In Defense of Free Capital Markets: The Case against a New International Financial Architecture. By David F. DeRosa, Princeton, NJ: Bloomberg Press, 2001.

David DeRosa's *In Defense of Capital Markets* would make a great secondary textbook for a macroeconomics or development economics course. The focus is on the financial crises in the modernizing world during the 1990s (Mexico, Thailand, Indonesia, Malaysia and Russia). The book's purpose is threefold: (1) to provide foreign exchange (ForEx) policy regime lessons learned for the modernizing world, (2) to provide a primer on this more than $1 trillion per day ForEx market, and (3) to describe why institutions such as the International Monetary Fund (IMF), the U.S. Treasury, and the U.S. Federal Reserve should not intervene to try to forestall these crises, in that these interventions remove national political accountability for a country's macroeconomic policies.

In Defense of Free Capital Markets is more than a free-market argument for reducing the moral hazards and reform stalling caused by bailouts and subsidized loans from the IMF in exchange for superficial "cookie-cutter" fiscal reforms. Throughout the book's survey of the causes and responses to the crises (and several near-crises, such as those in Brazil and Korea), are text boxes that provide basic technical descriptions of the ForEx market. These primers include "Spot and Forward Exchange," "Components of the Monetary Supply and the Basics of Monetary Aggregates," "The Mechanics of Currency Hedging," "What is a Current Account Deficit?" and "More on the Operations of a Currency Board." These instructional primers tie the mechanics of the market to policy implications.

DeRosa makes a case against the "bipolar" ForEx regimes currently supported by mainstream fiscal and monetary economists. The bipolar argument says that a country should either have free-floating ForEx or money that is fixed relative to a major currency (such as the U.S. dollar, the Japanese yen or the Euro). Bipolarity says that ForEx target zones (or floating pegs) are an unnecessary drain on the taxpayers in the modernizing world because pegs mean that a country is using its hard-currency reserves for trading positions in the ForEx market to support a noncompetitive currency that is devaluing because of unsound in-country macroeconomic polices. These hard-currency reserves are gained from central bank or treasury department interventions in nonfloating (nonmarket) private- and/or public-sector international financial transactions, that is, ForEx.

DeRosa shows that a fixed regime is also an unnecessary drain on the taxpayer unless it is in effect a complete "dollarization," that is, unless a country actually adopts a hard currency as its medium of exchange. The study

The views expressed in the article are my own and in no way should be construed to be that of USAID or the U.S. government.

supports this recommendation by showing that all of the crises in the 1990s were caused by unsupportable—meaning fixed or pegged—ForEx regimes.

Policymakers use a currency board to bridge the gap between a perceived heightened political risk, which causes a devaluation or other uncertainties (such as an actual political crises) and prevents foreign direct investment in a country, and the need of a country for this investment. These countries also face the need to support citizens' purchasing power in the international market. A planned and publicized process of dollarization or a devaluation that leads to a free-floating currency is used to soften the blow of political crises. However, DeRosa shows that these short-term solutions in the end cause a taxpayer bailout.

DeRosa summarizes his survey by stating that, because of the modern ForEx market, there is no longer a role for the IMF (which was created to support the gold standard). He acknowledges that "it is going to take a colossal effort to convince Washington to yield to the basic thesis, that crisis nations should look after themselves and that the private sector should be free to settle its own disputes with distressed and indebted nations".

Cameron M. Weber
Credit Program Controller
United States Agency for International Development (USAID)