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Globalization and the Myth of the Powerless State

The new globalist orthodoxy posits the steady disintegration of national economies and the demise of the state's domestic power. This article, instead, seeks to show why the modern notion of the powerless state, with its accompanying reports about the demise of national diversity, is fundamentally misleading.[1] It is undeniable that striking changes have taken place inside nation-states in recent times. On the social policy front, there has been a decisive move towards fiscal conservatism, whether from the Right or the Left, with reforms to taxation systems and the trimming of social programmes. In the economic sphere, governments have moved towards greater openness in matters of trade, investment and finance. These changes are often represented as prima facie evidence of the emergence of a new global 'logic of capitalism'. According to this logic, states are now virtually powerless to make real policy choices; transnational markets and footloose corporations have so narrowly constrained policy options that more and more states are being forced to adopt similar fiscal, economic and social policy regimes. Globalists therefore predict

convergence on neoliberalism as an increasing number of states adopt the low-taxing, market-based ideals of the American model.[2]

In contrast to the new orthodoxy, I argue that the novelty, magnitude and patterning of change in the world economy are insufficient to support the idea of a 'transnational' tendency: that is to say, the creation of genuinely global markets in which locational and institutional—and therefore national—constraints no longer matter. The changes are consistent, however, with a highly 'internationalized' economy in which economic integration is being advanced not only by corporations but also by national governments. Proponents of globalization overstate the extent and 'novelty' value of transnational movements; they also seriously underrate the variety and adaptability of state capacities, which build on historically framed national institutions. My argument therefore seeks not simply to highlight the empirical limits and counter-tendencies to global integration. More importantly, it seeks to elucidate theoretically what most of the literature has hitherto ignored: the adaptability of states, their differential capacity, and the enhanced importance of state power in the new international environment.

Given such variety, even where globalization has gone furthest, as in finance, we continue to find important differentials in national levels of savings and investment, the price of capital, and even the type of capital inflows and outflows. This suggests that any significant 'weakening' in the capacity for macroeconomic management—to the extent that this has occurred—may owe at least as much to 'domestic' institutions as to global processes.

Indeed, evidence from Japan and the East Asian NICs (newly industrialized countries) indicates that strong states—that is, those with fairly firm control over socio-economic goal setting and robust domestic linkages—are often facilitating the changes identified as 'globalization'. Thus, rather than counterposing nation-state and global market as antinomies, in certain important respects we find that 'globalization' is often the by-product of states promoting the internationalization strategies of their corporations, and sometimes in the process 'internationalizing' state capacity. However, because state capacities differ, so the ability to exploit the opportunities of international economic change—rather than simply succumb to its pressures—appears much more marked in some countries than in others.

Since much—though by no means all—of my evidence of robust state capacity is drawn from East Asia, it is important to clear away at the outset any possible misconceptions which recent events (notably, the Thai currency crisis) may have encouraged. It needs to be emphasized that,

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[1] This article draws on my forthcoming book, *The Myth of the Powerless State: Governing the Economy in a Global Era*, Polity Press, Cambridge 1998. I would like to thank William Coleman, Robert Wade, David Levi-Faur, John Ravenhill, James Richardson, John Hobson, Robin Blackburn and participants at the ANU seminar on 'Globalization' for their comments.

[2] For an argument which is more open-ended than conventional accounts about the impact of economic globalization, see Jonathan Perraton, David Goldblatt, David Held and Anthony McGrew, 'The Globalization of Economic Activity', *New Political Economy*, vol. 2, no. 2, 1997, pp. 257–77.

due to historical-geopolitical, institutional and policy differences, the state capacity concept does not apply in any uniform sense to the countries of East Asia. Even at the most basic level there are major differences between first- and second-generation NICs in the number, quality and organizational commitment of career bureaucrats who might be mobilized to coordinate transformative projects. The relatively weaker developmental capabilities of states in the second-generation NICs—that is, the Southeast Asian economies, Malaysia, Indonesia, and Thailand—have rendered these economies more vulnerable to external pressures than their northern counterparts.[3] In Thailand in the 1990s, for example, the availability of easy finance coupled with the virtual absence of investment guidelines contrasts dramatically with the highly coordinated investment strategies put in place earlier by the Taiwanese, Koreans, and Japanese at a similar stage of development. Whereas the state-guided strategies of the latter generated high levels of investment in strong-growth industries, the Thai's uncoordinated approach has encouraged intense speculative activity, leading to a frenzy of over-investment in the property sector and ultimately contributing to the recent currency crisis.[4]

If these points remind us that no region or country is 'crisis-proof', they should not be taken to imply that the East Asian region as a whole—as opposed to some parts of it—is inherently fragile.[5] The Western media has certainly helped to propagate this image, offering up every crisis emanating from the region as somehow portending the end of the 'East Asian miracle'. While some short-term spillover effects are unavoidable in a highly integrated system, such episodes often tell us more about the relative weakness of domestic institutions in particular countries than about the generalized strength of globalization pressures. Indeed, the evidence suggests that East Asia's industrial star is still on the rise, the region's transformative potential far from exhausted.[6]

Different Hypotheses of 'Globalization'

While I have thus far alluded only to the 'strong globalization' hypothesis, there are in fact at least three hypotheses that can be identified in the literature:

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[3] For an informative study of north-south differences, see Richard Doner and G. Hawes 'The Political Economy of Growth in Southeast and Northeast Asia', in M. Dorraj, ed., *The Changing Political Economy of the Third World*, London 1995.

[4] In response to the Thai crisis, a number of commentators have suggested that the real challenge for Thailand is to 'overhaul its bureaucracy' which, among other things, would mean increasing pay to improve its quality; see, for example, the *Far Eastern Economic Review*, 29 May 1997, p. 15; 12 June 1997, p. 74.

[5] The Thai crisis has led both Malaysian and Indonesian governments to issue lending guidelines to local banks detailing how much they should spend on any one sector. See the *Economist*, 12 April 1997, p. 76; *Far Eastern Economic Review*, 12 June 1997, p. 72. But such measures proved too little and too late to head off the financial crisis.

[6] Support for this view comes not only from strong export growth, but also from the changing composition of exports as more countries shift manufacturing from lower to higher value-added—for instance, from textiles to computers. See, for example, the *Asian Wall Street Journal*, 16–17 May 1997; *Far Eastern Economic Review*, 19 June 1997, p. 63.

i) Strong globalization; state power erosion.[7]
ii) Strong globalization; state power unchanged.[8]
iii) Weak globalization (strong internationalization); state power reduced in scope.[9]

The findings of various studies summarized in the following section provide strong grounds for rejecting the first and second propositions in favour of the 'weak globalization' thesis. However, I find no compelling evidence for that part of the third proposition which claims that the state's role is now generally reduced to that of legitimating decisions initiated and implemented elsewhere. Instead, I propose a fourth proposition that stresses the differential capacities of states and how the world economy, far from eliminating such differences, is more likely to sharpen and further emphasize their salience for national prosperity:

iv) Weak globalization (strong internationalization); state power adaptability and differentiation emphasized.

The full development of this proposition rests on more extensive comparative material than can be mustered here. Nevertheless, I shall present a two-step argument, for the globalization thesis can be tackled in two different ways. The more common strategy to date has been to evaluate the extent of economic globalization: how far has it gone? What are its limits and counter-tendencies? Most of the literature has adopted this quantitative approach, often with considerable ability and finesse. Though such assessments are indispensable, they are also controversial. The controversy arises as much from the notorious inaccuracies of the available data as from the different uses to which the data are put. For these reasons, I shall confine this first part of my account to highlighting some of the main findings, and where relevant, the pitfalls.[10] The second part of my argument is concerned with the impact of so-called globalization and its implications for the ability of states to pursue particular policy goals.

I. Limits To Globalization

There is clearly some substance to the new globalist orthodoxy. The sheer volume of cross-border flows, of products, people, capital and, above all, of money is impossible to dispute. The important issue, however, turns on the meaning of these flows. Do they point to a clear globalization tendency? If such a tendency existed, one would expect to find evidence indicating that the changes in question conformed to at least three crite-

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[7] See, for example, K. Ohmae, *The Borderless World*, New York 1990; R.B. Reich, *The Work of Nations*, New York 1992; M. Horsman and A. Marshall, *After the Nation State*, London 1994.
[8] This position is best expressed by the *Economist* (for instance, 7 October 1995, pp. 15–16) which holds that the state never had the (macroeconomic planning) powers it is said to have lost, and that those powers it continues to have are still (regrettably) significant.
[9] This position is exemplified by Paul Hirst and Graham Thompson, *Globalization in Question*, Cambridge 1996.
[10] A more extended analysis of the limits of globalization can be found in *The Myth of the Powerless State*, ch. 6.

ria: i) novelty—is it unusual or without parallel, thus suggesting secular growth rather than oscillation? ii) magnitude—how substantial is it in size? and iii) distribution—to what extent is it world-wide in scope? I summarize the main counter-evidence under these three headings.

The Novelty of Global Flows

Are contemporary international flows without historical precedent and therefore posing perhaps novel challenges? Are the post-war trends onward and upward? If the answer to both questions is in the affirmative, then we have clear evidence of a globalization tendency, of secular growth rather than oscillation. The answer, however, varies greatly according to when one starts to measure the changes, hence the often conflicting claims in the literature. At least two findings suggest room for caution.

First is the existence prior to 1913 of trade and capital flows not dissimilar in size to flows in the recent post-war period. A number of studies concur that the level of international openness was in certain respects no less remarkable in earlier periods than today. Thus for a range of industrialized nations, the ratios of export trade to GDP in 1913 may actually have exceeded the level reached in 1973. As late as 1991, the OECD shares of exports in GDP (17.9 per cent) did not enormously outweigh those estimated for 1913 (16 per cent).[11] As with trade, the ratios of capital flows relative to output appear higher during the Gold Standard period than even in the 1980s. Indeed, the level of financial openness appears to have oscillated historically, reaching a high point in the classical period of the gold standard, up until 1914. From then up until the 1970s, the combination of depression and war, followed by the strong political consensus for Keynesianism, helped to weaken financial integration and strengthen autonomy in policy matters. Distinctive features no doubt exist for each period, yet it seems hard to disagree with the conclusion reached by Hirst and Thompson that 'the present period is by no means unprecedented'.[12]

The second finding is straightforward. The post-war trend towards greater trade integration, especially marked since the 1960s has been weakening. While world trade has grown much faster than output, this growth has actually been slowing over the 1980s and 1990s, the ratio declining from 1.65 in 1965–80 to 1.34 in 1980–90. Moreover, as Robert Wade has argued, there are not only cyclical but also structural reasons for expecting this slow-down to continue. Structurally, a gradual shift away from manufacturing within the OECD will mean less rather than more trade integration as the share of less trade-intensive services rises.[13] Thus, from the perspective of our first criterion, evidence of an unprecedented tendency is not compelling.

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[11] See Andrew Glyn, 'Social Democracy and Full Employment', NLR 211, May-June 1995, p. 44.

[12] For studies supporting such a conclusion, see among others the excellent chapter by Robert Zevin, 'Are World Financial Markets More Open?', in Tariq Banuri and Juliet B. Schor, eds, *Financial Openness and National Autonomy*, Oxford 1992.

[13] This paragraph draws on Robert Wade, 'Globalization and Its Limits: Reports of the Death of the National Economy are Greatly Exaggerated', in S. Berger and R. Dore, eds, *National Diversity and Global Capitalism*, Ithaca 1996, p. 66.

The Magnitude of Global Integration

How big are the changes? The answer depends not simply on when one starts measuring, but on what changes are measured. I will address this point with two examples commonly offered up by globalists as evidence of globalization: Foreign Direct Investment (FDI) and capital mobility.

FDI

Globalists identify the transnationalization of production as the driving mechanism of economic integration, drawing readily on aggregate FDI figures in support of that hypothesis. However, the use of aggregate FDI figures as proxies for the so-called 'globalization of production' seriously distorts reality.

If one simply takes the aggregate measure of FDI flows, as key accounts have done, one might well conclude that manufacturing production is becoming increasingly interconnected and thus 'denationalized' as multinational companies (MNCs) relocate more and more of their production process offshore.[14] But this conclusion is highly misleading. Three problems, which have received surprisingly little attention, deserve highlighting in this context.

i) *Preponderance of non-manufacturing in FDI*: the major part of global FDI is directed towards technically 'non-productive' assets or speculative ventures and financial services—golf courses, real estate, hotels, department stores, banking and insurance, and so on. Japanese FDI is probably more manufacturing—that is, production—oriented than most. So Japanese figures are especially revealing. For even the leading industrial investor nation in Asia—whose FDI in the Southeast is in many ways driving the industrial integration of the region—puts almost two-thirds of its world FDI (61.3 per cent) into non-manufacturing areas. These are 1995 figures, representing an increase of 16 per cent over the previous year.[15]

ii) *Concentration within manufacturing FDI on existing ventures rather than new activities*: a considerable amount of manufacturing FDI is concentrated on merger and acquisition (M&A) activity. Throughout the 1980s, cross-border M&A expenditure grew at the expense of 'new establishment' investment. Often more speculative and 'arms length' in character, M&A investment often justly invokes the idea of 'paper entrepreneurship'. The large outward flows from Sweden and the UK in the 1980s were mainly for 'portfolio' purchases of this kind, involving mergers and acquisitions of existing assets.[16] Over

[14] See, for example, Barbara Stallings and Wolfgang Streeck, 'Capitalisms in Conflict? The United States, Europe, and Japan in the Post-Cold War World', in B. Stallings, ed., *Global Change, Regional Response*, Cambridge 1995, p. 78.

[15] Of course, foreign companies often borrow locally so that their investments go unnoticed in official FDI—for instance, Japanese investors already in Thailand borrowing from Japanese banks operating in Thailand—but this does not challenge the basic point about FDI composition: such locally raised funds probably find their way more readily into non-manufacturing ventures, especially construction, real estate markets, and financial services.

[16] Glyn, 'Social Democracy and Full Employment', p. 49.

the same period, M&A ventures expanded dramatically in the United States, rising from 67 to 80 per cent of inward activity.[17] Given the coincidence of heightened M&A activity in several industrialized countries with a relatively sluggish industrial performance in the 1970s and 1980s, it may be more plausible to see in such investment trends the signs of an embattled productive system than of a growing global economy.

iii) *Sharp decline of FDI as a proportion of total long-term investment flows:* another perspective on FDI can be gained by noting that it constitutes both a relatively small and declining form of investment. Simply put, overall FDI has been steadily dwarfed by 'portfolio' investment—various arms-length investments, including bonds and mutual funds. In the ten years up to 1991–92, total FDI declined from 21 to 18 per cent of total long-term transfers from the thirteen major OECD countries. By contrast, portfolio flows rose 28 per cent to account for half of all long-term capital transfers.[18]

Taking a more disaggregated approach to the investment figures, we can therefore see why FDI does not automatically extend economic linkages, especially in those areas of multinational economic activity that might have a direct bearing on state policies. If the level of FDI is indicative of a globalization tendency at work in the sphere of production, present trends do not point in that direction.

A more realistic indication of the extent to which the 'national' economy is being outflanked by transnational linkages can be gained by measuring inflows and outflows of FDI as a percentage of gross domestic investment. By this standard, the rates of FDI are actually quite modest. With certain notable exceptions—for instance, Britain and Sweden—gross domestic investment in Europe exceeds total FDI, both outbound and inbound, by at least 90 per cent.[19]

Capital Mobility

Globalists assume that the world economy is now so integrated that the constraints of location and of institutional frameworks are increasingly irrelevant; that corporations—whether satisfied or disgruntled with a particular national environment—can simply take a 'random walk' in the world market, escaping the confines of any one nation-state. It is this footloose quality of MNCs—above all the threat of exit—that is seen to pose the greatest threat to territorially constituted forms of governance. The reality, however, is at odds with this vision. For, as many studies report, the number of genuinely transnational companies is rather small.

[17] Hirst and Thompson, *Globalization in Question*, p. 72. Has M&A activity slowed in the 1990s, in keeping with the popular view that the United States economy is booming?
[18] From the point of view of both sustainable world growth and the effectiveness of domestic policy, this imbalance is far from a desirable trend. Compared with FDI which is more difficult to withdraw at short notice, large flows of portfolio capital have the potential to destabilize domestic policy, as seen in the Mexican crisis precipitated by the non-renewal of bonds. By contrast, these distinctions have been more readily appreciated in East Asia where tighter controls have maintained short-term flows at a relatively low level.
[19] Glyn, 'Social Democracy and Full Employment', pp. 48–9, Table 2.

On virtually all the important criteria—share of assets, ownership, management, employment, the location of R&D—'the importance of a home base remains the rule, not the exception'.[20]

Conventional wisdom nevertheless tells us that cost-reduction is the driving force compelling MNCs toward a footloose career, and that new transport and information technology liberates and encourages MNCs to exploit low-cost production sites, resulting in a globalization of production. Yet, if cost-reduction were the driving force behind the mobile MNC, we would expect to find most, or at least a very sizeable chunk of FDI going to the developing countries. However, the evidence firmly contradicts that expectation. As of 1991, a good 81 per cent of world stock of FDI was located in the high-wage—and relatively high-tax—countries: principally the US, followed by the UK, Germany, and Canada. Moreover, this figure represents an increase of 12 points since 1967. Indeed the stock of FDI in the UK and the US exceeds the stock in Asia and the entire South.

Such figures underline the point that MNCs do not by and large invest where wages and taxes are lowest. Why not? Three considerations seem relevant. First, new technologies place a premium on fixed costs (equipment, machinery and so on), while reducing the importance of variable costs (such as wages and raw materials). While certain types of labour—especially knowledge-intensive labour—tend to be treated increasingly as a fixed cost, the general effect of this overall transformation is to reduce the cost savings to be gained by moving to low-income sites. Second, new production methods emphasize the growing importance of physical proximity between producers and suppliers—especially in non-assembly operations. These methods privilege local supplier networks, thus driving a trend towards the constitution of regional, not global, sourcing networks. A third factor, underscoring the critical importance of a home base, is the advantage firms derive from domestic linkages: national institutional frameworks which enmesh business in support relationships with trade associations, training and financial institutions, and national and local governments. In sustaining high-wage economies, one of the most important of these support systems is the relationship between government and business, which underpins the national innovation system. Being generally exclusive rather than open to all, support relationships of this kind constitute a competitive advantage.[21]

These considerations suggest that the advantages of maintaining a firm 'home' or regional base may be stronger than ever, perhaps for most companies outweighing those to be gained from 'going global'. It would therefore appear that not only the incidence but also the advantages of mobility have been overstated. But the case against a strong globalization tendency does not rest here. We turn next to evidence concerning how the changes are distributed.

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[20] Yao-Su Hu, 'Global or Stateless Corporations are National Firms with International Operations', *California Management Review*, Winter 1992; Hirst and Thompson, *Globalization in Question*; Winfried Ruigrok and Rob van Tulder, *The Logic of International Restructuring*, London 1995.

[21] This argument is developed in a comparison of state capabilities and state-industry relations in Sweden, Germany, Japan and the East Asian NICs in *The Myth of the Powerless State*.

The Distribution of Trade and Investment

Up to this point, my objective has been to show that the novelty and the magnitude of change has been overplayed. I have not sought to deny the existence of a more integrated world economy, a fact which I broadly acknowledge. My concern here is to draw attention to the way trade and investment are distributed. Three trends are inconsistent with a globalization tendency.

i) *The national bases of production*

First, even if we accept that national economies are more integrated through trade and investment flows than in the recent past, it appears that in all but the smallest economies, trade constitutes quite a small share of GDP, with exports accounting for 12 per cent or less of GDP in Japan, the US and the EC. This means that in the main industrialized economies around 90 per cent of production is still undertaken for the domestic market. The national bases of production—and, as we saw, for investment—therefore seem as pronounced as ever.[22]

ii) *North-South divisions*

A second pattern runs counter to the idea of a globalizing tendency. Whereas globalization predicts more even diffusion between North and South, in fact world trade, production and investment remain highly concentrated in the OECD—that is, in the rich North. Over the 1970–89 period, the North's share of trade grew from 81 per cent to 84 per cent—though the decline of the South's share in world exports masks their changing composition, with largely negative growth of primary product exports, and a rising share of manufactured exports. Investment has followed a similar pattern, with around 90 per cent going to the North over the same period.

iii) *Regionalization*

Finally, this predominantly Northern trade and investment is itself becoming more geographically concentrated in intra-regional patterns. For example, intra-European trade now accounts for some 62 per cent of its total export trade. Intra-regional trade within the American region—the US, Canada and Mexico—increased between 1980 and 1992 from 68 per cent to 79 per cent of total US-Japan and US-EU trade. Intra-regional trade has also become the dominant trend in Asia—China, ASEAN, Japan and the NICs—as the region has steadily enhanced its importance as export market and production site for Japan and the NICs. Intra-Asian trade in the period 1986–92 rose from 32.4 to 47.7 per cent of total exports, thus reversing the traditional dominance of trade with the US. In short, trade within Asia has been growing more rapidly than trade between Asia and the US.

A similar story can be told for investment. In Asia, especially since the 1985 Plaza Accord, investment-driven economic interdependence has dramatically increased, Japan having now replaced the US as Asia's primary source of FDI. In 1980, Japan's cumulative investment in the rest of

[22] Data for this and the following paragraph are drawn from Wade, 'Globalization and its Limits', pp. 66-7.

Asia was worth little more than half as much as America's, at $9.8 billion.[23] By 1990, it was worth around 30 per cent more, at $41.8 billion. This development has also boosted intra-regional trade and fostered the development of regional production networks.

The US, Europe and Japan are not simply regional traders. However, current trade patterns do make it clear that intra-regional trade is increasingly important for the Big Three. Exports within North America, Asia, and Europe rose from 31 per cent of total world exports in 1980 to 43 per cent in 1992. Thus, overall, trade *within* the three regions has grown to overshadow trade among its members (US-Japan, US-EU, Japan-EU).[24]

Compelling evidence for a strong globalization tendency has thus far been wanting. In some respects, indeed, counter-tendencies seem more apparent. If we turn to the finance sector, however, the reality of a global market seems unassailable.

Since formal removal of the gold standard in 1971 and subsequent liberalization of exchange controls, international capital flows have reached truly spectacular levels. Whichever way we look, it is hard to escape the reality of global money markets where enormous sums are traded daily. This is the 'casino' face of capitalism, unleashed by national governments which now appear powerless to contain its destabilizing effects. It is this change which has given most life to the idea and reality of 'globalization'.

However, there is evidence of national diversity even in money markets. First, the price of capital has not converged. While studies disagree on whether real interest rates in different national markets continue to diverge, the price differential for both loan and equity capital remains considerable.[25] Second, whereas globalization implies equalization, marked differences in savings and investment rates persist. For example, in 1992, the ratio of savings to GDP in eleven countries ranged from 0.5 to 25 per cent. In the lowest band (0.5-2 per cent) sat the US, the UK, Australia and Sweden; Germany and Austria occupied the middle band (10–15 per cent); and in the highest band (20–25 per cent) were Japan, Taiwan and Korea. The differentials in national investment rates tend to parallel those for savings. In 1992, investment as a percentage of GDP ranged from around 15–36 per cent, with the US, the UK, Australia and Sweden in the lowest band (15–19 per cent), Germany, Austria and Taiwan in the middle (22–25 per cent), and Japan and Korea in the highest (31–36 per cent).[26]

This strong correlation between savings and investment rates has been interpreted to mean that countries do not draw freely on other countries'

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[23] See James Fallows, *Looking at the Sun*, New York 1994, p. 265.
[24] Stallings and Streeck, 'Capitalisms in Conflict?', p. 73.
[25] For references to this dispute, see Wade, 'Globalization and its Limits', p. 75. It should also be noted here that even in the major industrial economies, such as Germany, governments continue to shape net price differentials in borrowed funds by instituting particular tax regimes designed to favour certain kinds of investment.
[26] Author's calculations. For the comparative data for 1950–93, see *The Myth of the Powerless State*, ch. 6.

savings. Robert Wade, however, reports a fall in the OECD savings-investment correlation from 75 per cent in the mid-1970s to 60 per cent in the 1980s. Financial markets, he suggests, have therefore become more integrated, even if the mobility of capital is somewhat less than anticipated.[27]

Finally, 'dualism' rather than 'transnationalism' seems to distinguish the operation of financial markets, most notably in the area of company shares. These tend to be fixed to specific national stock markets, thus contrasting dramatically with other parts of the financial market—for example, the bond, currency and futures markets—which are genuinely 'transnational'.

These qualifications to 'global' finance suggest that the relevance of national institutions is far from insignificant. Thus, the conclusion to the first part of my argument is that while national economies may in some ways be highly integrated with one another, the result—with the partial exception of money markets—is not so much a globalized world (where national differences virtually disappear), but rather a more internationalized world (where national and regional differences remain substantial and national institutions remain significant). What does this mean then for the power of governments to govern?

II. The Extent of Government Powerlessness

For many commentators, the power of global finance—especially of the bond market—to undermine the monetary and fiscal policies of governments seems an incontrovertible truth. It is also viewed as the key constraining feature of a globalized economy: forcing all governments to adopt similar neoliberal—deflationary, fiscally conservative—policies. From this perspective, two conclusions follow. First, global money markets are all-powerful, forcing on governments fiscal conservatism —read 'powerlessness'. Second, it matters not whether a state is weak or strong; all national governments are impotent in the face of global finance. Here I will examine each of these claims in turn.

The problem with the 'powerlessness' argument is not that it is wrong about the new constraints on government capacity to make and implement policy. Rather, it is the assumption that such constraints are absolute rather than relative, and that they represent 'the end of state history' rather than an evolving history of state adaptation to both external and internal challenges. Three weaknesses in particular deserve highlighting.

Overstating Earlier State Powers

First, globalists tend to exaggerate state powers in the past in order to claim feebleness in the present. Whilst financial globalization is commonly identified as the factor undermining governments' ability to practise effective macroeconomic management—of the Keynesian reflationary variety—some commentators have recently questioned just how effective Keynesian demand management ever was.[28] While in theory

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[27] Wade, 'Globalization and its Limits', p. 74.

the fixed exchange rates guaranteed under the Bretton Woods system provided a more stable policy-making environment, in reality there is little compelling evidence that the state has ever had the sorts of powers that allegedly it has been forced to relinquish.

What can be said, as Michael Mann has noted, is that while rapid growth provided the fiscal surpluses to spend, expansionary macroeconomic policies by post-war governments certainly seemed to produce results. But more than two decades of troubled growth, recession, and falling real income in the OECD have removed the fiscal surpluses.[29] The point to emphasize here is that many of the difficulties national policy-makers have experienced with macroeconomic management—for example, balancing budgets, mobilizing sufficient revenue to fund programmes and so on—have more to do with internal fiscal difficulties caused by the recession, and little to do with 'globalization' tendencies.

From a wholly contemporary vantage point, it has appeared to many that the pressures on governments to reduce the tax burden and restructure the tax system are a result of increased openness: that is, ultra-mobile capitalists who can shop around the globe for the best tax environment. But from a much longer historical perspective, such pressures are in fact the norm. As Michael Mann argues on the basis of earlier work:

> at least since the thirteenth century, citizens have only consistently agreed to pay a higher proportion of their incomes in taxes during wartime. Their reluctance to stump up during the peaceful 1970s and later, in a period of recession (when their real incomes were stagnant or falling), is hardly surprising. It is the historical norm, not the unique product of 'postmodernity' or 'globalism'.[30]

The recent trend towards fiscal conservatism owes much to such domestic pressures. Prolonged economic recession coupled with demographic changes have required governments to raise more taxes to support the increasing number of jobless and citizens retiring from productive work. These pressures on the public purse are occurring at a time of stagnant living standards. In such a context, and in the absence of national emergency or external threat, electorates are increasingly reluctant to sustain tax and spending increases. Prolonged peace, of course, provides only one contextual variable for the new conservative agenda. Equally important in explaining apparent policy convergence, at least after 1973, are the common effects of the oil shocks, and the inflation they accelerated. As Zevin concludes, rather than being the result of a sudden strengthening of international interdependence, policy convergence can best be explained 'by common responses to the inflation and perceived policy errors of the 1970s'.[31]

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[28] See, for instance, *The Economist*, 17 October 1995, pp. 16–17.
[29] For a fresh perspective on globalization tendencies more generally, see Michael Mann, 'The Global Future of the Nation State', paper presented at the Direction of Contemporary Capitalism Conference, Sussex, April 1996.
[30] Ibid., p. 10. The contrasting 'globalist' argument can be found in Sven Steinmo, 'The End of Redistribution? International Pressures and Domestic Tax Policy Choices', *Challenge!*, vol. 37, no. 6, 1994.
[31] Zevin, 'Are World Financial Markets More Open?', p. 73.

To conclude that the difficulties faced by national policy makers are largely attributable to prolonged recession and internal fiscal difficulties is not to deny that some forms of global finance can play havoc with government policy. But the important point is that such 'havoc' might well prove irrelevant in the context of renewed and sustained growth. In the absence of sustained growth in the future, one can predict continuing difficulties for governments, in turn continuing to nourish the idea of all-powerful global finance.

Overstating Uniformity of State Response

The fact that not all governments follow neoliberal dictums surely throws into question the central assumptions of the powerlessness argument. Far from acting in concordance with neoliberal prescriptions, Germany (that is, formerly West Germany), which remained aloof from Keynesianism for much of the post-war period, has recently sustained a massive tax levy to help finance unification. Moreover, as the German banks pursue increasingly conservative lending strategies, the German federal government has stepped into the breach, acting as primary source and coordinator of industrial investment in the East. In Japan, where the importance of various government programmes to protect employment has been evident at least since the two oil shocks, the unpopular consumption tax has recently sustained a sharp rise, ostensibly to help sustain further such programmes.

It is not only 'strong' states like Germany and Japan that have adapted to their external environment, finding new ways to pursue their programmes.[32] Weaker states too have displayed degrees of adaptive capacity. Thus despite the pervasive rhetoric of 'economic rationalism' in Australian policy in recent years, the Labor government pursued an expansionary policy, using deficit spending to fund welfare, labour market, and industrial policies. It was not the power of money markets that undermined these policies, but an electoral shift from Labor to the long-excluded conservative coalition pursuing a neoliberal agenda.

Thus, if global finance has not exerted the uniformly debilitating effects so often claimed for it, why then, we may ask, has the idea of the powerless state seemed so persuasive to so many?

The Political Construction of Helplessness

Perhaps more than anything, it has been the rise of monetarist policies in the 1980s, the emergence of fiscal retrenchment in bulwarks of social democracy like Sweden, and the various speculative attacks on national currencies that have led globalists to conclude that—while governments may reign—the global economy rules.

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[32] By 'strong' state I mean not a coercive state but one with the organizational capacity for governing industrial transformation. For a theoretical analysis of the domestic foundations of state capacity as well as a discussion of its main varieties in Germany, Sweden, and East Asia, see Weiss, *The Myth of the Powerless State*. For a more general discussion of strong and weak states, see Linda Weiss and John M. Hobson, *States and Economic Development*, Cambridge 1995.

It must be said, however, that political leaders—especially in the English-speaking world dominated by neoliberal economic philosophy—have themselves played a large part in contributing to this view of government helplessness in the face of global trends. In canvassing support for policies lacking popular appeal, many OECD governments have sought to 'sell' their policies of retrenchment to the electorate as being somehow 'forced' on them by 'global economic trends' over which they have no control.

While it is true that governments are responding to similar pressures in the world economy—the long slump in world-wide demand, stagnant or falling living standards—it is quite misleading to conclude that these pressures derive solely or largely from 'globalization' tendencies, or that the latter produces a uniformity of response.

III. Convergence Versus Varieties of State Capacity

Globalists have not only overstated the degree of state powerlessness. They have also *over-generalized* it. It is to this final weakness in the globalist argument that we now turn.

The variety of 'national capitalisms'—continental European, East Asian, Anglo-American—finds a parallel in the variety of 'state capacities' for domestic adjustment strategies. In a different context, I will undertake to show how the two may be linked. At issue here, however, is the variety, as opposed to the convergence, of state capabilities. Contrary to globalist predictions, I propose that national differences are likely to become more rather than less pronounced in a highly internationalized environment, thus exacerbating rather than diminishing current differences between strong and weak states.

Yet even those who agree that 'globalization' has been highly exaggerated, nevertheless part company when considering the effects of economic internationalization on state capacity. While some conclude that the nation-state persists as an important locus of accumulation, and that national—and international—actors and institutions continue to structure economic space,[33] others see state powers much more circumscribed through the shedding and shifting of traditional responsibilities.

In a comprehensive recent study, Hirst and Thompson propose that certain traditional powers are declining: 'The power of nation states as administrative and policy-making agencies has declined' while the state's role as an economic manager is 'lessening'. In this respect, they appear to overlap with the globalists. In a more nuanced approach, however, they insist on the enduring importance of the nation-state—not in traditional terms as sovereign power or as economic manager, but

[33] For two recent accounts respectively emphasizing these conclusions, see Wade 'Globalization and its Limits' and Mann 'The Global Future of the Nation State'.

as the key source of legitimacy and the delegator of authority to powers above and below the national level. Its territorial centrality and constitutional legitimacy assure the nation-state a distinctive and continuing role in an internationalized world economy, even as conventional sovereignty and economic capacities lessen: 'Nation-states should be seen no longer as "governing" powers... Nation-states are now simply one class of powers and political agencies in a complex system of power from world to local levels...'[34] According to this interpretation of current tendencies, state power is being reduced and redefined on a broad scale, stripped to the basics, becoming even a shell of its former self: still the supreme source of legitimacy and delegator of authority, but exercizing no real capacity over its economic domain. The question is whether one can identify any clear cases which might fit this conception, and whether, having identified them, they represent not simply a group of traditionally 'weak' states, but a group where real power shifts are in train.

It is doubtful that the 'basic state' hypothesis fits even the EU experience, which appears to inform so much of this kind of reasoning. In the German case neither sub-national nor supranational agencies have supplanted the national state's coordinating capacities. Indeed, in a number of important respects—technological innovation and industrial investment—coordination has been growing, not declining, over the past two decades.

Although Hirst and Thompson do insist on the state's continuing importance as the source of legitimacy and the rule of law, and would therefore probably reject the 'weak state' characterization of their position, it is hard to see what kind of substantive powers the state would retain if it is no longer where the action is. If the state is increasingly becoming merely the place from which law is promulgated, authority delegated, powers devolved, then is that not simply a form of power shrinkage by stealth—somewhat akin to the centrifugal tendencies of feudalism? After all, their image of the evolving role of the state (as *Rechtsstaat*) has much in common with the role envisaged by eighteenth-century liberals: thus, not an eclipse of state power as some globalists are led to claim, but certainly a very narrowly defined power.

This seems to me mistaken. For it is blind to state variety and to adaptation. I, too, would emphasize change, but change is hardly novel to the state. Adaptation is the very essence of the modern state by virtue of the fact that it is embedded in a dynamic economic and inter-state system—even the evolving forms of warfare must be seen in that context. My argument is that nation-states will matter more rather than less—and, though not elaborated here, this will advance rather than retard development of the world economy. The argument is in three parts, emphasizing: i) state adaptation rather than decline of functions; ii) strong states as facilitators not victims of internationalization; and iii) the emergence of 'catalytic' states consolidating national and regional networks of trade and investment.

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[34] Hirst and Thompson, *Globalization in Question*, p. 190.

Adaptiveness of the State

The whole issue of state capacity for economic adjustment has been misleadingly cast as a choice between either Keynesian or neoliberal macroeconomic policies. Since they are both macroeconomic in focus, they are, to say the least, a choice between highly restricted alternatives. Yet, as the East Asian experience has shown, there is much more to governing the economy than macroeconomic policy. Industrial policy continues to play a large role in the Asian region. Even in the EU, where one would most expect to find uniformity, industrial policy is far from dead. It has simply changed its character. In Germany, for instance, the state still has an important impact on corporate strategies, in particular industries, through policies shaping strategic partnerships and innovation strategies. More generally, the federal government provides support for 'steady state' industries through the self-governing national system of innovation. But it takes an active role where a steady state no longer applies: at points of crisis management relating to issues of industrial decline, or industry creation—as in the East—or competitive pressures for new technology.

So used to treating states as 'prisoners of a fixed genetic code', to use Ikenberry's phrase,[35] many commentators have also readily chorused the 'death of industrial policy' in Japan. Japan's industrial bureaucrats in the Ministry of International Trade and Industry (MITI) have understandably played a key role in cultivating this myth, largely to assuage American complaints about 'unfairness' in trade disputes. Thus in recent years, the foreign visitor to MITI in Kasumigaseki in downtown Tokyo could expect to be greeted with the solemn statement that MITI's main function in these times is to promote imports. Of course, if this were true, one would have to wonder why MITI's renowned prowess in promoting exports has not translated as smoothly to imports.

The key point is that MITI no longer needs to promote exports, nor preside over industry creation. It may have 'lost' many of its former policy instruments—for instance, capital, foreign exchange and licensing controls—as all the standard accounts repeatedly tell us, but this is by no means the end of the story. For MITI continues to create new tools, more suited to the new environment and to the new tasks that this engenders: supporting self-governing cartels in basic materials, promoting—and diffusing—technological innovation through cooperative arrangements, as well as facilitating the internationalization of corporate activity through the use of Overseas Development Aid (ODA) and other instruments.

The tendency to expect institutional convergence and the failure to recognize state variety are two sides of the same coin. Both are based on a 'policy instrument' theory of state capacity in which the relevant instruments are somehow predetermined and fixed in character. Any diminution in the importance of a particular *policy tool* is taken as evidence of a loss of state power.

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[35] G. John Ikenberry, '"Funk de Siècle": Impasses of Western Industrial Society at Century's End', *Millennium*, vol. 24, no. 1, 1995, p. 125.

But state capacity for adjustment strategy cannot be reduced to policy instruments. The point to underline here is that it is not the state as such which is enfeebled by economic integration. If anything, it is the efficacy of specific *policy instruments* which is in question—in particular, *macroeconomic* adjustment strategies which focus almost exclusively on fiscal and monetary policies. Both Keynesian and neoliberal policies are similar in this regard, implying a focus on short-term macroeconomic objectives. In both cases, the instruments of intervention are predetermined; there is little room for creative adjustment. This may, of course, account for the greater appeal of macroeconomic policy in settings lacking strong state traditions.

But the very opposite is the case with *industrial*—read also 'technology'—policy. In so far as industry itself is constantly changing, 'industrial policy' must of necessity be creative. Hence it cannot be defined once and for all in static, 'snap-shot' terms. So many commentators have looked for 1960s-style Japanese industrial policy in the 1990s and unsurprisingly concluded that it doesn't exist! It must be stressed however that *the very capacity for industrial policy is one that requires the state to constantly adapt its tools and tasks*.[36]

Institutional arrangements, domestic linkages and state capacity

The major point to emphasize is that the capacity for domestic adjustment strategy does not stand or fall with macroeconomic capacity, whether of the reflationary or deflationary variety. It rests, perhaps more than ever, on industrial strategy, the ability of policy-making authorities to mobilize savings and investment and to promote their deployment for the generation of higher value-added activities.

This capacity for a coordinated and strategic response to economic change depends, in turn, not so much on specific policy 'instruments' or levels of 'integration into the world economy'. The contrasting cases of Singapore and Britain are testimony to this. Highly integrated Singapore —whose per capita GDP now exceeds that of Britain—maintains strong control over its savings and investment rates, thus engineering upward mobility in the international system.[37] By contrast, highly integrated Britain, with little capacity for industrial adjustment, has failed to arrest its downward slide in the international order—Britain's traditional strength in promoting its financial sector being part of that drama. Thus, high integration does not necessarily mean the displacement of 'national' economies as the locus of accumulation, or the weakening of national economic management.

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[36] As the French discovered, industrial policy based predominantly on the tools of state-led industrial credit has proved vulnerable to financial liberalization. But the conclusion from the French case should not be 'the end of industrial policy' in general, but rather the need for new tools to meet the new transformative tasks set in motion by international competition.

[37] Singapore's remarkably high savings rate (approximately 45 per cent of GDP) has been achieved through a system of forced savings which channels compulsory contributions from employers and employees to the Central Provident Fund (CPF). Singapore's dominant social security institution, the CPF contributed 30.1 per cent of gross national savings in 1990. For a discussion of the government's use of these funds in a scope much broader than social security, see Garry Rodan, ed., *Singapore Changes Guard*, New York 1993.

Rather, a state's capacity for a coordinated and strategic response primarily rests on institutional arrangements which make key decision-makers in the economic bureaucracies at once 'autonomous' and in some important respects 'accountable'. The character of 'autonomy' applies in so far as decision-making is largely—though never perfectly—insulated from clientelistic political pressures and the plurality of special interests that in most liberal democracies tend to privilege the politics of distribution over the politics of growth. This is not to suggest that growth and equity—or indeed welfare—are incompatible—quite the contrary, as the German, Japanese and NIC experiences would indicate. Rather, the issue is one of national priorities. No less contentious in discussions of East Asian bureaucracy, 'accountability' nevertheless can be said to apply in so far as the effectiveness of industry policies depends on domestic linkages: notably, institutionalized structures for the exchange of information and for participation of the business groups whose involvement is central to successful implementation.

In the East Asian Three—Japan, Korea and Taiwan—the institutional arrangements in question concern the core economic bureaucracies as well as the financial sector, together with a host of agencies for technology development and diffusion, and the acquisition and exchange of industrial information. These arrangements which pull together state and industry in close—albeit not tension-free—cooperation, have underpinned rapid structural change and technological learning.[38]

Thus, rather than attributing the current proclivities for macroeconomic adjustment to 'globalization', one should look in the first instance, domestically, to a country's governing institutions, and thus to differences in national orientations and capabilities. This leads to the second strand of my argument as to why the state's importance is increasing rather than diminishing in ensuring more equitable participation in the world economy.

The State as Victim or Facilitator of 'Globalization'?

In failing to differentiate state capacities, global enthusiasts have been blinded to an important possibility: that far from being victims, (strong) states may well be facilitators (at times perhaps perpetrators) of so-called 'globalization'. Although those researching in the field have yet to explore this possibility, there is sufficient evidence to suggest that this would be a promising line of enquiry. Such evidence as exists for Japan, Singapore, Korea, and Taiwan indicates that these states are acting increasingly as catalysts for the 'internationalization' strategies of corporate actors. As 'catalytic' states (see below), Japan and the NICs are taking the bull by the horns, providing a wide array of incentives to finance overseas investment, promote technology alliances between

[38] For individual studies of Japan and Korea, see respectively Chalmers Johnson, 'The Institutional Foundations of Japanese Industrial Policy', *California Management Review*, vol. 27, no. 4, 1995; and Peter Evans, *Embedded Autonomy*, Princeton, NJ 1995. For a comparative analysis of Japan and the NICs, see Weiss and Hobson, *States and Economic Development*; on technological learning, see John A. Mathews, 'An Emerging Silicon Valley of the East: How Taiwan Created a Semiconductor Industry', *California Management Review*, vol. 39, no. 4, 1997.

national and foreign firms, and encourage regional relocation of production networks.[39]

'Internationalization' in Japan has become a key strategy of its bureaucracy. Through agencies such as MITI, Japan has sought to manage the trade imbalance with the US by facilitating the off-shore relocation of the production process in industries such as micro-electronics. Firms in this sector have for some time been required by MITI to submit plans detailing how they plan to reduce their surplus over a five-year period, and have been provided with state assistance in relocating.[40] Whilst Japanese companies were relatively slow in taking up MITI's inducements in the pre-Plaza period, once the Plaza accord was in place and the value of the yen soared, business response to the relocation project was dramatic. The point, however, is not that MITI alone achieved this outcome, or that business was pushed by the state to relocate, or even that relocation was simply a response to US pressure over trade imbalances. The key point is that relocation was much more a publicly coordinated effort than an ad hoc response by individual firms acting alone. It thus provides a useful example of how a government itself may be a *part* of the 'globalization' process. While the latter is so often invoked as the enemy of state power, here we see state capacity as a *condition* of successful internationalization.

An even larger point can be extracted from these observations: domestically strong states may be able to adapt, and to assist firms to adjust, more effectively to the external environment by creatively adapting its tools and 'internationalizing' state capabilities. The Japanese bureaucracy, for example, has creatively used ODA as a means of externalizing its domestic alliances. As a condition of ODA disbursement, Japan has not only stipulated the import of Japanese goods, but also required placement of Japanese bureaucrats in government offices abroad—which also opens opportunities for the teaching of Japanese-style economics to governments open to advice—thus ensuring a more receptive environment for its own governed-market model of economic management.[41] Japan has thereby externalized aspects of its model of government-business relations beyond the home territory as part of the integration process. While institutional differences may thwart Japan-style developmentalism in Southeast Asia, it is likely that through Japan's influence many regional neighbours will absorb at least some of the lessons of Japanese institutions and industrial policy. Thus, writes *Business Week*, by early next century, this sort of 'missionary work' could exert 'a profound effect on world capitalism'. As a result, regionalism in this part of the world should continue to look quite different from neoclassical American-style capitalism.[42]

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[39] The importance of MITI's industrial policy role since the mid-1970s is contentious and cannot be defended here. For the most recent attack on the Chalmers Johnson school, from the Kent Calder stable, see Scott Callon, *Divided Sun: MITI and the Breakdown of Japanese High-Tech Industrial Policy*, Stanford 1995. For a critique, see Weiss, *The Myth of the Powerless State*.

[40] See Warren Davis, ed., *The Semiconductor Industry*, Washington 1992.

[41] For an intriguing account of the contests between Japanese and World Bank officials, representing opposing models of capitalism, in the making of the controversial World Bank report on East Asia , see Robert Wade, 'Japan, the World Bank, and the Art of Paradigm Maintenance: *The East Asian Miracle* in Political Perspective', NLR 217, pp. 3–36.

[42] *Business Week*, 12 December 1994, p. 30.

Pushing Firms Abroad

This conclusion contrasts sharply with the claim that 'Unlike bureaucrats... large multinational firms are not territorially bound in their operations' and that as a matter of course they 'seek the lowest-cost capital, components, information, and even government support to be found anywhere in the world'.[43] If this were true, then Japanese capital should surely have been much more responsive to the strong relocation opportunities offered prior to the Plaza agreement and the strong yen. The Japanese bureaucracy is not unique in its capacity to promote internationalization. Other institutionally strong states, Singapore for example, which are able to provide corporate actors abroad with the developmental infrastructure, inducements, and government-business relations similar to those enjoyed at home, have also taken to promoting offshore relocation. As a consequence of growing affluence and diminishing space, the Singaporean government has for several years been prodding its local and MNC companies to move off-shore to Singaporean-created industrial parks throughout the region—chiefly to China, Malaysia, Hong Kong, Indonesia, and more recently Thailand and Vietnam. When some years ago Dr Goh Keng-Swee, then Minister for Economics, announced the project to shift more business operations offshore, few Singaporean firms were willing to take the plunge. In Goh's words, firms have to be 'pushed'.[44]

The 'regionalization' of the Singaporean economy has thus been much more a directly top-down affair, with the government driving the process. As well as initiating government-business visits to the region to explore investment opportunities, the city-state also set up government-to-government bodies—like the China-Singapore Joint Steering Council—to facilitate relocation of Singaporean companies, and financed and administered the industrial parks and infrastructural projects abroad. Following upon the government's provision of economic data, incentives, capital infusions, investment guarantees and training programmes to potential off-shore investors, a great string of industrial parks is now under construction, stretching from Indonesia to China and Vietnam, with some of them already linked to the island's service industries. If successful, they are most likely to advance regional integration not at the expense of state power, but by its internationalization via reproduction in extenso of the Singaporean model.

Parallel stories can be told for Korea and Taiwan where the state has not only abolished many of the restrictions on outbound capital flows, but has also moved directly 'to facilitate the globalization strategies of national firms'.[45] At least three strategies can be distinguished. First, the state has encouraged local firms to raise money in foreign capital markets in order to finance their investment projects. Second, state agencies supplement private overseas investment with ODA to assist business expansion in

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[43] Kent Calder, 'Japan's Changing Role in Asia', in *The Japan Society*, New York 1991, p. 27.

[44] As cited in the *Far Eastern Economic Review* collection, *Japan in Asia*, Hong Kong 1991, pp. 116–17.

[45] Chu, 'The East Asian NICs: A State-Led Path to the Developed World', in Stallings, *Global Change*, p. 221. Though the argument developed here is my own, discussion of the three strategies that follow is based on Chu.

developing countries.[46] Third, local firms receive strong financial support to enter joint ventures or technology partnerships with MNCs in strategic sectors—for instance, in aerospace, semiconductors, telecommunications, and biotechnology. In Taiwan, for example, the state's financial support, according to Chu, underpinned every major merger and take-over proposal of Taiwanese firms in the US high-tech industries.[47] In Korea, similar concerns are reflected in the dramatic policy reorientation of the Export-Import Bank, which has been authorized to shift from export financing to the support of overseas investment.

Finally, one can add a fourth category of state-facilitated internationalization. This involves direct assistance for firms to relocate operations overseas, as in the case not only of Singapore, but of the Taiwanese government establishing an off-shore version of its Hsinchu Science Park at Subic Bay in the Philippines.

This sort of evidence is hard to square with the favoured image of states being passive victims of powerful 'transnational' forces. There is no attempt to suggest that all states are thus engaged in facilitating corporate internationalization. The point is that some are—amongst them, the most industrially dynamic and highly coordinated market economies—and that this attests to state adaptiveness and to the increasing rather than diminishing salience of state capacity.

In the light of the East Asian experience, it appears that state capacity for industrial transformation is alive and well, at least in those countries where post-war development has occurred under the aegis of so-called 'developmental states'.[48] This implies that in spite of a more integrated world economy, the high-performance industrial economies (Japan, Korea, Taiwan, Singapore) are now in a relatively strong position—especially compared with the uncoordinated market economies of Anglo-America—to mobilize the savings and investment required to sustain growth and higher value-added job creation. One further implication is that, as the advantages of coordinated market economies continue to be highlighted, potential adaptors of the Asian model are more likely to emerge—at least in the Asian region—than blind followers of the neoliberal model of capitalism.

More generally, so-called 'globalization' must be seen as a politically rather than a technologically induced phenomenon. It is political, firstly, in the general sense that the opening up of capital markets has occurred as a direct result of governments, either willingly or unwillingly, ceding to pressure from financial interests. But it is political also in the more specific sense discussed here: that a number of states are seeking directly to facilitate rather than constrain the internationalization of corporate activity in trade, investment, and production.

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[46] In this respect, the management of ODA tends to follow Japanese practice, being tightly linked to trade and investment and focused on infrastructure projects of significance to the investment activities of national firms.

[47] Chu, 'The East Asian NICs'.

[48] The classic source for this concept is Chalmers Johnson, *MITI and the Japanese Miracle*, Stanford 1982. See also the important new collection edited by Meredith Woo-Cummings, *The Developmental State* (forthcoming).

The Emergence of 'Catalytic' States

The final strand in my argument is that we are witnessing changes in state power; but these changes have to do not with the diminution but with the reconstitution of power around the consolidation of domestic and international linkages.

As macroeconomic tools appear to lose their efficacy, as external pressures for homogenization of trade regimes increase, and as cross-border flows of people and finance threaten the domestic base, a growing number of states are seeking to increase their control over the external environment. State responses to these pressures have not been uniform. They have varied according to political and institutional differences. But, in general, one of two strategies has prevailed. Both involve building or strengthening power alliances: 'upwards', via inter-state coalitions at the regional and international level, and/or 'downwards', via state-business alliances in the domestic market.

To the extent that states are seeking to adapt and reconstitute themselves in these ways, they can perhaps best be seen as 'catalytic' states, to use Michael Lind's term. Catalytic states seek to achieve their goals less by relying on their own resources than by assuming a dominant role in coalitions of states, transnational institutions, and private-sector groups.

As a catalyst, this kind of state is one that seeks to be indispensable to the success or direction of particular strategic coalitions while remaining substantially independent from the other elements of the coalition, whether they are other governments, firms, or even foreign and domestic populations.[49] Thus, far from relinquishing their distinctive goals and identity, states are increasingly using collaborative power arrangements to create more real control over their economies—and indeed over security. As such, these new coalitions should be seen as gambits for building rather than shedding state capacity.

There are many who would support the claim that we are witnessing the end of an era marked by the 'integral state', with assured territorial control over the means of legitimacy, security, and production. But at a time when serious analysis of 'state power' or the 'state's role' has become academically unfashionable, there will undoubtedly be less support for Lind's assertion that in place of the integral state we are now witnessing the rise of the catalytic state.

To what extent can the catalytic state be generalized? The first point to make is that 'catalytic' is being contrasted with 'integral'. It is a way of highlighting the tendency of states to seek adaptation to new challenges by forging or strengthening partnerships with other (state and non-state) power actors, rather than going it alone. Consolidation of such alliances is taking place primarily at regional and international level, between states, though also domestically, between states and corporate actors. The proliferation of regional agreements between nation-states—includ-

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[49] Michael Lind, 'The Catalytic State', *The National Interest*, no. 27, Spring 1992, p. 3.

ing the EU, APEC, and NAFTA—can be seen as one manifestation of this tendency. The evolving character of close domestic government-business cooperation, most notably in East Asia, is another.

The second point, however, is that even catalytic states have differential capabilities: some, like Japan and Germany, have both domestic and international clout, and hence are able to use their domestic leverage to position themselves advantageously, for example, in regional coalitions. Others, like the United States, exploit strong international leverage but at the expense of domestic adjustment capacity. Still others, like Russia, are so lacking in domestic capability that they are not even serious candidates for the kind of regional coalitions they otherwise might aspire to lead or join.[50]

Recent examples of states using international agreements as a means of pursuing domestic economic goals include such initiatives as NAFTA and APEC. While both weak and strong states enter into such alliances, it is often the domestically weaker states which take the lead in seeking out this external path, aspiring to constrain others to adopt their own more 'hands off' approach to trade and industry. Australia's enthusiastic efforts in seeking to establish APEC, and the United States' leadership of NAFTA can be seen in this light. These states, with their traditional 'arms length' approach to the corporate sector, lack the more strategic capacities of their East Asian counterparts. In the absence of a normative and institutional base for strengthening developmental capabilities at home, both countries have sought instead to 'level the playing field' outside their domain. To this extent, one might agree with the conclusion that unlike the EU, such moves are driven not by a supranational vision but by 'insecure governments' seeking 'new tools to stimulate growth, employment, and a stable regional policy community'.[51] To make the point in slightly different language, regionalism (inter-state coalitions) without domestic capacity (public-private coalitions) is only half the story, akin to conducting a war of movement without having established a war of position.

What this analysis suggests is that the most important power actors in these new inter-state coalitions will not be those initiating them—for instance, the US and Australia—but those who participate in them from a position of domestic strength. For the major solidity of Japan as a catalytic state in international coalitions is that it has developed robust capability at home via domestic (government-business) linkages. By contrast, the major weakness of the US is the underdevelopment of such linkages, reinforced by the overdevelopment of external strength.[52]

If this reasoning is accepted, then we must enter a caveat to the notion of the rise of the catalytic state. Domestically strong states will more likely

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[50] I am grateful to Victor Sumsky for the observation about Russia.
[51] Ikenberry, 'Funk de Siècle', p. 124.
[52] For an accomplished discussion of this issue, undertaken from an historical and comparative perspective, see John M. Hobson, *The Wealth of States: A Comparative Sociology of International Economic and Political Change*, Cambridge 1997.

act in concert with others; while domestically weak states—especially large ones like the United States—will not completely lose their 'integral' character. In such cases, rather than a concentration on power-sharing we can expect to find an oscillation, as weak states shift between acting alone—through, for instance, defensive protectionism and bilateralism—and with others.

Thus, in this new era, the most successful states will be those which can augment their conventional power resources with collaborative power: engaging others—states, corporations and business associations—to form cooperative agreements and 'consortia' for action on this or that issue. But by far the most important of these coalitions will be partnerships of government and business, for this goes to the very heart of state capacity.

In contrast to Hirst and Thompson's conception discussed earlier, both domestic and regional coalitions imply that the state is not so much 'devolving' power—in a negative sum manner—to other power actors from whom it then maintains a passive distance. Rather, the state is constantly seeking power sharing arrangements which give it scope for remaining an active centre, hence being a 'catalytic' state.

Responses to Globalization

Against the hypotheses of advancing globalization, diminishing state capabilities, and eroding institutional diversity, this paper has advanced three propositions. First, the world economy is an internationalized economy, increasingly a regionalized economy; but it is not genuinely a globalized economy in which territorial boundedness and geographic proximity have declining importance for economic accumulation. While money and finance have increasingly become 'global' in some—but not all—aspects of their operation, the same cannot be said of production, trade or corporate practice.

Second, convergence towards a neoliberal model of political economy is highly improbable. This is not simply because economic 'globalization' is rather more limited and subject to counter-tendencies than many accounts would suggest. It is also because nation-states themselves exhibit great adaptability and variety—both in their responses to change and in their capacity to mediate and manage international and domestic linkages, in particular the government-business relationship.

Finally, however, because domestic state capacities differ, so the ability to exploit the opportunities of international economic change—rather than simply succumb to its pressures—will be much more marked in some countries than in others. For while current tendencies in the world economy subject more and more national economies to similar challenges and opportunities, these are likely to solidify the institutional differences that separate the weaker from the stronger performers. Change is indeed occurring, but by the end of the millennium, one should be able to see more clearly that the changes in process in different national systems are those of adaptation rather than of convergence on a single neoliberal model.

The rise of East Asia, the national responses elicited by that challenge, together with the proliferation of regional agreements suggest that we can expect to see more and more of a different kind of state taking shape in the world arena, one that is reconstituting its power at the centre of alliances formed either within or outside the state. For these states, building state capacity, rather than discarding it, would seem to be the lesson of dynamic integration. As we move into the next century, the ability of nation-states to adapt to internationalization—so-called 'globalization'—will continue to heighten rather than diminish national differences in state capacity and the accompanying advantages of national economic coordination.

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