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Review of "Casino Capitalism"

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rate of return, or by raising taxes which reduces private savings. At the same time, these governments can earn investment income at the tax-free rate. Despite the many legal restrictions that limit many governments' ability to arbitrage, Gordon and Slemrod show that relatively poor communities tend to rely more on bond financing than wealthy communities, a result that is consistent with their arbitrage theory.

The next two papers look at the empirical implications of some particular state and local government policies. In "Property Taxes and Firm Location: Evidence from Proposition 13," Michelle J. White uses the natural experiment created by the passage of Proposition 13 in California to study business location decisions. She finds that property taxes play a significant role in the location of retailing and service firms, but not manufacturing firms. In "Welfare Effects of Marginal-Cost Taxation of Motor Freight Transportation: A Study of Infrastructure Pricing," Kenneth A. Small and Clifford Winston provide empirical evidence that suggests that the introduction of a nationwide program of marginal cost pricing for heavy highway vehicles will result in a major welfare gain.

The paper by Daniel R. Feenberg and Harvey S. Rosen, "State Personal Income and Sales Taxes, 1977–1983," utilizes some of the data that have been collected and analyzed as a part of the National Bureau's state and local public finance project. Feenberg and Rosen's paper shows the incredible heterogeneity in tax structures that exists among the fifty states. Whether and to what extent these differing structures are due to economic (as opposed to political and historical) motivations remains an interesting, largely unanswered question.

In an excellent concluding paper, "Education, Welfare, and the "New" Federalism: State Budgeting in a Federalist Public Economy," Steven G. Craig and Robert P. Inman develop a general analytic framework for evaluating the effect of federal grants on state and local governments. Unlike most earlier work which has been highly aggregative, Craig and Inman look jointly at education, welfare, other expenditures, and revenues. The empirical portion of the paper provides strong support for the view that, if enacted, the New Federalism program will lead to reduced government spending on social programs such as welfare and education.

All in all, the papers are of unusually high quality, as are the brief, but useful set of comments on each. With interesting and careful empirical work in this area still an undervalued commodity, the editor and the authors should be commended for their valuable contributions.

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REFERENCE

QUIGLEY, JOHN M. AND RUBINFELD, DANIEL L. "Budget Reform and the Theory of Fiscal Federalism," *Amer. Econ. Rev.*, May 1986, 76(2), pp. 132–37.

400 International Economics

430 Balance of Payments; International Finance

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Casino capitalism. By SUSAN STRANGE. Oxford and New York: Blackwell, 1986. Pp. vii, 207. $24.95. ISBN 0–631–15026–9. *JEL 87–0504*

Ever since the relative tranquility of the fifties and the pre-Vietnam sixties was replaced by the turbulence of the seventies and eighties *Casino Capitalism* has been an apt label for advanced capitalist economies. When a position in a batch of principal-only mortgage securities can cost a firm as well disciplined as Merrill Lynch about a quarter of a billion dollars on literally the turn of a card, the economic order's resemblance to a gambling den becomes striking. Furthermore when exchange rates and financing terms emulate a yo-yo, as they have during the past fifteen years of floating exchange rates, with serious consequences for jobs, prices, asset values and investment, the gambling den is unsavory.

The flavor of concerns that should have been central to Strange's volume was captured by Keynes in a passage in *The General Theory* that is part of the currency of every economist:

> Speculators may do no harm on a steady stream of enterprise. But the position is serious when enterprise becomes a bubble on a whirlpool of speculation. When the capital development of a country becomes a by-product of the activities of a casino, the job is likely to be ill done. (p. 159)

The implication of Keynes' comment, and therefore of the title that Strange appropriated, is that speculation and efficient investment—

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capital development—are inversely related.

It follows that a volume on *Casino Capitalism* needs to begin with a serious consideration of the determinants of investment in capitalist economies with sophisticated and ever evolving financial structures. Although in the beginning of the book some awareness of the relation between speculation and efficient investment is evident, Strange does not examine closely how the capital development of capitalist economies was affected by the financial evolution of the past decades. What she does do is present in a discursive and somewhat journalistic fashion the development of the international financial structure in recent years as well as a partial review of some interpretations of the import of financial arrangements.

In spite of her approach the volume is useful. Economists, especially those who are comfortable wearing the blinders of neoclassical theory, tend to believe that the evolution of markets and institutions results mainly from the utility and profit seeking behavior of units. To this Strange offers the useful antidote that "a monetary system cannot work effectively unless there is a political authority . . ." (p. 25), i.e., contracts need to be enforced. Therefore the outcomes in both the short and the longer runs are the joint result of decisions by market participants and authorities. Furthermore, economic evolution leads to shifts in the balance of power between markets and states.

This insight helps explain how the Bretton Woods system broke down. The "chaos" that Strange now finds in the international monetary regime is imputed to key decisions and nondecisions, mainly by the United States, both early on in the postwar period and after 1971. Her main point is that domestic concerns dominated decisions in the United States both when the United States acted and when it did not. As a result havoc was played with the order needed for world economic stability.

I would have liked to report that Strange offers a coherent view of the evolutionary processes that have transformed (and continue to transform) the international economy since Bretton Woods, but I cannot. Her basic premise that evolution results from the interplay of market and authority is a unifying concept that is potentially powerful. This potential power is vitiated because Strange suffers from a common British addiction, which is to blame the United States for all that goes wrong, at the same time never holding it responsible for things going well.

It is evident that the world's financial markets have become more fragile and the volatility of rates and instruments has increased. This combined with the irresponsibility and ignorance of governments has adversely affected many national economies. However there was nothing in U.S. economic policy or in the evolution of financial markets that determined that Mexican nationals would literally steal the nation's oil enterprise blind or that Argentina's junta would stash away billions.

The continuum between flight capital and portfolio diversification and the issues this raises is completely absent from Strange's analysis. The mess to which she continuously refers is in good part due to the attractiveness of assets in the United States for international portfolios; this was a factor in the disastrous run up of the dollar as the growth of trade literally forced the authorities to liberalize markets. Strange is not happy with fluctuating rates, but she does not examine the impact of portfolio choices upon exchange rates as a means of explaining why the fluctuations are far greater than the theoretical arguments had indicated. The impact on trade balances of the overvalued dollar that resulted from portfolio choices has reduced the United States to a hat-in-hand giant, dependent upon the favors of trading and investing partners.

Beggar my neighbor is a useful term that describes the behavior of economies that maintain domestic employment and profit levels by devices that depress profits and employment of their trading partners. Keynes' scheme, for a sterile international asset for settlement purposes that the banking authorities of countries with substantial international asset positions would *have* to accept if they persisted in maintaining surpluses, was an attempt to make beggar-my-neighbor policies obviously foolish. In today's global financial market nationals of countries that beggar the United States acquire dollar earning assets, so that such behavior seems to have a positive payoff and therefore is not obviously foolish.

Strange seems to despair of bringing order out of the chaos she sees. Because her view

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does not encompass portfolio choices she does not recognize that the task is easy in principle though difficult in execution: order will replace turbulence when surplus economies that have substantial foreign assets, at present Germany and Japan, are forced by the international arrangements to become deficit countries on their trade accounts.

Professor Strange has been ill served by the lag between the time her thinking for this book was fixed and the time this review is being written, for her integrating premise that the United States is dominant is now obsolete. Nevertheless her message that an analytical system needs to integrate politics, institutions, authority and markets if it is to be useful in helping us understand how systems behave and evolve is valid and important. It survives the gaps in analysis, the chronic blaming of the United States, and even her exasperating errors. She was not well served by her editors: for example Frank H. Knight wrote *Risk, Uncertainty,* (not Certainty) *and Profit,* The New Deal's NRA was the National Recovery (not Rehabilitation) Administration, and Felix Royahtan is at Lazard Freres, not Salomon Brothers.

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600 Industrial Organization; Technological Change; Industry Studies

610 Industrial Organization and Public Policy

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The bigness complex: Industry, labor, and government in the American economy. By WALTER ADAMS AND JAMES W. BROCK. New York: Pantheon Books, 1986. Pp. xiii, 426. $22.95. ISBN 0–394–54721–7. *JEL 87–0525*

In this lively but polemical book, Adams and Brock point to severe deficiencies in the economic performance of U.S. big business, and take issue with both right and left wing views on the appropriate public policy response. From what they refer to as the "Darwinian" persepctive of the right, espoused by economists of the Chicago school and fervently embraced by the Reagan administration, government efforts to curb or reverse the growth of bigness are inevitably counterproductive, since sustained size and power in free markets reflect superior economic efficiency. From the left or "neoliberal" point of view, the government must play an active role in some sort of industrial policy, or tripartite *dirigisme* with industry and labor, to strengthen and revitalize the economy in response to the challenge of world competition.

According to Adams and Brock, both Darwinians and neoliberals make the same fatal errors in attributing the rise and continued predominance of big business in this country to its superior economic performance, and in accepting the corollary proposition that antitrust is an outmoded and harmful pulbic policy concept.

To dispel the "quintessential myth . . . that industrial giantism is the handmaiden of economic efficiency and consumer welfare" (p. xii), Adams and Brock examine efficiency at three levels, considering first operating efficiency, or cost of producing a given product, then dynamic efficiency, or innovation in both products and manufacturing processes, and finally social efficiency, or the desirability of the combination of goods and services produced. The record of big business, they conclude, has been deficient at all three levels. Abysmal performances by the steel and automobile industries weigh heavily in their indictment.

The founding fathers' and Adam Smith's views on economic power and its political control are examined and found inadequate for today's needs, leading to a lengthy discussion of the crucial role of antitrust in promoting competition and controlling private business power. Existing law dealing with collusive conduct is considered effective, provided it is enforced rigorously. But the courts' emphasis on intent and the need to show conduct aimed at monopolizing are not fully consistent with the economic view of monopoly as a structural problem of market power. The law is quite ineffectual in dealing with oligopoly where overt collusion cannot be shown. Finally, antitrust has failed to halt a "general trend toward increased concentration" (p. 204) by merger, because of indifference by the Reagan administration, but more fundamentally because the need to show a lessening of competition or tendency toward monopoly in a narrowly defined relevant market hamstrings the law in an era of conglomerate merger.

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