

The book highlights some useful distinctions for economic historians studying environmental impacts and change. Path dependency of environmental quality can be measured by several different sorts of scientific parameters, including soil nutrients, species composition, biomass, and nutrient cycling in soil and air. The scientific studies indicate that as human interventions and multiple uses of the forest over millennia have changed the structure and composition of the New England forest in visible as well as less direct ways. The forests are not in a long run steady state equilibrium; nor does restoration to a “pre-human” influence appear a feasible, or even possibly desirable, goal.

The Harvard Forest has conducted a number of experiments described in the book that highlight the complications of managing nature, even when we are attempting to manage it as nature would have done in the absence of human influence (such as prescribed burning to mimic natural fire disturbances, which has been a controversial goal of many public land managers in recent years). The reader may not absorb all the scientific details of phosphorus uptake, nitrogen fixing, or ecosystem respiration, but she should come to appreciate the ways in which long-run forest dynamics are inextricably entwined with human decisions regarding land use.

The book’s insights into the evolution of species composition over time may prove most useful as we face increased disturbances from pests and invasive species that have already removed the American chestnut and elms as dominant species in our Eastern forests and now threaten the eastern hemlock significantly as well. Although the research may not provide solutions that allow these species to thrive, it may serve two other important roles: to enhance our scientific understanding of their ecology, giving us the information needed to create the best chances for survival; and to enhance our economic understanding of how the patterns of human resource use drive long-term ecosystem change so that future forests and their users might benefit from more knowledgeable decision making. The founders of the Harvard Forest had foresight, and the authors of these pages make admirable use of a unique and rich data source to provide today’s decision makers with better information about our past impacts.

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GENERAL AND MISCELLANEOUS

Global Capital Markets: Integration, Crisis, and Growth. By Maurice Obstfeld and Alan M. Taylor. Cambridge: Cambridge University Press, 2004. Pp. xviii, 354. \$65.

The process of global financial integration has attracted more than its share of controversy. While many point to the potential economic benefits of free trade in capital, others argue that the benefits are outweighed by the risk of international financial crises. This book, which summarizes almost a decade of work by two distinguished international economists, examines the history of global financial integration from the late nineteenth century to the present with a view to resolving this controversy and extracting lessons for policymakers today. Combining a wide range of hard data with qualitative historical analysis, the authors present a nuanced view of the costs and benefits of international financial integration. One conclusion, albeit carefully qualified, is certain to be controversial: many developing countries would gain from the re-introduction of some form of capital controls.

The book is divided into four parts. After a preamble, Part 2 begins by charting the evolution of international capital market integration over the past century and one-half using a variety of quantitative measures. Chapter 2 examines both stocks and flows of international capital, while chapter 3 presents evidence on the relative absence of arbitrage opportunities in both asset and goods markets. Both chapters paint an overall picture in which international financial integration increased at the end of the nineteenth century before collapsing due to the combined effects of two world wars and the Great Depression, only to re-emerge with increasing speed throughout the latter half of the twentieth century.

The core of the book is contained in Part 3, which examines the inter-relationship between international financial integration, economic conditions, and politics. The organizing theme for this part is what the authors refer to as the “fundamental macroeconomic policy trilemma.” Familiar from the Mundell-Fleming model, the trilemma asserts that a government can attain no more than two of the three objectives of stable exchange rates, monetary policy independence, and international financial integration.

From this perspective, the history of international financial integration is a history of the evolution of choices about how to resolve this trilemma. Chapter 4 takes up this theme and presents a qualitative history of international capital markets, which divides the period into four separate regimes in which the trilemma was resolved in four distinct ways. Under the Gold Standard, countries surrendered monetary policy independence in order to attain the benefits of free capital flows and exchange-rate stability. In the interwar period, with the world moving towards autarky, the benefits of capital mobility were reduced, and many countries were concerned about the role of the fixed exchange rates in transmitting international financial crises. The resulting breakdown in the policy consensus led some countries to float their exchange rates while others closed their capital markets in order to retain domestic policy autonomy. In the postwar period under Bretton-Woods, a consensus arose that the benefits of monetary policy autonomy and stable exchange rates outweighed any benefits from capital mobility. The final period, beginning in the 1970s and continuing to the present, has witnessed an increase in the number of countries floating their exchange rate and opening up to flows of capital.

Chapters 5 and 6 present a range of evidence that is useful in assessing the tradeoff implied by the trilemma. Drawing on work co-authored with Jay Shambaugh, Chapter 5 examines how the relationship between interest rates across countries has varied with the form of capital controls and exchange-rate regimes. The evidence is in line with the trilemma hypothesis: absent capital controls, countries with pegged exchange rates lose monetary policy independence and their interest rates follow movements in the “world” interest rate. Chapter 6 examines whether the decision to give up monetary policy autonomy delivers benefits in terms of lower borrowing rates on international capital markets. For the prewar period, the authors find that adherence to the gold standard alone was sufficient to lower borrowing costs. This effect remains even after controlling for membership of the British Empire, default, war, and strong economic and fiscal conditions. This pattern was reversed in the interwar period: a return to gold was less important than alternative explanations of spreads, possibly reflecting the lower credibility of the gold standard.

The finding of Chapter 6 contains a potentially important lesson for developing countries: credible commitments to fixed exchange rate regimes have a payoff in terms of lower borrowing costs. However, the lesson needs to be tempered by the fact that they require a *credible* commitment, which in the light of the interwar evidence is difficult to manufacture. Moreover, the gains may be small, amounting to less than 20

basis points in some specifications. There is also the possibility that the authors' specification may overstate the gains. For although the authors control for contemporaneous defaults, wars, and economic conditions, yields also reflect expectations of future events. And if countries abandon gold in expectation of adverse future shocks, or if domestic political institutions simultaneously make adherence to gold more difficult *and* future default more likely, the benefits to fixing exchange rates might be illusory.

Part 4 of the book attempts to draw lessons for the future of the international financial system from the historical evidence, and in particular asks how the trilemma might be best resolved today. Chapter 7 documents the fact that capital flows are much more concentrated amongst the rich countries today than they were during the gold standard. What is different about the modern period? One possibility discussed in Chapter 8 is that, in contrast to the nineteenth century in which high returns could be found in newly settled countries, the benefits to investing in poor countries today are low because of a host of factors that manifest themselves in low returns.

But if this is the case, the benefits to international financial integration are low. And the costs, in terms of an increased propensity for financial crises may be severe. The authors are careful to point out that the evidence on the costs of crises, and their relationship to international financial integration, is weak but present some evidence that they may be larger than the benefits of international financial integration in the first place. The conclusions the authors draw are suitably nuanced, but certainly provocative: unless developing countries can reform themselves in ways that make the returns to foreign borrowing large, these countries may benefit from restricting capital flows.

This conclusion will, no doubt, spark some controversy of its own. But even if we accept the argument that capital controls are desirable, are they feasible? Recent experience with the imposition of capital controls in countries such as Brazil (see, for example, the excellent review in Marcio Garcia and Marcus Valpassos "Capital Flows, Capital Controls and Currency Crisis: The Case of Brazil in the Nineties." in Felipe Larrain, ed. *Capital Flows, Capital Controls, and Currency Crises: Latin America in the 1990s*, University of Michigan Press) suggests that the private sector is often quick to find ways around capital controls. If so, are we left with the pessimistic conclusion that developing countries are doomed to live with costly crises? The authors give us reason for optimism: if crises are the result of policy makers failures to respect the tradeoff implied by the trilemma, the first step in avoiding crises is to educate policy makers about this tradeoff. That education should start with this book.

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The Divergent Dynamics of Economic Growth. By Richard H. Day. Cambridge: Cambridge University Press, 2004. Pp. xiv, 241. \$65.

Because the function of a book review is to direct busy readers towards good books and away from bad ones, a good book review and a kind book review are often incompatible. This is one of those unfortunate occasions. Even though Richard Day notes promisingly in the preface that "I felt my mission to have been that of providing a better characterization of economic change" (p. x), no economic historian is going to benefit from delving into this book.

The first problem of the book is that it is a book only in the sense that its pages have consecutive numbering. The volume is composed of 12 essays, based mainly on pre-