'THE STATE IS DEAD' – OH NO IT ISN'T!

That was then; this is now

'State denial'[1] has formed a central claim of the 'hyper-globalizers' (and many social scientists) over the past 40 years: that we live in a borderless world where states no longer matter. A combination of the revolutionary technologies of transportation and communications (see Chapter 4) and the increasing power of TNCs (see Chapter 5) has, it was argued, shifted economic power out of the control of nation-states to 'the market'. 'Market fundamentalism' – a neo-liberal agenda urging the reduction of state involvement in the economy, the privatization of state economic and social assets, lower direct taxation, unfettered trade and financial movements, a reduction in the state's social welfare role – became the mantra, especially in the USA and the UK. 'Government', argued the US President, Ronald Reagan, in the early 1980s, 'was not a solution to our problem, government is the problem.' A similar sentiment was echoed by the UK government of Margaret Thatcher (and revived by the Conservative-dominated UK coalition government of 2010–15). Such a free market ideology formed the basis of what came to be called the 'Washington Consensus', the set of views that exerted immense influence on both developed and, especially, developing countries.

That was then.

This is now – and how the world has changed! The cataclysmic events that stunned the global economy in 2008 saw a dramatic reversal in the apparently unchallenged dominance of the free market and a revival of the view that 'states really do matter'. The change was most apparent in the financial sector (see Chapter 16), where the 'Masters of the Universe'[2] had to go on bended knee to the state to be rescued, but also in such industries as automobiles (see Chapter 15). Governments poured billions of dollars, pounds and euros into propping up the financial sector. In some cases, notably in the USA and the UK, this amounted to little short of nationalization, a *bête noire* of the market fundamentalists. Quite how this will play out over the next few years is not yet clear. However, there is a generally held view that things will never be quite the same. The state is back.

In fact, the state never really went away. The notion that the power of the state had been totally emasculated by globalizing forces was always highly misleading. While some of the state's capabilities were reduced, and there may well have been a process of 'hollowing out',[3] the process was not a simple one of uniform decline on all fronts:[4]

> Much of the *'end of the state' … literature focuses on western notions of statehood and experiences* … Implicit is a common experience of the emergence of the state in the nineteenth century and its zenith in the postwar Fordist regime of accumulation … *In many parts of the world, however, experiences of statehood have followed a quite different trajectory and*

> *are, in a postcolonial context, still being actively constructed, strengthened and extended rather than weakened.*[5]

The state unquestionably remains a most significant force in shaping the world economy, despite the hyper-globalist rhetoric. It has *always* played a fundamental role in the economic development of *all* countries[6] and, indeed, in the process of globalization itself. After all, an increased facility to transcend geographical distance made possible by transportation and communication technologies is of little use if there are political barriers to such movement. An important enabling factor underlying globalization, therefore, has been the progressive reduction in political barriers to flows of commodities, goods, finance and other services.

In fact, the more powerful states have *used* globalization as a means of increasing their power:

> States actively construct globalization and use it as soft geo-politics and to acquire *greater* power over, and autonomy from, their national economies and societies respectively … [for example] … The US and the G-7's other dominant members design and establish the international trade agreements, organizations, and legislation that support and govern the trans-border investments, production networks, and market-penetration constitutive of contemporary economic globalization. Advanced capitalist states, particularly, use these political instruments to shape international economic decision-making and policy in their interests.[7]

Governments have also used the rhetoric of the supposedly unstoppable forces of globalization to justify particular kinds of domestic policy (including not taking certain kinds of action) on the argument that 'there is no alternative'.

States, nations, nation-states

We need to be clear about what we mean by the terms 'state', 'nation' and 'nation-state':[8]

- A *state* is a portion of geographical space within which the resident population is organized (i.e. governed) by an authority structure. States have externally recognized sovereignty over their territory.
- A *nation* is a 'reasonably large group of people with a common culture, sharing one or more cultural traits, such as religion, language, political institutions, values, and historical experience. They tend to identify with one another, feel closer to one another than to outsiders, and to believe that they belong together. They are clearly distinguishable from others who do not share their culture.' A nation is an *imagined community*. Note that whereas a state has a recognized and defined territory, a nation may not.

- A *nation-state* is the situation where 'state' and 'nation' are coterminous. 'A nation-state is a nation with a state wrapped around it. That is, it is a nation with its own state, a state in which there is no significant group that is not part of the nation.'

Although it is often regarded as a natural institution (for all of us it has always been there), the nation-state is actually a relatively recent phenomenon. It emerged from the particular configuration of power relationships in Europe following the Treaty of Westphalia that ended the Thirty Years War in 1648. Since then, the map of nation-states has been redrawn continuously, sometimes peacefully and incrementally, often violently through revolution. During the second half of the twentieth century, two particular events had a profound effect on the map of nation-states. First, the waves of decolonization that swept through Africa and Asia in the 1960s created a whole new set of nation-states. Second, the collapse of the former Soviet Union, after 1989, resulted in the creation not only of a new Russian Federation, but also of a number of newly independent states throughout Eastern Europe. As a result, the number of nation-states, as measured by UN membership, has grown dramatically (Figures 6.1 and 6.2).

But that is not all. An important feature of today's world is the tension between the triad of nation, state and nationalism. Increasingly, it seems, there are more and more 'nations without states', manifested in separatist movements engaged in conflict with the state in which they are (wrongly in their view) embedded (obvious

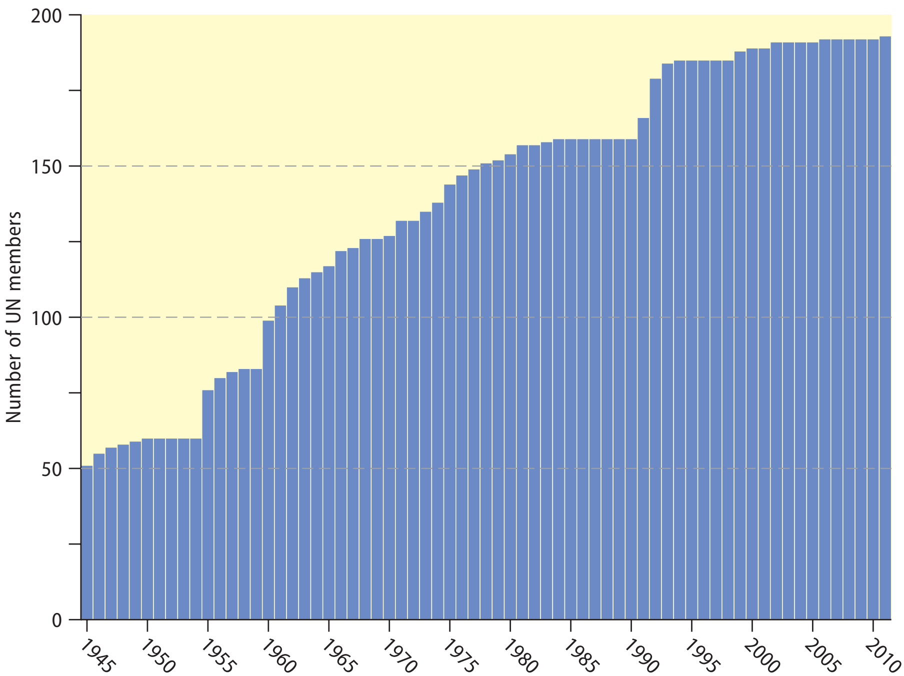

Figure 6.1 The increasing number of nation-states: growth in UN membership

Source: United Nations

Figure 6.2 A world of nation-states

examples include the Basques in Spain and France, the indigenous groups in Chiapas, Mexico, the East Timoreans in Indonesia, the Palestinians in Israel).

STATES AS CONTAINERS

The 'black box' of the state acts as a kind of 'container' of distinctive practices and institutions. Of course, the term 'container' should not be taken literally. It is used here as a loose metaphor to capture the idea that nation-states are *one* of the major ways in which distinctive cultures, practices and institutions are 'bundled together'.[9] Of course, such containers are not (except very rarely) hermetically sealed off from the outside world. A major impact of modern communications systems, especially the Internet, is to make national containers even more permeable. But that does not mean that the container no longer exists. Indeed, there is a good deal of compelling evidence to show the persistence of national distinctiveness – although not necessarily uniqueness – in structures and practices which help to shape local, national and global patterns of economic activity.

States as cultural containers

All economic activity is enmeshed in broader cultural structures and practices,[10] although 'culture' is an extremely slippery concept to define. Here it is taken to be

> a learned, shared, compelling, interrelated set of symbols whose meanings provide a set of orientations for members of a society. These orientations, taken together, provide solutions to problems that all societies must solve if they are to remain viable.[11]

From an economic perspective, there are relatively few comprehensive and robust analyses of how cultures vary between countries. The most widely known is Geert Hofstede's classic study of more than 100,000 workers employed by the US company IBM in 50 different countries.[12] Hofstede claimed that, by focusing on a controlled population within a common organizational environment, he was able to isolate *nationality* as a variable. On this basis he identified four distinct cultural dimensions:

- *Individualism versus collectivism*: societies vary between those in which people, in general, are motivated to look after their own individual interests – where ties between individuals are very loose – and those in which ties are very close and the collectivity (family, community, etc.) is the important consideration.
- *Large or small power distance*: societies vary in how they deal with inequalities (e.g. in power and wealth) between people. This is reflected in the extent to which authority is centralized and in the degree of autocratic leadership within society.

- *Strong or weak uncertainty avoidance*: in some societies, the inherent uncertainty of the future is accepted; each day is taken as it comes, that is the level of uncertainty avoidance is weak. In other societies, there is a strong drive to try to 'beat the future'. Efforts (and institutions) are made to try to create security and to avoid risk. These are strong uncertainty avoidance societies.
- *Masculinity versus femininity*: societies can be classified according to how sharply the social division between male and females is drawn. Societies with a strong emphasis on traditional masculinity allocate the more assertive and dominant roles to men. They differ substantially from societies where the social gender role division is small and where such values are less evident.

Hofstede went on to show how different countries could be characterized in terms of their positions on varying combinations of these four dimensions (Figure 6.3).

Group	1. Anglo	2. Germanic	3. Nordic	4. More developed Asian
Characteristics	Low power distance Low to medium uncertainty avoidance High individualism High masculinity	Low power distance High uncertainty avoidance Medium individualism High masculinity	Low power distance Low to medium uncertainty avoidance Medium individualism Low masculinity	Medium power distance High uncertainty avoidance Medium individualism High masculinity
Countries	*Australia Britain Canada Ireland New Zealand U.S.A.*	*Austria Germany Israel Italy South Africa Switzerland*	*Denmark Finland Netherlands Norway Sweden*	*Japan*
Group	**5. Less developed Asian**	**6. Near Eastern**	**7. More developed Latin**	**8. Less developed Latin**
Characteristics	High power distance Low uncertainty avoidance Low individualism Medium masculinity	High power distance High uncertainty avoidance Low individualism Medium masculinity	High power distance High uncertainty avoidance High individualism Medium masculinity	High power distance High uncertainty avoidance Low individualism Whole range on masculinity
Countries	*India Pakistan Philippines Singapore Taiwan Thailand*	*Greece Iran Turkey*	*Argentina Belgium Brazil France Spain*	*Chile Colombia Mexico Peru Portugal Venezuela*

Figure 6.3 National variations in cultural characteristics

Source: based on Hofstede, 1980: p. 336

Although Hofstede's work has stood the test of time remarkably well,[13] it has its critics. For example, Shalom Schwartz[14] argued that not enough countries were included fully to capture national cultural variation and that the respondents were too narrowly drawn to be truly representative of the entire population. Using rather different methods, he identified the following seven distinctive cultural dimensions:

- *Conservatism*: places an emphasis on preserving the status quo and in restricting behaviour likely to disrupt the traditional order.
- *Intellectual autonomy*: the extent to which people are free to pursue their own intellectual ideas.
- *Affective autonomy*: the extent to which people are free to pursue their own personal and emotional desires.

- *Hierarchy*: the extent to which an uneven allocation of power and resources is legitimized.
- *Egalitarian commitment*: the extent to which individuals are prepared to subjugate self-interest for the greater communal good.
- *Mastery*: the extent to which individual self-assertiveness is legitimized as a means to achieve specific goals.
- *Harmony*: the importance placed on fitting harmoniously into the environment.

Although there is obviously some overlap between these two schemes, what matters here is not so much the detail as the fact that there *are* identifiable cultural attributes that appear to vary across countries and that this, in turn, affects both how the major actors we identified in Chapter 3 are likely to behave and the kinds of institutions within which such behaviour is organized and regulated. Although it is always rather dangerous to classify phenomena into statistical boxes, the categories shown in Figure 6.3 seem intuitively reasonable. Most of us would be able to recognize our own national contexts, while also realizing the danger of using simple stereotypes without due care.

For example, East Asia's emergence as the most dynamic growth region in recent decades has often been attributed to its having a very distinctive set of value systems: specifically an emphasis on collective responsibility rather than individualism and on the roles and responsibilities of the state, which is seen as essentially paternalistic. Figure 6.4 sets out the major components of this concept of 'Asian values' which, in effect,

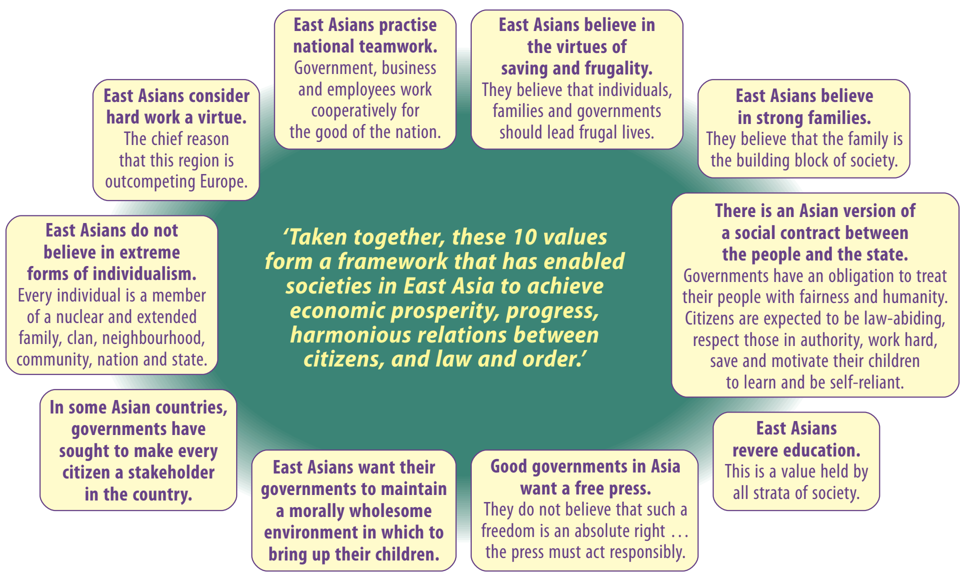

Figure 6.4 'Asian values'?

Source: based on material in Koh, 1993 'recast "Asia" as a moral opposite of the West. Thus … the Asian penchant for hard work, frugality and love of the family are unproblematically figured as things the West lacks or has lost.'[15] It is extremely doubtful that this reflects the situation across the whole of East Asia (let alone of Asia as a whole). This is, after all, a region of immense social, cultural and religious diversity. But insofar as these attributes reflect at least *some* of the social and political characteristics of *some* successful East Asian economies, they form a considerable contrast with the situation in other parts of the world.[16]

Variegated capitalisms

The specific cultural and institutional forms that have evolved over time in different national contexts have resulted in distinctive modes of economic organization, even within the apparently universal ideology of capitalism. Capitalism, in other words, is *variegated*, not uniform.[17] The traditional 'varieties of capital' literature focuses on just two broad categories of 'national' capitalism:

- the *liberal market economy* (LME), generally associated with the USA and, to a large extent, the UK;
- the *coordinated market economy* (CME), most commonly associated with such countries as Germany, Sweden and Japan.

This is not a very satisfactory classification.[18] In particular, the CME category encompasses enormous diversity and needs to be further unpacked. Here we identify four variants of capitalist organization, based on differing conceptions of the 'proper' role of government in regulating the economy:

- *Neo-liberal market capitalism*. Market mechanisms are used to regulate all, or most, aspects of the economy. Individualism is a dominant characteristic; short-term business goals tend to predominate. The state does not overtly attempt to plan the economy strategically. Capital markets are decentralized, open and fluid. The dominant philosophy is 'shareholder value' – facilitating maximum returns to the owners of capital. Exemplified by the USA and, to a large extent, the UK.
- *Social market capitalism*. In contrast to neo-liberal market capitalism, a higher premium is placed upon collaboration between different actors in the economy with a broader identification of 'stakeholders' beyond that of solely the owners of capital. The concept of 'social partnership' is more prominent. Capital markets tend to be bank centred. Exemplified by Germany, Scandinavia and many other European countries.
- *Developmental capitalism*. The state plays a much more central role (although not necessarily through public ownership of productive assets). The state sets substantive social and economic goals within an explicit industrial strategy. Capital

markets tend to be bank centred. There is a strong emphasis on tight business networks. Exemplified by Japan, South Korea, Taiwan, Singapore and most other East Asian countries (excluding China). Variants on this model include 'the "democratic development capitalism" of India and Brazil, with their strong social agendas to go with their growth aspirations'.[19]

- *Authoritarian capitalism*. Here, a highly centralized political system is combined with an increasingly open capitalist-market system. The prime example is China, where the process of liberalizing the economy (in a highly controlled way) began in 1979. Nevertheless, the Chinese Communist Party retains tight political control. In the case of Russia, the system is rather messier. Both political and economic structures were liberalized after 1991 but the Russian state still exerts strong control (though less effectively than in China).

Of course, this four-fold typology is also highly simplistic and, like all such schemes, should be seen in dynamic rather than static terms. However, there is little doubt that a *variegated*, rather than a single, system of capitalism (of whatever kind) is likely to persist in the future:

> There are inherent obstacles to convergence among social systems of production of different societies, for where a system is at any one point in time is influenced by its initial state … Existing institutional arrangements block certain institutional innovations and facilitate others … There are critical turning points in the history of highly industrialized societies, but the choices are limited by the existing institutional terrain. Being path dependent, a social system of production continues along a particular logic until or unless a fundamental societal crisis intervenes.[20]

An alternative view is that the pressures exerted by globalizing forces will inevitably produce a convergence of economic governance systems towards a 'best-practice' form. Until recently, many argued that the neo-liberal model, based on the success of its leading advocate, the USA, would come to replace national systems. In other words,

> even though the unique kinds of state capacities found in Japan and Germany have deep-rooted political preconditions, these face the prospect of 'permanent dismantling' by way of gradual 'liberal erosion'.[21]

But, as we have seen, the 'pure gold' of the neo-liberal model is now looking distinctly tarnished and it is difficult to imagine that it will retain its attractiveness. If this is so, then variegated capitalisms will continue to be the norm although in a dynamic, not static, form in which the state is likely to have a larger (though varied) role:

> The wide divergences among high-income countries over the size of the state, the generosity of welfare systems, the structure of corporate governance and the pervasiveness of financial markets all demonstrate the possible divergences.[22]

> We can safely predict … that the Anglo-American view will become less influential … [while] … virtually all Asian models of capitalism involve a more active role for government. And the rise of these models is taking place as the US approach is discredited by abuse, shrivelling opportunities and a shrinking middle class. Among the alternatives, the US model is now the outlier.[23]

STATES AS REGULATORS

Recognizing that countries continue to differ as 'containers' of distinctive structures and practices is important in emphasizing that we do not live in a homogenizing world. In this section, we focus specifically on some of the ways states *regulate* how their economies operate as they attempt to control what happens within, and across, their boundaries.

The competition state

> The transformation of the nation-state into a 'competition state' lies at the heart of political globalization.[24]

Books, government reports, newspaper articles, TV programmes in virtually all countries resonate with the language and imagery of the competitive race between states for a bigger slice of the global economic pie. Indeed, the Swiss business school IMD publishes an annual *World Competitiveness Yearbook* with a 'competitiveness scoreboard' (or 'league table') of 49 countries based on no fewer than 286 individual criteria!

States compete to enhance their international trading position in order to capture as large a share as possible of the gains from trade. They compete to attract productive investment to build up their national production base that, in turn, enhances their international competitive position. One of the most graphic expressions of competition between states is their intense involvement in what have been called 'locational tournaments': the attempts to entice investment projects into their own national territories. There has been an enormous escalation in the extent of *competitive bidding* between states (and between local communities within the same state) to attract the relatively limited amount of geographically mobile investment (see Chapter 7).

Most states continually search for a magic key to enhance their economic competitiveness. One of the most widely adopted has been Michael Porter's 'competitive diamond' framework, in which he argues that national competitive advantages are created through highly localized processes internal to the country. Figure 6.5 shows these as an interconnected, mutually reinforcing, system of four major determinants.

Porter's 'competitive recipe' has been adopted by many governments in their attempts to improve their competitive position, although he sees government itself as merely an 'influence'; a contingent, rather than a central, factor. In fact, *all* states perform a key role in the operation of their economies, although they differ substantially in the specific measures they employ and in the precise ways in which such measures are combined.

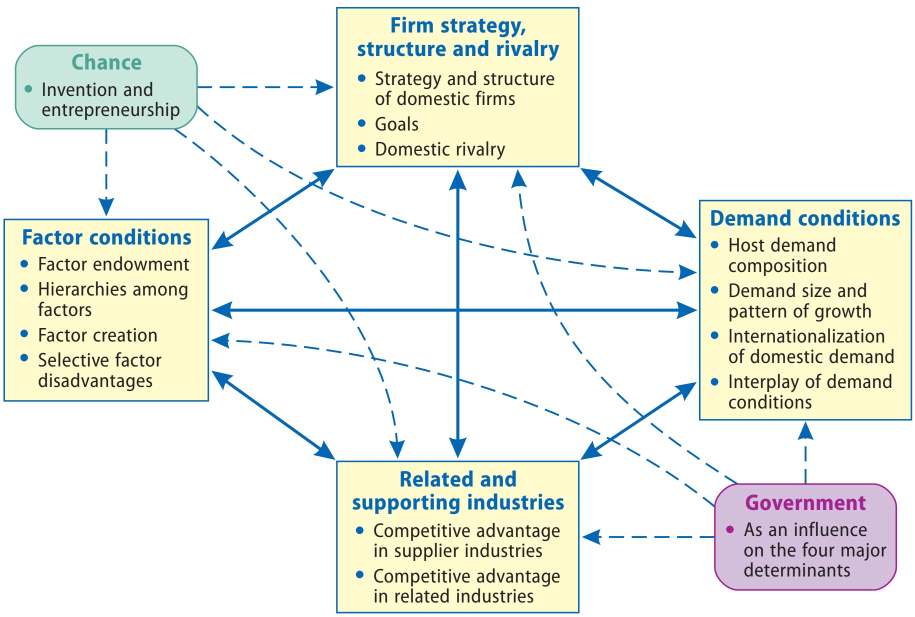

Figure 6.5 National competitive advantage: the Porter 'diamond'

Source: based on material in Porter, 1990: chapter 3

Managing national economies

> The institutions of the state … are not simply involved in regulating economy and society, for *state activity is necessarily involved in constituting economy and society* and the ways in which they are structured and territorially organized.[25]

In other words, states do not merely 'intervene' in markets; they underpin and help to constitute their very existence.

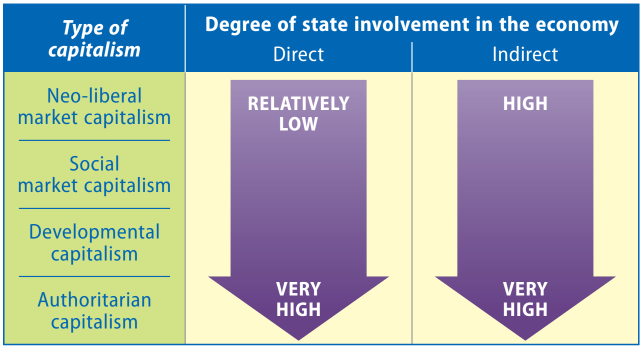

Figure 6.6 **State economic involvement in different types of capitalism**

Although a high level of contingency may well be involved in how states strive to manage their economy, certain common themes are evident. These reflect the kinds of cultural, social and political structures, institutions and practices in which the state is embedded. Specifically, the degree of direct and indirect state participation in economic management varies with the type of capitalism involved (Figure 6.6). The precise policy mix adopted by a state will also be influenced by:

- the *size* of its national economy;
- its *resource endowment*, both physical and human;
- its *relative position* in the world economy, including its level of economic development and degree of industrialization.

Two basic types of macroeconomic policy are used by the state to manage its national economy:

- *Fiscal policies* to raise or lower taxes on companies and/or individual citizens and to determine appropriate levels and recipients of government expenditure. Raising taxes (either direct or indirect) dampens down domestic demand, lowering taxes stimulates demand. However, such automatic responses to changes in fiscal policy do not always occur. For example, consumers may choose to save rather than spend any tax gain they receive. Similarly, raising or lowering public expenditure or targeting specific types of expenditure can influence the level of economic activity in the economy.
- *Monetary policies* aimed at influencing the size of the money supply within the country and at either speeding up, or slowing down, its rate of circulation. The main mechanism employed is manipulation of the interest rate on borrowing. Lowering interest rates should stimulate economic activity through increased investment or private expenditure while, conversely, raising interest rates should dampen down activity. Again, however, rapid and automatic adjustment

does not always occur. The 2008 financial crisis has led most countries to keep their interest rates at exceptionally low levels (close to zero in some cases) for a very long period of time. At the same time, injecting money into the economy (sometimes called 'Quantitative Easing' – QE) has become common. Most spectacularly, in 2013 the Japanese government decided to double the volume of money in circulation in an attempt to reverse the long-standing problem of deflation in the economy. Inevitably, monetary policies impact upon a country's international currency exchange rate, whose level and volatility affect the costs of exports and imports.

Such policies are also underpinned by the state's regulation of financial services (see Chapter 16).

At a more tangible and material level, governments generally provide – or at least secure the provision of – those 'conditions of production that are not and cannot be obtained through the laws of the market'.[26] One example is the *physical infrastructure* of national economies – roads, railways, airports, seaports, telecommunications systems – without which private sector enterprises, whether domestic or transnational, could not operate. They are the providers, too, of the *human infrastructure*, in particular of an educated labour force as well as of sets of laws and regulations within which enterprises must operate.

For several decades after the end of the Second World War in 1945, the role of the state in the developed economies progressively expanded, notably through the provision of welfare benefits for particular segments of the population and the development of a considerable (though varied) degree of public ownership of productive assets. The majority of economies, outside the command economies of the state-socialist world, became *mixed economies*. In many countries certain economic sectors, such as telecommunications, railways, energy, steel and the like, became state owned or controlled. As a result, government spending as a percentage of GDP rose very substantially. In the OECD countries, such spending increased from less than 20 per cent of GDP in the early 1960s to 35 per cent in the early 1990s. In the developing countries, the average growth was from around 15 per cent to 27 per cent. Of course, the pattern varied a lot between countries.

Starting in the mid-1980s, many states reduced their direct involvement in their economies, most notably through a systematic process of *marketization*: extending the principles of market transactions into more and more aspects of public life. This was apparent not only in the older industrialized countries, but also in many developing countries and, most dramatically of course, in the former state-socialist countries of Eastern Europe, the former Soviet Union and in China. Such *market liberalization* consisted of two related processes:

- *Deregulation*. Virtually all industrialized countries jumped aboard the deregulation bandwagon to varying degrees. However, the issues are far less simple than the 'deregulationists' claim. Because no activity can exist without some form of regulation (otherwise anarchy ensues), 'deregulation cannot take place without the creation of new regulations to replace the old'.[27] In effect, what is often termed *de*regulation is really *re*regulation. Processes of deregulation spread to most economic sectors, most notably in financial services (see Chapter 16), telecommunications and utilities (such as energy and water). The labour market also became a particularly significant focus of deregulation (see below).

- *Privatization*. The state pulled out of a variety of activities in which it was formerly centrally involved and transferred them to the private sector. The selling of state-owned assets, and the greater participation of the private sector in the provision of both 'private' goods (the 'de-nationalization' of state-owned economic activities) and 'public' goods (such as health care or education), has been a pervasive, continuing, though uneven, movement. However, this has not reduced government expenditure as much as might have been expected; the rhetoric has often been stronger than the reality, as Figure 6.7 shows. The average GDP share of government spending in the 26 countries shown was 46.6 per cent in 2011 compared with 43.1 per cent in 2000.

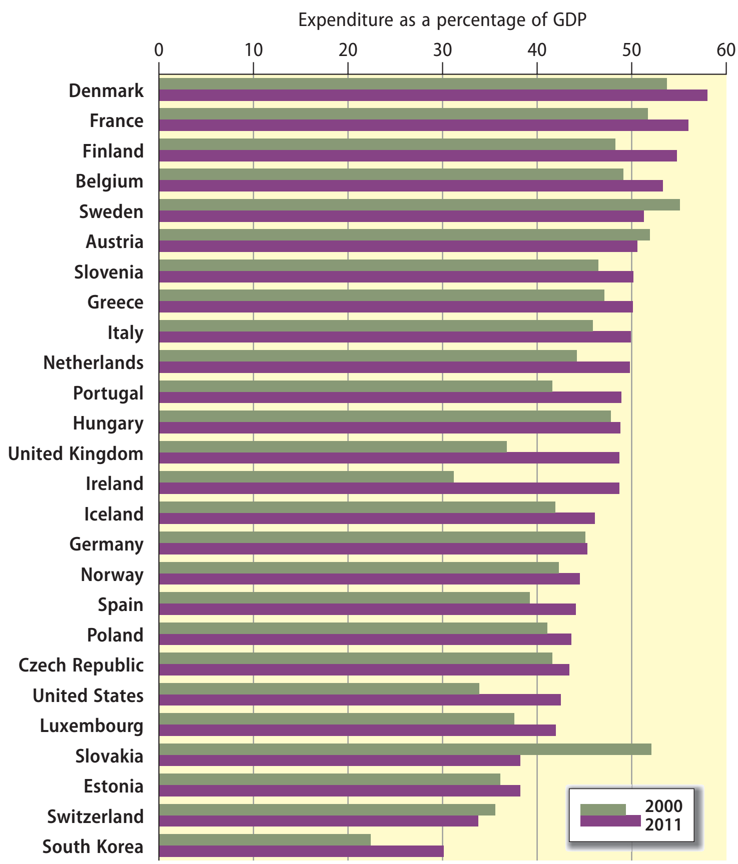

Figure 6.7 Central government spending as a share of GDP

Source: OECD data

In response to the post-2008 crisis, all governments intervened massively to re-stimulate their economies. The figures involved are astronomical.[28] The combined stimulus expenditure of the G20 countries for 2009 was $692 billion, the equivalent of 1.4 per cent of their GDP. The USA accounted for almost 40 per cent of this. The other countries with very large stimulus packages were China ($204 billion), Germany ($130 billion) and Japan ($104 billion). Since then, the debate has focused around either continuing or increasing stimulus expenditure to kick-start economic growth or cutting expenditure in key areas as part of austerity programmes. This debate has been especially acute within the EU but is by no means confined to Europe and continues within the G20 countries.

Such large-scale intervention during a period of economic recession reflects the influence of John Maynard Keynes, whose analysis of the 'Great Depression' of the 1930s demonstrated that markets do not necessarily correct themselves.[29] Under certain circumstances, they have to be stimulated by government actions – possibly in a very large-scale way – through, for example, reducing interest rates, providing financial assistance to specific firms and sectors, and investing heavily in infrastructure.

Regulating and stimulating the economy

National governments possess an extensive kit of regulatory tools with which to try to control and to stimulate economic activity and investment within their own boundaries and to shape the composition and flow of trade and investment across them. These tools may be employed as part of a deliberate, cohesive, all-embracing national economic strategy or, alternatively, individual policy measures may be implemented ad hoc with little attempt at strategic coordination.

Trade

Of all the measures used by nation-states to regulate their international economic position, policies towards trade have the longest history. The shape of the emerging world economy of the seventeenth and eighteenth centuries was hugely influenced by the mercantilist policies of the leading European nations. Figure 6.8 summarizes the major types of trade policy pursued by national governments. In general, policies towards imports are restrictive whereas policies towards exports, with one or two exceptions, are stimulatory.

Policies on *imports* fall into two distinct categories:

- *Tariffs.* These are taxes levied on the value of imports that increase the price to domestic consumers and make imported goods less competitive (in price terms) than otherwise they would be. In general, the tariff level tends to rise with the stage of processing, being lowest on basic raw materials and highest

Policies towards imports	Policies towards exports
1. Tariffs	Financial and fiscal incentives to export producers
2. Non-tariff barriers	Export credits and guarantees
Import quotas (e.g. 'voluntary export restraint', 'orderly marketing agreements')	Setting of export targets
Import licences	Operation of overseas export promotion agencies
Import deposit schemes	Establishment of Export Processing Zones and/or Free Trade Zones
Import surcharges	'Voluntary export restraint'
Rules of origin	Embargo on strategic exports
Anti-dumping measures	Exchange rate manipulation
Special labelling and packaging regulations	
Health and safety regulations	
Customs procedures and documentation requirements	
Subsidies to domestic producers of import-competing goods	
Countervailing duties on subsidised imports	
Local content requirements	
Government contracts awarded only to domestic producers	
Exchange rate manipulation	

Figure 6.8 Major types of trade policy

on finished goods. The purpose of such 'tariff escalation' is to protect domestic manufacturing industry while allowing for the import of industrial raw materials. Thus, although tariffs may be regarded simply as one means of raising revenue, their major use has been to *protect* domestic industries: either 'infant' industries in their early delicate stages of development or 'geriatric' industries struggling to survive in the face of external competition.

- *Non-tariff barriers (NTBs)*. While tariffs are based on the value of imported products, NTBs are more varied: some are quantitative, some are technical. Although, in general, tariffs have continued to decline, the period since the mid-1970s witnessed a marked increase in the use of NTBs. Indeed, today NTBs are more important than tariffs in influencing the level and composition of trade between nation-states. It has been estimated that NTBs affect more than a quarter of all industrialized country imports and are even more extensively used by developing countries. Certainly much of what has been termed the 'new protectionism' consists of the increased use of NTBs.

National trade policy is unique in that since the late 1940s it has been set within an *international* institutional framework: the GATT/WTO. We will have much more to say about this in Chapter 11. Here we merely need to note the basic features of this regulatory system. The purpose of the GATT was to create a set of *multilateral rules* to facilitate free trade through the reduction of tariff barriers and other types of trade discrimination. The GATT was eventually replaced by the WTO in 1995, an institutional change which greatly broadened the remit of the trade regulator. Today, around 97 per cent of world trade is covered by the WTO framework.

FDI

In a world of transnational corporations and of complex flows of investment at the international scale, national governments have a clear vested interest in the effects of FDI, whether positive or negative. Few national governments operate a totally closed policy towards FDI, although the degree of openness varies considerably.

Figure 6.9 summarizes the major types of national FDI policy. Most are concerned with inward investment, although governments may well place restrictions on the export of capital for investment (e.g. through the operation of exchange control regulations) or insist that proposed overseas investments be approved before they can take place. Historically, there have been large differences in national policy positions towards inward FDI. In general, developed countries have tended to adopt a more liberal attitude towards inward investment than developing countries,[30] although there were exceptions. For example, among developed countries France had a much more restrictive stance than most other European countries. Among developing countries, Singapore had a particularly open policy, far more so than most other Asian countries. In the past two decades, however, national FDI policies have tended to converge in the direction of liberalization. Attempts to regulate at the international scale have not been successful (see Chapter 11).

Policies relating to inward investment by foreign firms

Entry
- Government screening of investment proposals.
- Exclusion of foreign firms from certain sectors or restriction on the extent of foreign involvement permitted.
- Restriction on the degree of foreign ownership of domestic enterprises.
- Compliance with national codes of business conduct (including information disclosure).

Operations
- Insistence on involvement of local personnel in managerial positions.
- Insistence on a certain level of local content in the firm's activities.
- Insistence on a minimum level of exports.
- Requirements relating to the transfer of technology.
- Locational restrictions on foreign investment.

Finance
- Restrictions on the remittance of profits and/or capital abroad.
- Level and methods of taxing profits of foreign firms.

Incentives
- Direct encouragement of foreign investment: competitive bidding via overseas promotional agencies and investment incentives.

Policies relating to outward investment by domestic firms

- Restrictions on the export of capital (e.g. exchange control regulations).
- Necessity for government approval of overseas investment projects.

Figure 6.9 Major types of FDI policy

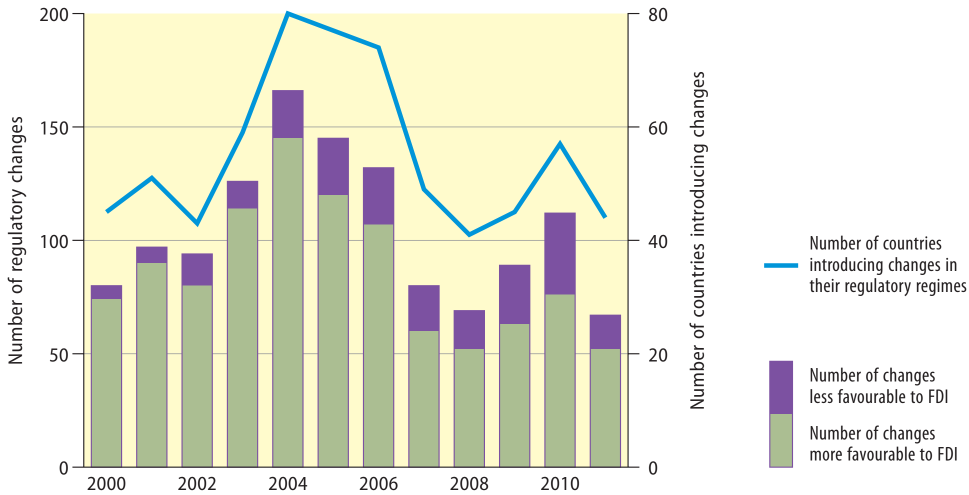

Figure 6.10 Changes in national regulation of FDI

Source: based on UNCTAD, 2009: Table I.14; 2012: Table III.1

Although national differences still exist, therefore, they are now rather less stark than in the past. Figure 6.10 summarizes the major regulatory changes towards FDI between 2000 and 2011. The proportion of regulatory changes that are more favourable to FDI continues to far outweigh those that are unfavourable, although 'in the last three years, 30 or 40 per cent of the laws have gone in the direction of being less welcome to investment'.[31]

Industry and technology

There is much debate about whether or not governments can, or should, attempt to pursue a focused industry strategy, especially in the more neo-liberal, free market economies. In fact, ever since Britain emerged as the world's first fully industrialized nation in the late eighteenth and early nineteenth centuries,

> every successful industrial power at some point in its history has carried out an activist industrial policy.[32]

Most influential historically were the ideas of the nineteenth-century German economist Friedrich List.[33] List heavily criticized Britain for advocating free trade policies only after it had attained a position of global industrial leadership. In fact, all the 'newly industrializing economies' of the nineteenth century – in particular the USA, Germany, France, other European nations, as well as Japan – adopted a set of policies that were strongly protectionist and developmental in order to nurture their infant industries, before relaxing some of the trade barriers when these industries were seen to be strong enough to face external competition.

Today, some governments – notably the neo-liberalist US and UK – still tend to be in denial that they should pursue an active industry policy involving the public sector. But this is a smokescreen. Governments across the board continue to be heavily engaged, either directly or indirectly, in trying to stimulate their industrial sectors. Indeed, there are whole areas of the economy – notably those dependent on big, long-term investments in science and technology – where government is absolutely central. The real distinction, then, is between an overt and a covert stance, for example over whether government can or should attempt to 'pick winners'.[34]

The range of potential industry and technology policies

- Investment incentives
- Taxation policies
- Technology policies
- Labour market policies
- State procurement policies
- Small firm policies
- Policies to encourage industrial restructuring
- Policies to promote investment
- Merger and competition policies
- Company legislation
- National technical and product standards
- State ownership of production assets
- Environmental regulations
- Health and safety regulations

Some or all of these policies may be applied either generally or, more commonly, selectively. Selectivity may be based on several criteria:

1. Particular geogaphical areas, e.g.
(a) economically depressed areas,
(b) areas of 'growth potential' ('cluster policies').

2. Particular sectors of industry, e.g.
(a) to bolster declining industries,
(b) to stimulate new industries,
(c) to preserve key strategic industries.

3. Particular types of firm, e.g.
(a) to encourage entrepreneurship and new firm formation,
(b) to attract foreign firms,
(c) to help domestic firms against foreign competition,
(d) to encourage firms in import-substituting or export activities.

Figure 6.11 Major types of industry and technology policy

Figure 6.11 outlines the major types of industry and technology policies that may be used by national governments. Such policies may be applied *generally* across the whole of a nation's industries or they may be applied *selectively*. Such selectivity may take a number of forms: particular sectors of industry, particular types of firms (including, for example, the efforts to attract foreign firms), particular geographical locations. Especially, there has been a deluge of interest, in most countries, in trying to encourage the development of *growth clusters*: an attempt to capture the virtual circle of growth that has come to be associated with the kinds of technology clusters described in Chapter 4.

Related to this is the almost universal adoption of various kinds of *technology (R&D) policy* by national governments in an attempt to develop and exploit technological innovations. At one level, such policies tend to focus on stimulating investment and entrepreneurship through, for example, various kinds of tax incentive. But at the macro level, the major role of governments is in providing the basic, high-risk, exceedingly costly scientific and technological infrastructures and innovations upon which companies depend. Mariana Mazzacuto develops a very powerful case to show that in most of the 'high-tech' sectors, such as ICT, pharmaceuticals and nanotechnology, most of the spectacularly successful private companies have depended on being able to 'piggyback' on the huge, long-term investments by government:

> Most of the radical, revolutionary innovations that have fuelled the dynamics of capitalism – from railroads to the Internet, to modern-day nanotechnology and pharmaceuticals – trace the most courageous, early and capital-intensive 'entrepreneurial' investments back to the State … [for example] all of the technologies that make [Apple's] iPhone so 'smart' were government funded (Internet, GPS, touch-screen display and the recent SIRI voice activated personal assistant). Such radical investments – which embedded extreme uncertainty – did not come about due to the presence of venture capitalists, nor of 'garage tinkerers'. It was the visible hand of the State which made these innovations happen. Innovation that would not have come about had we waited for the 'market' and business to do it alone – or government simply to stand aside and provide the basics.[35]

Labour markets

States, especially in the older industrialized economies, have become increasingly involved in labour market policies, particularly in attempting to make labour markets more *flexible*. A new conventional wisdom has emerged: the need to remove *rigidities* in the labour market to make it more in tune with what are seen to be the dominant characteristics of a globalizing world economy. The 'flexibilization' of labour markets through deregulation involves greatly increased pressures and restrictions on labour organizations, the drastic cutting back of welfare provisions, and the move away from welfare towards *workfare*.[36]

The process has gone furthest in the USA. Its apparent success in continuing to create large numbers of jobs (albeit with the widening of income gaps) has 'been the most persuasive argument for neo-liberal policies'.[37] It certainly stimulated the UK government to move along the same path. As yet, the countries of continental Europe have not moved as far, or as fast, down the labour market flexibility path. Most European governments are concerned that the social costs of reducing unemployment using the US model may be politically unacceptable in a system in which the social dimension of the labour market is very strongly entrenched. But there are clear signs of change as governments become increasingly concerned about the financial costs of sustaining existing practices and the continuing loss of competitive edge. As a result, a variety of labour market measures, employed in various combinations in different European countries, has emerged (Figure 6.12).

The range of potential labour market policies

- The use of more temporary and fixed term contracts
- The introduction of different forms of flexible working time
- Moves to encourage greater wage flexibility by getting the long-term unemployed and the young to take low-paid jobs
- Increased vocational training to provide more transferable skills
- Reforms in state employment services
- Incentives to employers to take on workers
- Measures to encourage workers to leave the labour market
- Reductions in the non-wage labour cost burdens on employers
- Specific schemes to target the long-term unemployed

Figure 6.12 Elements of labour market policies

Economic strategies in the older industrialized economies

As we saw earlier, the continental European countries, on the one hand, and the USA and the UK on the other, represent distinctively different types of capitalism. Historically, a major difference has been the centrality of industrial policy, together with a greater degree of social accountability of business in Europe, and the absence of such policy and accountability in the USA.[38] The UK occupies an intermediate position between the virtually pure market capitalism of the USA and the kinds of social market capitalism practised in continental Europe, but with a tendency in some areas (notably labour market policy) to be closer to the USA.

The policy stance of the *USA* reflects both the sheer scale and wealth of its domestic economy and also a basic philosophy of non-intervention by the federal government in the private economic sector. But, as we have seen, US governments have been immensely important in funding fundamental science and technology research, which has underpinned the growth of high-tech private sector firms. As far as industry in general is concerned, the role of the federal government has generally been *regulatory*: to ensure the continuation of competition. Action at the federal level has been based primarily on fiscal and monetary macroeconomic policies. The aim has been to create an investment climate in which private sector institutions could flourish. This has not, however, prevented the federal government from rescuing specific firms – especially very large ones – from disaster. At the other end of the size spectrum, the Small Business Administration has provided aid to stimulate new and small firms. Federal procurement policies are generally non-discriminatory but the sheer size of federal government purchases, particularly in the defence and aerospace industries, has exerted an enormous influence on US industry. Entire economic sectors, regions and communities are heavily dependent on the work created by federal defence and other procurement contracts and on subsidies in such sectors as agriculture (Chapter 13) and automobiles (Chapter 15).

US policy towards international trade during most of the post-war period has been one of urging liberalization through *multilateral* negotiations through the GATT/WTO. However, there has been an increasing willingness to develop bilateral trading arrangements with other countries. US trade policy is complicated by the structure and composition of the US Congress and the ways that new trade policies have to be negotiated with domestic interest groups.[39] As the strongest economy, the USA, like Britain in the nineteenth century, has been the leading advocate of free trade. Even so, the federal government has intervened with the use of tariff and non-tariff barriers to protect particular interests. A 'Buy American' initiative was part of the Obama administration's stimulus measures introduced in 2009.

In the eyes of many parts of the world, the USA is seen as having a strong *unilateralist* tendency, very much at odds with its traditional multilateral trading stance. The USA has become increasingly embroiled in a whole series of trade disputes, particularly with East Asian countries (primarily this means China) and with the EU. There is also concern that the USA has a tendency to introduce *extra-territorial* trade legislation to achieve its broader political objectives.

Within *Europe*, despite the existence of the EU, an ideological divide continues to exist between the so-called 'market' and 'social' models of how the economy should be organized, that is between the UK's more 'neo-liberal' position and that of France and Germany, where the principle of the 'social market' remains strongly entrenched. However, the lines are not always quite as clear as is often claimed. Although the *UK's* policy position does contrast in a number of ways with that of continental European countries, and is closer to that of the USA, the UK has been more interventionist than the USA, at least until recently.[40] Nevertheless, the UK has strongly adopted economic policies of privatization and deregulation. Its labour market policies, in particular, are far closer to the US model than to the EU model.

There are considerable differences in policy emphasis between continental European member states. Of the leading EU states, *France* maintains the most 'nationalistic' economic position, having long had the most explicit state industrial policy, a reflection of a tradition of strong state involvement dating back to the seventeenth century. A major component of French industrial policy has been the promotion of 'national champions' in key industrial sectors, often through state ownership of large-scale enterprises. France's current policy position retains many of these traditional qualities (and an especially strong antagonism to the Anglo-American neo-liberal economic model). Despite considerable privatization the French state retains a very considerable direct involvement in the economy.

Germany is the major exception among the continental European nations to a more centralized approach to industrial policy. In part, at least, this reflects its federalist political structure, with power divided between the federal government and the provinces (*Länder*). But although often described as 'light', the federal government's role has been far from insubstantial. It has pursued policies of active intervention in industrial matters, including a substantial programme of financial subsidy. Such involvement has to be seen within the German model of a social market economy.[41] The German economy is characterized both by a considerable degree of competition between domestic firms and by a high level of consensus between various interest groups, including labour unions, the major banks and industry. The major challenge facing Germany after 1990, of course, was to cope with the fundamental transformation of the economy brought about by reunification. Putting together the strongest economy in Europe (the former West Germany) with one that, for half a century, had existed in a completely different ideological system, was an immense undertaking. It placed enormous strains on the federal budget because of the huge problems of rebuilding infrastructure and dealing with problems of unemployment brought about by restructuring.[42]

Among the older industrialized economies, *Japan* stands apart in its policy stance. Japan can be regarded as the archetypal *developmental capitalist state*.[43] There has long been a high level of consensus between the major interest groups in Japan on the need to create a dynamic national economy. This consensus is often regarded as a cultural characteristic of Japanese society, with its deep roots in familism. But it also reflected the poor physical endowment of Japan and the limited number of options facing the country when, in the 1860s, it suddenly emerged from its feudal isolation. In other words, consensus was also a pragmatic stance built up over more than a hundred years. Given virtually no natural resources and a poor agricultural base, Japan's only hope of economic growth lay in building a strong manufacturing base, both domestically and internationally, through trade. In this process, the state played a central role not through direct state ownership, but rather by *guiding* the operation of a highly competitive domestic market economy.

For more than 50 years after the end of the Second World War, the key government institution concerned with both industry policy and trade policy was *MITI* – the *Ministry of International Trade and Industry* (renamed *METI*, the *Ministry for Economy, Trade and Industry*, in 2001). After its establishment in 1949, MITI became the real 'guiding hand' in Japan's economic resurgence. Until the 1960s Japan operated a strongly protected economy and it was not until 1980 that full internationalization of the Japanese economy was reached. During the 1950s and early 1960s MITI, together with the Ministry of Finance, exerted very stringent controls on all foreign exchange, on foreign investment and over the import of technology.

Initially, MITI focused on the basic industries of steel, electric power, shipbuilding and chemical fertilizers, but then progressively encouraged the development of petrochemicals, synthetic textiles, plastics, automobiles and electronics. Japan was transformed from a low-value, low-skill economy to a high-value, capital-intensive economy. The foundation of this transformation was the clearly targeted, selective nature of Japanese industry policy together with a strongly protected domestic economy.

A key element in Japanese economic policy was the specific treatment of inward FDI which, for much of the post-war period, was extremely tightly regulated. The technological rebuilding of the Japanese economy was based on the purchase and licensing of foreign technology and not on the entry of foreign branches or subsidiaries. Since the early 1990s, Japanese policy has been especially exercised by the problem of a high-value currency, with contentious trading relationships with the USA and Europe, and especially with the deep domestic recession which accompanied the collapse of the so-called 'bubble economy' at the end of the 1980s.

These diverse characteristics of industry policy in the older industrialized economies persist. However, the post-2008 financial crisis dramatically changed their context and called into question at least some of their elements. Faced with the enormous problems of huge financial deficits and sluggish economic growth, all of the older industrialized economies are struggling to redefine their strategies. Here, the ideological position of individual governments is extremely important. For example, a 'new' UK industrial strategy was in process of construction in 2013 but the coalition government's persistence with a deep austerity programme – and the overhang of the banking crisis – inevitably limited the scope for industrial policy initiatives. In late 2013, France set out a new 10-year industrial policy based around 34 sectors.[44] In Germany and France, where explicit industry policy is the norm, the problem is less ideological than practical, given the problems of the eurozone (see later in this chapter). In the USA, the position is rather different, given the long-standing reluctance to accept even the notion of an industry policy. In fact, of course, the USA always had an industry policy – it was the label that was avoided. In Japan, a developmental strategy never went away; the problems there have been the two-decade stagnation since the 1990s.

Jump-starting economic development

As we saw earlier, activist trade and industry policies were fundamental to the early economic development of all of today's older industrialized economies. A similar strategy has been followed by the new wave of NIEs of East Asia and Latin America – the 'latecomers' – in the second half of the twentieth century:

> Countries arriving late on the industrial scene suffer from enormous disadvantages … The latecomers have to meet the powerful incumbents with only their temporary advantages of lower costs. They have to devise strategies that capitalize on these lower costs … In this, they do have two potential advantages, in (1) not being burdened with past

> technological and organizational commitments … and (2) being able to devise institutions that make up for the deficits found in underdeveloped countries. These potential advantages are not handed on a plate to latecomers, or achieved automatically through operation of some 'economic law' … They are only achieved through strategizing, which is through the formulation of firm- and national-level policies and programmes designed to mesh with the current situation and capture the potential advantages that can be identified.[45]

From import substitution to export orientation

The essence of most policies aimed at 'jump-starting' the process has been one of an initial emphasis on import-substituting industrialization (ISI): the manufacture of products that would otherwise be imported, based upon protection against such imports. The aim is to protect a nation's infant industries so that the overall industrial structure can be developed and diversified and dependence on foreign technology and capital reduced. To this end, many of the policies listed in Figures 6.8, 6.9 and 6.11 have been employed.

The ISI strategy, in theory, is a long-term *sequential* process involving the progressive domestic development of industrial sectors through a combination of protection and incentives. The realization that an import-substituting strategy cannot, on its own, lead to the desired level of industrialization began to dawn in a growing number of countries, some during the 1950s, rather more during the 1960s. Generally it was the smaller industrializing countries that first began to shift towards a greater emphasis on *export orientation* because of the constraints imposed upon such a policy by their small domestic market. Increasingly, an export-oriented industrialization (EOI) strategy became the conventional wisdom among such international agencies as the Asian Development Bank and the World Bank.

Such a shift was facilitated by a number of factors:

- the rapid liberalization and growth of world trade during the 1960s;
- the 'shrinkage' of geographical distance through the enabling technologies of transportation and communications;
- the global spread of TNCs and their increasing interest in seeking out low-cost production locations for their export platform activities.

Export orientation was invariably based upon a high level of government involvement. The usual starting point was a major devaluation of the country's currency to make its exports more competitive in world markets, together with the whole battery of export trade policy measures shown in Figure 6.8. In effect, these amounted to a subsidy on exports that greatly increased their price competitiveness. Of course, the major domestic resource on which this EOI rests was the labour supply – not only its abundance and relative cheapness, but also its adaptability and, very often,

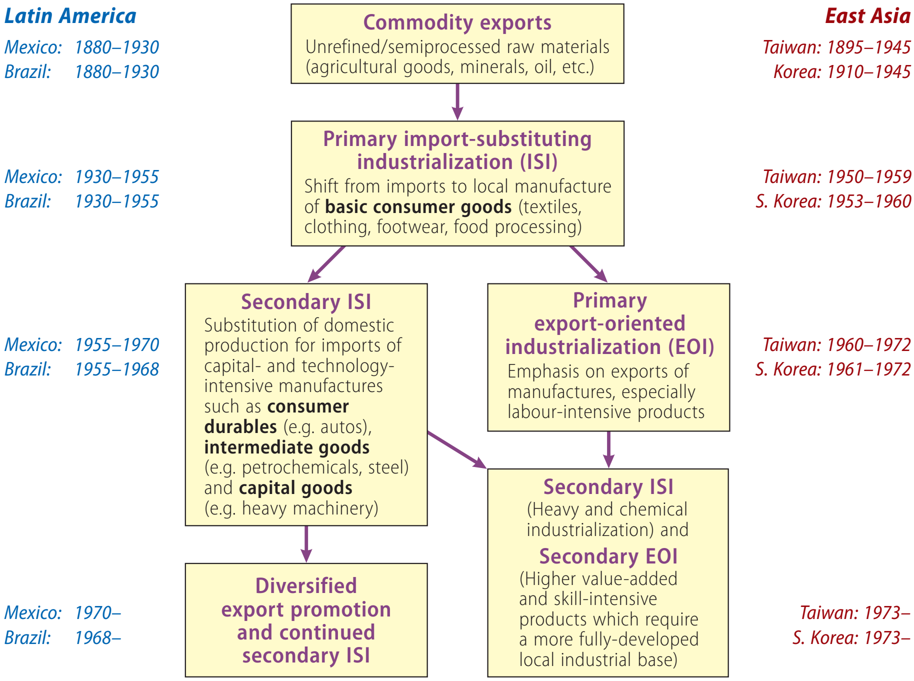

Figure 6.13 **Paths of industrialization in Latin America and East Asia: common and divergent features**

Source: based on material in Gereffi, 1990: Figure 1.1; p. 17

its relative docility. Indeed, in many cases, the activities of labour unions have been very closely regulated and often suppressed.

In fact, the 'paths of industrialization' followed by individual NIEs have been rather more complex than is often suggested.[46] Figure 6.13 sets out a five-phase sequence of industrialization based upon the experiences of the Latin American and East Asian NIEs into the 1990s. A number of important points can be made:[47]

- The distinction commonly drawn between inward-oriented Latin American industrialization strategies and outward-oriented East Asian industrialization strategies is misleading.
- The initial stages of industrialization were common to NIEs in both regions; 'the subsequent divergence in the regional sequences stems from the ways in which each country responded to the basic problems associated with the continuation of primary ISI'.[48]
- 'The duration and timing of these development patterns varied by region. Primary ISI began earlier, lasted longer, and was more populist in Latin America than in East Asia … The East Asian NICs began their accelerated export of manufactured products during a period of extraordinary dynamism

in the world economy … [after 1973] … the developing countries began to encounter stiffer protectionist measures in the industrialized markets. These new trends were among the factors that led the East Asian NIEs to modify their EOI approach in the 1970s.'[49]

- Some degree of convergence in the strategies of the Latin American and East Asian NIEs began to occur in the 1970s and 1980s. Each 'coupled their previous strategies from the 1960s (secondary ISI and primary EOI respectively) with elements of the alternate strategy in order to enhance the synergistic benefits of simultaneously pursuing inward- and outward-oriented approaches'.[50]

The attraction of FDI has been an integral part of both ISI and EOI in many developing countries, although to varying degrees. Among all the measures used by many developing countries to stimulate their export industries and to attract foreign investment one device in particular – the *export processing zone* (EPZ) – has received particular attention.[51] The ILO defines EPZs as:

> Industrial zones with special incentives set up to attract foreign investors, in which imported materials undergo some degree of processing before being (re-)exported again.[52]

Figure 6.14 shows the rapid growth in EPZs, especially during the past 30 years. Some 90 per cent of all EPZs in the developing countries are located in Latin America, the Caribbean, Mexico and Asia. However, in terms of employment, Asia is by far the most important region for EPZs, with 85 per cent of the total. Of these, the biggest concentration is in China, which has 40 million of the world total of 66 million EPZ workers.[53]

EPZs come in a number of different forms: 'free trade zones, special economic zones, bonded warehouses, free ports, and *maquiladoras*'.[54] Within developing countries, EPZs have been located in a variety of environments. Some have been incorporated into airports, seaports or commercial free zones or located next to large cities. Others have been set up in relatively undeveloped areas as part of a regional development strategy. EPZs themselves vary enormously in size, ranging from geographically extensive developments to a few small factories; from employment of more than 30,000 to little more than 100 workers.

EPZs in developing countries share many common features. The overall pattern of incentives to investors is broadly similar, as is the type of industry most commonly found within the zones. Historically, the production of textiles and clothing and the assembly of electronics – both employing predominantly young female labour – dominated. However, the position is not static:

> Zones have evolved from initial assembly and simple processing activities to include high tech and science zones, logistics centres and even tourist resorts. Their physical form now includes not only enclave-type zones but also single-industry zones (such as the jewellery zone in

Thailand or the leather zone in Turkey); single-commodity zones (like coffee in Zimbabwe); and single-factory (such as the export-oriented units in India) or single-company zones (such as in the Dominican Republic).[55]

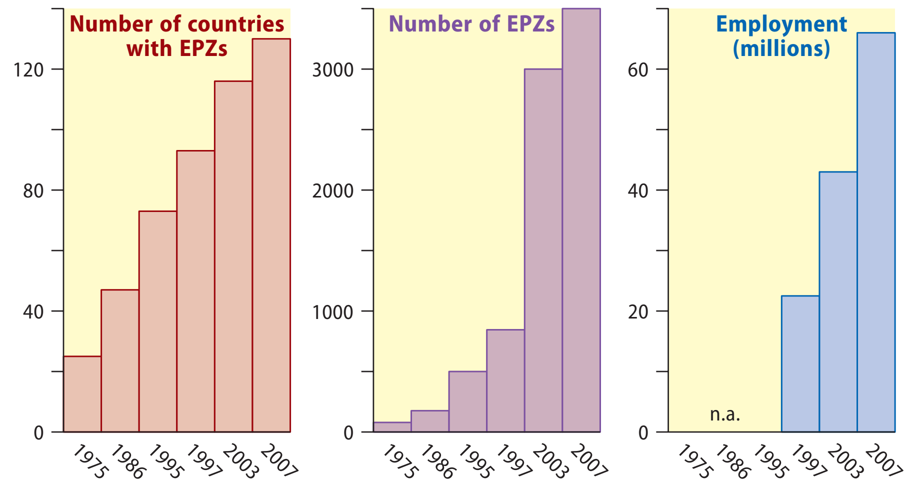

Figure 6.14 Growth in EPZs

Source: ILO, 2003: Table 1; 2007a: pp. 1–2

Variations on a theme

The recurring theme running through the development of all NIEs is the central involvement of the state. But its precise nature varies, a reflection of each country's particular historical, cultural, social, political and economic complexion.[56] In some cases, state ownership of production has been very substantial; in others it has been insignificant. In some cases, the major policy emphasis has been upon attracting FDI; in others FDI has been tightly regulated and the emphasis placed on nurturing domestic firms.

As we noted earlier (Figure 6.13), NIEs in East Asia and Latin America initially followed similar, though distinctive, 'paths to industrialization'. Of the two geographical areas, the East Asian NIEs have been significantly more successful in creating dynamic economies.[57] Three examples from East Asia can be used to illustrate how the state has been involved in each case.

South Korea (the Republic of Korea) came into being in 1948, following partition. From 1910 to 1945, Korea was a Japanese colony, very tightly integrated into the imperial system. Between 1948 and 1988, when political liberalization occurred, South Korea was governed by a succession of authoritarian, military-backed and strongly nationalistic governments that operated a strong state-directed economic policy articulated through a series of five-year plans.[58] Indeed, 'South Korea [represented] perhaps the strongest form of the developmental state among the three [East Asian NIEs].'[59] Two important developments during the 1950s helped to provide the basis for industrialization: the land reform of 1948–50, which removed the old landlord class and created a more equitable class structure; and the redistribution of Japanese-owned and state properties to well-connected individuals which helped to create a new Korean capitalist class.[60]

A powerful economic bureaucracy was created, with a key role played by a new Economic Planning Board (EPB). At the same time, the financial system was placed firmly in the hands of the state. This highly centralized 'state-corporatist' bureaucracy, in effect, 'aggressively orchestrated the activities of "private" firms'.[61] In particular, the state made possible – and actively encouraged – the development of a small number of extremely large and highly diversified firms – the *chaebol* – that continue to dominate the Korean economy (see page 134).

By controlling the financial system, particularly the availability of credit, the Korean government was able to operate a strongly interventionist economic policy. The *chaebol* were consistently favoured through their access to finance and very strong, long-term relationships were developed between them and the state. From the 1960s Korean policy had a strong sectoral emphasis as the state decided which particular industries should be supported through a battery of measures, including financial subsidy and protection against external competition.

Like Japan at a similar stage in its development, Korea generally eschewed the use of inward FDI to acquire technology. Indeed, Korea adopted the most restrictive policy towards inward foreign investment of all the four leading Asian NIEs. Korean government policy has been to build a very strong domestic sector. As a consequence, the share of FDI in the Korean economy remains very low (Table 2.2).

In the early 1980s the policy emphasis shifted towards a greater degree of (restricted) liberalization. Indeed, much of Korea's traditional industry policy was gradually diluted.[62] Major changes were made in policies of financial regulation, exchange rate management and investment coordination. The formerly tightly controlled financial sector was significantly liberalized and the policy of exchange rate management virtually abandoned. The central pillar of South Korean industrial policy for 40 years – the coordination of investment – began to be dismantled.

When the East Asian financial crisis of 1997 hit Korea, the country's problems – as for the other affected East Asian economies – were attributed by the IMF, and by the Western financial community in general, to an over-regulated, state-dominated economy with excessively close (even corrupt) relationships between government and business. Yet, in the case of Korea, that was no longer entirely the case. It could be argued, in fact, that the Korean government had already gone too far in abandoning the principles on which its spectacular economic growth had been based. Clearly, certain reforms were needed as both the Korean economy itself and the broader global environment were changing. Not least was the need to reform the *chaebol*, which distort the economy by, in effect, 'choking the development of small and medium-sized companies'[63] and which were, themselves, in great financial difficulty. That battle is still being fought. The *chaebol* argue that the proposed reforms will leave them vulnerable to foreign takeover; the government argues that reform of cross-shareholdings will make them more competitive. The issue of 'foreign takeover' remains, however, a very sensitive issue in Korea as a whole.

Singapore demonstrates a very different model of industrialization, albeit one in which the state has also played a dominant role.[64] Singapore is by far the smallest of all the East Asian NIEs: a city-state with a population of only around 5 million. Like both Korea and Taiwan, it had a very long history as a colony (in Singapore's case as a British colony). But it was less tightly integrated into its imperial system, although its strategic geographical position gave it a highly significant role as a commercial *entrepôt*. Singapore became fully independent in 1965 when it separated from Malaysia. Since then, although Singapore is a parliamentary democracy, it has been governed by one political party (the People's Action Party).

From the outset, the Singapore government pursued an aggressive policy of export-oriented, labour-intensive manufacturing development. Concentration on manufacturing – especially labour-intensive manufacturing – was adopted because of the need to reduce a very high unemployment rate in a society that, at the time, had one of the fastest population growth rates in the world. The twin pillars of the policy were those of complementary economic and social planning, the latter being much more overt than in other East Asian NIEs.

In contrast to both Korea and Taiwan, the central pillar of Singapore's export-oriented strategy was attracting FDI.[65] As a result, the economy has become overwhelmingly dominated by foreign firms (Table 2.2). The most explicit industrialization measures, therefore, were those of incentives to inward investors, using a sectorally selective process. The government agency responsible was the Economic Development Board (EDB), which still plays an extremely influential role in the Singapore economy. With a few exceptions, Singapore operated a free port policy with little use of trade protectionist measures. The second set of direct measures used to promote industrial development was the establishment of a high-quality physical infrastructure.

At the same time, a series of *social policy* measures was introduced aimed at creating an amenable environment for foreign investment. Most notably, the labour unions were effectively incorporated into the governance system: 'Strikes and other industrial action were declared illegal unless approved through secret ballot by a majority of a union's members. In essential services, strikes were banned altogether … These labour market regulations resulted in the creation of a highly disciplined and depoliticised labour force in Singapore.'[66] Thus, through a whole battery of interlocking policies, the Singapore government created a very high-growth, increasingly affluent, industrialized society in which foreign firms played the dominant economic role in production but within a highly regulated political and social system.

Today, Singapore promotes itself as a global business centre on the basis of the very high quality of its physical and human infrastructure, its strategic geographical location and its business-friendly policies. Government policy incorporates an explicit strategy to 'regionalize' the Singaporean economy by encouraging domestic firms to set up operations in Asia, while Singapore develops as the 'control centre' of a regional division of labour. The government introduced a series of initiatives using government-linked corporations to develop major infrastructural projects in Asia and, more broadly, to develop international networks.[67] At the same time, the emphasis on high-technology research and development and technological upgrading[68] has intensified with, for example, specific emphasis on biotechnology to enhance its already significant role as a pharmaceuticals centre and on IT. Two recent policy initiatives have been the greater liberalization of the financial system and a push for greater 'Asian regionalism'. The key question, however, is the extent to which this highly paternalistic state is able to loosen its grip on the country's political and social life without damaging its economic influence.

The dominant role of the state is, of course, most obvious in the case of *China*.[69] The People's Republic of China (PRC) came into existence in 1949 with the replacement of the nationalist government by a communist government led by Mao Zedong. For the next 30 years, China followed a policy of economic self-reliance. This policy was pursued through a series of major, often extreme, measures. Initially, the new government followed the example of the Soviet Union in establishing a Five-Year Plan (1953–57). This relatively successful policy was jettisoned in 1958 when Mao announced the 'Great Leap Forward': a total transformation of economic planning, with the emphasis on small-scale and rural development. Although this initiated rural industrialization, the Great Leap Forward had disastrous consequences, including mass famine. In 1966, policy changed again with the introduction of the 'Cultural Revolution', a phase that lasted for some 10 years with, once more, disastrous human and social implications.

The period after Mao's death in 1976 was one of political hiatus that was eventually resolved by the emergence of Deng Xiaoping as leader. It was under Deng's leadership that China began to jettison the self-reliance policy of the previous 30 years and to make links with the world market economies. This has been done, however, without substantial political change. In the words of the new Party Constitution of 1997, it is 'Socialism with Chinese characteristics'; in our terminology, it is an *authoritarian capitalist state*.

The pivotal year was 1979, when China began its 'open policy' based upon a carefully controlled trade and inward investment strategy. This was set within the so-called 'Four Modernizations' (concerned with agriculture, industry, education, and science and defence). A central element was the opening up of the Chinese economy to foreign direct investors. As we saw in Chapter 2, FDI has grown very rapidly indeed in China since the early 1980s and now accounts for 10 per cent of GDP (Table 2.2). The organizational form of these investments varies from wholly owned foreign subsidiaries to equity joint ventures with Chinese partners and other partnership arrangements.

A distinctive feature of the open policy has been the explicit use of *geography*. Partly in order to control the spread of capitalist market ideas and methods within Chinese society, and partly to make the policy more effective through external visibility and agglomeration economies, FDI was originally steered to specific locations. Initially, these were the four Special Economic Zones (SEZs) established in 1979 at Shenzhen, Zhuhai, Shantou and Xiamen (Figure 6.15). Significantly, each of these was located to maximize their attraction to investors from overseas Chinese, notably in Hong Kong, Macau and Taiwan. The Chinese SEZs offered a package of incentives, including tax concessions, duty-free import arrangements and serviced infrastructure. The original SEZs were located in areas well away from the major urban and industrial areas in order to control the extent of their influence. However, since the mid-1980s, there has been considerable development and geographical spread of Economic and Technological Developments Zones (ETDZs), as Figure 6.15 shows.

Despite massive inflows of foreign capital and technologies, China remains a centrally controlled economy in which state-owned enterprises (SOEs) predominate,

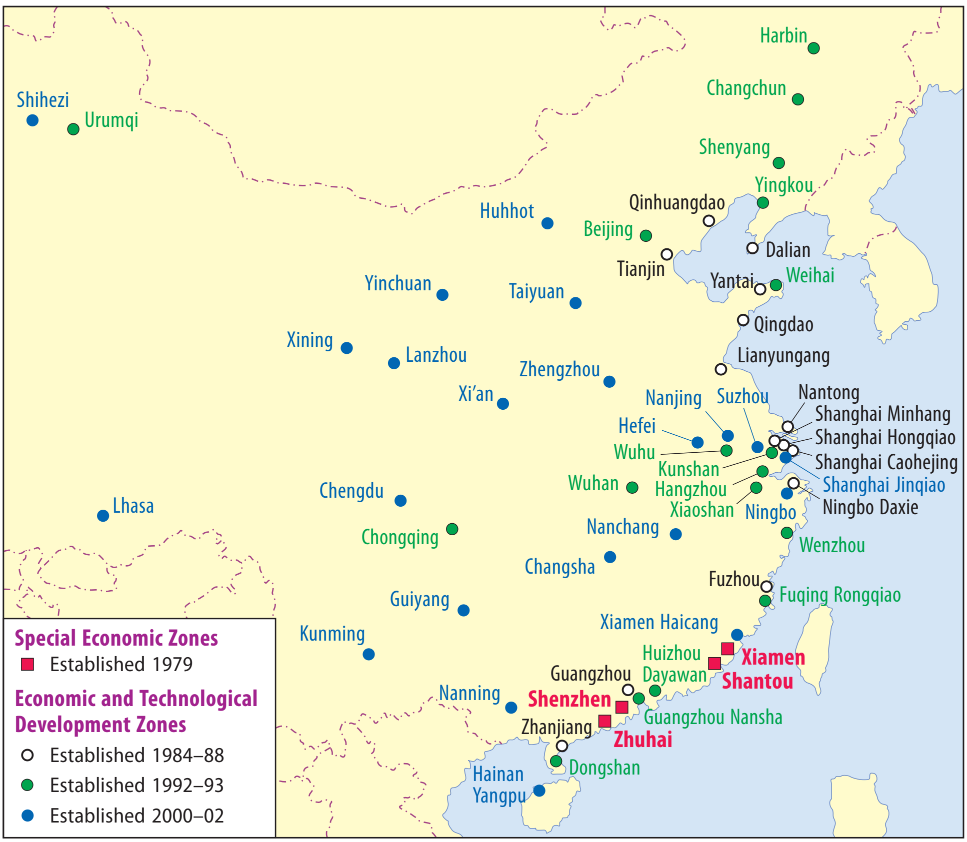

Figure 6.15 The geography of China's 'open policy'

despite more than halving in numbers. Reform of the SOEs is an immense task and one surrounded by massive controversy. A major problem for a country trying to 'modernize' its economy is the sheer inefficiency (by Western standards) and high levels of corruption in many of the SOEs. SOEs are embedded within the Communist Party system and this fact pervades their operations.[70]

The problems posed by the SOEs were intensified with China's accession to the WTO in 2001. Although this greatly enhanced China's economic potential it also imposed severe stresses on the domestic economy and institutions. Not only have tariff levels fallen from their previously high levels, thus exposing Chinese enterprises to intense competition, but also NTBs, matters relating to intellectual property rights, safety regulations, financial and telecommunications regulations were all affected. It is notable that the Chinese government now actively encourages Chinese businesses to invest overseas and there have been a number of significant Chinese acquisitions of foreign businesses, notably the IBM PC business by Lenovo in 2004. Financially, China continues to be under pressure to revalue the *renminbi*, not least because it has the largest trade surplus in the world.

Overall, the institutional structure of the Chinese economy is in a state of flux, with a greater variety of forms. As in the past, however, the key lies in the internal political power struggles between the 'modernizers', who wish to sustain and develop the open policies of the recent past, and those who wish to retain a degree of isolation. So far, China's reform policies have proved remarkably successful. But the key test of the survival of such policy is its continued success in delivering economic growth and raising incomes for the majority of Chinese, and not just those in the more developed parts of the country. For a country so large geographically, so populous and still heavily rural, this is a very tall order indeed:

> China has an unsustainable growth pattern and it will have to pay a cost in the form of slower growth … To make its growth sustainable China must shift to a new growth pattern that relies more on domestic rather than external demand and consumption instead of investment, especially real estate investment.[71]

In this context, the arrival of a new president, Xi Jinping, in 2013 is highly significant for the next decade of Chinese economic development. In a speech to a Business Forum in Hainan in 2013, Mr Xi asserted that

> 'China will sustain relatively high economic growth, but not super-high economic growth … would protect the lawful rights and interests of foreign-invested companies and ensure their rights to equal participation in government procurement and independent innovation … China will never close its doors to the outside world.' Mr Xi said a slowing of the pace of growth would help China rebalance its

economy towards a domestic-consumption-led model rather than an export-driven model, something it has been trying to achieve for years. 'It does not mean that we cannot maintain economic growth at a very fast pace, but because we don't want it any more.'[72]

STATES AS COLLABORATORS

As we saw in an earlier section of this chapter, states – like firms – are competitors in the global economy. But they are also – again like firms – often *collaborators*: involved in trade agreements with other states. Indeed, what the WTO terms *regional trade agreements* (RTAs) have become a pervasive feature of the global economy. At least one-third of total world trade occurs within RTAs.

The basis of RTAs is the preferential trading arrangement (PTA). Technically, PTAs are not necessarily 'regional', that is involving states that are geographically proximate. They simply involve states agreeing to provide preferential access to their markets to other specified states wherever they are located – primarily through tariff reductions, at least initially. However, the WTO uses the term *regional trade agreement* for all such arrangements. RTAs have a two-sided quality: they liberalize trade between members while, at the same time, discriminating against third parties.[73]

The proliferation of regional trade agreements

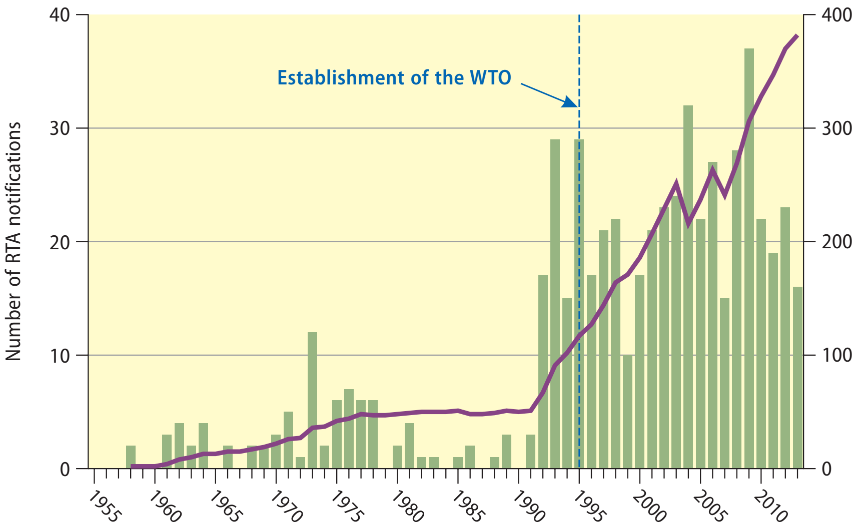

Figure 6.16 The acceleration in RTAs

Source: WTO data

There has been an especially marked acceleration in RTA formation since the early 1990s (Figure 6.16) and the development of a complex tangled web of interstate connections (Figure 6.17). Most have a strongly defensive character; they represent an attempt to gain advantages of size in trade by creating large markets for their producers and protecting them, at least in part, from outside competition. There is also an undoubted 'bandwagon' effect: a 'fear of being left out while the rest of the world swept into regionalism, either because this would be actually harmful to excluded countries or just because "if everyone else is doing it, shouldn't we?"'.[74]

Despite a widespread view that RTAs are a relatively new phenomenon they have been an important feature of the global economic landscape since the middle of the nineteenth century. But their basis and their nature have changed over time. Historically, four 'waves of regionalism' can be identified:[75]

- During the second half of the nineteenth century there were a number of trade agreements in place, especially in Europe: for example, the German *Zollverein*, the customs unions between the Austrian states, and between several of the Nordic countries. 'As of the first decade of the twentieth century, Great Britain had concluded bilateral arrangements with forty-six states, Germany had done so with thirty countries, and France had done so with more than twenty states' (p. 596).
- After the disruption of the First World War (1914–18) a new wave of regional arrangements occurred but, this time, in a more discriminatory form. 'Some were created to consolidate the empires of major powers, including the customs union France formed with members of its empire in 1928 and the Commonwealth system of preferences established by Great Britain in 1932. Most, however, were formed among sovereign states … The Rome Agreement of 1934 led to the establishment of a PTA involving Italy, Austria and Hungary. Belgium, Denmark, Finland, Luxembourg, the Netherlands, Norway, and Sweden concluded a series of economic agreements throughout the 1930s … Outside of Europe, the US forged almost two dozen bilateral commercial agreements during the mid-1930s, many of which involved Latin American countries' (p. 597).
- Since the end of the Second World War (1939–45) there have been two distinct waves of regionalism. 'The first took place from the late 1950s through the 1970s and was marked by the establishment of the EEC, EFTA, the CMEA, and a plethora of regional trade blocs formed by developing countries. These arrangements were initiated against the backdrop of the Cold War, the rash of decolonisation following World War II, and a multilateral commercial framework, all of which coloured their economic and political effects' (p. 600).
- A further wave of economic regionalism – from the late 1980s onwards – occurred in the drastically changed geopolitical circumstances of the collapse of the Soviet-led system and the increased uncertainties of a more fragmented political and economic situation. 'Furthermore, the leading actor in the

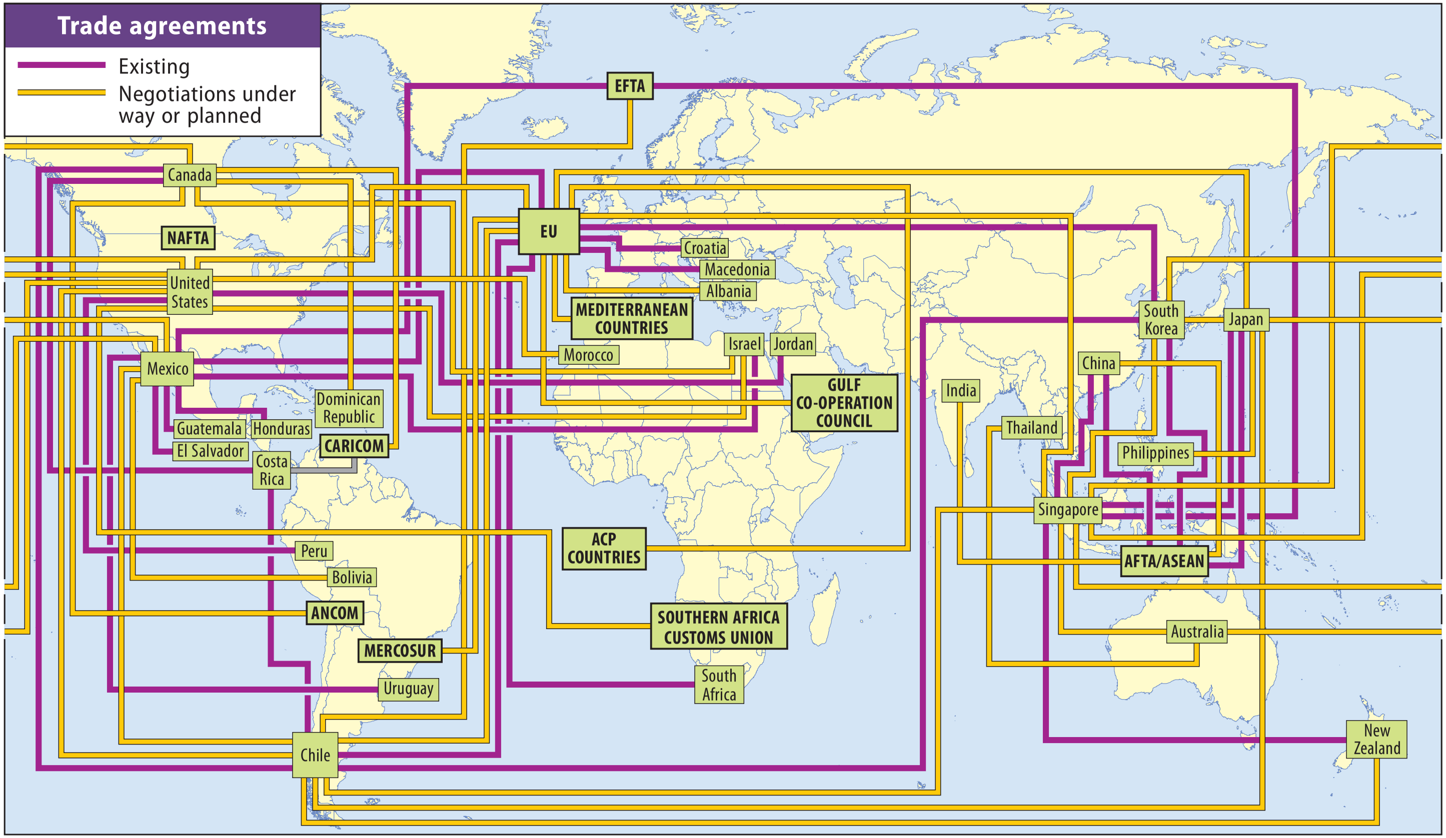

Figure 6.17 The tangled web of RTAs

Source: based on WTO data; *Financial Times*, 19 November 2003; press reports international system (the US) is actively promoting and participating in the process. PTAs also have been used with increasing regularity to help prompt and consolidate economic and political reforms in prospective members, a rarity during prior eras. And unlike the interwar period, the most recent wave of regionalism has been accompanied by high levels of economic interdependence, a willingness by the major economic actors to mediate trade disputes, and a multilateral (that is, the GATT/WTO) framework' (p. 601).

Types of regional economic integration

RTAs come in a variety of shapes, sizes and degrees of integration. As Figure 6.18 shows, the progression is cumulative: each successive stage of integration incorporates elements of the previous stage, together with the additional element that defines each particular stage.

Levels of economic integration	Free Trade Area	Customs Union	Common Market	Economic Union
Removal of trade restrictions between member states	✓	✓	✓	✓
Common external trade policy towards non-members		✓	✓	✓
Free movement of factors of production between member states			✓	✓
Harmonization of economic policies under supra-national control				✓

Figure 6.18 Types of regional economic integration

Most RTAs fall into the first two categories shown in Figure 6.18: the free trade area and the customs union. Indeed, around 90 per cent of all RTAs are free trade areas. There are a small number of common market arrangements, but only one group – the EU – comes close to being a true economic union. In fact, not only is there enormous variation in the scale, nature and effectiveness of these RTAs, but also there is, in some cases, a considerable overlap of membership of different groups. Figure 6.19 shows the major regional integration agreements currently in force.

What effects do such RTAs have? The classic economic analysis of their trade effects identifies two opposing outcomes:

- *trade diversion* which occurs where, as the result of regional bloc formation, trade with a former trading partner (now outside the bloc) is replaced by trade with a partner inside the bloc;
- *trade creation* which occurs where, as the result of regional bloc formation, trade replaces home production or where there is increased trade associated with economic growth in the bloc.

In addition, regional trading blocs have a major influence on *flows of investment* by TNCs. The effects of regional integration on direct investment, like that on trade, can also be conceptualized in terms of 'creation' and 'diversion'. In the latter case, the removal of internal trade (and other) barriers may lead firms to realign their organizational structures and value-adding activities to reflect a regional rather than a strictly national market (see Figure 5.17). This, by definition, 'diverts' investment from some locations in favour of others.

Regional group	Membership	Date(s)	Type
EU (European Union)	Austria, Belgium, Bulgaria, Croatia, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Poland, Portugal, Romania, Slovakia, Slovenia, Spain, Sweden, UK	1957 (European Common Market) 1992 (European Union)	Economic union
NAFTA (North American Free Trade Agreement)	Canada, Mexico, US	1994	Free trade area
EFTA (European Free Trade Association)	Iceland, Lichtenstein, Norway, Switzerland	1960	Free trade area
Mercosur (Southern Cone Common Market)	Argentina, Brazil, Paraguay, Uruguay, Venezuela (2006)	1991	Common market
ANCOM (Andean Common Market)	Bolivia, Colombia, Ecuador, Peru, Venezuela	1969 (revived 1990)	Customs union
CARICOM (Caribbean Community)	Antigua and Barbuda, Bahamas, Barbados, Belize, Dominica, Grenada, Guyana, Haiti, Jamaica, Montserrat, St Kitts and Nevis, St Lucia, St Vincent and the Grenadines, Suriname, Trinidad and Tobago	1973	Common market
AFTA (ASEAN Free Trade Agreement)	Brunei Darussalam, Cambodia, Indonesia, Laos, Malaysia, Myanmar, Philippines, Singapore, Thailand, Vietnam	1967 (ASEAN) 1992 (AFTA)	Free trade area
China–ASEAN Free Trade Agreement	Brunei Darussalam, Cambodia, China, Indonesia, Laos, Malaysia, Myanmar, Philippines, Singapore, Thailand, Vietnam	2010	Free trade area

Figure 6.19 Major RTAs

Regional integration within Europe, the Americas, East Asia and the Pacific

In Chapters 2 and 5 we identified a strong tendency for a disproportionate share of global production, trade and FDI to be 'regionalized'. Such geographical concentrations reflect, first and foremost, the basic economic–geographical processes of preference for proximity to markets and suppliers and a general tendency to 'followership' in location decision making. But there are also rather different kinds of regional integration agreement in each of the three major regions.

The EU

> The European Union is the duck-billed platypus of the political world: a curious-looking animal that defies simple categorization. Some people think it resembles a bird, others a reptile or a mammal. Similarly, everyone interprets the EU according to their own preconceptions rather than seeing it for the singular institution it is.[76]

The EU is by far the most highly developed and structurally complex of all the world's regional economic blocs. Although initially established as a six-member European *Economic* Community (EEC) in 1957, it was always – and remains today – more than simply an economic institution. The EU is a *political*, as well as an economic, project. Indeed, the initial stimulus was the desire to bring together France and Germany in such a way that their traditional enmities could no longer find their outlet in another round of European wars and also to strengthen Western Europe in the face of the perceived Soviet threat. Figure 6.20 shows how the EU

Figure 6.20 The EU: from 6 to 28 members (and beyond?)

has grown from its original 6 member states in 1957, to 12 in the 1970s and 1980s, 15 in the 1990s, 25 in 2004, to its current 28 member states.

Since the early 1990s, four developments have been especially important for the EU.

The *first* significant development was the completion of the *Single European Market* in 1992. Almost 40 years after the Treaty of Rome, individual countries were still resorting to tactics which prevented, or delayed, the import of certain products from other member nations through the use of various kinds of NTB. The Single European Act aimed at the removal of the remaining physical, technical and fiscal barriers; the liberalization of financial services; the opening of public procurement; and other measures. Such internal liberalization and deregulation, it was argued, would create a virtuous circle of growth for the European Community as a whole, its member states and for those business firms successfully taking advantage of the changes.

The *second* major development in the EU since the early 1990s was the *Treaty on European Union* (TEU), signed at Maastricht in 1991. This introduced a far more ambitious political agenda, aimed at creating a fully fledged *economic union*. In particular it:

- strengthened social provisions by (a) the incorporation of the Social Charter, (b) the enlargement of the EC Structural Funds, (c) the creation of a new Cohesion Fund to assist poorer areas of the Union;
- set out the mechanisms for the creation of a single European currency and monetary union (EMU).

European Monetary Union (the *eurozone*) came into effect in 1999, when 11 (later 12) of the 15 member states joined the system. Today, 18 of the 28 member states are in the eurozone. The issue of monetary union, and the adoption of a single European currency (the *euro*), crystallized some of the most difficult political problems within the EU, notably the sensitive issue of national sovereignty. Within the eurozone national control over monetary policy – notably the setting of interest rates – has been passed upwards to the European Central Bank (ECB) based in Frankfurt. The ECB, therefore, has an immense influence over the economies of individual member states. Each member state in the eurozone has to comply with the Stability and Growth Pact, which sets limits on permissible budget deficits and debts. We will return to the problems within the eurozone towards the end of this section.

The *third* major development was the dramatic *enlargement of membership* from the mid-2000s to 28 states, with the potential of further enlargement. In this regard, the most contentious outstanding applicant is Turkey. The majority of the new members were previously embedded within the Soviet-dominated system, with very different recent histories and socio-political structures from the existing EU members. Others are smaller countries like Cyprus and Malta. Significantly, the income gap between existing and new members was much wider than in previous rounds of enlargement. The average GDP per head of the 10 new members in 2004 was only 46.5 per cent of the existing EU average. This compares with the average of 95.5 per cent for Denmark, Ireland and the UK, when they joined in 1973, and the 103.6 per cent for Austria, Finland and Sweden on their accession in 1995. Such huge income differences pose massive problems for the already stressed EU budget.

The greatly increased size and diversity of EU enlargement make the process of consensus in decision making even more difficult, hence the *fourth* major development was the implementation of the Lisbon Treaty on 1 December 2009. This was an immensely tortuous and contested process over several years, with a number of states refusing to ratify the original 'EU Constitution'. The result was a considerably less ambitious structure but one that, nevertheless, involved some important changes. In particular, the position of the European Parliament was strengthened with greater powers regarding EU legislation, the EU budget and international agreements. National parliaments were to have greater involvement, especially in ensuring that the EU only acts where it will result in better results than would occur at the national level (the principle of 'subsidiarity'). The aim was to create 'a more efficient Europe, with simplified working methods and voting rules, streamlined and modern institutions for a EU of 27 [now 28] members and an improved ability to act in areas of major priority for today's Union'.[77] Significantly, it made it possible for a member state to leave the EU.

Political–economic integration in the EU is unique in its extent and depth. Many – though not all – of the economic policies of individual member states have been 'relocated' to the supra-national EU level. For example, there is just one EU trade commissioner representing the EU in the WTO and in all other international trade negotiations. There are EU-wide policies on competition, on subsidies (both industrial and agricultural) and on investment incentives. On the other hand, there are significant areas where policy is set at the national level: for example, in labour markets and taxation.

However, even in areas of 'common' EU policy, the differing ideological positions of individual member states clearly affect the process of reaching consensus. Trade negotiations, for example (including issues relating to the Common Agricultural Policy – CAP), have become increasingly contested within the EU, with a sharp divide opening up between states with a more protectionist stance (notably France, but also Poland) and those espousing more open trade policies (notably the UK and some of the Northern European states). In the sphere of competition policy, as well, there is much heated argument over the acquisition of domestic firms even by firms from other EU member states.

In the post-2008 world, not surprisingly, major cleavages have developed within the EU, both between members of the eurozone and between the eurozone and the other EU member states. The pros and cons of a single European currency were always finely balanced. The major benefits are the reduced costs and uncertainties associated with having to deal with many separate currencies within a single market and the overall stability this is intended to produce. Set against this is the fact that an individual state's ability to use monetary mechanisms to deal with periodic economic crises is hugely reduced. Such constraints on national freedom of manoeuvre become especially apparent during major financial crises, as has happened since 2008. Massive crises developed, initially in Ireland and Greece, necessitating large-scale bailouts of both economies. Bigger EU economies, notably Spain and Italy, as well as Portugal, have been drawn into the financial morass and others may well follow. The ECB undertook to take 'whatever measures were necessary' to sustain the eurozone but the cost has been draconian austerity measures imposed on struggling economies as the price of financial help. The tension between the EU's strongest economy, Germany, and these states has become acute.

The result is the intensification of social tensions within and between EU states:

> The big challenge is unemployment and growth. About 26m people are out of work across the EU and the unemployment rate for the 17-nation eurozone has hit a record 11.8 per cent … Worse, the eurozone-wide rate conceals stark country-by-country differences. Joblessness is still near two-decade lows in Germany but in Spain and Greece one-in-four people are out of work with the rate nearing 60 per cent among those under 25 … These social strains have started to be expressed in a rekindling of smouldering separatist and regionalist tensions … Many countries are experiencing the most severe economic crises in living memory … The social contract around which a country coalesces may become increasingly strained.[78]

Inevitably, therefore, there is intense speculation about the future of the euro itself and, more broadly, over the future shape of the EU as a whole. In the case of the euro, some argue that it will inevitably fail; others that it will survive, primarily because 'they underestimate Europe's deep political commitment to the euro's survival, in some form or other … The euro will neither fail nor succeed. Defective but defended, it will simply endure.'[79] One distinct possibility is that the 'geometry' of the EU will change, perhaps into a three-tier structure:

> The first tier will probably – as France and Germany are proposing – have its own budget separate from the EU budget, to help countries that suffer economic shocks or are introducing painful structural reforms … A second tier, consisting of countries that aspire to join the euro, is already known as 'eurozone plus'. This group, which includes Poland, will accept much of the same supervision of budgetary and economic policy as the first tier … The third tier will consist of the UK and a few others that do not wish to give up any more economic

> sovereignty. They will, however, wish to remain involved in the single market, trade policy, farm policy, foreign policy cooperation and other things that the EU does.[80]

Of course, this is all speculation. Only time will tell how the EU will turn out.

The Americas

Whereas the history of political–economic integration in Europe has been one of progressive deepening and widening – albeit with many interruptions and uncertainties – the history of attempts to create regional integration agreements in the Americas has been far more fragmented and shallow. To a great extent, this reflects the overwhelming dominance of the USA in the region and the fact that, until very recently, the USA had chosen not to enter into bilateral or regional trading arrangements. It reflects, too, the limited success of Latin American countries in creating robust and lasting regional agreements. The picture in the Americas, therefore, is of a mosaic of regional trade agreements of different type and scope (Figure 6.21).

The *North American Free Trade Agreement* (NAFTA) is by far the most important RTA in the Americas. By integrating two highly developed countries (the USA and Canada) and one large developing country (Mexico) into a single free trade area it radically changed the economic map of North America. The NAFTA came into force in 1994, but its origins can be traced back into the 1980s. One important building block, although this was not its intent, was the Canada–US Free Trade Agreement (CUSFTA) signed in 1988 and implemented in 1989. As the CUSFTA was being signed, two other developments were also occurring. President George Bush (Senior) had made freer trade with Mexico a campaign issue in 1988. At the same time, President Carlos Salinas of Mexico made clear his determination to negotiate a free trade area with the USA. Within a short time of bilateral talks starting, Canada had joined in an obvious defensive response.

The arguments in favour of creating the NAFTA varied among the three parties. For the USA, it formed part of its long-term objective of ensuring stable economic and political development in the western hemisphere and also gave access to Mexican raw materials (especially oil), markets and low-cost labour. The Canadian government was anxious to consolidate the recent CUSFTA. The motives of the Mexican government were primarily to help to lock in the economic reforms of the previous few years, to create a magnet for inward investment, not only from the USA but also from Europe and Asia, and to secure access to the US and Canadian markets.

The aims of the NAFTA were gradually to eliminate most trade and investment restrictions between the three countries over a 10- to 15-year period. The possibility of other countries joining the NAFTA was left open to negotiation. The NAFTA is not a customs union; it does not incorporate a common external trade policy. Each member is free to make trade agreements with other states outside the NAFTA. In contrast to the EU, political–economic integration is minimal so that, unlike the EU, there are no social provisions within the NAFTA.

Figure 6.21 The mosaic of RTAs in the Americas

The NAFTA remains a highly controversial issue in all three countries. Against the claimed benefits of an enlarged economic space (from both a production and marketing point of view) is set a number of concerns. In the USA, there were particular worries about environmental and labour impacts. In the latter case, a former presidential candidate, Ross Perot, offered the spectre of a 'giant sucking sound' as jobs left the USA for Mexico.[81] A similar fear was expressed in Canada. One politician saw the NAFTA as a 'nightmare of US continentalists come true: Canada's resources, Mexico's labour, and US capital'.[82] In Mexico, the fear was expressed that the country would become even more dominated by the USA. The jury remains divided.

Not surprisingly, attempts to create a Central American Free Trade Agreement (CAFTA) between the USA and four Central American countries (Costa Rica, El Salvador, Honduras, Nicaragua), plus the Dominican Republic, have been far from smooth. Although the legislation was passed in the USA in July 2005, the agreement has not been fully implemented. The major opposition has come from US labour organizations and sugar farmers fearing job relocations to the cheap-labour economies (and poorer working conditions) of Central America. On the other hand, CAFTA is seen as being a way for Central American producers of sugar and of garments to gain better access to their biggest markets. In fact, unlike the NAFTA, which removed most US barriers to imports from Mexico and Canada, 'CAFTA largely makes permanent the access Central America already has to the US market … under the Caribbean Basin Initiative … in exchange for significantly greater access to the Central American market.'[83]

In contrast to the USA, Latin America has a long history of attempts to create free trade areas and customs unions, dating back to 1960 with the establishment of the Latin American Free Trade Area (LAFTA).[84] As Figure 6.21 shows, there has been a complex overlapping of bilateral and multilateral agreements between Latin American countries. Some of these agreements have failed to develop, notably the LAFTA, despite its reinvention as LAIA (Latin American Integration Association) in 1980.

Two Latin American regional integration agreements have had rather more staying power: the Andean Community and Mercosur. Of the two, *Mercosur* is the more significant.[85] It was established in 1991 with the intention of liberalizing trade between the four founding member states, establishing a common external tariff, coordinating macroeconomic policy and adopting sectoral agreements. Economically, Mercosur has certainly increased the degree of internal trade.

In some respects Mercosur has some features in common with the EU. Like the EU, one of its primary motivations was to deal with security relationships between Argentina and Brazil (a parallel with the Franco-German relationship in Europe). It certainly goes some way beyond a simple free trade area (such as the NAFTA). On the other hand, Mercosur does not have any of the supra-national institutions that are at the heart of the EU:

> Conflict continues to plague the organization because of a lack of coordinated economic policies and supranational institutions. Deepening of the integration process has slowed because member

> states have not established common mechanisms for coordinated macro-economic policy nor have they truly committed themselves, despite the rhetoric, to establishing a regional institutional framework … rather, loose regulations and shallow institutionalism have been maintained at a relatively low political cost … Put simply, the member states of Mercosur want the maximum economic and political benefits from integration while foregoing as little sovereignty as possible.[86]

Looming over all attempts to create a more vigorous regional economy in Latin America is the USA, which aspires to create a pan-hemispheric Free Trade Area of the Americas (FTAA), encompassing North, Central and South America. So far, progress in the negotiations involving 34 countries have stalled. Partly to subvert an FTAA, there are counter-moves to create a South America Community of Nations, whose core would be a merger, over 15 years, between Mercosur and the Andean Community.

East Asia and the Pacific

Regional trading arrangements in the Asia-Pacific are much looser, less formalized and more open than the EU and NAFTA.[87] Until 2010 there were two main regional economic collaborations (AFTA and APEC) and a host of bilateral agreements. The *ASEAN Free Trade Agreement* (AFTA) was initiated in 1992 between the ASEAN countries. ASEAN itself had been established in 1967 as a group of four, then six, South East Asian countries (Singapore, Malaysia, Thailand, Indonesia, the Philippines, Brunei). ASEAN's membership grew to 10 countries in the 1990s, with the addition of Cambodia, Laos, Myanmar and Vietnam (see Figure 6.22):

> ASEAN as an intergovernmental institution established to promote regional cooperation, offers a striking contrast to the Western institutions such as EU and NAFTA … it is … based on a different concept of institutionalisation …
>
> Paying full respect for the sovereignty and independence of each member state is one of the fundamental principles of the Association … most of the decisions have been made by consensus through the 'consultation based on the ASEAN tradition', which means to negotiate and consult thoroughly till achieving an agreement …
>
> [The] mechanism for dispute settlement also reflects ASEAN's preference for an informal approach. This is a striking contrast with the Western approach to dispute settlement in which preference is clearly on the side of judicial settlement based on clear rules and binding decisions.[88]

Such a system has both strengths and weaknesses.[89] A strength is that it has helped what is a very diverse group of countries to maintain positive relationships. A weakness is that a firm and rapid response to problems is often difficult, especially in light of the principle of non-interference in domestic matters of member states. ASEAN has had only limited success in stimulating economic activity. As a consequence, in 1992, the original six member states agreed to initiate an ASEAN Free Trade Agreement (AFTA).

Increasing competitive pressures on the ASEAN region from other East Asian countries (notably China) has forced the organization to look towards making agreements with other countries in East Asia. Some ASEAN members, notably Singapore, have negotiated bilateral trade agreements with China, South Korea,

Figure 6.22 The China–ASEAN Free Trade Agreement

Japan, and with the EU, the USA, Canada, Mexico and Chile. However, the China–ASEAN agreement (Figure 6.22), which came into being in January 2010, is at a different scale:

> The deal creates the third largest regional trading agreement by value after the European Union and the North American Free Trade Agreement, covering countries with mutual trade flows of $231bn (€161bn) in 2008 and combined gross domestic product of about $6,000bn … However, the deal remains short of genuine free trade. The trade in goods agreement provides for each country to register hundreds of sensitive goods on which tariffs will continue to apply, in many cases until at least 2020.[90]

At the same time, a free trade agreement has been reach between ASEAN, Australia and New Zealand. An agreement has also been negotiated with India to establish an Indo-ASEAN free trade area by 2012.

The other major regional economic organization in East Asia is the Asia-Pacific Economic Cooperation Forum (APEC), established in 1989 on the initiative of the Australian government. Figure 6.23 shows the extremely diverse composition of

Figure 6.23 **The Asia-Pacific Economic Cooperation Forum (APEC)**

APEC. It includes not only the obvious East and South East Asian states themselves (including China and Taiwan), but also Australia and New Zealand on the one hand and the USA, Canada, Mexico, Peru and Chile on the other. However, APEC is, so far, little more than a broadly based 'forum' and little real progress has been made in fulfilling its stated goal of 'open regionalism'. Particularly following the Asian financial crisis of 1997, APEC became increasingly criticised by Asian participants:

> APEC's failure to provide any meaningful response to the biggest economic crisis in the Asia-Pacific region since 1945 made it, if not irrelevant, then less important for many Asian members … Increasingly, Asian observers evaluated APEC as a tool of American foreign economic policy. And the resistance of Asian policy makers to a strengthened APEC was caused by their fear of US dominance … APEC has not been successful in creating a joint identity as the basis for further pan-Pacific cooperation and the lack of tangible benefits has been progressively criticized … APEC has failed to provide much needed political legitimacy for the wider regional liberal economic project.[91]

At its summit meeting in 2012, APEC's 21 members promised to find ways of stimulating economic growth but in rather vague ways.

This failure of APEC has led to various initiatives within East Asia to create a more robust regional economic (and financial) framework. None, so far, has come to fruition.

Potential Transatlantic and Trans-Pacific Initiatives

The development of new regional trade agreements continues. For example, the EU is discussing one such agreement with Japan (it already has a recent agreement with Korea). The USA, likewise, continues to explore various bilateral trade agreements. But the most ambitious proposals are those involving a possible US–EU agreement and a US–Asia-Pacific agreement. Formal negotiations between the EU and the USA began in early 2013 over a potential *Transatlantic Trade and Investment Partnership* (TTIP):

> A deal to abolish tariffs, remove regulatory barriers and create an integrated marketplace could add about 0.5 per cent annually to national income on either side of the Atlantic. It would also establish the US and EU as the pre-eminent standard-setter for the rest of the world … [However] getting rid of tariffs will be the easy bit … Delve deeper into the worlds of competing standards and cultural preferences, intra-company trade, competitive tax regimes or intellectual property rights and defining a free trade area becomes almost a metaphysical exercise.[92]

Negotiations over a *Trans-Pacific Partnership* (TPP) agreement involve Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, USA and Vietnam. Although less ambitious than the TTIP, it is likely to take some considerable time to negotiate and implement. Of course, neither project may actually happen, given the complexity of the politics (both domestic and international) involved. The current atmosphere of distrust between the USA and others over the revelations of the wholesale monitoring of communications by US intelligence agencies (helped, to a degree, by the UK) certainly does not augur well. This should remind us that, even though such projects are ostensibly economic in focus, they are, like all such projects, fundamentally *political*.

NOTES

1 Weiss (1998: chapter 1).
2 This was the term coined by the novelist Tom Wolfe in *The Bonfire of the Vanities* (1988).
3 Jessop (1994).
4 See Gilpin (2001), Gritsch (2005), Hirst et al. (2009), Hudson (2001), Jessop (2002), Wade (1996), Weiss (1998, 2003).
5 Kelly (1999: 389–90; emphasis added).
6 Rodrik (2011).
7 Gritsch (2005: 2–3). Nye (2002) also addresses the question of 'soft power' in the context of the geopolitical position of the USA.
8 Glassner (1993: 35–40).
9 Agnew and Corbridge (1995) and Taylor (1994) discuss the general notion of states as 'containers' and the nature and significance of territoriality and space in geopolitics.
10 See Granovetter and Swedberg (1992), Lee (2009), Smelser and Swedberg (2005).
11 Terpstra and David (1991: 6).
12 Hofstede (1980).
13 A study of 700 managers across a large number of countries confirmed the persistence of significant cultural differences (*Financial Times*, 15 October 2004). See also Drogendijk and Slangen (2006).
14 Schwartz (1994), Drogendijk and Slangen (2006).
15 Yao (1997: 238).
16 Jacques (2012: chapter 5) provides an extensive discussion of these issues.
17 See Berger and Dore (1996), Brenner et al. (2010), Hall and Soskice (2001), Hollingsworth and Boyer (1997), Peck and Theodore (2007), Whitley (1999, 2004).
18 Peck and Theodore (2007: 750–8).
19 Rothkopf (2012).
20 Hollingsworth and Boyer (1997: 266, 267–8).
21 Peck and Theodore (2007: 756).
22 Wolf (2008: 1).
23 Rothkopf (2012).
24 Cerny (1997: 251).
25 Hudson (2001: 48–9; emphasis added).
26 Hudson (2001: 76).

27 Cerny (1991: 174).
28 Brookings Institution (2009), www.brookings.edu/articles/2009/03_g20_stimulus_prasad.aspx.
29 Keynes (2007). See Skidelsky (2010).
30 Mortimore and Vergara (2004) and Mytelka and Barclay (2004) discuss FDI policies with particular reference to developing countries.
31 *Financial Times* (25 April 2008).
32 Gilpin (2001: 201).
33 List (1928).
34 Mazzucato (2013) provides an excellent analysis. See also Chang (2011: chapter 12).
35 Mazzucato (2013: 3).
36 Peck (2001: 10).
37 Faux and Mishel (2000: 101).
38 See Gilpin (2001: chapter 7).
39 See Chorev (2007).
40 See, for example, Beath (2002).
41 Contributors to Vitols (2004) explore the extent to which the 'German model' is sustainable.
42 Gretschmann (1994: 471).
43 Accounts of Japanese economic policy are provided by Dore (1986), Johnson (1985), Porter et al. (2000).
44 *Financial Times* (13 September 2013).
45 Mathews (2009: 9–10). See also Yeung (2014).
46 See, for example, Rodrik (2011).
47 Gereffi (1990: 18).
48 Gereffi (1990: 21).
49 Gereffi (1990: 21).
50 Gereffi (1990: 22).
51 ILO (2003, 2007a), Farole and Akinci (2011).
52 ILO (2003: 1).
53 ILO (2007a).
54 ILO (2003: 1).
55 ILO (2003: 2).
56 Douglass (1994: 543).
57 Yeung (2014) explores the relationship between East Asian developmental state policies and global production networks. Henderson (2011) and Studland (2013) discuss variations in economic policy within East Asia.
58 Especially useful accounts of Korean industrialization policy are by Amsden (1989), Chang (2007), Koo and Kim (1992), Pirie (2012), Wade (1990, 2004).
59 Yeung (2014: 85).
60 Koo and Kim (1992).
61 Wade (2004: 320). See also Amsden (1989).
62 See the detailed analyses provided by Chang (1998a), Pirie (2012).
63 *Financial Times* (17 July 2013).
64 Singapore's developmental policies are discussed by Lall (1994), Ramesh (1995), Rodan (1991), Yeung (1998, 2006a,b,c, 2014).
65 Yeung (2014: 86).

66 Yeung (1998: 392).
67 See Yeung (1998, 1999, 2006b,c).
68 Coe (2003b), Yeung (2006a).
69 Spence (2013) provides a comprehensive account of the development of modern China. See also Benewick and Wingrove (1995), Crane (1990), Jacques (2012), Nolan (2001), Zheng (2004).
70 Nolan (2001).
71 Yu Yongding, quoted in the *Financial Times* (23 January 2013).
72 BBC News Business (8 April 2013).
73 Mansfield and Milner (1999: 592).
74 Schiff and Winters (2003: 9).
75 Mansfield and Milner (1999: 595–602). Numbers in parentheses refer to pages in this work.
76 Thornhill (2008).
77 www.europa.eu/lisbon_treaty/glance/index_en.html.
78 *Financial Times* (23 January 2013).
79 Cohen (2012: 689).
80 Grant (2012).
81 Lawrence (1996: 72–3).
82 Quoted in McConnell and MacPherson (1994: 179).
83 *Financial Times* (23 February 2005).
84 See Grugel (1996), Gwynne (1994), Kaltenthaler and Mora (2002).
85 This discussion of Mercosur is based upon Kaltenthaler and Mora (2002).
86 Kaltenthaler and Mora (2002: 92, 93).
87 Bowles (2002), Dieter and Higgott (2003), Haggard (1995), Hamilton-Hart (2003), Higgott (1999).
88 Liao (1997: 150–1).
89 Narine (2008).
90 *Financial Times* (2 January 2010).
91 Dieter and Higgott (2003: 433).
92 Stephens (2013).

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