Guiding Globalisation: The Renewal of Developmental Purpose in Korea and Taiwan[1]

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Introduction

Capitalism has never been monolithic. It comes in different varieties.[2] Nowadays, however, the future of that variety is in doubt: pressured from below by capital mobility and from above by supranational forms of governance such as the WTO, it is most unlikely to endure say the globalists.

By the first half of the 1990s, the demise of state-guided capitalism (so-called 'developmental state' model) in East Asia was widely anticipated as an unavoidable by-product of economic success. As the technology gap is narrowed, as democratic institutions are established, and - above all - as the economy becomes internationalised through the lowering of barriers to trade, investment, and finance,

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[2] Appreciation of capitalist diversity began with Ronald Dore's *British Factory, Japanese Factory;* it flourished with the publication of Chalmers Johnson's (1982) seminal study of Japan and came into its own after the cold war ended, with the appearance in 1993 of Michel Albert's popular *Capitalism vs. Capitalism.*

the rationale and support for, as well as the efficacy of, the developmental state (DS) must inevitably decline, argued numerous commentators.

The financial collapse of 1997 sharply reinforced this conviction, though for reasons that had more to do with perceived 'failure' than success. As one commentator put it in a statement typical of the mainstream view, 'the economic crisis of 1997-98 raises serious questions as to the ability of an Asian form of capitalism to survive the liberalising demands of the IMF and United States' (Crane 1998: 64). When invoking an 'Asian' form of capitalism, most commentators appear to have in mind the 'developmental, state-guided capitalism' which emerged first in Japan. It was then adapted by Japan's former colonies, South Korea and Taiwan, and effectively modified to fit Singaporean conditions. But beyond these four countries, developmental states have not emerged in the Southeast Asian region. What we find instead is a mix of more or less 'interventionist' states (some with patrimonial and predatory tendencies). Strictly speaking, then there is no 'Asian' form of capitalism. The 'Asian capitalism' idea seems to stem from the view that the Asian economies are more like one another than any one of them is like the United States. The main point to emphasise, however, is that in spite of the 'interventionism' of states in say Malaysia, Thailand, and Indonesia, this does not amount to the consistency of purpose and institutional capacity that has long distinguished 'developmental' from mere 'interventionist' states, as discussed below.[3] It is the developmental states with Japan-style institutions which are seen to be the most deviant from the free-market model and it is the forced retreat of DS from economic governance that defines the standard view inside and outside the academy at the end of the millennium. As the 'strongest' states in the region (having relatively robust developmental priorities and institutional capacities), they offer a more fruitful test of the globalisation-state retreat arguments.

So how well does the standard view match the patterning of change in East Asia's guided market economies? How have developmental states responded to the constraints and challenges of economic openness and how may these responses sustain or erode state guidance and the government-business relationship? In short, where is state-co-ordinated capitalism now and what kind of role is it likely to maintain in an era of economic openness?

In order to assess the nature and extent of domestic changes and, in particular, to see where the impact of globalisation comes into play, I compare Taiwan and Korea - arguably post-war capitalism's two most successful examples of state-guided development, outside of Japan. As such, they offer a fruitful context for appraising 'endist' and convergence arguments.

The discussion reports on research undertaken for a larger project. Some of these

[3] On Northeast-Southeast Asian differences, see Weiss (1999a).

findings are of a more preliminary nature than others (e.g., in some cases, they report on changes that are still in the process of implementation, especially regarding Korea). Nonetheless, the thrust of the evidence to date does indicate that there continues to be considerable scope for state guidance in national economic management and for government-business co-operation, even - or perhaps especially - as economies restructure to meet the new conditions of economic openness. In Taiwan, the state's capacity to co-ordinate structural change has been enhanced by economic liberalisation; in Korea, where significant dismantling of the DS had occurred prior to the Asian crisis, a newly created state agency is now hastening chaebol restructuring and preparing firms to withstand the entry of foreigners.

The analysis is set out in two parts. The first focuses on Korean developments both prior to and since the 1997 financial crisis. It shows how, after a period of considerable state dismantling, the government-business nexus is being reconstituted and how state guidance in post-crisis Korea lies at the centre of efforts to strengthen the nation's industry and financial sector as increasing openness is forced upon the Korean economy. The section on Taiwan highlights the continuing developmental purposiveness of its decision-making elite for whom the persistent threat to national security from China makes state retreat unthinkable. It shows how increasing economic openness has gone hand in hand with an enhancement of the state's catalytic role in economic restructuring and its regulatory control of international financial flows.

By way of introduction, however, we preface that analysis with a brief overview of the developmental model and its particular evolution in Taiwan and Korea.

Developmental capitalism in Taiwan and Korea

The concept of DS means more than a state that is 'pro-development'. As originally conceived and applied to Japan, Korea, and Taiwan (and Singapore) during their high-growth periods, developmental states could be distinguished by their 'transformative', production-enhancing, growth-oriented priorities; their organisational arrangements (a relatively insulated pilot agency in charge of that transformative project); and institutionalised government-business co-operation (formal and informal links with organised economic actors privileging sectors or industry associations rather than simply individual firms) as the basis for policy input, negotiation, and implementation. In addition to the three fundamentals, one should note the importance of a political system which supports a shared project of economic transformation, where there is elite cohesion over core national goals, and where the economic bureaucracy is given efficient scope to take initiatives and act

effectively (see the contributors to Woo-Cumings 1999; also Weiss 1998).

Thus, transformative goals, a pilot agency, and institutionalised government-business co-operation form the three essential ingredients of any developmental state. In the absence of the first two criteria, the state lacks an insulated co-ordinating intelligence and is vulnerable to capture by special interests. In the absence of the third, the state lacks the embedded (quasi-corporatist) quality of effective policy design and implementation, and is vulnerable to information blockage and policy failure. I call this institutional set-up 'governed interdependence', which in its most evolved form involves negotiated policy making under government sponsorship.

Control over key resources such as finance is also very important, but the significance of specific policy tools should not be overstated. While Korea relied more heavily on state-directed credit to increase private-sector investment and create large industrial conglomerates (chaebol) during the high-growth phase (c.1960-1980), Taiwan placed more emphasis on tax credits for the private sector and the control of large public enterprise in key sectors of upstream production (such as petrochemicals and steel). Moreover, as the relevant tasks of economic transformation have evolved, so have the instruments for achieving them. This evolution is clearly illustrated in Taiwan where the strong post-war emphasis of the industrial bureaucracy on increasing investment and exports gave way in the 1980s to promoting technological diffusion and continuous upgrading. The success of that shift appears less marked in Korea, where the state has moved between two extremes: on one hand, total reliance on financial control in the 1960s and 1970s to achieve its objectives of creating a Korean presence in all the major export industries and, on the other hand, gradual relinquishment of control over financial institutions and state-guided investment in the decade up to 1993. Thus as President Kim Young-Sam led the first all-civilian, democratically elected government that year, the new administration looked more to the free-market ideas of the United States than to Japan for a guide to financial liberalisation.

The politics of that change and its larger consequences (e.g., Korea's increased vulnerability to, and ultimately direct involvement in, financial turmoil) are very important, but quite separate issues which cannot be discussed here. Suffice to note that a key reason for Korea's shift away from state-directed credit and the guided-market model in the decade or so prior to the 1997 financial crisis was not so much a response to external pressure being applied by the US administration,[4] as an effort to overcome the contradictions of the Korean model which had resulted in a pronounced stalemate between government and business. We return to this point

[4] For example, most 'pressure' coming from the US aimed at gaining access to Korean markets for American financial institutions, not at capital account opening. Ironically, Korea remained protective on market access, while opening its capital account to short-term inflows. The fact that reporting requirements only applied to loans of more than one-year maturity was a key regulatory weakness that sent the freshly deregulated banking system (borrowing short, lending long) spinning out of control.

below.

Since my aim in this paper is to cover the major globalisation challenges and how state-guided systems are able to respond to these, I shall not attempt to 'compare' Korea and Taiwan across parallel adjustment episodes. Rather, I shall pay attention to those episodes that have significantly tested state capacities in each national setting. Thus, in the Korean context, I focus in particular on post-crisis reforms which seek to restructure industry and finance in response to market opening measures required by the IMF conditionalities and the WTO Financial Services Agreement. In Taiwan, where financial crisis was averted, I turn instead to major episodes of industrial restructuring and financial liberalisation - the first in response to world currency movements, the second driven in large part by geopolitical concerns to strengthen Taiwan's international links (and thus bolster its security against mainland aggression).

Korea: relinquishing and retrieving state capacity

A stylised account of the Korean development model as it evolved up to the mid-1980s would highlight the following ingredients: a strong state in command of the financial system; a strategic industrial policy oriented towards closing the technology gap, involving 'disciplined support' - i.e., generous benefits in exchange for performance outcomes; subsidised, tightly co-ordinated investment via the Economic Planning Board (EPB) - the state's pilot agency in charge of national economic management; creation and nurturing of large industrial conglomerates; and rapid structural transformation (e.g., the shift from light to heavy to technology-intensive production). At least since the early 1990s, Korean developments have seemed to many to herald the retreat of this state-guided model. This is partly because, of all the developmental states, the Korean was the most 'top-down' in approach and thus the most 'deviant' from the free-market model. But it was also in part because, in recent years, the Korean model had become the most contested domestically (both inside and outside the state sector), and thus the most subject to redefinition. The 1997 financial turmoil and subsequent intervention of the IMF have helped reinforce the conviction that state-guided capitalism must give way to the power of global markets. Korea is now seen by many outside observers to have little choice other than to transform its system along neoliberal lines. Under IMF guidance, many believe economic openness is bringing Korean economic management into line with the so-called 'Washington consensus'.

The evidence, we will see, is contrary to expectations for, in the aftermath of the crisis, two patterns stand out. First, major restructuring is underway, but that process

is being driven by the state, not the market. Second, increased market opening is taking place alongside extensive reregulation. But before we turn to current developments, we must begin with the pre-crisis unravelling of the Korean model.

The unravelling of 'Korea Inc.' prior to 1997

For two reasons, the Korean experience seems a misleading gauge of globalisation's transformative powers. First, the very features of the Korean case which brought the state-guided model into contestation and led to its considerable unravelling in that country prior to the Asian crisis are features that are specific to the Korean setting. They concern the deep tensions that issue from interactions between, on one hand, a strong state given to top-down, often repressive, control and, on the other, huge concentrations of industrial power based on family-centred conglomerates. The contradiction stemmed from the fact that the chaebol, in their continuing quest for diversification and expansion, had become financially 'over-enmeshed' in the DS, while in their structure and ambition had grown more and more independent of it. It was this contradiction within the Korean model itself that state actors sought to address from the early 1980s onwards, in response to an earlier financial crisis. Two related courses of action remained: restructure the chaebol and the financial system.

Korean efforts to this end were aimed at reducing the state's role in industrial finance, partially liberalising the financial sector to create alternative sources of corporate funding, reducing chaebol business units to core activities, and thus limiting their levels of debt. Accordingly, in the decade prior to the Asian crisis, the key challenge for the DS, at least as state actors approached it in Korea, shifted from that of being guide and 'midwife' (Evans 1995) - helping to bring new projects to fruition - to one of seeking to impede and control the expansionary tendencies of its industrial behemoths. As we shall see, it would take almost two decades and ruinous financial collapse before the state's restructuring efforts would begin to bear fruit.

More to the point, however, significant state dismantling took place *prior* to the crisis, culminating in the 1993 abolition of Korea's pilot agency, the EPB. Dismantling had been driven by reformist-minded bureaucrats who viewed state retreat from industrial finance (and thus industrial policy) as the solution to the government-business impasse. Thus, unlike their Taiwan counterparts who used financial reforms to enhance their co-ordinating powers, the Koreans approached financial liberalisation as a means of distancing the state from industry. Neoliberal ideas thus gained a stronger foothold among Korea's economic bureaucrats than in either Taiwan or Japan. The reason they did so was largely because such ideas resonated with efforts to overcome a specifically Korean problem: that of 'developmental blockage', whereby massive business structures were firmly bound to the state, while at the same time increasingly constraining its capacity to discipline those structures. Thus, the more the chaebol were financially dependent on state-directed credit, the more the state was bound to protect them against failure.

Thus, on the eve of the Asian crisis, Korea's state-guided development model had undergone significant unravelling. State withdrawal from industrial policy nevertheless came with its own price for it left a highly-indebted corporate sector free to over-extend its financial obligations and to invest in overlapping (oversupplied) sectors. Partial, but ill-conceived financial liberalisation deregulating short-term flows in the first half of the 1990s - a mark of Korea's 'free-market' credentials intended to seal its membership in the OECD - further increased vulnerability to financial turmoil, as the events of 1997 made clear. With its direction uncertain and its domestic institutions weakened, the Korean state proved ill-equipped to manage internationalisation. Dismantling in short, left Korea more vulnerable to economic turmoil and paved the way for global flows to wreak their havoc.

Restructuring in post-crisis Korea

A rather different, yet equally important, consideration casting doubt on globalisation's role in Korean state dismantling is that even a 'post-developmental' Korea is likely to have more in common with what preceded it than with the Anglo-American outcomes anticipated by global convergence arguments. Current forms of state involvement in industrial restructuring offer support for this proposition, as I shall presently illustrate with reference to aspects of regulatory reform in post-crisis Korea.

Headed by President Kim Dae-Jung, Korea's new administration has declared its intention to drive through corporate restructuring, yet maintain the principle of upholding market mechanisms and refrain from intervening in chaebol affairs. To this end, the state would determine the deadlines and extent of corporate restructuring, but allow the chaebol to decide which business units to retain and release. But deadlines came and went as the chaebol refused to relinquish existing subsidiaries and piled up further debt. By the end of 1998, however, all this would begin to change with the rise of a new reform bureaucracy centred on a single supervisory body, the Financial Supervisory Commission (FSC).

The FSC (rather like the EPB in its prime) is authorised to do much more than regulate the entire financial services industry. Because the FSC can deploy traditional policy mechanisms of credit rationing and refusal, the chaebol are also effectively under its control. The FSC is thus empowered to implement the state's corporate restructuring policy and has made clear its intention to discipline any bank or financial institution that lends to firms not considered viable by the government. In this respect, the FSC represents significant recomposition of state capacity.

With its newly enhanced leverage over the chaebol and a renewed sense of public purpose to put Korea back on track, the state appears at last to have broken through

the government-business impasse. Thus the Korean state is leading the drive for industrial restructuring. Corporate restructuring is perceived as critical, not only to national recovery, but also to the nation's ability to meet the key globalisation challenge: that of preparing Korean firms in industry and finance to fend off competition from outsiders as Korean markets are pried open by the WTO and IMF agreements. The strategy, in short, is to 'streamline' the chaebol, using a mix of sanctions and incentives to force them to divest non-core units and consolidate business lines in a series of swaps, mergers and acquisitions. Through these so-called 'big deals', the aim is not only to reduce the high debt-to-equity ratios of the chaebol, but also to create a few lean and highly competitive players in strategic industries, especially in the critical export sectors of automobiles and electronics. Essentially, the government is seeking to create new 'national champions' to withstand the entry of foreign multinationals. Thus, while occasionally, the chaebol may be forced to sell a subsidiary to a foreign firm, for the most part the government has acted to minimise such sell-offs in Korea's key export sectors. This is equally clear in the banking sector, as we shall see below. In this light, the government-business nexus is being reconstituted to strengthen Korean control of its assets.

While the chaebol struggle hard against reform - just as they did in the decade prior to the crisis - the main difference is that the state now has something it lacked before the crisis: a renewed sense of direction and national purpose and, somewhat paradoxically, the external authority of the IMF under which to pursue its long-sought objectives of corporate reform.

Reregulating the financial sector

A similar story can be told for financial restructuring. The Korean state is reregulating foreign financial institutions and leading a merger drive in the domestic banking sector at the same time that Korean financial markets are being opened up by the WTO and IMF agreements. It is widely understood that IMF conditionalities require greater foreign participation in Korea's domestic banks. Nevertheless, two years after the crisis, the IMF found it necessary to complain that little had changed.[5] Most foreign involvement in Korean banking has taken the form of minority shareholdings. Indeed, having injected more than $50 billion into the sector in the past two years, the state is seen to have effectively 'nationalised' the major banks, at least in the short term.

While the administration lays claim to being strongly committed to a liberalised economy and to foreign investment in every sector, it has not interpreted this to mean an unregulated environment or one that leaves outcomes entirely to the survival of the fittest foreigners. On the contrary, its new focus on 'prudential regulations' aims

[5] As part of its commitment to the IMF, Korea had agreed to sell two of its leading commercial banks within two years of its rescue. In December 1999, with only one sold and the overseas sale of the ailing Seoul Bank having failed, the IMF renewed its call for greater foreign participation in Korea's domestic banks (*Korea Times*, 3 December 1999).

to reverse earlier damage caused by deregulatory haste. Thus, as well as supporting domestic institutions by limiting the participation of foreign banks, the state has stepped up regulatory measures to control foreign bank operations. The new measures set limits to their financial expansion in the domestic arena by redefining a foreign bank's capital, setting new credit ceilings, and establishing new monitoring mechanisms.

The first two measures are aimed at curbing overall domestic lending by foreign banks and reducing the amount of credit they can extend to individual chaebol. The third targets forex transactions. While removing restrictions on foreign exchange, the new regulations require all banks to submit up to 100 daily on-line reports to the Bank of Korea 'to prove the legitimacy of every single foreign currency transaction in the market'.[6]

Foreign bank managers may appear perplexed that in Korea liberalisation goes hand in hand with reregulation. But as Steven Vogel's (1996) comparative study of regulatory reform has shown, 'freer markets' generally mean 'more rules'. Depending on the ideational and institutional context, the new rules may either hasten state disengagement or maintain its involvement. In post-crisis Korea it is the latter that leaps to the eye. State guidance and the renewal of the government-business nexus are the counterpart to increasing economic openness.

However unclear the outlines of what is emerging, we should not anticipate a neoliberal outcome. Whether the challenges to developmental states are rooted in domestic or international processes, the outcomes of regulatory reforms are more likely to be consistent with pre-existing structures, rather than overturn them.

Taiwan: globalisation challenges, state capacity enhancement

Turning to Taiwan, I shall focus on a different set of adjustment episodes in response to three major 'globalisation' challenges since the second half of the 1980s. The 'challenges' in question can be classified as the need to adjust to world currency shifts, international financial flows, and the new trading regime under the WTO. This is not to suggest that Korea has not faced similar pressures for adjustment over the years. To reiterate, my purpose is not to 'compare' and 'contrast' these two countries by examining their responses on identical dimensions. Rather, it is to show how Korea and Taiwan are 'managing openness' and in various ways 'enhancing capacity' for co-ordinating change, even under conditions of globalisation. If it is

[6] *Korea Times*, 18 March 1999.

true that Taiwan has nonetheless been somewhat more open to trade and foreign investment than Korea in recent years, this has much to do with its peculiar diplomatic position and thus the perceived need to counteract its isolation from world affairs.

Three cases of domestic response to international economic pressures are presented here, one highlighting Taiwan's use of industry policy, the others its approach to financial liberalisation. In each case, as we shall see, officials across a range of state agencies - chiefly, the Ministry of Economic Affairs (MOEA), Ministry of Finance (MOF), and the Central Bank of China (CBC) - co-ordinated responses that enhanced domestic institutions and transformative capacities.[7] Taken together, Taiwan's responses illustrate how efforts to meet globalisation challenges have served to enhance rather than diminish domestic capacities.

I begin with some examples of industrial restructuring in Taiwan, undertaken at two different points - the first in the mid-1980s in response to world currency shifts; the second (in the current period), in response to the new trading regime under the WTO. Both give some insights into how, as a small open economy, Taiwan was largely able to avoid becoming embroiled in the financial crisis of 1997 and to maintain a vigorous performance as an exporter of high-technology products. (This is in striking contrast to Thailand, for example, which failed to upgrade, became caught in a 'low-technology trap', and piled up balance of payments deficits as its currency rapidly appreciated.)

Adjusting to currency appreciation

Taiwan's first major globalisation challenge came in the form of world currency shifts in the the 1985-87 period, which rapidly strengthened the NT dollar and made its exports less competitive with those of Southeast Asia's low-cost producers. (The Taiwan dollar rose by 28% against the yen and by 40% against the US dollar in this period.) Faced with a strongly appreciating currency, officials within the MOEA worked in concert with business associations to press forward a two-pronged strategy: on one hand, the deepening of high-technology at home via a national upgrading program that would shift skills and technology up market in the domestic arena; on the other hand, the relocation of labour-intensive production in the regions. Officials within the Industrial Development Bureau within the MOEA report the intensive face-to-face involvement and lengthy on-site visits that were made in order to convince business leaders of the benefits of moving up market at home - rather than simply sticking to one's knitting and moving offshore (especially to the Chinese mainland).

[7] By 'transformative capacity', I refer to 'the ability of a state to adapt to external shocks and pressures by generating ever-new means of governing the process of industrial change' (Weiss 1998: 4). The same source provides an extended discussion from a comparative perspective.

This process of transformation (and the state capacity that underpins it) is not well captured by standard views of the 'strong state' or 'top-down' development. Government and business have been involved from the outset in Taiwan's upgrading program. The economic ministry has formed an elaborate network drawn from the industrial bureaux, research institutes, business groups and industry experts to identify and select industries, technologies, and products for promotion. Coordination between the Ministry of Economics, the Central Bank, ITRI (the state-sponsored technology research institute), and industry helped business and government undertake the deepening of high-technology industry at home, while relocating labour-intensive production offshore. This policy shift became institutionalised as the Statute for Encouraging Industrial Investment was replaced in 1989 with the Statute for Promoting Upgrading, and subsequently extended. The support infrastructure that it provided laid the foundations for constant upgrading,[8] contributing to greater export focus in advanced technology sectors, larger export surpluses, and sustained high reserves, reducing Taiwan's vulnerability to financial turmoil.[9] Changing world currency markets were therefore central to Taiwan's rethinking of industrial strategy, internationalisation of production, and deepening of high-technology production in the second half of the 1980s.

But the story of adjustment does not rest there. Today it is not world currency movements that are causing concern, but the impact of the WTO. The key problem for Taiwan - which is not yet a member - is the threat posed by China moving into Taiwan's markets. Thus, as the world trade regime evolves, we may expect Taiwan's policymakers to maintain rather than abandon this strategic orientation. To see why, we turn to a discussion of the challenges posed by Taiwan's entry to the WTO.

Managing the impact of the WTO

As Taiwan prepares to join the WTO, the agency charged with enforcing world trade agreements, globalists would predict that the state's capacity to pursue its developmental ambitions and co-ordinate adaptive change will be seriously constrained, if not eclipsed altogether by the new regime. Many commentators have of course begun to question the authority and capacity of the WTO to carry out its responsibilities. But whether or not a strengthened WTO will emerge from the Seattle debacle may be irrelevant to the issue of how far the existing regime may undermine developmentalism. For although WTO rules set limits to the forms that state involvement can legitimately take, these are unlikely to be so tight or so rigid as to rule out all transformative action, as the evidence presented below would indicate.

[8] The strategy's effectiveness is reflected in the changing composition of industrial output - in which the high-technology component leapt from 20 percent to 30 percent in the 1981-1991 period, with a forecasted share of 40 percent by 2002. Some 50,000 applications for patent rights were filed in Taiwan in 1998 and almost 6,500 in the US in 1997, second only to those submitted by Japanese and German firms among overseas applicants (*Free China Journal*, 11.12.1998, p. 7). On the guided development of high-technology capabilities of East Asian firms, see Mathews and Cho (1999).

[9] For the comparative evidence and development of this argument, as applied to the Asian crisis, see Weiss (1999a).

While admission to the WTO will require tariff reductions that will impact negatively on Taiwan's domestically-oriented sectors (in particular, home appliances and agriculture), this is regarded as an unavoidable but acceptable cost.[10] Of far greater concern for Taiwan's policymakers is the adjustment required by Taiwan's high-technology industry as a result of China's admission to the WTO and the further increase in foreign investment that it will stimulate on the mainland. Officials anticipate that China will therefore move rapidly into Taiwan's PC product markets. The response from Taiwan is once again to mobilise public purpose and government-business innovation networks to drive through a new round of technological upgrading. MOEA officials now define the challenge as that of moving towards a 'post-PC' era. So they have introduced new programs to shift industry's focus from personal computers to products such as CD-ROMs, DVDs, and LCDs, in addition to developing the biotechnology industry.

In each case of adjustment - in the 1980s and again at the turn of the century - the external challenge has been met with a similar response: a national strategy to co-ordinate rapid upgrading of products. And in each case, the state has used a mix of tax incentives and subsidised public-private R&D networks led by ITRI, the state agency driving the island's high-technology push, as the main instruments of Taiwan's upgrading strategy. Such networks have been generally based on a 50-50 contribution from government and firms.

But how will the WTO rules impact on Taiwan's adjustment strategy once it joins the world trade body? WTO rules now require that government subsidies be removed wherever these relate to traded goods and services. Will this therefore put an end to Taiwan's transformative ambitions and thus its effectiveness in moving up the technology ladder? The answer appears contrary to expectations and suggest that there is considerable scope for national governance - even within the existing framework of the WTO.

A good deal also depends on how the state approaches industry support. In Taiwan, for example, as revenues have become increasingly constrained by the new demands of democratisation, government has shifted more of the costs of industry policy to industry itself. Thus, where government funds are outlaid to assist firms to acquire new capabilities, these must be reimbursed once the technology has been commercialised and sales achieved. The key point is that since the Taiwan approach is one in which the 'subsidy' element virtually disappears - industry eventually pays for its own subsidies! - it does not infringe WTO rules. So industry restructuring may continue to depend on good governance rather than being left to the market. Such examples would suggest that states with transformative ambitions and capabilities like Taiwan can still find ample scope within the existing framework to nurture,

[10] Tariff adjustments on 8,100 items (out of 8,700 imported items) will cut import duty by an average of 8.25%, reducing the average import duty to 7.55% within a year after WTO entry.

preserve, or strengthen national enterprise, whether in preparation for entry to the WTO or beyond.

Regulating international financial flows

Our final example of adjustment concerns financial markets - an area of the global economy believed to be the most testing for states, especially small states like Taiwan. It is widely believed that when states liberalise the financial sector and open their capital account, they more or less relinquish the tools for national economic management. Some studies, however, have found that regulatory reforms, in certain settings, offer up new tools of economic management and investment strategy.[11]

This idea is nicely illustrated in the case of financial liberalisation in Taiwan, a phased process which began in the second half of the 1980s. As a small open economy, the experience of Taiwan in confronting financial liberalisation offers an instructive illustration of how, even when a state agency appears to be acting in a strictly 'regulatory' capacity, it can use the rules to enhance developmental capabilities and achieve substantive outcomes.

Thus, when the CBC liberalised access to the overseas corporate bond market in 1993, for example, it used the new regulatory arrangements to reinforce rather than relinquish co-ordinating powers. The new rules were deployed to favour *productive* investment by Taiwanese firms, while guarding against foreign exchange speculation. This is how it works: Taiwanese firms are allowed to issue corporate bonds overseas and to remit the proceeds to Taiwan in NT dollars on condition that the funds be invested in a long-term project for new plant or plant expansion. Financial regulators have thereby used the reforms simultaneously to guard against sudden inflows disrupting money markets (in particular, the risk that inflows would be used to speculate against the currency) and to enhance the state's developmental capacity.

The way Taiwan has regulation foreign exchange both before and since the Asian crisis provides an insight into the overall strategy, which I call 'managed openness'.[12] In Taiwan there are no restrictions in principle on foreign exchange. The forex market is an open one, but the transactions are highly supervised. Both local and foreign banks are subject to extensive reporting requirements to account for all such transactions (an approach now being adopted by the Korean authorities who paid the price of their deregulatory haste).

Foreign banks like Citibank may be free to indulge in daily forex transactions, but

[11] See, for example, Vogel (1996).
[12] See Weiss (1999b)

they cannot avoid reporting such operations to the authorities. 'Freer markets, more rules' - to repeat Vogel's paradoxical formulation - thus has strong resonance for the international banking community in Taiwan as well as Korea.[13]

Whether states will seek to use regulatory controls in this way is likely to depend on the pre-existing orientations, priorities, and institutional arrangements. In Korea's case, as we saw earlier, the crisis and financial collapse have discredited the idea that financial liberalisation by itself - i.e., without careful reregulation - can bring benefits. Korea is thus rebuilding capabilities that it had previously sought to dismantle in favour of more market-oriented solutions to the government-business impasse. In Taiwan's case, persistent geopolitical pressures have preserved public purpose and encouraged a more consistently managed approach to the process of global integration, especially in finance. Exposed to a constant security threat from the mainland, for Taiwan the possibility of financial destabilisation remains ever present (vividly illustrated by the nine-month missile crisis in 1995-6 which precipitated a run on the currency resulting in a $17 billion depletion of Taiwan's reserves). It is this pressure that remains paramount in the calculations of Taiwan's financial authorities. Diplomatic isolation and cross-straits relations reinforce state purpose, preserving the developmental orientation. (Even the unusually large foreign reserves - reflecting strong capacity to upgrade and maintain trade surpluses - are related to this external impulse.)

Moreover, as Taiwan is not a member of the IMF or the World Bank, it cannot rely on support from these institutions in the event of a serious financial threat. Accordingly, the Executive Yuan in September 1999 approved draft regulations to establish a stabilisation fund designed specifically to cope with serious market fluctuations. As these sorts of considerations help to explain, when the MOF and CBC approached the task of financial liberalisation from the late 1980s onwards - in contrast to officials in pre-crisis Korea, as we saw earlier - they did so with a view to enhancing state capacity, not effecting state retreat.

Opening the stock exchange to foreign investors has also involved a similar degree of care and caution. Indeed, from Taiwan's point of view, the most significant aspect of its impending accession to the WTO is the Financial Services Agreement (FSA), implemented in March 1999, which requires, *inter alia*, removing restrictions on foreign investment in the local stock exchange.[14] For Taiwan's monetary authorities, the dilemma has been that of how to allow free access to local equities, yet ensure against losing control. As of January 1, 2000, Taiwan had phased out all remaining barriers to foreign investment in listed stocks. But the groundwork for market

[13] As to whether the CBC is an effective regulatory authority, consider that forex operations - the major source of profits for overseas-based banks in Taiwan - declined by 48% in 1998 as the bank targeted international currency speculators (*Free China Journal*, 17.6.1999, p.7).

[14] The FSA, covering banking, insurance, securities, asset management and financial information, seeks to remove restrictions on the entry and access of all foreign financial enterprises to the local market.

opening has been carefully prepared over a lengthy period. There is little doubt, for example, that the state has purposefully refrained from introducing a capital gains tax in order to encourage a strong local market for equities. Whatever the precise mix of factors, by the late 1990s, the tax-free incentive had helped to produce a very vigorous domestic market. Indeed, so strong is local participation in Taiwan equities (exceeding 96% of capitalisation) - ostensibly 'crowding out' foreign ownership - that officials have felt sufficiently confident to remove, ahead of the deadline, the remaining barriers to foreign entry agreed with the WTO. Capital opening, in short, is not expected to alter this ownership structure to any significant degree.

Several other 'market governing' measures are relevant to the overall argument that, in new ways, globalisation pressures are enhancing not destroying state-guided capitalism. Limitations of space however prevent their discussion. But one should at least note a similarity with Korea in the way government is openly urging mergers in the finance sector in response to the WTO's financial services agreement. Under a new financial merger and acquisition law, the state is promoting national firms capable of withstanding competition from foreign firms in banking, insurance, and securities. Together with new performance standards established for financial institutions, these measures offer evidence of the state's continuing capacity to co-ordinate restructuring, even under conditions of globalisation.

While a great deal of emphasis has been placed on globalisation's impact on states, much less attention has been paid to the way the constraining impact of capital flows is mediated - and thus either neutralised, softened, or exaggerated - by the domestic regulatory and institutional context. The experience of Taiwan demonstrates that in spite of extensive liberalisation (not to mention full-fledged democratisation), developmentalism[15] remained relatively robust at the turn of the century. Accordingly, international and domestic constraints notwithstanding, the state centred on Taipei retains both a key role in defining financial and industrial strategy and a capacity for effective implementation.

Conclusion

The question with which I began this discussion is straightforward: 'Is the decline of developmental capitalism a necessary evolution?' Must the DS inevitably undergo dismantling and transformation into something quite different? If so, what are these 'unavoidable' pressures? The retreat, eclipse, or collapse of the developmental state has been a widely anticipated outcome in search of a single compelling cause - 'globalisation' being only the latest in a strong line-up of potential assassins.

[15] I define 'developmentalism' as both institutionalised outlook and set of policy orientations in which the state interacts closely with business to pursue shared projects of economic transformation.

The evidence reported here gives us reason to doubt the decline and transformation thesis. Neither the experience of Korea nor of Taiwan offers support for the view that capitalist diversity is doomed or that institutional uniformity is being driven by economic forces external to the nation-state (so-called 'globalisation'). At the very least, the findings reported here give us pause to consider ways in which globalisation pressures may actually strengthen or recompose state capacities. The approach of Taiwan to financial liberalisation both before and after the region's financial crisis, together with Korea's post-crisis reforms, offers support for the proposition that increasing openness is compatible with the strengthening of national governance. Rather than dictating state disengagement, liberalisation can lead to capacity enhancement.

Whether we continue to call the current configurations in Korea and Taiwan 'developmental' or something else, the important point to extract from the evidence is that state-guidance and government-business co-operation are by no means incompatible with advancing economic openness. For the countries examined here, robust state capacity appears essential to 'good' national governance in an era of economic interdependence. The critical issue then is not whether but *how* to manage openness to domestic advantage.

In internationalizing their economies, Taiwan and Korea, though in somewhat different ways, are undergoing a process of 'adaptive' change - change that is consistent with, not overturning, what went before. If Taiwan's approach has been more consistent and robust than the Korean - where significant dismantling occurred prior to (and arguably contributed to) the financial collapse - this owes much to the greater strength and persistence of geopolitical pressures. For unlike Korea, Taiwan's security environment has been marked by a persistent and credible threat in combination with diplomatic isolation and uncertain allies.

With or without those pressures however, institutional and ideational diversity are likely to persist, even if in newly modified form. The important point is that we need to take seriously the idea that change within particular politico-economic systems is less likely to override or negate the past than to take its cue from pre-existing norms and arrangements, even while embracing the new. This idea has been variously encapsulated in notions of 'path dependency' and 'institutional legacy'.[16] While such concepts give some sense of the mechanics of change, we lack the appropriate tools to conceptualise outcomes. What, for example, should we call a DS that has in some ways toned down its developmental activism, perhaps reformed certain institutional arrangements, and redefined its catch-up goals - yet remains distinctively different

[16] 'Path dependency' is a term from evolutionary economics used in other social science disciplines to convey the idea of societies as systems of historically interlocked institutions that shape the trajectory of change. Such concepts help to shed light on a well-known puzzle: why it is that even when commonly experienced external shocks may appear to elicit common national responses, the domestic outcomes often differ. This has important implications for understanding globalisation's impacts. See Weiss (2000)

from its neoliberal Anglo-American counterparts? In greater or lesser degree, changes of this nature can be identified in all four DS - Korea, Japan, Taiwan, and Singapore. Should we therefore pronounce the DS and, with it, state-guided capitalism, dead? Or should we rather seek to encapsulate its modifications - the 'post-developmental' state - in new ways? The latter task, though more challenging, seems more in step with reality.

There is a larger lesson to draw from the cases analysed here. They indicate that the scope for national governance may be considerable wherever state capacity - embodied in public purpose, priorities, and institutions - is thus directed. The global economy may appear formidable; but its impact on local and national networks is not self-determined (pure?), thus its outcomes are not pre-determined. Rather, it is the frailty or strength of domestic institutions and domestic orientations in particular that largely determine the character and degree of globalisation's impacts. In the cases presented here, one can see its effects being mediated through national arrangements designed to shape the emerging interaction and engagement with the global arena (such as the local equities market in Taiwan being progressively opened to foreign investment). This is a less expected but much more interesting outcome than the widely canvassed 'convergence'. It shows that state institutions equipped with the relevant sense of purpose and capacities can guide the impact of globalisation - just as they guided the process of development in the first DS phase.

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