the real action is to be found. 'Extraordinarily high profits in foreign trade "intermediation" activities', Khan and Hossain remark, 'have encouraged potential entrepreneurs to pursue these activities instead of engaging in manufacturing'. Meanwhile, small domestic producers face competition from aid-financed imports and are hampered by inadequate infrastructure.

Perhaps the most sobering lesson to be drawn from the Bangladesh case study is that official development assistance in an inegalitarian setting can foster and entrench a profoundly anti-developmental order. Foreign capital inflows to Bangladesh (mostly concessional loans and grants) rose from 3 percent of GDP prior to independence to 11 percent in the post-independence period, while domestic savings fell from 8 percent of GDP to 2 percent. Although foreign aid thus had a rather small impact on total investment, it reshaped the country's political economy. It provided the glue for the fragile political alliances of successive ruling cliques, and brought unprecedented wealth to a thin stratum of the population. As the authors observe, however, 'Few of the accumulated riches were channelled into productive investment'.

The experience recounted by Khan and Hossain should be required reading for all students of the theory and practice of economic development.

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This book provides a partial equilibrium treatment of trade policy under various forms of market structure. The market structures considered are predominantly Cournot and Bertrand oligopolies. In these models the concept 'perceived marginal revenue' – that is, marginal revenue ignoring the reaction of other firms – makes it possible for problems to be handled by making use of more or less simple graphs. The main problem in writing an instructive book review here is that new variations of the models are presented after every four pages. Therefore we shall only briefly indicate the most interesting features of the book and add some remarks on their potential usefulness for future research on less developed countries. (A more extensive summary that goes somewhat beyond the length of a book review is available upon request).

An introductory chapter gives a rough indication of what the problems are.

Chapter 2 provides a brief summary of some standard lessons in the
partial equilibrium, perfect competition framework, which is useful for comparison with the new results. Some empirical phenomena are presented as ‘puzzles’.

In Chapter 3 domestic market power is assumed to exist. The main question is whether tariffs are better than quotas. In comparison with the equivalence of tariffs and quotas under perfect competition shown in Chapter 2, the additional problem considered here is the impact of the two alternatives on monopoly power. Tariffs turn out to be better than quotas, except in a cartel situation where, according to the Rotemberg/Saloner argument, quotas raise the expected profits to be gained from breaking the cartel agreement and going to an oligopoly equilibrium. In this latter case, there is the paradox that quotas may increase output because the cartel has to decrease its price in order to make breaking out of the cartel less attractive. In cases other than those of a cartel, tariffs are better because quotas increase monopoly power through limiting access to the market. In the case of domestic monopoly, a second paradox occurs. Tariffs may reduce domestic output, because a continuous increase in tariffs yields an expansion of domestic output at the expense of foreign competitors, and if the latter are driven out of the market, a further increase in the tariff leads to a movement along the demand curve.

Commodity agreements often leave the impression that their aim is higher as well as more stable prices. What the Rotemberg/Saloner argument makes clear here is that a quota – if compared to the tariff – imposes restrictions on the prices which make the cartel viable. Therefore quotas limit the ability of cartels to raise prices. This fact should be taken into account in future arrangements. An interesting example here is the Wheat Agreement of the thirties, which broke down because Argentina was dissatisfied with its quota. Using the Rotemberg/Saloner argument, it is conceivable that lower cartel prices and larger output would have led to higher quotas, making the cartel viable.

Chapter 4 discusses foreign market power under the assumption that the domestic industry is perfectly competitive. The central question here is how to recapture some of the monopoly rents from the foreign firms. The following topics are discussed: price ceilings, minimum import requirements, optimality of tariffs versus subsidies depending on elasticities of demand, kinked demand curves due to specialization, ad valorem versus specific tariffs (subsidies) and quotas under Bertrand oligopoly. Here we find (among other things) the paradox that subsidies may lead to an improvement in the terms of trade in the case of constant elasticity demand curve.

The problem in this chapter is quite similar to the one faced by developing countries in their negotiations with multinational firms. The large variety of instruments rigorously discussed in this chapter may contribute to further research on this problem.
Whereas in the previous chapters there was only one-sided market power, in Chapter 5 two-sided market power is assumed. The central question is how to benefit most in a third market if the good in question is not consumed at home. Of course the latter assumption is an extreme case, and the authors warn the reader not to take it too seriously for policy purposes. The chapter may be characterized as a spirited fight against the argument that subsidization of an oligopolistic firm in a Cournot game is a good policy to gain Stackelberg leadership. The counter arguments are that the result no longer holds if (i) there are more domestic firms, (ii) the foreign reaction to a subsidy is weak, (iii) the game is of the Bertrand type, (iv) there are increasing returns due to fixed costs, (v) there is competition for domestic resources, or (vi) subsidization by the second government in the Cournot game would shift both competitors away from their joint monopoly position, which is desirable on third markets. A paradox in this chapter is that export subsidies may raise the subsidized firm’s profit by more than the subsidy itself.

If the third market is an LDC, all welfare conclusions are of course quite the other way round; if taxes are better for the duopoly under a Bertrand game than subsidies are under a Cournot game, then a Bertrand game implies greater exploitation from the point of view of the LDC consumers. Thus, the trade policy question for developing countries is how to treat different forms of oligopoly.

Chapter 6 investigates whether or not a tariff and a quota are beneficial if there is a two-sided oligopolistic power in the domestic market and consumers demand the product in question. Parts of this chapter are explained too briefly. An interesting result is that under Bertrand oligopoly an equilibrium does not exist in the case of a quota.

Chapter 7 deals with intra-industry trade. Consumers’ preferences are represented by a Spence-Dixit-Stiglitz utility function defined over a given number of differentiated products. These are produced under decreasing unit costs. In equilibrium the number of products is determined endogenously. Trade occurs under some ‘iceberg costs’ (some percentage of the quantity is lost in transit), and economies of scale make trade profitable. The outstanding paradox here is that tariffs may lower prices due to the circumvention of iceberg costs or due to the existence of transport costs in a different framework with price discrimination.

The model in Chapter 7 is very similar to the one used by Krugman to analyze the circular cumulative causation problems of regional development as suggested by Myrdal. So we could expect that the policy lessons drawn in this book may in the future provide some qualitative answers to the regional problems of LDCs.

Chapter 8 examines the question of which of the models use in the previous chapters is empirically most convincing. There are three main
variants: (a) those where the number of firms is fixed, (b) those where entry competes away all profits, and (c) general equilibrium analysis. Within each type of model, assumptions have to be made about demand curves, cost functions and industry conduct. Efforts to check the assumptions are reported. The literature is not very comprehensive at present, but much can be learned from clever approaches to testing the underlying assumptions. The authors finish this chapter by mentioning three suggestive results from quantification efforts: mild protection can raise general welfare; gains from protection are small; and gains from free trade are larger than one would have previously supposed.

Chapter 9 discusses the concept of perceived marginal revenue, the paradoxes mentioned above and the value of these models for policy. The latter, it is argued, is rather limited, because it is likely that a real world government would not be able to decide which model is most relevant. Hence, free trade, though not optimal, may be a good rule of thumb. Suggestions for further research are also given.

All in all the book is nicely written. The formal parts are kept to a minimum. Nevertheless, a good understanding of some of the remaining formal parts did require some pages of computational work (which are available upon request).

An important caveat is that all paradoxes – with the exception of that in Chapter 7 – have been derived for the case when the number of firms is given, which may raise the question of whether these results are relevant for policy at all. Moreover, no good rationale is given for this assumption. Our subjective evaluation concerning the relevance of this book is that the results obtained from the partial equilibrium models may help us to understand those from models with an endogenous number of firms and general equilibrium conditions. There are very few of the latter results in this book, a lack which future research on the above topics should address.

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Development economists have long been interested in the role of labor market and other economic institutions in economic development, particularly as potential explanations of the poor performance of modern industrial