BOOK REVIEW

FALSE ECONOMY

– A surprising economic history of the world

By Alan Beattie

Reviewed by

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"History has many cunning passages, contrived corridors and issues..." says Thomas Eliot. Economic history as narrated by Alan Beattie in this book would seem to bear out the poet's haunting admonition. "The paths taken by different countries largely reflect the decisions they took, even if they were unaware they were making them. Had they made other choices, things might have turned out very differently".

This statement by itself with shades of hypertext fiction is almost threadbare, hardly the stuff for a seminal work. But Beattie elaborates his argument through a corpus of historical facts and their interpretation. Parts of his work are scholarly, but mostly it avoids the aridity of a research study in favour of an engaging treatment of a theme that is, after all, very much in the realm of public discourse today: trade and economic policy of nations.

Beattie's basic proposition is that countries that succeed are those that are flexible enough to learn from experience and that do not become captured by groups whose interests are sharply at odds with those of the country as a whole. The illustrative case that he describes is that of the United States and Argentina. As young and dynamic economies, these were rivals one century ago, offering a difficult choice in terms of opportunities to potential emigrants from Ireland

and Italy. Similarities between them included: vast land and agricultural wealth, westward movements enhancing in each case their attraction for mass emigration from Europe, possibilities in industry and rise to prosperity by 1914. But their differences in the Golden Age of globalization from 1880 to 1914 foreshadowed the continued dynamism of the one – the US – and the eventual decline of the other – Argentina. Beattie describes their distinctive development pathways: the US had a preponderance of high productivity farms characterized by smaller family holdings as against Argentina's elite of rich landowners and largely low-skilled Italian and Irish agricultural labour; the US learned from the European experience particularly in industrial entrepreneurship and creation of the financial sector while Argentina neglected those vital aspects to its cost; the US economic policy accorded primacy to the workings of the free market, but Argentina's preference was for cozy, safe monopolies protected by the government. In the following years, the "nimble and productive" industrial sector of the US, coupled with a resourceful financial sector, was found to be well placed to take advantage of the twentieth century's possibilities in contrast to Argentina's policy of endlessly borrowing foreign money on the doubtful strength of its grain and meat exports. Divergence of policy choices in the years after World War II – dynamism of the market economy and adaptive democracy in the US vs. import substitution, autarchy and long spells of dictatorship in Argentina – set the two countries deeply in their respective trajectories. With the experience of the largest government bankruptcy in history in 2001, Argentina, once the rival of the US, demonstrated that it was history and choice, not fate that determined which did what.

Pressing the argument further, Beatty makes the point that at dozens of different points of departure over the previous two centuries, it could have gone the other way round and that today it is the United States that may be deceiving itself with the thought that like Argentina over the years, "everything was fine as long as it could keep borrowing", thus exposing itself through its external indebtedness to the biggest threat to its financial system and economy since the Great Depression. "If America fails to recognize the flaws and correct them, as it slowly and painfully learned to do on that earlier occasion, the trajectory of its future wealth and power will be lowered… But its rise was not preordained and neither is its continued preeminence". Rather than end on such a Cassandra-like pronouncement, the author could have gone on to analyze what the US has as viable policy options in the current phase of globalization.

As with countries and national economies, history and choice are seen by the author to have played a determining role in the evolution of cities – from imperial Rome, an avaricious and parasitic city of rentiers, bureaucrats and hangers-on, which influenced the running of an empire and eventually its dissolution, to London, Paris and Moscow. Bloated capital cities that have resulted from the care lavished on them by unstable governments, dull and remote capitals created deliberately to be so like Washington, Canberra Wellington and Ottawa, differently managed urban expansion of Shanghai and Mumbai and the pattern of mass urbanization without mass industrialization in Africa – all speak of the central role that cities play as well as of the importance of the way the cities are run in the economic history of nations.

International trade based on factor intensities receives a similar treatment from the author in terms of the concept of virtual or embedded water. While it made perfect sense for Egypt, which is endowed with the water resources of the Nile, to export wheat to ancient Rome, it makes equally perfect sense at present for both Europe and Egypt itself to import their wheat from other sources where there are larger water resources and for populous Egypt which is one of the world's drier and hence relatively inefficient producers of wheat to be importing water from wetter countries in the form of embedded water of which there is so much in wheat. Such commerce in embedded water, much as it is beneficial all round and happens on its own, is constrained by transport costs, inertia and political resistance. While food security is a pre-occupation in the Middle East and North Africa, to the extent of countries subsidizing the overuse of water by their farmers through subsidies, the fact is that in terms of water footprint the Middle East started running short since the mid-1970s, but the region along with

Australia abounds in evidence of irrational use of water in export production. The author's view is that more trade in embedded water is needed – another way of advocating global trade on the basis of comparative advantage. He sees pursuit of national self-sufficiency in food as an impediment. The answer to that is : so much the worse for the idea, because protection to domestic farming will remain fundamental to the economy and way of life of many developing countries.

The paradox of many countries being providentially endowed with rare and precious minerals but becoming worse off for having found them is another question addressed in the book. As regards oil, gas and minerals, the author points out that they generally require high technology skills, offshore platforms and vast systems of pipelines operated by a relatively small number of employees, so benefits mostly accrue to the owners of the equipment and the business and to a relatively small number of workers. This in combination with the phenomenon of Dutch disease and the adverse effects of idle wealth has repeated itself as a pattern not only in the well-known case of Zambia but also in Saudi Arabia which has a high unemployment of 25% concentrated among the youth that has proved vulnerable to the appeal of radical Islam. Iraq has accumulated a huge debt burden on the strength of its oil revenues while in Russia the dominance of oil and gas in the economy has led to the weakening of democracy. And then there are the traumatic experiences of Angola, Sierra Leone and the Democratic Republic of Congo. But it is not an unremitting tale of woe for countries that are mineral and oil-rich. For these to achieve a different outcome in terms of economic well-being two things need to happen, says Beattie. One, the revenue deriving from the resource needs to be managed in a way that does not distort the rest of the economy. Two, the revenue needs to be sufficiently fenced off from the acquisitive interests and the threat of political expropriation. Botswana is the best example in Africa; Beattie also mentions those of Malaysia and, more debatably, Indonesia. But the conditions that led to Botswana's success – a tough revenue-sharing agreement with the foreign extracting company, prudent exploitation of the resource, the setting up of a national fund for the development of the resource and sound political institutions to impose and oversee policies – exist in few African countries.

Islam and economic growth is another theme that Alan Beattie takes up with reference to the rise and decline of Islamic societies in the course of history – tracing it to the academic debate on religion and capitalism that originated with the often misrepresented but at any rate much disproved thesis of Max Weber. Since Islamic economies in their heyday just like the Chinese had been enormously successful in increasing wealth by trade and developed a sophisticated set of financial and trading institutions, Alan Beattie argues that what matter is less the precise doctrines than the uses to which religion itself is put and the willingness of societies to change or reinterpret laws grounded in religious belief. In the case of Islamic societies, their failure to open up further since the fourteenth century, their adherence to centralized states, their inability to evolve anything like the idea of the business corporation as in the Christian world were all facts that testify to how a religion's political role rather than ideology could hamper economic development. A similar process, namely ossification of social strata, also prevented India from adapting to new circumstances over the centuries while in China's case it was a deliberate policy of turning inward and desisting from trade with the rest of the world starting in the fourteenth century. Beattie's conclusion from all this is that while it is easy to infer causality from a casual look at economies and dominant religions, the reality is much more complex and more optimistic. So Muslim societies, like China and India today, can choose to succeed.

In his treatment of the role of lobbies in global trade, Alan Beattie provides a lucid analysis of the oddities in the Doha round of the WTO. The effect of reforming farm subsidies through the Doha round would cause only 1.4% average fall in the income of Japanese farmers; in the case of the US it would be statistically zero – yet, these countries have put up the heaviest roadblocks in the negotiations. For another, it is the failing industries which tend to get tariff protection so that the farmers' protectionism cause in France and elsewhere often wraps itself in the flag of nationhood.

Beattie traces the history of trade lobbies through the evolution of Britain's business in cotton handled by the East India Company and sugar, involving the West Indies colonies both pitted against the free trade movement. He points out that the abolition of slavery undermined the British vested interests in the sugar business which finally received their quietus from the parliamentary act in 1846 abolishing preferential duties. But he fails to complete the picture by bringing in the story of the Indian indentured labour to substitute for the slaves in the West Indies, Mauritius and Fiji and to shore up the benefits of the sugar interests through this iniquitous system.

On the other hand, Beattie brings out a crucial fact: the EU's Common Agricultural Policy that discriminates against efficient foreign agricultural producers through protection continues because it costs an average European family only about a thousand euros a year, not enough of a burden to make them campaign against the aggregate deadweight loss of welfare for the economy and the harm it causes to foreign producers. And in all debates on free trade and protection, whether it is in the past or now self-interest of the lobbies, is what clearly shows through.

There is a story of international trade in the last two centuries when its structure and process underwent transformation across several dimensions – from speed and efficiency of maritime transportation to the law of one price. Beattie relates this story with the trained facility of a journalist, evoking highlights like the disaggregated manufacturing and assembly line in East Asia. As for African countries yet to benefit from the present global supply chains, he asks the rhetorical question as to why they do not grow the high-value crop of coca and make cocaine rather than be a victim of the structural weakness of their foreign trade. More seriously, however, he observes that the real constraints in developing countries to competing with foreign producers are not of trade policy but the lack of something to sell and the inability to get it to market cheaply. Africa's pronounced disadvantages in this regard have mostly to do with the way it had been exploited by the colonial powers, beginning with the slave trade and the remorseless exploitation of its natural resources. Africa has been dealt a poor hand, says Beattie, but for the most part it could have played its cards a great deal better. Again, it is a question of governments of African countries making choices that have good consequences. Such choices and their implementation in Africa are bound up with a complex skein of constraints that are tragically peculiar to Africa.

Given the scope of the book, its treatment of corruption merits particular attention. Alan Beattie has some interesting views on the subject; notably, he is intrigued that East Asian countries have done well despite a long history of corruption. His overall view is that if corruption is unavoidable, it is best to have it in as efficient and streamlined a way as possible, illustrating the principle with accounts of Tanzania's honest leader Julins Nyerere leaving his people poor and, on the other hand, Indonesia's crooked leader Suharto achieving prosperity for his people. It is an amoral proposition, even faultless in its formulation, but with troubling implications all the same. Since corruption, in the ultimate analysis, is a moral issue one also senses an implied assumption here that a different moral standard for developing countries may be in order. On the other hand, the author's examination of systemic corruption in British India, Portuguese Goa and the United States brings out some interesting insights.

Beattie's comparative study of Russia, India and China in their current shift towards a market economy is also instructive. The economic turmoil in Russia in 1998 and the resulting backlash against the ideas of a free market economy and democracy are seen as evidence that Russians are not uncomfortable with the present centralization of power, but the dichotomy of a nascent market economy and an authoritarian and control-obsessed government would remain problematic. The Chinese, however, are perceived as having managed the combination of a one-party political structure with a limited form of market economy, helped by several factors including good models to follow in the region. The analysis of the Indian situation is more detailed, with focus on the caste system and challenges of economic development owing to the "sclerotic and inefficient state", but being a democracy it may not fear a revolution or some similar political upheaval in future, unlike China which will at some point have to undergo a traumatic change.

Beattie's picture of the larger world, as reflected in WTO negotiations under the Doha round, shows the recurrence of much the same patterns and problems as have characterized world trade throughout history, with the leading players influenced by entrenched interests or an alliance of interests. To them, Beattie's advice, which also sums up the conclusions of his book are as follows: "call the bluff of small interest groups who say that they have the welfare of the whole country at heart. For very poor nations, worry less about trade policy and more about customs procedures. Concentrate on rooting out the forms of bribery that will do the most damage and worry less about corruption that is moderate and predictable. Be aware when your country is getting struck on the wrong path and be alert for opportunities to shift it".

There goes the distilled essence of the set of ideas from this book, containing interesting nuggets from universal economic history, even if not quite conveying a coherent theme through its diverse lines of enquiry. For a clearer and more comprehensive exposition of a revisionist view on economic history, partly voicing Beattie's thoughts, one would need to turn to Eric S. Reinert who argues (in his book "Why Rich Countries got Rich and Why Poor Countries Stay Poor") that the world's wealthy nations who now belabour developing countries on the need for free trade have themselves been driven by a combination of government intervention, initial protectionism and strategically timed introduction of free trade and investments.

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