

## New Asian Drivers, Japan, Korea and the Lessons of History

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As a long-time observer of the Japanese economy, I found myself growing irritated as I read Raphael Kaplinsky's and Dirk Messner's Introduction to "The Impact of Asian Drivers on the Developing World" (<http://japanfocus.org/products/details/2677>). Of course China and India have already had a huge impact on the global economy and that impact shows every sign of getting yet larger. Two new economic behemoths pushing their way into the club of great powers are naturally going to upset many apple carts. No reasonable person could disagree with the proposition that the "questions" posed by the rise of "Asian Drivers," to use the authors' label for India and China, "need to be addressed in a systematic framework" and the list of such questions the authors volunteer on page 202 – what are the consequences; who wins and loses; what are the implications for the environment, for institutions of global governance, for other developing country plans and so forth – is a worthy enough

start.

But really coming to grips with these questions means getting the history and context right, and from the title on I began to have doubts. Asian Drivers? The last time I checked, the Japanese economy was still larger than that of both India and China combined. Japan invests more in China than does any other country, is probably China's largest trading partner, and, unlike the United States and the EU, runs a trade surplus with China. Chinese factories are stuffed with capital goods of Japanese origin. Japan in 2007 exported some \$200 billion of financial capital that "drives" economies worldwide. If the authors had labeled their piece "The Impact of New Asian Drivers" they would have had no quibble from me, but a piece that discusses "Asian drivers" while largely ignoring Japan is comparable to one on "European drivers" that slights Germany.

The title could be fixed easily enough, but when I encountered the sentence "So, unlike the case of Korea and Japan, which could grow without severe disruption to the global economy we have to suspend the 'small country' assumption in the

case of the Asian Drivers,” my doubts were compounded. Small countries? Japan and Korea are, respectively, the world’s second and ninth largest economies. Even by the measure of population – the authors’ sole criterion for evaluating size – both are among the world’s largest. There are some 220 independent countries in the world. Ranked by population, Japan comes in number 10 (well ahead of every country in Europe except Russia) and South Korea number 25. To be sure, India and China are far larger, but to call Japan and Korea “small” is to destroy the meaning of the word. Lesotho, #144, and one of the places the authors use as a case study to measure China’s impact on other developing economies, is a small country. Japan is not.

More to the point, Japan’s rise to global economic pre-eminence had momentous effects on both the world of the time and on everything that has happened since. Putting aside the pre-World War 2 history -- the fear in the West of floods of cheap Japanese imports that helped bring on the beggar-thy-neighbor policies of the 1930s for example -- it was the inability of the postwar Bretton Woods regime of fixed exchange rates pivoting on the dollar to accommodate the appearance of Japanese trade surpluses in the late 1960s that brought about its demise. If this doesn’t qualify as “severe disruption to the global economy” I don’t know what would. Since that time, we have seen Japanese competition lay

waste to whole industrial sectors in Europe and the United States. That competition was certainly “a” if not “the” explanation for the restructuring of the American economy in the 1990s with far reaching effects on such developing economies as Mexico that make their way primarily as suppliers to the United States. Japanese financing of the American external deficits was one crucial factor that has permitted the United States to live beyond its means for several decades, thereby propping up the external market into which “Asian drivers” could dispose of surplus production. To be sure, China today finances an even larger portion of American deficits than Japan does, but Japan has been at it for 35 years. In every global financial crisis since the Bretton Woods breakup – the 1978 dollar crisis, the 1982 developing country debt crisis, the 1987 stock market crash, the 1995 Mexican peso crisis, the 1997/98 Asian financial crisis – Japan has either played “best supporting” or “starring” roles (it was the floods of next-to-no-interest yen from Japan that provided the financial fuel for the 1997/98 crisis, for example, while the 1987 global stock market panic both started and ended in Tokyo).

This all matters not because the authors have inflated the importance of what has been going on in China and India – that would be almost impossible to do – but because the picture they present of a “bipolar world, dominated by the United States and Europe” that only recently had

to accommodate the rise of China and India is misleading. True, the authors acknowledge that the “bipolar” years were followed by the “emergence of an East and Southeast Asia trading group, largely reflecting the rise of Japan and the Asian Tigers” but they miss the significance of that “emergence” for their own story. For it was that “emergence” that created the conditions particularly for China’s subsequent rise -- both as an example to Beijing and as a source of financial and physical capital as well as a major market.

Practically every one of the six “distinct” challenges the authors contend are posed by China and India today were posed by Japan (and to a lesser extent by Korea) a few decades ago. We have already mentioned size, the first of the challenges. “Second, these economies (i.e., China and India) markedly embody different combinations of state and capitalist development compared with the industrialized world.” For decades now Japan’s example of state-guided capitalist development has exercised analysts and practitioners, most particularly the cluster of advisors around Deng Xiaoping who commissioned a translation of Chalmers Johnson’s 1982 classic MITI and the Japanese Miracle to study “how Japan did it.” If the authors had read this book or dipped into other parts of the vast literature on Japan’s development, they might have found it harder to write sentences such as “With access to cheap

(and often subsidized) long-term capital, (Chinese) firms operate with distinctive time horizons and are less risk averse than their western counterparts.” (First parentheses in the original) or “...Chinese firms often operate abroad as a component of a broader strategic thrust” as if such phenomena had never been seen before. It may be that “Asian Driver firms” will “interact with the global economy... in historically distinctive ways” but to make that determination, one needs to study how Japanese and Korean firms that enjoyed “access to cheap and often subsidized long-term capital”, had “distinctive time horizons”, were “less risk-averse than their Western counterparts”, and participated in a “broader strategic thrust aimed at dominating industries and markets” interacted with the global economy a generation before the Chinese arrived on the scene.



### 1960s Toyota Publica

Japan and Korea do not any longer combine “low incomes and low wages with significant innovative potential” – the third of the “distinct” challenges that China and India are said to pose.

But that was arguably the case fifty years ago when Japan had a per-capita GNP that is smaller than China's today at a time when the likes of Sony were seizing on the commercial potential for the transistor. One can accept that "China and India are associated with very different forms of regional integration" – the fourth so-called "distinct challenge." But the picture the authors present of China's integration – "the processing of imported raw materials and intermediates" -- has long also characterized Japan's and Korea's economic ties with the rest of the region.



**Sony**

#### **Superscope Tape Recorder, 1957**

The authors are right to stress that "foreign firms dominate China's exports", but this is the first really significant deviation the authors mention from the model built a generation ago by Japan. This would be a subject well worth exploring—why, and with what consequences, so much of China's external trade is in the hands of foreigners whereas Japan never allowed it. (A further related question that should command scholarly attention is why China and India, which long fiercely resisted foreign direct investment, have in recent years been so

hospitable to it while Japan and Korea were and are so much less so.) But again, to do that properly, one must have a grasp of what the world was like in the late 1970s when China made its momentous shift in direction.

That was a world that had seen Japan proclaimed as the world's number one economy by every criterion that mattered save sheer size. Japan had emerged from the mid-seventies recession more rapidly than any other developed country; the growth of its exports accounted for some 25 percent of total global growth in exports in 1976. Companies world wide lived in fear of Japanese competition. Japan had been the key player in the four country effort to rescue the dollar in the summer of 1978; three years later, Japan would be financing and enabling the American experiment in the simultaneous tight monetary and loose fiscal policies (aka the "Reagan Revolution") that would lay the groundwork for the restoration of the dollar's primacy in global finance and the American economy recovery.



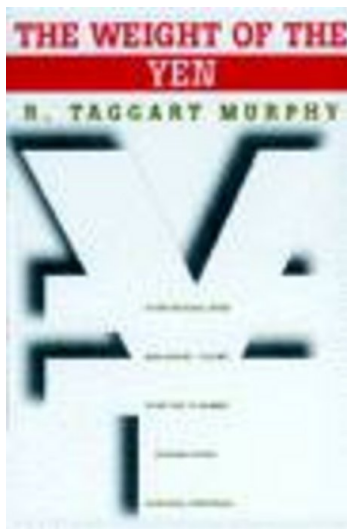
**Reagan and Thatcher**

This all provoked a worldwide fascination compounded of equal parts envy, resentment, and a burning desire to understand how Japan did it – nowhere more obviously than in the developing economies of Asia. Most particularly, this was because Japan seemed to have pulled it off by thumbing its nose at the two dominant development paradigms of the day: the “let the markets rip” neoliberal paradigm coming into ascendancy in the West with the elections of Margaret Thatcher and Ronald Reagan, and the Marxist/Leninist paradigm crumbling in the face of the ever-more-obvious sclerosis of the Soviet Union and from the repeated economic disasters inflicted on China by the recently deceased Mao Zedong. Japan seemed to demonstrate that a powerful bureaucracy could remain in control of economic outcomes while harnessing market forces to engineer a spectacular rise to global pre-

eminence. The effect of this demonstration on the likes of Singapore’s Lee Kwan Yew and Malaysia’s Mahathir Mohamad – not to mention the Chinese leadership – can hardly be exaggerated.

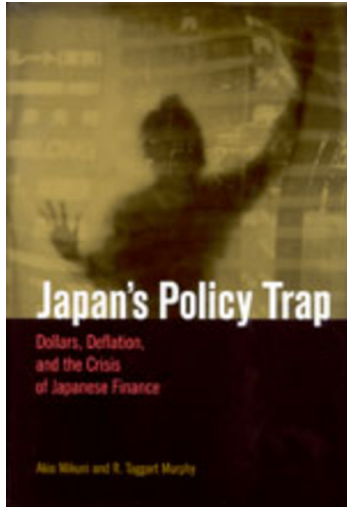
“The Impact of Asian Drivers” shows every promise of being a worthy project. But to make its full impact, it needs to demonstrate a better grasp of the world from which these “Drivers” emerged.

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