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Korean Choices and Patterns of Advanced Country Development

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INTRODUCTION

What can Korea learn from the political economies and development experiences of the most successful advanced countries? The lessons, as we shall see, cannot be reduced to a bullet list of policies and practices to copy or avoid. As we look to the advanced industrial nations for lessons, we must keep

in mind that each of them has found a distinct means to resolve the political as well as the technical problem of growth. The technical tasks are often evident: convert savings into investment, channel investment into the most productive uses, organize production competitively, and assure technological innovation and entrepreneurial activity. The political challenges are less precise, but economic development always implies social dislocations and the radical transformation of lives and communities. The losers from economic development will try to use whatever existing political position they have to resist changes that disadvantage them and to capture economic "rents", drawing subsidies that preserve their way of life but slow growth. Unless those that are dislocated and disadvantaged are bought off and co-opted through compensation, or simply beaten politically, an endless series of conflicts and disputes will disrupt the market. When prices become unstable, market rules unclear, and profit calculations unpredictable, even ordinary transactions become difficult. Runaway inflation, for example, is a sure sign of unresolved political conflicts and can be a real threat to the normal functioning of an economy.[1] During an intense period of inflation in Argentina in the winter of 1989, a sign in a store window read: "Closed for lack of prices".[2] In the 1960s and 1970s, struggles between unions and management in the British automobile industry impeded and distorted both product development and production innovation. Case after case teaches us that political stability is essential to economic development. The primary political goal, then, is reasonably straightforward even if difficult to make precise: establish a stable means of allocating the gains and pains of growth among the winners who profit from the process and the losers who are disadvantaged. Unless a country is able to effectively allocate the gains and pains of growth, it will sink into a morass of conflicts, powerless to adopt cohesive development strategies or even focus on immediate technical tasks. This central political challenge must not, however, disguise the equally important need to match the policy and marketplace capacities to the everchanging economic tasks that must be resolved. These are precisely the challenges the advanced industrialized countries have met, and why we look at them today for lessons.

Unfortunately, the advanced country models are varied and can teach different -- seemingly contradictory -- lessons. To begin with, there are diverse forms of capitalism and a range of successful market systems. There is no such thing as a single, idealized, natural form of the market economy whose proper functioning is only distorted by political intervention. There is no single best way to structure an economy, to reconcile resources and demand, to organize and promote markets; each particular economic circumstance must be matched with an appropriate political strategy for growth. We must be clear that political rules and institutions create markets; markets do not exist apart from political rules and institutions that structure how buying, selling, and the very organization of production take

place.[3] But despite the great diversity of the political resolutions we will observe in the advanced countries, similar technical tasks (how to channel resources and organize production) and political problems (how to assure a stable political foundation for markets) must be solved.

There is no single best way for a country to become rich and powerful. Firm strategies and government policies required for British success in the early 19th century, for example, were very different from those required by Germany toward century's end.[4] The organization of the shopfloor that supported British industry was in turn radically different from the American system of mass manufactures in our century. Success does not come from copying a dominant form, but from adaptation and local innovation. The pattern of flexible specialization created and unveiled in Northern Italy resulted (unexpectedly) from efforts to implement traditional models of mass production, just as the Japanese production system emerged from efforts to imitate America. Industrial success is only assured by continuous adjustment and adaptation. Solutions that worked in one era become obsolete when new tasks emerge that cannot be addressed by old approaches. What worked fifty even twenty years ago will almost certainly not work today.

Yet, at any moment, the political economies of the most successful economies become models for the others. The secrets of growth are sought in the particulars of corporate strategy, mechanisms of policy, and the means of organizing political life. When in the 1960s America was at its peak of power, the airport bookstores carried titles like The American Challenge and The Secrets of the American Giants.[5] Now, twenty years later, nearly identical titles substitute Japan for America--books like Trading Places and Kaisha.[6] Unfortunately for those who yearn for simple political and economic equations, when the institutional arrangements of one country are copied by another, the economic results are rarely the same. The special difficulty for the analyst, then, is not only to describe different national arrangements, but also to locate their critical and indispensable features. But even descriptions are problematic since there is no real agreement about how economies such as Germany or Japan actually operate. Different scholars often provide profoundly different pictures of the same place -- almost as if they have visited different countries and accidentally put the same country name on their writings. Cartoon caricatures compete for attention. And the most visible features are not always the most significant. How, then, do we reason about the experiences of the advanced countries and draw implications for Korea or other industrializing nations?

Let us review the line of reasoning this essay will undertake. The advanced countries often face quite similar problems in the effort to sustain growth, but they resolve them in different ways. The particular historical course of each nation's development creates a political economy with a distinctive institutional structure for governing the markets of labor, land, capital, and goods. That institutional structure shapes the

dynamics of the political economy and sets boundaries within which government policies and corporate strategies are chosen. Predictable patterns of policy and strategy emerge. The institutional structure induces particular kinds of corporate and government behavior by constraining and by laying out a logic to the market and policy making process that is particular to that political economy. These typical strategies, routine approaches to problems, and shared-decision rules create predictable patterns in the way governments and companies go about their business in a particular political economy. Those institutions, routines, and logics represent distinct a capacity to address particular sets of tasks.

As long as capacities match the tasks at hand, all is well. Unfortunately, growth demands that tasks evolve and capacities shift -- creating a need for continuous political and technical adaptation. The tasks required to sustain economic development evolve as a function of internal growth. Rising incomes change consumer demand, for example, and wealth changes the process of investment. The locus of industrial growth may shift from one industry or technology to another -- for example, textiles gave way to chemicals as the engine of growth in Europe in the 19th century; in our own era, electronics suddenly began to create new products, transform old ones, and alter the organization of production. Tasks also evolve as a country's place in the international system changes (the United States, for example, lost its capacity to singlehandedly organize international financial markets). Similarly, policy and corporate capacities are not fixed for all times but grow and degrade. The institutional structure of the political economy evolves in response to shifting political balances, the emergence of new interests and groups, and changing markets. Thus, for example, the financial systems of each of the advanced countries have been reregulated and deregulated over the last decade, creating a global wholesale financial market and changing the national mechanisms for assuring industrial investment.7 Solutions to new problems must always involve a new match between tasks and capacities.

This essay develops the implications for Korea of the experiences of the advanced countries in four steps. Part I draws a baseline in the post-WWII political economies of the advanced industrial countries. The cases of Japan, France, Germany, Sweden, Britain, and the United States are briefly reviewed. We then consider three models of industrial adjustment and change, models that represent three distinct ways of resolving the basic technical and political problems of industrial adjustment. The foundations of these models lie in the institutional structure of the economy. That institutional structure reflects the social arrangements and organizations in the market built by political settlements. Part II considers how the institutional structure, the foundation of each of these models, induces patterns of and sets boundaries to government policy and corporate strategy. Policy, corporate strategy, and arguably production organization in each country have distinctive

features that reflect those structures. The result is that countries and companies tend to do what they are good at. That is, they have distinctive capacities and tend to apply those capacities to problems, usually without regard to what works. Crisis occurs when there is a mismatch between task and capacity. Several countries are considered. The section also argues that the Japanese production revolution and consequent success in international markets is best understood in this way. Part III considers the evolution of the advanced countries' political economies in recent years. This is particularly difficult because there are multiple and sometimes contradictory trends, because many of the lines of development are not yet resolved, and because there is little agreement about what is in fact happening. The essay concludes by speculating on the implications of both the experiences and recent developments of the advanced countries for the choices Korea faces.

I. Political Settlements and Industrial Development: Advanced Country Patterns in the Postwar Years

For the advanced industrial countries, the period immediately following WWII offered more than the burden of physically rebuilding; it represented an opportunity for political and institutional reconstruction. No one development strategy dominated all these countries. These different roads to development demonstrated that several patterns of industrial change were possible, and that there was more than one way of arranging governments and markets to achieve growth. Indeed, three distinct models of industrial development and adjustment emerged. Each model embodied: 1) technical capacities for state action in industry; 2) a political settlement allocating the costs of industrial change; and 3) a political process by which that settlement was reached. The three models of change were:

(1) state-led adjustment with developmental objectives in which a distribution of costs and gains is imposed by political manipulation of the market.

(2) negotiated adjustment with a corporatist tone in which there were explicit bargains amongst elites representing segments of society.

(3) company-led growth with the government principally a regulator and umpire, with the political settlement simply left to the market, and with government providing some small compensation to those who complain the loudest.

The advanced countries shared the same central problem: how to reallocate resources among different economic sectors. In the quarter century from reconstruction to the great oil crisis, growth rates were very fast in one set of countries (see Table 1). These were countries that faced radical reconstruction and development --Germany, Japan, France are the examples here -- and transferred, in relatively short order, much of their resources out of agriculture and into industry. In the more mature

economies -- the United States and Britain, for example -- growth rates were slower; the challenge to reorganize production in already established industries proved surprisingly difficult. Industry and labor, whose political interests were deeply entrenched, had to be displaced. Political protection (in the form of trade restrictions and subsidies) was an alternative to the flexibility and adaptation that growth required. By the end of this long period of growth and development, all the countries eventually faced this problem of sustaining growth by reorganizing industry and adjusting it to competition in international markets, and we return to this problem in section III.

I.1. The Foundation of the Adjustment Models

These three models of industrial adjustment are distinguished from each other by the way their politics and markets are organized.8 Institutional arrangements of market and administration define the settings in which political fights about the economy occur. They structure the political conflicts over industrial change and economic policy. The institutions, both economic and political, in which those fights occur articulate how groups must organize to achieve their objectives, often who their allies will be, usually what their tactics must be, and certainly what can be obtained by them from government.9 Of course, these arrangements are evolutionary: institutional arrangements have their origins in the processes of industrialization and political development; they are, in a sense, the products of past conflict, and continue to respond to a country's economic and political shifts. But institutions, once created, are not infinitely malleable. Indeed, it is a fundamental feature of the advanced countries that their political and economic institutions do not radically change with each shift in the balance of political power. Rather, existing institutions are used for new purposes by new groups.

The institutional capacities that concern us as we examine the stories of the several efforts to maintain growth are:

(1) the government's institutional capacity to shape adjustment by setting rules and allocating resources selectively toward purposes it defines;

(2) the possibility of negotiations among the major producer groups; and

(3) the flexibility of the shopfloor.

Those capacities in turn hinge on character of the state, the financial system, and the labor market. We return to the foundations of these capacities after reviewing several of the national stories.

I.2. State-led Growth in Japan and France

State led development in France and Japan was ultimately a conservative modernization in which agricultural and traditional businesses were cushioned against (but not protected from) the consequences of development. The central process in both was a shift of resources out of agricultural into industry and a

modernization and then internationalization of industry. The political problem in both was that the very groups that had to be displaced -- agriculture and like groups in traditional society -- were the political base of the conservative governing parties. While the patterns of development were in many ways similar, Japan surged to a position of real industrial power while French growth often stuttered and stammered, leaving Germany today as the industrial leader in Europe. The differences between the two countries lay in the depth of the political commitment to rapid industrial development, the intensity of internal industrial competition, and in the creation of distinctive industrial advantage -- in each case greater in Japan than in France. However, if we focus only on Japan, we may be deceived into believing that the developmental model or state led model is, in itself, an automatic formula for development. It is not; there are substantial political and technical risks for those who attempt such a strategy. A strident political challenge by the outsiders and losers is automatically invited by this strategy. The principal technical risk of state led growth is a government's temptation to try to compel markets to conform to its preferences and purposes, which often produces huge waste and market failures. The more successful government policy alternative is to use the instruments of support to accelerate market processes. For our purposes, the French story of state-led growth is as important as the more popular Japanese saga.

In the state-led model of development, the government bureaucracy attempts to orient the adjustment of the economy by explicitly influencing the position of particular sectors, even of individual companies, and by imposing its choices on the politically weakest groups in the polity. The state seeks to select the terms on which sectors and companies confront the market, either by explicitly providing resources to favored groups or by creating conditions that will force the recalcitrant to adjust. The state is an economic player; that is, an actor in the market system working toward purposes it defines, pursuing a specific agenda of economic development. It is not simply a regulator or administrator. When the state is an economic actor, finance can act as an instrument of the bureaucrats, permitting them to intervene in the affairs of particular firms and to allocate capital between competing uses. A state-led adjustment process politicizes and centralizes the process of industrial change. Those firms and groups excluded from the circle of the "court" favorites are evident, and they can plausibly blame whatever plights befall them on their political weakness rather than on their economic incapacity. Consequently, a government imposed balance of the costs and gains of change rests on the continuing ability of the executive and the groups who are political winners to exclude the losing groups from policy making. The system is inherently taut.

The institutional structure of our two state-led economies, Japan and France, are very similar. With an institutional map of the American economy as guide, an analyst or visitor would be lost in either Tokyo or Paris; but a visitor from Paris can find

common institutional and political referents in Tokyo, and, as a result, such visitors often misunderstand how different the economies of Japan and France work. What, then, are the common features between the two countries? First, there is a state executive with considerable autonomy from the legislature and which has a hand in shaping the interest groups that lobby it. Second, a credit-based financial system provides the executive of both governments instruments to shape -- on a selective basis without direct legislative intervention -- the overall flow of funds in the economy. This financial system also allows the executive to intervene in a detailed way in industry. Indeed, this credit based-system was a important base of autonomy since the routine management of finance provided the executive with discretionary control over a truly significant piece of the nation's finance -- discretion that could be used for purposes formulated by the executive alone. Third, there was no centralized coherent labor movement which linked power at the shop floor to power in politics. (The fragmentation of labor and the government's means for limiting autonomous influence in the factory were, however, very different in each country -- with the result that Japan had fundamentally different capacities for production reorganization and technical innovation.) In each case a conservative coalition, facing the similar political problem of managing the transition to an industrial economy with a political base rooted in small towns and agriculture, used this structure to create a state-led strategy of development.

Japan: The story told here is of Japan in its post-war development phase, a system of state-led growth.10 The character of growth and the logic of the political economy have evolved, but we need at least a clear baseline to understand those changes. The Japanese government, dominated in the years after WWII by a conservative coalition, used the institutions of a centralized state to create a developmental policy. Crucial elements of market arrangements that facilitated rapid adjustment and growth were the product of conscious choice in the post war years. The Japanese government has pursued a conscious strategy of industrial development that has influenced the nation's patterns of domestic growth and international trade. The government influenced and shaped the dynamics of a highly competitive market economy, generating a system of controlled competition. Competitive markets induced the investment that underlay rapid growth and manufacturing innovation. The particular character of the interplay between policy, markets, and corporate strategy created and continue to sustain the logic which patterns Japanese development and foreign trade.11

"Bureaucrats rule and politicians reign," a phrase popularized in the United States by Chalmers Johnson, captures the flavor of the system. The conservative dominated legislature controlled by the LDP assured support for the broad objectives of growth and development. The multiseat district helped mute substantive policy and personality conflict and certainly facilitated the emergence of the LDP that diffused and mastered opposition. The

then secondary bureaucracies -- such as post and telecommunication, education, construction, and transportation -- provided means for patronage that could support a particularized electoral system. However, the ministries with broader economic objectives such as MITI and the Ministry of Finance had substantial autonomy. The general concern of the government, both prewar and postwar, was development, leading it to be labeled a developmental system.

Policy had two crucial elements: controlling the links between Japan and the external economy, and promoting industrial development within. The government, to use T.J. Pempel's phrase, was gatekeeper and promoter.12 As gatekeeper it controlled the terms on which foreign investment could enter the country and on which technology could be licensed. This consequently broke apart the package of the multi-national corporation, permitting Japanese controlled firms to develop product and technology in Japanese markets. By preventing Japanese firms from bidding against each other for licenses, the government kept the price of imported technology low. As a promoter its efforts were diverse. The government supported corporate efforts to import foreign technology at low prices. It assured financing to favored sectors and helped sustain a flow of investment by guaranteeing bank lenders that the risk of industrial failure would be minimal. Its role in supporting domestic research to develop imported technology has been depicted in projects such as VLSI. Equally important, the government supported technology diffusion through joint research efforts and through networks of technology agents that spread advances to small and middle size firms.

A crucial instrument in the promotional policy was the credit-based financial system. The financial system, as Kenneth Courtis of Deutsche Bank has remarked, was an instrument of policy not an object of regulation.13 Without entering into the details of the system, administratively set interest rates and a shortage of capital investment encouraged industry's demand for bank funds, demands that exceeded the supply of available. Firms therefore found themselves dependent on bank finance, and banks in turn found themselves dependent on the good will of the Bank of Japan and the Ministry of Finance, which created money to fill the excess demand for funds. The government thus assured funds to the most important growth sectors in the economy, setting up channels that collected funds from agriculture and funnelled them into industry. Yet agriculture and small business were not denied funds either. Through subsidy and dedicated lending facilities their needs were met also.

As important as the policies for industry were, the character of the labor relations system created the basis for flexible adaptation and adjustment in industry. There were political arrangements which limited the direct national confrontation between labor and industry and effectively excluded labor from political power. At the same time, labor was effectively integrated into shopfloor operations and given real responsibility. An odd mix, but it worked.

Industrialization is by no means a straightforward outcome of

policy intent. Policy, as we have noted, only structures the logic of markets by creating a pattern of incentives and constraint, and in that sense induces corporate response. An interpretation of industrial outcomes must therefore characterize the organization of industry. Japan is characterized at once by very intense domestic competition and by a range of mechanisms for cooperation or collusion. Whether it is joint planning of expansion in capital-intensive industries to avoid excess capacity and to assure the introduction of plants of sufficient size to capture scale economies, or joint research on generic technologies, or reallocation of domestic market share in the aluminum industry to firms that move production offshore, or efforts to allocate domestic market to foreign firms -- the evidence is overwhelming that competition is bound or orchestrated. The deals may or may not be stable; that is, the market divisions may or may not be fixed. However, market outcomes are certainly different because mechanisms for collaboration, collusion, and bargains exist. Elaborating how this Japanese system works requires specifying the rules of controlled competition -- in other words, the terms and circumstances of competition and the terms and circumstances of collaboration, a task not undertaken here.

A second major feature of the economy is that Japanese industry combines the strengths of large firms that are able to mobilize substantial resources in the pursuit of long term objectives and the flexibility and innovative nature of small firms. And indeed Japanese government policy supports both. We will return to the consequences of the their interaction later.

Inflation reconciled the political and technical problems of growth in these years, as I will argue in detail in the French case. That is, money was provided to meet the nominal demands, but those producers who could expand and increase productivity most rapidly were the winners. The expanding sectors could outbid (i.e., pay more) the traditional sectors for productive resources. Thus over time the market shifted the position of the different groups in the economy, but shifted them with inflationary consequences. Inflation was a means of avoiding direct confrontations. Excess money supply was tolerated, itself inflationary. The costs of buying a shift in resources out of industry into generated a demand shift inflation. Winners were those sectors with the greatest potential for expansion and productivity growth who could pay the most in the competition for resources, drawing people and funds to them. Losers were those who could not keep up with the inflation or whose relative position deteriorated. The result was that the apparent direct contradiction between the technical requirement of satisfying industrial needs and the political requirement of satisfying an agricultural and small business constituency was sidestepped.

France: In France, very similar institutional arrangements were employed to shift the political balance in favor of policies that supported rapid growth and development. On balance, government policies before WWII supported the suppression of markets, or better, their control to limit social dislocation

from growth and development. The broad consensus that existed in Japan to support development did not exist in France. After WWII a coalition of modernizers had to be built, and sustained. Indeed, only WWII and the later Algerian crisis permitted a small modernizing elite with limited popular support to re-orient the economy. That elite broke the established group's hold on economic policies.14 The Planning Commission was established and helped reformulate government purposes. The state treasury, the tresor, transformed and expanded its function, giving the government the capacity to implement some of its ideas. But the electoral foundations of a developmental strategy did not yet exist.15 This first phase of reform--the de Gaulle interregnum between the war and the creation of the new 4th Republic--amounted to a re-orientation of the state and creation of new instruments of policy.

The Algerian War generated a second break in French political life. When de Gaulle returned to politics he established a presidential political regime that became the instrument of a growth strategy. In the name of French national glory, de Gaulle rallied many social elements that would have opposed a project of development and economic transformation. In that regime many traditionalist electoral elements, whose economic interests would lead them to oppose developmental strategies, found themselves trapped in a national coalition in support of de Gaulle. The groups were held in place in the coalition by nationalism, and then transformed by the market. This established a new political base for a developmental strategy. It pitted the traditional elites of France's rural and small town past against the forces that favored industrial development. In response to this conflict, the state pursued competing and seemingly contradictory purposes -- fostering growth while simultaneously containing its political consequences. The arrangements of the financial system enabled it to target financial flows to specific uses, the government was able to subsidize groups that resisted change while strengthening the market forces that favored growth. In short, it can be said that the government devised a policy mix that force-fed the economy's high-growth engine high octane fuel while at the same time stepping on the brakes.

One limit to the French strategy lies in the character of French industry. French industry after WWII was composed primarily of small to medium size companies that had been insulated from foreign competition for decades. Long protected and often cartelized, most of the industry had experienced little internal competition. Following a growth strategy, government acted to force French firms to adjust to competition and international markets. Part of that strategy involved creating a more competitive domestic market by inviting foreign competition. The creation of the European Community exposed French industry to intense German competition and drove the weaker firms to turn to state assistance. The state assisted the transformation of the insular French firms into modern corporations. The specific industry policies, many of which were badly mistaken, must be measured against the political challenge of keeping French

industry alive while it changed and adjusted. France, though, could never really implement a full blown development strategy. It did not have the powerful mix of large and small firms tat existed in Japan. Nor could the French insulate their market, since French policy makers needed the EEC to force competition and corporate modernization. As a result, the French ended up with a state-led policy of limited development; indeed political commitment to growth was partial and forced.

One real difficulty the French experienced in implementing a strategy of state-led growth arose from the government's inability to follow the market; that is, use the instruments of intervention to amplify market signals. Instead, it had to create the market and generate market pressures. State policy tended to push firms to adopt strategies that were not viable in the international market, a problem we return to in a moment.

The deeper problem was political. A state-led strategy where the government was thought to be capable of creating industrial and distributional outcomes made it difficult for a government to avoid responsibility for virtually any economic or social outcome. As a result, the conservative political strategy inevitably became, at least in part, confrontational. It was a politics of social division. Part of the strategy turned on the need to isolate the Communist Party. Or, more precisely, because of the presence of the CP, the conservatives could organize a nationalist strategy of confrontation against a class and country enemy. It was, as well, a strategy of labor exclusion, a strategy aided by the divisions inside the labor movement itself. For the conservatives, organizing against the CP was an opportunity.16 Remove from the political calculus the CP's twenty percent share of the vote and the electoral arithmetic meant that the non-communist left simply could not capture power.17 The non-communist left could only win (and in fact did win in 1981) in alliance with the communists. Consequently, the conservative parties consistently campaigned against the Communist threat to both private property and national integrity, suggesting that any left coalition was profoundly dangerous to French traditions. Without reviewing French political history between the world wars, we must simply note that the virtual civil war over both national and international political issues gave, in the end, even greater power to the conservative appeals. The strategy contributed to a sharply divided society and a sharply divided factory floor. The divisions inside the conservative party (the party conflicts between Gaullists and non-guallists, to simplify a quite complex political map) were, in turn, eventually exploited by the left. Led by François Mitterand, the Socialists in alliance with the communists took power in 1981. Surprising to many, a decade of left power saw a steady relaxation of social and political tension.

In sum, the French commitments to development were weaker than those made in Japan. They were commitments created only by marginal political victory and external pressure. The absence of the kind of broad political consensus Japan enjoyed prevented any possibility of a strongly focused national growth strategy. So

although France and Japan had similar set of institutions, they were used differently in each country.

I.3. Negotiated Growth in Germany and Sweden

Negotiated growth involves explicit and continued bargaining over the terms of industrial change by the predominant social partners. The notion of partner, in fact, is central. Although the several groups -- labor, management, agriculture, for example -- have distinct interests, those interests are thought by all to be pursued best within common frameworks. Bargaining among partners implies that a number of outcomes are recognized as legitimately being settled by discussion rather than in the market or by political dictate; that is, settled by compromise rather than imposition. Democratic corporatist bargaining implies that the stronger do not use their advantages to take away the negotiating rights of the weaker; that is, deprive them of effective representation or attack vital interests.18

The bargaining base of these social partners rests on both the organization of politics and policy making as well as the institutional arrangements in the market. In the Netherlands, for example, the character of parties and interest groups creates the basis of negotiation. In Sweden, by contrast, labor market organization and a powerful labor party establishes the foundation of the negotiated system. Although politics and policy making were dominated for many years by labor, corporate decision-making remained the norm of the economic system. In Germany, the powerful universal banks play an almost parapublic role in the financial system and in resolving the particulars of corporate crises. At the same time, a strong Social Democratic party, strong unions, and effective mechanisms of labor representation within companies (they are not the same in Germany) create a second institutional foundation for bargaining. The Swedish and German cases suggest that a powerful position in one market -- labor or capital -- can provide the basis for entering into political bargains about the operations of other markets.

Note that this conception of the foundations of bargaining is much more extensive than the widely discussed notion of neo-corporatism. The conception here includes the bargaining ties between finance and industry as basis for social bargaining, as well as arrangements in the party/political system as a solution to divisions rooted in ethnic, religious, and language divisions. Neo-corporatism focuses on the social democratic cases and the important place of labor as a foundation for negotiated settlements. Fritz Scharpf provides us with a clear definition of neo-corporatist bargaining founded in social democratic parties. He argues:

> "Neo-corporatism implies specific organizational structures of unions and employer associations, specific types of industrial relations, and specific relations between the 'social partners' and government policy makers. As an ideal type, which was approximated in Scandinavia and Austria during the 1960s and 1970s, the neo-corporatist models is

defined by the coexistence of the following characteristics: a monopolistic union movement without ideological cleavages or competing craft unions and concentration on the employer side; centralized collective bargaining; and participation by the peak organizations of labor and capital in the formulation of government economic and social policy."19

The set of social democratic countries is particularly important because during the 1970s, and arguably early 1980s, these countries were quite successful in their fight against unemployment and inflation, even as they expanded the welfare system.20 The response from a critic of these countries might well be that while they were successful at managing the price and employment dislocations of the 1970s, they were much less successful in the 1980s arranging the structural and production reorganizations required by fundamentally changing patterns of international competition. The reason seems simple. In the first period overall wage growth arrangements had to be reconciled with productivity growth to avoid inflation and to maintain competitiveness. In the second period, the problem became one of adjusting the relative wages different sectors and re-arranging shopfloor labor rules

Why are such bargaining arrangements useful? Again, Scharpf is helpful. He notes that if government is to influence economic actors, those actors must be able to recognize unequivocally the direction of policy. In a chaotic world the overall direction of government policy as well as the action of other critical actors is difficult to determine. Therefore, when "union and management elites are continuously and jointly involved in economic policy making, they are likely to be fully aware of each other's interests and interpretations; and if opportunities for improving overall economic performance through joint action exist, they are more likely to make use of them".21 In the language of this essay: the search for a technical solution becomes entangled with the search for a political solution.22

For Korea there are two particularly significant issues in the stories of the countries with negotiated patterns of industrial adjustment. First, in each of these cases a negotiated aspect to market processes did not occur automatically; it was not derived from historically rooted features of the society. Rather, each system of negotiation was created to resolve specific political conflicts that could at the time threaten to tear the society or paralyze industrial adjustment. The character of the political settlement is evident in the Scandinavian cases. Through the twenties and thirties labor conflicts led to intense industrial conflict, the threat of authoritarian solutions. Then, quite abruptly, political deals were struck that moved many issues from the corporate to the policy arena and strike rates dropped dramatically.23 Second, in each case a legitimate position for labor within political and industrial life produced flexibility, policy flexibility and shopfloor flexibility.

We consider two cases here, Sweden and Germany. Sweden is important because it has been in the past a full blown form of Social Democratic corporatism. Germany is significant both

because of its evident central economic importance within Europe -- which makes it crucial to the last part of our essay -- but also because it suggests the importance of financial market arrangements in this model.

Sweden: Sweden, along with its Scandinavian neighbors, is a small, very wealthy country in a rich part of the world. It, like its peers, has become wealthy both by adding value to products often innovated elsewhere and by finding market niches that it can defend. It also has a few very powerful firms that are European and often world leaders, such as ABB in power generation, Erikson in telecommunications, and Electrolux. With enormous traded goods sectors, these small countries must adjust both their production structure and macro-policy to international shifts. How they do this is the question.

The original corporatist pattern of governance emerged as a response to economic crisis during the 1920s. Sweden developed a strong centralized labor union movement, the LO, and a Social Democratic Party that has now governed -- alone or in coalition -- for almost all of the period from the late 1920s to 1991 (with the exception of the years 1976-79). The September election brought the conservatives back into power. It is unclear whether this conservative government will simply be an interlude that ends with a recreation of a labor-agriculture alliance or, as the conservatives intend, an end to the welfare era.

After WWII Sweden evolved a very distinctive model of macroeconomic management, a model perhaps possible only in Sweden's institutional environment.24 The model operated from the late 1950s through the 1970s. The model really ended in the early 1970s -- before the first conservative victory -- when the farmer's party withdrew from the coalition.

The Swedish strategy at once settled both macro-economic issues and set the terms for the structural adjustment of industry. An industrial policy was pursued through wage policy. The elements were worked out self-consciously and executed purposively. First there was a solidaristic wage policy which aimed at raising low wages or more precisely at reducing wage differentials. This policy required centralized wage bargaining to harmonize wage rates among sectors and social groups. It also required mechanisms for limiting wage drift so that the broad national bargains would not be undermined by sector and company specific deals. Wage rates were set that could be accommodated not just by the top few, but by most above-average firms as well. Since wage rates set for above-average firms would arguably limit profits for those below average firms that didn't reach that standard, those weaker firms would be forced to adjust or exit. The policy notion was to run a budget surplus that would be re-channeled into industrial investment. Government savings would supplement company savings.

Those relatively high wage rates and the continuous pressure to reduce wage differentials did put real pressure on all but the best firms. It encouraged both structural shifts (the movement of resources from sector to sector) and production reorganization

(changes within the firm). That was the intent. A retraining strategy to relocate labor to expanding sectors and firms and away from less productive operations, proved a crucial element of the strategy.

Finally, the government distinguished firms engaged in international trade and facing sharp international competition from those in protected sectors that produced only for the domestic market. Government and corporate structures operated under the assumption that the competitive position of Swedish industry could only be maintained if the sectors exposed to international competition took leadership in wage negotiations. Protected sectors, therefore, had to follow the wage settlements of internationally competitive sectors. The Swedish model began to break down first with the end of the labor-farmer alliance and then in the late 1970s with the defeat of the Social Democrats. The central issue in the 1976 election was nuclear power, yet the radical shift in the broad competitive position of Swedish industry certainly created the basis of the Social Democratic defeat.

The competitive position of Swedish industry changed abruptly with the emergence of countries like Japan and later Korea in global markets for autos and ships. The adjustment problem was profoundly altered. Previously, the task had been to shift labor from one metal bending activity to another, or for firms to find the niches in which they could capture substantial value added. Suddenly, as a set of Swedish firms found themselves in trouble, the task changed. At the same time, changes in the international financial system added competitive pressure. The collapse of the dollar-centered international system saw a mark based European financial system and limited devaluation strategies of adjustment. Production had to be reorganized internally to meet dramatically new competition. Workers required re-education, not just retraining.

In power, the conservatives between 1976-79 found no policy alternatives to the Social Democratic adjustment formula. Without fully mastering the situation, conservative governance saw a sharp expansion of the public sector and the deficit. The Social Democrats retook power in the election of 1979, but the negotiated arrangements of adjustment were never recreated. Both the management of the public sector and the adjustment within firms became an enduring problem. In the last few years the Social Democrats have sought a new adjustment strategy as their electoral position weakened. Sweden applied for membership in the European Community and radically reorganized the tax system. Once out of whack, an adjustment strategy is hard to recreate. It will be some time before we can assess whether the conservatives can invent a new formula.

Germany: West Germany projects the image of a liberal market economy in which the most important decisions about the uses of the nation's economic resources are made by company managements driven by profit motivations and responding to price signals, not by bureaucrats following their plans or by politicians simply

following their voters. Indeed, during the 1970s the German case was used to demonstrate that if government would only ignore businessmen and workers in their demands to be protected from foreign competition and to be insulated from domestic change, inflation-free growth would result -- benefiting even those who bore the direct costs of adjustment. The inflation free nature of Germany's industrial resurgence was facilitated by an industrial structure that was well suited to the needs of postwar competition. The German economic success also suggests that it is much easier to avoid protection and restriction when rapid growth does not involve major structural change within industry. Nonetheless, the image of a liberal German economy -- with individual and self-contained firms competing in markets umpired but not managed by government -- is overdrawn. There are important elements of negotiated capitalism in the German story.

The German version of negotiated markets capitalism has more diverse foundations than the labor based Social democratic model in Sweden.25 The foundations consist of a centralized society and economy (a bank dominated financial system; a corporatist structure of interest group representation with centralized semiofficial trade associations; a strong union movement with labor rights in corporate management) and a decentralized state with considerable political autonomy in the lander or state government.26

Let us begin with the centralized economy and society. German capitalism developed a quality of organization, concentration, and centralization that the late Andrew Shonfield labeled "organized private enterprise".27 German industrial development, as Alexander Gerschenkron has taught us, required a rapid mobilization of resources for deployment in capital intensive sectors.28 Consequently, it followed a distinct course, different from that of, say, Britain. The commercial threat of its industrial predecessors and the military threat of its political rivals both urged quick growth and protection from competitors. The development of heavy industry required substantial concentrations of capital. A development strategy was constructed on trade protection with large firms, cartels, semi-official trade associations, and large banks. From the beginning giant export oriented firms were instruments of industrial growth in many sectors of the German economy. But concentration alone does not distinguish the German case. Giant firms and industrial concentration are typical of all advanced countries, though some countries such as France came to large firms late and others such as Japan and Italy maintained pools of small firms throughout industrial development. Organized arrangements between businesses were never viewed with automatic hostility, but were thought to provide elements of order in the unsteady world of market relations. Policy debate has asked whether particular cartels serve a useful public purpose, not whether they should exist at all. In Germany even small and middle size firms have been highly organized. An indispensable element of industrial development and export success, these largely independent firms (organized in many cases in industrial districts) have been a

crucial part of the capital goods and production equipment expertise that distinguished Germany throughout the years. Yet they too are organized into important trade associations and industrial districts.

Banks are an important cornerstone of organized German capitalism -- "prefects" monitoring order and leaders in the process of industrial adjustment. What is unclear is whether securitization and liberalization in the financial markets or the financial integration of the 1992 process will truly alter that system. The power of the German banks in industrial affairs rests on a foundation of legal allowances and unique financial structure. The legal right to own substantial stock in corporations and to exercise proxy votes for other shareholders permits a special latitude for the German universal banks. There are no prudential limits on banks' holdings, giving them the possibility of direct control. As recently as a decade ago the banks held in enough proxy accounts to vote 85% of all privately held shares and fully half of all shares outstanding. That voting power was concentrated in the three largest banks, which in the l970s voted 35% of the shares at annual meetings of the 75 largest companies.29 The unique structure of the German financial system forms the second foundation of bank influence.30 The banks as a group have a distinct place in the German system of financial markets. The securities market has traditionally been small, forcing firms to obtain capital through bank loans which meant that access even to equity was mediated by banks. Moreover, access to the securities markets was controlled by the banks. The major banks with industrial voting rights and influence over access to equity and debt sit at the center of the system of corporate finance.

Society, not just the economy, is centralized which also contributes to a style of elite negotiations by creating political parties. The institutions of interest representation are quite centralized, and equally important, often define semi-autonomous policy arenas. The result of the interest group centralization is to create for specific social groups the basis for negotiation from coherent islands of influence. Traditionally, when German interest groups are small with sharply defined boundaries they often do not face institutionalized opposition.31 The rules and regulations for that particular subgroup are then structured by the subgroup for itself, keeping the community at large at arms length. This is the case of doctors and farmers, for example. Recently, in policy arenas such as finance and international competition, European Community proposals have forced adaptation on these previously autonomous groups.32

The dominant economic interest groups, employer associations, and unions are centralized and class-based. Since the mid- to late-19th century, employer associations have been centralized -- in part to help promote the economic integration of the German community. Different business associations represent broad policy interests (BDI) and collective bargaining problems (BDA). Also a separate association for small business exists. (DIHT).33

The workers are much less organized (roughly 40% or less are in unions) than the business community (80-90%). While unions are organized principally along sectoral lines and a few principally white collar unions and civil service groups keep independence, there is a centralized union association (the DGB) representing the bulk of the organized working class with some seven and one half million members.34 Importantly, on collective bargaining matters, the union acts independently with their own strategies and strike funds. But one union, the metal workers with two and one half million members, has set broad patterns of wage and technology bargaining.35

Three elements of the labor movement must be highlighted to understand the framework of negotiated bargaining in industry within Germany. First, the unions and the dominant left party, the SDP, both stepped away from socialist commitments three decades ago (1963 for the unions and 1959 for the party). Consequently, both are committed to pragmatic resolutions of concrete problems. Second, the SPD is a viable alternative to the Conservatives, having held power alone or in coalition often since the war. Labor concerns are therefore expressed both through the political system and through the labor relations system, and labor positions are entrenched in both. Third, the system of co-determination, of worker participation in corporate management structures, is entrenched in Germany throughout the bulk of industry. The representatives are elected from a company's workers, not appointed by the unions. This both extends labor's voice and provides an independent institutional counterpoint to the unions. Equally important for challenges of industrial adjustment, the mechanisms of co-determination have linked the shopfloor to general management. Although these mechanisms were seen as a threat to capitalism and community when they were created, they now provide within firms an important means for adjusting to the new requirements of production.

In contrast to the highly centralized society and economic community, the state structure is very decentralized -- a characteristic which permits multiple points of discussion and initiative. German federalism, reminiscent of the United States, is remarkably strong when compared with Japan, Britain, France, or Sweden. Germany, recall, was created as a forced bargain amongst independent Principalities to provide a single market and common defense. West Germany was recreated after WWII with the intent of restraining central authority. The states have real and primary authority in many areas, from education and cultural affairs through the organization of the bureaucracy and the regulation of local government. Moreover, the administrative system itself is highly decentralized. The result is that the "federal [i.e., central] government has no choice but to negotiate and cooperate with centers of state power over which it has not control".36 Consequently, issues that cannot be negotiated at a national level will often be resolved at a regional level.

This decentralization of the state has significant industrial consequences. For example, small and middle size businesses have

always been crucial in Germany, despite the evident importance of the big business sectors. It is not simply that these firms are dependents of the larger companies; they also provide an autonomous source of product development, innovation, and exports. There are several different sets of small and medium sized firms (with quite distinct historical roots) which now depend heavily on local community institutions.37 Without this political autonomy it is doubtful such sets of firms could have emerged or adapted to survive in international competition.38

The national system of centralized society and decentralized state is stitched together by the overlap of administrative responsibilities between states and the federal government, by political parties, and by a group of parapublic institutions such as the Bundesbank.39 For example, Germany's Central Bank, the Bundesbank, has considerable independence -- greater than that of any other European Central bank -- and is a fixed point for policy. The Bundesbank's clear commitment has been to control inflation and the money supply. The strong union movement and labor-based political party have applied pressure to maintain employment, but over the long haul the Bundesbank's control of critical monetary variables has proven dominant; its weight generally fell on the side of inflation control at the expense of growth and employment. This was particularly evident in the consistent decisions to maintain high interest rates that pushed the value of the mark up, risking export markets.

As the mark strengthened over the years, creating the basis of a German mark dominated European Monetary System, German industry faced a perpetual adjustment and adaptation. To help industry adapt to these measures, a second kind of parapublic institution was formed: the German (really West German) system of vocational training that links public education to private industry. "Public vocational schools teach for a day or two each week general subject and some theoretical aspects of occupational training. The rest of the workweek apprentices acquire practical skills at the workplace..." 40 There are more than four hundred programs set up jointly by business and unions that are officially sanctioned and jointly funded but supervised by the chambers of commerce.41 The result has been, for the most part, slow and iterative change rather than radical policy redirections -- continuity with experimentation.42

As political party coalitions shift, the direction of this system of centralized society and decentralized state has shifted too. In the first phase, from the late 1940s to the mid-l960s, the conservative party (under the primary leadership of Adenauer) oversaw the creation of a welfare state, the inclusion of labor into the institutions of politics and corporate management, and the entrenchment of a commitment to market principles. The second phase lasted from the late sixties to the end of the seventies and was dominated by a center-left coalition of the SPD/FDP in the first years and by a broad national coalition of conservatives and social democrats in the later phase. This period saw collaboration among "the major producer groups, senior civil servants, and political leaders ...[to] bolster West

Germany's competitive position in international markets".43 The third period, one of a conservative government, has seen a troubled struggle to establish new lines of growth and development, culminating in the collapse of the Berlin Wall and the recreation of a unified German nation.44

The West German political-economy's style of negotiated adjustment has been very successful. Economic and industrial growth from the reconstruction, after WWII, to the unification has been remarkable. Both growth and productivity rates have been quite high compared to the other OECD countries, although the rates have not been as rapid as those of Japan or the East Asian Nics. The Germans have consistently chosen price stability over accelerated growth when choices had to made. The German pattern of trade shows broad strength across a range of sectors including advanced-technology, scale-intensive, and production-equipment (see Figure 1).45 German producers have even maintained strength in so-called traditional sectors -- by reorganizing production and product mix. The adaptation of industry must be broken into several groups.46 In the capital-equipment sector, German industry has been very powerful, often competing with innovations in sectors that are not price sensitive.47 In science-based sectors, German industry has been powerful in chemicals and pharmaceuticals. Its position in advanced electronics, by contrast, has been very weak, as indeed has been true of European industry as a whole. In scale-intensive sectors, German industry's position has been mixed. Mass production strategy came late and uneasily even to the automobile sector. Eventually Volkswagen did make adjustments.48 The late adjustment is either a new problem, making German industry vulnerable to Asian-based flexible-volume production strategies, or an advantage, permitting German industry to jump to new flexible specialization strategies.49

Germany has adjusted successfully to a series of sharp changes over the last few decades. Industry adapted to a rising mark; the economy slowed, but adapted to the oil crisis and stagflation. Now, even as East Germany is being absorbed, the debate is focusing on the Japanese and Asian challenge. The central question is whether negotiated adjustment will suffice in supporting industry to compete with new Asian competitors.

I.4. Textbook Economics and American Growth

Any standard American economics textbook will provide a clear statement of the third development model: company-led growth. Certainly all capitalist economies are organized around firms responding to price signals, and all western democracies assume the individual to be of central value and consequently at the root of political life. Nonetheless, conceptions of the market and political life vary. Some democratic political traditions -- including the French -- assign a creative, integrative role to government, the state, and political-economic life, while others picture social groups as central units in politics. The American conception of company-led growth is, then, a stark version of market capitalism and pluralist politics rooted in extreme

notions of individualism.50

In the American model of company-led growth, the government's only appropriate role is as an umpire,assuring that rules are followed; even regulation is often viewed as an improper interference with market processes, benefitting a few at the expense of the many. Instead of social partners seeking common technical solutions within a politically agreed frame, there are interest groups that have to be beaten back to maintain the market. Instead of an etatiste or corporatist style of politics, we have classical pluralism. In this arrangement, the government cannot, and indeed should not, have a strategic view. Only the market can signal the economic future, and only pluralist interest groups competing in an open system can determine political values. Consequently, government action in the market can only mean distortion and inefficiency on behalf of arbitrarily selected objectives.

Thus, in this system of company led growth with a regulatory state, the basic choices are made by individual firms without negotiation with government or other social groups. The result leaves workers or communities who are displaced or damaged to fend for themselves or to seek compensation as special interests making special pleas. The costs and gains of change are fundamentally allocated through the market. And because market outcomes are assumed to be legitimate, they are politically difficult to challenge. To be clear, there are analytic mechanisms for judging "market failure" and determining when private decisions based on prices do not express the best economic outcomes. Notions of "externalities" -- gains not expressed in price signals to individual parties, or spillovers and linkages between activities that affect future prospects--are expressed in theory. Those notions, though, are not the core of the theory and are awkward to use in practice or debate. Above all, the government does not take a view of the long run development of the economy and nor does it assume a developmental strategy other than to follow the market. All economic activities are judged by their current return, and future prospects are revealed, not created, so that a dollar's worth of semiconductors has the same inherent value as a dollar's worth of potato chips. The financial system then becomes a vehicle which allocates resources among competing uses, not an instrument for social negotiation or state intervention.

The American model of textbook liberal markets is a 20th century creation. The American model was in fact very different in the 19th century when there was an implicit, often even an explicit, strategy of development. America's de facto policy for industry now has three components. First, there is autonomy for corporate management, guaranteeing freedom from outside interference and particularly from government intervention. The extensive interchange and conversation between senior executives and the bureaucracy typical in much of the rest of the world is not present. Second, there is a basic consensus on the process of union management conflict and collaboration, a consensus that though open to negotiation has, in practice, reserved to

management the right to select production and technologies and lay off workers. (America is sometimes said to have a comparative advantage in closing plants.) Third, while there has been principled opposition to national and international trade restrictions, in practice policy has accommodated demands for protection by specific troubled sectors. So although a strategy is eschewed, there is an extensive web of ad hoc government policies that promote and control industry. The myriad efforts of state and local governments to promote their own firms or attract plants are not seen as an industrial policy. In a sense then, America has a multitude of industry policies that compete with each other while denying there is any policy at all. But if industry policy is understood as a conscious federal strategy linked to tactics at the macro policy, regulatory policy, and sectoral level, then indeed there is no policy.

This "policy of no policy" rests on a set of structural features that constrain a government's executive discretion and autonomy and limit the instruments of intervention available. First, and critically, the apparatus of government divides powers and makes the system responsive to particular interest group demands. At the Federal level the legislature has a remarkable control of detailed policy, and the weakness of the political parties fragments authority even further. The extensive authority of state and local government in central policy domains further decomposes the government as a unitary actor. The extent of the effective sovereignty of subnational politics is usually difficult for those outside the United States to fully grasp. Second, the decentralized and independent judiciary constrains executive authority, as it was designed to do. In essence, the judiciary is a third party introduced into the dealings between business and the state that cannot be controlled by the executive and may serve as a means for those outside limited alliances of government and business to enter into their dealings. Third, the financial system rooted in equity markets with power diffused into markets deprives the executive of an instrument that is important to state action in France and Japan. American policy sought to fragment markets and limit national banking precisely to avoid a concentration of financial power. The result, of course, is that government is not only disallowed instruments of direct intervention, but also has no financial partners to develop or implement a policy for industry. The American system did, however, work effectively in the period after WWII. As the industrial and financial leader with the most developed economy, the United States did not require structural change to achieve its domestic purposes. The market was producing satisfactory results.

The entrenched patterns of American political economy have come under pressure from foreign competition in the past decade. That pressure was first felt in textiles, then steel, consumer electronics and later automobiles. Now it is felt in advanced technology sectors--from semiconductors and computers through aircraft--as well as in finance, where the once internationally powerful American banks have been displaced as the dominant

global players. The American response has been murky, in part because policy reaction has been to either deny that there is a problem or blame others for our troubles. This is expressed in part by the core policy strategy of the past decade--an aggressive strategy of unthinking deregulation which has provoked extremely expensive problems, particularly in finance. But we return to these issues later.

I.5. Common Problems, Diverse Solutions: The Institutional Structure of The Political Economy

After WWII, then, the advanced industrialized countries found diverse solutions to the common challenge of sustained growth--solutions that addressed the technical tasks at hand while preserving political stability. Those diverse solutions, however, can be usefully grouped into three sets of political economies: state-led, negotiated, and company-led. The distinctions are rooted in the way politics and the market are institutionalized in each country.

The institutional structure of the political economy represents a set of capacities. When those capacities are appropriate to the tasks that must be resolved, growth and political stability unite. Real political difficulty often results when new tasks require new capacities. Consider the case of Britain. The first, and long the dominant, industrial power, it grew to pre-eminence in the 19th century with financial and political institutions suited for company led growth. After WWII however, it could not find a stable model of development. No longer a leader and on the slope of decline, the UK required a new solution -- a new technical approach and a new political bargain. The efforts to create new capacities for either a state strategy of development or a more negotiated approach to growth shattered on institutional limits and the political problem of lifting those limits. Britain which had been governed from the political center after the war found the swirl around this issue radicalizing its political life as the extreme left and right captured control of the labor and conservative party respectively. Indeed, Margaret Thatcher represented a political resolution; her basic strategy being to recreate the conditions of company led growth.

Let us recall the political-economic capacities that concern us: the government's institutional capacity to shape adjustment by setting rules and allocating resources selectively toward purposes it defines; the possibility of negotiations among the major producer groups; and the flexibility of the shopfloor. As previously noted, these capacities rest on: 1) the character of the state; 2) the nature of the financial system; and 3) the arrangements of the labor relations system. Let us, very briefly, consider each in turn.

The Character of the State: Differences in the character of the state -- or, more specifically, the structure of the political executive -- produce differences in the process of adjustment because such arrangements affect a government's

capacity to construct a long term economic strategy and mobilize economic resources to serve it. State-led strategies of adjustment require state structures that permit bureaucrats partial autonomy from parliament and from the interest groups that attempt to influence them. Bureaucrats have both the legal discretion to discriminate between firms when implementing policy and the administrative and financial instruments to exert their will. Negotiated adjustment also demands a state with the capacity to formulate and implement a view of where the industrial economy should go. Without this capacity the state cannot be a negotiator, because it would have no notion of what to negotiate for. In market led growth the state does not need a view or conception of industrial development.

A state structure's capacity for influencing strategic policy can be defined by four characteristics: 1) the method by which it recruits the national civil service; 2) the extent to which its power is centralized; 3) the legal extent of administrative discretion; and 4) its degree of autonomy from the legislature and interest groups. This last element, the degree of executive and bureaucratic autonomy, requires several comments. The place of the legislature and the character of interest groups are essential. The ability of the legislature to control the executive in a detailed way (as is the case in the United States but was not in France or Japan during the high growth years) is certainly one element. But the nature of interest groups is also powerfully important.51 In the pluralist model that prevails in the United States, interest groups can be formed spontaneously, passing demands from the populace up through the legislature. Consequently, intense policy pressures from these groups can constrain the state. At the other extreme, the state forms and authorizes interest groups, or promotes them by rewards or special policy access. This has been the case in France, Japan, and Germany at various points. In this case, the corporatist interest arrangements can serve the purposes of the government. The state executive's autonomy and influence is increased in circumstances where the legislature does not have detailed or effective control over the bureaucracy, and /or when interest groups do not easily or autonomously form. The greater the degree of administrative discretion in making and applying rules, the greater the state's capacity for autonomous action.

The Nature of the Financial System: The state, however, cannot act in the economy without tools to implement its objectives. In some countries, the financial system acts as a hand to implement the will of the state; in others it represents a clear barrier to state intervention. In the postwar years, certainly up through the early 1980s, there were three distinct types of financial systems, each of which had different consequences for the political ties between banks, industry, and finance as well as different implications for the process by which industrial change occurs. The most crucial feature differentiating the three financial systems is how savings are transformed into investment and how those funds are allocated

among competing users.52 A complete picture of the systems would also need to elaborate how investments and loans are monitored and how bankruptcy is managed. The political implications of marketplace arrangements in the financial system is set by three elements; 1) Does one or several financial institutions exert discretionary power over financial flows, that is, influence who uses funds on what terms? 2) Is market power used selectively and intentionally to affect the decisions of firms or the organization of an industry? (The alternative is that any market power is used simply to achieve financial gain rather than to influence industrial behavior.) 3) Can government employ the financial system or institutions as an instrument in its dealings with the industrial with the industrial economy? It can do this either by discriminating between firms or sectors in granting access to funds or by creating financial packages that can be used to bargain with companies.

We consider changes in the financial system later. For now, we note the three types. First there is a capital market based system with resources allocated by prices established in competitive markets in which security issues -- stocks and bonds -- are the predominant source of long term. This model places banks, firms, and governments in distinct spheres from which they venture forth to meet as autonomous bargaining partners. The second model is a credit-based system with critical prices administered by government. Market interrelations are dominated by the government--administered prices, generating inherent disequilibriums in the market, provide the government a menu of discretionary actions it can use for varied purposes. The stock and bond market is not easily accessible to private borrowers, though it is often used by the government as a means of raising money for its projects. This state becomes a linchpin in the system of industrial finance; government is drawn in to bolster the system and to make the administrative choices about allocation. The borderline between public and private blurs, not simply because of political arrangements, but because of the very structure of the financial markets. The third model is also a credit-based system but one in which a limited number of financial institutions dominate the system without themselves being dependent on state assistance. Markets, not administrative actions, determine prices, but the movement of prices in the markets reflects this concentration of financial power. In this model, the state pursues aggregate instead of allocative objectives, and it does so through market operations instead of administrative techniques. As a result, the financial institutions influence the affairs of companies through their lending power and their domination of access to securities markets. Government does not have the apparatus to dictate allocative choices to the financial institutions and consequently has no independent instruments in the financial system with which to influence companies. Banks, however, can serve as policy allies for government, on terms negotiated between the government and finance. To situate these models, the second and third are solutions to late development, whereas the first is tied to

earlier industrial transformation. The market differences themselves become important elements in shaping the responses of each country to its present economic problems.

The Labor Relations System: The institutional arrangement of the labor market, the character of "worker representation and participation" sometimes labeled the labor relations system, is the other feature of the political economy important to our story. The role of labor both at the national political level and at the industrial level is an essential part of industrial restructuring, production reorganization, and technological change. In the past decade, production reorganization and innovation have become viewed as critical elements in national industrial competition. Flexible production that involves flexible work organization seems to turn on labor's integration into managerial decision making, "defined as substantial participation on the part of unions or works councils in discussions with management regarding plans to reorganize work, prior to actual decisions on the shape of new organization and the pace of implementation".53 That can happen, as in Japan, through company controlled unions and a labor movement that is weak in national politics; it can happen, as in Germany, with a strong, independent, cohesive labor movement that has powerful legal rights to participate in management decisions* at the company and plant making while unions negotiate sectoral bargains; it can happen as in Sweden where the powerful national political position is offset by substantial management rights within the company. As Turner argues, "Where unions are integrated into processes of managerial decision making, as in West Germany and Japan, industrial relations practices have been relatively stable in the 1980s."54 Strong effectively centralized labor movements are an essential feature of the negotiated patterns of industrial change, but labor integration into company decision making has apparently become essential in all countries. Price stability was the concern in the earlier period from the mid-1950s through the mid-1970s, and consequently the focus was on the wage and benefits demands. The assumption was essentially that the key issue was keeping wage demands in line with productivity increases, the problem of production organization -- though present -- was of secondary consequence. The crucial question was how each of the several national political economies resolved this problem of setting wages and work conditions. In the 1980s and 1990s, of course, the issues become quite different.

II. Institutions, Governments, and Markets

This essay has contended so far that advanced countries must at once solve the political and technical problems of development, and that they have done so in three distinct ways in the post-war years. The first section argued that the institutional structure -- the foundation of each of these models of national adjustment -- induces patterns of and sets national

boundaries for government policy and corporate strategy. In each country, policy, corporate strategy, and arguably production organization have distinctive features that reflect those structures. The result is that countries and companies tend to do what they are good at. They tend to apply their distinctive capacities to problems, usually without regard to what will work effectively. Crisis occurs when there is a mismatch between task and capacity. These policy and corporate patterns are not immutable, but they are deeply entrenched. The institutions evolve slowly, radically altered only by political conflicts and the settlements that follow.

This section looks more closely at the link between the structure and patterns of policy and corporate strategy. For convenience we focus on policies for industry in France and the policy and corporate strategies that led to the Japanese production revolution. In section III we turn to the mismatches that emerged in the 1980s between the tasks of a new era and the institutional capacities that had been built to respond to the problems of an earlier epoch.

II.1. Patterns of Policy in France

French political-economic institutions produced constant responses to a diverse set of industrial problems in the period from the end of WWII until the mid-1980s. A core strategy was implemented in four waves after WWII: initial reconstruction, modernization in the late fifties and sixties; management of outside structural adjustments in the seventies; and the effort to reinforce the structure of state intervention and influence after the Socialist victory in 1981. By that time, the governing socialists, led by President François Mitterand, had discovered the limits of a purely national development approach in Europe and therefore adopted a strategy of economic liberalization, producing a new political settlement and a reform of the institutional structure.55 This in itself was an odd and unexpected outcome of years of a socialist communist alliance, but that is a separate story.

The core French strategy for industry has been evident. The French executive has the capacity to formulate and pursue an interventionist strategy: the executive has considerable autonomy from selective legislative interference; the administrative system is centralized with considerable discretion in its implementation of the law; and the financial system is under the influence of the state. Viewed from the vantage of a senior political executive, the French system could be understood as a series of circles of power and influence emanating out from a core defined by the prestigious tresor in the Ministry of Finance. The second circle would include the parapublic banking institutions, and the third, the commercial financial institutions. Since market relations among these groups were defined by the credit-based system of administered prices, each circle contained a series of instruments of intervention and influence in industry. The limits on that influence were defined by 1) the political buffers of trade associations, which acted as

insulation from state authority; and 2) the industrial structure, which consisted of non-competitive, tradition-bound small firms that had been historically protected from foreign threats while competition was organized at home. Consequently, the state preferred large projects with goals that could be centrally defined and large institutions with which it could deal directly.

The French solution worked when the tasks at hand required the mobilization of resources, when it was possible to define a limited number of technological results, and when the competitive market could be suppressed, controlled, or oriented by the state. Success is evidenced by Ariane, Airbus, the TGV, and the Minitel system. The French strategies in competitive industries therefore concentrated on the means to control market signals and the creation of large domestic players to act in oligopolistic markets. But when France could neither dominate nor negotiate the markets, it simply suppressed market signals and insulated its firms, hindering their adjustment. To limit dislocation, the government encouraged growth by merger rather than by victory of the stronger, often leading to awkwardly structured and clumsy giants. Not surprisingly, the strategy didn't work when a company had to rapidly adapt its products and processes to changing international market conditions. As a result, the French position in consumer electronics and now high-volume digital electronics has been weak; its position in electronic components untenable. Overall, French trade reflects this pattern: it is strong in capital goods sectors and armaments, where government support is effective in developing products and selling goods; but consumer durable sectors are weak, since there these strategies are often harmful.

The pattern of French policy is evolving in the 1980's. Each of the elements of concern, noted at the end of section I, are changing: the character of the state is transforming in light of EEC integration; financial markets are liberalized and are evolving as France becomes more wealthy; the labor relations system has been altered by a decade of expanded socialist power and the decline of the Communist party. Perhaps a new pattern will only become clear when the institutional structure of the New Europe is settled.

II.2. Policy and Corporate Innovation: Production Revolution in Japan

The institutional structure of an economy shapes not only policy but corporate strategy and, as a result, even production organization. Japanese interventionism produced a distinct pattern of policy and market response. The government acted, as we suggested, as a gatekeeper to develop the technology in an insulated market under Japanese control. Japanese policy produced intense internal competition, but the competition it created was managed and controlled. In this system of intense but managed competition, pursuit of market share was the best way to pursue profits.56 This had two important consequences: production innovation in the firm combined with a search for technology around the world, and waves of excess capacity

translated into dumping abroad.

Let us examine this more carefully. The logic rests on three aspects of the Japanese political economy. First, the Japanese market was relatively closed to the implantation of foreign firms. Consequently, competition was restricted to Japanese firms. Second, there was a rapidly expanding domestic demand. Financial resources channeled to expanding sectors by government policy permitted firms to satisfy demand by building production capacity. Third, foreign technology was easily and readily borrowed. Under these conditions, market logic encouraged Japanese firms to aggressively pursue market share as a means of maximizing profits -- goals traditionally assumed to be contradictory. Formally, firms faced long-term declining cost curves. They could jump quickly from one product/process generation to the next by borrowing technology abroad during the catch-up years of an expanding domestic market. That meant that as firms increased volumes -- ideally capturing more market share in the expanding market -- costs would fall, allowing prices to drop to increase sales, thus starting the cycle over. A firm borrowing product or process technology abroad could drive down its costs by steadily expanding production, and also capture both scale and learning economies by building pricing and building capacity in anticipation of demand. Borrowing again, it could start the process over. Faced with long term declining cost curves, firms developed the ability to move new technology to market quickly, price and build capacity in anticipation of market, and implement rapidly what they learned as production expanded. These became basic characteristics of Japanese companies.

As all firms sought to maximize market share by heavy capacity investment, excess capacity and excessive competition resulted. This, in turn, led to efforts to regulate competition that included creating cartels or production controls negotiated among firms. Equally important, constant efforts to import and develop foreign technologies created a basis for a government organized technology consortia which likewise structured and bounded competition. None of these arrangements are stable, however, because, as Yammamura notes, the imperatives of pushing down the cost curve further and faster will induce firms to break industry agreements or seek special advantage in consortia. Nonetheless, these arrangements have often served to bound or regulate the consequences of excess capacity.

The interplay of public policy and corporate strategy also affected trade and trade politics. Very simply, the pursuit of market share spilled over into international markets, as Yammamura and others have argued.57 Companies in Japan competed for market share, which required them to build production capacity in anticipation of demand. Excess capacity was almost inevitably the result. (This excess capacity would necessarily be even greater with any market downturn.) What would happen to that excess capacity? It would be sold abroad. Since much of the production capacity was then a fixed cost, the temptation was to sell at marginal production cost in foreign markets. As long

as the domestic market was insulated and foreign markets open for sale of excess capacity, Japanese firms had a constant incentive to build in anticipation of demand and offload the consequences of over-ambitious judgments onto foreign markets. In fact, when the domestic market became saturated, a group of firms would begin to export at the same time. The result, in the phrase translated from the Japanese debate, was a "downpouring of exports". The sudden flood of exports into the major export market -- the United States -- caused intense political conflict with America in a series of sectors beginning with textiles and continuing through sectors such as televisions, automobiles, and, later, semiconductors.58

Market share competition pushed then in two directions. First, the effort by all firms to capture market share by building capacity in anticipation of demand inevitably resulted in bouts of excess capacity in the domestic market. That in turn encouraged firms, Yammamura and others argue, to sell abroad at marginal costs. The periodic battles over Japanese dumping are thus a function of the domestic pattern of competition in which market share is key.

With large protected domestic markets and access to borrowed technology, Japanese firms were then encouraged to grow rapidly, to pursue market share, and to exploit increasing returns. The corporate practices fashioned in the era of rapid growth significantly affected the tactics of production organization in the factory. The key to organization became flexibility. Those Japanese firms that could organize themselves flexibly to capture the gains of introducing successive waves of borrowed technology had an advantage domestically. Competition among Japanese firms turned, in no small part, on manufacturing innovation and the introduction of new product. Consequently, firms were organized to sustain constant evolution in their production processes to improve productivity and sustain the flow of product. In fact, the particular strategies for production that emerged in Japan created distinct and enduring advantages in global markets.

II.3. Summary

This section suggests that while the growth puzzle can be resolved in a variety of different ways, the particular political and institutional solutions set down enduring patterns of policy and create a market logic that induces patterns of corporate strategy. Those patterns and strategies represent capacities for addressing categories of tasks. While here we have looked at industrial intervention policies for two countries with state-led growth, the same arguments about the particular influence of institutional arrangements can be made by looking at macro-economic stabilization policies in social democratic political economies. These capacities are not immutable, but evolve slowly as institutions are restructured and as markets are recast. Developments occur with incremental reforms to institutions and market rules as well as with the more basic restructuring that results from the settlement of deeper political fights.

The obvious question, then, is what happens when there is a

mismatch between structural capacities and the tasks at hand? If the tasks are not important, then the policy failures will be inconvenient, inefficient, and expensive, but not central to the fate of the economic growth or political stability. If, on the other hand, the new tasks are essential, affecting the capacity of the economy to adjust and compete, or the ability of politics to allocate the costs and gains of change, then the disjuncture may prove critical. The next section of the essay considers what happened to the models of adjustment built in the advanced countries after WWII when the tasks they confronted shifted dramatically.

III. Adapting to the Permacrisis

For two decades after World War II the advanced countries found solutions that supported enduring growth with political stability . Some were more successful than others. There were real battles and losers, let there be no mistake. That era ended sometime around 1970. Beginning perhaps with the French upheaval in 1968 and the Italian hot summer in 1969, but certainly by the oil crisis of the early 1970s, the old bargains began to unravel. The national postwar settlements and institutional structures were suddenly found wanting or inappropriate: the economic problems the advanced countries faced had changed. In search of new economic solutions and in response to changing domestic politics, the national systems began to transform. To capture the essence of the changing strategies of development we proceed in two steps. First, we characterize some of the problems and pressures that have affected all the advanced countries. Second, we consider specific responses of the United States, Japan, and Europe. Note that suddenly we must consider Europe rather than the singular responses of France, Germany, and Sweden. That in itself is a dramatic shift. But most of all we will find that clear, stable solutions -- new definable models of adjustment -- have not yet emerged.

III.1. The Permacrisis of the Advanced Countries[59]

Beginning in the early 1970s, a seemingly independent series of problems, crises, and disasters plagued the advanced countries, forcing them to alter the way they did business. The basic tasks of development and industrial adjustment were changing, and the adaptation was difficult. Highlighted here are several of these developments.

We start with the oil crisis of the early seventies, since a number of processes were either first evident or amplified then. Politically, stagflation in the seventies exploded the distributional settlements made in the preceding decades. The oil price increase of the early seventies is itself best characterized as a tax by oil producers on the oil consuming countries.[60] The question, of course, was who would pay the tax. Each social group's effort to avoid the tax -- and force another group to pay it -- generated inflationary pressures. Each country's political capacity to impose a distributional solution

produced the basis for a return to macro-economic stability.61

Stagflation and the distributional fights that followed the oil shock were common to all the advanced countries. However, the politics in each were defined by pre-existing political arrangements and divisions. In a country like Britain, which had once been among the richest countries and was rapidly losing its position, inflation and rising taxes provoked radical labor responses as real take-home incomes stopped growing.62 It became clear that those most organized would become the relative winners; consequently, Britain's white collar middle-class workers began to unionize.63 Strike waves suddenly swept not only industry but public services. Both conservative and labor governments would fall in the face of these conflicts until Margaret Thatcher finally imposed radical solutions that weakened the position of labor. For France and Japan, where the conservatives had managed industrial development, there was a common problem. In each case the conservatives' electoral support derived primarily from traditional sectors of peasants and small business. It was precisely these traditional groups who were displaced and whose worlds were transformed by industrial development. This political balancing act -- the need to create political support in a newly industrial society -- was made more difficult by the economic downturn in the seventies that imposed additional stress on all. The Japanese LDP was able to manage this, but the French conservatives were not. In Germany, Sweden, and Austria, where a negotiated process of adjustment prevailed, the challenge of the seventies was to maintain the bargaining processes while new macro-economic solutions were sought.

At first glance, the inflation and slowed growth of the early seventies formulated a new task; that is, re-establishing macro-economic stability by sticking to a more disciplined economic strategy.64 Or, by extension, it was a matter of re-establishing, or modifying, the political bargains on which macro-economic policy rested. But there was more--the macro-economic crisis that began the seventies had by the end of the decade become a matter of structural adjustment. Sustained growth increasingly required a fluid movement of resources from one sector to another. Then global competition amplified this pressure for structural adjustment. Those nations that could not make structural adjustments would be less competitive and face more difficult economic futures. Success in export markets, or lack of it, became for all countries important to maintaining employment and restraining inflation. Again, at the beginning of the sixties and the beginning of the seventies it appeared that national winners, the more successful economies, would be those countries that controlled wages and prices without disruptive political combat. Negotiated corporatism was in vogue in political debate. By the end of the decade the key to success was competitiveness and adjustment.

The first part of the adjustment problem was tied to the oil crisis. The advanced countries had to focus on re-orienting production both to sustain output in the face of the downturn and

to export to pay the new oil bill. The painful oil readjustment was really only a one-time re-orientation. But then new dynamics of international trade and competition, more permanent and structural in nature, were also revealed. It soon became clear that crucial assumptions about trade among the advanced countries were incorrect, and that a substantial reassessment was needed to understand the new, emerging patterns. In the 1960's and 1970's it was hoped that an expansion of intra-industry trade would permit countries to become interdependent and grow rich together. Everyone could have a car industry; Germans would buy Renaults and Americans would buy Volkswagons. Intra-industry trade was a congenial game that all could win. It would replace the earlier, nastier game of inter-industry trade in which the British, for example, would specialize in textiles and industrialize, while the Portuguese would specialize in port and remain poor. Intra-industry trade promised to expand trade since technology was widely available and production costs would converge. Production costs among the advanced countries, it was believed at the time, would steadily converge as factor costs of labor and finance converged. Trade between nations would then be based on differences in national taste as producers specialized in particular niches. Fundamental structural adjustment -- closing an auto industry or shipbuilding industry -- would not be necessary. Trade would then be, if not frictionless, at least not politically disruptive. All the countries would grow together, and consequently the goals and interests of all the advanced countries could be accommodated if each bore the temporary pains of industrial adjustment. The original conceptions of interdependence, we should note, rested on these ideas, but these notions were, if not wrong, quite limited.65

Production costs did diverge for two reasons. First, labor costs diverged. As we all know, standard production technologies spread to a group of countries, of which Korea is one, that became known as the Newly Industrializing Countries (NICs). These countries could initially enter a range of industries--from textiles through steel--on the basis of lower wages and lower production costs. Producers could then often combine their low-cost labor with subsidized finance and often protection. The advanced countries limited access to their markets, often using restrictions such as Voluntary Restraint Agreements (VRAs) that encouraged new products in new locations and prodded existing producers to move to higher value-added market segments. NIC producers eventually moved to an ever wider range of products and to industries that included automobiles, automotive parts, and electronics. Firms in the advanced countries were constantly pressured to move into more defensible high-value niches by a range of means that included differentiating product, speeding product entry, and raising quality. And of course their competitors followed. Second, innovation in production process allowed some advanced countries' producers to gain an enduring advantage over competition.

So production costs did not converge; and technological advantage on which product and production "rents" were built

could be created by government policy and corporate strategy. Instead of Japanese consumers buying Fords and Renaults, Japanese producers simply displaced production in America and then in Europe. The results were significant. First, the countries that most successfully adjusted and innovated became the most able to sustain growth over the next years. Those countries that did not adjust well found their positions more troubled. A second and related result was that this domestic adjustment often expressed itself in a very strong export position.66 In fact, a production revolution had begun that would soon affect the development and position of all the advanced countries.

By the mid 1980s it was clear that a profound revolution in the organization of production was underway. That revolution expressed itself in a series of operational code words such as flexibility and just-in-time production and metaphysical historical code words such as post-fordism, An evolution in production control clearly intersected the need to create new, more defensible high-value niches in world markets. Substantively new ways of approaching production that at once lowered cost, raised quality, and speeded up product introduction emerged. These innovations came both from Japan and Europe, Japan introducing forms of volume flexible production, and Europe introducing forms of flexible specialization in regional communities. While both forms represented new and important innovations, Japanese models proved the most powerful for international trade as a whole. Industrial adjustment and trade success, then, suddenly required recognizing, understanding, and implementing new forms of production. That required, as it turned out, a broad range of specific innovations from accounting changes to labor relations. In passing we must note, first, that these innovations were mostly generated in Europe and Japan, and second, that the United States was slow in adjusting and adapting to these developments.67 The results are evident in global trade patterns.68 Importantly, these innovations seem most effectively introduced where labor is integrated into decision making, at least at the plant level, and where job tasks are broadly defined, which requires forms of labor management reconciliation--again, at least at the plant level.

In the 1970's, also, it seemed that the world economy was going global, a conclusion that remains premature. But the economies, and their policy making processes, did become more interconnected. For example, the oil crisis accelerated, if it did not actually cause, the development of global wholesale financial markets as the banks of the industrialized countries recycled the oil tax (that is, the deposited funds of the OPEC countries).69 Many analysts now hold that globalization, or at least the globalization of wholesale markets, then drove domestic financial liberalization -- that is, the deregulation of the domestic financial markets.70 It was argued that price competition in international wholesale financial markets created disequilibria in domestic national financial markets compelling national deregulation to create greater freedom of price movement. An alternate view contends that the national processes

of deregulation demonstrated a very different logic, rooted in each case in national politics, but justified by the economic ideology of deregulation pouring out of the United States.71 In this view, markets were not deregulated, but reregulated; the purpose of the regulator was often not to accommodate international financial markets, but to influence the national place within those international markets. The outcome of the individual national deregulations and reregulations was an adaptation of national financial systems.

Even in Europe, where in principle a single financial market is being created, national retail financial channels remain firmly in place. Consider France. Following the decision in 1983 not to withdraw from the European Monetary System, the French Socialist government took on a liberal market orientation. In the name of eliminating privilege (but practically to reduce the expensive state subsidies by removing the costly and contradictory layers of financial incentives) the French Minister of Finance radically re-oriented and indeed liberalized its financial system. Or consider Japan, whose national system remains firmly in place. At its core, Japanese firms' high profits reduced their dependence on bank finance, deconstructing the development-based financial system. Rising government debt affected the terms on which banks and the Ministry of Finance dealt with each other.72 Foreign pressures to open Japanese financial markets meant altering the terms of regulation. Some new form of regulatory structure, quite apart from any global financial pressure, was needed. The eventual resolution created the basis for a capital investment boom in the mid 1980s as well as an investment free-for-all. Finally, consider the United States, where an unconsidered belief in markets created the intellectual basis for a policy strategy of deregulation. Deregulation would itself increase financial market efficiency, the story went, though as it turned out -- financial theory aside -- deregulation did not increase the effectiveness of finance at supporting the real economy. As much as market pressures ideology and political purposes changed national financial structure, readjusting markets to fit government notions of crucial problems and central interests. In sum, converging global wholesale financial markets and securitization of the process of transforming savings into investments have altered the national financial markets, but national markets remain, and national institutions and regulatory systems continue to be crucial to financial intermediation. Interconnected international financial markets were not a first step in economic globalization that would force national economies to converge creating a more homogeneous, not simply interdependent, world. That convergence has not happened, but the broader debate surrounding liberalization and deregulation has been important.

Deregulation emerged as one political strategy for dealing with the problems of stagnant growth. But deregulation is a catchall phrase that expresses not only diverse national policies for varied sectors but also two quite different intents. Viewed one way, deregulation can mean the withdrawal of government

intervention and regulation from market processes, leaving pure market processes to determine outcomes. Those outcomes, being market outcomes, are then assumed to be the best possible results. In reality, though, market rules are never eliminated, and market outcomes always reflect politically constructed institutional and regulatory arrangements. Viewed a second way, however, rules can be changed to produce specific outcomes, a process that should really be labeled reregulation, not deregulation. When those objectives are the intentional development of industry or the creation of an infra-structure that will support a more competitive industry, then we should refer to it as developmental reregulation.73 Thus in Japan the process of administrative reform in telecommunications is one of developmental reregulation to establish the infrastructure for the economy and help position firms in global competition.74 In the United States, by contrast, a simplistic conception of deregulation has prevailed. The deregulation of American telecommunications is largely the application of anti-trust laws intended to insure a more competitive market place. Unfortunately, the results are: an unthinking opening of the domestic market without negotiated reciprocity; an enormous experimentation with new telecommunication services; the risk that the most advanced new services will not be widely available; and the danger of an incoherent telecommunications infra-structure.

III.2. Regions and Nations in a Global Economy

National politics and national regulatory policies remain important even in a supposedly global and interdependent economy. A more global international economy is certainly visible in trade, direct investment, and finance. Yet the responses to the new competition are generated within particular places, not by world corporations that stand outside a home base, and the foundation of economies remain national, or at least regional. Multinational corporations and global financial institutions do not sweep away the national foundations of trade, finance, and technology. Perhaps someday that will happen, but not yet.75 To continue our discussion of the politics of advanced country economic adjustment, we must sketch the regional economic context.

The increasingly regional character of the global economy is now evident. It has emerged over the last two decades. We know that there are three increasingly co-equal and distinct, though interconnected, regional economies. The United States/Canada and Western Europe each represents about 25% of the global GDP. In 1987 Japan plus the four Asia tigers represented 15.8% and were growing more rapidly than the others. Each of those regions trades predominantly and increasingly with itself. Numbers suggesting a general growth of international trade now disguise the even more rapid growth of intra-regional trade. Europe has been coalescing as a trade and political region over the past three decades, a process that has accelerated in recent years. Japan has increasingly become the center of an Asian region

constructed around Japanese trade and financial flows.

We must focus on the critical problems that this regionalization poses for the dominant countries in each area. Consider the Japan centered and increasingly yen-based Asian trade and investment region. Borrus and Zysman have argued that: "By almost any measure Japan rather than the United States is now the dominant player...The regional production network appears to be very hierarchically structured and dominated by Japan. Japanese technology lies at the heart of an increasingly complementary relationship between Japan and its major Asian trading partners."76 In 1987 MITI noted the "growing tendency for Japanese industry, especially the electrical machinery industry, to view the Pacific region as a single market from which to pursue a global corporate strategy."77 The crucial question here is whether the region will remain a staging ground for Japanese global corporate strategy or whether the other Asian countries can establish an independent position. Much will turn on Japanese trade and investment policies.

The European story must be understood in relation to the competitive advance of Japan and the difficulties of the United States.78 The European community was created after WWII when Europe found itself no longer at the center of the international system but rather a frontier and cushion between two new superpowers. There were two objectives of the original bargain in the 1950s: to contain Germany by binding it to the rest of Europe and to restart European growth.79 In the 1980s, the real shift in the distribution of economic power was one of the sparks to re-ignite the European integration process. Plainly put, relative American decline and Japanese ascent forced European elites to rethink their roles and interests in the world economy. "The United States was no longer the unique source of forefront technologies; in crucial electronics sectors, for example, Japanese firms lead the world. Moreover, Japanese innovations in organizing production and in manufacturing technologies mean that the United States is no longer the automatically most attractive model of industrial development. In monetary affairs, some Europeans argue that Frankfurt and Tokyo -- not Washington -- are now in control. In short shifts in relative technological industrial and economic capabilities are forcing the European to rethink...[their goals and the means of achieving them]"80 In light of the weakening of the socialist/communist left, European elites searching for a new growth formula turned to market oriented strategies. The details of the process leading to Europe 1992 are not important here. It is crucial only to understand what kind of issues will shape the options for the dominant European economies.

The third region is North America. Organized around the United States, the North American free trade region seems to be emerging from two quite different deals. The American-Canadian agreement brings together two complementary advanced countries which already have extensive ties. While the American economy and population are each roughly ten times the size Canada's, the institutional and economic matches are such that arrangements

seem fairly straightforward. However, the second bargain, that with Mexico, raises a number of issues. After stymied growth in a debt trap created in the 1970s, Mexico is attempting a dramatic change in economic direction, shifting from an aggressive, state-sponsored import-substitution strategy to one focused on adaptation to global markets and a search for competitive advantage. This bargain proposes two advantages for the United States. First, Mexican migration to the United States, which creates serious social problems and direct budgetary costs, would potentially slow. Sustained growth in Mexico and an increase in Mexican incomes would relieve the migration into the United States.81 Second, there are direct economic advantages. Some suggest that since the Mexican economy is only 5% the size of the United States' economy (its population is about one-third) that it will have only limited consequences in any case. The Mexican-American bargain hinges on the expansion of the Mexican economy which should, in principal, lead Mexico to import capital goods while exporting labor-intensive products. Integrating Mexico into a North American region should provide North American firms a more differentiated production network so that they can source more labor-intensive components within North America rather than Asia, thus creating their own regional base for global competition. But will things work out this way? Not necessarily. American capital goods have lost competitive position in global markets, and Mexico may subsequently purchase equipment from Europe and Japan while continuing to export standard industrial products to United States. Labor displaced from labor-intensive sectors in the United States will not smoothly move to sectors requiring capital and education. In fact, recent studies suggest that because of the lack of skilled workers American firms have deskilled production--perhaps introducing a slide of declining wages and slowing productivity. The crucial question, then, is whether the United States will adjust upwards toward a higher-skilled high technology economy--or slip, at least relatively, in international competition.

In each region, but most centrally in both Asia and North America, the regional "architecture of supply"--the structure of markets through which components, materials, and equipment technologies reach producers--is a central issue.82 There are two questions: first, how does the structure of the supply base influence the competitive position of each region; second, what is the degree of autonomy (or, conversely, the extent of interdependence) of the three regional networks, and as part of that what economic/industrial influence (or dependence) exists?

For Korea, the implication of a regionalization makes its technology and market position in relation to Japan all the more critical. Will Japan, in effect, regulate Korean development by its allocation of markets and technology? Or can Korea develop an autonomous strategy?

III.3. Continuity and Change: The Response of the Advanced Countries

As advanced countries have responded a series of crises and

emerging economic regionalism, their individual domestic political economies have evolved. Here we try and assess the character and direction of each.

The American Strategy of Unregulated Markets: The Reagan revolution was at its core a response to the era of stagflation. As an aggressive recommitment to a company-led strategy it reasserted the image of untrammeled market competition.. The movie image of the American 19th century settlement is of the lone pioneer, Daniel Boone, moving west, the single gunfighter standing off the badguys at the OK corral. The reality of the 19th century was the cooperation of wagon trains, the support of the government in agricultural and transportation development. There was a conscious development strategy of state support for settlement and industrial development. The movie image of the American 20th century is perhaps of Horatio Alger or Henry Ford, the single entrepreneur creating a new world. But the reality of the 20th century also included state support for the diffusion of agricultural technology (in the form of the Agricultural Extension Service) as well as the massive government support for the construction of national highway, airtravel, and communications infrastructure. The movie image of the Reagan revolution was the freeing of industry from the heavy hand of regulation and taxation. In practice, the Reagan strategy has shattered the coalition for growth that for years subordinated distributional fights to a joint consensus for consumer-led growth. Whether measured by international competitiveness, domestic debt, international debt, family or manufacturing income growth, or income distribution, the last decade has not been the remarkable success hoped for. The central problems of American industrial adjustment have simply been postponed for a decade.

The Reagan argument presumed that the stagflation had been created by an extension of the state into the market. Substantial intellectual support was mustered for the notion that market processes were slowed, and the gears of the economy clogged, by selfish interest groups using government to capture private benefits.83 Business had been unfairly burdened by unnecessary regulated costs that were disadvantaging them in international competition. In transportation, telecommunications, and finance, many felt that regulatory distortion was depriving the economy of real gains. Markets were conceived as a form of self-regulating natural phenomena that would produce the best of all economic worlds. This conception of the public interest fitted the self-interest of particular business groups so a strategy of deregulation was adopted across a whole range of sectors. Rather than rethinking the purposes of regulations and creating a regulatory regime that would use competition as an instrument, deregulation expressed ideological zeal. The results have been, at best, mixed. Consider the case of telecommunications. Firms have become competition-driven, aggressively experimenting with new technologies and business strategies based on their development. The competition is not simply in long distance voice and data networks or in equipment

but also in local loops. Cable television companies will, if allowed by regulators, attempt to become alternate local phone companies. But the risk for the US is substantial. Chaotic fragmentation of networks may keep the nation from capturing the full possibilities of 21st century telecommunications technology despite the headstart provided by the initial deregulation. Consider the case of finance. Deregulation has initially produced disaster--whatever the final balance sheet. By any measure the several hundred billion dollar direct cost of the collapse of the American savings and loan system will have to be set against any gains of efficiency. Deregulation, as demonstrated by both of these cases--telecommunications and finance--did not increase gains, or increased gains at the expense of structural health. While these sectors found new competition, the lack of direction--the lack of cohesive, long-range strategy--produced outcomes arguably worse than those of the preceding regulatory era.

The second measure taken to spark an economic resurgence through private sector initiative was to reduce government expenditures and cut taxes so as to release investment. In principle, this would reduce the government deficit and raise private savings and investment. The tax cut was seen to be self-financing. Its proponents argued that the loss of revenue from tax cuts would be made up in part by expenditure cuts. More importantly, tax revenues would grow again with the economy and make up the losses. The reality, however, was a spectacular domestic deficit. The deficit then became a constant pressure to restrain domestic social spending. It also induced an influx of foreign capital to finance the deficit, which drove up the dollar's value, amplified the trade deficit, and weakened American firms. In the short run the strategy financed a boom based on a government deficit, a new financing twist on a classic Keynsian strategy. Instead of an investment boom based on increased domestic savings, the US was left with a consumption boom based on increased national deficits. In the longer run the average growth over the last decade has not been higher than that of the decade before.

The United States is now in a critical political trap that makes it difficult to solve its policy problems. The country faces dramatic domestic/internal adjustments to new competition. This challenge will undoubtedly require investment in several areas: skills and health of the workforce; new products and production techniques; and infrastructures for the next century such as telecommunications. Yet there is no longer a political coalition for public, or private, investment. The tax cuts which financed a sustained expansion in the 1980s helped solidify a presidential electoral coalition that also elected Bush. Tax increases to support public investment would be difficult, moreover, because real incomes in the United States have declined; family incomes rose for a time as women entered the work force, have now again flattened out. The slowed relative growth of the United States then becomes a barrier to the investments needed to rebuild the basis of continued development.

The enormous deficit means that further unfunded expenditures cannot pay for the public investments. Only a new political coalition, organized within either the Republican or Democratic parties, can break the lock on America's trap. In sum, the United States responded to the 1970s by seeking to perfect an idealized image of company-led growth.

The Response in Japan: The crucial question about Japan is whether the core of the Japanese developmental system of state-led growth is still in place, and whether, if in place, its use to create position and advantage for Japan disadvantages its trade partners. Has the old mold been broken or has adaptation simply updated the original strategy? The power of the Japanese economy created in the decades of fast growth (and the continuing level of investment at home and abroad that is entrenching advantage created in a diverse set of sectors) makes the domestic political choices of global interest. The concern outside Japan is that the basic developmental policy objectives remain, but that the instruments have become more subtle. The tasks of development may have changed, the argument goes, but the central purposes of the state and the society may not have.

Certainly there have been important changes. The balance of relations among government, industry, and finance in Japan has clearly shifted from the mid-seventies. The growing competitive strength and profitability of the firms unquestionably gives them a new independence from both banks and government. Governments always have the most influence when firms are weak and need support; conversely, profitable firms that are competitive in global markets have the greatest independence from state influence. In the 30 years following WWII, Japanese firms were --loosely speaking -- short of capital and technology followers, often depending on government and trading companies for a knowledge of foreign markets. Now these firms are among the strongest in the world, technology leaders in many fields, and marketing innovators in many countries. There are fewer things that government can give or deny them. Yet government mechanisms for regulating competition, such as recession cartels in declining sectors, are still in place. In advanced sectors, the government tools of promotion remains pervasive and crucial to global market outcomes.

The politics of industrial policy have also changed, but a loosening of the developmental system does not mean government withdrawal from policies aimed at creating the market outcomes it prefers. Reform does not mean that the developmental system has simply been dismantled and that the government has simply assumed the role of umpire. It can simply re-orient policy objectives and re-calibrate policy instruments. Consider the reregulation and sometimes privatization (what the Japanese call "Administrative Reform") of a range of services including railroads, telecommunications, and finance.84 The railroads were privatized in part to shift labor conflict from the public to private sector. The telecommunications was reregulated and NTT privatized--the reregulation serving a complex set of agendas and

reconciling a set of competing political purposes.85 The list of winners in the reform is long. The process led by NTT to establish an integrated broad-band telecommunications network as the infrastructure for twenty first century growth was launched. A number of industrial groups will gain a share of the network markets as competitors, albeit controlled competitors. Privatizing NTT removes telecommunications issues from government control, relieving direct trade and political pressures. On balance, promotional objectives in telocommunications are not eliminated, but the winners in industry and government are reshuffled. Similarly, the financial system was reregulated, not deregulated to approximate a liberal order. It was restructured to manage finance in the 1990s better. Part of those adjustments were successful. In the past five years, for example, Japan has invested 2.3 trillion in capital equipment for a new industrial era, adding to its industrial muscle. Moreover, Japan has not only reinvested its trade surplus abroad but also reorganized domestic market and production position. It takes a special and focused analysis of Japanese finance to decipher the story, but several elements stand out amidst the positioning for political and market advantage. Whether by calculated intent or accident, land has dominated the story. The financial foundations of Japanese banks were reinforced to meet BIS standards. and the mechanism of doing so was revaluation of land. The land boom in turn permitted Japanese firms to raise borrowing. Increasing land prices then fueled a stockmarket boom, which raised values all around again. Recognized industrial players were insulated from speculation by their brokers. As the game springs apart in the fall of 1991, there are very few casualties and no real regulatory restructuring. On balance though, financial reregulation looks very much like an effort to structure the financial system to carry the Japanese economy, under the continuing tutelage of the Ministry of Finance, into the 21st century. Even severe political and market abuses have not weakened the Ministry of Finance's control or created a truly liberal system.

At the core of the Japanese developmental system were the twin tools of promotion and an insulation. Mechanisms for promotion, formed in government-industry compacts, have not been abandoned, though their importance is diminished in many industries. Nor has the market been truly opened. Certainly the insulation has loosened and formal tariff walls are very low. Although manufactured imports have risen in recent years, the absolute levels of imports remain very low. In sectors where Japan has created defensible advantage in world markets (in other words, where entry for foreign firms is now most difficult), the Japanese markets are the least restricted. However, in sectors where Japan has lost advantage or sectors, markets are much less open. Recession cartels and other restrictions limit sectors losing position; certainly in all countries, sectors in trouble receive protection from imports. However, where Japanese firms are seeking advantage the mechanisms of outright restriction -- non-tariff barriers -- remain substantial.86 The character of

business arrangements replacing outright government restriction is suggested by the corporate cross-holdings that emerged in the 1970s prior to market liberalization. Those cross-holdings protect firms against outside takeovers. Moreover, the list of firms compensated for market losses by investment banks in 1991 includes no foreign firms, suggesting both the continued, closely held character of Japanese business and the apparent exclusion of foreign firms from its critical inner circles.

On balance the argument that the government still actively seeks to assist firms to create enduring competitive advantage in global markets and that domestic markets are still reserved for Japanese firms is supported by substantial evidence. Many of the elements of a state-led system of industrial development are still in place, even though the precise mix of policy and corporate strategy has changed.

Recasting the European Bargain: Europe is in flux; policy processes are being profoundly altered. The European bargain has been recast by national governments seeking to adapt to the problems of a changed global economy and a suddenly altered security situation. Europe 1992 must be understood as an effort by European governments and business elites to: 1) meet the permacrisis of slowed growth and higher levels of unemployment; 2) respond to the changing American and Japanese capabilities; 3) promote their collective position in the international order.
The political economies of the European countries must now be understood as part of an increasingly important European structure. The national arrangements continue, and continue to matter, but they are being altered by the expanding reach of Europe. Before even thinking about the national cases, we must consider how the political-economic game has changed in Europe. There will be a European Monetary Union, but the form and governance will be settled over the next years. There will be some version of a European Political Union, but whether Europe will begin to act as a single protagonist in foreign and security policy will not be decided at the summit in December 1991, but by the crisis that are collectively addressed -- or not -- in the next decade. But it is not simply that the big questions are unsettled; rather, the dynamics of European and national politics are being reset.

European choices, both decisions made by the Brussels institutions and those made jointly by the governments outside those institutions, increasingly bind national choices. But the pattern of Brussels influence is varied and uneven. Brussels has more power in competition policy than in trade policy, more in monetary policy than in tax policy.87 Within the category of competition policy, Brussels has more influence over mergers than state aid. In trade policy, European positions are created in negotiation among commission and national governments. The 1979 creation of the EuropeanMonetarySystem of linked national currencies has forced a coordination of national monetary policy (though a single European Central Bank and currency have not yet been adopted). But in tax policy the governments have retained a

strong hold.[88]

At the same time, the logic of national politics in each European country has been increasingly altered in important though diverse ways by the growing influence of Brussels. Policy making in Brussels mixes together elements of inter-governmental bargaining represented institutionally for example by the Council of Ministers and of supra-national governance represented institutionally by the Commission and the Court that are only distantly controlled by Parliament and very distantly connected to any electorate. Who should national constituencies hold responsible? Critically governments can use the ambiguity of responsibility at the European level and the lack of an electoral check to implement policies they favor but cannot implement within the constraints of national politics. A second consequence may be the unwinding of national corporatist bargains. In most European countries there are tight bargains between interest groups and the state, which in many countries involve labor. That is, government certifies particular groups as privileged interlocutors, which is an exchange of special status for influence. These national corporatist arrangements are dissolved, or at least weakened by moving decisions to Brussels. That is, no particular group will retain special status and all will have to compete as lobbyists. The result may be that diverse national interest groups will compete to influence policy in a competitive environment in Brussels rather than manage policy in corporatist bargains in their national capitals. A final example would be the possibility -- not likely but a possibility nonetheless -- that Europe will become a community of sub-national regions as much as of nations.[89]

It is not simply the European evolution which is uncertain. The political development of the several countries is also very ambiguous. Consider Germany. With unification Germany becomes, at first glance, the dominant player in Europe. It has the largest population, the strongest industry, and occupies a historically pivotal geography between Western and Central Europe. But the first glance assumes a smooth transition of the Eastern Germany into the unified state. That, so far, has not happened. Indeed, a separate Eastern identity may endure. The scale of the transformation has generated a budget deficit, trade deficits, stunning unemployment, and new concerns. The political bargain that allowed quick unification involved merging currency and labor rules that suddenly made East Germany an unproductive and high wage region. The costs of construction and reconstruction have been and continue to be astronomical. It remains unclear how rapidly the transformation can be managed and more signs show Germany heading down the worst-case path. That is, East German requirements sap investment and raise interest rates. Higher interest rates drive up the mark which raises export prices for German industry. Industry in the former West Germany, which has withstood similar increases, might not be overly troubled. However, producers in Eastern Germany (where productivity is in any case too low to support viable integration) are being devastated.

A closer look also suggests that the bargains and the bargaining process in German adjustment may be altered. The political basis of German negotiated adjustment has rested on a strong Social Democratic Party capable of governing on its own or in alliance with the centrist Free democrats and a strong labor movement. That balance could be transformed by: 1) an entrenchment of a conservative hegemony based on the unification; 2) a radicalization of Eastern unemployed who have no clear attachment to the major parties; or (though less likely) 3) an extension of union power that channels the discontent. At the time of this writing, speculation on the outcome is rife, but there are no clear lines of development. European competition and financial services rules may loosen the institutional foundation for bargained adjustment in Germany.

Likewise in France, the pillars of the traditional national model (in this case, state-led growth) are, if not eroding, at least taking different form. In fact, the last decade is a confusing saga. The 1970s saw slowed growth and high unemployment, which culminated in Conservative defeat at the hands of the Socialists in 1981. Socialist economic strategy first rested on an expansionary macro-economic policy which would restart growth lowering unemployment and a commitment to nationalization that would hold the coalition with the Communists together while providing instruments for state sponsored efforts to create globally competitive firms. The implementation of the policy of nationalization may have damaged the job possibilities of a certain segment of senior Conservative bureaucrats on leaving office, but it did not harm the middle class stockholders, and rarely changed the core of the management structure. Ironically in many ways the real authority of the state was reduced. The strategy of expanded demand, implemented in a period of global downturn and American recession, had the consequence of sparking a trade deficit and currency crisis which brought about a policy reversal that had the Socialist implementing the conservative policy mix. So by the mid-eighties the Socialists were cooking an odd policy brew of nationalization, demand restraint, and market liberalization. They came to power advocating a nationally based strategy of state led industrial adjustment were leading the call for a European centered policy of market shocks and demand restraint.

It simply is not clear how much of the French post-war etatiste apparatus and strategies will endure. Consider three diverse elements. First, postwar modernization strategies rested on a refinement of the state bureaucracy. It was not simply that its power was extended or its instruments refined. Rather, the state bureaucracy became the institutional bastion of the modernizing coalition through changes in recruitment and training. The fundamental task of supporting the market driven shift of resources from agriculture to industry is completed. In developing an industrial policy the state bureaucrats had considerable administrative discretion in applying law, increased their autonomy from the legislature, and preserved a tradition of status and influence. That discretion is now limited by

Brussels, particularly in the arena of state aid and market access. Increased competition in the domestic market, moreover, limits the utility of state action. Yet the traditional role of the state as promoter and market maker continues in large scale technology projects such as airbus, the highspeed train, minitel, and HDTV. And many of the French government's development strategies are now being implemented through Brussels. Second, the financial system has been reformed, making its prices more a function of market processes and reducing the pervasiveness of the influence of the state in the selective allocation of credit. The emergence of a commercial paper market for example limits the dependence of large firms on the banks. The state's role may be diminished, but it is not eliminated. Yet that state role may be further diminished if the 1992 reforms and the establishment of a European Monetary Union creates even more integrated European financial markets.90

In sum, the European national growth models of the post-war years are all being recreated. For each there is the same, new fact -- Europe. The expansion of policy and policy initiative in Brussels is dramatic and significant. The balance between national capitals and Brussels is yet to be set, and indeed the balance between nation and region may itself be altered. Equally, the economic dislocations of the last years has shaken the national models themselves, which is part of the reason that the governments have supported the relaunching of the European idea. No new model -- either at the national or European level -- is yet in place.

Do the Models still Matter?

Certainly the tasks of sustained growth and development have changed. There are certainly common problems that must be resolved by the advanced countries. Those problems include the reorganization of production that the new industrial revolution demands, the reregulation of service and industrial markets, and the adjustment of domestic macro-economic policy to a more integrated, but regional, world of trade and finance.

The particular countries are now experimenting to create new solutions. New models do not yet exist. But for the moment the original adjustment models still distinguish the national responses because they set the frameworks of national experimentation. The American policy pattern has been reinforced, but arguably without addressing -- and indeed postponing -- needed industrial and economic adjustments. The result may be a period of sharper and more sudden policy shifts based on possibly radical--and not clearly imagined--political bases. Japanese policies have evolved, as Japan has become richer, with the result that the interplay of government and industry has changed. But the developmental objectives remain the same. Europe is watching both the recasting of the bargain among the nations and a reconfiguration of policy processes within the countries. The last decade simply emphasizes the intense difficulty of creating new "models" of political economy, both the difficulty of identifying the problems and creating new

institutions and tools to address them.

IV. Korean Choices: Inventing New Solutions for Growth

Let us return to where we began. What can Korea draw from the experiences of the advanced countries? Since my knowledge of Korean politics and economics is at best superficial, let me base my remarks on the core idea developed in this essay. While there are a several alternative political strategies for growth, a successful solution must: 1) resolve the technical problem of how to move and reorganize productive resources, both within and between sectors; 2) maintain political stability while allocating the costs and gains of development. As the economic tasks evolve and political possibilities are redefined, mismatches between tasks and capabilities emerge. National development strategies must be adapted to refit policy capabilities to economic requirements. But those adaptations are difficult political moments.

Korea would seem, from even my superficial understanding, to face several delicate junctures. Authoritarian development solutions that worked in an era of fast industrial growth may not provide either viable technical economic policies nor effective political strategies today. The political problem would seem evident. Economic development is the transformation of poor rural agricultural societies into richer, urban industrial ones. (Failed development may of course leave a country urban but neither rich nor industrial.) Korea's successful development has already transformed the society by creating urban working and middle classes, transforming, consequently, the political problem.

Political stability almost certainly requires that mechanisms be found to involve and incorporate the emerging middle class and labor communities into politics. The question is on what terms, or rather whose terms, will that incorporation come? State orchestrated development has generally involved conservative leadership structuring the terms in which labor, and often the mass political community in general, participates in politics. In the late 19th century the Prussian leader Bismarck created the first self-conscious welfare system -- shocking his conservative allies -- precisely to tempt the emerging working class to forsake its political ambitions for material advantage. In the mid-twentieth century Japanese leadership managed to orchestrate party politics and labor organization to limit the direct voice of the labor movement in forming governments and making policy. But labor in Japan has gained real influence in wage formation, real participation in work reorganization, and very substantial material gains. There has been real incorporation at the firm level if not at the political level. In France, we have seen by contrast, long standing social rifts, ideological confrontations, and sharp divisions within labor prevented the conservatives from implementing a similar strategy of co-optation and integration of labor into a conservative dominated society. The tense confrontational atmosphere in large-scale industrial complicated

French development and finally contributed to political realignment. Stability and growth in conservative-led development has required real and substantial material gains and even an entrenched place in the processes of wage and work formation. By contrast, the societies with a negotiated style of adjustment -- in this essay Sweden and post-war Germany -- have empowered highly organized labor and business groups. True corporatism involves real political positions for labor. The problem for Korea is not just one of political stability and order. The evolving economic tasks sharpen the political choices. Let us consider three issues.

First, as argued in section III, a profound transformation in industrial production is altering the dynamics of international competition. The code words of the transformation have become flexibility and speed. The new production model allows producers to gain static flexibility (the capacity to produce a range of products from a single process) and dynamic flexibility (the capacity to advance the process and introduce new product more quickly). At the same time, quality, measured in such forms as defects, is raised and costs often reduced. The production transformation at its core is not technological but rather emerges from new understandings of the production problem, new conceptions of how to organize work, and new notions of how to link together steps in the the production process. We are watching, as one IBM engineer remarked, a shift in paradigms about what is to be done and how to do it. Now highly automated versions of flexible volume production are emerging, but the technology serves to amplify the power of the new paradigms. It is the new paradigms, not the technologies that implement them, that are core. Product variety and speed-to-market are capabilities that firms use to carve up standard markets into groups of niche markets. The volume capital-intensive production strategies used to force entry into standard goods markets are becoming obsolete; producers who do not adapt will be perpetually forced into low value-added segments of important sectors.

On the surface, responding to this shift in production paradigms is a technical task, but more fundamentally it is proving to be a social and political matter of the place of labor and small firms in production and politics. This revolution in production demands the effective integration of labor into production. The classic image of a shopsteward's control of recalcitrant workers to extract surplus-value simply evaporates.91 The images that guide us must become ones of labor collaboration, responsability, and, of necessity, trust. Endemic confrontation becomes an impediment to the continous adjustment and adaptation that flexible production requires. Shopfloor peace is necessary but not sufficient; broad job definitions, worker initiatives and toleration for reorganization are needed. Skilled workforces become key to decisions about how to organize production and arrange the process of product development. Labor must be committed to the effective functioning of the production system to maintain and improve rapidly adjusting production processes and implement a constantly shifting product mixes. Effective

links from shopfloor to strategic management are ultimately required. Japanese firms have managed to incorporate labor into production and planning while excluding them from political power or formal corporate position. In Germany, a strong industrial union movement and formal labor rights in corporate governance are complement a strong Social Democratic Party capable of governing. A political settlement must achieve more than simply labor acquiesence and political stability--it must assure the labor foundations for flexible volume production.

Second, networks of small to middle size firms provide an important element of the networks of suppliers that create the basis of production flexibility so essential in global markets. In Germany, Japan, and Italy these small firms were dismissed twenty years ago as anachronisms of an earlier capitalism, anachronisms that survived with subsidy and would eventually vanish.92 Now they are admired as elements of just-in-time supply networks or flexible specialization. These smaller firms adapted to the needs of the new production organization and provided flexibility in the economy as a whole. This adaptation was facilitated by policies and programs as diverse as robot leasing firms, regional banks, and trade associations acting as technology brokers. Will Korea manage to find a policy balance to support large firms that provide muscle in international competition and smaller firms that create crucial flexibility? This of course comes to central policy choices: what will be the political and market role of the large firms and what purposes will financial reregulation pursue?

Third, the global economy has become increasingly regional, and the Asian region has become increasingly centered around Japanese finance and technology. If the three major trade groups begin to cordon themselves off in competition creating some version of a 21st century neo-mercantilism in which the prize is an advantage in development, then Korea's position within Asia and its ties to Europe and Japan may become all the more critical. The problem, simply put, is: how can Korea avoid dependence on the strongest regional power, Japan? This is partly a matter of product development, partly of markets for exports, and partly a matter of technology access and development. One approach might be development alliances for advanced products with Europeans and American firms with individual product arrangements embedded in joint market strategies that permit partners to understand the longer term mutual gain. Korea may represent a volume production platform for European companies having difficulty in the American market. Possibilities for such alliances might exist in sectors such as electronics and cars.

We return at the end to what seems to this observor to be the central issue. The Korean domestic political problem is altered by the social transformations industrialization has brought. Political strategies that permitted the state to influence both the course of economic growth and the distribution of the gains of development must be adapted to accomododate the emerging middle and working classes. The alternative is confrontational

politics that undermine or derail growth. At the same time, economic strategies that emphasized capital-intensive volume production of standard product must be reconsidered. As the 21st century unfolds and high technology products are rapidly introduced to the market by skilled workforces, the integration of labor into corporate operations will prove even more crucial than it has in the past. For once, the political imperative and the economic necessity are the same.

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1. That is, as a government fails to reconcile the claims on its resources, it simply prints more money. See Leon Lindberg, The Politics of Inflation and Economic Stagnation: Theorectical Approaches and International Case Studies, (Washington, D.C.: Brookings Institution, 1985).
2. Reported to me by Fernando Saboya de Castro.
3. Political scientists now debate how to characterize these relationships, using notions such as the strong or weak state, "policy compacts", state led growth, developmental system, and corporatism. However, they rarely try to establish that these institutional relationships, however characterized, shape market behavior. Economists, by contrast generally ignore or caricature the role of institutions and proceed with their analysis either as if institutions did not exist and as if history did not matter or by reducing the role of institutions to an arrangement of transactions and the roots and processes of historical development to the jargon of historisis.
4. See Alexander Gerschonkron, Economic Backwardness in Historical Perspective, (Cambridge: Belknap Press, 1962).
5. Francois Hetman, Les Secrets des Geant Americans, (Paris: Seuil, 1969). See also, Jean Jacques Servan-Schreiber, The American Challenge, (New York: Atheneum, 1988).
6. George Stalk and James Abeglan, Kaisha: The Japanese Corporation, (New York: Basic Books, 1985). Also see, Clyde Prestowitz, Trading Places, (New York: Basic Books, 1988).
7. There is a progression in each national case from the emergence of the industrial economy through a series of major economic and political crisis. The functions and logic of the institutions of a political economy are a product of how they were created and evolved. The institutional structure, the institutions of the market, form the artifacts for an archeology of these economies so that we can understand their dynamics and the shifting matches of tasks and capacities.
8. John Zysman, Government, Markets and Growth, (Ithaca: Cornell University Press, 1983).
9. Seen in this way, variation in the power of social groups accounts for policy and economic outcomes within each national economy or adjustment model, rather than distinguishing between them. Changes in social power within a society will be reflected by changes in the groups that benefit from policy, but those changes do not easily alter the basic political processes associated within industrial change in the advanced countries.
10. See Chalmers Johnson, MITI and the Japanese Miracle, (Stanford: Stanford University Press, 1982) Also see the

sections on Japan, pp. 233-251 in Zysman, op. cit.
11. See Johnson, Tyson, Zysman, Politics and Productivity, (New York: Ballinger Publishing Co., 1989). Also see, Daniel Okimoto, Between MITI and the Market, (Stanford: Stanford University Press, 1989).
12. See T.J. Pempel, "Japanese Foreign Economic Policy, the Domestic Bases for International Behavior", in Peter Katzenstein ed., Between Power and Plenty, (Madison: University of Wisonsin, 1978).
13. Kenneth Courtis of the Asian Capital Group has argued this in many places.
14. During World War II significant elements of the elite collaborated with the Nazi occupiers or worked with the puppet Petain government. After the war in a political vacuum and before groups rooted in the traditional economy could reorganize themselves, Charles de Gaulle, the one national symbol of French resistance, established new state institutions committed to growth.
15. When the 4th Republic was constituted, and de Gaulle withdraw from politics for a decade, the traditional economic groups reestablished their political position.
16. As important, deep divisions ran through society. Fights about the very character of French society dating from the French revolution in 1789, fights that divided both left and right, rose to the surface of French political life.
17. There are many analyses of this issue. My favorite is R.W. Johnson, The Long March of the French Left, (London: Macmillan Publishing Co., 1981).
18. Peter Katzenstein, Small States in World Markets, (Ithaca: Cornell University Press, 1985).
19. Fritz Scharpf, Crisis and Choices in European Social Democracy, (Ithaca: Cornell University Press, 1991), p.9.
20. Ibid.
21. Ibid., p. 13.
22. To that I would add that, the failure to find a technical solution in the first round of effort need not lead to antagonistic and disruptive actions by the individual actors.
23. Douglass Hibbs, "On Political Economy of Long Run Trends and Strike Behavior", British Journal of Political Science, Vol. 8, p. 153-175.
24. Andrew Martin, "Trade Unions in Sweden", in Peter Gourevitch ed., Union and Economic Crisis: Britain, West Germany, and Sweden, (London, Boston: Allen and Unwin, 1984). Also, see Scharpf op. cit.
25. See "The Wallenbergs: the Empire Strikes Back", in The Economist, March 2, 1991,Vol. 318, no. 7696, p. 62-3.
26. Peter Katzenstein, Policy and Politics in West Germany, (Philadelphia: Temple University Press, 1987).
27. Andrew Shonfield, Modern Capitalism: The Changing Balance of Public and Private Power, (London, New York: Oxford University Press, 1965).
28. Gershenkron, op. cit.
29. See James Medley, "German Monetary Policy and Industrial

Policy", a report to the U.S. Congress Joint Economic Committee for the House Committee on Banking.
30. This is based on several works: Peter Readman, The European Money Puzzle, (London: Joseph, 1973); Dimitri Vittas ed., Banking Systems Abroad, (London: Inter-Bank Research Organization, 1978); and Medley, op. cit.
31. Peter Katzenstein, Policy and Politics in West Germany, (Philadelphia: Temple University Press, 1987).
32. Douglass Webber, "Institutions, Structures, and the Intermediation of Interests Under the Christian-Liberal Coalition in West Germany, a paper presented to the Institutions, Structures and Intermediation of Interests ECPR Joint Sessions, Bochum, April 2-7, 1990.
33. Bundesverband der Deutschen Industrie (BDI), Bundesvereinigung der Deutschen Arbeitgeberverbande (BDA), and Deutscher Industrie-une Handelstag (DIHT)
34. Deutscher Gewerkschaftsbund (DHB)
35. See Kathleen Thelen, Union of Parts, forthcoming Cornell University Press, January 1992.; Lowell Turner, Democracy at Work: Changing World Markets and the Future of Labor Unions, (Ithaca: Cornell University Press, 1991); and Peter Katzenstein ed., Industry and Politics in West Germany, (Ithaca: Cornell University Press, 1989).
36. Katzenstein, Policy and Politics in West Germany, p.16.
37. Gary Herrigel, "Industrial Order and the Politics of Industrial Change", in Katzenstein ed.,Industry and Politics in West Germany, op. cit.
38. Ibid.
39. Katzenstein, Policy and Politics in West Germany, op. cit.
40. Ibid., p.12.
41. Ibid.
42. Katzenstein, Industry and Politics in West Germany, op. cit.
43. I have slightly restructured a sentence of Peter Katzenstein (Ibid. p. 8), but I believe the sense remains identical.
44. The final complexity, of course, is that German domestic politics and the politics of the economy have been profoundly shaped and constrained by the effort to reconstruct post-war Europe. One of the purposes of the creation of the European Economic Community was to contain Germany, and part of the German objective in forming the Community was to bind itself to the West. Adenauer's commitment to national unification wrote a check that he never expected to cash, but which was honored with great political gain by Kohl nearly forty years later.
45. From Paolo Guerrieri, Technology and International Trade Performance of the Most Advanced Countries, Berkeley Roundtable on the International Economy working paper #49, 1991. The following relates to Figure 1.

The indicator of the contribution to trade balance (ICTB) of a country (j) with respect to a given group of products (i) is the following:

$$ICSi = (Xi - Mi) * 100 - (X - M) * (Xi + Mi) * 100$$

(X + M)/2   (X + M)/2   (X + M)

Xi = total exports of country (j) in the product group (i).
Mi = total imports of country (j) in the product groups (i).
X = total exports of country (j).
M = total imports of country (j).

If the contribution (positive or negative) of each group pf products to trade balance is proportionally equivalent to its weight in total trade (import plus export), then the values of the ICTB indicator for that groups of products is equal to zero. Hence, positive ICTB values indicate those product groups whose positive contribution to trade balance is greater than their weight in total trade. Symmetrical consdiderations are associated with negative ICS values. The sum of the indicators with respect to the various product groups (i) in which the total trade of a country is disaggregated, is equal to zero (see CEPII, 1983). This indicator has been here worked out with respect to the 9 group products in which total trade has been disaggregated for each country.

46. Ibid.

47. The capital equipment and heavy industry orientation, though, may have created a line of technology that is oriented away from the flexible volume production that has formed the core of Japanese production strategy.

48. Horst Kern and Michael Schumann, "New Concepts of Production in West Germany" in Katzenstein ed., Industry and Politics in West Germany, op. cit.

49. Ibid. See also Gary Herrigel, "Industrial Order and the Politics of Industrial Change" in Katzenstein ed., op. cit.

50. Louis Hartz, The Liberal Tradition in America, (New York: Harcourt Brace, 1955).

51. The clearest estimate of this is made in the introduction of Suzanne Berger ed., Organizing Interests in Europe, (Cambridge: Cambridge University Press, 1981).

52. Scharpf, op. cit.

53. Lowell Turner, op. cit.

54. Ibid., p. 421.

55. John Zysman, Political Strategies for Industrial Order, (Berkeley: University California Press, 1977). The same position was adopted by the Review of French Innovation Policies, French Examiners Report, (Paris, OECD, 1986).

56. Laura Tyson and John Zysman, "Developmental Strategy and Production Innovation in Japan", in Johnson, Tyson, and Zysman, Politics and Productivity: The Real Story of Why Japan Works, (New York: Ballinger, 1989).

57. See Kozo Yamamura ed., Policy and Trade Issues of the Japanese Economy, (Seattle: University of Washington Press, 1982).

58. See Johnson, Tyson, and Zysman, op.cit.

59. My thanks to my colleague Steve Cohen for this adaptation of his title.

60. For non-oil producing developing countries with limited capacity to expand exports to pay the tax, the burden was

certainly the greatest. But it did create serious problems in each advanced country.

61. See Linberg, op.cit.

62. Robert Bacon and Walter Eltis, Britain Economic Problems: Too Few Producers, (London: Macmillan, 1978).

63. Robin Gaster, The Politics of White Collar Unionism in Great Britain, doctoral dissertation, University of California at Berkeley, 1986.

64. Paul McCracken, et al., Towards Full Employment Price Stability, (Paris: OECD, 1977).

65. Richard N. Cooper, The Economics of Interdependence: Economic Policy in the Atlantic Community, (New York: McGraw Hill, 1968).

66. Robert Boyer, The Regulation School, (New York: Columbia University Press, 1990).

67. See Stephen Cohen and John Zysman, Manufacturing Matters, (New York: Basic Books, 1987); also by Cohen and Zysman, "Manufacturing Innovation and American IndustrialCompetitiveness" in Science, Vol. 239, March 4, 1988, P. 1110-1115. Also see, Michael Piore and Charles Sable, The Second Industrial Divide, (New York: Basic Books, 1984), and the MIT Commision's, Working Papers of the MIT Commission on Industrial Productivity, (Cambridge, London: MIT Press, 1990).

68. Paolo Guerrieri, Technology and Internatioanl Trade Performance of the Most Advanced Countries, Berkeley Roundatble on the International Economy (BRIE) working paper #49, 1991

69. Susan Strange, Casino Capitalism, (Oxford, New York: B. Blackwell, 1986). The emerging Euro-currency markets expanded as the funds of the OPEC countries were moved about, ultimately connecting wholesale money markets around the world. When Citibank's view that sovereign nations would not default on loans proved painfully wrong, the American banks retreated. The statistics of trade and finance became understood more widely: despite global wholesale profits, banks remained rooted in their national economies. The global position of these banks rested on the investment of the national trade surplus, on the support of the nation's industrial firms, and -- in general -- their domestic deposit base. The retreat left European and Japanese banks the global giants. See Philip Wellons, Passing the Buck: Banks, Government, and Third World Debt, (Boston: Harvard Business School Press, 1987).

70. David M. Meerschwam, Breaking Financial Boundaries: Global Capital, National Deregulation, Financial Services Firms, (Boston: Harvard Business School Press, 1991).

71. For a different version of this see; Stevel Vogel, Japanese High Technology, Politics and Power, BRIE research paper #2, March 1989.

72. See Yamamura op. cit.

73. Michael Borrus among others was the first to use this phrase.

74. Steven Vogel doctoral dissertaion, Changing the Rules The Politics of Regulatory Reform in Comparative Perspective is a remarkable piece of work on this subject. See Johnson, "MITI, MPT and the Telecom Wars" in Johnson, Tyson, Zysman op cit. Also

see, Takashiro Yamada and Michael Borrus, Change and Continuity in Japan's Telecommunication Policy, BRIE research paper #4, forthcoming 1991.
75. See Globalization and Production, BRIE working paper #45, 1991.
76. See John Zysman and Michael Borrus, "Industrial and American National Security", in The Highest Stakes: The Economic Foundation of the New Security System, Oxford University Press, forthcoming Spring 1992.
77. Malaysian data from Malaysian Industrial Develpoment Authority as cited in "The Rising Tide: Japan in Asia", Special Supplement, Japan Economic Journal, 1990, p.4.
78. John Zysman and Wayne Sandholtz, "Europe's Emergence as a Global Protagonist", in The Highest Stakes, op cit.
79. Wolfram Hanrieder, Germany, America, Europe: Forty Years of German Policy, (New Haven: Yale University Press, 1989).
80. Zysman and Sandholtz op. cit.
81. See Raul Hinojosa-Ojeda and Sherman Robinson, Alternative Scenarios of US Mexico Integration: A Computable General Equilibrium, Department of Agricultural and Resource Economics working paper #609, April 1991.
82. Zysman and Borrus op. cit.
83. See for example Mancur Olsen, Rise and Decline of Nations, (New Haven, Yale University Press, 1982).
84. See Vogel, op. cit.
85. See Johnson, "MITI, MPT and the Telecom Wars" in Johnson, Tyson and Zysman, op. cit. Also see, Yamada and Borrus op. cit.
86. Most fully argued in Politics and Productivity, op. cit.
87. John Goodman, Political and Social Schanges in the 1990s, in eds. Norman Ornstein and Mark Perlman, The United States Faces a United Europe, (Washington D.C.: American Enterprise Institute, 1991).
88. Goodman op. cit.
89. Because of the funds Brussels offers, some regional groups seek to bypass their national capitals. Regional autonomy is, in fact, routinely increased when the local authorities, as in Germany, already have the capacity and responsibility for policy-making. The national government continues to intermediate when authority is more centralized. For example, the Basques in Spain actively seek autonomy from national authorities. In some cases national governments resist EC intervention as part of a broader political drama.

Reinforcing a tendency toward regional responsability is the fact that many of the most innovative dynamic segments of European industry are concentrated in regional agglomerations such as Prato in Italy or Bad Wurstenberg in Germany. These industrial "districts" consist of horizontal connections among firms that cooperate to provide an infrastructure even as they compete in international markets. These regional interests are potentially creating new political attachments.
90. Several comments cannot be incorporated in the text but should be made. First, the conservative defeat was triggered by a strategy of economic management which emphasized the necessity

of policy discipline to return to the orderly normal growth of the 1960s, a strategy that over time developed a political tone of conflict and confrontation. The left exploited that tone to give credence and meaning to its ideology of class conflict. Second, Mitterand was faced with two choices when his initial policy failed -- the Socialist-left's aggressive national strategy that demanded abandoning the EMS and many other European commitments, or an imitation of the conservative policy -- Mitterand chose the latter. That policy decision also meant a political break with the Communists. Third, the modernizing coalition began to erode after deGaulle's defeat in 1969, and by the time of the victory of the Socialists in 1981, the political base of the conservatives had narrowed dramatically. Now the base and reach of the Socialist party dwindles, and its rival but ally to the left collapsed as a political force long before the fall of the Berlin Wall. In fact the collapse of the CP has directly fed the emergence of the racist National Front of the demagogue, Le Pen. The nature of the next political settlement, the basis of the next enduring governing coalition, and the policy strategies it may follow are not at all clear.

91. William Lanzonick, Competitive Advantage on the Shopfloor, (Cambridge: Harvard University Press, 1990).

92. Suzanne Berger and Michael Piore, Dualism and Discontinuity in Industrial Socities, (Cambridge, New York: Cambridge University Press, 1980).

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