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event, there seems to be some inconsistency between the estimates in Table 7.5 and Table 2 on this issue. The paper ends with the conclusion that tariff cuts on unprocessed goods will have to be accompanied by steep reductions in protection of processed goods. Otherwise there is a danger that the Uruguay Round will increase effective protection on the developing countries' processing industries.

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***Financial Liberalization and Economic Development: A Reassessment of Interest-Rate Policies in Asia and Latin America.* By Ronald I. McKinnon.** San Francisco, California, 1988. Pp. 48.

In 1973, Ronald McKinnon published a seminal book relating financial development to economic development. The message was that "repressed" financial markets had to be liberalized before economic growth could take off. This message ran counter to that preached by many development economists at the time: their view was that credit to the industrial sector should be subsidized. Moreover, they advocated "forced" saving through inflation. Unless the financial sector was manipulated or repressed in this fashion, they argued, it could not lead the development process.

By now, that view has been almost totally discredited. It is widely agreed that saving and investment should be voluntary, and that interest rates should be at market levels. Only then can substantial flows of loanable funds be generated, and allocated efficiently to the most productive final users. Also, everyone now agrees that high inflation is completely disfunctional since it dramatically distorts relative prices and signals for resource allocation; in addition it leads to socially wasteful hedging.

But what is no longer clear is whether rapid financial liberalization will work unless inflation has already been brought well under control. In the late 1970s and early 1980s, Argentina, Chile, and Uruguay all tried to deregulate their banks and fight inflation at the same time. Real interest rates skyrocketed. There were two unfortunate results. First, dozens of banks failed, or nearly failed and had to be bailed out, because they were induced to make high risk loans. Second, high interest rates sucked in foreign capital, and debt burdens rose sharply. The question thus arises whether financial liberalization ought not to be slowed down until inflation is fully licked.

Professor McKinnon's 1988 monograph begins with some cross-country comparisons of interest rates, inflation, and real financial growth. He shows that countries with high real financial growth — defined as growth in ratios of money supplies to GNP — are also countries with high real output growth. The countries he identifies are Germany, Japan, Korea, Taiwan, and Singapore. He then shows that among developing countries, positive real interest rates have also been associated with high real growth. He concludes that non-repressive financial policies contribute to higher economic growth.

The monograph then looks at post-war Japan. It is argued that despite superficial appearances, the post-war Japanese financial system was not particularly over-regulated. But neither, initially, was the banking system fully liberalized. There were ceilings on interest rates, and banks were not allowed to borrow freely abroad: liberalization began only in the late 1970s. The Japanese proceeded cautiously. First, they established a record of stabilized monetary growth and low inflation; second, they laid an infrastructure of broad and deep non-bank capital markets: securities trading and finance, insurance and pension firms. Third, they never relied on the banking sector exclusively to intermediate capital flows from abroad. The result of this rather gradual liberalization process was that crises were avoided.

Professor McKinnon then looks at Taiwan, which since 1960 has promoted real financial

growth more consistently than any other developing country. Taiwan's ratio of money to GNP is now five times that of the typical Latin American country. Real interest rates have been high, inducing Taiwanese savers to accumulate bank deposits. All this was achieved, even more than in Japan, against a background of very stable monetary growth and low or even negative inflation.

Financial decontrol in Chile provides the contrast. There, between 1976 and 1982, the banks were denationalized and deregulated while inflation was still high and unpredictable. The result was unprecedented levels of nominal and real interest rates, a proliferation of bad loans, and, in 1982-1983, renationalization of the banks. Professor McKinnon concludes that deregulation was excessive and premature.

A review of the Chilean experience takes up the middle one-third of the monograph. At the end is a brief, four-page discussion of Korea between 1979 and 1983. Korea's inflation rate, though much lower than Chile's, averaged 20 per cent during 1979–81. By 1983 it had been reduced to 3 per cent. In contrast to Chile, Korea did not try to use a fixed exchange rate to force price stabilization via international commodity arbitrage: rather, the won was allowed to fall against the U.S. dollar a bit faster than the inflation rate. Also in contrast to Chile, Korea manipulated the nominal interest rate downward, sending an advance signal of central bank intentions to the market. The combined effects of these exchange and interest rate policies were to curb the incentives to incoming foreign capital that plagued the Chileans.

The common thread running through these short case studies is that full financial deregulation must proceed cautiously and only after inflation and inflationary expectations have been brought under control. Nevertheless, Professor Mckinnon's 1973 message survives largely intact: liberalization remains, in his words, "the only game in town". But "[i]t is perhaps a sign of advancing age", he concludes, "that I am now more inclined to emphasize the pitfalls."

* R. McKinnon, *Money and Capital in Economic Development.* (Washington, D.C.: The Brookings Institution, 1973).

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The Population of Peninsular Malaysia. **By Saw Swee Hock.** Singapore: Singapore University Press, 1988. Pp. 342.

Saw Swee Hock has produced a substantial volume of up-to-date information across the full range of demographic components. The task of collecting, organizing, and making as compatible as possible the wide range of statistics cited in the book has been a major one, and Professor Saw is to be congratulated on the substantial contribution he has made to the literature and to the accessible body of data on Peninsular Malaysia's population.

This is a statistician's book, not so much in the complexity of the methodology, which for the most part is simple and clear; nor because it is aimed at statisticians (which is not the case as the information is readily accessible and can be understood by any informed reader); but in the clear focus on numbers and a reluctance (with one or two notable exceptions) to move far from the statistical record, either back into causality and explanation or forwards into implications and consequences. For example, in the earlier part of the book a recurrent explanation of historical developments in the population is that they were determined by the extent of British colonial influence, the level of economic development and type of economic activities, and government policy. This is undoubtedly true, but some elaboration of how this worked and more examples of the impact of the process would have been useful. To some readers, however, the factual and pre-