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Contents

THE ASIAN DEVELOPMENTAL STATE AND THE FLYING GEESE PARADIGM

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Abstract

East Asian economies have been subject to theoretical debates, especially regarding the principal factors that have contributed to their impressive development performance. Many economists familiar with the region's institutional particularities believe that their catching-up process has much to do with the role of the neo-mercantilist state, often embedded in the concept of the developmental state. On the other hand, the recent phenomenon of regional industrial dynamism, most clearly after the mid-1980s, has drawn attention to the concept of the Flying Geese paradigm. The question at hand is compatibility between the neo-mercantilist concept of the developmental state based on nationalist sentiment on the one hand, and the neo-liberal concept of the Flying Geese (FG) paradigm based on market rationalism on the other. In a sense, this resembles the old state vs. market debate. The paper contemplates an outlook of the developmental state in the light of growing regionalist drive in East Asia. More specifically, it explores the possibility of developmental regionalism. Developmental regionalism, in our framework, upholds a hybrid of limited liberalism at the national level and protectionism at the regional level. It is also a hybrid of North-South and South-South cooperation for achieving agreed specialization. While our discussion is at the exploratory stage with respect to concrete policy implications, developmental regionalism could contribute to bridging the aforementioned two contending concepts.

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INTRODUCTION

The impressive development performance of East Asian economies has historically been subject to various theoretical debates. As opposed to mainstream neoclassical observers,[1] many heterodox economists who are familiar with the region's institutional particularities believe that their remarkable performance has much to do with the role of their state, rather than (or in addition to) that of market forces.[2] The analysis of the Asian model of development has usually carried out in the framework of the national economy. Metaphorically, the model can be seen as a fabric woven from various threads, such as good macroeconomic management and stability, a competent bureaucracy, symbiotic state-business relations, publicly controlled financing for development, industrial policy in a broad sense, etc. – which are closely related to the state. In short, the East Asian development has been attributable considerably to the region's individual developmental states.

On the other hand, the recent phenomenon of regional dynamism, particularly after the mid-1980s, has also attracted renewed intellectual attention, where the framework of the Flying Geese (FG) paradigm has often been used to explain the region-wide catching-up process. Here, it is postulated that hierarchically lined-up regional economies are systematically recycling comparative advantage through the "orderly" migration of industrial activities. It is implicitly assumed that late industrializers can catch up – sooner or later – rather than permanently remain underdeveloped, provided that they relate themselves with early industrializers along market rationalism.[3]

The question at hand is how the nationalist concept of the developmental state can coexist with the regionalist concept of FG paradigm.[4] It may well be that the concept of the developmental state and the concept of the FG paradigm are sequential in the national development process, where the former, an important concept at the early stages of development, tends to be taken over by the latter at the later stages. This paper argues that many elements of the developmental state still are (and should remain) relevant in the framework of the FG paradigm. Its main objective is to explore the question as to how East Asian states can transform their policy measures in order to make their national economies better fit in the evolving regional context.

The remainder of this paper consists of the following parts. Section I introduces the prototype concept of the developmental state, particularly focusing on its Asian (notably, Japanese) version. Section II presents a summary of the historical evolution of the FG paradigm. Section III discusses how the geopolitical context of post-World War II (post-war) international relations (most importantly the United States position) has affected the Asian developmental states. Section IV, the heart of this paper, explores the

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[1] The neoclassical orthodoxy accounts for the rapid and successful development of major East Asian economies as a result of market-driven, export-led industrialization coupled with cheap labour, realistic exchange rates and *minimal* state interference (Yoshimastu, 2003: 65). It is thought that their states have allowed comparative advantage in international trade to direct the allocation of productive resources. By creating stable, non-inflationary and open economic environments, these states have encouraged to take advantage of low unit labour cost and engage in labour-intensive export oriented production (Burkett and Hart, 2000: 25). For a thoughtful discussion on the applicability of the "neoliberal model" to Asian economies, particularly those in the first-tier NIEs in this paper, see Brohman (1996).

[2] Radice (2009: 1153) explains: "Given the marginalization of dependency theory and of Marxism more broadly in the past twenty years, the DS [developmental state] became by 1990 the major ideological rallying point for those who wish to contest the appropriateness of neo-libealism and the Washington Consensus as a framework for effective governance and economic development in the global South."

[3] In this regard, the FG paradigm, in contrast with underdevelopment (dependency) theory, holds a more optimistic outlook of modernization perspective. Modernization theory explains the transformation from a traditional/agricultural society to a modern/industrial society as an inevitable evolution, even though some factors within the society may contribute to some delay of the evolutionary process.

[4] In a similar fashion, scholars have pointed out the tension between the notion of nationalism and that of globalism (globalization) (for further discussion, see Bandelj and Sower, 2010).

role (potential and real policy implications) of the state in the FG paradigm. The conclusion sums up the principal elements of the preceding discussions.

I. THE DEVELOPMENTAL STATE: WHAT IS IT?

A. Historical background

The idea that the state should play a central role in economic development stretches back to the pre-modern mercantilist period. In general, the reality of market failure (including imperfect market competition, necessity of public goods, positive and negative externalities resulting from production and consumption, etc.) has long been identified as the principal justification for state intervention.[5] And more recently, i.e. since the Keynesian revolution of the 1930s, the idea of an interventionist state for macroeconomic counter-cyclical fine-tuning, particularly in coping with involuntary unemployment, became an accepted norm.[6]

In the early post-war period, the period of anti-colonialism, general enthusiasm toward development theory designated the states as the essential agent of development in newly independent countries. As a result, the states in most of these countries undertook the initiative of development planning, often within a five-year planning horizon. As a matter of course, these states were involved extensively in various aspects of the national economy, with policy and institutional initiatives, for instance, fixing prices of goods and services, as well as regulating labour, foreign exchange, and financial markets. Partly due to the influence of socialist thinking, many states also built up large state-owned enterprises (SOEs) in public utilities, nationalized mining and agricultural operations.

The concept of the developmental state is based on the assumed role of the state in facilitating the structural transition from a primitive/agrarian to a modern/manufacturing society. The developmental state is meant to play the social engineering role (i.e. the role of restructuring the national economic system) for promoting long-term (industrial) development. In many cases, the facilitation of growth – the prerequisite for the structural transition – is based on the emergence of an agricultural surplus that can be transferred to the emerging modern sector. The whole scheme of thought here reminds us of the dualist model of Lewis (1954) where the "modern" (manufacturing) sector is indispensable as it absorbs labour from its "primitive" (agricultural) sector. Industrial policy, the core of the developmental state's policy actions, is to nurture a competitive and dynamic manufacturing sector, or industrialization in short.

It has been thought that the manufacturing sector has a special role in growth due to its greater scope of generating high levels of productivity (particularly at early stages of development) and externalities (Weiss, 2011: 2). Evans (1995: 7–8) argues that the main objective of the developmental state is to encourage a country's production structure to move up to higher rungs on the industrial ladder, thereby occupying better niches higher up, in the global division of labour. The developmental state is also committed to resolving conflicts in the on-going process of social restructuring as it tends to induce winners and losers. Conflict management in this regard involves ensuring that the benefits, or expected benefits, of the process are widely shared (Chang, 1996). Thus the state is expected to facilitate the process of restructuring, ideally in such a way that would not adversely affect efficiency and productivity (UNCTAD, 2009: 33–34).

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[5] It is understood that market failure occurs when the market fails to allocate resources efficiently, thereby creating a deviation from the general equilibrium that is expected in perfectly competitive markets (UNCTAD, 2009: 32). The state whose intervention is very "routinized" in a systemic fashion may be called a regulatory state, which is concerned mainly with setting the rules of the game rather than with shaping outcomes (UNCTAD, 2009: 29). For an authoritative survey on the economics of development which includes a section on the state vs. market debate, see Stern (1989).

[6] The developmental state has been a recurrent subject of debate during different times, in different circumstances and in different geographical locations. Arguably, the peak period of the discussion of the Asian developmental state was the decade from the mid-1980s to the mid-1990s. Routley (2012) provides an excellent literature survey of a wide coverage on the subject.

The developmental state is also understood to be identified with its actual achievement of economic growth, since its legitimacy stems from the significant improvement in standards of living for a broad cross section of society. This association between a state's actions and their outcomes means that it would be difficult to identify a developmental state *prior* to its attainment of successful development. Since no state openly opposes development as such, what we have are developmental states with a wide range of achievement (from a very successful one to a totally unsuccessful one). At any rate, the extent to which policymakers can enjoy broad public support, particularly regarding the right to rule and ensure political order, heavily depends on their ability to contribute broadly to the significant improvements in standards of living. In short, the developmental state is a lot more than a state that implements defensive protectionist measures.

B. The Asian developmental State: contributions of Chalmers Johnson

The discussion of the Asian developmental State, as we usually understand it, has a more recent origin, associated with the types of economic policies followed by East Asian States in the second half of the 20th century. More specifically, it is often related to Johnson's seminal analysis (1982) of Japan's industrial policy.[7] His central contention was that much of Japan's remarkable industrial development – during the 1925–1975 period – was achieved thanks to the role of its state's leadership in the process.[8]

Johnson (1982) explains that the industrial policy undertaken by the Japanese developmental State consists of two basic components: industrial rationalization policy and industrial structure policy. Industrial rationalization policy, which focuses on the micro aspect of the national economy, includes detailed measures for the operation of specific industrial sectors or individual firms, with the intention to improve their operational efficiency. He notes that industrial rationalization policy has appeared in *every* industrialized country. On the other hand, industrial structure policy (often known as selective or strategic industrial policy) – which is more controversial – concerns the identification of the strategic sectors to be developed as well as the selection of the non-strategic sectors to be converted to other lines of work.

Johnson (1982) explains that Japan's industrial structure policy was based on such standards as income elasticity of demand, comparative costs of production, labour absorptive power, environmental concerns, investment effects on related sectors, and export prospects (Johnson, 1982: 27–28). In concrete terms, industrial structure policy concerns the proportion of agriculture, mining, manufacturing, and services in the country's total production; and within manufacturing it concerns the percentages of light and heavy as well as of labour-intensive and knowledge-intensive sectors. The related policy measures reflect the state's attempts to change these proportions in ways that are deemed advantageous to the country.

In Japan and the Republic of Korea in particular, incentives and resources to guide private sector activities were result-oriented, i.e. contingent upon performance. The adopted performance standards were usually linked to production and trade (export) objectives that could be monitored at the firm level. State support, which often involved contests among firms, was time-limited. To ensure the effective use of state support, firms were made subject, though *gradually*, to the discipline of competition through international markets (UNCTAD, 2009: 34).

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7 Scholars, including Johnson himself, argue that the Asian developmental state is a descendent of Fredrich List, the main representative of the German Historical School, who insisted that Germany needed to take a state-led approach to development in order to catch up with Great Britain (Johnson, 1982: 17).

8 The State's leadership in Japan's catching-up campaign, however, was already seen in the 1870s and 1880s – the early years within the Meiji Period (1868–1912). Furthermore, while Johnson's research focuses on the second and third quarters of the twentieth century is half-century period, Japan's industrial policy obviously did not die off after the period.

The evolution of the developmental State in East Asia has not followed a single path; however, for the institutional characteristics, the prototype Asian developmental State has the following two institutional attributes, namely, competent bureaucracy and embedded autonomy:

Competent bureaucracy: At the centre of the successful developmental State of Japan – as well as those in Taiwan Province of China (Wade, 1990), the Republic of Korea (Amsden, 1989) and Singapore (Huff, 1999) – was a competent bureaucracy of a pilot agency dedicated to devising and implementing a *planned* process of economic development, like Japan's Ministry of International Trade and Industry (MITI).[9] The pilot agency staffed by the country's best human resources, is charged with the task of directing the course of the country's development. Such pilot agencies generally enjoy a high degree of prestige and legitimacy that allows them not only to continue recruiting outstanding personnel, but also to utilize policy tools that tend to give them additional authority. As a result, the aforementioned economies have developed the greatest state capacity not only to formulate development policies but also to implement them effectively.

Embedded autonomy: A competent bureaucracy should be able to maintain effective relationship, especially regarding the direction and funding of industrial investment, with the domestic business sector. In an influential comparative study of industrialization in Asia and Latin America, Evans (1995) coined the term "embedded autonomy" to describe the ideal relationship between the developmental state and the indigenous business sector. According to him, the successful developmental state needs to be sufficiently embedded in society so that it can achieve its development objectives by acting through "social infrastructure", but not so close to business that it risks 'capture' by particular interests.[10]

In the initial stages of the developmental project where the private sector cannot take the effective leadership, the aspiring developmental state – if it has the requisite capacity and vision – is likely to stimulate the development (catching-up) process. The Asian developmental State has also been extensively involved in public investment in education with policies to ensure the equitable distribution of opportunities and wealth (Martinussen, 1997: 239). It should be added that while being capable of maintaining stability, the state has tended to restrain, often in an authoritarian fashion, "growth-compromising" demand from interest groups (such as labour and civil society movements). A developmental state is not always synonymous with authoritarianism, but many Asian states have been authoritarian to a degree (again at the earlier stages of development), perhaps due to the historically-based attitude of Asian paternalism. Authoritarian states have often been accepted, given that they proved capable of achieving both steady high rates of economic growth and structural change in the production system (Low, 2000: 413).[11]

The organizational relations have evolved through distinct historical background within each society as well as its surrounding external context (for further discussion, see section III).

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[9] The central bureaucracy responsible for industrial policy in the pre-war period was the Ministry of Commerce and Industry (1825–1945), which was later replaced by the Ministry of Munitions (1943–1945). In the early post-war period, the Ministry of Commerce and Industry was reestablished, and lasted until 1949 when it was reorganized as MITI. In 2000, MITI was transformed into the Ministry of Economy, Trade and Industry (METI).

[10] A variety of institutional forms have enabled effective information flows between the state and business leaders in East Asia. They include, for instance, blue-ribbon policy consultation bodies, state-sponsored industrial associations, export cartels and inter-personal connections based on lineage, hometown, or "old-boy" network (Chu, 1989: 659). But Japan's numerous "deliberation councils", designed at the sectoral levels, may be an archetype institutional form in East Asia.

[11] It should be noted, however, that authoritarianism covers a wide range of regimes from dictatorships to traditional patrimonial systems. Even fascist and communist states are sometimes referred to as authoritarian. Yet, there is a critical difference between regimes where a cohesive and purposive Weberian bureaucracy exists on the one hand, and regimes where bureaucrats are only personal servants of patrimonial rulers on the other. And both of these regimes may be equally repressive but only the former possesses developmental structures (Vu, 2010: 247).

C. Variations among the Asian developmental States

Among the first-tier NIEs (newly industrialized economies) – the Republic of Korea, Taiwan Province of China, Singapore and Hong Kong (China Special Administrative Region) – in East Asia, the Republic of Korea's interventionist policies in the 1960s and 1970s relied heavily on close consultations between the state (with a notable role played by state-controlled financial sector) and business leaders, and very large diversified corporate conglomerates (*Chaebols*). This closely resembled the Japanese situation with *keiretsu* business groups. [12] In contrast, the state-business relationship in Taiwan Province of China, particularly in its formative years, was more distant and fragmented, largely due to strained relations between the transplanted political structures (bureaucracy and military) from the mainland and the indigenous business elites. As a result, large state-owned enterprises (SOEs) in some key sectors coexisted with smaller firms elsewhere, and with room for the evolution of a good deal of strategic planning in between (Kozul-Wright and Rayment, 2007: 240).

Since its 1959 independence (with the exception of a turbulent 18-month union with Malaysia which ended in 1965), Singapore has maintained one party that dominates electoral politics. Unlike Japan and the Republic of Korea, its successful developmental state has always emphasized economic openness, especially foreign direct investment (FDI), at first chiefly through manufacturing for export and subsequently also as a major exporter of services.[13] Huff (1999) argues that large and growing foreign transnational corporations (TNCs) have helped the Singapore State to exclude the local Chinese business community, previously the main entrepreneurial class, which was predominantly Chinese-educated and oriented towards China (Huff, 1999: 221). Singapore's Economic Development Board (EDB) has grown into an principal agency to deal directly with private investors in line with the city State's overall development strategy (for Singapore's principal policy measures, see section IV).

The second-tier NIEs in Southeast Asia (Indonesia, Malaysia and Thailand) have been faced with typically complex class structures, and they have tended to rely on the continuing importance of resource production. Their natural resource wealth has given rise to agro-based leading sectors in their economies. In comparison with Japan and the Republic of Korea, they have initiated their development with a far more modest role for the state. It is pointed out that the second-tier NIEs have generally adopted a much less demanding policy regime (i.e. less interventionist industrial policy), and concentrated on more conservative macroeconomic management (Kozul-Wright and Rayment, 2007). In comparison with Japan and the Republic of Korea, they have also pursued more liberal trade and FDI policies.[14]

Export-processing zones (EPZs) have been created in many parts of East Asia, particularly in the second-tier NIEs, where foreign firms have been granted various preferential treatments. (In the case of Singapore among the first-tier NIEs, its entirety has been a state-directed export-oriented economy.) The situation led to the rise of numerous export-oriented enclaves. Nevertheless, competition as well as interactions with local firms was deliberately avoided until the mid-1980s (Kimura, 2006).[15] A classic preference treatment was the (partial) exception from corporate income tax. Another policy measure often implemented was

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[12] The State of the Republic of Korea went further down the road than that of Japan, pursuing some of the most selective industrial policies, using an extremely powerful pilot agency (the Economic Planning Board, or EPB) and total ownership of the banking sector. Both of these elements were missing in Japan (Chang, 2010: 83).

[13] During 1980–1989, Singapore received a bigger absolute level of FDI than any other developing country, and during 1985–1995, it drew more FDI per capita than any country, developed or developing, and twice as much as the country ranking second (Huff, 1999: 229–230).

[14] While being much more open to the strategy of utilizing FDI, they remained rather cautious towards foreign firms and tried to place them under tight control until the mid-1980s (Kimura, 2006: 337).

[15] With the Chinese EPZs emerging as effective locations for FDI in the 1990s, the second-tier NIEs rapidly liberalized their FDI regulations. As a result, competition over hosting FDI has become fierce (Kimura, 2006: 338).

to reduce or exempt tariffs on imported capital equipment and components. For instance, tax breaks were given to firms that exported a sizeable portion of their exports.

In the second-tier NIEs, the State-business relationship in those countries is not straightforward, as it is heavily influenced by inter-ethnic distributive pressures and the resulting need to manage challenging political and economic issues at the same time (Woo-Cumings, 1999: 19). While their bureaucracies are not well insulated from these pressures, this does not disqualify them altogether as developmental states. After all, these states have *not* succumbed entirely to business or personal interests, and retained *some* mechanism to encourage a developmental orientation (Hayashi, 2010: 52). Malaysia's attempt at strategic industrial policy did have some success in certain sectors, especially following the adoption of the Industrial Master Plan in the mid-1980s, which strengthened incentives for technological deepening and domestic sourcing of inputs in strategic firms, and sought to strengthen linkages between foreign and domestic firms (Akyüz, Chang and Kozul-Wright, 1998: 20). Thailand, while being less inclined to undertake large scale projects, has rather successfully utilized tariff protection and other measures to promote some selected sectors. While its effectiveness has been hotly debated, Indonesia has retained an important wing of the bureaucracy devoted to developing advanced industrial sectors, such as aviation, automobiles, steel and shipbuilding. Thus, policy interventions in the second-tier NIEs have encouraged the development of an indigenous manufacturing sector. Referring to the second-tier NIES, Jomo (2001: 481) observes:

> There is little doubt that the structural transformation and industrialization of these economies has gone well beyond what would have been achieved by relying exclusively on market forces and private sector initiatives.

In China, the role of the State in industrialization has been historically larger than in Japan and the first-tier NIEs. In the years following the communist revolution in 1949, all industrial firms were brought under public ownership.[16] Initially, economic policy followed the example of the Soviet Union. National Five-Year Plans were introduced, with the physical production goals for all industrial sectors being predetermined and laid down. As in many economies in East Asian, China succeeded in high level of savings, but unlike them all investment in China was done via the public sector. The choice of heavy industrials sectors and the role of the state were linked:

> *Heavy* industries require investment with long gestation period, imported capital goods and large lump-sum investments. In a predominantly agricultural economy, capital is scarce, market interest rates are high, foreign exchange is scarce and the economic surplus is small. In order to make large-scale industrial enterprises possible, one needs distort macro-economic policies (cheap energy prices, low interest rates, low wages, overvalued exchange rates), which require government intervention (Szirmai, 2004: 465).

In December 1978, China announced a policy shift which involved some economic liberalization. It started with a liberalization of the agricultural sector (including the abolition of the commune system) which led to an explosive growth in agricultural production. More far-reaching were the creation of special economic zones (SEZs) and the identification of some areas that have been granted special priority for FDI.[17] When the SEZs were established in 1979 there were strong controls by the State, but since the mid-1980s some policies of market reforms have been progressively introduced, which included more autonomy for firms, and a greater openness to foreign trade (Kiely, 1998: 112).[18] Since the early 1990s,

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[16] Large-scale land reforms were implemented. The land of large landowners was nationalized without compensation and redistributed among the peasants. After that the agricultural sector was collectivized step by step, starting with voluntary cooperatives in the early 1950s and ending with the establishment of immense communes.

[17] In the early 1980s, levels of FDI were relatively low, and concentrated in the service sector and in oil exploration. From the mid-1980s, there was a marked shift toward manufacturing investment, most of which originated from Hong Kong (China SAR) and located in the neighbouring Guandong province.

[18] Firms in the SEZs operated under different rules than those that applied in the rest of the country; they had access to better infrastructure and could import imports duty-free. Rodrik (2011: 152) states: "The SEZs generated incentives for export-oriented investments without pulling the rugs from the under state enterprises."

China has been one of the most dominant FDI recipient countries in the world. Most of this investment remains concentrated in labour-intensive activity, some observers point to the partial shift away from the zones and into the inner-land.

As stated earlier, the second-tier NIEs (and Singapore among the first-tier NIEs as well as recently China) have relied more on foreign investment than their Northeast Asian counterparts. Nevertheless, it should be noted that policy activism on the part of their States – through investment incentives, subsidies and the like – has provided the critical catalyst with which to accelerate the developmental process.

The main conclusion of the preceding discussion is that the developmental state may adopt a variety of specific policy measures. In this regard, one of the clearest divergences in the policy stance adopted by the various developmental states may be seen in their attitude toward FDI.

II. THE FLYING GEESE PARADIGM – A HISTORICAL EVOLUTION[19]

A. Kaname Akamtsu's original Flying Geese paradigm

During the 1930s, a Japanese economist, Kaname Akamatsu, initially sketched out a long span of history involving the evolutionary interrelationships of a developing Asian country (Japan) with the advanced West. His interest was to examine how developing countries in general may catch up with the advanced ones through their mutual interactions. This interest in interactive relationships stands in clear contrast to the dependency school's position with regard to its focus on bi-polar centre-periphery relationships. The term, flying geese, which Akamatsu used for the first time in 1935, came from the graphic presentation of three timeseries curves for a particular product group (or more broadly a particular industrial sector) with the time dimension on the horizontal axis. The curve that appears first represents the import of a product group, the second represents its domestic production, and the third presents its export. They – in an import-production-export (M-P-E) sequence – all rise and fall forming an inverted V or U shape.

In these presentations, the vertical axis indicates the value of import, production and export of the product group in question. Implicitly, therefore, the vertical distance at a specific time between the production curve and the export curve shows the portion of the local production that is domestically consumed. Akamatsu asserted that this M-P-E sequence usually occurs for each product group (or each industrial sector), although the exact shape of each curve and the cascading timing of the sequence depend on the nature of the product group in question as well as the socio-economic conditions of the country at a particular moment of time.

The *geese* in this one-country-one-product model represent these time-series curves, each of them depicting the historical contour of import, production and export, respectively. These three curves together characterize the level of competitiveness of the relevant sector in the country. In other words, the M-P-E sequence for each particular product group indicates the change of competitiveness of the national economy in producing the product group. Competitiveness in production as such does not exist during the period when the domestic market for the product group is supplied totally by imports (i.e. no local production). In due course, competitiveness is expected to rise with the commencement of local production.[20] As the competitiveness rises further, not only are imports being increasingly replaced by

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[19] For detailed studies on the historical evolution of the FG paradigm as well as its interpretations, see Kojima (2000), Kasahara (2004) and Schröppel and Nakajima (2002).

[20] Akamatsu's explanation of industrial development does not rely on changes in relative competitiveness due to different endowments, as modern theorists would predict. It is rather the result of "demand linkages" and "complementarities" of different products. Schröppel and Nakajima (2002: 217) explain: "[I]t is not relative absence of competitiveness in a particular segment of the market, but the presence of complementary products and industries that leads to economic development."

locally supplied products but some excess products eventually also exported (i.e. a vent for surplus).[21] Initially, products are simple, crude and cheap, but gradually the level of quality is elevated. This sort of procedure is repeated, and eventually leads to a process of national economic development with the import of consumer goods being gradually taking over the import of machinery.[22]

Akamatsu warrants that there are many kinds and qualities of consumer goods and capital goods, and the M-P-E sequence occurs not only in connection with capital goods following consumer goods, but also in the progression from crude and simple goods to complex and refined goods (Akamatsu, 1961: 208, and 1962: 16–17). Akamatsu also notes that the product improvement tends to associate with the changes in overseas markets, from a low-income area to a high-income area (Akamatsu, 1962: 17). Thus, Akamatsu's FG paradigm includes 1) the M-P-E trade pattern for consumer and capital goods; 2) the sectoral shifts of production and export from consumer to capital goods, and 3) the inter-national alignment from advanced to backward countries in accordance with their stages of development. As seen above, these four stylized stages already presented rudimentary forms of the multiple sequence of patterns of modern FG paradigm (to be discussed below).

By putting the M-P-E sequence of a late-industrializing country's economy in the context of its trade relations with an advanced country, Akamatsu presented a historical pattern of "dialectical dynamism", i.e. a period of homogenization (in a contemporary jargon, the trend of convergence in comparative costs that impedes trade) repeatedly alternates with a period of heterogenization (the trend of widening

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[21] The commencement of the export phase of local products, which requires overseas marketing efforts, may necessitate local firms (producers) to establish some sort of association with internationally established firms or trading companies. This is the area that modern researchers have extensively explored.

[22] Akamatsu presents a stylized four-stage model of evolving trade patterns of a typical developing country along its development process (catching-up), where the existing manufactured products are clustered into two broad categories: "consumer goods" and "capital goods".

The First Stage (with exports consisted of primary goods, and imports of consumer goods): This is the stage at which a developing country enters the international economy, where the domestic demand dictates the import of consumer goods that cannot be produced at home. The balance-of-payments pressures oblige the country to engage primary goods exports typically to distant developed countries with dissimilar economic structure, rather than to neighbouring (developing) countries with similar economic structures (Akamatsu, 1961: 206).

The Second Stage (with exports made of dominantly primary goods with some consumer goods, and imports increasingly less of consumer goods and more of capital goods and raw materials): At this stage, with its imports being higher profits as compared with domestic industry, the country's domestic situation begins to induce starts local capital to the import-substituting production with the domestic market as an outlet. But capital goods such as machinery must be imported from developed countries for the emerging consumer industries. As a result, the country's imports from developed countries gradually shift from consumer goods to capital goods (Akamatsu, 1961: 206–207). For establishing such domestic industries, there must be an abundant supply of raw materials, which may be obtained domestically or from abroad. In the latter case, not only capital goods but also raw materials must be imported from abroad (Akamatsu, 1962: 14–15).

The Third Stage (with exports made of dominantly consumer goods with some capital goods, and imports of capital goods and raw materials): At this stage, the growth of its consumer goods production makes it possible for the country to begin to export some of outputs, typically light industry products to its neighbouring countries, while it imports raw materials and food staffs from them. The import-substituting production of consumer goods which was initiated by the imports of capital goods develops into export sectors, and the domestic production of capital goods also is slowing beginning slowly (Akamatsu, 1961: 206–207).

The Fourth Stage (with exports whose position being further shifting from consumer goods to capital goods, and imports of consumer and capital goods as well as raw materials): At this stage, the export of consumer goods begins to decline and be replaced by that of capital goods. Meanwhile, imported capital goods are steadily replaced by domestically produced counterparts, and the latter eventually develop into export sectors (Akamatsu 1961: 207, and 1962: 15). However, the domestic production of machinery as well as its exports (typically to other developing countries) may raise tensions with the advanced countries with respect to capital goods exports (Akamatsu, 1962: 15).

What is important in this four-stage model is the generalized evolutionary process of trade patterns along industrial development. After all, in reality, these stages overlap (or coexist with) each other.

divergence in comparative costs that promotes trade).[23] These periods occur as the catching-up countries' economic structures are upgraded (homogenizing), and as the advanced countries themselves in turn strive to introduce innovations in order to stay ahead (heterogenizing). This dynamism – complementary co-acceleration (Akamatsu, 1961: 18) – allows the collective advancement of all trading parties along industrial development. In the early 1940s, Akamatsu developed the concept of relocation process of industrial activities from advanced to developing countries during latters' catching-up process (Schröppel and Nakajima, 2002: 216)

One aspect of Akamatsu's version, which is crucially important to our discussion, is the influence of the German Historical School which emphasized the role of state in the national integration and development through protectionist measures. Akamatsu himself admits that his M-P-E sequence framework was similar to an earlier version formulated by Friedrich List (Akamatsu, 1961: 207). However, Akamatsu was more optimistic about the possibilities of transforming innovations, skills and technologies from advanced to developing countries than List. Whereas List advocated a comprehensive system of protection of new industries from imports, though not the complete prohibition of them, Akamatsu, who regards imports as generally beneficial, argues that imports lead to increases domestic consumption and transfer of product-related knowledge. Both, in turn, lead top domestic production (Schröppel and Nakajima, 2002: 211).

B. Modern versions

The publication of Vernon's (1966) product cycle (PC) theory stimulated modern Japanese theorists to modernize the FG paradigm, although for a while it remained as a matter mostly of academic curiosity (Korhonen, 1994). Furthermore, Kojima's efforts (2000) to promote the FG paradigm led to a "westernization" (by framing it in a neoclassical fashion) of Japanese ideas on economic development as expressed in the FG paradigm (Schröppel and Nakajima, 2002: 217). Kojima explains national development and its accompanying changes in trade pattern in the factor proportions (Heckscher-Ohlin) theorem.[24] One central concept of his argument is the dynamic capital accumulation (via high savings ratio) as incorporated in national factor endowments (Memis, 2009: 43). With the imports of capital (and intermediate) goods, the capital-labour ratio tends to rise, and the economy will shift its productive activities towards the more capital-intensive good (Memis, 2009: 43). In other words, the change in the structure of comparative advantage among Asian countries tends to induce changes in the production and trade patterns (Kojima, 2000).

Vernon's PC theory presented a perspective on a major individual firm with respect to how it makes decisions on the location of its production facilities, by distinguishing products by the degree of their maturation and standardization. The PC theory looks at the location of the production of a particular product during its life cycle. Vernon's argument, in a nutshell, was that when new products develop into mature products and later reach the stage of standardized ones, the production locations (undertaken by the original exporting firms) changes from the United States (the most advanced country) first to other industrialized countries, and later to developing countries. Here outward FDI (thus overseas production) is understood to replace export.

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[23] Akamatsu's "dynamic" framework is built on Hegelian dialectics such that any given national economy, being in perpetual motion, tends to move forward, i.e. to higher stages of industrial development (Korhonen, 1994).

[24] Bernard and Ravenhill (1995: 173–174) explain: "Liberal economists (primarily Japanese, but not exclusively so) have attempted to synthesize aspects of Akamatsu's and Vernon's arguments into a model of East Asian regional development. They have incorporated Akamatsu's discussion of industrial diffusion across nations with Vernon's model direct foreign investment and foreign sourcing of products by innovating firms. The two have in turn been linked to neoclassical notions of comparative advantage to describe a 'rational' pattern of industrial diffusion from Japan to the East Asian newly industrializing countries…, to ASEAN and most recently to China."

As mentioned above, modern FG theorists – mostly Akamatsu's students and particularly Kiyoshi Kajima – developed the original paradigm further by incorporating the PC concept. Kojima presented the FG paradigm in the post-war context in the 1970s, in a wider debate on the role of transnational corporations (TNCs), by integrating the phenomena of Japanese FDI into the paradigm. Kojima added one aspect of Vernon's perspective, i.e. "reverse import" into Akamatsu's framework. Reverse import for a product occurs when its declining domestic production and export are combined with the rising offshore production and (eventual) import from follower countries.

Modern theorists, including Kojima, depict the harmonious mechanism of collective advancement by means of consecutive catchingup efforts. (As mentioned earlier, Akamatsu's dialectic model is not as harmonious as the modern versions.) With the postulation of a pattern of continuously altering product-cyclebased trade, the modern FG paradigm focuses on the regionally contextualized transformation of national economies (thus, macroeconomic in nature) rather than on the strategic behaviour of large firms of the PC theory (thus, microeconomic in nature). The FG paradigm presents large firms (via FDI) as "benevolent" transmitters of industrial knowledge – mostly industry-specific rather than firm-specific – from one national economy to another.

According to modern theorists, the key to the national development and systematic regional integration is the simultaneous occurrence of three types of *orderly* sequence – thus "multiple sequences" – of economic activities within and among national economies:

1. **The product-cycle sequence** of a particular product (or a product group): This sequence explains that the national economy follows the trade framework of the product life cycle, consisting of *four* stages: import, production, export, and finally again import (i.e., reverse import). This is presented in a "single-country-single-product" framework.
2. **The inter-industry sequence** of domestic development: This sequence depicts the gradual development of industries in a manner compatible with a national economy's changing factors and technological capacities (collectively, endowments), meaning that the country shifts the production (thus export) activities from lower value-added, more labour-intensive and less capital-intensive industries to higher value-added, less labour-intensive, and more capital-intensive industries. (Akamtasu touched upon this, but modern theorists are much more elaborating.) This sequence is presented in a "single-country-multiple-product (industry)" framework.[25]
3. **The inter-economy** sequence of regional development: This sequence indicates that the orderly transfer of industrial activities occurs among national economies along regional hierarchy as follower economies come to obtain the endowments most suitable to the transfers of activities. (As mentioned earlier, Akamatsu's "dialectic" inter-economy sequence is much more conflict-prone than modern versions.) This sequence is presented in a "multiple-country-single-product (industry)" framework.

For the sake of historical accuracy, Akamatsu already introduced, though in a much less stylized fashion, these sets of sequences in the 1930s and 1940s. The more recent discourse, as discussed below, tends to concentrate on the last one, the inter-economy sequence (Schröppel and Nakajima, 2002: 211).

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[25] According to Ozawa (2008, 2009), there are five distinctive stages in the inter-industry sequence, as a "flight map" for follower geese to be guided in their drive to catch up on growth. Stage 1 is the endowments-driven (resource-intensive or labour-intensive light industries) stage, such as textiles, raw industrial materials and agricultural products. Stage 2 is the physical scale-driven (capital-intensive, natural resource processing) stage, with mostly non-differentiated products, such as steel and basic chemicals. Stage 3 is the consumer-oriented stage, such as clothing and higher level manufacturing, such as automobile. Stage 4 deals with R&D-based sectors, such as microchips and computers. Stage 5 is Internet-based, such as information services. Under this framework, the most developed stage is currently information technology. Each of these stages goes through the M-P-E sequence, although the mechanism of transition from one stage to the next presents considerable challenges. Ozawa also names these five stages after corresponding economists and entrepreneurs: Stage 1 with Heckscher-Ohlin, Stage 2 with Adam Smith, Stage 3 with Henry Ford, Stage 4 with Joseph Schumpeter, and Stage 5 with Marshall McLuhan (Ozawa, 2008, 2009).

C. Implication on regional integration

The modern versions of the FG paradigm contain a framework of regional development and integration, by adding the dimension of FDI – more specifically, investment from Japan to its neighbours – to the paradigm (Terry, 1996: 188). While Vernon's publication implies a theoretical base for regional integration, it is Japanese theorists that linked various overseas activities of Japanese TNCs (through sub-contracting, licensing arrangement, joint ventures, FDI, etc.) with the theme of regional integration (particularly in East Asia). Kojima (1978) argues that flows of both real and financial assets from Japan combined and sent to follower economies as a package, will augment the benefit of inter-economy linkages. Focusing on FDI, Kojima (2000) asserts that it creates substantial spillover effects:

> Foreign affiliates generate, through backward and forward linkages, support industries and employment. They contribute to developing local entrepreneurship and managerial and technical skills. They improve the quality and morale of labour through training and education. Ultimately, FDI induces 'reform' in production methods, employment systems, business management, and even laws and political organizations (Kojima, 2000: 383).

Such FDI, which began to grow in the 1970s but dramatically accelerated after the mid-1980s, has facilitated Japan's industrial restructuring, scaling down those industrial sectors losing competitiveness, thereby releasing resources for other sectors gaining "competitiveness".[26]

It is pointed out that FDI from Japan ostensibly aids in replicating (regionalizing) the Japanese development pattern in East Asia (Arase, 1994; Hatch and Yamamura, 1996; Hatch, 2010).[27] In this Japan-centric scheme, the role of the Japanese State was to assist the implementation of the FG paradigm as a vehicle of regional integration (ibid.).

Let us note that the imperative perceived in Japan for promoting regional integration has been externally imposed. We witnessed the intensifying protectionist sentiment in the United States and Western Europe in the late 1970s and the early 1980s. It was this external factor that prompted Japan to systematically cap its export surges by means of voluntary export restraints (VERs)[28] as well as FDI in these markets. Furthermore, labour-cost differentials between Japan and a large part of the rest of the East Asian region were widened more in the mid-1980s with the rapid appreciation of the Japanese yen. These factors contributed to the mass exit of Japanese firms from their home. By the end of 1989, Japan accumulated a total of $254.4 billion in FDI outflows. In absolute terms, the United States received the largest amount of Japanese FDI – $104.4 billion (or 41 per cent of the total) – and the EC as a whole received $40 billion (15.7 per cent) (for these data cited and further discussion, see Cai, 2008: 188–219). However, the East Asian economies received the lion's share of Japanese FDI to non-OECD member countries. While the Japanese outward FDI lost momentum after 1990, the shift of investment to East Asia became even more evident, particularly to China. The proportion of Japanese FDI in East Asian total FDI grew from 10 per

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[26] United States FDI dominated the East Asian region in the 1950s and 1960s; however, starting in the late 1960s, Japanese firms were taking an increasingly larger share of regional FDI. Particularly, stimulated by massive trade surplus and the rapid appreciation of the yen (after the 1985 Plaza Accord), Japanese FDI had a big boost.

[27] However, the exact replication of the Japanese development policies in dealing with FDI may turn out to be "self-contradictory". If the East Asian economies faithfully imitated Japan, they would have to put restriction on FDI and make their economies relatively closed. On the other hand, if they emulated the closed system, Japanese firms, which have organized this region as their production sites and markets, would be constrained in their activities. As long as the expansion of Japanese economy is concomitant with the regional development, it is impossible for the East Asian economies to model after Japan (Yun, 2005: 46).

[28] VERs – for specific sectors, such as steel, machine tools, televisions, automobiles and alter chips – were undertaken *not* by Japanese firms alone; many exporters in the Republic of Korea and Taiwan Province of China were also pressured to implement them.

cent in 1991 to 50 per cent in 1997 (Park, 2009: 158). It is important to note that a high proportion of Japanese FDI has been in manufacturing sectors in East Asia.

The exit of manufacturing activities from Japan in the post-bubble decade of the 1990s was partly due to the slower growth in domestic demand. Similarly, first-tier NIEs began to follow Japan's policy footsteps with respect to transferring some of their manufacturing firms (and its domestic sub-contractors) to the second-tier NIEs in the late 1980s.

In sum, Japan's industrial restructuring has provided special incentives to the first-tier NIEs to move into some of Japan's export-oriented industries. Meanwhile, the Japanese State was ready to focus, amplify and sometimes orchestrate the efforts of its business sector (Terry 1996). As mentioned above, the similar restructuring has been taking place in the first-tier NIEs. Thus, the regional industrial restructuring process – which is closely associated with contemporary regional integration – is a "top-down" rather than a "bottom-up" process.

III. CHANGING GEOPOLITICAL CONTEXT FOR THE ASIAN DEVELOPMENTAL STATE

A. United States stance: aid giving for Asian reconstruction and policy tolerance

The successful emergence of East Asian economies cannot be fully understood without considering the context of the Cold War, i.e. the existence of external and internal threats as well as diplomatic, financial and in some cases military aid from the United States (Beeson, 2007; Cumings, 1984; Stubbs, 2009). Here one of the most critical threats must be one from Asian communism.[29] In the early post-WWII period, concern of the United States with geopolitics prompted the strategy to forge a hub-and-spoke network of bilateral security treaties with Asian "front-line" States. This dependence on the United States protection, however, constrained the security policies of the region's States. Furthermore, the region's economies soon came to depend heavily on the United States market, shipping on average 20 to 30 per cent of their exports to it (Tsunakawa, 2005: 105).

Japan, the most important Asian ally of the United States, was a beneficiary of massive, stimulatory procurements resulting from the Korean War – totalling US$3.4 billion, or one-fourth of all United States merchandise imports at that time (Cumings, 1984). Johnson (1982) went as far as to describe massive United States demand for goods and services from Japan resulting from the Korean War as a virtual equivalent of the Marshall Plan for Europe. A similar effect was also seen in the case of the Viet Nam War on the Republic of Korea and Taiwan Province of China. Over the period of 1946–1978, the Republic of Korea received total of nearly $6 billion in t economic grants and loans. During the 1950s alone, the United States aid accounted for five-sixths of the Republic of Korea's imports. The United States military deliveries to these economies in 1955–1978, i.e. excluding the Korean War, totaled $9.05 billion (ibid.).

The Cold War also provided a "relatively" permissible environment in which the Asian developmental States continued to protect and nurture their strategically important manufacturing sectors, while the United States maintained a tolerant attitude toward the neo-mercantilist position of its Asian allies (Harvie and Lee, 2002: 10). Referring specifically to Japan, Beeson (2009: 15) explains: "[The country] was able to take advantage of a rapidly expanding international economy and relatively unfettered access to important markets in Europe and North America, without having to open up its own markets and, crucially, while maintaining control of the domestic financial system." The United States policy to keep its market open

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[29] Particularly for the Republic of Korea and Taiwan Province of China, the perception of extremely intensive and long-term threats emanating from the People's Republic of Korea and China, respectively, played the key role in creating their developmental states. For further discussion on the threat perceptions as an important factor that underpinned their developmental states, see Zhu (2002).

to Asian Allies, particularly to Japan, was to compensate for costs resulting from its insistence to them on not trading freely with China (Pempel, 2005: 8).

The United States's hub-and-spokes alliances through a series of bilateral *security* agreements with its Asian allies allowed (if not encouraged) Japan to take the leadership in directing intra-regional *economic* relations, through the provision of substantial amounts of aid to its neighbours. Japanese official aid, which began in the 1950s as war reparations[30] to several Southeast Asian counties in the 1950, has always been one piece of a broader programme of economic cooperation that included both public aid and private investments (Arase, 1994). In sum, while the Cold War indirectly helped the developmental States to operate in East Asia, it facilitated the emergence of economic regionalism in a particular fashion against this background.

B. Diminishing tolerance, rising criticisms, enforcing pressures

During the 1970s and the early 1980s, the capacity of States in many developing countries was seriously restrained by rising energy prices and recession of the world economy (Bandelj and Sower, 2010: 178). In the 1980s, the international community increasingly adopted the policy stance of neo-liberalism toward economic development. This became particularly prominent in Latin America and Africa after the outbreak of the Debt Crisis in 1982. The previous optimism about the benevolence and competence of the state came under a serious challenge. The emerging perception was that the state itself had become a part of the problem of underdevelopment rather than the solution. Nevertheless, the crisis did not critically affect East Asian countries which, with the overall good performance, could retain their own state-centred pattern of development.[31]

In the 1970s and the early 1980s, the United States administrations had favoured an issue-by-issue approach in negotiating economic disputes with Asian economies (particularly Japan), but such an approach reportedly limited the areas of negotiations. This United States diplomatic approach gradually induced negative publicity in domestic politics. Eventually, changing economic and security circumstances in the mid-1980s prompted the United States to re-evaluate its relationships with Asian economies (Beeson, 2009). Consequently, the United States policy towards Japan shifted in the 1990s to measures designed to open the Japanese market, by pressuring it to make structural changes in the domestic political economy (Hook et al 2001).[32]

As aid money from the West (and the East) became scarce with the ebbing of the Cold War in the second half of the 1980s, the availability of funds to "buy" political ability began to dry up (Fritz and Menocal, 2007: 540–541). However, Japan's aid commitment towards its Asian neighbours remained firm. From the

[30] These reparations typically involved export credits, tied loans, plant exports, and long-term investment projects that relied on Japanese money. As a result, they opened markets for Japanese firms as well as providing tremendous opportunities for personal profits by business and political leaders (Pempel, 1998: 57).

[31] During the 1980s, some innovative approaches emerged as the United States firms strove to achieve greater access to overseas markets. Among these markets, the concern was particularly notable with respect to those in East Asia. For instance, problems of access to the Japanese market were the motivations for the Omnibus Foreign Trade and Competitiveness Act of 1988, which included a provision calling on the President to identify unfair trading partners and to specify products for negotiation with these partners. In 1989, Japan was named as an unfair trading partner and three areas, namely, forest products, telecommunications satellites, and supercomputers, were selected for negotiations. This action exemplified the continuing mood of dissatisfaction over access to Japanese markets at the end of the decade.

[32] They included the MOSS (market oriented, sector specific) talks agree to in 1985, the Structural Impediments Initiative (SII) (1989–1990), the Framework Talks on Bilateral Trade (1993–1995), as well as explicit efforts at "managed trade as a second-best alternative," embodied in the bilateral Semiconductor Trade Agreement (1986 to 1991) (for a detailed discussion, see Hook et al., 2001: 105–117).

end of the 1980s until the start of the new millennium, Japan, as the world's largest aid donor, continued to reserve its aid money largely for Asia neighbours. Hatch (2010) documents:

> Most of this aid was delivered in the form of yen loans for dams, bridges, electricity transmission lines, telephone lines, and other infrastructure projects that are needed to support industrialization. Indeed, it was routinely criticized by other wealthy donor countries for focusing on such development projects rather than humanitarian programs (Hatch, 2010: 80).

In the first decade of the post-Cold War period in the 1990s, the United States, together with its Western allies, propagated further (i.e. to globalize) neo-liberal reforms. The disintegration of the socialist regimes was a decisive factor pushing public sentiment towards the neo-liberal orientation. Japan, being defensive within the donor community, attempted to reverse the increasingly prevalent world sentiment of discounting the role of the state, by financing the World Bank to undertake a major study (World Bank, 1993) on East Asian economic development (for further discussion see Terry, 1996; Wade, 1996).[33]

It was the financial crisis (1997–1998) that finally dealt a serious blow to the image of East Asia. Its formerly praised state-business relationships were now disparaged as forms of outmoded "crony capitalism", and synonymous with corruption and inefficiency (Beeson, 2007). But this critical view was not gain the universal consent.[34] One reason for that was that it could not explain how *some* Asian economies, such as Taiwan Province of China, managed to escape the crisis.

Some observers argued that it might have been the gradual exit of the developmental States in some of the East Asian region – i.e. rapid liberalization of their financial sector – that had invited the crisis. Chang (1998), for example, points out that the cause of the crisis in the Republic of Korea was *not* due to the existence of the developmental state, but due to its disappearance in the late 1980s onward. At any rate, the neo-liberal policy prescriptions came to be viewed as a direct threat to the developmental States in East Asia.

C. Resistance to criticisms

When Thailand and Indonesia appealed for emergency funding in 1997, the International Monetary Fund (IMF) assumed that the East Asian crisis (caused mainly by capital account deficits due to "hot money" flows[35]) was similar to the Latin American crisis in the 1980s (caused by current account deficits due to public debts and high inflation). As a result, the IMF instructed these countries to reduce public spending and open their markets further, to impose higher interest rates, and to force their banks failing to meet the capital adequacy ratio to shut down. The idea was to cut demand and liquidity and encourage foreign investors to deploy their capital to kick-start again the economies in trouble.

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[33] At a more fundamental level, many Japanese economists have long argued that development promotion with extensive protectionist measures have been universally observed at early stages of development for all advanced counties. They argue that neo-liberal ideas are a distortion of the historical reality (for further discussion see Lee, 2008).

[34] Before and after the crisis, Taiwan Province of China, like the Republic of Korea, abandoned key policy tools in the developmental state armory, including planning, widespread public ownership and the selective state direction of private investment. Rapid financial liberalization exposed the entire region of East Asia to speculative risks. Radice (2009: 1167) explains: "[Taiwan Province of China] was protected by its particular role in the very different Greater China miracle."

[35] In the 1990, many of the Easy Asian economies became increasingly open to inflows of highly mobile portfolio capital and short-term lending in a way that was not the case in the earlier period. This was due to the external pressure to follow the neo-liberal orthodoxy and open their capital account, allowing much greater (and unregulated) movements of capital. By the mid-1990s, inflows of private capital grew much faster than public loans (up to 75 per cent of inflow, of which half was highly mobile portfolio capital. Another noteworthy feature that emerged in the 1990s was that much of the debt increased was short term (Beeson 2007: 206–209).

The effects of the crisis on the region's economies turned out to be neither exceedingly detrimental nor long-lasting (with the exception of Indonesia). Many observers now do not subscribe to the idea that the relatively rapid recovery of the region from the crisis was due to either its austerity prescriptions with extensive reform suggestions by the IMF, or the reduced role of their developmental states. Instead, the dominant public opinion in the region was that the excessive intrusive role of the IMF converted the initial currency crisis into a deep economic recession and a social tragedy (Chang, 2008).

Many of the region's leaders shifted blame for the crisis to outside influence, thereby, in a way, justifying their economic policies. According to Higgot (1998), many regional economies that had to endure the austerity policy measures prescribed by the IMF were engaged in a "politics of resentment" toward the organization. One important side-effect of the crisis, Higgot further argues, was a psychological bond among regional leaders on the ground that they were common victims of a major disaster, and that East Asia should become a "single market". Referring to Malaysia's experience during the crisis, Beeson (2007) argues:

> [I]t exacerbated tension between East Asia and the USA, giving renewed life to Mahathir's aborted proposal for an East Asian Economic Caucus (which would ultimately re-emerge as ASEAN+3) and sparking interest in the possibility of developing regional monetary mechanisms with which to ward off future crises (Beeson, 2007: 210).

It could be argued that the strict adhesion to neo-liberal prescriptions, including the element of reducing the role of the state, has considerably lost its potency (Gore, 2000). This is partly because of the poor performance – in terms of growth and distribution as well as stability – of many developing countries in Africa and Latin America in particular as well as economies in transition (former socialist countries) that have adopted extensive neo-liberal policy measures. As mentioned above, the rapid East Asian recovery after the crisis certainly did not revive trustworthiness of the neo-liberal prescriptions; instead, it instigated widespread mistrust of them in the region.

IV. THE ROLE (REAL AND POTENTIAL) OF THE STATE IN THE FLYING GEESE PARADIGM

A. National policy measures related to industry, trade and FDI

As discussed earlier, many East Asian States have been known for their *selective* industrial policy – equivalent to what Johnson (1982) calls industrial structure policy – toward their strategically targeted sectors. They have often used their domestic financial sector (publicly controlled) for providing firms within these sectors with subsidies of different kinds, combined with various trade- and investment-related preferential treatments. Instead of being static, however, the emphasis on policy measures undertaken has been shifted over time within each national economy as well as across different national economies (UNCTAD, 2009). Yet one fundamental point remains unchanged: the States – with the exception of Hong Kong (China SAR) – have been heavily engaged, as the principal agent, in the conflict-prone process of industrial development involving different social actors. This is because, most fundamentally, not all factors of production (i.e. tangible and intangible productive assets) are readily transferable between sectors (Chang, 1996). In general, East Asian States have successfully undertaken the social engineering role of guiding the process of socio-economic restructuring.

Selective industry policy measures once widely used in East Asia were based on a broad industry targeting through administrative regulations and guidance for strategic/priority sectors and firms. These measures were to restrict foreign competitors' access to the domestic market in general or its specific sectors in particular. As noted above, the measures for protecting, and thereby nurturing, the targeted sectors and firms included, among others, financial subsides of various kinds – credit subsidies, production subsidies, tax subsidies, export subsidies, and so forth – together with preferential market licensing, adjustment assistance and manpower training (UNCTAD, 2009: 151).[36] Let us note again that their infant industry protection was accompanied by stringent conditions, such as those of achieving specified export targets with a rigid time limit.[37] Over time, East Asian States have retained some of these measures, but modified (liberalized) or discontinued others.

Trade-related measures[38] include import tariff and non-tariff measures (particularly in earlier days) and export promotion.[39] Tariff measures (import duties) have been structured in such a way (with their drawbacks) as to reduce the pressures from external competition on the one hand, and to facilitate imports of capital goods (machinery) and essential inputs on the other. Typical non-tariff measures on imports, which many Asian States have implemented, include import bans, import quotas, import licensing, and safeguard measures. In a broader definition, non-tariff measures also include public procurement measures (preference of domestic products over imports), foreign exchange regulations and controls, and exchange rate policy. It is anticipated that these import-related measures would enable domestic producers to charge higher prices for their import-substituting products and thus to pay higher wages, thereby inducing labour to move the targeted sectors (Kreinin, 1971: 260). Export promotion measures include overseas marketing via export promotion agencies, export finance/insurance guarantee, export quality management, and export processing zones (EPZs) (UNCTAD, 2009: 151). An important export promotion measure is the maintenance of competitive exchange rates (with occasional currency devaluation). In general, these measures (mostly on imports) have been considerably softened throughout the region.

As for investment-related measures, East Asian States have placed various sectoral restrictions and guidance on domestic and foreign investment, again with some financial assistance to the targeted sectors/firms. Particularly notable are those measures related to *inward* FDI. It is well known that Japan, the Republic of Korea and Taiwan Province of China used to tightly regulate inward FD with strict performance requirements, such as those on technology transfer, local content, and joint venture arrangements and export orientation. As discussed earlier, Cold War geopolitics of the 1950s, 1960s and 1970s presented a tolerant external environment to these economies. In contrast, the second-tier NIEs have been somewhat less protectionist in trade, and more reliant on inward FDI – particularly in the late 1980s and onward with the extensive use of EPZs – as a way of integrating into trade networks regionally and globally.[40] (Let us point out that to some extent, the beginning of rapid growth of the second-tier NIES coincided with the rise of neo-liberalism in the 1980s.)

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[36] Singapore is an exception to this rule, as it has always embraced *foreign* TNCs, with various incentives, as its overall development strategy. Similarly, China could be regarded as another exception, given the fact that its growth in export of manufactured goods has been substantially due to foreign TNCs as well.

[37] It is interesting to note that Singapore has been free from the concern of ensuring firms in receipt of State subsidies to use them in productive. Huff (1999: 225) argues: “Because multinationals came to Singapore almost entirely to export, international pressures to remain competitive answered the need for the market-conforming behaviour enforced by governments in other developmental states … , where subsidized firms were set export targets, but typically lacking in subsidization by soft states. Along with education and training, policies that tied investment incentives to higher technology activities helped to avoid a further potential problem that multinationals would come to Singapore, take whatever subsidies were on offer and then depart, leaving the republic a still decidedly low-wage center.”

[38] Obviously, trade-related measures are not solely for promoting industrialization. Two other principal objectives are: the correction of external imbalance, and the generation of public revenue. The correction of external imbalance (persistent payment deficits) is undertaken by import contraction, export expansion or both. Revenue tariffs (normally duties on imports but also on exports) are quite significant for many developing countries where the domestic authorities have a limited administrative capacity of taxation.

[39] Historically, mercantilist policy occasionally restrained export for security and developmental purposes. For instance, the British State prohibited exports of machinery in order to prevent others (European countries and its own colonies) from catch up with it in industrial development. This prohibition remained in force until the 1830s (Shafaeddin, 2005: 164).

[40] Some observers, particularly those from the dependency perspective, are critical of such integration strategies, arguing that the extensive external dependence on management, technology (capital goods), parts and components have made their development illusory. These critical views, which were dominant in the 1960s and 1970s, have considerably subsided in the recent past.

Generally speaking, the Asian developmental States have sought a process of strategic integration with the world economy, in which the timing, speed and sequencing of opening in relations to different types of international flows was decided on the basis of how they support the national interest in promoting economic growth and structural change (UNCTAD, 2009: 31).

Whereas the policy measures discussed above appear to be most relevant during the early catching-up period, we would argue that the state should remain relevant even later on. As the "advantage of backwardness"[41] is gradually eroded in the course of development, the competitive pressure could rise on the catching-up economy. The situation may become especially critical when the state's policy measures have eventually helped its economy reach the leading edge of production and knowledge. In East Asia, this question is very pertinent to Japan and the first-tier NIEs. Once the advantage of backwardness is fully taken advantage of, the state faces the problem of revising ways for keeping-up, moving ahead, or simply staying ahead of others. Weiss (2000: 27) argues:

> [K]eeping up with the change in the modern industrial economy entails many more important tasks than looking for the next big invention. These tasks include assisting an orderly retreat or restructuring for industries in decline, regaining ground lost to competitors in strategic industries …, maintaining a long-term investment programme for upgrading in mature industries, promoting new infant industries in high technology, as well as tracking areas with new products and technological potential.

Weiss (2000) further argues that the new task of "keeping-up" may entail a different array of policy instruments, but not necessarily the abandonment of a "transformative project". Using the term "transformative state", she argues that the interventionist state needs to remain active with various restructuring measures in the post-catching-up period (Weiss, 2000: 29). In this regard, the emigration of firms (i.e. the outward movement of industrial activities) partly implies the internationalization (regionalization) of the state's development (or restructuring) initiatives, thus not always indicating a weakening of the role of the state (see a further discussion see below).[42]

B. Does the Flying Geese paradigm reflect the weakened state?

Neo-liberals stress that the rise of cross-border economic transactions has resulted from the state's progressive disengagement from market interventions. The developmental state is a transitory (archaic) institution because a range of viable/permissible policy measures have diminished over time. After all, investment decisions are essentially made by firms, and trade is similarly pursued by exporting/importing firms, not by states (Memis, 2009: 34). In this sense, the FG paradigm, as a framework of regional integration, may imply the weakening role of the state.

The FG paradigm postulates that industrial upgrading of all inter-linked economies in East Asia reflects is a process through rational market transactions, where the existing inter-country hierarchy can potentially provide all aspiring states (more importantly, their firms) with a ladder of development starting with the most labour-intensive segments of industrial activities. This is in clear contrast to the dependency argument of underdevelopment resulting from the "centre-periphery" relations. The upgrading of manufacturing activities in the lead economies has opened up opportunities for less developed ones to enter the regional division of labour by picking up less complex activities. Here, it is understood that large firms (rather

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[41] In Gerschenkron's (1962) argument, late-industrializing economies have the opportunities to take over technological know-how from advanced ones, without having to bear the R&D costs of new technologies. They can choose from a tremendous arsenal of new production techniques, which were not available previously. Thus if they are able to absorb new technologies, late-industrializing economies can experience faster economic growth than the early developers. This is the advantage of backwardness.

[42] On the other hand, some observers argue that outward FDI from Japan may be a response, in part, of its firms wishing to escape the obligations and costs associated with the social and institutional organizations of the Japanese economy (Henderson, 1998: 374).

than states) have provided foreign firms with a powerful tool through the transfer of technology and skills. Ozawa (2009) calls it a mechanism of "recycling comparative advantage". According to the FG paradigm as a framework of regional division of labour, the developmental task of the state is being taken over by that of the market (i.e. firms). One implication of this reasoning is that state actions that *defy* the "rational" market in the region are likely to frustrate the collective catching-up process; therefore, the state must be the follower of the market, rather than the other way round. Indeed, it may be argued that the FG paradigm and neo-liberalism share a common "critical" view toward the state.

However, in our view, the reality is more nuanced, mainly because East Asian states have proactively affected regional movements of their firms (FDI and trade).[43] As mentioned earlier, the states of Japan and the first-tier NIEs have promoted outward FDI partly for reducing political tensions with their Western major trade partners (importers). They have also done so with a view to upgrading *their* industrial sectors (and abroad).[44] Japan, and more recently some of the first-tier NIEs, have provided their aid money to East Asian neighbours (and beyond) to develop their local infrastructure, thereby making aid-recipients more accommodating toward newly arriving industrial activities from abroad (for Japan's case, see Arase, 1994). More recently, China, the emerging powerhouse in East Asia, has also distributed massive aid money to its neighbouring economies (as well as to others).

As for host economies of FDI (the second-tier NIEs and China), their States have solicited, in a strategic fashion, investment from abroad with various incentives and conditions. Admittedly, for these economies, industrial immigration (arrival of foreign firms) could complicate the politics of State involvement, particularly when local firms establish alliances (such as joint ventures) with foreign firms. The situation may not follow the classic process of developing/upgrading the *genuinely* local industrial sectors, as joint ventures no longer comprise a *purely* domestic constituency for protection and nurturing. The interests of firms involved (domestic and foreign) are much *less* neatly bound up with the enhancement of local productive capacities. Yet, again, joint venture requirements have been a practical policy choice for promoting higher levels of local sourcing (UNCTAD, 2001: 167).

C. Situating the developmental state in the Flying Geese paradigm

The logic of the FG paradigm (as understood in its typical modern versions) emphasizes the importance of the orderly (market-rational) sequence – nationally and regionally – in industrial development. It is thought to be not rational for any country with an abundant unskilled labour – as the potential basis of its comparative advantage – to try to take up the task of building the capital-intensive high-tech or knowledge-intensive R&D-driven sectors. Instead, it should start out with the lower tiers among such sectors that are commensurate with the local conditions of labour abundance and technological scarcity (broadly "endowments"). The development prescription of the FG paradigm would be: the catching-up economy should act *realistically* in identifying the sectoral targets for promotion, rather than attempt to jump *unrealistically* rungs of the industrial ladder (for further discussion see Lin, 2011). It should be easier for a catching-up economy to pick up those industrial sectors that are losing competitiveness in *slightly* more advanced economies that are *relatively* similar in economic environment.

This does not mean, however, that the state should stand idle, waiting for the "natural" maturation of its economy. Many agree that development will not happen purely through market forces and will need state interventions. Let us recall that Akamatsu, the originator of the FG paradigm, did recognize the role

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[43] A totally different explanation is also possible. A case in point is Japan in particular. From this perspective, the internationalization (including regionalization) of Japanese (Asian) firms is partly due to their desire to escape the social and institutional organization of their home economy (economies) (Henderson, 1997: 374).

[44] Industrial migration strategies may take several forms. The specific destination could be these importers (particularly the United States or Europe), or third countries (typically East Asian neighbours).

of the state in facilitating the transition from import to domestic production (and export) in his M-P-E sequence model, although he did not adequately elaborate on concrete measures that the state ought to take (Akamatsu, 1962: 23).[45] One major area of the current debate on the role of the state on industrial promotion is related to comparative advantage (domestic factor endowments). There are those who argue that state interventions should conform to a country's comparative advantage. UNCTAD (2009), for instance, argues that the state's efforts should be such that the opportunities of current relative cost advantages are exploited to the full but at the same time to promote investment and learning in economic activities where comparative advantage can be expected to lie in the *immediate* future as its economy develops and other late industrializing competitors catch up (UNCTAD, 2009: 31). But there are others who argue that state initiatives should defy its present comparative advantage in order to upgrade its industry (see, for instance, the debate in Lin and Chang (2009)).

While the state has lost some of its traditional regulatory power in the global age, it is premature to dismiss its role in economic management altogether.[46] At the fundamental level, it must maintain an enabling environment for development, i.e. macroeconomic stability with effective counter-cyclical fiscal policy. The state should improve the conditions of the domestic factor markets, perhaps most importantly, the levels of public health and of skills and knowledge of its labour force, and provide effective infrastructure, including power, transport and communications. Needless to say, public security (political stability and order) is indispensable. But the question still remains as to whether some (if not all) of these traditional policy measures discussed earlier can (and should) remain relevant to regional dynamism envisaged by the FG paradigm. We would argue that the state's developmental initiatives could be effective in the regional context.

Contemporary regional trade in East Asia has been dramatically expanded as a result of the development of fragmentation of production (cross-border production sharing), particularly for such products as electronic appliances and automobiles. The entire production of some products involves fragmented production blocs located in different national economies. Thanks to the technological development in transport and communications, they are well linked through intra-industry and/or intra-firm trade. Characteristics of multi-step production processes allow firms in catching-up countries to partition their production activities into "slices". It is no longer necessary for them to master entire production chains and to organize them by themselves. Instead, they can now focus on mastering just one facet of production. This is likely to entail large savings in learning costs and can allow small and medium-sized firms (as local suppliers) to coexist with large foreign firms (UNCTAD, 2002: 74).

But the question still remains as to which facet of production firms should be engaged in. Should it be decided totally by the market? It is known that foreign affiliates tend to source the most sophisticated and complex parts and components either internally or more dominantly from preferred (often foreign-owned) suppliers within or outside host country, depending on the capabilities of local firms (UNCTAD, 2002: 75). Therefore, the efforts on the part of regional states to promote the productive capacities of their local firms, thereby enhancing production linkages with foreign affiliates must remain important (UNCTAD, 2001; Memis and Montes, 2008).

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[45] Unlike many modern FG paradigm theorists, Akamatsu (1961, 1962) did not subscribe to the idea that the ranking order among Asian economies within regional hierarchy is rather fixed.

[46] Regarding state interventions, Biersteker (1990) thoughtfully provides a typology of 4 forms, according which they may be designed to: (1) "influence" (i.e. to promote and/or constrain) private firms' behaviour, (2) "moderate" conflicts among social stakeholders (particularly between capital and labour), (3) "redistribute" social and private products, and (4) "produce" goods and services. He argues that the influence of neo-liberal prescriptions have most clearly effected a reduction in the state interventions in the area of "production". Neo-liberals have pushed the policy prescriptions generally directed against the more extensive forms of state interventions associated with "state capitalism" and Keynesianism (Biersteker 1990: 488).

The intensifying catching-up process within the hierarchical order among regional economies has induced enormous pressures on all of them (most of all, Japan and the first-tier NIEs, but also the second-tier NIEs as well) from below. Given that each rung of the industrial ladder is not occupied by a single economy and that each economy occupies more than a single rung, with China being a case in point for the latter. The process has tended to raise the degree of similarity (convergence) among East Asian economies in the manufacturing structure and production activities, which in turn has raised problematic issues, such as overproduction and dumping practices, all of which have contributed to the region-wide trend of terms-of-trade deterioration.[47] One additional negative consequence is the rise of protectionist measures in the importing countries (outside the region) towards Asian economies as a group. In our view, the framework of strategically cooperative regionalism can somewhat ease the situation, as will be discussed below.

The FG paradigm was explicitly the theoretical foundation when the Japanese State proposed the new Asian Industrial Development Plan in 1987. The plan aimed at promoting industrial development through state programmes such as comprehensive master plans and the guidelines for sector-specific development. Unlike the previous aid programmes directed toward economic infrastructure and humanitarian objectives, the new plan sought to link aid money to fostering export sectors by offering Japan's expertise and know-how in industrial development (Arase, 1994: 129–134; Hatch and Yamamura, 1996: 138–139). Yoshimatsu (2003: 69) argues that Japan continued or strengthened the developmental state approach that sustained steady industrial restructuring, in conjunction with the industrial upgrading of East Asia as a whole. While the plan no longer appears in Japan's overall foreign policy toward East Asia, some of the perceived merits in the plan may have remained among the region's decision-makers.

The following section is an extension of the above discussions on finding a place for the developmental state in the FG paradigm. It will specifically look into the possibility of "development regionalism" as the concept that may provide an intellectual solution.

D. Developmental regionalism: situating national development measures in a regional context

The concept of developmental regionalism[48] frames national development measures – with appropriate modifications – in a regional context. Policy measures under discussion here include, first of all, those that promote "passive" or "shallow" integration. Regional preferential treatments, such as the removal of barriers to trade and FDI, and freer flows of labour, are likely to facilitate regional production networks and supply chains, since they tend to reduce transaction costs and perceived risk (UNCTAD, 2012: 4).[49] This alone underscores the need for regional states to transform traditional domestic development measures into something more appropriate in the regional context. Here, however, let us note that developmental regionalism retains the mercantilist sentiment of protectionism not very much at a national level but more at a regional level. We would also argue that developmental regionalism should go beyond "passive" or "shallow" integration measures. It can aim at "proactive" or "deeper" integration, by means of coordination and harmonization of various policy measures, including state interventions to promote industrial development (Memis 2009). It takes "agreed specialization" or "negotiated specialization"

[47] Memis (2009) argues that given its unique size and nature, one should not expect China to follow exactly the same transformation experiences in Japan and the first- and second-tier NIEs. She expects that shifts in Chinese exports towards more sophisticated products will take a much longer time as compared to earlier experiences of others due to the large labour pool in the interior of the country and restrictions on labour migration between domestic regions.

[48] The term developmental regionalism has not been used extensively. One of the earliest uses was in Nasadurai (2003).

[49] In fact, many East Asian countries, particularly some members of the Association of South East Asian Nations (ASEAN), have implemented "de facto" regional preferential arrangements in trade, by setting the "applied" tariffs for regional imports below the legally announced "bound" tariff rates (Hale, 2011). The regional bias in applied tariffs is driven by regional production networks that must move components and parts across national borders. As discussed later in the text, ASEAN members have attempted to reduce the differences in their own regulatory systems with respect to trade and FDI so as to attain various development gains.

among regional states as an effective method for increasing the complementarity among regional economies and the capacity of their region as a whole.[50]

Given that East Asia is a region of a mixture of vertical (North-South) and horizontal (South-South) integration, developmental regionalism should also follow a dual process of integration. When countries at different stages of development undertake a regional cooperation project (vertical integration), the FG paradigm readily presents a theoretical ground for mutual benefits for all. Here, good diplomatic relations (commercial diplomacy) among counties at different stages of development would be a prerequisite for enhancing market-led growth of the region as a whole. We witness the rapid growth of North-South bilateral agreements on trade and investment within the region, but they are yet to be harmonized. Indeed, regional diplomacy could be complex, as East Asian economies are increasingly operating at similar stages of development (convergence in manufacturing activities), tending to raise the potential of inter-state conflict resulting from rising competition. But the trend only underlines the greater importance of inter-state consultations for reducing political tensions.

Developmental regionalism is probably most pertinent to the more finance-scarce catching-up economies of the region. South-South integration may be a theoretical spin-off of the developmental state, where, as pointed out earlier, the latter's mercantilist sentiment is transformed into a regional context. Practical measures based on development regionalism include resource pooling – such as joint expenditure on human resource development (e.g. education, training and migration) and R&D as well inter-state infrastructure development (e.g. power and transport facilities, as well as trade facilitation) – and the extended regional diffusion of technology. Cooperation based on developmental regionalism would also reduce the costs of exploiting natural resources across national boundaries. South-South developmental regionalism would likely strengthen the collective bargaining power of the states (and firms) in host countries vis-à-vis such powerful foreign firms with their regional industrial plan that may complicate the developmental potential of these countries (UNCTAD, 2002). Indeed, such cooperation would also improve the chance for these states involved to follow their own preferred growth path consistent with their priorities (Kozul-Wright and Rayment, 2007: 312). This could be especially important, as North-South developmental regionalism could be dictated in a "top-down" rather a "bottom-up" fashion.

As stated above, we believe that specialization based on negotiated agreements – in North-South and South-South developmental regionalism – could be a harmonious solution to many contemporary problems in East Asia. What is required is a shift in the states' self-image from as a competitor to as a collaborator. Yet, the regional states must remain collectively competitive vis-à-vis outsiders. The pursuit of such collective efforts could be politicized and time-consuming, but it could contribute to the nourishing of emerging domestic (and regional) firms eventually into internationally competitive ones. In addition, such regional integration could ease the process for foreign firms to realign their organizational structures and value-added activities to reflect a regional rather than a strictly national market (Dickson, 2011: 203).

Developmental regionalism, whether in the North-South or South-South framework, would require the availability of accurate information on levels of productivity and wages among the regional economies. This implies the need for stable exchange-rate relations among local currencies to present "reliable" price signal. Developmental regionalism as manifested in mutual financial support, which is within the policy domain of states, would probably reduce another risk associated with increasing regional interdependence,

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[50] Kojima (2000) suggests "agreed specialization" as a way to create opportunities for all economies in East Asia. While admitting "agreed specialization" as a valid solution in theory, Memis (2009: 30) is skeptical about its validity in practice: "When considered within the context of state business and today's complicated production network nexus, one can easily see that it is unlikely to mobilize common interests on the agreed specialization at the national level."

namely, serious contagion from external shocks as seen in the Asian financial crisis.[51] One important lesson from the crisis was potential vulnerability of regional economies, by highlighting that the then existing institutions – national and regional – for financial management was inadequate. All of these issues have raised the recognition of creating stable financial (foreign exchange and capital) markets.[52] Again, developmental regionalism could be a helpful hint.

In addition, developmental regionalism can lead to the resolution of distorted (unhealthy) investment patterns, including military build-up, emanating from political conflicts. Reduced security tension would allow each member of the region to use its resources for more productive purposes. Recent territorial disputes only highlight the importance of regional consultations for their peaceful resolution. Developmental regionalism can reinforce regional initiatives to maintain social stability by adding social security issues and elements of distribution in its cooperative agendas. By doing so, it could, in the long run, provide the regional economies with certainty and credibility about their future policies and economic environment.

V. CONCLUSION

While some observers continue to argue that East Asian developmental States can still play an important role in directing the course of development, others hold that the institutionalized relationships that were formerly effective have become outdated, and even turned into obstacles to the reforms that are required. It is not totally clear whether the developmental state can remain reasonably functional – i.e. being free of capture by particularistic economic, ethnic or political interests, or capable of guiding the development process. Historical changes in geopolitics have also reduced tolerance of the West (particularly the United States) toward State interventionism in East Asia. The propagation of neo-liberal ideas has also dictated firms, perhaps at the cost of states, to assume greater responsibility for creating the rules and regulations. Nevertheless, we argued that states should not abandon their developmental role, because unilateral liberalization could not only subject the vulnerable domestic economy to overwhelming external competition, but also induce premature deindustrialization (Shafaeddin, 2005). Furthermore, given the fact that each state now has to respond effectively to the challenges emanating from increasingly integrated international economic relations, this requires the capacity of the regional states to handle external shocks singularly and/or collectively.

The modern FG paradigm closely follows the logic of market, postulating that the location of production for tradable products must change in accordance with the development of factor endowments of national economies. The initiatives of the region-wide collective catching-up come from those countries located at the higher positions in regional hierarchy that are shading industrial activities. This mechanism, in our view, is a disguised framework of trickle-down effect. A critical question is whether such a mechanism of rational market together with a limited role of the state would promote long-term development in all of the economies involved. The complex reality of East Asia (with diverse characteristics among regional countries) does not neatly present itself for an orderly catching-up process.

We pointed out that East Asia contains new networks of power and coordination with a mixture of vertical and horizontal integration. The regional policy of the states to pool their political power may be helpful

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[51] The most concrete regional initiative was the Chiang Mai Initiative agreed in 2000, which expanded the existing ASEAN swap arrangements to include all ASEAN members and set up a network of bilateral currency swaps and repurchase arrangements among ASEAN and three major economies in the region, namely Japan, China and the Republic of Korea. The aim of the initiative is to provide additional short-term hard currency for members facing possible liquidity shortfalls. The initiative has also undertaken better monitoring of financial flows, regional surveillance, and training of personnel. The initiative has gone through various reforms to scale up its operation.

[52] Many East Asian economies have strongly supported the idea of increasing the availability of emergency financing during crises and to establish new procedures for timely and orderly debt workouts.

in coping with the pressure from the outside. Thus regional states may have to take a deliberate approach with a properly sequenced set of policies. The FG paradigm would require the successful coordination among region's states where the identification and timing of the industrial migration should be *mutually* understood. Here, traditional mercantilist sentiment of nationalism could be a serious obstacle to regional integration. It is shown that developmental regionalism is a hybrid of two kinds. It upholds a hybrid policy of limited liberalism at the national level and protectionism at the regional level. It is also a hybrid framework of North-South and South-South cooperation for achieving "agreed specialization". While it is still at the exploratory stage, we would argue that the concept of developmental regionalism seems to contain a promising potential in terms of filling the gap between the developmental state and the FG paradigm.

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UNCTAD Discussion Papers

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