criticisms from among Soeharto loyalists, and even the rising and rapacious business interests of the Soeharto children from the mid-1980s.

When Soeharto was suddenly pushed out of office in May 1998, and with the economy in free fall, it was assumed that those closest to him would lose everything. Liem, by then in his early eighties, was at the top of the list. His house was ransacked and, although he was out of the country at the time, the event led him to take up permanent residence in Singapore. However, although Liem lost much of his business empire, in one of corporate Asia’s most remarkable recoveries, piloted principally by Liem and his son Anthony, the Salim group was rebuilt. It is once again a leading and highly diversified Indonesian business conglomerate. In the latest Forbes rich list for Indonesia, the Salim family ranks third, with an estimated net worth of US$5.9 billion.

While a riveting read, at almost 600 pages, perhaps the text could have been pruned somewhat, also to allow scope for the authors to venture into some more analytical and comparative territory. For example, does Indonesia conform to what we know about business groups in developing countries? By the usual indicators of institutional quality, corruption, and so on, it ranks about where one would expect it to be as a lower middle income economy. But it is unusual in at least three respects: its economy has grown faster than most over the past half-century; it experienced a sudden and thus far successful transition from authoritarian to democratic rule in 1998-99; and its modern business sector continues to be dominated by a very small ethnic minority, the Chinese community numbering about 3 per cent of the total population.

One is also left wondering about one of the most hotly debated issues in Indonesian and neighbouring business circles: are its key business figures ‘rent-seekers or real capitalists’, to borrow from the subtitle question posed in an earlier, seminal study of Malaysia’s business leaders? (Peter Searle, The Riddle of Malaysian Capitalism, 1999.)

But these are minor quibbles. This is business and political history at its finest: both a ‘pot boiler’ and a study of amazing depth. It will surely provide material for an outstanding documentary, and perhaps even a movie.

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Economic Management in a Volatile Environment: Monetary and Financial Issues
Ramkishen S. Rajan and Sasidaran Gopalan

This book features a collection of the authors’ research papers on contemporary issues in international banking and finance. Some of these papers were previously published in journals; the authors have updated them for publication in this book.

The book is divided into two parts, with each part containing five essays. The first part covers issues in real exchange rate volatility, accumulation of foreign reserves, sterilisation of foreign reserves, taxation on capital flows, as well as other capital controls in emerging market economies in general and the developing countries in North and Southeast Asia in particular. The second half of the book covers issues in financial crises, especially the Eurozone crisis and the 1997–98 Asian currency financial crisis, and reviews the role and performance of foreign banks in emerging market economies. The contents of each of the book chapters and the key findings are reviewed below.

Chapter 1 uses monthly data to investigate the extent of de facto sterilisation of foreign exchange reserves and capital mobility in China during the period June 2000 to September 2008. It reports econometric findings that suggest China sterilised most of its accumulated foreign reserves over the study period. However, using rolling recursive regression techniques, the authors have obtained evidence of increasingly mobile capital flows in China. This suggests a diminishing independence of monetary policy in China that existed under a pegged exchange rate system with capital controls and its modern business sector continues to be dominated by a very small ethnic minority, the Chinese community numbering about 3 per cent of the total population.

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exposed to shocks of both domestic and foreign origin.

Chapter 2 decomposes real exchange rate volatility for a group of countries during the period 1990 to 2010 and estimates the importance of internal prices of tradables vs. non-tradables in real exchange rate fluctuations. It examines the role of economic fundamentals in the relative contribution of non-traded components in real exchange rate fluctuations. The chapter also examines how much volatility of the real exchange rate in selected Asian countries was driven by deviations from purchasing power parity (PPP) in the tradable sector vs. internal prices. The authors report findings that are different for two groups of Asian countries. For north Asian countries, the real exchange rate volatility was driven by deviations from PPP, while for smaller Southeast Asian economies, internal price fluctuations contributed most to the volatility in real exchange rates. These findings suggest that the volatility of prices of non-tradables is more important for commodity exporters. This is consistent with the view that PPP holds better in countries engaged in commodity trade. Overall discussion of this chapter is analytical and remains difficult for general readers. Though tightly written, it features minimum discussion on findings and policy.

Chapter 3 deploys a data set on financial globalisation, compiled by M. Schindler of the International Monetary Fund, to investigate the issue of whether various capital-control measures lower the volatility of different types of capital flow after controlling a set of economic, financial, and institutional factors. Mostly an econometric analysis, the main conclusion drawn from the empirical findings is that when the objective of capital controls is to reduce the volatility of capital flow, the controls on capital inflow fail in the sense of either raising own capital inflow volatility (debt) or worsening corresponding volatility for equity or foreign direct investment (FDI). Control of FDI outflow is preferable in this regard, although it has the unintended consequence of raising the volatility of equity outflow. Control of equity outflow may be better than other types of capital controls in the sense that while the control of equity flow does not have much impact on equity outflow per se, it has a positive unintended consequence of reducing the volatility of other types of capital outflow as well as its own inflow. The overall message emerging from statistical analysis is the limited efficacy of capital controls insofar as the reduction of the volatility of capital flow is concerned. The general discussion on capital flows is minimal while the analysis remains restricted to a set of narrow issues in capital movement.

Chapter 4 reviews the issue of whether international taxation on capital flows could be effective in reducing exchange rate volatility when a country operates under a freely floating exchange rate system. The discussion focuses on developing countries that experience exchange rate volatility and boom–bust cycles due to unpredictable, large-scale capital movement. The key finding is that the effect of taxation on exchange rate volatility depends on the nature of the speculation and whether the focus is on capital inflows or outflows. Although the issue of exchange rate volatility can be analyzed in different contexts, that currency taxation is just one approach to addressing exchange rate volatility is not highlighted. Central banks have a range of instruments within the framework of macro-prudential regulation and supervision, and these instruments can be deployed to deepen foreign exchange markets and keep the exchange rate stable. Overall, the authors have correctly noted that currency taxation or similar control measures are not inconsistent with capital account convertibility. Capital control measures, however, do not diminish the need for improving economic fundamentals to reduce exchange rate instability. For example, the development of money and capital markets remains critical for absorbing external shocks, including large-scale capital flows.

Chapter 5 reviews the trends of large-scale foreign reserve accumulation in emerging market economies. The authors have made a comprehensive review of the major theories and propositions behind the rapid accumulation of foreign reserves in some emerging market economies. Along with discussion on the factors behind reserves accumulation, they have highlighted the opportunity costs of reserve accumulation in terms of foregone consumption and investment, as well as alternative uses to which these reserves could be put, such as paying down sovereign short-term external debt, investment projects, and infrastructure projects. They correctly point out that there is no optimal level of foreign reserves as it varies with the country, its economic circumstances, the exchange rate regime, the openness of current and capital accounts, the macroeconomic
policies followed by the country, the level of short-term debt, and the country's credit rating, which determines its credibility in international financial markets. Nevertheless, the authors highlight that those countries holding large foreign reserves performed better during the financial crises than those that had lower levels of reserves. Although this chapter does not contain any empirical analysis, the perception remains that any causality between large reserves and macroeconomic performance is bidirectional.

Chapter 6 reviews the linkage between the financial crisis in Europe and the underlying issues in competitiveness that contributed to this crisis. It then draws a comparison between the Eurozone crisis and the 1997–98 Asian currency financial crisis, and identifies the common elements and differences in these crises. The Eurozone crisis put an end to the suggestion that Asian countries should consider having exchange rate coordination in the form of say, monetary union, for the foreseeable future, although they should persist with a weaker form of monetary cooperation, which could be useful to countries facing external shocks. The authors draw two important conclusions: first, the roots of the Eurozone crisis can be traced to the formation of the euro when political considerations outweighed economic considerations, when several countries forming the monetary union did not meet the criteria set by the theory of optimal currency areas. The second conclusion follows the experiences of Europe; that is, countries in Asia should not rush into a monetary union when there is lack of interregional factor mobility and there is also difficulty in coming to consensus on macroeconomic coordination or, at the least, a fiscal union. To avoid any financial crisis, like the Euro crisis, Asian countries instead should adopt a flexible exchange rate system to absorb external shocks and maintain fiscal discipline.

Chapter 7 reviews the literature on the linkage between financial liberalisation and economic growth. It defines financial liberalisation in a usable form by making a distinction between domestic and international financial liberalisation. International financial liberalisation is then classified as bank-based and non-bank-based. Banking internationalisation is concerned with the removal of barriers to entry and any discriminatory treatment of foreign banks, as well as the cross-border provision of banking services. Non-banking internationalisation is concerned with capital account liberalisation. It involves the removal of capital controls and restrictions on the convertibility of domestic currency. After defining financial liberalisation, the authors discuss the appropriate sequencing of financial liberalisation by drawing lessons from the experiences of countries across the globe. Finally, they discuss the trends of asset holdings of foreign banks and suggest the costs and benefits of foreign banks in emerging market economies. Foreign banks generally raise efficiency by lowering costs, improving operational efficiency, introducing new technology and products, raising marketing skills and management, and developing corporate governance structures. Simultaneously, foreign banks could be a conduit for the transmission of external credit shocks to domestic credit availability. Further, foreign banks may cherry-pick creditworthy borrowers in developing countries, leaving only the riskier borrowers ('lemons') for domestic banks, possibly causing a net reduction of aggregate credit availability in the economy and affecting its performance.

Chapter 8 provides a comprehensive review of the theoretical and empirical literature on the factors behind the relatively high efficiency of foreign banks versus domestic banks in emerging market economies. After discussing the key issues in measuring banking efficiency, the authors distinguish between structural and non-structural methods to estimate banking efficiency in emerging market economies. To explain the finding that foreign banks are more efficient than domestic banks, they highlight the institutional differences and similarities between the source and host countries. Foreign banks in general have better risk management strategies as they deploy sophisticated information technologies and management techniques. In addition, they pick up the most creditworthy borrowers and therefore raise banking efficiency and profits. Foreign banks do have some disadvantages, however. They operate within a different cultural environment, have information disadvantages, and generally navigate through dissimilar regulatory structures and procedures. Overall, the entry of foreign banks either in the form of ‘greenfield’ operations or mergers and acquisitions increases banking competitiveness and hence raises the efficiency of the banking sector as a whole. The authors also report findings for some countries that suggest foreign banks have either negligible or adverse effects on banking efficiency. This finding is not totally
unexpected, because the effects of foreign bank entry on the efficiency of domestic banking depend on macroeconomic conditions and the institutional environment of the host country. Further, there is a strand of literature that suggests domestic private banks are as efficient as foreign banks, indicating that the ownership of banks remains important in raising banking efficiency and profits.

Chapter 9 reviews the key issues in foreign bank entry and firms’ access to credit in emerging market economies. The authors review two prominent hypotheses with respect to bank lending. The first is linked to the market-power hypothesis, which suggests that the entry of foreign banks into domestic markets lowers market concentration and increases the availability of bank credit. However, as higher market concentration implies less competition, this may raise the availability of bank credit for small opaque firms. The second hypothesis is concerned with information asymmetry. Foreign banks operate under limited information and this lowers the access of small firms to bank credit. Foreign banks generally cherry-pick the most creditworthy borrowers, leaving smaller borrowers not considered creditworthy for domestic banks. Consequently, domestic banks are eventually forced to exit the market. This cherry-picking behaviour is more prevalent in cases of the greenfield variety of foreign banks compared with a situation where foreign banks enter into the market through mergers and acquisitions. Although the review of the literature, theoretical or empirical, suggests no linkage between banking sector competition and access to bank credit, the authors report empirical results that suggest foreign banks are negatively associated with the growth of private credit in emerging market economies. They suggest that increased credit information availability can play a key role in the decision-making of foreign banks to extend bank credit in emerging markets.

Chapter 10 reviews the key factors that encourage foreign banks to venture into emerging market economies. Although profit remains the key factor, the decision of banks to enter into foreign markets involves multiple factors. The literature on this issue is closely related to the theory of multinational enterprises, namely the internationalisation theory and the eclectic paradigm of foreign investment. The key idea of both these theories is that the source-country firms possess some intangible firm-specific advantages in domestic markets that can be deployed effectively in foreign markets. This is the key rationale for banks to expand their activities abroad.

In summing up, this book includes papers covering topical issues that have come to the forefront of policy discussion since the beginning of globalisation in the 1970s in general and the onset of financial crises in recent decades in particular. Most papers are both well and tightly written and organised, providing historical context and analysis drawing on extant and varied literature on the issues involved in different contexts. Most analysis is also insightful and remains relevant to the understanding of contemporary policy issues in banking and finance. However, the themes highlighted remain somewhat disjointed. In general, as the essays are self-contained, there is limited discussion on the issues in an integrated form. In particular, there is minimal discussion on the monetary and fiscal policies expected to play a critical role in maintaining macroeconomic-financial stability. Discussion on interactions of monetary and fiscal policies is unexplored. Finally, although the concept of an open-economy trilemma is implied in most discussion, it is not articulated to reveal any policy contradictions and complexities in analysing macroeconomic issues.

Despite such shortcomings, I recommend this book to advanced undergraduate students specialising in economics, finance, and development studies, to researchers, and to policymakers, all of whom will benefit immensely from the surveys of the literature and the varied information on key issues in international banking and finance in the context of emerging market economies in general and those in Asia in particular.

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Japan’s Economic Planning and Mobilization in Wartime, 1930s-1940s: The Competence of the State
Yoshiro Miwa

Professor Yoshiro Miwa is no pushover. In taking positions, he is fully prepared to be argumentative, to combat intellectual enemies of all stripes,