EAST ASIAN REVIEW Vol. 14, No. 4, Winter 2002, pp. 19-41

Globalization and East Asia: Challenges to Governance and Its Developmental Future

Chung Jin-young

INTRODUCTION

Five years after the financial crisis, East Asian countries find themselves at another crossroads in their journey towards development. The euphoria of rapid recovery from the crisis is over now, and in its place, economic deterioration and political instability cast a dark gloom over the region once again.[1] Most countries have lost the confidence that they can revive their economies and are more concerned about what can and shoul be done just for economic survival. Is East Asia heading toward an era of degeneration similar

1) There are many symptoms of economic slowdown, and even recession in most East Asian countries. *The Economist* (July 7, 2001) has published an editorial entitled "East Asia Falling (again)," in which we can find a rough picture of the slowdown: "Real GDP fell in Singapore, Taiwan and Thailand in the first quarter and probable shrank again in the second. Singapore’s industrial production fell by 11 % in the year to May. South Korea and Hong Kong will be lucky to see GDP growth of 2-3 % this year, down from rates of 9 % and 10 % respectively in 2000. Exports from East Asia, excluding China, have fallen by around 10 % over the past year, compared with growth of almost 30 % in early 2000.”

East Asian Review, 14(4), Winter 2002, pp. 19-41

Published by the IEAS, 508-143 Jungrung 2-Dong Songbuk-Ku Seoul 136-851 KOREA

to what Latin America experienced in the 1980s? Or, perhaps East Asia is simply suffering the momentary pain that comes with structural changes necessary for its future stability and prosperity. It is unclear which path East Asian nations will follow toward economic and political development, but East Asia's future depends largely on how those nations deal with the current impasse.

Why has East Asia failed to recover from the crisis, instead falling into the current situation? Can East Asian countries regain their momentum toward rapid and healthy development? The key lies in how they cope with looming challenges of globalization. Globalization is not the sole cause of East Asia's current problems. It is easy to identify other diverse causes, both internal and external. As for internal causes, massive bad loans, highly leveraged firms, weak financial institutions, interventionist governments, social unrest, moral hazard, and lack of transparency are the culprits. External causes include massive and rapid capital mobility, international financial instability, pressures on policy and institutional changes, fierce competition, and governments' weakened leverage over the wild flow of capital. However, we believe that most of these causes are related, directly or indirectly, with the challenges of globalization, and that East Asia's developmental crisis therefore comes mainly from the conflict between their development models and globalization. Simply put, the so-called East Asian development model cannot work as effectively in the era of globalization as it did previously.

Moreover, globalization has posed serious challenges to governance in East Asian countries. Crises in development have greatly eroded the legitimacy of the existing political economic model, while East Asian governments' failure to overcome the crisis has brought about political instability. Succeeding governments have come to power with promises to carry out necessary reforms, but are unable to keep promises in face of economic difficulties and opposition. The capacity of governments to deal with domestic problems has been significantly reduced as firms, financial institutions, and social groups have gained new freedom, including the power to challenge government regulations. In short, East Asian countries have failed to develop a new, cooperative political economic model to achieve benefits such as economic development, democratic stability, and social peace.

This essay argues that East Asian countries have so far failed to cope with the challenges of globalization successfully and have fallen into development and governance crises. In a desperate effort to overcome them, especially since the 1997-98 financial crisis, they have adopted three measures[2]: tightening capital control and reducing interdependence; adjusting and reforming national economic structures; and advancing East Asian regional economic cooperation. Malaysia advocates the first type of response, and has achieved some success at least for the time being. It is difficult, however, for other East Asian countries to follow in Malaysia's footsteps. Most countries, including crisis-hit South Korea and Thailand, Japan and, to a lesser extent, China, pursue various combinations of the second and third types of response. The results for the second group, however, have been unsatisfactory. What direction will East Asian countries take in the face of future globalization?

In the next section, a general overview is presented on the relationship between globalization and governance. Section III features a discussion of the challenges of globalization, and its effect on East Asian development. In Section IV, the continuing challenges to governance in East Asia are reviewed. The conclusion presents some scenarios of risk.

2) Chung Jin-young, "Debating East Asia's Currency and Financial Crisis and Its Developmental Future" (in Korean), *Korea and World Politics*, Vol. 16, No. 2 (2000).

GLOBALIZATION AND GOVERNANCE: CHALLENGES AND IMPACTS

Globalization is a process of integrating the globe through increasing flows of capital, products, services, ideas and people across international borders. This process has been brought about both by the revolutionary development of information and telecommunication technologies and by the liberalization of trade and finance in major countries.[3] To a certain extent, globalization is a natural byproduct of market tendency expand as firms and people pursue business opportunities. In this sense, globalization is inevitable at the current stage of human history. However, it is also an outcome of the conscious efforts of some leading countries and firms in the world economy. Accordingly, it is possible to control and manipulate the speed and trajectory of globalization.

Regardless of the origin and nature of the driving forces for globalization, globalization has exerted tremendous impacts on the lives of people, firms, and states on this globe: how they can survive and who can win is now determined to a great extent in global markets. Globalization has transformed the environment in which the actors live and compete, and they have been forced to change the way they live and do business in order to survive and succeed. The challenges they face are two-fold. The first is the challenge of adapting to global standards. In order to participate in the global economy and the world community, nations and firms are required to act in accordance with globally accepted rules and norms.

---

3) One can identify numerous forces that drive globalization. Emphasis on two factors here is similar to what Jeffrey Frankel points out: "The two major drivers of economic globalization are reduced costs to transportation and communication in the private sector and reduced policy barriers to trade and investment on the part of the public sector." Jeffrey A. Frankel, "Globalization of the Economy," *NBER Working Papers*, 2000), p. 45.

Certainly, pressures from international organizations such as the International Monetary Fund (IMF) and the World Trade Organization (WTO) and powerful states like the United States play a major role.

The second challenge relates to upgrading international competitiveness. Nations and firms are now exposed to boundless competition, and their fate is greatly dependent upon how well they do in competitive world markets. In other words, competitiveness is now a life-or-death question for both. Then, the question is how to improve competitiveness, knowing how difficult it is to win the race. The competitiveness of a nation is not simply determined by a national firms' adopting advanced technology and marketing strategy. It also requires other variables including political stability, industrial peace, good policies, well-functioning financial markets, and abundant human resources, among others.

It is in this context that the question of governance arises in an era of globalization. As globalization proceeds, it becomes more clear that the existing governing mechanisms do not fit to the changed environment, or do not work effectively anymore. Individual countries are now required to adapt their existing rules and norms to global standards and to upgrade their international competitiveness in order to survive and succeed. Ironically, their capacity to meet with these challenges tends to be limited by the process of globalization itself.

The concept of governance is widely used nowadays. We can often hear expressions like global governance, regional governance, corporate governance and national governance. However, partly because of the widespread usage of the concept, it is difficult to find a clear consensus on the definition. Those who are concerned with global governance tend to use the term as a way to explain the possibility of international order without government. James Rosenau, for example, conceives of it as "a system of rule that is as dependent on intersubjective meanings as on formally sanctioned constitutions and charters." For Rosenau, "governance is a more encompassing phenomenon than government. It embraces governmental institutions, but it also subsumes informal, non-governmental mechanisms."[4] Similarly, Robert Keohane and Joseph Nye Jr. define governance as "the processes and institutions, both formal and informal, that guide and restrain the collective activities of a group."[5]

However, those who are concerned with governance at the national level tend not to emphasize the difference between governance and government. For instance, Asian Development Bank (ADB) defines "governance as the manner in which power is exercised in the management of a country's social and economic resources for development." Certainly, even by this definition, governance is different from, and broader in meaning than government. But governance is mainly related with what and how the government does in economic as well as political spheres. Thus, governance involves not only governmental activities but also the functioning of various markets and market-related organizations in a society.

For the purpose of this essay, ADB's definition of governance is far more relevant than those of international relations scholars. Moreover, ADB's discussion of the "four pillars of governance" is also informative to us in discussing the impacts of globalization on

---

4) James Rosenau, "Governance, Order, and Change in World Politics," in J. Rosenau, and E. Czempiel, eds, *Governance without Government: Order and Change in World Politics* (Cambridge: Cambridge University Press, 1992), p. 4.

5) Robert Keohane, and Joseph Nye Jr., "Introduction," in J. Nye Jr., and J. Donahue, eds., *Governance in a Globalizing World* (Washington, D.C.: Brookings Institution Press, 2000), p. 12. According to them, "Government is the subset that acts with authority and creates formal obligations. Governance need not necessarily be conducted exclusively by governments and the international organizations to which they delegate authority. Private firms, associations of firms, non-governmental organizations (NGOs), and associations of NGOs all engage in it, often in association with governmental bodies, to create governance; sometimes without governmental authority."

governance.[6] They are *accountability*, *transparency*, *predictability*, and *participation*. For good governance, officials should be accountable to those they serve, and the general public should be able to easily access relevant and timely information. Laws and regulations should be so "clear, known in advance, and uniformly and effectively enforced" that government activities are predictable. Finally, participation is necessary for obtaining "reliable information" and for "a reality check and watchdog for government action."

In today's globalized world, governments are under intense pressure to maintain good governance in order to meet global standards and to gain more confidence from investors and international credit rating agencies. Good governance is also a prerequisite for international competitiveness in today's global markets because of the increased international mobility of capital and human resources. In this sense, globalization pushes governments to be accountable, transparent, predictable, and participatory. But globalization itself tends to put heavy constraints on the government's ability to carry out what is necessary for good governance. And good governance does not necessarily mean good democracy. The quality of governance is judged mostly by major actors in the global markets, while the quality of democracy is judged primarily by its people. What is good for the former may or may not be good for the latter, and *vice-versa*. Nevertheless, the quality of both economic governance and political democracy is greatly influenced by the impacts of globalization.

David Held and his associates[7] provide a useful typology for the discussion of the impacts of globalization, consisting of four types: *decisional*, *institutional*, *distributive*, and *structural impacts*. This typology will be used for the discussion of the challenges of globalization to development and governance, but with a slight

---

6) Asian Development Bank, *Annual Report* (1998), p. 17.

7) David Held, *et al*., *Global Transformations: Politics, Economics and Culture* (Stanford, CA: Stanford University Press, 1999), p. 18.

modification in each type as follows:

Decisional Impacts. Globalization impacts decision-makers' policy choices through changing "the relative costs and benefits of the policy choices." It is easy to understand, as Helen Milner and Robert Keohane point out, that globalization "affects the opportunities and constraints facing social and economic actors, and therefore their policy preferences."[8] For instance, those who can take advantage of globalization to expand their external markets will favor globalization, while those who have to compete with foreign interests in domestic markets will oppose globalization.

Institutional Impacts. The impact of globalization is not limited to decision-makers' preferences. Globalization can also change the agenda of and the relevant institutional set-up for decision-making structure. Globalization brings new issues and options into the decision-making process, an important example of which is to build a new institution to cope with the challenges of globalization. For instance, as countries opt for, or are forced to choose financial liberalization, they find it necessary to establish or strengthen a financial supervisory institution.

Distributional Impacts. It is often pointed out that globalization holds significant consequences for "the distribution of power and wealth within and between countries."[9] One gloomy prediction for the advance of globalization is the emergence of a "20:80 society" in which 20 percent of the population will garner and enjoy most of the benefits of globalization, while the remaining 80 percent will be isolated from them.[10] In this scenario, globalization can intensify distributional conflicts and damage social peace.

---

8) Helen Milner, and Robert Keohane, "Internationalization and Domestic Politics: An Introduction," in R. Keohane, and H. Milner, eds., *Internationalization and Domestic Politics* (Cambridge: Cambridge University Press, 1996), p. 4.

9) David Held, *et al.*, *op. cit.*, p. 18.

10) Hans-Peter Martin, and Harald Schumann, *The Global Trap: Globalization and the Assault on Democracy and Prosperity* (London: Zed Books, 1998).

Structural Impacts. Structural impacts refer to the ways in which "globalization conditions patterns of domestic social, economic and political organization and behavior" so that "globalization may be inscribed within the institutions and everyday functioning of societies."[11] For instance, globalization shifts the balance of power between states and markets in favor the latter. The diffusion of political power and the shift from government to governance are also good examples of the structural impacts of globalization.

Certainly, these impacts are not automatically translated into policy shifts or institutional transformations. Milner and Keohane emphasize the role of political institutions in mediating the impacts of globalization on the domestic community: "political institutions can block and refract the effects of [globalization]."[12] Held and his associates[13] are far more specific about this:

> The structural consequences of globalization may be visible over both the short and the long term in the ways in which states and societies accommodate themselves to global forces. But such accommodation is, of course, far from automatic. For *globalization is mediated, managed, contested and resisted by governments, agencies and peoples*. States and societies may display varying degrees of sensitivity or vulnerability to global processes such that patterns of domestic structural adjustment will vary in terms of their degree and duration. (Italics inserted by author.)

Thus, countries respond differently to the impacts of globalization. Due to the variations in domestic political and institutional configurations, different countries respond differently even to the same external challenge. Some countries are able to adapt

11) David Held, *et al.*, *op. cit.*, p. 18.
12) Helen Milner, and Robert Keohane, *op. cit.*, p. 5.
13) David Held, *et al.*, *op. cit.*, pp. 18-19.

themselves to the changing global environment, while others lag behind, an important determinant of the rise and fall of nations. Those who can overcome the challenges of globalization and take advantage of the opportunities will succeed, while those who cannot will fail. East Asian countries, indeed, East Asia as a region, stands at a crossroads on the journey towards development.

GLOBALIZATION AND THE CRISIS OF EAST ASIAN DEVELOPMENT

The financial crisis of 1997-98 dramatically revealed the shaky foundation and the vulnerability of East Asian economies in the era of globalization. Without intending to raise another controversy over the existence and nature of the East Asian development model in this essay, it is clear that the nations involved had several important components in common in their development strategies: the state's active role in resource mobilization and allocation, the intimate relationship between the government, business, and finance, high saving and investment ratios, and export promotion. When we use the term "East Asian development model," we simply indicate these common elements in their development strategies.

In a certain sense, the mechanism of the East Asian miracle was very simple. As long as development-oriented governments could channel mobilized resources into productive investments and industrial products could be absorbed in export markets, East Asian countries could achieve rapid growth. Firms could expand rapidly with massive borrowings, and banks could lend freely without worrying about risks thanks to the explicit or implicit guarantees of government. Rapid growth accompanied rapid employment increases and, in turn, rapid rises in wages, leading to East Asian "miracles" in many countries.

Why, then, did the once-successful development model stop working effectively? Certainly, this question is directly related with the various discussions about the causes of the East Asian financial crisis of 1997-98. However, the primary concern here is with the impact of globalization on East Asian development, not on the causes of the crisis in general. The argument is that East Asian countries could not maintain their previous development model in the face of globalization. In other words, although East Asian countries could have avoided the financial crisis, they could not avoid spillover when their development strategy became less and less relevant. The crisis of East Asian development came when the old development model lost compatibility in the changed global environment, yet, a new model had not been found, leaving a vacuum.

Systemic Contradictions

At the most fundamental and structural level, East Asian economic systems did not simply differ from, but contradicted Western, especially American, systems.[14] This has two important implications with regard to competition in global markets. First, Americans feel that East Asians follow different rules and, therefore, are unfair competitors. Second, American capital can experience difficulty in penetrating East Asian markets, so that it is less able to reap the fruits of rapid growth there. To resolve these problems, the United States placed heavy pressure on East Asian countries to open up their domestic goods and financial markets through international organizations like the IMF, WTO and the Organisation for Economic Cooperation and Development (OECD). The spread of neo-liberal ideology also contributed to the weakened legitimacy of the East Asian development strategy. Many economists and businessmen began to accept that the state was inefficient while markets were

14) Yoon Young-kwan, "East Asian Development Model and Global Capitalism," (in Korean) in Baek Kwang-il, and Yoon Young-kwan, eds., *East Asia: The Political Economy of Crisis* (Seoul: Seoul National University Press, 1999).

efficient, and the result was criticism of state control in East Asian development. Therefore, at the structural and ideological level, the crisis of East Asian development reflects American influence over East Asia in the struggle for global supremacy. East Asia, dependent upon Western markets and capital and divided among themselves, was deprived of the opportunity to decide its future role in the global economy, and subsequently, fell into the developmental crisis.

Social Rigidity and Inflexible Responses

Can East Asians change their economic systems with American-style market systems and compete equally on the global market? Theoretically, nothing is impossible. Furthermore, it is often argued that East Asians have no choice but to Americanize their economic systems and policies because it is the only way to achieve necessary international competitiveness. In a practical sense, however, East Asians will encounter many roadblocks on the way to systemic and policy changes. Change will meet with opposition. An existing institution or policy reflects a balance of power among various interested groups, and, accordingly, any change in policy or institution will have different impacts on different groups.

In East Asia, practices such as lifetime employment and government-business-finance collusion, the Confucian culture, and the lack of social safety nets, among others, hinder both business and government from responding quickly and flexibly to the changing environment. Uncertainty prevails when old rules become irrelevant, yet new practices do not work. A long period of muddling through will ensue, and in the meantime, East Asia's political and economic uncertainties will continue.

Institutional Inadequacy

Globalization has rendered many existing institutions obsolete, but it has also spurred establishment of new ones. Nations have set about to reorganize governmental structures and to abolish old agencies while building new social and economic institutions. South Korea is a good example. Successive administrations since the late 1980s have continued efforts toward governmental reorganization so that it can effectively cope with the challenges of democratization and globalization. Various institutions were also established to deal with the tasks of financial supervision, management of industrial relations, and social welfare, among others. However, outdated institutions are still numerous, and they compete with new ones for power and resources.

While some institutions once worked effectively, they cannot function effectively in their present stage of development. As ADB[15] observes, old institutions may even hinder further development: "Although economic systems tend to evolve as economies mature, the policies and institutions developed for, and appropriate to earlier stages of economic development tend to get locked in, posing obstacles to further development." Ongoing institutional adaptation and renovation is necessary, yet impossible. As a result, East Asian countries suffer from inadequacies of their institutions in the face of the challenges of globalization and the crisis of development.

Loss of Policy Autonomy and Consistency

In the past, East Asian governments have enjoyed autonomy in planning and carrying out development policies. There was little pressure, from inside or outside their countries. Political leaders often demonstrated a strong commitment to national development, which worked as a firm guide for the direction of economic policies. However, globalization has brought about significant changes in the policy environment, especially in incentive structures for policy options. First, foreign capital and firms have come to play a far

15) Asia Development Bank, *Asian Development Outlook 2001 Highlights* (ADB, 2001), p. 29.

greater role in domestic markets. Also, pressure is being exerted on governments for deregulation and liberalization. In order to take advantage of other markets, a country must open its own domestic markets, and in order to allow domestic firms to access to low cost international financing, it must undertake financial liberalization. But deregulation and liberalization have a price: governments lose leverage and power over private firms and banks. For this reason, governments often fail to carry out necessary policy changes and institutional reforms. Moreover, strong social and economic groups tend to oppose deregulation and liberalization to protect their own interests. As a result, government policies often show conspicuous inconsistencies and provide confusing and conflicting signals to markets.[16)]

What is worse, governments often adopt policies or policy changes without preparing adequately for their possible negative impacts. Financial liberalization is a good example. Massive and abrupt inflows and outflows of foreign capital have had grievously negative impacts on national economies. Yet, governments still focus only on attracting foreign capital when they opt for financial liberalization. The massive inflow of foreign capital creates an economic bubble, and when that bubble bursts, loss of capital flow brings about a financial crisis such as occurred in 1997.

East Asian countries fell into the crisis of development in face of globalization, when the so-called developmental state lost both its legitimacy and its effectiveness. The government-business-finance collusion turned out to be a major source of corruption and moral hazard, proving that when private firms and financial institutions pursue their own self-interests, the state is unable to coordinate them towards socially desirable activities. Economic reforms were in disarray, and the spirit of hard work was displaced by distributional conflicts.

---

16) Stephen Haggard, *The Political Economy of the Asian Financial Crisis* (Washington, D.C.: Institute for International Economics, 2000).

GLOBALIZATION AND GOVERNANCE IN EAST ASIA

Democratic versus Economic Governance

Governments are now evaluated in global markets, and are rewarded or punished according to their performance.[17] The criteria of evaluation may include the components of good governance we mentioned above with reference to ADB's "four pillars." Those governments that receive a good evaluation can access international financial markets for cheap, easy money, as well as other benefits: The inflows of capital accelerate economic growth, raise stock prices, and heighten the popularity of the incumbents. If, on the other hand, governments cannot meet market expectations, they are severely punished. The situation raises a serious question of who governs in today's globalized world. The following statement by Martin and Schuman[18] bears this out:

> Currency and security dealers acting on a world scale direct an ever-growing flow of footloose investment capital and can therefore decide on the weal and woe of entire nations, and do so largely free of state control.... More and more often, politicians and electorates throughout the world see how the anonymous actors of the money markets are taking control of their economy, so that politics is left only with the important bystander.

---

17) With regard to the evaluation of governments, international credit rating companies such as Moody's and Standard and Poor's play a very influential role. Their ratings determine the terms of governments' accessibility to international financial markets.

18) Hans-Peter Martin, and Harald Schuman, *op. cit*., p. 46.

As East Asian governments are extremely sensitive to how global markets evaluate their activities, they cannot be excluded from this trend. When a government chooses policies, it must take into account how that choice will be perceived in the markets. Of course, they want to avoid punishment by the markets by choosing market-conforming policies. Governments now pay as much attention to the vote of confidence in the markets as they do to the popular vote in elections.

Is there any contradiction between the two votes? Governments that have the confidence of the market will have a better chance of being rewarded in the elections, while those with a poor market evaluation will probably lose power. Then, how about governments with strong popular support? Will they receive a vote of confidence from the markets? Considering the social and economic conditions in today's most East Asian countries, there is no positive answer. As was the case with most Latin American countries, policies for popular support will be different from what the markets demand. In this sense, East Asian countries are currently suffering from the pains of the "double transitions" which Latin American countries experienced in the 1980s.[19]

Many countries in East Asia face the dual task to consolidate their shaky, new democracies and to carry out economic reforms, and yet, requirements for the two tasks often contradict one another. On the one hand, democratic consolidation requires a broad base of support for the new democracies, which can usually be achieved through the adoption of popular policies. On the other hand, economic reforms tend to increase opposition, not amity, towards governments, because such measures usually damage the interests of socially influential groups. Therefore, East Asian countries face a dilemma, albeit to a varying degree. That struggle between good

19) Stephen Haggard, and Robert R. Kaufman, "The Challenge of Consolidation," in L. Diamond, and M. Plattner, eds., *Economic Reform and Democracy* (Baltimore: Johns Hopkins University Press, 1995).

economic governance and good democratic government is a fundamental challenge of globalization in East Asia.

In addition, East Asian countries have faced, and continue to face several other serious challenges.

Economic Uncertainties

With its development model delegitimized and economic reforms faltering, East Asian countries are in a confusing state with regard to their economic future. Rapid, radical reforms could be the answer to economic renewal and revival, but that would be extremely difficult, politically as well as technically.[20)] Years of efforts toward economic reform failed to reap any visible successes. Table 1 by the Swiss-based Institute for International Management Development (IMD), provides an example of this. Based on competitiveness rankings, it shows no discernible progress in the competitiveness of East Asian countries. Rather, Japan and four crisis-hit Southeast Asian countries have experienced continued deterioration in their international competitiveness. Although Korea and Taiwan did a little better than Southeast Asian countries, their competitiveness did not improve significantly, either.

Another line of efforts for the future of East Asian development is to construct a regional economic cooperation mechanism. Since the 1997-98 crisis, most East Asian countries have shown thier eagerness

20) A recent evaluation by the Economist on the difficulties of economic reform in East Asia is relevant here: “As countries bounced back from the crisis faster than expected, governments concluded that reform could wait. Firms have been slow to sell off assets and reduce debts. Banks have been slow to write off bad loans. Governments have failed to deregulate services, which could have created new jobs to offset the collapse in IT exports. Fragile banking systems and inadequate corporate restructuring continue to cramp domestic expansion. Lower interest rates are less effective in stimulating demand because banks saddled with too many bad loans are reluctant to lend more and debt-laden firms cannot borrow.” *The Economist*, July 7, 2001.

Table 1. The World Competitiveness Scoreboard: East Asian Rankings

Country / Year	1997	1998	1999	2000	2001
Singapore	2	2	2	2	2
Hong Kong	3	5	6	12	6
Taiwan	18	14	15	20	18
Japan	17	20	24	24	26
Korea	30	36	41	28	28
Malaysia	14	19	28	27	29
China	27	21	29	30	33
Thailand	31	41	36	35	38
Philippines	29	32	31	37	40
Indonesia	38	40	47	44	49

Source: http://www.imd.ch/wcy/ranking/pastresults.html.

to participate in a regional economic group.[21] Japan proposed an Asian Monetary Fund right after the outbreak of the crisis in mid-1997. Members of the Association of Southeast Asian Nations (ASEAN) have been active in promoting a linkage between ASEAN and three Northeast Asian countries—Korea, Japan, and China—as well as in deepening their own cooperation. Especially, the ASEAN+3 formula appears promising for East Asian cooperation. At its initiative, for instance, a network of currency swap agreements was established among East Asian countries. Recently, China and ASEAN have agreed to negotiate for their bilateral Free Trade Area. However, it must be acknowledged that the prospect for East Asian regional cooperation is still limited by two prevailing determinants: strong American opposition to the formation of any East Asians-only club and the potential rivalry between Japan and China for regional hegemony. Therefore, East Asian cooperation can hardly be an escape route from the current impasse.

---

21) Chung Jin-young, *op. cit.*

Diminishing State Capacity

It is often argued that East Asia's strong state is the major source of the problem nowadays. However, less than a decade ago, it was praised as the engine of growth for East Asia's miracle.[22] The theory of the developmental state was well received in the literature on development.[23] According to those theorists, a state's strength is not the problem, rather it is the solution. Indeed, it was through a strong, not a weak state that East Asian countries could effectively participate in the world economy. The existence of a strong state was not a source of weakness but of competitiveness, as Peter Evans points out: "high stateness may even be a competitive edge in a globalized economy."[24]

However, as we mentioned above, East Asia's developmental state has been discredited as the major source of numerous problems experinced by East Asian countries since the outbreak of the financial crisis. According to Peter Evans,[25] this reflects "the ideological face of the current global order." In fact, what East Asian countries need is not a weak state or the eclipse of the state. Rather, they still need a strong state, considering the challenges they have been facing. Certainly, the role of the state in the contemporary world should be very selective and limited. Therefore, the kind of state East Asian countries need today is a "small but strong" state. In

---

22) World Bank, *The East Asian Miracle: Economic Growth and Public Policy* (Oxford: Oxford University Press, 1993).

23) Alice H. Amsden, *Asia's Next Giant: South Korea and Late Industrialization* (New York: Oxford University Press, 1989); Robert Wade, *Governing the Market: Economic Theory and the Role of Government in East Asian Industrialization* (Princeton: Princeton University Press, 1990); Peter Evans, *Embedded Autonomy: States and Industrial Transformation* (Princeton: Princeton University Press, 1995).

24) Peter Evans, "The Eclipse of the State? Reflections on Stateness in an Era of Globalization," *World Politics*, Vol. 50, No. 1 (1997), p. 68.

25) *Ibid*., p. 70.

fact, this is what most countries have been pursuing through their governmental reorganizations.

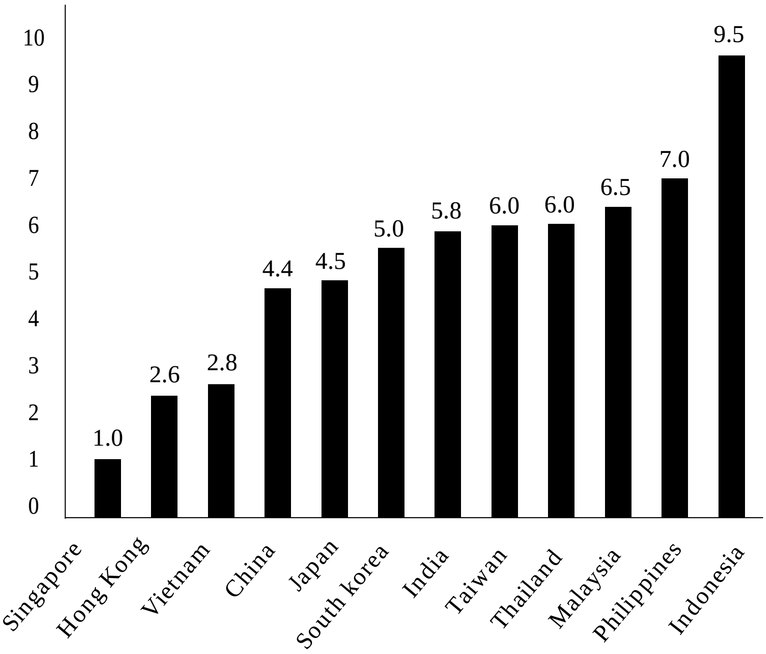
Nevertheless, building a "small but strong" state poses huge challenges.[26] Bureaucratic restructuring is usually faced with strong opposition, and downsizing of governmental organizations and budget is an nearly impossible. Even as new organizations are built, existing ones continue to survive. Structural adjustments to speed recovery and social spending to provide social safety nets for the poor simply add to the huge government debt. In consequence, the goal of a "small but strong state" usually ends up being a "large but weak state." Such a state will introduce problems rather than solve them, and will trigger a whole array of negative impacts on economic and political development.

Political Instability

In recent years, most East Asian countries have suffered from political instability. Thailand, the Philippines, and Indonesia are

26) It is related with a time lag in establishing appropriate institutions. Especially for those developing countries that lack effective institutions, responding to the challenges of globalization is doubly difficult. Merilee Grindle makes this point: "Policymakers face a difficult balancing act in responding to the dual imperative of strengthening institutions and adapting policy to the exigencies of globalization. Strengthening and creating appropriate institutions takes time, yet the challenges of globalization are current and insistent. Institutional reform can produce greater stability in policymaking and implementation, but the reform process often exacerbates political tensions. Governments are pressed to take actions, yet institutional weaknesses increase skepticism about their legitimacy to do so. As far as the responsibilities required of governments in developing countries, the state is clearly not being hollowed out. Yet in the capacity to respond to insistent sources of domestic need and international vulnerability, policymakers can easily come to believe that the state is becoming ever less competent." Merilee Grindle, "Ready or Not: The Developing World and Globalization," in J. Nye Jr., and J. Donahue, eds., *Governance in a Globalizing World* (Washington, D.C.: Brookings Institution Press, 2000).

Figure 1. Government Stability



* Grades are scaled from zero to 10, with zero being the best grade possible and 10 the worst.

Source: *Asian Intelligence* (April 4, 2001).

three very conspicuous examples of continuous governmental or presidential turnover. Malaysia's leader, Mahathir Mohamad has also lost much of his support in the Malay communities. Japan has been notorious for its continuing political paralysis. South Korea and Taiwan have also witnessed increasing social and political disintegration in recent years. Figure 1 provides us a rough measure of political instability in East Asian countries. It shows that Southeast Asian countries demonstrate the greater political instability, Japan and Korea fall in the middle range, while Singapore and Hong Kong are most stable.

Of the two major sources of political instability in East Asia, the first is economic deterioration. Economic decline and people's concern over their economic future bring down the governments' approval rate, while political instability deepens economic uncertainties. In this way, economic and political conditions are closely interrelated. When governments fail to revive the economy and carry out necessary economic reforms, political instability ensues. Second, political practices are also an important source of political instability in East Asia. Although most East Asian countries have achieved formal democratization, the quality of democracy is still unsatisfactory. While citizen's awareness and the socioeconomic environment have radically changed, politicians and the nature of their political game remain basically intact. Therefore in most countries, the general public is frustrated and distrustful of politics and politicians.

Faced with a fundamental dilemma and several other important challenges, East Asian countries tend to slide into the crisis of governance nowadays. Political leaders come and go with their rosy promises unfulfilled. The fate of national economies lies in global market fluctuations. And with political instability hindering economic reform and economic deterioration deepening the political paralysis, a cloud of crisis is beginning to settle over most East Asian countries.

CONCLUSION

Which path are East Asian countries heading for? The crisis of development has already robbed East Asians of their confidence in realizing a prosperous future and the emerging crisis of governance will deprive them of a sense of direction and determination. The combination of economic deterioration and political instability, or the dual crises of development and governance, is certainly the worst possible scenario. Yet it is a distinct possibility. After the debt crisis, Latin American countries spent the 1980s in a "lost decade." Japan lost the decade of the 1990s after the burst of its bubble economy. It is now quite possible that East Asian developing countries are going to experience that "lost decade" phenomena in the very first decade of the 21st century.

Certainly, we can expect some significant differences among the countries in their responses to the crises and the degrees of economic and political deterioration. South Korea could possibly overcome the impending crises and move forward on the road to development. Its industrial base is quite strong, and social and political disintegration is still manageable. Moreover, the public can quickly adapt to the changing environment. However, South Korea has also many negatives: It suffers from national and regional divisions. Democratic politics is still immature and political leaders have lost much of the public confidence. Moreover, the government has a propensity to intervene. Finally, sovereign debt is rapidly accumulating. In all, South Korea will be lucky if it can escape the fate of its East Asian neighbors in the years to come.