volatility.

Yet comparable fears permeate the first world. The head of IBM's global securities and capital markets operations observed, "What's happened in the last 25 years is that enormous risk has been added to the financial markets. There's liquidity risk, interest-rate risk, exchange-rate

12. "Mexico's New Politics," *Wall Street Journal*, 4 Sept. 1997.

13. "Mercosur Approach to FTAA Advances," *Latin American Weekly Report*, 5 Aug. 1997, p. 364.

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risk, portfolio-composition risk."[14] An explosion of innovative mechanisms to hedge risk, to arbitrage differences between international interest and exchange rates, and to speculate on exchange-rate volatility accounts for the explosive growth of international currency trading referred to earlier. But awareness that the societal rewards from this frenzied finance are negative is also spreading, as are fears that the increasing frequency of financial crises could terminate in an uncontrollable one.

Still largely unnoticed in the euphoria over the falling rates of inflation and nominal interest rates in the G-7 since the early 1980s are increasing indications that the global financial boom is unsustainable and that its deflation could severely injure production and employment. Despite falling inflation, real interest rates of the G-7 have been rising. In each of the G-7 countries during the past decade, the real rates on ten-year treasury bonds have averaged over twice the real growth rate of GDP. With ratios of government debt to GDP and business and household debt leveraging also increasing, the rentier share of G-7 national income has been rising sharply. As it must stop well short of 100 percent, the crucial question is whether the globalized financial markets can level off the rentier share without a major crisis.

History is not encouraging on this subject. In the heyday of the gold standard, 1881–1913, the real rates on ten-year treasury bonds of the G-7 averaged slightly less than the real rate of GDP growth, suggesting that the rentier share did not rise. In the interwar decades, real interest rates of the G-7 averaged more than double the real GDP growth rate but mainly because the Great Depression flattened GDP.[15] Nor is the fact that equity markets have boomed, despite the unprecedentedly high real interest rates, an encouraging sign. A high real interest rate increases the cost of capital, which should deter real investment and depress asset prices, but thus far it has done only the first. The boom in equities seems to have been sustained primarily by the pursuit of large capital gains from asset plays. In such pursuits, a high cost of capital is a minor deterrent, more than offset by lowered perceptions of political risk as the cold war ended and by the spread of market liberalization, which has provided a lucrative supply of privatized assets at discount prices and a tolerant environment for consolidations that increase market concentration. But the "fundamentals" are inadequate to justify the high prices of assets. Productivity growth rates, which depend primarily on the growth of real investment, remain depressed, while resistance to further wage cutting is rising. Deficient fundamentals and high real interest rates will sooner or later deflate the equity boom.

Preemptive moves by the G-7 authorities to rein in the freedom of

14. Kent Price, as quoted in "Japanese 'Big Bang' Is Leading to Big Boon for U.S. High-Tech," *Wall Street Journal*, 16 Sept. 1997, p. 1.

15. For the comparative data, see Felix (1997–1998, t. 9).

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finance capital to move globally would increase chances for a soft landing. Yet one sees no signs that they are prepared to do so. Tobin's prologue to *The Tobin Tax* may help explain why. He proposed the tax with two objectives in mind. First, it would reduce exchange-rate volatility by making short-term speculative forays more costly. Second, the tax would "promote the autonomy of national macroeconomic and monetary policies" by widening the range of interest rates within which national governments could exercise that autonomy free from onslaughts from the international arbitraging of portfolio capital. The first objective raises mainly technical issues about the tax's effectiveness, but the second stirs up political and ideological passions. Greater national autonomy over macroeconomic and monetary policy means reducing the power of finance capital to discipline national policies. More economic space becomes available to implement growth-with-equity policies and other heterodox proposals for rolling back the neoliberal programs in first as well as third world countries. This danger may explain why a modest proposal like the Tobin tax has been kept off the G-7 agenda and why Washington bullied the United Nations Development Programme, sponsors of *The Tobin Tax*, into abandoning post-publication plans to promote the book.[16]

A Summing Up

The drive to globalize free-market policies is running into heavy weather. But is it stalling? The books and articles reviewed here focus on the heavy weather, but from partial perspectives that are inadequate to answer the larger question. Most shortchange the role that lifting first world capital controls and globalizing financial markets have been playing in driving free-market policies. And most simplify their analysis by assuming that first world countries have been exempt from the slow growth, increased financial turbulence, and rising inequalities afflicting most of the third world in the past quarter-century.

My assessment has therefore concentrated on filling in these two lacunae in an attempt to answer the larger question. A tentative answer is that the heavy weather the free-market drive is encountering in the third world is being reinforced by political reactions in first world countries to the accumulation of adverse effects that are not so dissimilar from those that are sapping political support in third world countries. The heavy weather might merely produce a midcourse detour were the hegemonic powers to act to reduce some of the turbulence by reining in their disruptive financial markets and accept the greater national autonomy over economic policy formation that would ensue. Then again, they may persist in pressing for still greater freedom for financial capital to flow globally. In

16. For details, see "Le projet de taxe Tobin, bête noire," *Le Monde Diplomatique*, Feb. 1997.

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that case, the weather will get stormier and the likelihood greater that financial storms will blow the globalization project much farther off course.

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