US–Asia Economic Relations

A political economy of crisis and the rise of new business actors

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Preface and acknowledgements

There has been an unmistakable upward trend in the volume of foreign investment circulating in the global economy since the 1980s. These numbers, on their own, imply a broad-based acceptance of the merits of foreign investment across the world. However, the tense headlines that continue to this day on foreign acquisitions suggest that foreign investment remains a deeply politicized issue in most economies. Few countries match the liberal UK model of foreign takeovers, which a Manchester University academic summarized well: "if someone offers you a good price for anything, you sell it." One need only think of the corporate actors that have sparked alarmist reactions across a range of countries in recent years: Gazprom, private equity funds, sovereign wealth funds, Unocal, Wal-Mart and World Ports. While the cases change – earlier discussions singled out actors ranging from Exxon-Mobil to Japanese multinationals to global consumer brands Nestle and Nike to privatized European water utilities – a backlash against foreign investors has been a common theme in international economic relations.

This book critically evaluates two longstanding issues in the debate over foreign investment: the potential market opening opportunities afforded by financial and economic crises in developing markets and the perceived global pre-eminence of US capital, including in emerging markets. The thesis of the book is that only by disaggregating the US state and US capital, and moving beyond representations of tightly linked American power, can US economic behaviour be understood. The late 1990s and early 2000s highlighted several important features of America's relationship with Asia: the rise of investment banks, private equity houses and other new business actors, the restrained investments of traditional US multinational corporations and the relative autonomy, yet short-term commitment, of the US Treasury Department.

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Justin Robertson
Hong Kong
March 2008

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1 Introduction

Opportunism, resistance and divergent US economic interests in post-financial crisis Asia

Foreign economic behaviour in developing and emerging markets continues to be a contentious issue. Over the past decade, one of the central claims of neoliberal critics has been that American and other foreign actors have exploited periods of economic turbulence in the developing world. In economic crisis after economic crisis – from Mexico to Thailand to Turkey and beyond – American financial and economic power has been a central theme. This important and recurring international economic theme is the subject of closer scrutiny in this book. When the economies of developing countries falter, US actors often intervene, despite the reservations of some political elites.[1] American interventions include formal involvement in providing advice and funding in financial rescue packages, as well as the equally important market activities of US companies.

While American involvement in the management of financial crises is highly probable, this book contends that the rationality, coherence and impact which can be attributed to these US actions remains in dispute. On the one hand, numerous analysts have depicted American policy-makers and firms as dictating economic policy and assuming greater control of domestic economies in crisis settings (Bello 1998a; Bhagwati 1998; Cumings 1999; Gills 2000; Higgott 1998a; Johnson 2000; Wade 1998a; Weiss 1999). This approach can be referred to as the "strong American power" understanding of financial crises. On the other hand, a competing school of thought has maintained that the interests of foreign actors are blocked by resilient domestic political and economic institutions (Beeson 2002; Jayasuriya 2001; Lever-Tracy and Tracy 1999; Robison *et al.* 2000; Rodan *et al.* 2001a; Rosser 2003; Whitley 1999). This competing perspective can be labelled the "resistant domestic political economy" approach.

The primary objective of this book is to determine the extent to which crises in developing countries present opportunities for American actors to advance their interests, an issue of continuing relevance in a world fraught with the potential of financial instability. The book sets out to test US economic interests in developing economies through an analysis of the aftermath of one recent

1 As former US Treasury Secretary Robert Rubin correctly observed about the Bush Administration's desire to reduce involvement in international economic crises, "I said to myself: they say they won't interfere. But they will. And they did" (Rubin and Weisberg 2003: 297).

crisis – East Asia's financial crisis. It does so by establishing market opening in Asian countries and foreign direct investment (FDI) by American firms as indicators of US economic interests and examining developments in these issue areas in Korea and Thailand in the period after the crisis.[2] With a multi-year empirical record to serve as a testing ground, it is now possible to turn to a theoretically informed and methodologically rigorous assessment of the aftermath of the financial crises that swept emerging markets during the late 1990s and early 2000s, and hit Asia particularly hard. This issue continues to be important today with growing uncertainty about the fate of policy reform and foreign capital in the book's two case studies, Korea and Thailand, as well as in other key emerging markets, such as Russia and Venezuela. The analysis in this book demonstrates that models based on either commanding American power or impenetrable domestic politics do not accurately reflect the manner in which foreign and domestic forces interacted in post-crisis Asia. Instead, the concept of divergent US interests is advanced as a more suitable theoretical framework for studying crises and a more accurate empirical description of the crisis outcome in both Korea and Thailand, which featured the rise of new business actors and the absence of more conventional forms of US capital.

The puzzle to explain: an unanticipated outcome to the Asian crisis

After intensive prognostication on the role of the US in the Asian financial crisis, the subsequent years witnessed some surprising developments. When public and private sectors in Asia underwent major change, American actors stepped in as key advisors. Beyond this specialized advisory role, however, US companies did not aggressively invest capital in the Asian region as was widely anticipated. When Asian economies opened further to international capital after the crisis, European, Singaporean and Japanese firms stepped forward as the leading foreign investors. Taking these parallel trends into account, the central finding of this study is that US economic interests have diverged in Asia since the crisis.

This unforeseen outcome can be sketched out in matrix form (Table 1.1). Based on the relationship between the indicators of Asian market opening and US FDI, there were four possible outcomes for US economic interests after the Asian crisis. The findings of this book can be categorized in the bottom-left corner, denoting that important market reforms took place, albeit with only limited US firm penetration. The two dominant positions conceptualized the crisis outcome in either the top-left corner (significant openings to foreigners and widespread US firm penetration) or the bottom-right corner (insignificant openings to foreigners and minimal US firm penetration).

The outcome of the Asian crisis points to a divide between new types of US

2 The Republic of Korea, or South Korea, is referred to as "Korea" throughout this book.

Table 1.1 US interests after emerging market crises: possible outcomes and differing perspectives

	Significant market opening in emerging markets	*Insignificant market opening in emerging markets*
Widespread US firm penetration	Strong American power interpretation	US firms oppose market reform interpretation
Minimal US firm penetration	Divergent US interests interpretation	Resistant domestic political economy interpretation

actors that provide consultancy services to domestic actors undergoing restructuring, as well as investing capital in non-traditional ways, and mainstream US investors that are less commercially involved. The first category includes advisory firms, investment banks, private equity funds and a more conventional actor, the US Treasury Department, whereas the second category is comprised of flagship US multinational companies and banks.

The disjuncture between the push for liberalized markets by some US actors and the relatively limited engagement of US firms through FDI forms the central research problem of the book. This puzzle raises two important questions:

- Why did US firms invest only small amounts of FDI in Asia, despite considerable market opening?
- What explains the much larger presence of US public and private institutions working on market reform issues in Asia?

To explain the different approaches taken by US actors in response to Asia's economic downturn, the book develops a theoretical framework named "divergent US interests." The central theoretical point is that there are divergent interests at play after crises, which result from the range of American public and private actors with differing international agendas and operations. In the first instance, the argument is that cautious post-crisis American FDI is more a function of the narrow range of US firms interested in Asia than a function of either the exercise of American political power or the obstacles presented by domestic political factors. Even if the US state presses for emerging market openings, US firms may not follow the state's lead. In other words, market opening processes in the developing world do not always correspond neatly with the strategies of US business. In the second instance, US market access pressures are argued to be driven by the ideological positions of government officials and the profit-maximizing behaviour of consultants in the US private sector rather than by a captured state acting on behalf of aggressive US companies.

This analytic framework brings US firm behaviour to the fore and argues that it must be incorporated into any comprehensive explanation of developments in East Asia during the last decade. In most respects, analyses of the Asian crisis either inadequately theorized or neglected the American firm as an actor – and yet US firms possess distinct attributes in the international and Asian economies, attributes which played a significant part in determining American reactions to the changed regional conditions. The larger point is that while foreign actors undoubtedly gain leverage in countries experiencing a crisis, and while American power is clearly mobilized, much closer attention needs to be paid to the exact form of US engagement.

America's economic relationship with Asia has been undergoing a reorientation in the 1990s and 2000s, and Asia's experience with crisis points to some emerging features of US capital in the world economy. The profile of US business in Asia has changed through the rise of new business actors, including advisory firms, investment banks and private equity funds, as well as the development of new business models, such as outsourcing and specialized services. The economic face of the US in Asia is no longer blue-chip industrial companies. It is American bankers facilitating mergers and acquisitions (M&A), American private equity funds scouring Asian markets for buy-outs and contract manufacturers managing the supply chains of US companies. These are some of the major developments that are presented in the book's seven core chapters.

To begin, the introduction surveys the broader context of economic and financial crises in the international economy and the debates over foreign opportunism and domestic resistance that follow in their wake. Next, the research problem, analytic framework and methodology are outlined. After drawing out the limitations of the leading approaches, the chapter proceeds to a discussion of the empirical findings on the consequences of the Asian crisis for American economic and financial interests.

Patterns in the study of emerging market crises

The role of foreign actors in responding to international economic crises has been the focus of a lengthy discussion, with American opportunism one of the first chords usually struck by both local and international critics. In this view, US actors initiate, guide and ultimately benefit from the economic liberalization of crisis-prone countries. While American opportunism tends to be one of the immediate reactions to foreign interventions, another school of thought asserts that local forces are able to resist international pressures. In this argument, crises do not necessarily force open trade and investment markets and bring changes to local business practices. Rather, domestic political and corporate elites slow the pace of reform and stall sales of domestic assets to foreigners. Whether or not these two ideal types capture the relationship between foreign and domestic forces after emerging market crises is one of the central themes of this book.

Several illustrative examples of opportunism and domestic resistance in earlier financial crises can be cited. During the Latin American crisis of the 1980s, the US government demanded that Mexico sell oil to the US at below market prices in order to receive a bailout (Lustig 1997) and Citibank turned debt from Argentina into substantial profits (*FEER* 1999). In the aftermath of Mexico's 1995 crisis, acquisitions placed outsiders in control of over 80 per cent of the country's banking assets[3] and Brazil's economic problems during the mid-1990s, according to some critical scholars (Petras and Veltmeyer 2003) induced a "recolonization" process with foreign firms establishing dominance over mining, power, services and telecommunications. General Electric (GE) is a prime example of an American firm making acquisitions during periods of crisis. GE acted aggressively in the US savings and loans crisis of the late 1980s, the European recession of the early 1990s and the Asian crisis of the late 1990s (Lowe 2001).

Occasionally, the reverse even holds true and economic crisis in the US is linked to foreign encroachment. The anxiety sparked by Japanese investments in a declining US economy during the 1980s speaks to the intensely political nature of foreign investment, whether in developing or industrialized markets. Charting a possible future scenario, a provocative and widely read article foresees an oncoming American economic crash in which foreign companies like Toyota take advantage of a precipitous decline in the value of the US dollar and stock market to take over blue-chip US companies at bargain prices (Fallows 2005).

The resistant domestic political economy tradition, by contrast, holds up the socio-political structures of developing countries as sufficiently complex to temper outside pressures, even during periods of severe economic distress. It rejects the logic of overwhelming foreign dominance. For example, Russia's privatization process benefited not foreign investors but rather a small number of domestic oligarchs (Gould-Davies and Woods 1999) because divesting state-owned firms to foreign investors was "a politically difficult path to follow" (Rutland 1999: 191). In Indonesia, the sale of companies that the Indonesian government took over during its $60 billion assumption of business assets following the Asian crisis virtually ceased due to the opposition of entrenched domestic interests and a power struggle over the government agency in question (Robison 2003). Foreigners even shied away from making bids for well-operated Indonesian enterprises that were available and that should have attracted interest.[4]

This book's point of departure is dissatisfaction with the perennial cycle of opportunistic interpretations of emerging market crises followed by competing interpretations at the domestic political level. Not only is this pairing of approaches limiting, but neither approach has received anywhere near sufficient empirical testing to be considered a well-formed research programme. Market turbulence understandably prompts a certain amount of conjecture on future growth and development trajectories. However, when these assessments of economic change in developing societies and the significance of American influence should be receiving attention after crises, fatigue with the further study of crises

3 US acquisitions proved particularly profitable. For example, Citibank's Mexican acquisition, Banamex, generated a profit of nearly $1.5 billion alone in 2003 (*WSJ* 2004).

4 Assessing the prospects for Lippo Bank, a banker noted "it's a good bank ... but no one has ever made money by partnering up with the Riadys" (*FT* 2003a: 32). The Riadys are the former owners who maintain minority shareholdings.

sets in.[5] Yet if one is interested in the consequences of a crisis, then it is only possible to do so with the data and perspective afforded by hindsight. Should we heed the stark warnings of either American hegemony or stubborn domestic resistance following economic crises in the developing world? Empirical tests covering several years of post-crisis developments allow us to make a better judgement as to whether US interests act opportunistically when faced with international financial instability. This book is one of the first to systematically examine how US business and the US government reacted to Asia's economic vulnerability in the wake of the regional crisis.

Opportunism and resistance after the Asian financial crisis

Developing Asia, which I define as those East Asian economies other than Hong Kong, Japan, Singapore and Taiwan, clearly presents itself for an analysis of foreign economic behaviour in crisis settings. The freefall experienced by several Asian economies started in July 1997 when the government of Thailand allowed its currency to float freely. Over the next two years, currency values plummeted in several Asian economies and the viability of large numbers of domestic firms, even the best managed ones, was jeopardized. An international bailout ten times larger than that necessitated by the 1980s US savings and loans crisis was put in place.

Themes of foreign power and domestic politics were prominent throughout the crisis period. While a debate raged over whether domestic crony capitalism or herd-like international investors sparked the Asian crisis, an equally contested issue pitted those who foresaw Asian countries succumbing to Western economic and commercial interests against those who believed these societies would resist this incursion. The debates over both the causes and consequences of the Asian crisis took place at competing levels of analysis with opportunism informing many international-level arguments and resistance framing many domestic-level arguments.

Those envisaging internationally-driven change in Asia believed that the crisis would be used as a vehicle to impose Western worldviews on trade, finance and even democracy.[6] A focal point was the perception that American actors took advantage of the crisis. Various American-led consortia were said to

5 Economists, however, deserve some credit for their continued interest in lessons from financial crises and possible changes that could be made to the international financial architecture. Two recent projects assessing the lessons to be drawn from financial crises are exceptions in Political Science. Oxford University's Pathways from Crisis project gathered a group of senior officials from emerging markets to reflect on their experiences in responding to financial crises. The "L20: Bridging the Gaps in Global Governance" project, sponsored by the Centre for International Governance Innovation, has identified financial crises as one of seven key global governance issues for which new ideas and mechanisms are needed.

6 IMF head Camdessus called democracy one of the key crisis outcomes (2000: 38) and US Secretary of State Albright expressed hope that the crisis would prompt democratic change in Indonesia (US Official in Asia anonymous interview).

be directing crisis management, from a "Wall Street-U.S. Treasury complex" (Bhagwati 1998) to a broader "Wall Street-U.S. Treasury-U.S. Congress-City of London-U.K. Treasury-IMF complex" (Wade 1998a: 1546). IMF policy, in this interpretation, was "manipulated by its principal and strongest stakeholder, the United States, to push trade and investment reforms that would principally benefit U.S. economic interests" (Bello 1999: 138). Global consultants advised that the conditions were opportune for deal-making in Asia (BCG 1998).[7] Top newspapers repeatedly touted fire sales of assets to American buyers.[8] Wade (1998a: 1547) went as far as to predict that the Asian crisis would prompt the largest transfer of assets from domestic owners to foreign owners – particularly American – in recent world history. The American firm was widely depicted as a vulture investor about to descend on Asia.

As the crisis deepened, numerous analysts pointed out that developing Asian countries would resist international pressure because of the resilience of their domestic political and economic systems. This analysis embraced a range of arguments that show how international pressures are mediated by domestic systems with well-defined elite and institutional structures. Domestic politics, it was argued, led many regimes to abandon IMF policy prescriptions shortly after the crisis and materialized in Asian governments that were unwilling to sell prime assets to foreign investors. In Thailand, some saw the crisis as a turning point, in which Thais felt threatened by global capital,[9] an attitude that had been absent during the earlier boom years (Baker interview, Bangkok). Given these sites of resistance, one journalist noted of Thailand that "for all the talk of reform, the same families and groups still dominate the economy" (*Asiamoney* 1999: 25). In Korea, Deutsche Bank, Ford and HSBC were "among those who have tried and failed to take control of South Korean companies, wasting millions of dollars … in the process" (*FT* 2002a).[10]

The Asian crisis is consistent with the general pattern in the study of financial crises whereby opportunism is the first dominant theme. A vigorous response

7 McKinsey consultants predicted that close to half of Asia's banks would change hands in the 1999–2001 period (*Asian WSJ* 1999b). A survey by Andersen Consulting found leading multinational companies preparing for expansion in developing Asian markets (*Sydney Morning Herald* 1999).

8 Representative headlines included "Some Companies Jump into Asia's Fire Sale with Both Feet" (*Chicago Tribune* 1998), "Some U.S. Companies See Fire Sale in South Korean Crisis" (*LA Times* 1998), "While Some Count Their Losses in Asia, Coca-Cola's Chairman Sees Opportunity" (*WSJ* 1998a), "Investing in South Korea: Bargains Galore" (*The Economist* 1998a) and "Going Cheap" (*The Economist* 1998b).

9 When a large Thai company, Thai Petrochemical Industry, resisted bankruptcy proceedings, "99 per cent of Thais believed that foreign banks were unjustly taking away a Thai person's assets" (Stotz interview, Bangkok).

10 Other examples of media stories that cautioned that Asian reform and sales to foreigners risked being stalled included "Asian Rebound Derails Reform as Many Suffer" (*NY Times* 1999a), "Asia's Dangerous Reform Slowdown" (*Asian WSJ* 1999a) and "As Asian Reforms Go Into Eclipse, Growth Outlook Darkens" (*IHT* 2001b).

based on the strength of domestic structures follows. And then, once recovery starts to take hold, the status of foreign economic interests tends to fade from scholarly and wider public consciousness, even though the debate remains unresolved. While there are a handful of valuable retrospective works on the post-crisis record on economic reform (Beeson 2002; Haggard *et al.* 2003; IMF 1999, 2001; Independent Evaluation Office 2003), there is little corresponding research on foreign firm penetration.[11] In particular, no study has adequately addressed the scope of American involvement in post-crisis Asia. Did US economic actors benefit from the Asian crisis and, if so, to which specific US interests did gains flow? The analysis in this book is one step toward answering this question.

A methodology to examine post-crisis developments

In order to ascertain the nature of American participation in Asia following the crisis, the book establishes two indicators of US economic interests: market opening and US firm penetration. Market opening is defined as changes that facilitate the entry of foreign business and includes liberalization of the financial, investment and trade regimes, deregulation of business laws, privatization and upgrading of the regulatory framework surrounding issues such as bankruptcy and competition. US firm penetration is defined as the inflow of FDI from American multinational corporations.[12] FDI occurs when foreign companies assume a significant ownership stake in a business in another country.[13] The book assesses these indicators for the five-and-a-half years that followed the crisis outbreak in July 1997 in an empirically rigorous manner using a range of research sources, including data on foreign business activity and elite interviews.

Market opening and foreign investment in developing Asia are strong indicators of US interests in their own right, but it is their interaction that lies at the heart of much scholarly work on economic restructuring in developing

11 Several important collections are in press resulting from conferences revisiting the Asian financial crisis – hosted by the Asian Development Bank, the Australian National University, the Federal Reserve Bank of San Francisco and the Institute of Development Studies – but the research focus again is largely on processes of domestic and international economic reform rather than on the foreign firm as an actor.

12 Foreign firms operating internationally are classified according to their home nationality. As seen in the aftermath of the Asian crisis, and as discussed throughout the book (see especially Chapters 3, 6 and 7), firms continue to behave differently in the international economy according to their country and region of origin. In political economy terms, foreign firms compete against each other and governments still largely consider their nationally-owned corporations as key engines of national growth.

13 The US government defines FDI as "investment in which a resident of one country obtains a lasting interest in, and a degree of influence over the management of, a business enterprise in another country" (BEA 1995: 1). To be classified as a direct investment, a US investor must own at least 10 per cent of a foreign business enterprise. This definition excludes portfolio investment. As Lavelle (2004: 127) notes, "foreign institutional holdings are passive by their nature as broadly diversified portfolio investment."

countries. The key issue is whether US actors use crises to force open developing economies to foreign investment and whether US firms, in turn, advance their business positions in the wake of crises. The liberalization and deregulation of emerging markets is framed as either facilitating foreign investment, or, if thwarted, as limiting it. In the case of the Asian crisis, analysts informed by the rival perspectives of American power and domestic politics disagreed as to whether market reform would be significant and based on this outcome, whether American firms would be able to increase their investments in Asian markets.

FDI is the principal focus of analysis. When financial crisis enveloped parts of Asia in the late 1990s, FDI markets in the region were relatively more closed to foreigners than trade markets and, therefore, of more strategic interest to American policy-makers and the US business community. Historically, US firms have traded more with East Asia than using the region as an investment host (Urata 2003) and since the 1980s Asian countries have undertaken significant trade liberalization through the World Trade Organization (WTO) and Asia-Pacific Economic Cooperation (APEC) processes. In comparison, making foreign investments in certain sectors, and merging with and acquiring local companies, proved more difficult for international firms. Not surprisingly, then, the agreements signed between Korea and Thailand and the IMF devoted more attention to international investment issues than to international trade issues. In fact, other than an occasional paragraph stating a commitment to trade liberalization in the case of Korea, there were no practical steps taken on trade reform – Thailand did not even make a reference to trade policy in its IMF submissions. Liberalizing the foreign investment regime, on the other hand, joined financial, fiscal and macroeconomic policies at the heart of the IMF agreements with these two countries.

Finding direct evidence of foreign influence on the economic policies of developing countries is a difficult research task. Even an "insider" admits that it was impossible to determine whether IMF staff or the IMF's Executive Board played the critical role in the IMF's Asian crisis response (Stiglitz 2000).[14] The journalist Blustein (2001) made one useful contribution with his thorough investigation of US influence during the crisis, offering significantly more examples than those offered in the critical strand of literature. Unfortunately, Blustein's analysis stopped at the end of 1998 and his research was primarily restricted to state actors.

While the motives and actions of the US state in its initial crisis management policy are important, such an analysis needs to be balanced by an assessment of how other US actors behave over the longer course of a crisis and its aftermath. More to the point, even if American firms can be linked to some form of foreign

14 Another person closely involved in international discussions on responding to the crisis noted, "Korea made a very bold move in comprehensively opening its capital account, after which US financial services providers benefited. But was the US advice to the Korean government on capital account opening coloured by commercial interests? It's hard to tell" (Fisher interview, Washington).