

**East Asia's Economic Success: Conflicting Perspectives, Partial Insights,  
Shaky Evidence**



Robert Wade

*World Politics*, Volume 44, Issue 2 (Jan., 1992), 270-320.

---

Your use of the JSTOR database indicates your acceptance of JSTOR's Terms and Conditions of Use. A copy of JSTOR's Terms and Conditions of Use is available at <http://www.jstor.org/about/terms.html>, by contacting JSTOR at [jstor-info@umich.edu](mailto:jstor-info@umich.edu), or by calling JSTOR at (888)388-3574, (734)998-9101 or (FAX) (734)998-9113. No part of a JSTOR transmission may be copied, downloaded, stored, further transmitted, transferred, distributed, altered, or otherwise used, in any form or by any means, except: (1) one stored electronic and one paper copy of any article solely for your personal, non-commercial use, or (2) with prior written permission of JSTOR and the publisher of the article or other text.

Each copy of any part of a JSTOR transmission must contain the same copyright notice that appears on the screen or printed page of such transmission.

*World Politics* is published by Johns Hopkins University Press. Please contact the publisher for further permissions regarding the use of this work. Publisher contact information may be obtained at <http://www.jstor.org/journals/jhup.html>.

---

*World Politics*  
©1992 Johns Hopkins University Press

JSTOR and the JSTOR logo are trademarks of JSTOR, and are Registered in the U.S. Patent and Trademark Office. For more information on JSTOR contact [jstor-info@umich.edu](mailto:jstor-info@umich.edu).

©2001 JSTOR

## Review Article

# EAST ASIA'S ECONOMIC SUCCESS Conflicting Perspectives, Partial Insights, Shaky Evidence

By ROBERT WADE\*

Alice Amsden. *Asia's Next Giant: South Korea and Late Industrialization*. New York: Oxford University Press, 1989, 379 pp.

Stephan Haggard. *Pathways from the Periphery: The Politics of Growth in the Newly Industrializing Countries*. Ithaca, N.Y.: Cornell University Press, 1990, 276 pp.

Helen Hughes, ed. *Achieving Industrialization in East Asia*. Cambridge: Cambridge University Press, 1988, 377 pp.

Don't listen to "comparative advantage" advice. Whenever we wanted to do anything the advocates of comparative advantage said, "We don't have comparative advantage." In fact, we did everything we wanted, but whatever we did, we did well.

—Governor Park  
Korea Central Bank<sup>1</sup>

I do not believe that the firms could have organized a supercomputer project themselves because businesspeople did not believe in the feasibility and profitability of this kind of supercomputer in the near future. Our pressure or promotion was needed.

—Senior MITI official<sup>2</sup>

### THE NEOLIBERAL INTERPRETATION OF EAST ASIAN SUCCESS

OVER the past two decades a literature big enough to fill a small airplane hangar has been produced on the causes of East Asian economic success. Of that which is economically literate the mainstream adopts what could be called a "neoliberal" interpretation. This says that

\* The author acknowledges Adrian Wood, Ronald Dore, Manfred Bienefeld, Olivia Cox-Fill, Julie Gorte, and Michael Lipton. The usual exoneration applies with more than usual force.

<sup>1</sup> Quoted in Yoginder Alagh, "The MITI and the Developing Asian and Pacific Region: A View from South Asia," *Asian Development Review* 7, no. 2 (1989), 116. I thank Devesh Kapur for this reference.

<sup>2</sup> Cited in Martin Fransman, *The Market and Beyond: Cooperation and Competition in Information Technology in the Japanese System* (Cambridge: Cambridge University Press, 1990), 176.

the East Asian countries were more successful than others in terms of long-run growth because, in essence, they stuck more firmly to the prescriptions for short-run efficient resource allocation derived from the theorems of neoclassical economics.

Neoliberal here refers to a subset of neoclassical economics. Its members believe that as a general rule the neoclassical prescriptions for short-run optimal resource allocation are also the core recipe for maximizing the rate of long-term growth. Other neoclassicals, by contrast, draw more of a distinction between the two kinds of analyses, introducing a more complex array of variables into growth issues than they use for questions of optimum resource allocation. Neoliberals are inclined to think that "getting the prices right" is both a necessary and a nearly sufficient condition for maximizing the rate of long-term growth ("getting" in the sense of letting prices find their right levels, and "right" in the sense of the relative prices established in freely operating domestic and international markets); other neoclassicals would say that it is no more than necessary. Relatedly, neoliberals believe that most market failure is a result of government policies and that, even in those uncommon cases where market failure occurs for other reasons, the welfare costs of remedial government intervention can often be expected to be greater than the welfare gains. This weighting of probabilities is based on a relatively coherent theory of perverse government, as set out, for example, in the works of William Niskanen and David Colander.<sup>3</sup>

In the neoliberal view, growth is a natural or inherent property of capitalist economies. Governments have an important role in providing those "public goods," such as physical infrastructure, law enforcement, macroeconomic stability, and perhaps education, that are difficult to arrange through private contracts. But beyond that they should not go, except in those rare cases of market failure referred to above. The problem is that most governments have in fact gone well beyond these limits,

<sup>3</sup> Niskanen, *Bureaucracy and Representative Government* (Chicago: Aldine-Atherton, 1971); and Colander, ed., *Neoclassical Political Economy: The Analysis of Rent-seeking and our Activities* (Cambridge: Ballinger, 1984). For an academic example of neoliberal development economics, see Deepak Lal, *The Poverty of Development Economics* (London: IEA Hobart Paperback no. 16, 1983). For a policy paper based on neoliberal assumptions, see, e.g., *Accelerated Development in Sub-saharan Africa: An Agenda for Action* (Washington, D.C.: World Bank, 1981), commonly known as the Berg report. For an example of tendentious use of evidence in the neoliberal cause, see Michael Michaely et al., *Liberalizing Foreign Trade: Lessons of Experience from Developing Countries*, vols. 1-7 (Oxford: Blackwells, for the World Bank, 1991), esp. summary volume. For a critique of neoliberalism, see Christopher Colclough, "Structuralism versus Neo-liberalism: An Introduction," in Colclough and James Manor, eds., *States or Markets? Neo-liberalism and the Development Policy Debate* (Oxford: Oxford University Press, 1991). For a critique of the study by Michaely et al., see David Evans, "Institutions, Sequencing, and Trade Policy Reform" (Geneva: UNCTAD, May 1991).

adopting policies that interfere, intentionally or not, with the free working of markets. East Asian governments have stayed within these limits. Hence, East Asian economic success, which in turn resoundingly vindicates the general neoliberal prescriptions.

Those who outline this argument as a preliminary to a critique often find themselves accused of setting up a straw man; no respected economist is as simplistic as that, they are told. So it is important to establish that this *is* a fair short summary of the core neoliberal position, that it is what respected economists say. Enter Helen Hughes,<sup>4</sup> editor of *Achieving Industrialization in East Asia*, definitely nobody's idea of a straw man. What policies have been critical to economic success in East Asia? she asks. Her answer:

The conclusion is that "unshackling exports" (that most of the East Asian countries had themselves at first shackled) has been *the key to success*. However, it is also clear that successful performance needs several [other] policy strands. Political stability and the rule of law are essential. Economic policies apparently distorted prices less than was the case in most other developing countries; macroeconomic management was relatively successful, all economic sectors, particularly agriculture,<sup>5</sup> were developed, and public investment in social and physical infrastructural facilities was productive. Where these economic conditions did not prevail, as in the Philippines, the economy faltered. Governments thus provided the environment for growth; but private enterprise, despite risk and uncertainty, made the investments necessary and through exposure to international competition became efficient and profitable. (pp. xv-xvi)

As for replication by poorer countries, "There seems little doubt that if other developing countries had followed similar economic policies they would also have grown more rapidly and would thus have been able to alleviate the poverty of their low income groups as well as avoiding high national indebtedness"<sup>6</sup> (p. xvi). This is cast in the past tense—"if other

<sup>4</sup> Professor of economics and director of the National Center for Development Studies at the Australian National University, formerly a high-ranking official at the World Bank.

<sup>5</sup> It is not clear what Hughes means at this point, but she presumably means that the government directed its attention to developing agriculture, among other sectors. But state policies toward agriculture in Korea and Taiwan differed greatly from standard market-based prescriptions. For an account of the highly dirigiste role of the state in developing Korean and Taiwanese agriculture, see Wade, "South Korea's Agricultural Development: The Myth of the Passive State," *Pacific Viewpoint* 24 (May 1983); idem, *Irrigation and Agricultural Politics in South Korea* (Boulder, Colo.: Westview Press, 1982); Mick Moore, "Economic Growth and the Rise of Civil Society: Agriculture in Taiwan and South Korea," in Gordon White, ed., *The Developmental State in East Asia* (London: Macmillan, 1988).

<sup>6</sup> In addition to the chapters mentioned in this paper, the book includes papers by Chenery (on alternative views on industrialization in East Asia), Parry (on the role of foreign capital), Wade (on the role of government), Harberger (on growth, industrialization, and economic structure in East Asia and Latin America), Lal (on ideology and industrialization in India and East Asia), Hirano (on Japan as a model), Haggard (on the politics of industrialization

developing countries had followed"—but it is clearly intended to apply today.

According to Hughes, then, economic development really is simple. The experience of East Asia confirms Adam Smith's insight of two hundred years ago that "little else is requisite to carry a state to the highest degree of opulence from the lowest barbarism, but peace, easy taxes, and tolerable administration of justice; all the rest being brought about by the natural course of things."<sup>7</sup> Conversely, governments of the less successful developing countries stand condemned for holding back the escape from poverty and high national indebtedness, among other ills, by interfering with markets and undersupplying public goods.

James Riedel,<sup>8</sup> also nobody's idea of a straw man, concludes his overview essay in the Hughes volume on the same note: "The policy lessons that derive from the experiences of the East Asian countries are simple and clear-cut, and for that reason are all too readily ignored or dismissed" (p. 38). The lessons are, above all, that

neo-classical economic principles are alive and well, and working particularly effectively in the East Asian countries. Once public goods are provided for<sup>9</sup> and the most obvious distortions corrected, markets seem to do the job of allocating resources reasonably well, and certainly better than centralized decision-making. That is evident in East Asia, and in most other parts of the developing and industrial world, and is after all the main tenet of neo-classical economics. (p. 38)

What evidence does Riedel provide? He readily admits that "governments have been *deeply involved* in the economies of all the East Asian countries," including Hong Kong.<sup>10</sup> They have been "actively engaged in managing the system of industrial incentives." For example, "The level of protection in the Republic of Korea, apart from that faced by exporters, has remained *high*" (p. 32; emphasis added). One might have expected him to address the obvious next question. If the level of protection on domestic sales has remained high (not further specified), why has Korea's economic performance been so good, given that the most central of all neoclassical development prescriptions concerns the benefits of nearly free trade? He agrees that "the area of government involvement

---

in Korea and Taiwan), Mackie (on the politics of growth in ASEAN), O'Malley (on culture and industrialization).

<sup>7</sup> Smith, *An Enquiry into the Nature and Causes of the Wealth of Nations*, ed. E. Cannan (New York: Random House, 1937).

<sup>8</sup> Professor of international economics at The Johns Hopkins University.

<sup>9</sup> It is possible to define a public good to permit huge amounts of state activity.

<sup>10</sup> But Riedel also says (Hughes, 35) that the Hong Kong government "has confined itself largely to *minimal* functions," from which we could infer that he intends the term "deeply involved" to cover involvement limited to "minimal [Smithian] functions."

most difficult to evaluate is the management of the system of incentives which guide private economic activity." Nevertheless, he leaves the reader with the strong presumption that "governments' main contribution to economic success in the East Asian countries was . . . principally in *removing the obstacles to growth which they themselves put there* in the first place," that East Asian governments made their task unnecessarily complicated by having to "anticipate and offset the market distortions that result from [their own] *dirigiste* strategies of industrialization" (p. 37; emphasis added). So while the fact of "government intervention" in East Asia is acknowledged, it is given scant analysis; the effects of intervention are asserted with virtually *no* basis in evidence. In particular, key challenges, such as the combination of Korea's admitted high protection with its admitted good performance, are ignored. The dirigiste strategies of industrialization are presented as mistakes that required further government intervention to offset them (such as export subsidies to offset import protection); the idea that those dirigiste strategies might have *helped* industrialization is not even entertained.

The chapter in Hughes by Seiji Naya<sup>11</sup> displays the same habits of thought. Naya, too, recognizes that "the incentive system applied in the NICs was, of course, not entirely free of bias. Some industries, particularly intermediate and engineering goods industries, enjoyed heavily protected domestic markets at the expense of traditional consumer goods industries" (p. 84). But he gives no evidence for the magnitude of the incentive bias and says not a word about its effects on output. He merely repeats the conventional conclusion that "the better performance of the NICs with respect to economic growth, employment and income distribution compared to the resource-rich ASEAN countries can, to a large extent, be related to a combination of more thorough and timely adoption of outward-looking, market-oriented policies and rapid improvements in human resource and institutional development" (p. 93). Neither he nor the other contributors to *Achieving Industrialization in East Asia* examines issues having to do with technological change. As in most simple neoclassical writing, technology is assumed away, treated implicitly as an intermediate dependent variable that adjusts easily once the correct (trade-policy-derived) incentive structure is set in place in the economy as a whole.<sup>12</sup>

<sup>11</sup> Director of the Resource Systems Institute at the East-West Center, formerly the chief economist of the Asian Development Bank.

<sup>12</sup> There is, however, a neoclassical economics of induced innovation, both technological and institutional, that is serious and interesting, though lacking (1) a supply side of science, (2) a theory of government-directed institutional and technological innovation (powered by things other than factor scarcities), and (3) a theory of institutional inertia.

Much of what these neoliberal authors say about the causes of East Asian success is unexceptional. Hughes is right to highlight the role of private enterprise—although it has been a long time since any serious economist urged public enterprises as the main vehicle of development. She is right to imply that in many less developed countries public policies have made matters worse, and that these countries could have done better had their policies been more like East Asia's. And Riedel is quite right to say that markets allocate resources better than do central decision makers without markets (if these are the only choices). But this is pretty anodyne stuff. The problem is that these and other neoliberal economists shy away from subjecting their beliefs to serious empirical test, yet they are powerful enough to get those beliefs widely accepted, especially via international financial institutions like the IMF and the World Bank.

#### EAST ASIA'S SUCCESS?

Let us first consider the starting point of the whole exercise, the claim that what is to be explained is the superiority of capitalist East Asia's economic performance compared with that of other "newly industrialized," "late developing," "intermediate," or "semiperipheral" countries. We concentrate on South Korea, which has received the bulk of the attention. Has Korea really been outstandingly *successful*? It is to be remembered that as recently as the mid-1970s some prominent analysts on the Left were writing off Korea as "a house built on sand," a "tottering neo-colony," an export platform whose success would last only as long as wages were kept below those of competitors—this, in explicit contrast to the more viable communist economy of the North.<sup>13</sup> The analysts lambasted the South with chapter titles like "GNP vs. the People" and "South Korean Society: The Deepening Nightmare."

It is true that Korea's record contains plenty that could qualify a eulogy of growth. Life expectancy at birth (sixty-nine years in 1986) is below Sri Lanka's, yet Sri Lanka's per capita income is only a sixth of Korea's; and Korea is in the bottom half of a life expectancy ranking of upper-middle-income countries.<sup>14</sup> The environment has become seriously polluted: Seoul's air is said to have one of the highest concentra-

<sup>13</sup> Aidan Foster-Carter, "North Korea: Development and Self-reliance, a Critical Appraisal," *Bulletin of Concerned Asian Scholars* 9, no. 1 (1977). See also Gavin McCormack and John Gittings, eds., *Crisis in Korea* (Nottingham: Bertrand Russell Peace Foundation, for Spokesman books, 1977). For more discussion on interpretations of South Korean development, see Wade (fn. 5, 1982).

<sup>14</sup> World Bank, *World Development Report 1988* (Washington, D.C.: World Bank, 1988), Table 1.

tions of sulfur dioxide in the world.<sup>15</sup> Its traffic crawls at not much more than half the speed of traffic in New York or London. Much of the country's urban tap water is said to be unfit for drinking. There is some evidence that the application of exceedingly high levels of chemical fertilizer to meet government targets has harmed the chemical composition of the soil.<sup>16</sup> And in terms of civil and political rights no one holds up South Korea as a model, except in comparison with the North. In the 1970s it came about halfway down a ranking of civil and political rights in middle-income countries; in 1983, about two-thirds of the way down.<sup>17</sup> Surveillance by the secret police has been pervasive, and a formidable coercive capacity remains in place. Independent labor unions have been repressed. The male-female industrial wage gap is, according to Amsden, about the biggest in the world, rivaled only by Japan's. What has happened to such values as civic responsibility, sacrifice, loyalty, and happiness I do not know.

Moreover, Korea's economic importance is often exaggerated, as though it is on the verge of becoming another Japan or Germany (as in Amsden's title, *Asia's Next Giant*). In fact, it accounts for only 0.87 percent of world population (against Japan's 2.6 percent) and only 0.8 percent of world GDP (against Japan's 15.4 percent). In area it is a quarter the size of Japan and less than a quarter of California. Its per capita U.S. dollar income, expressed as a percentage of the average of the Northwest European and North American core, was only 8 percent in 1960, 13 percent in 1980, and 20 percent in 1988. These figures pale alongside Japan's: 23 percent in 1960, 76 percent in 1980, 118 percent in 1988.<sup>18</sup> Korea is hardly a "miracle" in the Japanese context. And it remains, as in 1960, by far the poorest of the four East Asian newly industrialized countries (NICs): per capita income in 1986 was only two-thirds of Taiwan's, one-third of Hong Kong's, and less than one-fifth of Japan's; and it was one-quarter of Britain's and 14 percent of the U.S.'s.<sup>19</sup>

This having been said, Korea is nevertheless outstandingly successful by at least four key indicators. The first is the gain in its relative eco-

<sup>15</sup> *Economist*, "The Environment: A Survey," September 2, 1989, p. 7; Sonya Hepinstall, "A Smell of Success in the Battle against Pollution," *Far Eastern Economic Review*, July 18, 1989, p. 70. Cited in Waldon Bello and Stephanie Rosenfeld, "Dragons in Distress: The Crisis of the NICs," *World Policy Journal* (September 1990).

<sup>16</sup> Wade (fn. 5, 1982), 103 and chap. 5.

<sup>17</sup> Wade, *Governing the Market: Economic Theory and the Role of Government in East Asian Industrialization* (Princeton: Princeton University Press, 1990), 254.

<sup>18</sup> Giovanni Arrighi, "World Income Inequalities and the Future of Socialism" (Binghamton: Braudel Center, State University of New York, 1990).

<sup>19</sup> The figure was \$2,372 in 1986, as against \$17,475 for the U.S. and \$8,870 for the U.K. See Wade (fn. 17), Table 2.1.

conomic command over world resources, measured by the increase in per capita income expressed in U.S. dollars.<sup>20</sup> In 1962 Korea ranked 99th in the world, and U.S. aid officials are said to have wondered audibly "whether [it] was to remain indefinitely a pensioner of the United States."<sup>21</sup> A quarter century later, in 1986, it was 44th. In Giovanni Arrighi and Jessica Drangel's large sample of countries, Korea is the only country to have jumped from their "periphery" to their "semiperiphery" between 1938-50 and 1975-83 (Taiwan would have been there, too, had it been included).<sup>22</sup> Its performance was especially good over the 1980s. Whereas in 1976 its per capita income (\$670) was less than Malaysia's and a bit more than half of Mexico's and Brazil's, by 1988 its figure of \$3,600 was far above the figures for Malaysia, Mexico, and Brazil and about equal that for Portugal.<sup>23</sup> Indeed, Korea (and Taiwan) stand out from virtually all other countries of Eastern Europe and the Third World for having *reduced* the income gap with the Northwest European and North American core between 1980 and 1988. Everywhere else the

<sup>20</sup> Note that use of per capita dollar income to measure increasing or decreasing gaps between countries or regions is always problematic because of the complications introduced by changing real exchange rates (to say nothing about intracountry income distribution). To get a gap measure that more accurately reflects welfare, one should use purchasing power parity measures of income (now available in the tables in the World Bank's annual *World Development Report*) or qualify the dollar gap by changes in real exchange rates (and add terms of trade changes as well). This is especially important in the context of the trend reported later in this paragraph, of a dramatic widening of the gap between core countries and almost everywhere else during the 1980s. The polarization would be less, though still serious, if either of these adjustments were made. Adrian Wood finds that for the period 1965-83 about two-thirds of the increase in the per capita *GNP* gap between industrial market economies and low-income countries, measured in current U.S. dollars, was due to real changes in the exchange rate; for middle-income countries the gap would have narrowed but for real changes in the exchange rate. See Wood, "Global Trends in Real Exchange Rates, 1960-84," *World Development* 19, no. 4 (1991); and idem, "Puzzling Trends in Real Exchange Rates: A Preliminary Analysis" (Mimeo, Institute of Development Studies, Sussex University, Brighton, 1986). Arrighi's important work is marred by insufficient attention to these matters; the same holds for my own use of per capita income comparisons (fn. 17). Anyone concerned to explain trends in the distribution of world wealth or income must address the question of the real income effects of the secular appreciation of the exchange rates of industrial countries relative to those of the rest of the world. Have such changes caused systematic changes in income distribution between or within countries or regions?

<sup>21</sup> Edward Mason et al., *The Economic and Social Modernization of the Republic of Korea* (Cambridge: Harvard University Press, 1980), 181. This claim, that many observers in the 1950s and into the early 1960s considered Korea a "basket case," is often repeated, the better to highlight the subsequent success. I have not seen actual evidence from documentary or other sources. Larry Westphal says (in a personal communication) that Mason et al. drew on his own verbal report, based on U.S. documents that he saw but did not copy while employed as a foreign adviser in the Korean planning agency in the late 1960s. To my knowledge the "basket case" story rests on this.

<sup>22</sup> Arrighi and J. Drangel, "The Stratification of the World-Economy: An Exploration of the Semiperipheral Zone," *Review* 10 (Summer 1986).

<sup>23</sup> World Bank, *World Development Report* (Washington, D.C.: World Bank, 1978, 1990), Table 1.

dollar gap has widened calamitously.<sup>24</sup> Brazil's average income, for example, rose from 12 percent of the core's in 1960 to 18 percent in 1980, only to drop like a stone back to 12 percent by 1988. This is the Brazilian "miracle."<sup>25</sup>

The second indicator of Korea's success is trade performance: in 1962 Korea was the 40th biggest exporter of manufactures to the U.S.; in 1986, the fifth.

The third indicator is industrial transformation. This does not refer to the rapid rise of industry in total GNP, for by the industry/GNP ratio even Eastern Europe does quite well, thanks partly to the odd way these things are measured. (In a highly protected economy the domestic prices at which industrial products are measured are not world market prices, so the less efficient a sector is in world prices the greater its apparent contribution to GNP.) Rather, the indicator of industrial transformation refers to the rise of skill-intensive, high-value-added industries that are competitive at world market standards of cost and product specifications. The most spectacular Korean case is the semiconductor industry, maker of the leading input of the new technological paradigm.<sup>26</sup> Korea is the world's third biggest producer, after Japan and the U.S., of advanced semiconductor memory chips. Most of the chips are produced by Korean-owned firms, which are drafting closely behind the world leaders, well ahead of all European semiconductor makers. Several other Korean industries—notably, computers, automobiles, steel, and construction—are also having a sizable impact on the world economy.<sup>27</sup>

The final indicator is the removal of poverty, the elimination of severe economic hardship, the expansion of *positive* rights.<sup>28</sup> Consider the number of hours of work it takes an adult male unskilled city laborer to earn the equivalent of one hundred kilograms of the basic food grain. (A composite measure for food plus shelter, qualified by rate of unemployment, would be much more accurate, but data are not available.) Fernand Braudel presents this figure for sites in Western Europe between 1400 and 1950, using wheat. In the fifteenth century and first half of the sixteenth the figure was below 100 hours; it then rose and remained above 100 hours until 1880; by 1920–30 in France it had fallen to between 40 and 60 hours.<sup>29</sup> I have made the calculation for Taiwan, not for Korea,

<sup>24</sup> South Asia is an exception. Its average income in relation to the core fell only slightly, from a dismal 2 percent in 1980 to 1.8 percent in 1988. But see fn. 20.

<sup>25</sup> Arrighi (fn. 18).

<sup>26</sup> See Giovanni Dosi, ed., *Technical Change and Economic Theory* (London: Pinter, 1988).

<sup>27</sup> For a brief account of Korea's automobile industry, see Wade (fn. 17), 309–12; on steel, see Amsden, chap. 12.

<sup>28</sup> C. Fried, *Right and Wrong* (Cambridge: Harvard University Press, 1978).

<sup>29</sup> Braudel, *Civilization and Capitalism, Fifteenth–Eighteenth Century*, vol. 1, *The Structures*

but the Korean trend would be similar. In Taiwan during the 1950s the figure was in the range of 150–200 hours (as in France from 1700 to 1850). By the early 1980s it had fallen to 40–60 hours, about the same as in France between 1920 and 1930.<sup>30</sup> In Korea it was probably more like 60–80 hours by the early 1980s, like France at the turn of the century. Having lived in an Indian village where a sizable proportion of the population has to put in 230 hours,<sup>31</sup> and in the United States where the figure for those earning the minimum wage was about 15 hours in the mid-1980s (my own figure was half an hour), I give this huge reduction in hardship a big weight in any notion of progress.

Taking these several criteria together, I have no qualms about accepting the mainstream view that the question is, indeed, to explain why Korea and the other Asian NICs have been more successful than other poor countries in the postwar era.<sup>32</sup> As for what those critics on the Left said in the mid 1970s, it is hard to think of a clearer refutation in the whole of social science.<sup>33</sup>

#### WHAT THE NEOLIBERAL EXPLANATION IGNORES

To say that the Left critics got it wrong is not to say that the neoliberals got it right. The neoliberals have tended either to ignore contrary evidence *or* to acknowledge it without thought for its theoretical implica-

---

*of Everyday Life* (London: Collins, 1981), 135, chart 15. Note that the chart excludes the seventeenth century. And note the mistake in the vertical scale: the line marked 0 should be 10, the line marked 10 should be 20, the line marked 20 should be 30, and so on, in logarithmic order (using units of ten hours). Due to this mistake, I mistakenly reported the results in earlier publications, saying that real wages "rarely" fell so low in western Europe as to cross the 200-hour line. In fact, between 1700 and 1860 about one-third of the observations are at or above 200 hours, and between 1560 and 1600, about two-thirds. This is not rare. See Wade, *Village Republics: Economic Conditions of Collective Action in South India* (Cambridge: Cambridge University Press, 1988), 35; idem, "What Can Economics Learn from East Asian Success?" *Annals* 505 (1989); and idem (fn. 17), 39.

<sup>30</sup> Wade (fn. 17), Table 2.4 and p. 39. The figure for New Delhi in early 1991 was 140–67 hours (Rs. 25–30 per day, 7 hours a day, rice at Rs. 6/kg.); for Cape Town at the same time, about 50 hours (but there commuting costs would be unusually high). The difference highlights South Africa's industrialization problem.

<sup>31</sup> Wade (fn. 29, 1988), 35.

<sup>32</sup> North Korea may show a similar reduction in this indicator of hardship, via central planning, and may have eliminated poverty in food and savings earlier. If so, these are important achievements. But the capacity of the North Korean economy to provide rising real wages and a diversified consumption bundle is much lower than that of South Korea; its political and civil rights are also far more attenuated, and the conditions of work in agriculture and industry probably are far worse.

<sup>33</sup> Another good case is Pahl and Winkler's 1974 prediction that a system of corporatism would be established in Britain "by 1980." See R. Pahl and J. Winkler, "The Coming Corporatism," *New Society* 10 (October 1974). It would be interesting to hear from Gittings, McCormack, Foster-Carter, and the others why they think their predictions for South Korea and North Korea turned out to be so wrong.

tions. This selective inattention to data that would upset the approved way of interpreting things and the use of repetition as a chief weapon of argument are two strong signs that the neoliberal paradigm is in a degenerative stage, taking on attributes of a disciplined delusional system. Like much Marxist writing of the 1970s, in fact.<sup>34</sup> And like classical economics during the Great Depression, before Keynes's theoretical breakthrough.

Where are the responses to David Evans's finding that the height of protection and static efficiency are much less important for economic performance than the exchange rate and the wage rate?<sup>35</sup> Or to Colin Bradford's finding that "on average there is not any association between outward versus inward orientation and a general measure of price distortion in the two key variables (the exchange rate and the real interest rate)"?<sup>36</sup> Or to Hans Singer's finding that per capita income is a better predictor of economic performance in a large cross section of countries than is inward or outward orientation?<sup>37</sup> Where are the *detailed* examinations of the trade regimes of Korea, Taiwan, and especially pre-1970 Japan—of their inner workings and their effects on both the structure of incentives and output?<sup>38</sup> Where are the detailed neoliberal analyses of the vigorous government efforts to expand national technological capacity in East Asia—efforts that are intended to be selective between industries and that therefore conflict with the injunction against "targeting"?

It is not just that challenges from other scholars are often ignored. It is also that neoliberal interpreters of East Asia are prone to avert their

<sup>34</sup> By way of example, think of the scholasticism of much Marxist writing on a theory of the state. See Martin Carnoy, *The State and Political Theory* (Princeton: Princeton University Press, 1984).

<sup>35</sup> Evans, *Comparative Advantage and Growth: Trade and Development in Theory and Practice* (Hemmel Hempstead: Harvester-Wheatsheaf, 1989), sec. 9.6.

<sup>36</sup> Bradford, "The NICS: Confronting U.S. 'Autonomy,'" in R. Fienberg and V. Kallab, eds., *Adjustment Crisis in the Third World* (New Brunswick, N.J.: Transaction Books, 1984), 125.

<sup>37</sup> Hans Singer, "The World Development Report 1987 on the Blessings of 'Outward Orientation': A Necessary Correction," *Journal of Development Studies* 24, no. 2 (1988).

<sup>38</sup> Why has Jagdish Bhagwati, one of the most creative of trade theorists, not done more than an elliptical pirouette around the East Asian cases? See Bhagwati, *Protectionism* (Cambridge: MIT Press, 1988). It is curious that so few of those who believe passionately in free trade have looked carefully at Japan's pre-1970 trade regime, which would seem to be a critical case. For further discussion, see Wade (fn. 17), chaps. 3, 5, 10; idem, "How to Manage Trade: Taiwan as a Challenge to Economic" (forthcoming); and idem, "The Rise of East Asian Trading States: How They Managed Their Trade" (Mimeo, Trade Policy Division, World Bank, Washington, D.C., 1988). The latter was written while I worked in the same division of the bank that prepared the bank's policy paper on trade reform. The paper defined issues in import reform as being about how to lift restrictions; it ignored issues of how to manage imports better and said virtually nothing about the East Asian experience of import management.

eyes from contrary data even when it stares them in the face. So we find that Ian Little,<sup>39</sup> as part of his general argument that Korea succeeded in large part because the government allowed the "right" prices to prevail, cites the fact that the government set high real interest rates through the banking system, as is "right" in a capital-scarce economy. He relates how these high rates stimulated savings, which in turn permitted high levels of (labor-intensive) investment. And at that point in the discussion of the capital market, he stops. But markets, like scissors, have *two* sides: a supply side and a demand side. Had Little moved from the supply side of the capital market to the demand side, he would have had to confront the way that credit was being allocated in Korea. At that point the detailed involvement of the government in credit allocation would have been hard to ignore. The government used "liberal" methods (high administered interest rates, which are liberal only in the sense of corresponding more closely to scarcity value) to get savings into the banking system; it then allocated those savings by "nonliberal" methods, being able to do so by virtue of the fact (not mentioned by Little) that it owned the banks. Its involvement became all the more intense after the early 1970s, when the real interest rate on a large share of bank loans was made very low. For (another detail Little fails to note in a paper written nearly ten years later) the so-called liberal high real interest rate policy prevailed for only a short time, from about 1967 to 1971.<sup>40</sup>

The literature on Taiwan resorts to the same device. In an overview of how Taiwan "did it," Walter Galenson says, "The government made a major contribution toward the facilitation of capital formation by keeping its expenditure down. . . . Taxes were maintained at a relatively low level, averaging about 14 to 15 percent of the GNP."<sup>41</sup> Although Galenson wrote these words in 1981, it had last been true in 1967; in the interim taxes were always higher. In another overview of Taiwan, Little writes that "public industry has until recently been of rapidly declining quantitative importance."<sup>42</sup> But he neglects to mention that from the early

<sup>39</sup> Little formerly held a chair in economics at Oxford University.

<sup>40</sup> Little, "The Experience and Causes of Rapid Labour-Intensive Development in Korea, Taiwan Province, Hong Kong and Singapore; and the Possibilities of Emulation," in Eddy Lee, ed., *Export-led Industrialization and Development* (Geneva: Asian Employment Programme, International Labour Organization, 1981). For the role of the Korean government in credit allocation, see Leroy Jones and Il SaKong, *Government, Business and Entrepreneurship in Economic Development: The Korean Case* (Cambridge: Harvard University Press, 1980).

<sup>41</sup> Galenson, "How to Develop Successfully: The Taiwan Model," in Galenson, *Experiences and Lessons of Economic Development in Taiwan* (Taipei: Institute of Economics, Academia Sinica, 1982), 80. Galenson retired as professor of economics at Cornell University.

<sup>42</sup> Little, "An Economic Reconnaissance," in Walter Galenson, ed., *Economic Growth and Structural Change in Taiwan: The Post-war Experience of the Republic of China* (Ithaca, N.Y.: Cornell University Press, 1979).

1950s onward Taiwan has had one of the biggest public enterprise sectors outside the communist bloc and sub-Saharan Africa.<sup>43</sup> Both Galenson and Little ignore or downplay facts that would obstruct the neat fit between Taiwan and neoclassical precepts.<sup>44</sup>

To see the same practice outside the East Asian context, consider what Anne Krueger offers as "suggestive evidence," in her phrase, about the effects of government intervention in developing countries, a subject of much interest to political scientists. "There is no evidence that living standards fell in the now-developing countries prior to 1950, a time which many observers associate with a period of *laissez-faire*," she reports. "In many African countries, however, living standards have been falling—in some cases precipitously—since. The latter period has been one of active government intervention, and there is no other obvious reason for the difference in performance in the two periods."<sup>45</sup> Note several things about this argument. First, for India (which contained more people than Africa and Latin America combined) there *is* evidence that per capita income fell in the several decades prior to independence;<sup>46</sup> and for Africa there is simply no good evidence one way or the other before 1950. Second, colonial governments often went well beyond *laissez-faire*: in West Africa marketing boards came to be highly extractive organizations;<sup>47</sup> in India the British colonial government used protection against non-U.K. imports to stimulate industry and in this and other ways could not possibly be described as *laissez-faire*. Third, most *non-*

<sup>43</sup> Wade (fn. 17), Table 6.2.

<sup>44</sup> The recent survey of development economics by Gustav Ranis and Theodore Schultz provides many more examples of how the neoclassical confidence is based on selective inattention—even when the data are in the same volume or the same paper; see Ranis and Schultz, eds., *The State of Development Economics: Progress and Perspectives* (Oxford: Blackwell, 1988). The editors assert that "outward-looking [less developed countries] have achieved relatively rapid growth . . . and have withstood [shocks] better." In the same volume T. N. Srinivasan destroys the evidence for the second part of the proposition; and Ronald Findlay finds the first part "incontrovertible" (p. 79) but then shows (pp. 90–93) that the normal sequence, in Germany, Japan, Britain, and Korea, involved not trade neutrality or "outward-lookingness" but heavily interventionist mercantilism, first protecting import substitutes and then promoting exports. See Michael Lipton's review, *Economic Journal* (September 1989).

<sup>45</sup> Krueger, "Government Failures in Development," *Journal of Economic Perspectives* 4, no. 3 (1990), 12. Krueger was the senior-most economist and the vice president for research at the World Bank between 1982 and 1986.

<sup>46</sup> There is not much doubt that India's food grain availability per person per year declined; but there is some dispute as to whether nonagricultural output increased fast enough to prevent per capita income from falling. Heston's calculations show stagnation in per capita income between 1911 and 1946, but most others show a decline. A. Heston, "National Income," in Dharma Kumar, ed., *The Cambridge Economic History of India*, vol. 2 (Cambridge: Cambridge University Press, 1983).

<sup>47</sup> Peter Bauer, *West African Trade* (1954; reprint, London: Routledge and Keegan Paul, 1963).

African economies, *including the most successful cases*, have grown subsequently under more interventionist regimes. Indeed, most sub-Saharan African economies grew between 1950 and 1970, even in per capita terms, and many grew faster in the (postindependence, more interventionist) 1960s than in the 1950s. Fourth, to say that there is "no obvious reason" for the difference in Africa's performance between the two periods other than greater government intervention in the second is to ignore several important points. (1) "External" factors have impacted especially adversely on African economies, for reasons that do not reduce to the characteristics of African governments. (2) At independence African economies suffered a major loss of skilled manpower from an already tiny base. (3) The problem is less "too much" government intervention in Africa than that governments are too weakly institutionalized to maintain centralization and control—a combination that quickens the use of "primordial" connections to capture state resources and evade state demands.<sup>48</sup> In short, this evidence is shoddy, not suggestive; or if suggestive, then only in the sense of the pornographer.<sup>49</sup>

My own evidence, illustrated above, suggests that neoliberal economists have been pioneering a whole new principle of causal inference—that to explain superior economic performance one may either simply ignore everything that is not in line with neoliberal prescriptions or assert that it hindered what would otherwise have been an even better performance. When this principle is combined with a wider professional propensity to treat "power" as a third-rank concept (the new 4,000-page *Palgrave Dictionary of Economics* has no entry for "power"),<sup>50</sup> the result

<sup>48</sup> Zambia at independence in 1964 had all of twelve hundred high school graduates. In Botswana in 1965, the year before independence, thirteen students passed their O-level exams. Most sub-Saharan countries at independence were taken over by governments whose leadership group was comprised mainly of people with a primary school education or less. Compare East Asia; see Wade (fn. 17), 64, 190, 217–25. One should (as Krueger does not) link the question of the appropriate types and amounts of government intervention to the educational competence of the government. On the significance for Africa's growth of its debt burden, falling terms of trade, unstable exchange rates, falling aid, and agricultural policies and textile protection in the West, see, e.g., Adrian Hewitt and Hans Singer, "How to Foster Diversification, Not Dependence," *Africa Recovery* 4 (October–December 1990), 36–39; and Gerald K. Helleiner, "Structural Adjustment and Long-Term Development in Sub-Saharan Africa" (Paper for workshop on Alternative Development Strategies in Africa, Oxford, December 11–13, 1989); and idem, *Sub-Saharan Africa: From Crisis to Sustainable Growth* (Washington D.C.: World Bank, 1989). On the "weak government" hypothesis, see Joel Migdal, *Strong Societies and Weak States: State-Society Relations and State Capabilities in the Third World* (Princeton: Princeton University Press, 1986); the book is good on the "state" side but mischaracterizes African "society" as "strong."

<sup>49</sup> This is not to diminish Krueger's important contributions to economic knowledge, especially in the areas of rent-seeking behavior and trade policy.

<sup>50</sup> Robert Heilbroner, "Economics without Power," *New York Review of Books*, March 3, 1988.

is an aversion to serious investigation of the role of the state in economic development. Assertions like "success has been achieved [in Korea] *despite* intervention" are put forth without a shred of evidence.<sup>51</sup> In this way the circle is closed, the paradigm is protected, and minds can be set at rest.

Although I have been talking of neoliberal development economics, I do not mean to imply that these strictures apply only to a small subset of neoclassical economics. Most Anglo-American development economists have a mistaken understanding of Korea and Taiwan as "low-intervention" countries, especially with reference to trade, and they rely on this mistaken understanding to validate a low-intervention prescription elsewhere. But because the neoliberals are both more extreme and more uniform than other neoclassicals, they make a sharper target; they also tend to be opinion leaders in the development field, which makes it doubly important to subject their arguments to scrutiny.<sup>52</sup>

Neoliberals say that growth is easy, provided governments do not act to obstruct the natural growth-inducing processes of a capitalist econ-

<sup>51</sup> Deepak Lal, *The Poverty of Development Economics* (London: IEA, Hobart Paperback 16, 1983), 46. Lal is an exponent of what I call the Ptolemaic fallacy; see Wade (fn. 17), 348–49.

<sup>52</sup> Ross Levine and David Renelt have recently provided more evidence of insufficient standards of proof, a problem that applies not only to the work of the neoliberals; see Levine and Renelt, "A Sensitivity Analysis of Cross-Country Growth Regressions" (Mimeo, Macroeconomic Adjustment and Growth Division, World Bank, November 29, 1990). They examine the vast literature on cross-country regressions of long-run growth against various policy variables, with a view to determining which conclusions are robust and which are fragile. Robust conclusions are those that survive small changes in the right-hand (i.e., independent) variables. "We find that there is not a strong independent relationship between almost every existing policy indicator and growth. . . . [T]he broad array of fiscal expenditure variables, monetary policy indicators, political stability indexes, human capital and fertility measures considered by the profession are not robustly correlated with growth; and newer indicators that we have assembled to capture exchange rate, tax, and fiscal expenditure policies are also not robustly correlated with growth" (p. 2). The one variable that could not be shaken off by fairly small changes in the specification of the independent variables was investment: "We found a positive and robust correlation between average growth rates and the average share of investment in gdp" (p. 26). I want to draw special attention to their findings on trade and price distortions, the subject that occupies the core of neoclassical development economics: "When controlling for the share of investment in gdp, we could not find a robust independent relationship between any trade or international price distortion indicator and growth" (pp. 19–20). These findings suggest that economists of all stripes ought to be a little more modest than usual in claiming to understand development. But note that the Levine and Renelt findings are based on an unusual notion of robustness; in their work robustness relates to which variables are included or excluded. More familiar notions of robustness relate to changes in sample size, time period, or functional form. Unrobustness in their sense is less significant than unrobustness in the other senses, because according to their criterion any hypothesized growth mechanism that depends essentially on several variables is likely to be found unrobust. For example, their finding that human capital variables are unrobust is unsurprising if one considers that human capital and physical capital are complementary, such that a high rate of human capital formation is unlikely to be an important cause of growth in the absence of fairly rapid physical capital accumulation.

omy. We come now to two recent books about the newly industrialized, late-industrializing, or semiperipheral economies, books that have in common an emphasis on the difficulties—the unnaturalness—of growth.

#### Alice Amsden's Interpretation of South Korea's Success

Amsden builds an interpretation of East Asian, specifically Korean, economic success on several kinds of stylized facts that run counter to neoclassical theory and that are ignored or treated with indifference in neoliberal accounts of Korea. They include the following. (1) The Korean state has acted as entrepreneur, banker, and shaper of the industrial structure. (2) It has deliberately distorted the price structure by way of, among other things, subsidies, protection, price controls, and restrictions on incoming and outgoing movements of finance and direct investment. By means of these distortions, it has generated an industrial structure different from what unguided entrepreneurs would have produced on their own. (3) The actions of the Korean state have been complemented by those of large, diversified business groups that have come to occupy a dominant position in the economy—so much so that the combined sales of the top ten rose from 15 percent of GNP in 1974 to (this is one of the most amazing of all Korean statistics) 67 percent in 1984 (Amsden, Table 5.1).<sup>53</sup> With firms of this size and level of diversification, a rather high proportion of transactions in the Korean economy are intrafirm, less subject to the discipline of the market than to the discipline of managerial hierarchies. (4) The state not only actively promotes the growth of the business groups, it also disciplines their use of subsidies and other supports, rewarding those who use subsidies "well" with further help and withdrawing support from those who do not. Its relations with them are anything but the arm's-length relations between government and firms sanctioned by neoclassical theory. These four facts suggest an economy in which government and firms depart quite substantially from the neoclassical model of a successful industrializer.

There is, however, another striking fact about the Korean experience that is more consistent with neoclassical precepts: whereas the government greatly restricted and channeled competition in the domestic market, it also strongly encouraged firms to export, thereby subjecting them to intense competition in foreign markets. Success in export markets came to be the main criterion of good use of subsidies (and hence of distribution of further subsidies); and neoclassical theory does suggest

<sup>53</sup> Sales, of course, are not equal to value added. The true share of these companies in GNP (total value added) is probably one-third to one-half of this 67 percent.

that that is quite a good proxy for efficient use of resources. (To be more exact, neoclassical theory says that success in export markets is a good proxy for efficiency in resource use provided there is zero bias in incentives to sell abroad or at home; by contrast, a more classical theory of long-run growth might sanction the same criterion even in conditions of net subsidies to exports.)

#### LATE INDUSTRIALIZATION

Amsden suggests that these and certain other facts about Korea can be explained as a response to the conditions of "late industrialization." These conditions refer to the handicaps and advantages experienced by market-based economies that initiate industrialization when technologically more advanced firms already exist in other countries. The firms of the late industrializer then have to compete with those established firms that can introduce new technologies fast enough to capture "technology rents" and thereby earn higher profits. This does, of course, allow the late industrializer to acquire, or "borrow," the more codified elements of a given technology without having to develop them for itself. But there is generally a great gap between buying or stealing the codified elements and mastering the technology in production. The lower labor costs of the late industrializer offer another partial advantage in such competition. But since its labor force is much less skilled, the lower labor costs may not compensate for differences in productivity. Late industrializers all tend to construct a similar set of institutions to respond to the handicaps and advantages of lateness. In particular, they tend to develop an entrepreneurial state and diversified business groups.

#### THE STATE

The state offers subsidies and protection ("subsidies" for short) both to offset the disadvantages faced by national firms in international competition and to move the present industrial structure toward one with higher value-added, more technologically dynamic activities. It does this faster and perhaps along a different path than the free market might have done on its own.

So, for example, as recently as the late 1960s the cost position of Korean manufacturers of cotton textiles was less favorable than that of their Japanese counterparts, *despite lower wages*. To enter export markets on a sizable scale the Korean industry needed subsidies. As Amsden puts it, "Subsidies in Korea were necessary not because of 'distortions' [in particular, the exchange rate was not much distorted] but because the Koreans could not, initially, compete against the Japanese, even in industries such

as cotton spinning and weaving in which the least developed, most labor-intensive countries supposedly have a comparative advantage" (p. 68). After several years of production experience, however, the cotton textile industry was competitive enough to be weaned off subsidies—a striking fact, in light of experiences elsewhere.

Indeed, (unsubsidized) profit rates in cotton textiles and other light industry came to be substantially *higher* than those in capital-intensive industries, yet from the mid-1970s it was the capital-intensive industries that had the highest rate of export growth. "One may infer from all this," says Amsden, that

as the capital-intensive industries showed themselves increasingly capable of exporting, they became more attractive for the government to promote. *Their long gestation periods and relatively low profitability through adolescence, however, rendered them relatively less desirable investments to the private firm. The initiative to diversify, therefore, fell to the state.* (p. 88 and Tables 4.1, 4.2; emphasis added)

And she shows further that the leading firms in light industry (notably textiles) did *not* grow into diversified business groups and did not lead the way into the new heavy and chemical industries, as one might expect from the conventional dynamics of comparative advantage. Instead, *new* firms with strong state support undertook the development of the heavy and chemical industry. According to Amsden, then, Korea's entry into heavy and chemical industries and the emergence of cotton textiles as the leading export industry together provide graphic evidence of the need for state dirigisme in conditions of late industrialization.

#### BUSINESS GROUPS

The business groups of the late industrializer diversify into many different, often unrelated industries in order to spread risks and allow cross-subsidizing of entry into a varied portfolio of necessarily low-end products. They also focus more on the shop-floor level of organization—that is, on the production process itself—because that is where borrowed technology is first made operational and later optimized. This contrasts with more advanced firms, which tend to compete on the basis of *innovation* instead. The strategic focus in those cases is less on the shop floor than on the corporate headquarters, especially the R and D complex, where the major profit-making opportunities are made (and also, one should add, the financial asset management complex, the source of much profitable "paper entrepreneurship"). Amsden makes the point in the form of a hypothesis:

Leading firms in late industrializing countries, if they are to penetrate world markets, must adopt unusually pro-active production and operations management policies. By pro-active we mean policies that assign high-quality managers to the shopfloor and inspire initiative on the part of such managers to develop the skills of the work force and to improve process performance. Otherwise the gap in productivity levels with leading firms in advanced countries will not be bridged while the advantage in wage levels narrows. (p. 160)

A disproportionate number of managers will have credentials in engineering, as distinct from a background in generic management or finance.

What matters, then, is not so much the newness of an industrialization process (as in "newly industrialized country"), as its lateness as compared with others. Amsden argues that

the general properties of an industrialization process based on learning, or borrowing, technology are entirely different from those of an industrialization process based on the generation of new products or processes—the hallmark of the First and Second Industrial Revolutions. Thus, the late acquisition of international competitiveness has given rise to certain common tendencies in otherwise diverse countries—Japan, Korea, Taiwan, Turkey, Brazil and Mexico.<sup>54</sup>

(Elsewhere she adds India, p. v).<sup>55</sup> These common tendencies concern the role of the state, the role of the market, and the structure and competitive strategies of business firms. Insofar as there is a single symbol that captures the difference, it is the subsidy.

The subsidy serves as a symbol of late industrialization. . . . The First Industrial Revolution was built on laissez-faire, the Second on infant industry protection. In late industrialization, the foundation is the subsidy—which includes both protection and financial incentives. The allocation of subsidies has rendered the government not merely a banker, as Gerschenkron (1962) conceived it, but an entrepreneur, using the subsidy to decide what, when, and how much to produce. The subsidy has also changed the process whereby relative prices are determined. (pp. 143–44)

#### WHY DOES KOREA DO BETTER?

Why has Korea, together with Japan and Taiwan, done so much better than the other late industrializers? Because, in a word, the institutions of late industrialization have functioned more effectively there than elsewhere. "It may be said that *growth has been faster in Korea not because markets have been allowed to operate more freely but because the subsidiza-*

<sup>54</sup> Alice Amsden, "Third World Industrialization: 'Global Fordism' or a New Model?" *New Left Review* 182 (1990), 14–15.

<sup>55</sup> Also *ibid.*, 5.

tion process has been qualitatively superior: reciprocal in Korea, unidirectional in most other cases" (Amsden, 145; emphasis added). By "reciprocal," Amsden means that in direct exchange for subsidies of various kinds, the state exacted certain performance standards from firms, notably in the field of exports. Most other late industrializers allocated subsidies without imposing any quid pro quo: "Where Korea differs from most other late industrializing countries is in the discipline its state exercises over private firms" (p. 14; emphasis added). Generalizing, Amsden puts forth an audacious proposition: "The more reciprocity that characterizes state-firm relations in these countries, the higher the speed of economic growth" (p. 146).

#### LEARNING AND INNOVATION

This argument about Korean and Third World industrialization in general, says Amsden, differs not only from the neoclassical, but also from the Schumpeterian, approach. Schumpeter recognized that by his time market structures had become less competitive than was consistent with the neoclassical paradigm. The new basis of competition—the new source of discipline over firm behavior—came from the creative gales of technological discoveries that uprooted old monopolies and raised productivity, not steadily but in spurts. Late industrialization, however, involves not innovation but "learning," that is, borrowing, adapting, and improving upon foreign designs. The new source of discipline over firm behavior is the state itself, a factor to which the entrepreneurially and technologically driven Schumpeterian model had understandably paid little attention. Late industrialization, much more than early industrialization, has been a political process, shaped by the exigencies of mastering (or learning) already existing technologies. Some commentators have taken the Japanese case as confirmation of the usefulness of the Schumpeterian approach, as in the Schmiegelows' statement that "the evidence of massive penetration of global markets by Japanese Schumpeterian entrepreneurs, of their competitive edge, and of their growing leadership in innovation is so unmistakable, and there is so little that mainstream economics can offer to explain it, that the Austrian [or Schumpeterian] approach enjoys prime facie validity in explaining Japan's impact on the structure of the world economy."<sup>56</sup> Amsden would presumably reply that the Schumpeterian approach is not the only alternative to mainstream economics and that hers does a better job of explaining the Japanese case prior to the early 1970s; she would probably agree with the Schmiege-

<sup>56</sup> H. Schmiegelow and M. Schmiegelow, "How Japan Affects the International System," *International Organization* 44, no. 4 (1990).

lows that the Schumpeterian better handles the subsequent era, when Japanese firms compete more than before on the basis of innovation and when the state has scaled back its "leadership" role in industrial transformation.<sup>57</sup>

### GLOBAL FORDISM

Her approach also differs from world systems interpretations that present industrialization at the "periphery" (including Korea) as the reflex of problems of capital accumulation in the "core." In Alain Lipietz's formulation,<sup>58</sup> for example, industry in the Third World arises as capital from the core extends the "scale" of its operations in search of new markets and cheap labor. Once installed by means of "primitive Taylorist" modes of labor control, it may then evolve into "peripheral Fordism" when growth in the *home* market for manufactured goods plays a large part in the national "regime of accumulation," as has been true in Korea since about 1973. At this point the tendency toward underconsumption—production exceeding the capacity to consume—becomes a stumbling block to further economic growth, as it is in the core. Amsden answers this sort of argument with several damaging facts about Korea. (1) Even after 1973 Korean growth has *not* been centered on the home market. (2) Korean wages have grown faster than in any other previous or contemporary industrialization, without undermining competitiveness, sustained by even faster productivity growth. (3) Work in the large business firms has not been managed in a Taylorist, top-down fashion.

Technical ignorance at the highest managerial level, and inexperience on the part of the workforce, have made it impossible for borrowed technology to be optimized through a top-down, Taylorist approach to productivity and quality improvements. Instead, the standardization of work has been accompanied by a more participatory (and, as it turns out, more productive) approach to work relations, not for cultural reasons but for reasons related to technology transfer.<sup>59</sup>

<sup>57</sup> But while MITI's leadership role in the domestic economy has decreased substantially, it has recently been expanding the reach of its industrial planning and coordination into foreign economies, in response to the explosion of Japanese investment abroad and the absence of coherent industrial policy in receiving countries. See Ivor Ries, "Japan's Mighty MITI Extending Its Reach," *Financial Review*, December 18, 19, 20, 1990. I thank Chalmers Johnson for this reference. On leadership as applied to industrial policy, see Robert Wade, "Industrial Policy in East Asia: Does It Lead or Follow the Market?" in Gary Gereffi and Donald Wyman, eds., *Manufacturing Miracles: Patterns of Industrialization in Latin America and East Asia* (Princeton: Princeton University Press, 1990).

<sup>58</sup> Lipietz, *Mirages and Miracles: The Crises of Global Fordism* (London: Verso, 1987). See Amsden (fn. 54) for a discussion of Lipietz.

<sup>59</sup> Amsden (fn. 54), 12–13.

(4) The state in Korea (and in other late industrializers) has gone well beyond its role in the Fordist model (largely one of creating both effective demand in response to crisis and protection for infant industries).

So neither the Schumpeterian nor the global Fordism approaches can explain the common tendencies of the late industrializers; still less can the neoclassical. Amsden's approach—which could be summarized as “*industrializing through learning, learning through reciprocity between government and diversified business groups, reciprocity involving price-distorting subsidies in exchange for performance*”—constitutes, she says, a new paradigm for understanding late industrialization, which is a new way of industrializing (p. 141).

In a field plagued by stale thinking *Asia's Next Giant* stands out as wonderfully original, powered by a militant, epigrammatic intelligence. The chapters toward the end, on the firm-level dynamics of the evolution of shipbuilding, textiles, cement, and steel, range from offering technical information about production to telling details about social organization. The author relates how, well before the first steel plant had been completed, workers were recruited and trained—even taken out to open fields to rehearse their jobs, shouting orders to one another along imaginary production lines. For given its lack of the cheap natural resources that other NICs like Mexico (gas) and Brazil (ore and hydro) could use to defray the high start-up costs of steel and other capital-intensive industries, Korea had no choice but to compensate by means of a supereffective deployment of its labor force, to discipline and train it as fast as possible.

But there are some serious weaknesses in the argument. Some key propositions are poorly supported, some key concepts are treated as self-evident when they are not, and some alternative mechanisms for which there is reasonable evidence are not considered. Einstein's aphorism that “*imagination is more important than knowledge*” is taken a bit too literally. In particular, Amsden misses many opportunities to incorporate neoclassical findings into her story, thereby rendering it much weaker than it need be in terms of economic analysis. Nowhere is this more apparent than in what she says about prices.

#### GETTING PRICES “WRONG” IN KOREA

This is the phrase that Amsden emblazons upon her escutcheon as the essence of her theory of economic development.<sup>60</sup> Reversing the conven-

<sup>60</sup> *Ibid.*, 23.

tional injunction (converting "right" to "wrong" and the sense of "getting" from "letting" to "setting") produces an arresting paradox. But what evidence does she offer, first, for the proposition that relative prices were "wrong" and second, for the proposition that the structure of "wrong" prices was a key element in output growth? Although she does not present it systematically, the evidence seems to be as follows:

1. The export effective exchange rate, which includes subsidies to export sales, was substantially above the official won/dollar exchange rate between 1960 and 1965 (see her Table 3.4, p. 67), and during this time exports took off. Amsden says that export subsidies, as indicated by the gap between the export effective exchange rate and the official exchange rate, "turned the tide." So the volume of exports was not determined by market factors alone, at least in the period covered by her numbers. Note several problems with this argument. First, six years and two sets of numbers are a slender base for causal inference. Second, she says that subsidies (as indicated by the gap between the two exchange rates) increased as exports increased, the former driving the latter. In fact, her own numbers show the opposite: the gap was greatest in 1960, when exports were small and stagnant, and least in 1964 and 1965, when exports were booming. Third, this gap is in any case a poor measure of the bias of the system for or against exports. For that one has to compare the export effective exchange rate with the import effective exchange rate. It is quite possible to increase export subsidies (as measured by her gap) while at the same time giving even more incentives to import substitution (perhaps via quantitative restrictions), making a net increase in the bias against exports. It is this bias, not her gap, that might drive exports; but we are not given the information. Fourth, nor are we given information about the real exchange rate (relative price of traded goods—exports and import substitutes—vis-à-vis nontraded goods). Lacking information on both export bias and the level and movement of the real exchange rate, we cannot make a judgment about whether these prices were "right" or "wrong." Certainly the fact that the export effective exchange rate differed from the official exchange rate (as in most other developing countries) does not in itself mean that either the official rate or the export effective rate was "wrong." In short, Amsden's evidence on this point does not support the conclusions she draws.

2. "Tariff barriers and nontariff barriers have comprised a key ingredient of Korea's industrial policy," she says (p. 145). But we receive virtually no information on the magnitude of protection over time, though such information is available.<sup>61</sup>

3. In the capital market a multiplicity of prices prevailed for loans of the same maturity—one for foreign loans, more than one for domestic commercial bank loans depending on whether they were for a priority use, and one or more for "curb" or informal market loans. Not all of these prices

<sup>61</sup> Wade (fn. 17), chap. 10.

could possibly have been "right," she says without further ado. This, too, is overly hasty. For one thing, to the extent that the curb market is used for riskier loans than can be granted by commercial banks, neoclassical analysis would predict curb market rates to exceed commercial bank rates on account of differential risk.

4. Price controls have been extensive. "At the end of 1986, as many as 110 commodities were controlled, including flour, sugar, coffee, red pepper, electricity, gas, steel, chemicals, synthetic fibers, paper, drugs, nylon stockings, automobiles, and televisions" (p. 17). A hundred pages later this expands to "the Economic Planning Board controls most prices" (p. 129). Is "most" really the same as "as many as 110"? We have no idea of the share of final demand that is price-controlled over time or of how much the controls bite.

5. Subsidies to the cotton textile makers were needed for quite a few years to enable them to get established in export markets against Japanese competition. Later subsidies to some heavy and chemical industries were needed to induce private capitalists to forgo higher short-term profits in light industry. Amsden's evidence on this score is more convincing than the rest.

Not stopping with the proposition that Korea succeeded because it got prices wrong, Amsden makes a still more arresting claim: "Although Korea industrialized on the basis of relative prices that deviated sharply from free-market equilibria, *such prices were less 'distorted' and provided big business with fewer bonanzas than prices in India, Turkey, and the Latin-American late-industrializing countries*" (p. 145; emphasis added). Or in a slightly different formulation, "In Korea the 'wrong' prices have been right because government discipline over business has enabled subsidies and protection to be less than elsewhere and more effective" (p. vi). This is an intriguing idea, but it is asserted without a shred of evidence. If Korean price distortions have in fact been less than in most other countries, how can we distinguish this argument from the central neoclassical claim that it is precisely *because* price distortions have been less that Korea was more successful?<sup>62</sup>

Furthermore, it is not self-evident that short-run equilibrium prices should be used as the standard of "right" against which actual Korean prices were correctly "wrong." After all, neoclassical theory acknowledges that even markets that operate without government interference

<sup>62</sup> Perhaps Amsden's argument could be clarified by distinguishing three senses of "distortion." One is deviation from the market equilibrium price, which just offsets disadvantages due to "market imperfections" elsewhere in the system. Another is deviation that pulls resources into uses expected to be to the country's future comparative advantage. The third is deviation that provides big windfall gains for little effort. Korea presumably had much less distortion in the third sense than other countries had, but presumably not in the second sense.

may experience "failures" due to externalities, complementarities, uncertain learning gains, imperfect capital markets, and economies of scale, scope, and time. In such a case the configuration of market prices, which no longer corresponds to economic values or opportunity costs, may send the "wrong" signals, even in conditions of free trade. Neoclassicals argue that empirically these sources of market failure tend to be less important than those caused by government intervention; they therefore prescribe free trade as the way to achieve the best results in the real world of special interests.<sup>63</sup>

Moreover, there *is* a modified neoclassical interpretation of the role of the Korean government: that its various interventions had the aggregate effect of compensating for these failures (as well as for those caused by the "politically driven" components of government intervention) and thus of creating the relative price structure that would have prevailed in an ideal free market. I have elsewhere called this the "simulated free market" theory of East Asian industrial success.<sup>64</sup> I do not find it very convincing, but it does have a place in the literature, and Amsden might have taken it up in an analytical dissection of "wrong" and "right" prices.

Even if we grant that the government helped to get prices (correctly) "wrong," there is still the separate question of the *output* effects of this rigged price structure. Again, this issue is barely raised, it being taken for granted that the effects were not just positive but so positive as to constitute the essence of why Korea did better than the rest. Perhaps Amsden would consider the success of the heavy and chemical industry drive of the 1970s (and she certainly considers it to have been highly successful) as evidence of benign output effects, for it was not the result of free-market forces. But this same heavy and chemical industry drive is routinely cited in the literature as the clincher for the *malign* effects of Korean dirigisme. Amsden might at least have responded to those who say that its costs swamped its benefits. (My own conclusion, incidentally, is that the medium- and long-term benefits did exceed the costs.)<sup>65</sup>

All told, this central plank in Amsden's theory remains in urgent need of empirical reinforcement. A generous reading might say that Amsden has done what many economists before her have done, which is to pre-

<sup>63</sup> See Colclough (fn. 3).

<sup>64</sup> Wade (fn. 17), 23–24.

<sup>65</sup> For a brief discussion, see *ibid.*, chap. 10, esp. 319–20. For a very useful recent study, see Richard Aury, "Creating Comparative Advantage: South Korean Steel and Petrochemicals," *Tijdschrift voor Econ. en Soc. Geografie* 82, no. 1 (1991).

sent a series of "stylized facts" about how, in her understanding, the world works, leaving it to those who disagree to muster counterevidence. A less generous reading might say that Amsden displays the same disdain for established principles of scientific knowledge as do the neoliberals cited earlier.

#### THE STATE IN KOREA

As the initiator of major new investments, the distorter of prices, and the discipliner of big firms and labor, the state has a central place in Amsden's story. Yet she takes what could politely be called an "abstentionist" view toward it. She says almost nothing about how the state is organized, its base of support, its means of survival, and how it maintains its discipline in the exercise of huge discretionary powers. So abstentionist is she, indeed, that the key agencies for industrial and trade policies, the Economic Planning Board and the Ministry of Trade and Industry, are given only three mentions between them in the whole 329 pages. Perhaps it is unfair to expect otherwise in a work of economics.

#### ROLE OF MANUFACTURING PRODUCTIVITY GROWTH

Amsden's argument assumes, implicitly, that the driving force of Korean industrialization was fast growth of productivity in manufacturing (driven by fast "learning"). Thus, her emphasis on the structure and management of business groups. She might have addressed some of the evidence, from Hollis Chenery, Moshe Syrquin, Howard Pack, and others,<sup>66</sup> that partly runs against this argument. To summarize, there is evidence to suggest that prior to the mid-1970s productivity growth in manufacturing was by no means high as compared with growth in other countries at roughly the same income level. But (1) Korea had poor natural resource endowments in comparison with many other low- and middle-income countries; it therefore had no comparative advantage in exports of primary products, which left manufactures as the only broad alternative. (2) It also had a high ratio of people with basic education to people without basic education, again compared with other countries at similar income levels. (3) Agricultural productivity was much lower than in manufacturing. And (4) the physical infrastructure was fairly good. The combination of middling productivity, a high ratio of basically ed-

<sup>66</sup> Chenery, "Growth and Transformation," in Hollis Chenery, Sherwin Robinson, and Moshe Syrquin, eds., *Industrialization and Growth: A Comparative Study* (New York: Oxford University Press, 1986); Syrquin, "Productivity Growth and Factor Reallocation," in Chenery, Robinson, and Syrquin; Pack, "Industrialization and Trade," in Chenery and T. N. Srinivasan, eds., *Handbook of Development Economics* (Amsterdam: North Holland, 1988).

ucated to uneducated people, a big agriculture-manufacturing gap in productivity, and a fairly good infrastructure allowed Korean manufacturing to compete internationally. But the real driving force before the mid-1970s, according to this argument, was the huge increase in capital and labor inputs into manufacturing (more and more young women behind more and more desks assembling more and more shirts and circuit-boards). It was a scale effect, not a productivity effect. These inputs came in substantial part from agriculture, and the economy-wide level of productivity grew fast as resources were reallocated from lower productivity uses in agriculture to higher productivity uses in manufacturing.<sup>67</sup> But the only way to absorb such large amounts of capital and labor in manufacturing without running into rapidly diminishing returns was to export the output, because the domestic market would have been able to absorb the extra output only at the cost of sharp falls in price. This is the single most important way that exports helped Korea's industrialization. Since the mid-1970s, however, with the completion of the reallocation from agriculture, the driving force has been productivity growth within manufacturing.<sup>68</sup> It may well be that the sorts of management practices and firm structure that Amsden emphasizes have been an important part of this growth. But much of Amsden's own account of firms and industries draws on data from *before* that time. This is not to suggest that Amsden is necessarily wrong for the earlier period—one can imagine ways in which her argument could be reconciled with the other evidence. But this other evidence is simply not addressed.

#### COMPARATIVE ADVANTAGE: RIGID, FLEXIBLE, OR IRRELEVANT?

Did Korea follow its prevailing comparative advantage (CA), or did it engage in activities that were out of line with CA? Neoliberals imply that its industrialization was governed by CA, except for the temporary aberration of the heavy and chemical industry drive that started in the early 1970s and more or less terminated around 1980, as economic rationality again came to prevail. Amsden and also Governor Park (in the epigraph

<sup>67</sup> For the agricultural end of these reallocations, see Moore (fn. 5); on the political control of Korean agriculture and the nonprice methods of achieving relatively high levels of agricultural productivity (cf. standard recipes for agricultural growth and mechanism of Fei-Ranis-type models), see Wade (fn. 5, 1983).

<sup>68</sup> This is likely, but most of the evidence I cite stops short of this period. Pack (fn. 66) suggests that even after the mid-1970s total factor productivity growth was not especially good, and he credits continued rapid absorption of factors, including extra investment. But subsequent evidence suggests to him that productivity growth within manufacturing has indeed been more of a driver than he thought when he wrote the article in Chenery and Srinivasan (fn. 66); Pack, personal communication with author.

to this article) imply either that it went against CA or that CA was somehow irrelevant. What is at stake? According to the standard theory, specializing according to CA makes for an efficient pattern of resource use, with more intensive use of the more abundant factors and less of the scarcer factors. A country may be able to produce goods out of line with its CA, but those goods, which require a lot of the scarce factors and few of the abundant factors, will not be profitable. Stereotypically, a low-wage, labor-abundant country should concentrate production and exports on labor-intensive products, while importing the more capital-intensive goods from countries where labor is scarcer and capital more abundant. (China can make and launch satellites, but such engineering-intensive industries are not in its CA.) So if Korea departed significantly from CA and yet was still outstandingly successful, one could conclude that something is seriously wrong with the theory. And since the theory forms part of the bedrock of neoclassical economics, this would sound the alarm in many quarters.

There is remarkably little evidence on this central question. It is true that exports have been far more labor-intensive than overall production, a prediction in line with CA theory. But it is also true that from the early 1960s, capital-intensive industries producing intermediates have experienced rates of growth much higher than the manufacturing average, a phenomenon less readily reconciled with CA theory. And we know, too, that most of these industries have had substantial levels of protection, which is also sometimes taken to indicate investment out of line with CA.

On the other hand, Patrick Minford and Adrian Wood<sup>69</sup> have recently argued, contrary to the general understanding, that capital-intensity is almost irrelevant for the determination of CA, especially because noninfrastructure capital is mobile between countries. Rather, it is labor force skills that count. Product categories can be ranked in terms of skill requirements, and the categories that are "appropriate" to a country at any one time (in the sense of being in line with CA) can be read off by comparing their skill requirements with the ratios of highly skilled to basically skilled to unskilled people in the labor force (these ratios determine the scarcity and relative cost of more or less skilled people and therefore

<sup>69</sup> See Minford, "A Labour-based Theory of International Trade," in J. Black and A. MacBean, eds., *Causes of Changes in the Structure of International Trade, 1960-85* (London: Macmillan, 1989); Wood, "A New-Old Theoretical View of North-South Trade, Employment and Wages," Discussion Paper 292 (Sussex: Institute of Development Studies, University of Sussex, 1991). Wood's paper is based on one chapter of his book, *North-South Trade, Employment and Inequality* (London: Oxford University Press, forthcoming).

the viability of investments that require different combinations of these people).

If this is accepted, we have to say that we simply do not know to what extent the fast growth of capital-intensive industries in Korea was in line with  $CA$ , because no one has calculated their skill intensities. We do know that all capital-intensive industries are not skill-intensive and that within industries defined at the three-digit level (industrial chemicals, for example) there are huge variations in skill requirements. We also know that the fact that these industries had protection does not in itself mean that they were against  $CA$ . Protection, that is, might have offset market imperfections elsewhere that would have rendered the industries financially unviable without the protection, even if they were economically viable with proper shadow prices. Nor does the fact that these industries grew faster than the manufacturing average in itself mean that they were out of line with  $CA$ , for all industrialization involves some growth of upstream sectors, for reasons of transport costs and other advantages of local production. And this growth may be very fast if it comes from a low base. The key question, then, is whether the capital-intensive industries grew faster as a result of policy measures than they would have under conditions of well-functioning free markets.

So one hypothesis is that Korea's industrialization—including the dual-track promotion of some capital-intensive intermediate (and later final) goods alongside labor-intensive goods for export markets—did not depart from  $CA$  to any significant extent. This implies that the capital-intensive industries remained within the (rapidly rising) limits of the skilled labor supply, which further implies that the capital-intensive industries of the 1960s and early 1970s (before the heavy and chemical industry drive) had rather low skill requirements.

Another hypothesis, which is more consistent with Amsden-Park, is (1) that Korea stretched its  $CA$  (as with a rubber membrane) to cover more skill-intensive industries than would be "normal" in relation to its skill endowments<sup>70</sup> and (2) that this stretching was especially pronounced during the heavy and chemical industry drive (though not absent earlier, as seen in those subsidies used to launch the cotton spinning and weaving industry against Japanese competition). By this interpretation, the Koreans excelled at "learning by doing," which increases the supply of scarce skills and thereby stretches the  $CA$  membrane. More precisely, the Koreans excelled at learning by doing *at low cost*. It is as though those

<sup>70</sup> I owe this idea of stretching  $CA$  to Adrian Wood.

men in the field shouting orders at each other on their imaginary production lines were a microcosm of the whole labor force. In many other countries efforts to stretch the CA membrane by investing in advance of skills so as to generate learning-by-doing effects have proved so costly that the projects have eventually folded.

How then to interpret the difficulties that beset many heavy and chemical industries in the late 1970s and early 1980s? The neoliberal hypothesis would say that these difficulties indicate that the heavy and chemical industry drive departed radically from CA. Another hypothesis suggests that the difficulties were due less to the misallocation of resources between sectors, as in CA theory, than to a non-CA-based macroeconomic mechanism. The sheer size and speed of the "big push," coupled with the long gestation period of these industries, caused inflationary pressures, depreciation in the exchange rate, deficits in the balance of payments, and budget deficits. These prompted the government to institute a stabilization package, which caused deflation just when the output from the new industries came on stream, shrinking the market and lowering the returns. The rebound of the Korean economy in the mid-1980s may have been due less to the economic liberalization of the early 1980s (the neoliberal position) than to a combination of the earlier stabilization plus the maturation of the heavy and chemical industries.<sup>71</sup>

The main point, however, is that little is known about the answer to the central question of whether, in what ways, and when Korea departed from its comparative advantage. This is a great handicap for political analysis of the role of the state. For a central question of such analysis is how much, and by what methods, the government determined a pattern of investment allocation that differed from what unguided private businesspeople operating in real markets would have produced. And if there was a difference, to what extent did the government stick to projects that, though financially unviable for private businesspeople, were nevertheless economic at proper shadow prices? Or to what extent did the government disregard this constraint and undertake projects that looked to be economically unviable according to conventional social cost/benefit analysis? This indicates the extent to which the government went against "market forces," and thereby the amount of state power needed to effect the desired investment pattern—the amount of "leadership" as distinct from "followership." Followership is indicated where government sup-

<sup>71</sup> I owe this point to Richard Auty.

port went to projects that looked to be more or less financially viable at the start. Type I leadership is indicated where government support went to projects that were financially unviable but economically viable *ex ante*. And type II leadership is indicated where government support went to projects that were economically as well as financially unviable *ex ante*. A project supported by type II leadership that turns out to be economically successful (for reasons other than unexpected exogenous price changes) poses a greater challenge to economic theory than does a successful project helped by government followership or leadership of type I. This is not to say that the latter two roles are of minor significance. They still give scope for the government to formulate a vision of the appropriate development path and to choose commodity groups within the wide band of CA-consistent products for intensified growth, coordinating entry to these industries so as to reduce the risks of surplus capacity, thereby producing a different, but still CA-consistent, growth path than would be produced by unguided private businesspeople on their own.<sup>72</sup> MITI's role in Japan's supercomputer project (see the second epigraph to this article) may have followed this logic.

Amsden, and the literature in general, pays too little attention to these issues. And one other key part of her argument is also insufficiently developed, as is also true of the wider literature. This concerns "learning."

#### INDUSTRIALIZATION THROUGH LEARNING

In Amsden's schema the central difference between the early and late industrializers is that the former were driven by Schumpeterian innovation and the latter, by "learning." But what is "learning"? It has certainly become a popular word in industrial economics over the past decade or so, for it exudes an aroma of fresh knowledge. Despite its popularity, however, there has been little effort to examine it analytically, to make clear whether and how "learning" differs from or adds to what was talked about before.<sup>73</sup> It remains a terminological disaster area. Ams-

<sup>72</sup> On government leadership and followership of the market, see Wade (fn. 57); and *idem* (fn. 17), chaps. 1, 10. See also Joseph Stern, "Industrial Targeting in Korea," Discussion Paper no. 343 (Cambridge: Harvard Institute for International Development, 1990). The latter makes an important contribution to the analysis of industrial policy in general and to the literature on Korea, and I regret not coming across it until this paper was going to press.

<sup>73</sup> See Sanjay Lall, *Learning to Industrialize: The Acquisition of Technological Capability by India* (London: Macmillan, 1988). "Learning" makes a jazzy title but receives little conceptual attention; it seems to be used as a single word to mean "technological change that leads to productivity growth." The problem is that the word seems to indicate some specific mechanism of causality, but this promise is not fulfilled in Lall's (or Amsden's) discussion. For a useful overview of some of the problems, see Martin Bell, "'Learning' and the Accumulation of Industrial Technological Capacity in Developing Countries," in Martin Fransman and

den sometimes talks of learning, implicitly, as any continuous technological change that is not pushed by formal research and development, leaving R and D to be linked to innovation. But to oppose learning and R and D as in some sense mutually exclusive is misleading. Japan as a late industrializer in the 1950s was doing plenty of R and D. And the recent Korean upsurge in R and D does not signify the end of Korea's status as a late industrializer (except in semiconductors). Most of its R and D is aimed at making it competitive in more advanced but still "follower" products and processes, as occurred in Japan up to the early 1970s. R and D in these cases has the primary function not of producing innovations but of allowing firms to absorb and master new knowledge produced elsewhere.

If the distinction between learning and innovation is less clear than Amsden would have it, the distinction between various meanings of "learning" has to be made sharper. There is first the learning of "the learning curve," the relationship between output per unit input and some measure of experience of production (cumulative volume or time). The relationship is described as the "rate of learning." Then there is the quite distinct sense of learning as an amassing of knowledge, of expertise—a change on the *inputs* side that may or may not be associated with changes on the outputs side. This in turn has to be subdivided. "Learning by doing," the focus of much work in industrial economics in recent years, is often and probably mistakenly taken to be a relatively automatic process by which a firm becomes more practiced, and hence more efficient, at what it is already doing. Finally, learning in the sense of "expanding absorptive capacity" refers to the ability of a firm, industry, or national set of industries to identify, assimilate, and exploit already existing technological knowledge about processes and products new to the firm, industry, or country.<sup>74</sup> Amsden is by no means alone in using the one label for the many concepts, but given that "learning" stands in her theory as gasoline to the automobile, it would have been helpful to have some explanation of her own usage. The Korean experience would confirm, I suspect, that much of the improvement in productivity commonly described as the result of "learning by doing" is the result of sustained, deliberate, and cost-full efforts at improvements—efforts to get more knowledge of production materials and of the ways they may be com-

---

Kenneth King, eds., *Technological Capability in the Third World* (London: Macmillan, 1984). I am grateful to Bell for discussion on some of these points.

<sup>74</sup> See Bell (fn. 73); and W. Cohen and D. Levinthal, "Innovation and Learning: The Two Faces of R&D," *Economic Journal* 99 (September 1990).

bined to permit machines to run at faster speeds, for example, efforts that are not (formal) R and D-intensive but that are certainly production-engineering-intensive. Indeed, Amsden's cases show that such effort was a dominant concern of Korean managers. What drives learning in this sense is the frame of mind that asks how a particular task can be performed better.<sup>75</sup> What is it that helps this frame of mind to become pervasive? And to the extent that learning is more than a matter of going out and acquiring a new machine, what other steps must be taken and how can public policy accelerate them? These questions should be central to a discussion of industrialization, comparative advantage, and industrial targeting. But before they can be asked, the distinctions have to be made.<sup>76</sup>

To recap: Key concepts in Amsden's argument—the state, learning, and wrong prices—are underdescribed and underanalyzed. Key causal arguments are not assessed against other possibilities—"learning via conditional allocation of price-distorting subsidies" against, for example, "reallocation from agriculture to manufacturing," or "heavy investment in education plus learning by doing at low cost," or "lower price distortions than in other developing countries," or some others to be referred to below. Nonetheless, Amsden is surely right to highlight the synergy between state industrial policies and the strategies of diversified business groups, and she has conceptualized this synergy in a promising new way.

#### STEPHAN HAGGARD'S INTERPRETATION OF EAST ASIAN SUCCESS AND LATIN AMERICAN FAILURE

Whereas Amsden challenges the neoclassical mainstream of development economics by reinterpreting one unusually successful case, Stephan Haggard jumps off from a standard neoclassical conclusion and goes on

<sup>75</sup> See Joseph Stiglitz, "Learning to Learn, Localized Learning and Technical Progress," in Partha Dasgupta and Paul Stoneman, eds., *Economic Policy and Technological Performance* (Cambridge: Cambridge University Press, 1987).

<sup>76</sup> Amsden is undertaking research in Thailand, Malaysia, and Indonesia to test an important but unsupported argument in the book: "The general properties of an industrialization process based on learning, or borrowing technology are entirely different from those of an industrialization process based on the generation of new products or processes. . . . Thus, the late acquisition of international competitiveness has given rise to certain common tendencies in otherwise diverse countries." That is, the other, less successful late industrializers have states with a set of roles broadly similar to Korea's that they carry out less effectively, price structures that are also "wrong" but less rightly "wrong," diversified business groups that are less diversified than Korea's but still more diversified and centrally managed than those of the West, and a strategic focus within firms on the shop floor but with fewer engineers and more top-down management.

to address the left-out politics. "The crucial difference between the East Asian and Latin American NICs," he says, "is the difference between industrialization through exports and import substitution" (p. 27). Given this, *why* have governments of industrializing countries adopted certain development strategies, and why, more importantly, have they changed them? For "the success of the East Asian NICs rested not only on certain discrete policies but on the particular political and institutional context that allowed the NICs to adopt those policies in the first place" (p. 21). Conversely, the relative failure of the Latin American NICs was due to a political and institutional context that strongly inclined their governments to adopt and maintain policies of secondary import substitution, despite the slower growth and income-unequalizing effects of those policies.

Haggard distinguishes three development trajectories among the NICs: the import-substitution (IS) trajectory, exemplified by Brazil and Mexico; the export-led (EL) trajectory, as in Korea and Taiwan; and the entrepôt trajectory, as in Singapore and Hong Kong. Each trajectory is in turn divided into phases. The IS trajectory begins with a primary product-export phase (Brazil, pre-1930; Mexico, prerevolution); that gives way to IS phase 1 (Brazil and Mexico, 1935-55); then to IS phase 2 (1955-65); then to IS phase 3 (1965-present). The EL trajectory also begins with a primary product-export phase (Korea and Taiwan, 1900-1945) that gives way to an IS phase 1 (Korea, 1945-64; Taiwan, 1945-60). That, however, is followed by EL phase 1 (through 1970) and next by EL phase 2 (1970-present). Each phase has an associated economic structure (or changes thereof) and associated economic policies. This schema highlights the disjunction between the two main trajectories at the end of IS phase 1 (the two prior phases are much the same, as also is the final phase of both). But the sameness of the final phase departs from a very different base, namely, the growth mechanism in place at the end of the penultimate phase, one based on secondary import substitution (that is, domestic production of capital and intermediate goods), the other based on exports of the consumer goods items whose imports were substituted for in IS phase 1. The key analytical question is therefore what accounts for the divergence. Why did the Latin Americans around 1955 continue to deepen their industry rather than export the consumer goods (and other light industrial goods) whose domestic production became well established in the prior phase? As the evidence came in during the late 1960s that the East Asians were doing better, why did the Latin Americans not switch to the superior pathway?

Haggard's general answer is that four kinds of factors bear on policy choices of this type: international factors, domestic coalitions, political institutions, and ideas. Further, he suggests on the basis of the six cases that their general causal weight can be stated as follows:

International pressures [e.g., balance of payments deficits, political conflicts with trading partners] are the most powerful stimulus to policy reform. The strength of different social groups—agricultural interests, labor, and business—can constrain or widen the feasible set of policy reforms, but it is difficult to explain policy outcomes by reference to coalitional interests alone, particularly where social groups are poorly organized, interests are subject to uncertainty, and states are “strong.” . . . [In addition] explaining the reform process demands we pay attention to the interests of politicians, the institutional context in which they operate, and the ideas available to them concerning economic growth. (pp. 28–29)

So in the Korean case, the fateful shift to EL growth in the mid-1960s “can . . . be traced to external pressures” (p. 61), namely, declining U.S. aid (which financed four-fifths of imports in 1955) and greater U.S. readiness to press for economic policy reforms using the threat of aid cutoff as leverage. This growing external pressure acted in conjunction with institutional and political changes initiated after 1961 at the domestic level by the incoming Park regime, a military regime that enjoyed much greater “autonomy” than the preceding Rhee regime. Using its greater autonomy, it concentrated decision making in the executive, rationalized the economic policy-making machinery, and developed new policy instruments for steering industrialization. But even with these institutional changes, the policies themselves differed little at first from those of the previous regime. In particular, the same lack of budgetary and fiscal discipline generated high inflation, as Park tried to buy support from key groups (notably farmers, with above-market food prices). As the imbalances grew, the U.S. in 1962 suspended all aid in an effort to bring spending and income into line. Unrest grew. At this desperate point, the political and military leaders granted the technocrats in the newly restructured policy-making apparatus more scope than before, and the latter's *ideas* about the industrialization process came to be a key factor in the determination of subsequent policy. They and U.S. advisers had for years been emphasizing the importance of stabilization, reform of the exchange rate, and promotion of exports; now, in crisis, their time came.

Compare Brazil a decade before, in the early 1950s. It was at an equivalent point in its trajectory, at the end of its is phase 1. The fact that it plunged into is phase 2 instead of switching to EL phase 1 is due, Hag-

gard suggests, to a combination of factors. First, frequent balance-of-payments deficits ("external shocks") in the late 1940s and early 1950s forced the government to consider changes in economic policies. Second, the choice of its deepening was influenced by the balance of class forces. Landed elites still constituted an important political force (in contrast to East Asia), but prior industrialization had spawned a substantial labor movement (also in contrast to East Asia) and had created a sizable business and professional middle class. A shift to outward-oriented policies, involving devaluation and import liberalization, would have benefited the existing agro-exporting sector over manufacturing. But those whose income derived from manufacturing "had an interest in continuing an inward-looking industrial course" (p. 172). Third, one important section of the agro-exporting elite also had an interest in avoiding outward-oriented policies, namely, the coffee growers. Since Brazil was a dominant supplier to the world market and since the demand for coffee was price inelastic, devaluation (instead of trade controls as a response to balance-of-payments difficulties) would have meant lower receipts for coffee.<sup>77</sup> Fourth, the commitment of the leading politicians (Vargas, Kubitschek) to the new course was important in overriding opposition to aspects of the 1954 package on the part of some of the middle class and some of the landed elite. (There was, for example, opposition to the expanded role of the state and to the entry of foreign firms.) That commitment was based upon the way that the various policies allowed politicians to weave together a support base from a coalition of disparate groups. And finally, the technocrats bought the "structuralist" ideas, then associated with Raul Prebisch and the Economic Commission for Latin America (ECLA), that sanctioned an active state role to promote secondary 19. So, too (sur-

<sup>77</sup> Haggard does not say why he thinks this is true. It would be worth a little economic analysis, even in a work of political economy—if only to be able to distinguish between "real" economic objections to devaluation and those that conceal some other agenda. A devaluation would *increase* local currency receipts from coffee at a constant world price. But then after a lag Brazilian supply would increase (assuming no production controls), pushing out the world supply curve and lowering the world price. Would this wipe out the gains to Brazilian coffee producers? Suppose Brazil had 50 percent of the world coffee market. Suppose a given devaluation gives rise to a 10 percent increase in Brazilian supply, making a 5 percent increase in world supply. For Brazil to lose revenue in foreign currency, this 5 percent increase in world supply would have to cause a fall in world price by more than 10 percent (demand elasticity of less than 0.5). I do not know whether these values are accurate for Brazil of the mid-1950s, but they could easily enough be checked. There is then a further complication. What mattered to Brazilian coffee growers was presumably not coffee revenues in foreign currency but the value of their domestic currency receipts; devaluation would have lowered the value of each unit of domestic currency, other things being equal, because imports would cost more. So the economics of the alleged opposition of the coffee growers to devaluation is not entirely straightforward.

prisingly in view of later trends), did U.S. advisers, who at this time had a significant role in Brazil, as in East Asia. So it is not the case that Brazil's new industrialization project of the early to mid-1950s simply responded to, or followed, coalitional interests: "Developmentalist economic policies led, as much as followed, the interests of this new coalition" (p. 173). The ideas of technocrats do matter, sometimes.

And that, in the context of Korea and Brazil, is Haggard's answer to the "profound puzzle" posed at the beginning of his book: "If neoclassical [EL] policies are so superior, why are they so infrequently adopted?" (p. 9). Haggard brings the trajectories up to the late 1980s and also traces the movement of Hong Kong and Singapore along their own *entrepôt* path.

To my knowledge, this is the first book by a single author to make back-to-back, political as well as economic comparisons between as many as six NICs in two regions. It outlines a usable framework for comparing and explaining development paths and, in a brave departure from conventional assumptions, pays attention to the importance of *ideas*—all in under two hundred pages. (The last third of the book is taken up with three stand-alone essays on the relationship between development strategy and foreign direct investment, income distribution, and political regime, respectively.) Some of the weaknesses of the argument can be put down to the severe compression of a mass of literature on each country; conversely, its very brevity (and abundant citations of the literature) make it a good overview of economic and political trends in these countries. Let us consider two of the weaknesses.

#### INDUSTRIALIZATION THROUGH EXPORTS AND IMPORT SUBSTITUTION

One problem lies in the starting assumption that "the crucial difference" in economic performance between East Asia and Latin America is "the difference between industrialization through exports and import substitution." Since this distinction is the key to the whole discussion, one would expect some clarification of what it means as well as some discussion of the empirical evidence on which it rests. There is none. In fact, a conceptual confusion between *outcomes* and *policy-based incentives* permeates the discussion. "Import substitution" can refer to outcomes (a rising proportion of consumption of a given item met from domestic production) or to incentives (net incentives to sell a given item on the domestic market rather than abroad). Growth may be export-led (in the sense of export growth causing output growth) without an export or outward orientation; and an outward orientation may not generate ex-

port-led growth. Distinctions like these need to be made if there is to be any objective basis for distinguishing between different phases of growth, as there is not in Haggard's discussion.<sup>78</sup>

I have discussed the empirical evidence about the importance of the distinction elsewhere.<sup>79</sup> Suffice it to say that there is some evidence against the propositions that (1) Taiwan and Korea had export-led growth, (2) they had outward-oriented trade regimes, and (3) they did so much better than Brazil and Mexico largely on account of either or both of these differences.<sup>80</sup> I do not say that this counterevidence is either straightforward or conclusive, still less that the trade *openness* of Taiwan and Korea had nothing to do with their superior performance. But it does seem important to start the political analysis with a clear statement of what the economic dependent variables are and with some discussion of the evidence about their importance.

It is important, too, to fashion a political explanation that takes account of economic constraints. It is misleading to imply that Latin America could simply have switched to EL phase I if only the balance of class forces and the "politics" had been different. The economic constraints, especially Latin America's relatively good endowment of natural resources and its effect on labor costs and labor skills, were much more limiting than such a "political" explanation suggests, as we shall shortly see.

### THIN POLITICS

A second problem with Haggard's argument is that the discussion of politics is curiously truncated. There is of course a lot about how "external shocks" (generally not specified as to magnitude) change the incentives facing incumbent or would-be political leaders and thereby trigger changes in strategy. There is also plenty about how the EL reforms were helped by preceding "political" changes, such as centralization of decision-making power and the greater autonomy of technocrats. But we never learn much about *why* these changes occur, although that would be a natural path to follow in doing political analysis.

<sup>78</sup> To be fair, there has been much confusion, conceptual as well as terminological, in the economics literature on trade policy. A first step toward clarity is to distinguish market and nonmarket bias, tradables and nontradables bias, and export and import bias, concepts that can be applied to many types of policies (not just to trade policies but also, for example, to labor market policies). A helpful paper is Sebastian Edwards, "Openness, Outward Orientation, Trade Liberalization, and Economic Performance in Developing Countries," PPR Working Paper 191 (Washington D.C.: World Bank, 1989).

<sup>79</sup> Wade (fn. 17), pp. 15-21, chap. 5, p. 308.

<sup>80</sup> *Ibid.*, esp. chap. 1, pp. 15-21, chap. 5, chap. 10, pp. 307-9, 333-42.

The most striking omission has to do with "social coalitions," however. Coalitions are, as we saw, one of four major sets of factors that affect the switch of development strategy. Accordingly, there are dozens of references to coalitions in Haggard's six country studies. Yet in not a single case is there any analysis of what the coalition is, how it is organized, what its role is, who its opponents are, how much influence it wields, and so on. Generally the existence of a "coalition" seems to be inferred from the fact that some economic categories (business, labor, landed elite) have some interests in common, or at least appear to an outsider as though they should have some interests in common. This inference is then used to support a proposition about their support or opposition to a particular policy.

Take a small example. Haggard argues that during the 1970s and 1980s Taiwan followed a more "liberal" course than Korea. Why? Partly because Taiwan's greater dependence on trade created "an export-oriented coalition heavily dependent on world markets" (p. 139) that was presumably stronger than Korea's "export-oriented coalition" (although this is not stated). Of the six countries in the sample I know Taiwan best, and I simply do not know what is meant by Taiwan's export-oriented coalition. Is it a set of organizations? If so, does it have significant autonomy? Does it lobby the government to do things the government would not otherwise do? Even without such a "coalition" would not the government in any event be responsive to the needs of exporters because of the importance of exports for growth and legitimacy? If yes, how important is the coalition in shaping Taiwan's more liberal course, assuming that it exists?

Or take the argument for Brazil summarized above. The fateful shift to its phase 2 occurred in part because of the commitment of leading politicians to the its phase 2 package. Why were they so committed? Because various parts of the package allowed them to "weav[e] together a coalition of . . . disparate groups." But this is the end of the analysis, not the beginning, and thus we have not a clue as to *how* the elements of the package allowed the leaders to weave together this coalition, whatever the coalition might have been. Given that the Latin American failure to go for EL phase 1 is the key focus for a *political* analysis (because, according to Haggard, the East Asian push into EL phase 1 was in line with economic rationality), the failure to analyze the coalitional basis for the transition is a serious drawback.

To be fair, "interest groups" and "coalitions" do lend themselves to the sloppiest kind of reasoning in the whole of political science. Their

existence is often inferred from the asserted fact of common interests, and their influence is in turn inferred from policy outcomes in line with those interests, their influence then being used to explain the outcomes—to yield, in sum, one great tautology. But this is no excuse for perpetuating the practice. From Haggard's book we learn regrettably little about what should be at the heart of a politics of economic growth: rulers' and would-be rulers' calculations, that is, how they attempt to secure support, by what mix of policies, designed to appeal to which groups, with what political success, and at what economic cost.<sup>81</sup> (Why, for example, was Park able to translate fast economic growth into political legitimacy whereas Chun was not?) Nor do we learn much about the circumstances in which "growth coalitions" form or the circumstances in which rapid growth occurs without growth coalitions or the circumstances in which growth coalitions exist without rapid growth.

These questions should have been addressed in the missing conclusion. Moreover, the country results could have been tested against some explicitly formulated hypotheses; for example:

1. Authoritarian regimes are more likely to succeed in switching and then sustaining development strategies, whatever the direction of the switch.

2. Newly formed governments are more likely to attempt to switch strategies.

3. A sudden worsening of economic conditions (say, a fall in per capita income by  $x$  percent over  $y$  years, or the near exhaustion of foreign exchange reserves) is likely to precede a switch in policy.

4. A struggle between "interest groups" (outside the state) is also likely to precede a switch in policy, with a tendency for polarization into antireform and proreform groups, the latter eventually becoming dominant.

5. A sustained switch to EL strategy is likely to be accompanied by a sizable inflow of foreign aid or loans, to bridge the gap between the bad news of the adjustment policies and the good news of the (expected) supply response.

The six case studies suggest additional issues for consideration, as well. A study of the politics of policy change should address the paradox of reform first enunciated by Machiavelli and cited by Haggard in his epigraph but not referred to again, that the reformer "has for enemies all who have done well under the old order of things, and lukewarm de-

<sup>81</sup> For a case study along these lines that provides a quantitative estimate of how much economic benefit Italy's rulers were prepared to give up in order to raise political support, see Wade, "Regional Policy in a Severe International Environment: Politics and Markets in South Italy," *Pacific Viewpoint* 23 (October 1982).

fenders in those who may do well under the new."<sup>82</sup> The balance can be tipped by such things as a short time between the costs being incurred and benefits being received, confidence that the government will persist in the new course, sizable expected benefits to important groups, and limited channels for expressing opposition.<sup>83</sup>

Amsden and Haggard have produced books that substantially advance our understanding of East Asian economic performance, one by proposing a new economic mechanism, the other by elucidating the politics behind the mechanism of the economics mainstream. But they do have certain shortcomings in common. Neither of them adequately addresses the connection between the world system and the development experiences of their chosen countries, and neither explains why the East Asian states remained relatively well disciplined in their use of an awesome amount of public power. These are central issues. My own short answers are as follows.

#### WORLD SYSTEM AND NATIONAL CAPACITY

To the neoclassical eye development is like a marathon: the determinants of each country's position are a function of factors largely internal to itself. All countries should be able, *conceptually*, to cross the finish line simultaneously. There is no inherent reason why some must remain behind others, no inherent hierarchical ordering. The experience of Korea, Taiwan, and Japan is taken to validate the belief that the opportunities for rapid development are virtually unlimited and open to any economy. The authors dealt with here, including Amsden, share this basic assumption. Of course, in Amsden's theory the institutions of latecomers are much shaped by the coexistence of more developed countries. The effort to compete against firms in the latter fosters the emergence of certain state roles and forms of business organization in the former. But beyond this Amsden says little about the impact of the world system on late developers. She differs from the neoclassicals mainly in her view of *how* latecomers avail themselves of the limitless opportunities: not by "market relaxation and state compression" but by "technological learning through condition-bound allocation of subsidies."

We should distinguish between the questions of what caused, or allowed, the NIC phenomenon itself and what determined which countries

<sup>82</sup> N. Machiavelli, *The Prince* (London: J. M. Dent, Everyman edition, 1968), 29.

<sup>83</sup> This paragraph draws on John Teye, "Interest Group Politics and the Implementation of Adjustment Policies in Sub-saharan Africa" (Mimeo, Institute of Development Studies, Brighton, 1991).

would become NICs. When Korea and Taiwan began their rapid rise up the world wealth hierarchy in the early to mid-1960s, several circumstances came together in the world economy that facilitated the NIC phenomenon. First, transport costs and trade barriers in core markets (North America and Northwestern Europe) were tumbling. Second, competition intensified within the U.S. market, especially with the entry of Japanese manufactures. Third, the accumulation of higher skills in the core work force made "unskilled" labor scarcer and therefore more expensive, which enhanced the comparative advantage of lower-income countries with a less-skilled labor force and created a demand for imports produced by such labor. All three factors combined to prompt U.S. buyers to search out low-cost suppliers in faraway places.

Latin America might have been chosen. But its abundant natural resource endowment (crudely expressed in a high man/land ratio) reduced the need to export any sort of manufactures, because enough foreign exchange came from natural resource exports to finance imports. Its natural resources therefore supported an exchange rate and wage rate too high to compete in world manufacturing markets against countries at similar income levels but without natural resources. This explains why the total volume of manufactured exports from Latin America remained small. Moreover, within this small total volume, the composition was skewed toward products that required highly skilled labor to produce and away from cheap labor products that required large amounts of basically skilled labor. This is because of the skill mix of the labor force. Latin America had a relatively low ratio of basically skilled to unskilled people and a relatively high ratio of highly skilled to basically skilled people. This skill mix, in turn, may have been caused by the ownership pattern of the natural resources and the resulting politics. Governments controlled by an elite that owned the natural resources saw no particular need to extend basic education throughout the labor force, for the exploitation of the natural resources did not depend on a large supply of basically skilled people. But the elites did want to expand tertiary education sufficiently to professionalize their own children. Hence, secondary education was often expensive; tertiary education was often cheap. For all these reasons, then, Latin America was an unlikely candidate for supplier of cheap labor manufactured exports. Notice that Latin America's notorious inward-looking trade regime emerges from this explanation as more a result than a cause of the region's poor performance in manufactured exports, quite contrary to the neoliberal argument.<sup>84</sup>

<sup>84</sup> This sets up a puzzle about Malaysia, which has drawn on a good natural resource

Korea and Taiwan benefited from the converse. They had no natural resources to cause a "Dutch disease" effect on the exchange rate and wages or to cause a government controlled by owners of natural resources to neglect education. Labor was their only resource; and their populations were unusually greedy for (comparative advantage-changing) education. Moreover, their timing was lucky. They began to experience the limits of further primary import substitution later than Latin America, just as U.S. buyers were beginning to hunt for foreign producers using cheap labor. And by this time they had developed a highly productive agriculture from which resources for further industrialization could be squeezed without imperiling food security.

In addition, they were blessed by geopolitics, located as they are on the fault line of post-Second World War global politics, abutting communist Asia. They therefore took on unusually great importance in U.S. eyes, which reinforced U.S. concern for their economic growth (more than for Latin America's), a concern that translated into massive aid, good access to the biggest, richest market in the world, and U.S. tolerance of their import barriers and state support for U.S. companies wishing to invest there. Location on the fault line eventually came to matter less than did proximity to Japan, since 1960 the most dynamic economy in the world. Proximity, cultural affinity, and historical familiarity all helped to create an important "neighborhood" growth effect, not just in terms of trade but also in terms of the plausibility of Japan as a model for emulation.

Of course, all these opportunities might have been frittered away. That they were not had a lot to do with the existence in Korea and Taiwan of a state apparatus that was both authoritarian in relation to its subjects and disciplined within itself, and that used its power to pursue the goals of military strength and national economic wealth. Why was it disciplined and competent? If it is true that bigger and better markets (often) need bigger and better states, it is also true that bigger states (often) seek to control or remove markets.<sup>85</sup>

There is no simple answer. We need to think in terms of an interacting combination of elements within which causal priority is difficult to determine—more in terms of opening a combination lock than a padlock.

First, there was the discipline of the market and private property. Unlike Russia, China, and North Korea, these states never carried their

---

endowment with much less of these predicted effects. Its per capita income is about the same as Korea's.

<sup>85</sup> Lipton, "The State-Market Dilemma, Civil Society, and Structural Adjustment," *Round Table* 317 (1991).

admiration for the state to the point of having it provide haircuts and make shoes. Control of most of the economy's productive assets by private capitalists meant that government officials had to pay close attention to how their decisions affected profits. Second, there was the discipline of a rapidly growing pool of technically educated manpower, which again differentiates them from the Asian communist cases and from most other developing countries as well. This rapidly growing pool provided the civil service with an ample supply of well-educated managers and professionals and at the same time provided a growing source of outside technical comment on government policies via a press that was fairly free to voice technical criticisms. Third, compared with many other developing countries, Korea and Taiwan were culturally fairly unified, removing a common source of indiscipline and making the creation of a strong nation-state that much easier.

The civil service could draw on an endowment of a long experience of state rule and well-institutionalized procedures. More than this, it had a culture of social responsibility inculcated by the educational system. State officials were products of a tradition in which the school played both roles that in Western societies are divided between school and church: developing the intellect and developing a conscience. The two were linked by the teaching of explicit ethical rules, the demands of conscience being strengthened by fear of angering an amorphous deity who demands not obedience but responsible behavior toward society. High prestige has accrued to public officials because they are considered to embody this ideal of social responsibility; many of the best and brightest still opt for a low-paid civil service job rather than a more lucrative one in "basely self-seeking = neoclassical profit-maximizing" private industry.<sup>86</sup>

The structure of state-society relations allowed the civil service to operationalize a sense of social responsibility with relatively little concession to the demands of narrow interest groups. Such groups were enfeebled or thwarted altogether by both the Japanese colonial and the postindependence governments (a result facilitated by the lack of a natural resource-owning elite). What emerged was an unattractive kind of regime,

<sup>86</sup> A study of Hong Kong, the U.S., and France found that the Chinese respondents had a significantly higher capacity "for understanding the abstract notion of socio-political responsibility at the societal level." A Taiwanese educator has written that "social science ought to emphasize the development in children of moral concepts, group consciousness, patriotic thoughts, habits of cooperation, the attitude of service and the spirit of sacrifice, etc.;" see Richard Wilson, "Moral Behavior in Chinese Society: A Theoretical Perspective," in R. Wilson, S. Greenblatt, and A. Wilson, eds., *Moral Behavior in Chinese Society* (New York: Praeger, 1981). See further Wade (fn. 17), chaps. 7, 10; and Ronald Dore, "Reflections on Culture and Social Change," in Gereffi and Wyman (fn. 57).

promoting a blend of puritanical nationalism and rule by police and military might quite similar to China's and North Korea's, except that it also contained violently anticommunist measures reminiscent of pre-Second World War agrarian fascist states like Portugal, Poland, and Hungary. On the other hand, at least Adam Smith's great fear of the invisible hand of merchants behind the very visible hand of government had not much basis here. And not being perforated and pressured by outside interest groups, the bureaucracy could more easily demonstrate competence. Furthermore, the weakness of middle-class organization, compared with Latin America, meant that less foreign exchange had to be spent on imported consumer goods, easing pressure on the balance of payments. At the same time the state created a variety of channels of information feedback about private sector capabilities and preferences.

But why did the rulers and the bureaucracy elevate *economic* goals to such importance? Here we have to bring in a number of external contingencies to complement the economic and bureaucratic endowments just described. First, the looming external threat: whereas the governments of most other developing countries know that they can fail economically and not risk invasion, the governments and elites of these countries knew that without fast economic growth and social stability this could well happen. This led them to make an unusually close coupling of national security and economic strength. As earlier in Japan, the economic bureaucracy was given responsibility for directing resources to enhance the war potential of manufacturing, an objective subsequently extended, with the same "can do" orientation, to joining the advanced Western world as fast as possible. The constant sense of external threat also helped to discipline the bureaucracy and to elicit more tolerance of measures of internal repression on the part of the population at large.

Second, the U.S. used its considerable influence to discipline the state's use of resources in line with economic (as well as military) goals. This reinforced the effect of the external threat by discouraging the rulers from using the state largely as an instrument of personal and group enrichment.

Third, rulers and officials were well aware of the Japanese prewar and postwar experience. This provided them with a tangible model of what a disciplined state could achieve both militarily and economically, which contributed to the development of a mission-oriented organizational culture in key government agencies.

As the rulers came to see their survival as dependent on economic success, they strengthened the hand of the economic technocrats within

the state. The technocrats in turn were able to implement industrial policies that had been pioneered earlier in Japan but had not yet been tried by postwar developing countries. The key policy feature was a "governed market," a system of mostly private enterprises cooperating and competing under state supervision, in the context of heavy investment in education. The state's dirigisme was guided neither by the half light of economic theory nor by the preferences of vote-seeking politicians. Rather, the technocrats paid attention to (1) the industries needed to increase military self-sufficiency, (2) the Japanese model, down to very specific organizational details, (3) results in export markets, and (4) private sector imports of capital and intermediate goods. With criteria derived from these sources they did plenty of what neoliberals say bureaucrats cannot do: they picked particular industries for special promotion, encouraging resources into them beyond what individuals were prepared to risk. They treated particular industries at any one time (latterly within information, electronics, and biotechnology) as the natural successors of the bridges and lighthouses of Smith's day—items he thought too critical for the general welfare to be left to market forces. And the onrush of technically educated people into the labor force helped to buffer the government from making mistakes in picking the winners: as the proportion of skilled people in the labor force rose, projects that were initially too advanced in relation to present comparative advantage soon ceased to be too advanced.

No other developing countries achieved this combination. Korea and Taiwan alone managed to obtain not only the economies of scale that come from acting in a wide economic space and the innovations induced by competition, but also the advantages of protection and selective industrial promotion. Both were able to ride the wave of global internationalization while at the same time imposing a politically determined directional thrust on resource allocation within the national territory. They thereby integrated and transformed the production structure faster than would have occurred had the controllers of capital been allowed to operate within an unconstrained logic of global profit maximization. The advantages of inserting some wedges between the international economy and the national economy were not just economic in the narrow sense. Buffering (but not insulating) people from the disruptions of market volatility helped to sustain the legitimacy of the market-based social order.<sup>87</sup> That in turn helped to avoid the acute

<sup>87</sup> See R. Bates, P. Brock, and J. Tiefenthaler, "Risk and Trade Regimes: Another Exploration," *International Organization* 45, no. 1 (1991); and Wade (fn. 17), chaps. 10, 11.

social and political instability that otherwise tends to characterize high-speed economic growth, making Korea's and Taiwan's more sustainable.<sup>88</sup>

What does this explanation suggest about the likelihood that other developing countries can transform their economies and raise incomes sufficiently fast to shoot up the hierarchy at something approaching the rates of Korea and Taiwan? It suggests the chances are a good deal slimmer than the neoliberal account would have us believe. Not only is the world economy much less expansive (a point we return to shortly), but also the political conditions needed to establish and sustain the key policy combination of competition, dirigisme, and education are too stringent to be met by many others. The stringency of this combination is consistent with Arrighi and Drangel's data on the *rarity* of country mobility from periphery to semiperiphery or semiperiphery to core over the past five decades.<sup>89</sup> As noted earlier, Korea is the only country in their large sample that moved from periphery in 1938–50 to semiperiphery in 1975–83, and Taiwan would be in the same class had it been in the sample. On the other hand, Malaysia, Thailand, and Indonesia (combined population 270 million) and the coastal provinces of China<sup>90</sup> grew rapidly over the 1980s, though from a low base. Perhaps some Latin American countries, squeezed by debt and by Asian competition in potential export markets, are moving from the semiperiphery to the periphery, leaving space in the semiperiphery for some of the Asian newcomers to move into. Perhaps Britain, with the most ill-educated labor force of all the core countries<sup>91</sup> and with a long-standing and recently reaffirmed commitment to an overvalued exchange rate, is moving out of the core toward the semiperiphery. This might leave space for some others, such as Singapore, Tai-

<sup>88</sup> This is obviously a highly stylized account. In a longer treatment we would have to deal with the dispersion around these tendencies—such as bureaucratic corruption and infighting, the Rhee period in Korea, and the early Chiang Kai-shek period in Taiwan. We might look at these questions in terms of the “Migdal effect”—the tendency of insecurely established leaders to pulverize the arms of the bureaucracy in order to prevent challenges to their rule from centers of power within the state while at the same time relying on those arms for policy effectiveness and legitimacy. See Migdal (fn. 48). For further discussion, see Wade (fn. 17), chaps. 7–10, esp. 333–42; idem (fn. 5, 1982), chap. 8; and idem (fn. 5, 1983). See also Bruce Cumings, “The Abortive Abertura: South Korea in the Light of Latin American Experience,” *New Left Review* 173 (1989).

<sup>89</sup> Arrighi and Drangel (fn. 22).

<sup>90</sup> See Ezra Vogel, *One Step Ahead in China: Guangdong under Reform* (Cambridge: Harvard University Press, 1989).

<sup>91</sup> See the discussion between senior British economic policymakers and academic analysts of British decline in Peter Hennessy and Caroline Anstey, eds., *From Clogs to Clogs: Britain's Relative Economic Decline since 1851*, Strathclyde Papers on Government and Politics (Glasgow: Department of Government, University of Strathclyde, 1991).

wan, Korea, Spain, and parts of Eastern Europe, to move into as they intensify world competition in corelike activities.

### THE CUSP OF NEOLIBERALISM

Whether or not one accepts the idea of a more or less fixed hierarchy, there is no doubt that international trade became more adversarial during the 1970s and 1980s. The escape upward of some of the low-income countries is encountering a more formidable challenge from existing NICs and from the older industrialized countries trying to hang on to existing markets. At the same time, some of the firms that are leading the escape are themselves financed and partly owned by firms from countries higher up the ladder. And within the older industrialized countries trade pressure from low-income countries is fanning political conflict. Those who speak for relatively unskilled workers and their employers are pitted against representatives of those who (whether because of their skills or for other reasons) are insulated from low-wage competition and who reap the benefits in cheaper consumer goods and services. This conflict is being intensified by the new flexible automation manufacturing technologies, with their reduced demand for both basically skilled and unskilled labor.<sup>92</sup>

In light of all this, it is curious that the neoliberal approach, with its emphasis on the mutuality of interests between rich and poor "countries" (treated as unitary entities), became the mainstream of development economics in the mid-1970s. For it was just then that unemployment, inflation, falling profitability, and increasing instability became prominent features of the OECD economies and that NIC expansion looked as if it would lead to serious conflicts of interest with groups in the industrialized economies. The vast outpouring of neoliberal research seems to dispel this fear. Yet as we have seen, the empirical basis for the neoliberal confidence is open to question, as also is its theoretical foundation.<sup>93</sup> This

<sup>92</sup> For a careful attempt to estimate the effect of trade with the "South" on workers of the "North," see Adrian Wood, "How Much Does Trade with the South Affect Workers in the North?" *World Bank Research Observer* 6, no. 1 (1991). See also Manfred Bienefeld, "The International Context for National Development Strategies: Constraints and Opportunities in a Changing World," in Bienefeld and Martin Godfrey, eds., *The Struggle for Development: National Strategies in an International Context* (Chichester: John Wiley, 1982); Paul Streeten, "Comparative Advantage and Free Trade," in Azizur Rahman Khan and R. Sobhan, eds., *Trade, Planning, and Rural Development* (Basingstoke: Macmillan, 1990); and Evans (fn. 35).

<sup>93</sup> The quintessentially neoclassical Heckscher-Ohlin theory says clearly that within each country some gain and some lose from the opening of trade. This is overlooked by many neoliberal practitioners. I should emphasize that my argument does not imply a blanket rejection of free trade policies. On the contrary, in stressing the importance of certain political

includes the contention that, whatever the condition of the world economy, economic liberalization in poor (as well as rich) countries promotes the mutual interests of rich and poor countries and within countries, of labor and capital, and further, that insofar as mutual interests are not being served, it is generally because the degree of liberalization is insufficient.

I wonder to what extent the continued dominance of this set of beliefs is related to the fact that much of the research has been financed by the main international financial institutions or else has been carried out by people who look to such organizations for careers and consultancies. These organizations believe that their ability to ensure the servicing of outstanding loans depends on the debtor countries' maintaining their commitment to liberalization, which is taken as the best way to promote the exports needed to repay the loans. So these organizations are well aware that liberalizing reform is in their interest as well as in the interest of the main private commercial banks.<sup>94</sup> They have thus campaigned vigorously for reforms of this kind. These two points together satisfy the requirements of a "political" explanation of the broad unanimity of neo-liberal research findings in development economics.

But this particular explanation is no doubt only a minor element in the overall assessment. A more important factor is the interests of the controllers of transnational capital and finance. As capital became much more internationalized after the early 1970s, so the power of those whose income is derived from transnational capital and finance multiplied. As a category they have both common and opposed interests. Those based in the high-technology industries (the upstream sources of the radical technological changes sweeping through the production structures of the industrialized countries) have been seeking occult protection and other state supports in order to restrict the corporate and country diffusion of these activities. At the same time they, together with their counterparts in the medium- and low-technology industries (which include the down-

---

conditions for gap-reducing gains in national income, it also suggests that free trade may be a second-best strategy in cases where the state cannot even begin to approach those conditions (as in some sub-Saharan African countries, for example). There is after all *some* truth to the neoclassical economists' implicit theory of power (also Marx's, in his writings on India) that the possibilities created by expanding markets erode existing power structures, so powerful is the incentive of profit; for that reason power structures are more or less ignored in the neoclassical analysis.

<sup>94</sup> This follows only if evidence shows that the liberalization of the structural adjustment package is usually good for export capacity, export earnings, and hence debt servicing. A recent World Bank report, carefully read, casts doubt on this and hence on what is in the bank's self-interest. See World Bank, *Adjustment Lending: An Evaluation of Ten Years of Experience*, Policy and Research no. 1 (Washington, D.C.: Country Economics Department, World Bank, 1988).

stream applications of the new technologies), have sought to open up third markets, especially in developing countries, to allow them to move their assets worldwide in search of the highest profits. The first of these two tracks involves confrontations as well as alliances between the various technology leaders, backed by their governments; but the second—opening third markets—is something that they can all agree on. So there has been a strong push by transnational capitalists, by governments of countries where transnational capitalists are powerful, and by international financial institutions to seek the removal of state controls over the use of economic assets in third markets and more generally to compress the developmental role of governments. This push has more recently been accompanied by overt support for national political arrangements that facilitate the ability of these groups to influence governments. But their interests need to be presented as entirely consistent with the common interests of national populations—for which the doctrines of “free trade and investment,” “democracy,” and “human rights” (including the right to use one’s property as one wishes) are very convenient.<sup>95</sup> In particular, an explicit model of malign state-market relations is promoted in the context of the technologically downstream activities, while occluding the implicit model of benign state-market relations in technologically upstream ones (occluding, too, the practice of nontariff protection of uncompetitive, low-technology, employment-intensive industries in industrialized countries).

In ways that are anything but straightforward, the power gains of transnational capital in the 1970s and 1980s have reinforced the consensus within economics that mutual interests are generally served by free trade<sup>96</sup>—reinforced it sufficiently to eliminate the earlier anomaly of a development economics that challenged this central tenet. The low professional esteem attached to empirical inquiry then serves to protect the belief against contrary evidence. (Asked what attainments contribute to success in the profession, only 3 percent of 212 graduate students in economics said that “having a thorough knowledge of the economy” was “very important”; 68 percent thought it “unimportant.”)<sup>97</sup> Only very compelling facts about situations close to home will serve to breach the

<sup>95</sup> I suggest no more than that the interests of transnational capital are one important set of causes of the wave of democratization in developing countries and of the salience of democracy and human rights in Northern strategy for North-South relations. See World Bank, *World Development Report, 1991* (Washington, D.C.: World Bank, 1991), chap. 7.

<sup>96</sup> Bruno Frey et al., “Consensus and Dissensus among Economists: An Empirical Inquiry,” *American Economic Review* 74, no. 1 (1984).

<sup>97</sup> David Colander and Arjo Klammer, “The Making of an Economist,” *Journal of Economic Perspectives* 1 (Fall 1987), 100.

defenses. The examples of Japan, Korea, and Taiwan have not been enough to do so. How much worse will the long-term economic performance of the U.S. and the U.K. have to get before the mainstream of the English-speaking economics profession begins to sound less like Herbert Stein, chairman of the Council of Economic Advisors during the Reagan years ("If the most efficient way for the U.S. to get steel is to produce tapes of 'Dallas' and sell them to the Japanese, then producing tapes of 'Dallas' is our basic industry"),<sup>98</sup> and less like Sir Terence Burns, chief economic adviser during the Thatcher years ("If we can't make money by manufacturing things, we'd better think of something else to do"),<sup>99</sup> and more like Governor Park of the Korea Central Bank and the senior MITI official quoted at the outset?<sup>100</sup>

<sup>98</sup> See U.S. Congress, House of Representatives, *Industrial Competitiveness Act House Report 98-697*, 98th Cong., 2d sess., April 24, 1984, p. 83.

<sup>99</sup> He was responding to complaints that tight monetary policies were destroying Britain's manufacturing industry; "Profile: Sir Terence Burns, Not Merely a Civil Servant," *Independent*, March 16, 1991, p. 16.

<sup>100</sup> This is not to endorse a "proindustry/antiservices" argument, nor is it to suggest that comparative advantage is irrelevant. Rather, the point is that Governor Park and the MITI official believe that government has some responsibility for formulating a view of the appropriate industrial and trade profile of the economy and for using public power to push in that direction, whereas Stein and Burns emphatically do not. It may be thought that a new interventionism has already arrived in mainstream economics, in particular, in the form of "strategic trade theory." But I am talking here of the developing country context, and most proponents of strategic trade theory would say it does not apply widely under developing country conditions. The World Bank has certainly tried to neutralize its polluting effect on neoliberal prescriptions. After summarizing strategic trade theory it concludes, "The trade theorists who helped develop the literature on strategic trade theory remain extremely sceptical about its policy relevance. Most fear that, rather than being used to enhance national welfare, these new ideas will do damage in the hands of interventionists who take cover behind the intellectual respectability these ideas provide." Note the implication that "interventionists" have no intellectual justification for their position and hence need a cover of intellectual respectability. See "Strengthening Trade Policy Reform (Washington, D.C.: World Bank, November 1989), Box 1-2. See also E. Helpman, "The Noncompetitive Theory of International Trade and Trade Policy," Annual Conference on Development Economics, supplement to the *World Bank Economic Review* (1989). Helpman concludes, "Policy should be designed on a case-by-case basis and . . . no intervention (free trade) remains a good rule of thumb" (p. 193). Only the first part of the sentence really follows from his analysis, the second being more the World Bank line. See also Wade (fn. 17), 14, 378. If a new interventionism has not yet entered the mainstream, there are signs of a new defensiveness. Consider, for example, the following. After the *Economist* published an unusually enthusiastic review of *Governing the Market* (June 1, 1991, pp. 102-3), the reviewer received over six transatlantic phone calls from World Bank officials ringing to complain about the *Economist* publishing a favorable review of a book by an interventionist. Several said the journal was lowering its standards. Another said, "Don't you know he is an *interventionist*?" The reviewer asked each whether he had read the book or even glanced at it. Answer: No, in every case. See James Fallows, "Economics of the Colonial Cringe," *Washington Post*, October 6, 1991, for an exactly opposite interpretation of the *Economist's* review.