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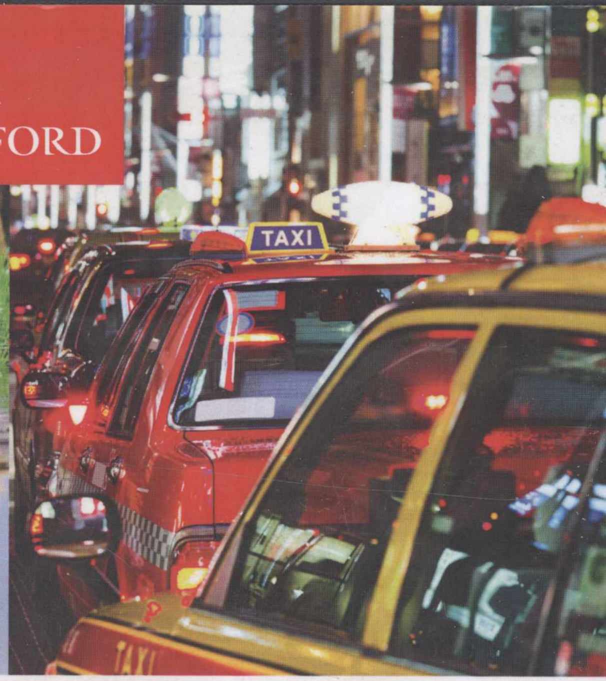

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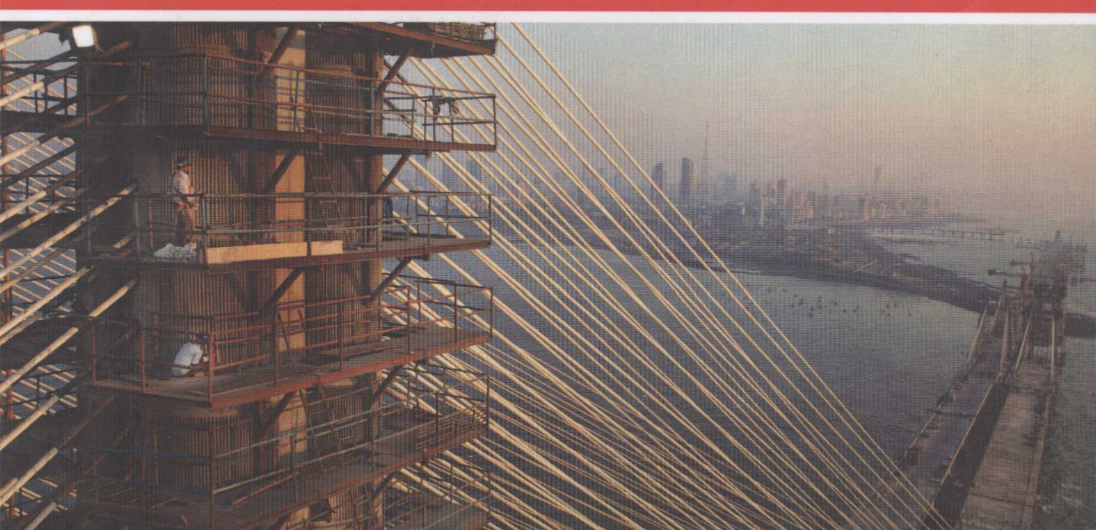

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Globalization and Economic Nationalism in Asia

Foreword

This book investigates the interactions between globalization and economic nationalism in Asian countries, an important subject, especially in the context of contemporary capitalism and the financial crisis that has dogged most of the advanced capitalist countries today. Here I consider the question of economic nationalism through the lens of economic openness.[1] Full globalization, which connotes total integration of national economies with that of the world economy, is the antonym of economic nationalism. I argue that economic openness is a multidimensional concept. A country can be open or not so open, in trade, exports, imports, finance, science, culture, education, migration, foreign investment, and investment by its citizens and companies abroad, among other things. There is no economic theory that suggests that a country has to be open in all dimensions simultaneously. Given its economic and geographical situation, a country may choose to be open in some areas and not at all, or only partially in others. I briefly present a discussion of the economic terrain in which the optimum degree of openness is an important issue.[2]

At the simplest level a policy of total autarky is not necessarily one that coincides with economic nationalism. National economic benefits may increase with some trading compared to no trade at all. Orthodox economists would argue that a nation's gains from trade with the rest of the world are best enhanced by the policy of free trade. I challenge this proposition by arguing that there are only narrow circumstances in which the orthodox stance is either analytically or historically valid, with the clear implication that states, other institutions, politics, and policies are all critical spheres of integration with the world economy. These are the themes that are discussed in this volume by Anthony D'Costa and his colleagues by richly illustrating the ways in which Asian states remain active even as they whole-heartedly play the globalization game.

One way of defining the optimum degree of openness is by using the theory of national planning. Despite our increasing ability to handle complex optimization models on more powerful computers, there are many reasons to believe that the approach is not entirely satisfactory. While a planning approach avoids easy and facile identification of the optimal degree of openness with a regime of "free trade," it suffers from a number of limitations. First, planning analysis cannot take into account issues connected with irreversibility over time except by resorting to very ad hoc procedures. Second, the only connection of this approach with history is through initial specification of vectors of primary factors, which are easily quantifiable. There are no simple and convenient ways of quantifying the states of knowledge in the community or its degree of absorptive capacity if inflows of factors from the outside world are considered to be relevant. Third, national planning models are rich in details for a single country. However, to be operationally meaningful they have to assume that the rest of the world is either going to stay constant or change only in a predetermined way. Strategic choices are excluded.

If one were to take these criticisms seriously then the alternative to planning exercises would be a somewhat looser but a more historically grounded approach, which emphasizes the advantages of trade and identifies certain factors that may make the country more vulnerable to outside influences. These may produce long-term, irreversible effects on the country's pattern of production and its ability to generate productive employment, among other things. It is important to note that such an alternative approach is quite consistent with the paradigm of classical economics, including in this respect not only Ricardo, but also Marshall. Ricardo was interested not in the artificial example of trade in wine and cloth between Portugal and England so mechanically reproduced in standard economics textbooks, but in the need to capitalize on the emerging revolution in textile production in the British economy. Marshall understood this very well, appreciating the historical specificity of the maxims of a policy of free trade, which have been treated by many as historical truths.

While Marshall clearly recognized how the changes in configuration of production forces can alter the degree and character of openness of the economy, Keynes, it would appear, was worried about schemes for post-World War II national reconstruction in maintaining equilibrium in the balance of payments of different countries. As he once put it, "To suppose that there exists some smoothly functioning automatic mechanism of adjustment which preserves equilibrium if only we trust to methods of 'laissez-faire' is a doctrinaire delusion which denigrates the lessons of historical experience without having behind it the support of sound theory" (Keynes 1980: 21–2). Now it is clear that in history there have been periods, in which, as Keynes himself acknowledged, payment arrangements have worked out satisfactorily. This permitted large expansions of trade and trade-induced growth. However, these have been episodes characterized by the presence of suitable conjunctures, as the study of the economy for the period after World War II, the "golden age," demonstrates (Glyn, Hughes, Lipietz, and Singh 1992).

A country wishing to open up when the conjuncture is adverse in Keynes's sense (that different economies are characterized by "persistent surpluses" or "deficits" without any mechanism to restore global equilibrium) may benefit much less and, in certain cases, may end up being much worse off than if its opening-up process were differently timed. If timing makes a difference—and timing is important—and if returns to scale are increasing, openness by virtue of assuring higher levels and growth rates of external demand may facilitate major structural changes in the economy, and induce higher labor productivity and growing per capita consumption. If on the other hand the timing is wrong, a country may have to go through painful processes of adjustment precisely because it is more "open" than not. This would once again suggest that we ought to deal with the problem of openness in terms of rate and pattern of growth of output with due recognition to carry out structural changes as and when circumstances warrant.

The traditional economic answer to the question of the optimal degree of openness for the economy is given in terms of the theory of free trade. This theory is, however, extremely restrictive. Its validity depends on various neoclassical assumptions such as full employment, no externalities or information asymmetries, and perfect knowledge about goods and services being traded. However, the benefits of free trade can be realized only under specific world economic conjunctures coupled with domestic policies that go considerably beyond the limits of commercial policy as traditionally defined. For example, two well-documented historical episodes where trade and growth-promoting forces interacted in a positive manner were linked to the hegemonic roles played by Britain and the USA respectively. Economic historians have pointed out that Britain's decision to adopt "free trade" as the major thrust of its commercial policy helped to trigger the secular boom of the second half of the nineteenth century. But changes in the geopolitical situation, coupled with altered industrial leadership consequent on the maturing of major new innovations during the second Kondratieff, as described by Schumpeter, led to severe strains towards the end of the nineteenth century and to the violent demise of the free trade system.

Openness can benefit an economy if relatively specialized resources are concentrated in production whose world demand: is highly income- and price-elastic; leads to diffusion of knowledge and thus upgrading of the quality of local factors of production; enhances efficiency due to increased competition, and alters the distribution of income, which can lead to greater share of production over time. The question of increasing returns to scale and imperfect competition has received considerable attention in the recent developments in the theory of free trade. This literature has been reviewed by Paul R. Krugman (1987).

However, as Krugman (1987) noted, in the type of "second-best" world relevant in the contemporary context, there is no automatic tendency for gains from trade to be realized. The scope of gains from trade does not necessarily decrease but the composition of trade changes significantly from inter-industry to intra-industry trade. Furthermore the need for government intervention can no longer be ignored. While Krugman himself ends up with a justification for free trade, he noted that "this is not the argument that free trade is optimal because markets are efficient. Instead, it is a sadder but wiser argument for free trade as a rule of thumb in a world whose politics are as imperfect as its market" (Krugman 1987: 143). The main reason behind Krugman's cautionary ending is that sophisticated interventionism is likely to be a difficult exercise in political economy. However, because of "nationalist" sentiments, the world trading system cannot be expected to gravitate to free trading. Instead, the argument better meets the need for "managed trade."

There are several reasons why trade needs to be managed. These have to deal with the fact that "openness" can be a mixed blessing. The point was well understood by Keynes when he changed his position from being a champion of free trade to that of an advocate for "national self-sufficiency" in the midst of depression during the 1930s. However, Keynes's argument was more subtle than that of simple-minded economic nationalism. He was all in favor of free movement of people between countries, freedom from passport controls, free educational and cultural exchange. But he was opposed to the free movement of capital and goods, as that led to mass unemployment. Furthermore, there are situations in which increasing the openness of the economy may harm the quality of locally available factors. The classic example of this is the adverse impact of British cotton textiles on Indian cotton weavers in the nineteenth century.

Generally, it has been seen that "openness" works positively if "learning" from contacts with the rest of the world is suitably institutionalized, and there is appropriate adaptation of policies involving strategic government interventions that make the domestic economy more responsive to change. The experience of Japan and the newly industrialized countries of Asia, and now China and India, seem to suggest that home market expansion can often trigger growth-promoting investment, which then leads sequentially to import and export substitution along highly efficient lines. In its turn, home market expansion may have much to do with increases in food productivity levels. Arthur Lewis (1966) strongly underlined the importance of food productivity growth as a mechanism of overcoming the terms of trade loss suffered by many tropical countries that specialized in primary commodity exports.

In the absence of a growing home market accompanied by suitable diversification of the industrial structure, the effect of "openness" can at best be a "once-for-all gain" from increased openness. On occasion it may lead to pronounced economic difficulties for the country, which liberalized its trade and investment policies in the expectation of sustained growth but without adequate preparation on the knowledge absorption side. To sum up, the phenomenon of learning over time is a more relevant paradigm for development gains through trade as distinct from the neoclassical emphasis on exploitation of arbitrage opportunities based on comparative advantage.

Since the demise of the golden age in the 1970s, the world economy has evolved. Most developed countries have adopted more or less free trade and more or less free capital movements since the 1980s. A number of developing countries have done the same since the 1990s. It is this regime of globalization integrating national product and capital markets that provides the backdrop to the discussion of issues of economic nationalism addressed in this book. The editor is quite right to point out that economic nationalism is still widely practiced, notwithstanding globalization, by most successful as well as unsuccessful countries. And there are political and institutional reasons why states continue their activism.

This book provides an analysis of economic nationalism in five leading Asian countries: India, China, South Korea, Japan, and Singapore. Each of these countries has adapted its interventions to the requirements of the new international trading and financial regime and changing domestic class forces. The detailed analysis offered indicates that globalization has not been negated by economic nationalistic measures adopted in one form or another by all five nations; nor has economic nationalism been able to overcome the institutional framework of globalization. To use a different language, what has happened is that Asian countries have sought not close integration with the world economy but strategic integration. They have been open in some spheres and not in others according to their national advantage. Before globalization, strategic integration or managed trade was relatively easy. However, under a revamped World Trade Organization (formerly the GATT) and international legislation, the policy space for most developing countries has been considerably reduced.

It is widely believed that financial globalization and the world financial system have been responsible for the most acute economic crisis to hit the international economy since the Great Depression 60 years ago (Singh 1997). The particularly poor performance of the advanced capitalist countries is regarded as proof of the failure of globalization. This is, however, a one-sided view that ignores the fact that the crisis occurred only in rich countries and not in poor countries. In fact, Asian countries have performed well prior to and during the crisis. Since the beginning of the new millennium and until 2007, the world economy grew at a historically unprecedented pace. Between 2003 and 2005, the world economy grew at a rate of 5% per annum in PPP terms, a rate never before achieved. The economic performance of India and China, the two most populous and hitherto among the poorest countries in the world, was stellar. Overall, the growth rate for developing countries was twice that of rich countries, thereby reducing the distance between the two groups of countries. In general, the level of poverty (defined as earnings below a dollar a day) fell by a large margin in many countries and in the world as a whole.

The essential reason for the good performance of Asian countries lies in the measures adopted by these countries following the lessons they learned from the Asian crisis of 1997–9 (Singh 2002). Since the crisis, these countries started to strive for current account surpluses and to accumulate reserves, which stood them in very good stead during the current crisis. Additionally, most of these Asian countries inherited the institutional basis for industrial learning and strategic intervention, which was established during the heady days of import substitution industrialization and mercantilist trade policies in East Asia. This was a triumph of economic nationalism over globalization. Developing countries did not repudiate globalization but took advantage of it while protecting themselves against its dangers by adopting nationalistic economic policies towards reserves, balance of payments, and strategic industrial policy.

What is crucial today is that both the North and South grow. The North needs full employment (Singh 1995) and the South high rates of growth to minimize poverty and improve the desperately low living standards of the people. Recent research indicates that if developing countries such as India and China were to grow at the desired rate, this would be incompatible with full employment growth in developed countries (Izurieta and Singh 2010; Cripps, Izurieta, and Singh 2011). However, the research also indicates that cooperation between rich and poor countries, particularly India, China, and the USA over technical progress (such as energy saving) can resolve these difficulties. Such cooperation is to be preferred to the narrow economic nationalism of the 1930s, which led to stagnation and crisis. A globalized world economy is in the interest of developing countries provided they have the policy space to enable them to achieve fast growth, reduce poverty, generate quality jobs, and ensure relatively equitable distribution of the benefits of growth. Globalization, together with international economic cooperation among nation states, is a far better goal for developing and emerging countries as long as they are able to manage strategically the economic vulnerabilities associated with international integration. More importantly, by regaining the policy space lost through globalization and committing to spread the benefits of growth widely to their citizenry, states will have justified their nationalist interventions.

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Notes

1. This is a condensed version of a keynote address delivered at the conference "Globalization and Economic Nationalism in Asia," organized by the Asia Research Centre, Copenhagen Business School, December 3, 2009. Financial support from Cambridge Endowment for Research in Finance, the Malaysian Commonwealth Trust, and the Centre for Business Research at Cambridge is gratefully acknowledged.
2. Views on the optimal degree of openness and the subsequent discussion on free trade are adaptations of those first presented in Chakravarty and Singh (1988).

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Preface

The global financial crisis of 2008 is a harsh reminder that capitalism as an economic system is still vulnerable to the whims of market dynamics. It is the convergence of the economic motives and aspirations of individuals, households, corporations, and governments that generates the systemic forces of capitalism and also drives economic growth and structural change at the global and national levels. There are occasions when structural imbalances between supply and demand and the inability of the regulatory institutions to stabilize the runaway economic forces produce periodic slumps, which sometimes are severe enough to warrant a depression-like economic stagnation. The recent "Great Recession" led by the housing bubble and Wall Street's financial excess in an era of deregulation and international economic integration is of crisis proportion even though unemployment has not been as severe as that of the Great Depression of the 1930s. However, the prognosis for the USA and the world economy in 2011 is for continuing slow growth and economic misery at least through 2013. The European financial crisis and sluggish Japanese growth—made worse by the recent tsunami and nuclear plant disaster—have added to global economic woes. In this sense, this may turn out to be the worst economic crisis to date.

In the midst of such a crisis, can we expect states to remain aloof and let the economic crisis run its course with the belief that the economy will right itself? But governments cannot watch from the sidelines, since states have a national responsibility to manage their economies and ensure social stability. Ambitious states have political legitimacy concerns and hence cannot remain passive in the face of the economic turbulence or the sluggish pace of change. Even those states that profess excessive allegiance to the virtues of free markets intervene when compelled. It is instructive that governments of varying political persuasions have responded with swift institutional moves to the recent financial crisis, including the USA, whose political distaste for regulation is widely known. Bank and industry bailouts, fiscal stimulus and monetary expansion, and re-regulation of financial institutions have been the principal forms of state intervention. Curiously, there was no talk of protectionism even though the *Economist* (February 9, 2009) sounded alarm bells, predicting economic nationalism would go wild and drag the world economy even further down. What is now evident is that states, despite neoliberal leanings more or less across the board, have become far more active in economic and financial management than they were before the crisis.

The 1980s neoliberal reforms rested on the presumed confidence in the workings of an unbridled market system, which added an unusual sense of invincibility among politicians, business, financial, and policy economists. Markets were seen as the answer to economic and social problems and orthodox protectionism in the post-WTO era was passé. The argument was that it was difficult to micromanage specific sectors in light of globalization, difficult to select national champions, and nearly impossible to wean vested interests that have become accustomed to state largesse in the form of subsidies. All of this was true. The economic development narratives were replete with stories of failed states, the exhaustion of import substitution industrialization, rent-seeking activities, and low economic growth. Furthermore, countries that allegedly pursued free markets and free trade policies were positioned better to grow rapidly and experience widespread social development. The high performing East Asian economies were exemplars of such virtuous change. Of course, this was a misreading of the development process. These countries did well because they avoided unproductive state intervention and not because they abandoned state activism; they exported not because of free trade policies but because of national concerns about balance of payments, benchmarking their competitiveness through aggressive exports. The story is thus nuanced: states remained active in these countries but they were reinventing their role by working with the market and seeking out global economic opportunities in a pragmatic fashion.

The common and mostly correct argument that economic performance in the first three decades of the founding of two of the world's largest countries, China and India, has been less than impressive was mainly due to unbridled state intervention. Notwithstanding their very different political systems, once the shackles of state ownership, rigid price controls, production regulations, and import tariffs were removed, both of these countries have taken off economically. This too is mostly correct. The 1978 reforms in China and the 1991 reforms in India have paved the way for high rates of economic growth and market deepening. However, aside from the thorny questions of determining when exactly higher growth rates began to occur and why, the story is largely—but still only partially—correct. Gradually freeing markets has been beneficial to both countries. But this popular view overlooks the fact that deregulation and liberalization have been engineered and orchestrated by the states themselves and at a pace that has been appropriate to particular political and institutional contexts. Governments in these countries continue to influence economic outcomes even though they have slowly, but not completely, moved out of direct production and removed many of the earlier policy instruments that regulated economic output and protected domestic business. Hence, though globalization has transformed the role of states, it has not eliminated the state in its pursuit of national economic interests. Instead, states have internalized global economic forces to the extent that they themselves are contributors to international economic integration.

In this volume, we address the basic question as to how Asian states today pursue economic nationalism: what do they do and how do they bolster their economies in the larger global system? Attention to this issue is prompted by two reasons: (1) Asian economies are dynamic and actively engaged with the world economy and thus presumed to be bereft of active states; and (2) most predictions indicate that they will constitute a new growth pole of the world economy. In this volume we undertake an inquiry into the nature of state activism under globalization in major Asian economies. As a region, Asia in the post-World War II period has quite solidly demonstrated the significance of the state's role in economic transformation. Today the region continues to be dynamic with new players such as China and India, whose penchant for state intervention is legendary, and who continue to use the state for national economic purposes.

Anthony P. D'Costa
Copenhagen
September 2011

Acknowledgements

The inspiration for this project came from an earlier paper, "Economic Nationalism in Motion: Steel, Auto and Software Industries in India" (D'Costa 2009),[1] where I argued that globalization has not made economic nationalism theoretically redundant or practically impossible. Rather, states have been active in carving out a role for national development as new opportunities and challenges emanated from the world economy, even as the coherence of their actions weakened due to their reinvented roles in working with the market. This paper was previously presented at the Asia Research Institute, National University of Singapore, and subsequently published as a working paper there. However, the paper itself was a product of a conference panel "Foreign Companies and Economic Nationalisms in the Third World," at the 2006 International Economic History Association Congress in Helsinki. I am grateful to Rory Miller of the University of Liverpool and co-editor of the *Journal of Latin American Studies* for inviting me and putting together a fine conference panel. But evidence from a single country such as India, analyzing only a handful of sectors, was clearly not adequate for an understanding of the continued role of the state in a highly integrated international economy. To broaden the scope and to capture the patterns and nuances of state intervention in promoting national interests in the twenty-first century, I organized a conference on "Globalization and Economic Nationalism in Asia" in Copenhagen in December 2009. This volume is a result of that conference. Most of the papers from the conference are included and two additional researchers were invited to contribute to the project.

The conference was financially supported by the Asia Research Centre at the Copenhagen Business School. Kjeld Erik Brødsgaard, Director of the center, wholeheartedly supported this project. Also, FUHU (the Danish Society for the Advancement of Business Education) and ØKs Almennyttige Fond (the East Asiatic Company Foundation) in Copenhagen co-sponsored the conference with financial contributions. I acknowledge the administrative support received from Niels Mygind, Head of the International Economics and Management Department, to pursue my scholarly engagement with India and Asia and for appreciating the intellectual and practical importance of the study of Asia in the department. Without their support it would not have been possible to organize the conference and invite scholars—both seasoned and upcoming—from the USA, Europe, India, Japan, and Australia. I am also grateful to the A.P. Møller-Mærsk Foundation for establishing an endowed professorship in Indian Studies, allowing me to pursue not just interesting intellectual questions about contemporary political economy of India, but also more generalized concerns about globalization and Asia's and China's place in the world economy today. I believe this is a good beginning to what I hope is a wide range of projects covering what is now a very dynamic part of the global economy.

At the Asia Research Centre, Bente Faurby, then Program Coordinator, organized and handled most of the logistical details of the conference. She was assisted by Koen Ruttan, now pursuing his Ph.D. at the London School of Economics. Janette Rawlings, also of the Asia Research Centre, generously provided invaluable editorial support. At Oxford University Press, it has been a pleasure to work with Adam Swallow, Commissioning Editor. We worked together on an earlier edited volume, *The New Economy in Development: Challenges and Opportunities,* when he was at the UN University's World Institute of Development Economics Research in Helsinki. Jenny Townshend and Aimee Wright at Oxford oversaw the finer details of bringing the project to completion. Three anonymous reviews helped greatly in the final shaping of this project.

I would like to thank Alan Irwin, Dean of Research at CBS, for giving me some time off from teaching to pursue several time-consuming editing projects. This is the second volume completed under his tenure. I also thank my colleagues at the Asia Research Centre who presented or served as officiating members at the conference, the invited participants, and a lively audience, representing faculty, students, and corporate executives. Alice Amsden of MIT, who passed away in early 2012, was aware of this project and left an intellectual imprint through her personal communications as well an incisive analysis of the role of the state in Asia and the "rise of the rest." Lastly, I deeply appreciate Ajit Singh's active participation in the conference as a keynote speaker and his willingness to write the Foreword to the book. A committed scholar and a true gentleman who shows no signs of slowing down, I believe he is also a great institutional bridge-builder between Copenhagen Business School and Cambridge University. None of the individuals or institutions bears any responsibility for any inadvertent errors or omissions.

Note

1. D'Costa, A.P. (2009). "Economic Nationalism in Motion: Steel, Auto, and Software Industries in India." *Review of International Political Economy*, 16 (4): 618–46.

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Alan Chong is Associate Professor at the S. Rajaratnam School of International Studies in Singapore. He has published widely on the notion of soft power and the role of ideas in constructing the international relations of Singapore and Asia. His publications have appeared in *The Pacific Review, International Relations of the Asia-Pacific, Asian Survey, East Asia: an International Quarterly, Journal of International Relations and Development, Review of International Studies*, and *Cambridge Review of International Affairs*. He is the author of *Foreign Policy in Global Information Space: Actualizing Soft Power* (Palgrave, 2007). He is currently working on several projects exploring the notion of "Asian international theory." His interest in soft power has also led to inquiry into the sociological and philosophical foundations of international communication. He is working on his next book entitled *The International Politics of Communication: Representing Community in a Globalizing World*. Professor Chong has been interviewed frequently in the Asian media and think tanks in the region.

Anthony P. D'Costa holds the Professorship in Indian Studies endowed by the A.P. Møller-Mærsk Foundation and serves as the Research Director of the Asia Research Centre, Department of International Economics and Management, Copenhagen Business School. Prior to this appointment in 2008 he was with the University of Washington for 18 years. As a political economist working with steel, auto, and IT sectors, he has written extensively on globalization, development, innovation, and industrial restructuring in India and other Asian countries. Of his eight books, his most recent are: *Transformation and Development: The Political Economy of Transition in India and China* (co-edited with Amiya Bagchi, forthcoming), A *New India? Critical Reflections in the Long Twentieth Century* (edited 2010), and *The New Asian Innovation Dynamics: China and India in Perspective* (co-edited with G. Parayil, 2009). He is currently working on his next book, *Global Capitalism and the Mobility of Technical Talent.* He has been a fellow of the Abe Program, Japan Foundation; American Institute of Indian Studies; Fulbright-Hays; Korea Foundation; Social Science Research Council, NY; and UN University's World Institute of Development Economics Research (WIDER) in Helsinki. He has also conducted commissioned projects for the ILO, World Bank, and WIDER. He served on the Board of Trustees of the American Institute of Indian Studies and currently serves on the International Advisory Board of India-US World Affairs Institute, Washington, DC, and the Nordic Centre in India.

Karl Gerth 's latest book is *As China Goes, So Goes the World: How Chinese Consumers are Transforming Everything*. After receiving his Ph.D. from Harvard in 2000, he taught at