

[Book review] "Rethinking the East Asian Miracle edited by Joseph E. Stiglitz and Shahid Yusuf"

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Despite these questions and inadequacies, the book is a highly valuable publication for the following four reasons.

Firstly, through their in-depth analyses of the beef industry's multi-tiered structure, even of the lower levels that are indiscernible from the publicly available data and published information, the authors have succeeded in presenting a thorough and wide-ranging examination of the industry.

Secondly, the authors' analytical framework for examining the beef industry, as well as other industrial sectors and the Chinese economy as a whole, is consistent throughout the book.

Thirdly, the available materials and records have been perused and utilized with scholarly care and faithfulness. There are two approaches in China studies. One is to study of the country by first delving into one discipline and then proceeding to other areas. The other is to start by learning to read Chinese and then studying China as an area study. The former approach is apt to make mistakes in comprehending the flow and interplay of China's many phenomena, because its study is limited to a specific area. The latter cannot go sufficiently deep into a specific area. For instance, the chart in Figure 10.1 (p. 209) showing each of the usable components of a typical cow and their weights (kilograms) cannot be prepared without knowledge of animal husbandry. The authors have had many opportunities of professional access to Chinese literature, and are well versed in the progress of the country's economic policy and promulgated ordinances. The reviewer, as a follower of the latter approach, has found few errors in the use of materials and interpretation of historical facts.

Fourthly, the figures and tables in each chapter are well prepared and laid out which greatly help the reader grasp the theme of the chapter. The boxes inserted from time to time also help clarify the flow of the text. The way appendixes are presented indicates the author's consideration for the reader's convenience. While noting that the market's draught power for boosting China's beef industry is still feeble, the book has been compiled with due consideration for the readership market. All these points make this book one of the superb analytical works on a vital Chinese industry. (Reeitsu Kojima)

Rethinking the East Asian Miracle edited by Joseph E. Stiglitz and Shahid Yusuf, New York, Oxford University Press for the World Bank, 2001, x + 526 pp.

The best way to begin a review of this book, *Rethinking the East Asian Miracle*, is by comparing it with its predecessor, *The East Asian Miracle*, published in 1993, also by the World Bank. As is well known, *The East Asian Miracle* verified the effectiveness of industrial policy. The volume's conclusions were threefold. First, industrial policy was effective in countries with competent bureaucrats, such as Japan and the Republic of Korea, and contributed to their economic growth, but such policy is not always effective in developing countries which lack such bureaucrats. Second, the export-led growth measures adopted by East Asian countries can be applied effectively to developing countries in other regions.

Third, low-interest finance policy (direct credit) is effective in some cases but not in others. However, these were provisional conclusions reached during an extended period of East Asian economic prosperity. During that time China got onto the path of high economic growth propelled by foreign capital introduced in the early 1990s. The country also showed a positive attitude toward industrial policy and in 1994 announced the outline of its industrial policy and a program to promote the automobile industry. Most East Asian countries were promoting export-led growth policies which started in Thailand and Malaysia in the 1980s and spread to Indonesia and the Philippines in the 1990s.

The outbreak of the Asian currency crisis in 1997, however, cast serious doubt on the conclusions in *The East Asian Miracle*. China, which had been considering the introduction of industrial policy like that adopted by Japan and Korea, abandoned the idea of protecting and nurturing its industries and switched to a policy of reinforcing the international competitiveness of its enterprises. To achieve this purpose, China did not hesitate to expose its industries to international competition by joining the World Trade Organization (WTO) in 2001. Behind this step was doubt about the role that government could play in economic growth.

In the aftermath of the Asian currency crisis, Shahid Yusuf and Joseph E. Stiglitz edited *Rethinking the East Asian Miracle*, a collection of thirteen contributions, in order to reexamine the effectiveness of industrial and export-led policies. In Chapter 1 Yusuf summarizes his conclusion that it is not advisable for developing countries to adopt industrial policies. Interestingly, however, in the last chapter Stiglitz supports the industrial policies pursued by Asian countries. As far as the reviewer knows, this view is still supported by some of the World Bank's staff including its Asian researchers. Of the various themes examined in this volume, this reviewer will focus on its analysis of industrial and the export-led policies.

Industrial Policy

In their respective analyses of China and Japan, Yingyi Qian (Chapter 7) and Tetsuji Okazaki (Chapter 8) argue that government control was effective at a certain stage of economic development. Qian maintains that China's experience shows the need for government control of corporate governance if only transitionally. According to him, government control of corporate governance in China evolved in two stages: from 1979 to 1993 and from 1994 onwards. During the first stage, the government intensified its corporate control and provided positive guidance. Control of firms by local governments made particular contribution to economic development. During the second stage, however, private ownership and a relatively active market economy evolved, making government control of firms less effective. Government control at the first stage was necessary because the country suffered from such factors as lack of the rule of law in securing property rights, lack of a functioning capital market, and lack of adequate taxation and fiscal institutions. With the correction of these shortcomings, however, government control began to lose its rationale. The problem was that government control could not be discontinued immediately when it became unnecessary. Nevertheless, Qian argues that the switchover was carried out rather smoothly with few obstructions from local governments, primarily because of the flexibility of China's institutional structure.

Is the China's example applicable to other countries? Many economists think not because it is difficult for an economy without competent bureaucrats to have such a flexible institutional structure. So the World Bank has been recommending that developing countries do not introduce industrial policy since the risk of failure is too great. However, the reviewer thinks that industrial policies that are modernized and modified to be workable in the context of globalization can be applied to countries such as Vietnam which has a competent bureaucracy. This new version of growth policy, which the reviewer calls the "Asian EPZ (export processing zones) model," will be explained later in this review.

Okazaki analyzes several cases of the success and failure of Japan's "bureau pluralism" in postwar relationships between the government and firms. Bureau pluralism is an institutional notion that includes governmental deliberative councils. It proved successful during Japan's rapid economic growth period but failed in later years. In a bureau-pluralistic nation, common interests of the private sector are siphoned to the business associations of each industrial field, and these associations, as representatives of the private sector, negotiate issues with the respective bureaucrats in charge of different industrial sectors. The bureaucrats attempt to coordinate the government's conflicting interests with the private sector first through intraministerial and then interministerial negotiations. This system is pluralistic in the sense that the people participate in policymaking and that bureaucrats represent the interests of the people. The bureau pluralism system worked effectively in adjusting various economic interests during the high economic growth period of the 1950s and 1960s. In subsequent years, however, it began to lose the ability to coordinate conflicting interests. *The East Asian Miracle* had also noted that Japan's deliberative councils were effective in adjusting the views between industries and the government. Finally, Okazaki points out that the stagnation of the Japanese economy in the 1990s was caused by the fact that the postwar system including this bureau pluralism continued longer than it should have. He analyzes this fact using dynamic game theory. In the reviewer's view also, Japan's experience seems to demonstrate that any system built up on successes tends to die hard. Indeed, even after entering the twenty-first century, Japan still has not extracted itself from the postwar system, threatening to spoil the efforts of the reform-minded Prime Minister Junichiro Koizumi.

In contrast to Qian and Okazaki, Perkins (Chapter 6) and Woo-Cumings (Chapter 9) advocate the reduction of the government role in economic development. Based on an analysis of industrial and fiscal policy in China and Vietnam, Perkins stresses the need for a new model that suits the present situation based on the East Asian experience. He proposes further economic deregulation in China and Vietnam by slashing government intervention, transforming state-owned enterprises into fully autonomous firms, prohibiting the government from choosing corporate managers, and establishing a modern banking system. For Vietnam, in particular, developing private enterprises is the key to its economic growth. Finally, Perkins emphasizes that the government should not only establish merger and acquisition (M&A) rules but also encourage M&A. As the author points out, in the process of shifting from a planned to a market economy, both China and Vietnam are consuming a great deal of time trying to reform state-owned enterprises in the case of China, and state-run enterprises in the case of Vietnam. In this connection, the reviewer would like to mention that his own research found that China has implemented reforms through trial and error

far more frequently than has Vietnam. The three-year program to reform enterprises implemented by Premier Zhu Rongji ended in 2001. The program's numerical target was reached, but apparently some reforms remain to be implemented. The government needs to further deregulate its controls.

Woo-Cumings analyzes the industrial policy of the Korean government and its policy to reform the corporate sector. He makes two conclusions. First, he finds in some East Asian countries that there is no causal relationship between industrial policy and their economic growth. He also confirms that their infant-industry promotion policy was not effective. Second, in Korea the government began to adopt in the 1970s various support measures to protect the advantages of the *chaebols*, Korea's big business groups, but these measures did not enhance the firms' international competitiveness. As a result, the government abandoned its *chaebol* support measures in the 1990s and switched to a laissez-faire policy which exposed those business groups to market forces. However, the author maintains that the bureaucracy seems to have regained its authority after the currency crisis of 1997. In this light, the author foresees the future of Korea as a democratic but strongly bureaucratic country. A good example of this was the government's support of the IT industry after the currency crisis. Because of this strong bureaucratic intervention, the IT industry experienced remarkable growth and became the engine for the recovery of the Korean economy.

The foregoing studies lend no positive support for industrial policy. The Japanese economy has been stagnant since the 1990s, while other Asian countries went through the currency crisis of 1997. Given these negative circumstances, the reviewer finds Stiglitz (Chapter 13) as the only contributor to this volume who sees East Asia's experiences in a positive light. Incidentally, the reviewer was assigned to the office of a chief economist at the World Bank in March 2000, when Stiglitz was a chief economist there. Contrary to my expectation, I had little chance to meet him because he resigned from the World Bank in June. It was about a year later that he won the Nobel Prize in economics. The originality of his analysis of imperfect markets is evident in Chapter 13 of this volume. Below I would like to review his positive evaluation of the role of government in economic growth.

Stiglitz argues that the government's role has been decisive for the East Asian economies, which are far from being fully competitive economies and where the government intervenes even in deciding wage levels. He focuses on three areas. First, the government's behavior has been the key to overcoming the problem of savings. This is because, in the short term, there could be multiple levels of equilibrium in the economy, and any attempt to shift the economy from low growth equilibrium to high growth equilibrium needed the government's push. Second, in the area of financing, in many East Asian countries it was the government which financed the founding of financial institutions such as banks. Third, the expanding liberalization of banking has increased financial risks which were clearly evident in the currency crises in Europe, Mexico, Asia, Russia, and Brazil in the 1990s. Stiglitz argues that the role for the government in such crises deserves greater attention.

Stiglitz's refutation of the criticism of Asian crony capitalism is also interesting. He contends that the occurrence of corruption out of mutual help among friends is seen not only in Asia but also in the United States, and asserts that no society is free from corruption. He cites the case of LTCM (Long-Term Capital Management), a financial institution that failed in the 1990s after investing in derivatives, and the U.S. government immediately covered its

deficit. This example may remind the readers of the Enron case in 2002, which revealed that crony capitalism exists in the United States.

Stiglitz gives a positive evaluation of the role of industrial policy in East Asian economic growth for three reasons. (1) Exports were promoted through the government's financing of direct credit. (2) It was advisable for the government to provide technology and know-how because these are related by nature to externalities and public goods. (3) In fostering small and medium-sized enterprises and specific sectors, the government in many cases successfully implemented industrial policy through intervention in financial markets. The reviewer knows few other authors who have expressed such a favorable opinion of industrial policy since the Asian currency crisis. In this regard, Yusuf (Chapter 1) remarks that we should not forget the problem posed by Stiglitz, which in essence is the question of whether the East Asian countries could have achieved better economic development than they actually did without industrial policies.

In summarizing the analyses in this volume, however, Yusuf notes that industrial policy became less effective in the 1990s. Based on Jomo (Chapter 12), Woo-Cumings (Chapter 9), and Lin and Yao (Chapter 4) as well as many studies made during the 1990s, and his own research, Yusuf ascribes this declining effectiveness to the progressive deregulation in Asia during the 1990s. For instance, he maintains that direct credit to Korean *chaebols* has gradually decreased, and that in Thailand and Indonesia such credit has created economic inefficiency. He also notes that export subsidies have failed to contribute to economic growth in Thailand and Indonesia, and he points out that economic liberalization implemented in China has led to high economic growth. As the reviewer has already mentioned, this view is prevalent in present-day academic circles.

Export-Led Growth

The conclusions by Lawrence and Weinstein (Chapter 10) regarding trade and economic growth are interesting. It has generally been considered that export-led growth has been important for the East Asian economies. However, these two researchers show that export-led policy has not actually contributed to economic growth. They show further that the removal of tariffs protecting domestic industry enhanced Japan's high economic growth between 1964 and 1973, and that increased imports helped strengthen domestic corporate competitiveness. In other words, they argue that East Asia's high economic growth can be explained by an import-oriented, rather than export-oriented, policy. This is an interesting view, but the reviewer is not convinced by their argument. He still supports the generally held view that Japan followed an export-oriented policy in the 1960s which is relatively compatible with the statistical evidence as well as with his personal experiences during that decade. Lawrence and Weinstein's conclusion remains to be judged by further examination.

Jomo (Chapter 12) argues that Southeast Asian economies have grown using an approach different from that followed by Japan, Korea, or Taiwan. The former have relied on export-led growth financed by foreign capital. According to Jomo, government intervention has been applied only in some specific areas such as trade, finance, human resources, technology, and international marketing. As he explains, concerning trade under an imperfect market environment, "it may be socially beneficial for the state to impose export targets in return for temporary protection in the domestic market" (p. 485). He goes on to add that: in

finance the state underwrites long-term investment; in human resources the government plays a major role in providing technical and vocational training as well as relevant secondary and tertiary education; and in technology and marketing the state should pay some of the costs for obtaining and sharing information on technology and international marketing.

Urata (Chapter 11) points out the role of foreign capital and trade. Using statistical analysis he focused on the formation of regional production networks by multinational corporations, and made the following three observations. First, East Asian foreign trade and foreign direct investment expanded rapidly in the 1980s and 1990s thanks to unilateral liberalization. Second, during this period East Asian international economic interdependence increased through trade and direct investment. Third, multinational corporations helped build up a regional production network in East Asia. Urata argues that this growth pattern is clearly different from the industrial policy adopted by Korea in the 1970s and by Japan in the 1950s. The reviewer concurs with Urata's findings. The reviewer calls this growth pattern which has depended on multinational corporations the "Asian EPZ model." He will explain this model in the next section.

Overview

The main issues in this volume are how to evaluate industrial policy and what challenges lie ahead for export-led growth. Discussions of these issues need to be based on the following three points. First, when evaluating industrial policy, changes in the environment of the world economy need to be taken into account. The tariff policy that Japan adopted immediately after World War II to protect its domestic industries from foreign competition was viable in the 1950s. However, for developing countries today, globalization has progressed rapidly since the 1980s, and the WTO has been demanding deregulation of their international trade and investment. At the same time, international organizations, such as the IMF and World Bank, have also been prodding developing countries to liberalize their trade and investment. These circumstances have made it difficult for enterprises in the developing countries, which had been protected by subsidies, to become adequately competitive against multinational corporations. Meanwhile governments are finding that they can no longer afford subsidies. Consequently, most developing countries find the type of industrial policy employed by Japan in the immediate postwar years virtually impossible to adopt. In this sense, Stiglitz's view (Chapter 13) sounds unconvincing for the 2000s.

Second, the reviewer believes that Korea's industrial policy in the 1970s and China's in the 1990s should be assessed differently from that adopted by Japan. Korea's industrial policy was implemented by introducing foreign technology and foreign parts and components. Under China's industrial policy, domestic enterprises are learning management from multinationals by accepting their equity participation. For instance, China has adopted a policy to foster its car industry by selecting priority enterprises which have tied up with two foreign multinational corporations to learn their way of management. In the reviewer's opinion, this is an industrial policy for coping with globalization. This is how China has modified its industrial policy in response to changes in the world economy. Another example of this is the policy adopted in 2002 to merge its big carmakers. Malaysia has also been following a policy to maintain its own national car development project. All this suggests that industrial policy has not been entirely rejected by East Asian countries, even with the intro-

duction of foreign management, capital, and other free market concepts.

Third, the reviewer believes that there are still some lessons to be learned from Japan's experience and those of other East Asian countries. Admittedly there have been more than a few opinions, even at the World Bank (when the reviewer was with that bank in 2001), contending that there is little to learn from the East Asian experience. These people point out how China has shifted in recent years to a policy of strengthening its international competitiveness in accordance with the WTO; they point to the plight of Korean financial groups in the wake of the Asian currency crisis, and to the disarray of the Indonesian economy. However, a couple of factors, which I would like to discuss below, suggest that the East Asian experience still offers some lessons for other developing countries.

The reviewer is particularly interested in two factors described in this book. First is the economic growth that was achieved through trade and foreign direct investment in what the reviewer calls the "Asian EPZ model." Second is, as Jomo points out, the significant role played by overseas Chinese. These factors deserve special attention because they point to the need for a more thorough analysis of the East Asian experience beyond the framework given in this book. More specifically, the questions are: when promoting growth through trade and foreign direct investment, what measures should a government adopt, and who should be the active players in the development process? On these questions, the reviewer would like to mention the vital role played by the EPZs. East Asian countries invited foreign investment to these zones between the late 1980s and late 1990s. The success of the EPZs can be attributed to their well-constructed infrastructure and their tax incentives to foreign companies. A notable point regarding the players is the fact that Japan's trading firms (*sōgō shōsha*) paved the way for Japanese companies to advance into ASEAN by constructing infrastructure in industrial zones and arranging local conditions to receive Japanese investors. This reminds us of the way overseas Chinese's companies have played an important role in advancing into Asian countries including China.

Rethinking the East Asian Miracle presents a tentative conclusion as to whether or not industrial policy is effective. As this is not a final conclusion, further studies on the East Asian economies as well as the players will help make the Asian experience more applicable to other developing countries. This suggests that the present volume, which is itself a sequel, will lead to yet another sequel.

(Akifumi Kuchiki)