

The Role of Institutions in Economic Change

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This paper is a preliminary effort to capture a dauntingly complex and under theorized topic. The authors will be grateful for any and all comments, criticisms and suggestions that might help them move from this version to a more fully elaborated version which is to be presented in August, 2000. Please send comments to <Ha-Joon.Chang@econ.cam.ac.uk> and <pevans@socrates.berkeley.edu>.

1. Introduction

Institutions are systematic patterns of shared expectations, taken-for-granted assumptions, accepted norms and routines of interaction that have robust effects on shaping the motivations and behaviour of sets of interconnected social actors. In modern societies, they are usually embodied in authoritatively coordinated organizations with formal rules and the capacity to impose coercive sanctions, such as the government or the firms. Everyone recognizes that institutions are fundamental to economic change (as well as to the maintenance of economic equilibria) but, despite a resurgence of “institutionalist” thinking inside and outside of economics, over the course of the past 25 years, we are still a long way from any kind of satisfying theory of institutions and their economic effects.

This paper is a modest attempt to push thinking about institutions and economic change forward. Our effort is built around two quite specific, but in our view also quite strategic, case studies of institutions with key roles in shaping economic change. The aim is to use these case studies to illustrate theoretical perspective that we would like to develop and, at the same time, to generate some substantive propositions about the causes and consequences of institutional change that should, in principle, have applications beyond these cases.

First, we will look at one of the institutions that has played the most dramatic role in reshaping relative national trajectories of economic growth in the late 20th century – the developmental state (section 3). The developmental state is a classic example of how institutions make a difference to economic change. The standard economic theories failed to predict the economic rise of the countries of East Asia because it had no basis for anticipating the possibility

that institutional transformation in the public sector could shift private incentives and set these countries on a more dynamic path of industrial accumulation. There was no place in this canon for idea that apparently hidebound mechanisms of bureaucratic governance might be adapt themselves to the management of growth and they would be in turn be able to shift the worldview and incentive structures of what had seemed to be a hopeless local entrepreneurial class. The developmental state, thus seen, is a clear example of the need for an alternative canon.¹

Our focus here is on the Korean developmental state, which epitomizes the particular institutional form. We have, however, chosen not to concentrate our discussion on the institutional effects that connected the developmental state with successful economic growth. Rather than reiterating the story of the emergence of the developmental state and its economic consequences, both of which have been very well documented, we have focused on the *fall* of the developmental state. Why should an institution of such obvious economic effectiveness be subject to political attack while still apparently at the apogee of its economic success and why should such an attack be so successful in undermining the institution? This is the questions that we focus on in this section.

Our second case study moves to the level of “global governance institutions” focusing particularly on the World Trade Organization (WTO) (section 4). We have chosen to focus our second case on the global level for two reasons. First, if institutional analysis is weak in the analysis of national economies, it is significantly weaker still in the analysis of the global arena.

¹ And this has indeed resulted in a significant modification of the mainstream view on economic development and the role of the state in it, as can be seen in, among others, World Bank (1993) and World Bank (1997).

Second, institution-building at the global level is in a formative phase during which new ideas are more likely to make a difference. It is no longer fanciful to see this set of organizations as the embryonic embodiment of global governance institutions that might eventually come to play a role at the global level analogous the role which states have played within their national territories over the last 400 years.

The global political economy is built on information flows and market exchanges, but it is also built on an intricate set of rules whose maintenance and enforcement require concrete organizations. Analysis of globalization cannot afford to neglect the institution building side of the process. Effective theorizing about ideal configurations of global rules requires us to ask: What kind of institution building is required to make the projected rules work and what is the likelihood that such institutions can be constructed? Assessments of the current operation of the global political economy also need an institutional component: How do the governance organizations that have already been created at the global level shape the way rules are made and enforced? Answers to both of sets of institutional queries are fundamental to any understanding of where globalization is going.

The case studies of the developmental state and the WTO complement each other substantively. Together they raise a gamut of issues regarding possibilities for economic governance (and the failure of economic governance) in the contemporary political economy. Our case studies also complement our general conceptual concerns, which are spelled out in a preliminary way in the next section of the paper (section 2).

In this section we argue that an institutional approach must do two things. The first task is to develop a more adequate vision of how institutions shape economic behaviour and

outcomes. Our proposal is that in order to construct such a vision we must get beyond the traditional view of “institutions as constraints” (i.e. understanding institutions primarily as impediments to the ‘natural order’ of the market). Instead, it is necessary to focus attention on institutions as devices which *enable* the achievement of economic goals and, perhaps even more important, on institutions as *constitutive* of the interests and worldviews of economic actors.

The second task, we argue, is to develop a more systematic and general way of understanding how institutions themselves are formed and change over time. Here again, the initial goal is to move beyond the more economistic models of the process that dominate the current discourse on institutions. Neither a functionalist view in which what is must be “efficient” since otherwise it would not exist, nor an instrumentalist view in which institutions are created and changed to reflect the exogenously defined interests of the powerful are adequate (which is not to deny that both are important factors in institutional evolution). Instead, we would argue for what we call a more “culturalist” (or perhaps Gramscian) perspective in which institutional change depends on a combination of interest-based and cultural/ideological projects (in which worldview may shape interests as well as *vice versa*). Simply put, changing institutions requires changing the worldviews that inevitably underlie institutional frames.

Obviously combining a view emphasizing the constitutive role of institutions with a culturalist perspective on their formation leads to a view in which institutions and economic actors are mutually constitutive. This in turn leads to the danger of imagining a self-reinforcing homeostatic system. If institutions shaped worldviews and worldviews shaped institutions in some simple way then stasis would be the outcome. The trick is to understand how the process of institutional construction and sustenance generates tensions and contradictions which force change and how exogenous shocks may set off or redirect such processes. Lacking systematic

theoretical leverage on this problem, we rely on the two case studies that follow our initial conceptual excursus to give us some purchase.

Following the analysis of the case studies the paper returns in the concluding section to more general issues, both substantively and theoretically (section 5). On the substantive level, we ask what are the implications of the institutional trajectories that we have described for the functioning of the contemporary political economy. In particular, we explore their implications for the possibility of shifting current patterns of global growth on to a more equitable trajectory. On a theoretical level, we ask what these cases suggest in terms of general hypotheses as to what role institutions play and how they change. Finally, we close with some thoughts on the prospects for building a real institutionalist alternative to the current canon.

2. Conceptualizing the Causes and Consequences of Institutional Change

In this section, we set out our general conceptual framework for understanding the nature and the changes of institutions, which will inform our discussions in the following sections.

2.1. Three Views on Institutions

Mainstream economists do not usually think about institutions, but as far as they do, they see them as “constraints” on free market that create inefficient “rigidities”. The limits of this view are increasingly well-known, so we do not need to dwell on them here.

What is surprising is that such rhetoric of “institutions as constraints” is also carried by many institutional economists of mainstream leaning – or the so-called New Institutional Economists (Douglass North, Oliver Williamson, etc.). For example, according to North, “institutions consist of a set of *constraints* on behaviour in the form of rules and regulations; a set of procedures to detect deviations forms the rules and regulations; and, finally, a set of moral, ethical behavioural norms which define the contours that *constrain* the way in which the rules and regulations are specified and enforcement is carried out” (North, 1984, p. 8; italics added).

Of course, the NIE people would not be seen as breaking new grounds, if they regarded these “constraints” as simply creating inefficiencies, as the mainstream economic theory does. Many of them are in fact saying that institutions are there only because they improve efficiency, even to the extent of committing functionalist errors (see section 2.2.1). However, by employing the rhetoric of “constraints”, they still maintain the myth that the unconstrained market is the natural order, while institutions are man-made substitutes which should be (and will be) deployed only when that natural order breaks down.

If we want to move away from the view of the institution as something “unnatural”, we need to employ a different rhetoric, namely, seeing institutions as “enabling” devices rather than constraints. For example, it is only because traffic rules make individuals drive in a certain way that we can drive faster. For another example, we can engage in innovation more aggressively because there are intellectual property rights, which remove the fear that other agents will copy our ideas and usurp the gains that should accrue to us. And so on.

This is, of course, *not* to say that institutions do not impose constraints. Just about all “enabling” institutions involve constraints on some types of behaviour by some people. In many cases that involve a collective action problem, these constraints are “general” constraints that apply to everyone. In these cases, we are putting constraints on everyone’s behaviour so that we can collectively do more things. However, in other cases, enabling of some people means constraining others. For example, affirmative action enables certain disadvantaged groups to have greater freedom to choose occupation by constraining the behaviours of the potential employers in choosing their employees.

So shifting our rhetoric to the “enabling” dimension of institutions from the “constraining” dimension does not mean that we are negating the constraining nature of institutions. However, this is an important shift of perspective because we are then implicitly negating the view implicit in the “institutions as constraints” rhetoric that the unconstrained market (if such thing is possible at all) is the natural order (or what we call the “market primacy assumption” – see Chang, 1997, and 2000a).

However, there is a third view of institutions, which gets relatively little attention among economists, but in our view is critical.² This view sees institutions not just as enabling or constraining, but also as “constitutive”. This is because all institutions have a symbolic dimension and therefore inculcate certain values, or worldview, into the people who live under them. In other words, as we continue to behave under a certain set of institutions, we begin to internalize the values embodied in those institutions, and as a result our selves begin to change.³

Of course, this would not happen if human beings take a totally instrumental attitude towards institutions and rule-abiding, because then they will only keep the rules which are beneficial to us (taking into account, of course, the costs of keeping such rules in terms of lost opportunities, etc.). In this situation, if they ever make “value-laden” statements and actions, these will be only cynical and manipulative “marketing ploys” to advance their own interests. And indeed this is what is often implicitly assumed in the mainstream economic literature on institutions, where institutions are seen as products of rational choice by selfish individuals interested only in material gains. However, if we follow this line of reasoning, we cannot really explain why institutions exist at all.

To begin with, if everyone is a selfish rational individual with an instrumental attitude towards rule-keeping, then there will be inordinate amount of cheating and shirking around. If this is the case, no institution will be sustainable, because then the cost of monitoring the possible deviations and punishing them will be truly prohibitive. Moreover, in this situation, it is questionable whether any monitoring and sanctioning mechanism against rule-breaking can exist

² This view is most explicitly adopted by non-economists such as Granovetter (1985), Douglas (1986), March & Olsen (1989), Friedland & Alford (1991), Fligstein (1996), Finnemore (1996), and Barnett & Finnemore (1999). Economists who adopt this view, although using somewhat different languages, include Simon (1983), Hodgson (1988), and Bowles & Gintis (2000).

³ Of course, the “original” selves are themselves products of the existing institutional structure.

at all. This is because the monitoring/sanctioning mechanism itself is a public good (in the sense that people who have not devoted their efforts in monitoring and sanctioning deviants can also benefit from the improved behavioural standards as a result of such activities), and therefore no selfish individual will find it “rational” to spend his/her time and resources in maintaining the monitoring and punishment mechanism.⁴

Therefore, unless we accept that people believe (in varying degrees across individuals, needless to say) in the values which lie behind the institutions concerned and that they usually act in accordance with these values without constant monitoring, we cannot explain the existence of any institution.

These three views of institutions that we outlined above are, of course, not necessarily mutually exclusive. There is no inconsistency in saying that institutions are constraining, enabling, and constitutive all at the same time. And indeed unless we recognize all three aspects, our analysis of institutions will not be complete, as we try to show below.

2.2. Formation and Change of Institutions

Different authors writing on institutions take different approaches to the origins of and the changes in institutions, although a single person is naturally able to hold a number of different views without creating too many contradictions. We can broadly divide these approaches into two groups, namely, the efficiency-driven approach and the interest-based

⁴ In the words of Mary Douglas (1986), “[c]ollective sanctions are a form of collective action” (p. 27).

approach, with sub-approaches in each group, each with very different theoretical and policy implications.

2.2.1. The Efficiency-driven Approaches

2.2.1.1. The Simplistic Version – Optimality of Institutions

In the most simplistic version of the efficiency-driven view on institutional change, institutions are seen as emerging when the market mechanism fails to allow all the potential efficiency-enhancing transactions to be realized. In this version, the rational wealth-maximizing agents will not fail to seize upon the opportunities for efficiency enhancement, if setting up a new institution – say, a firm – is going to increase the gains from trade. In this Panglossian vision, therefore, all institutions that exist are efficient (examples will include authors like early Douglass North, Harold Demsetz, Armen Alchian, and the “property rights school” of Frubotn & Pejovich and Yoram Barzel). And if any institution that is ostensibly capable of enhancing efficiency in a given context does not exist, it is only because the transaction costs involved in constructing such institution are larger than the benefits that the institution bring about, in which case they are not really worth having.

It is clear that in this simple form, the view is untenable for both theoretical and empirical reasons. Theoretically, when bounded rationality (the term is due to Herbert Simon; Simon, 1983, is the best summary of this view) is one of the important reasons that we have, it stretches our credulity to argue that individuals who are not even capable of doing the standard optimization exercise involving only resource costs is capable of engaging in a “meta-optimization” exercise involving both resource costs and decision-making costs (or transaction

costs). Empirically, we simply observe too many examples of inefficient institutions, whose persistence does not really serve anyone's interest.

As a result, some of those who hold this vision acknowledge that, at a given point of time, there may exist inefficient institutions, but they argue that these institutions will be "selected against" in an "evolutionary" process in the long run (Alchian, 1950, is the classic example).⁵ However, even this more sophisticated evolutionary version has an obvious limit. The problem is that institutions are, by definition, not easily malleable (a perfectly malleable institution will be as good as no institution), and therefore that typically "the rate of change in the environment will exceed the rate of adjustment to it" (March & Olsen, 1989, p. 168). If this is the case, there cannot be any presumption that institutional evolution is moving in an optimal direction.

2.2.1.2. The More Sophisticated Version – Path Dependency Recognized

In a more sophisticated version of the efficiency-driven approach to institutions, it is admitted that not all institutional changes are of efficiency-enhancing kind and therefore that many of them will not be optimal even in the longer run (so, the simplistic "evolutionary" argument is rejected). The reason for this, according to those who take this approach (Brian Arthur, Paul David, Joel Mokyr, and others who work mainly on technology issues), is that there is path dependency in the evolution of institutions.

In their view, certain institutions (say, technological regimes) may be chosen over others, not because of their inherent efficiency but because of certain irreversible "events" in history. The best example in this regard is probably that of "network externality", which gives the first-

movers a selection advantage through the frequency-dependent definition of “evolutionary fitness” (e.g., the competition between different computer operating systems). For another example, if certain irreversible investments have been made in certain physical, intellectual, and relational “specific assets” (the concept is due to Williamson, 1985) assuming the presence of particular institutions, the relative efficiency of the existing institutions vis-à-vis alternative institutions will have been enhanced, as the holders of these assets will have interests in preserving the existing institutions (see Chang & Rowthorn, 1995, for an elaboration of this point).

This perspective has allowed us to better understand the process of institutional changes. However, at least in its present form, it remains very “economistic” in that the process of institutional change is driven basically by technological factors, and in that individuals are seen as operating on the basis of purely “economic”, rational calculations (even though it is admitted that rational calculations by individuals do not necessarily amount to a socially optimal outcome). The essential problem with this approach is that there is no room for human agency in the sense that what people believe (instead of what they “should” believe, given the technological imperatives) does not make a difference to the process of institutional change.⁶

2.2.1.3. The Most Sophisticated Version – The Role of “Culture” Recognised

The most sophisticated version of efficiency-driven approach extends the argument to the “cultural” dimension in the sense that the worldview possessed by human agents matter. The proponents of this view start from the assumption that human agents have bounded rationality (a

⁵ For a comprehensive discussion of the evolutionary approaches in economics, see Hodgson (1993).

concept to which Williamson and other more “purist” efficiency-driven theorists give lip service to but do not really adopt in practice) and argue that institutions make the complex world more intelligible to them by restricting their behavioural options and also by confining their scarce attention to a truncated set of possibilities.

Bounded rationality, according to this vision, makes it inevitable that we operate with a mental “model” of the world (or value system, ideology, worldview, or whatever we may choose to call it) that may not necessarily be a good, not to speak of being perfect, model of the real world. Given the adherence to a certain worldview by the actors, they may prefer a certain institution because it happens to fit their worldview (or “moral values”), even when it is not necessarily efficiency-enhancing from an “objective” point of view. In this way, the optimality conclusion is negated, albeit not in the economistic (or technology-driven) way that the second version of the efficiency-driven approach disposes of it.

Some of those who espouse the “culturalist” version of the efficiency-driven approach go one step further and argue that what worldview people hold is not independent of the institutions under which that they have been operating – or that there is “endogenous preference formation” (see for example, Hodgson, 1988, and Bowles and Gintis, 2000). The argument is that institutions embody certain “moral values”, and by operating under certain institutions for a period of time, it is likely that people begin to internalize those values (this is what we called the “constitutive” role of institutions).

Note that even with these “subjective” elements (such as moral values and worldviews) thrown in, the approach is ultimately driven by efficiency – only that the definition of efficiency now takes on a subjective dimension. And in this sense, we can still call this a version of the

⁶ Chang & Rowthorn (1995) attempts to combine this approach with what we call the “culture-

efficiency-driven approach, however different it may appear from the crude efficiency-driven institutionalist theory that we discussed earlier (see section 2.2.1.1) and however more sophisticated its outlook may be.

2.2.2. The Interest-based Approaches

2.2.2.1. The Simplistic Approach – Neoclassical Political Economy

The most simplistic of the interest-based approaches to the origins of institutions and institutional change is the Neoclassical Political Economy (as pioneered by Anthony Downs, James Buchanan, Gordon Tullock, George Stigler, Ann Krueger, Jagdish Bhagwati, Mancur Olson, and Douglass North). The same view is found in some cruder version of Marxian political economy (those who see the state as the executive committee of the bourgeoisie) (for a critical review of this literature from an institutionalist perspective, see Chang, 1994, chs. 1-2).

In this view, institutions are but instruments of advancing sectional interests by interest groups that are politically organized enough to initiate changes in institutions in a way that suits their interests – the so-called rent-seeking theory of Buchanan, Tullock, and Krueger is a good example (Buchanan et al. (eds.), 1980, is the representative work). Advancement of “global” interests, as far as they happen, is treated as unintended consequences.

Another problem with this approach is the implicit belief that interests are *not* socially-structured but exogenously given at the individual level. So interest groups have no internal constraints in their agenda setting and decision-making, which is patently not the case in reality (see March & Olsen, 1989).

based structured-interest approach”.

Also, the proponents of this view believe that institutions can be quickly changed, as far as there is the political power base to support the change. In this respect, this view is similar to the most simplistic version of the efficiency-driven view of institutions, because in both views, institutions are seen as infinitely malleable, as far as there is a good reason to change them (be it some global “efficiency” or some dominant “interest”). In this respect, many of the criticisms that we lodged against the simplistic efficiency-driven view apply here too.

2.2.2.2. The more sophisticated version – Structured-Interest-Based Approach

The more sophisticated version of the interest-based view of institutions agrees with the first view that institutions change *not* on the basis of some global efficiency *but* according to sectional interests and are therefore fundamentally “biased” towards certain groups. However, in this version, interests are *not* exogenously given, but “structured” by existing political and social institutions. Hence the name we give to it, namely, “structure-interest-based” vision.

In his famous discussion of the emergence of the capitalist factory system, “What Do Bosses Do?”, Stephen Marglin (1974) argued that existing (capitalist) property relations determined the way in which capitalist style firm organization was chosen over worker-managed firms, when the latter did have efficiency advantages (but see Williamson, 1985, for a critique of this argument from an “efficiency” point of view). Robert Brenner, in his famous discussion on the revival of feudalism in Eastern Europe, argued that the same exogenous shock of rising grain prices led to the demise of feudalism in Western Europe whereas it led to its strengthening in Eastern Europe because of the differences in their existing institutions (**references to be supplied**). Sam Bowles and Herb Gintis, in a series of recent articles, have emphasized that the

“contested” nature of exchange relationships in credit and labour markets make the market outcomes dependent on the existing power relationships (**references to be supplied**).

The structured-interest-based view differs from the Neoclassical Political Economy view in that it does not see institutions as easily malleable as the latter view does. This is because the proponents of this view see interests as structured by existing institutions, which means that changing the balance of power between existing interests (which is necessary for an institutional change) is not going to be instantaneous or straightforward but will have to involve changes in deeper institutional structure.

2.2.2.3. The Most Sophisticated View – Culture-Based Structured-Interest Approach

The most sophisticated version of the interest-based view on institutional change may be called “culture-based structured-interest” view. Those who hold this view argue that there cannot be such thing as “objective interests, which can be understood independently of the actors’ understandings” (Friedland & Alford, 1991, p. 244). Therefore, while they agree with others who hold an interest-based approach that institutional changes are driven by interests, they argue that institutional changes are “simultaneously material and symbolic transformations of the world”, which involve “not only shifts in the structure of power and interests, but in the definition of power and interests” (Friedland & Alford, 1991, p. 246).

While the proponents of this view agree with those who believe in the most sophisticated version of efficiency-driven view that people internalize the values embodied in institutions, they also point out that “rules and symbols ... sometimes ... are resources manipulated by individuals, groups, and organizations” (Friedland & Alford, 1991, p. 254).

For example, Friedland & Alford (1991) argue that the success of American capitalists in the early 20th century in persuading the society to accept the (fictitious) legal status of a juridical person for a corporation was crucial in allowing them to institute limited liability, which then enabled large-scale mobilization of capital through the stock market (p. 257). They also argue that the success by the workers in advanced capitalist economies in making the wider society to accept the extension of the notion of citizenship rights of due process and even participation to employment relations in private firms allowed them to institute grievance procedures (p. 257).

Thus seen, the proponents of this view see the project of institutional changes not simply as a “material project” but also as a “cultural project” in the sense that changes in institutions require (or at least are helped by) changes in the “worldview” of the agents involved. And once we allow the possibility of “cultural manipulation”, the role of human agency becomes a lot more important than in any other version of the theories of institutional change that we have talked about, as it is necessarily the human agents who actively interpret the world (albeit under the influences of existing institutions) and develop discourses that justify the particular worldview that they hold. Indeed, we should not forget, to paraphrase Marx, that it is human beings who make history, although they may not make in contexts of their own choosing.

3. The (Rise and) Decline of the Developmental State – the Korean Case

3.1. Introduction – Why the Developmental State?

In the post World War II period, a small set of countries in East Asia stands almost alone in having been able to actually achieve significant shifts their position in the world hierarchy of nations (in a positive direction). The enormity of economic and social transformation that these countries have experienced has been frequently mentioned, but it may help to drive this point home again with a couple of simple numerical illustrations.

Very roughly speaking, during the postwar period, per capita income growth rates in Japan, Korea, and Taiwan have been in the region of 5-6% per annum. These rates of growth may not seem to be very much, but it may worth remembering that per capita income growth rate in the major now-advanced capitalist countries during the Industrial *Revolution* (1820-1870) was about 1% per annum.⁷ Especially if sustained over a long period time, they can produce some most remarkable results. For example, if a country's per capita income grows at 6% for, say, 40 years, it means that its per capita income will grow by something like 9 times by the end of the period. In contrast, if a country's per capita income is growing at around 2%, as that of India or Pakistan has done during the postwar period, its per capita income will barely double during the 40 year period.⁸

⁷ This figure is the arithmetic average of per capita output growth rate figures for the US, Canada, Japan, the UK, France, West Germany, and Italy. The same figure for the subsequent periods were 1.4% in 1870-1913 and 1.2% in 1913-1950. The figure was “only” 3.8% even during the “Golden Age of Capitalism” (roughly 1945-73). See table 8.1 (p. 117) in Armstrong et al. (1991). The weighted average of per capita income growth rates for all OECD countries was 3% during the “Golden Age” (see Maddison, 1987)

⁸ To put it in another way, if a country's per capita income is growing at around 1% per year, as that of Argentina has done during the postwar period, it means that it takes 70 years to double its per capita income - instead of the 12-15 years that took Korea or Taiwan to do it. Or if a country's per capita income is growing at 0.3%, as that of Bangladesh was doing until recently, it will take 230 years to double the figure.

And there is a consensus that in the process of this unprecedented economic and social transformation the developmental state has played a critical role in one way or another (the concept originates from Johnson, 1982; see Amsden, 1989, Wade, 1990, Chang, 1993, Evans, 1995, Woo-Cumings (eds.), 1999, for subsequent elaborations; World Bank, 1993 and 1997 also somewhat grudgingly acknowledge this).

With the recent economic crises in the region, of course, the developmental state has been suddenly cast by many people as the cause of economic troubles in the East Asian economies, but this perspective has a number of problems. First of all, whether or not the recent crisis is due to the “failure” of the developmental state, the economic and social progress achieved by the developmental states in the region cannot be erased from history. Secondly, as we shall point out later and as many commentators point out, the recent crises in the region are the result of the decline, rather than the persistence, of developmental state (e.g., see Wade, 1998, Singh, 1999, Chang, 2000b). Thirdly, as we shall argue later, the developmental state is a threatened institution not primarily because it was economically ineffectual, or even because its potential economic efficacy has been undercut by globalisation. The problems of the developmental state lie first of all in domestic politics and derive in part from the domestic political consequences of economic success. With these points in mind, let us look at the rise and decline of the Korean developmental state.

Even among the developmental states of East Asia, the Korean one stands out as a particularly striking case. When it was in its ascendancy, it was the most dramatic, if not necessarily most effective, specimen of this species, while its subsequent decline was the earliest and the most comprehensive.

The transformative projects envisaged and implemented by the developmental states of Japan and Taiwan during the postwar period were not as comprehensive and forceful as that of Korea. In the case of Japan, its longer history of industrialization not only required less state involvement in the transformative project, but also necessitated a more consensus-oriented approach in the state's dealing with the private sector. In the case of Taiwan, Kuomintang's position as an "occupation authority", as well its allegiance to the semi-socialist ideals of Sun Yat-sen's Three People's Principle, implied that the transformative project could not be as ambitious or as well-integrated with the activities of the private sector as that of Korea.⁹

Equally dramatic, however, was the decline of Korea's developmental state, although, as we point out later, its institutional and the ideological legacies still remain considerable and may even be revived in the future, depending on the economic and the political evolution of the country. While the other East Asian developmental states also went through changes that saw the decline in their dominance and legitimacy over time, these do not rival what has happened in Korea. The Japanese developmental state has been under considerable criticisms since the late 1980s and particularly recently with the continuing recession, but its loss of political legitimacy has not reached anywhere near the Korean level.¹⁰ In the case of Taiwan, the dominance of the developmental state continues, albeit in a somewhat muted form, as exemplified by its near-imperviousness to the worldwide trends of privatization and capital market opening.

⁹ What made the Korean case more dramatic was the charismatic figure of General Park Chung Hee. His dominance of the nation's politics was unrivalled even by that of longer-ruling Chiang Kai Shek of Taiwan, whose power base was much less "personalized" than that of Park, because of the highly-organized nature of Kuomintang party machinery.

¹⁰ All this was despite the fact that, as most well-informed observers agree, the current recession in Japan has far less to do with the shortcomings of its transformative project than with its macroeconomic mismanagement.

How can we then explain that once the mightiest, if not necessarily the most shrewd and agile, developmental state could fall so spectacularly? And what are the lessons that we can draw from this experience for the theories of institutional change? In order to answer these questions, we need to go back in time and briefly discuss the rise of the developmental state in Korea in the first place.

3.2. The Rise of the Korean Developmental State

The Korean developmental state emerged from a most unpromising environment. Although the legacies of the proto-developmental state that had existed under Japanese colonial rule (e.g., Kohli, 1994) were important, we should not under-estimate the enormity of the destruction of colonial institutional fabric between 1945 (the end of Japanese rule) and 1961 (when General Park Chung Hee came to power through a coup).

The end of Japanese colonial rule in 1945 unleashed a political turmoil, which wreaked havoc on the institutional structure left behind by the Japanese. The occupation of what eventually became South Korea by the Americans until 1948 also increased the institutional turmoil, as many American-style institutions were grafted onto the institutional structure left behind by the Japanese. It is needless to say that the Korean War (1950-53) exacerbated the social and institutional dislocation even further.

The regime of Syng Mahn Rhee that ruled South Korea from its birth in 1948 until 1960 was fundamentally anti-developmental. Its only stab at developmentalism worth talking about was the establishment of the Ministry of Reconstruction in 1955, although it mainly acted as a liaison agency with aid donors and did not even formulate a development plan until 1959, which

was never implemented anyway. The bureaucracy was nominally organized along a meritocratic line, but the practice was such that between 1949 and 1961, only 336 passed the High Civil Service Examination, compared to the 8,263 who got government jobs through “special appointments” (Cheng et al., 1998, p. 105). The quality of the bureaucracy was such that, until the late 1960s, several years after the civil service reform by the new military government was started, Korean bureaucrats were being sent to countries like Pakistan and the Philippines for extra training.

Things, as it is well known, began to change after the coup by General Park Chung Hee in 1961. It should be noted that, as some authors emphasize (e.g, Chibber, 1999), the Park regime did not come to the scene with a clear blueprint for a new developmental state and was engaged in a series of institutional experimentation in its early days. However, it had a fundamentally developmentalist outlook and implemented some critical institutional changes from its early days that laid the foundation for a full-fledged developmental state that we saw in action later. The more important of these changes included: establishment of the super-ministry, Economic Planning Board, with both planning and budgetary authorities, and the start of five-year plans; nationalization of the banks (many of which had in fact just been privatized by the Rhee regime in the late 1950s with prodding from the American aid officials); civil service reform; establishment and/or encouragement of various business sector “peak organizations”; establishment of public and semi-public agencies to help business, such as the state trading agency, KOTRA.

What is often ignored is that these institutional changes also resulted in a critical “ideological” or “worldview” change. The institutional changes made by the Park regime in the

early days embodied a nationalistic, pro-industry (vs. pro-finance), pro-producer (vs. pro-consumer) outlook, which emphasized capital accumulation, innovation, and structural transformation – namely the ideas associated with developmentalism. This outlook contrasts with the Anglo-American market liberalism with its emphasis on consumer welfare, price competition, and allocative efficiency, which had been emulated in a poor form by the Rhee regime.

3.3. The Decline of the Developmental State

In a sense, the challenge to the Korean developmental state had been present all the time – in the forms of the conservative, pro-democratic challenge of Yoon Bo Sun for presidency in the 1960s and of the challenge of pro-democracy, centre-left opposition forces led by Kim Dae Jung (the current president), and to a lesser extent by Kim Young Sam (president, 1993-8), since the 1970s. However, the biggest and the ultimate challenge came from the Neo-Liberal forces that began to crystallize from the late 1970s in an alliance between the “liberal” faction in the bureaucracy, the majority of the intellectual community, and the increasingly powerful business conglomerates (the *chaebols*).

The Neo-Liberal forces made a critical breakthrough after the assassination of General Park in 1979 by his intelligence service chief. Initially, the political vacuum left by the death of Park seemed to open a space for the pro-democracy centre-left forces led by the two Kims. However, they were soon crushed by the military coup and the Kwangju massacre staged by the “new military”, between 1979 and 1980, led by General Chun Doo Hwan.

General Chun was by no means a Neo-Liberal himself, but he allied himself with Neo-Liberal bureaucrats and implemented a series of institutional changes that signaled the start of a Neo-Liberal offensive against the developmental state. He adopted the anti-inflationary rhetoric of Neo-Liberalism in a bid to deal with the inflationary pressures created by the Second Oil Shock and the subsequent world recession exacerbated by the monetarist macroeconomic policies of major industrialized countries. He also privatized a number of banks while partially liberalizing the financial market in 1983. Also introduced was the Industrial Development Law in 1986, which, while clearly accepting the need for an activist industrial policy, shifted the country's industrial policy towards a more "functional" (as opposed to "selective") direction.

However, it will be a gross exaggeration to say that the changes made under Chun's rule made the subsequent demise of the developmental state inevitable. While its force was somewhat diminished, developmentalism still remained the overarching ideology of the regime, and proved formidably effective in certain areas, such as information technology industries (see Evans, 1995, for details). Many of the formal institutional changes in Neo-Liberal direction made under Chun, such as financial liberalization and the introduction of IDL, were limited in scope and had their effectiveness curtailed by the inertia stemming from the more-slowly-changing informal institutions such as bureaucratic convention and business practices (see Amsden & Euh, 1990, on financial liberalization and Chang, 1993, on the introduction of the IDL).

A more fundamental shift was set in motion, however, with the success of the mass pro-democracy protest in the summer of 1987 against Chun's attempt to hand the presidency over to his chosen successor and erstwhile collaborator, General Roh Tae Woo, through the rigged electoral college system (through which he himself was formally elected president). The success

of the protest led the military to capitulate to the public demand for a truly democratic presidential electoral system, although Roh managed to win the subsequent election held in late 1987.

The political discrediting of the military rule led to a rapid weakening of the legitimacy of developmentalism, because it was seen, in our view mistakenly, as the former's Siamese twin. What was decisive in this process was the increasing conversion of the intellectual elite, especially the bureaucratic elite, to Neo-Liberalism. The increasing number of elite bureaucrats and academics who got advanced degrees from the US meant that there were more and more people inside and outside the government who saw developmentalism as a "backward" ideology.

¹¹ It needs to be added that in this ideological battle, the Neo-Liberals were critically helped by the ideological dominance of Anglo-American academia and media at the world level. In this way, Neo-Liberalism established itself as the dominant ideology among Korean elite circles, including the elite bureaucracy, somewhere between the late 1980s and the early 1990s.

Many of the bureaucrats, however, still had instinctive attachment to developmentalism, as can be seen in the intellectual confusion found in policy documents of the time, where Neo-Liberal pronouncements on overall policy direction uneasily sat together with developmentalist policies in particular areas. However, there were many other bureaucrats whose conversion to

¹¹ Between the late 1980s and the mid-1990s, the height of Neo-Liberal ascendancy in US academia, Koreans accounted for around 15% of all economics Ph.D.'s produced by US universities (about 100 out of 700). Although some of these were Korean-Americans (exact proportion is unknown), it is unlikely that they accounted for more than a small fraction. This is an astonishing statistic, given that Korea accounts for less than 1% of world's population (40-45 million out of 5-6 billion) (**exact information to be supplied**). An overwhelming proportion of these economists subsequently returned to Korea, thus steering university economics education increasingly in a Neo-Liberal direction. In addition, many elite bureaucrats, who were increasingly being educated along Neo-Liberal line in Korean universities to begin with, were sent to the US for two-year advanced studies. Some of them even stayed longer to get a Ph.D.. Most, although not all, of them eventually returned to their old jobs in the Korean government.

Neo-Liberalism was wholehearted and sometimes even dogmatic. For example, by the early 1990s, one frequently encountered bureaucrats from the Economic Planning Board calling for a radical retreat of the state and especially for the abolishment of their own ministry on the ground that planning is not feasible anymore due to the increasing complexity of the economy, if it ever was desirable.

Moreover, since the late 1980s the *chaebols* increasingly came to the view that the Korean state has become more of a liability than an asset in their competitive struggle in the world market. A series of spectacular successes that they had in those export markets which were previously thought to be the exclusive domains of the most advanced economies, such as memory chips and automobiles, convinced them that they could now stand on their own. Their confidence was corroborated by the approval that they started gaining in international capital markets. By the mid-1990s, the leading *chaebols* were considered creditworthy enough to float bonds in advanced country capital markets. Their rapidly-growing foreign ventures, although still not on a scale that could lead to a significant change in their relationship with the state, also started to weaken their identification with the nationalistic outlook of developmentalism.¹²

By the mid-1990s, the *chaebols* have become staggeringly aggressive in calling for the withdrawal of the state from economic management. The “owners” and the top managers of the leading *chaebols* made public pronouncements against state intervention at every conceivable opportunity. The *chaebols* also set up a small but extremely well-funded research institute called Korea Centre for Free Enterprise, which churned out numerous documents with strong Neo-Liberal flavour, while translating a whole array of classical works in Neo-Liberal tradition (e.g.,

¹² By the mid-1990s Korea was one of the largest foreign investors in a number of developing and transition economies, not just in Asia but also in Europe (e.g., Indonesia, Vietnam, Poland,

Hayek, Buchanan, etc.) and inviting well-known American Neo-Liberal thinkers to give high-profile talks in Korea.

The height of this offensive was the ultra-Neo-Liberal policy report prepared by the Federation of Korean Industries (FKI), the club of the *chaebols*, in the spring of 1997. This report called for a radical retrenchment of the state and, among other things, called for the abolition of all government ministries except Defense and Foreign Affairs and the consequent reduction of government bureaucracy by 90%. Although the official withdrawal of this document at the public uproar following an unfortunate pre-publication leak showed that the Korean public was not yet ready for this kind of ultra-Neo-Liberalism, the mere fact that such report could be prepared as a public document by the FKI shows how aggressive the *chaebols* had become in their offensive against the developmental state.

It was not simply the *haute bourgeoisie* who wanted to dismantle the developmental state. The professional classes also started to revolt against the nationalistic and anti-consumer biases of developmentalism. These people had been previously happy to comply with the “buy Korean” policy and restriction on luxury consumption, but they now wanted to exercise their newly-acquired purchasing power in the purchase of domestic and foreign luxury consumption goods without having to feel guilty about being “unpatriotic” and “anti-social”. As a result, they now wanted further trade liberalisation and the lifting of restrictions on luxury consumption goods and luxury housing. They were also beginning to feel frustrated by the “protective” regulations concerning agriculture, urban planning, and small-scale retailing, which put restraints on their ability to engage in consumerism – a feeling that usually found its most vivid expression

Uzbekistan). It was also one of the largest investors in the UK as far as the electronics industry is concerned.

in their fascination with the “quality of life” in the US such as cheap food, spacious housing, and large shopping malls.

Further push towards Neo-Liberalism was provided by the US and other advanced countries. From the late 1980s, they started stepping up their demands on what they saw as a now-developed country to become more “responsible” by abandoning all those “unfair” protections of their industrial, and especially financial, enterprises and giving them better access to what was an increasingly attractive market. The decision made in 1993 by the Kim Young Sam government to join the OECD (which Korea joined in 1996) made it even more necessary to open up various markets as a condition for the membership.

The resulting changes that led to the dismantling of the Korean developmental state and, in our view, subsequently to the current crisis, are probably too well known to document at any length (see Chang, 1998, Chang et al., 1998, and Chang & Yoo, 1999, for further details). Industrial policy, the hallmark of the developmental state, started to be dismantled, initially tentatively, from the late 1980s, and was gone from the scene by the mid-1990. Financial liberalization, including capital account liberalization, gained momentum since 1991, but accelerated since 1993, when Korea signed a bilateral agreement with the US for financial market. Most symbolically, the 5-year plan was terminated in 1993 and the Economic Planning Board was abolished (as some of its own members have wished for some time) and merged with the Ministry of Finance to form the Ministry of Economy and Finance in 1994. Although certain residues of developmentalism could still be found in places (e.g., supports for R&D in certain high-technology industries), the dismantling of the developmental state was effectively finished by the middle of Kim Young Sam’s presidency (say, 1995).

The recent financial crisis, as well known, contributed to a further decline of the developmental state. At the ideological level, the discrediting of the developmental state model has become even stronger. Neo-Liberal forces inside and outside the country have managed to blame the current crisis on the developmental state, despite the fact that it was already effectively, if not completely, dismantled before the crisis – various models identifying on industrial policy, cronyism, and the so-called “logic of too big to fail” as the main cause of the crisis are examples of such efforts (see Chang, 2000b, for some detailed criticisms). And as a result, subsequently many additional institutional changes have been made by the current Kim Dae Jung government, sometimes willingly and sometimes under IMF pressure, that further destroyed the foundations of the developmental state.

The additional liberalization of financial markets, of international trade, and of foreign direct investments that were implemented in the early days of the crisis are well known by now. Less well-known is the re-writing of the central bank constitution to give it more independence and make it single-mindedly focus on inflation control, which goes against the pro-industry (and anti-finance) outlook of developmentalism (for further details, see Chang & Yoo, 1999). Even less known, however, are the changes in the organization of the government.

After the crisis, the head of the Ministry of Economy and Finance (MOFE) was demoted from the position of a deputy prime minister to a simple minister. The Ministry’s control of government budget, which in the days of the EPB (and of the old MOFE) gave it such a clout, was transferred to a new small ministry, the Ministry for Planning and Budgeting (set up in May 1999) in charge of budget, inter-ministrial coordination in budgetary matters, and “government reform” (although how much of the last is real substantive is questionable). The Ministry of

International Trade, Industry, and Energy (MOTIE) saw its trade function transferred to the Foreign Ministry (which consequently became the Ministry of Foreign Affairs and International Trade) and as a result becoming the Ministry of Commerce, Industry, and Energy (MOCIE).

These changes in government organization symbolize a fundamental shift in the vision of the role of the state in the economy. The further fragmentation of the functions that used to be performed by the EPB between the MOFE and the MPB (and the demotion of the MOFE minister) implies that whatever little remains of the government's planning function is not considered as a business that requires concerted efforts and serious inter-ministrial coordination anymore. Re-writing of the central bank constitution has resulted in an end to the inherent pro-industry bias in the institutions of macroeconomic management. Transfer of trade function to the Foreign Ministry means that trade policy is now seen as a part of diplomacy and not an integral part of industrial policy.

Another important post-crisis development to be noted is the weakening of the elite bureaucracy itself.¹³ As many people attributed the recent crisis to the *dirigiste* model of development, the elite bureaucracy as its protagonist naturally came under severe criticism. The criticism did not simply involve criticisms of particular policies. Now the very legitimacy of the institution of bureaucracy itself was, with the help of the Neo-Liberal "government failure" rhetoric, being undermined. At the same time, the Kim Dae Jung government has been keen to weaken the elite bureaucracy, which it sees as representing the corrupt and inefficient *ancien regime*, and imbue more "entrepreneurial" and "service-oriented" ethos into the bureaucracy by vastly expanding, and indeed setting up a quota for, "special appointments" – in other words, it

¹³ On the importance of Weberian elite bureaucracy in economic development, see Evans & Rauch (1999) and Rauch & Evans (2000).

has started the process of destroying the Weberian bureaucracy that was so critical in its development and moving to a more “American” model of bureaucracy.

All these have led to an unprecedented degree of de-moralization of the elite bureaucracy, and, when combined with an aggressive head-hunting policy by the *chaebols*, to an unprecedented degree of personnel hemorrhaging from the elite bureaucracy. For example, since the crisis, dozens of high-flying young bureaucrats in their mid-30s to the mid-40s in the elite ministries, especially the Ministry of Finance and Economy, have moved to *chaebol* firms – something that these people would have never done before the crisis (if the elite bureaucrats were moving to the private sector, it would have been after they have exhausted their career possibility within the government, say, in their 50s).

At this point, it should be noted that, despite these “*gestalt* shifts” and formal institutional changes that followed the crisis, the imperatives of crisis management have paradoxically re-activated some of the developmentalist policy devices that were laid to rest during the mid-1990s. For example, the Kim Dae Jung government implemented various programmes of state-mediated industrial and corporate restructuring, a staple of the Korean developmental state – such as the so-called “Big Deal” programme of “voluntary” business swaps and mergers among the leading *chaebols*, on the one hand, and the state-led restructuring of Daewoo and other bankrupt *chaebols*, on the other hand. For another example, the MOCIE recently introduced a programme of promoting “star firms” in parts and materials industries (which have been identified by many as a fundamental weaknesses of the country’s economy) and stepped up export promotion measures. We cannot yet tell how long-lasting or effective these “revivals” of

developmentalist policies will be, but they show how some institutional patterns can recur even in times of a most radical institutional overhaul.

More interestingly, there also has been some unexpected revival in the fortunes of developmentalism at the ideological level. Although the conversion of the elite to Neo-Liberalism seems almost complete (or at least strong enough to be able to silence most of the potential critics from within), there is a strong undercurrent of nostalgia for Park Chung Hee at the grassroots level. This admittedly started before the current crisis, as can be seen from the strong showing in the 1997 election by a Park Chung Hee-lookalike politician with a vague ideological nod to him, Yi In Je, who broke away from the then ruling party and ran as a third party candidate. However, Park's popularity seems to be persisting even after the crisis, despite the fact that many see his developmentalism as the root cause of the current crisis. In various opinion polls asking people to name individuals who they think are the most influential in the running of today's Korea (Koreans seem to love this kind of polls), Park, 20 years after his death, consistently ranks in the top 10, sometimes quite high.¹⁴ It is not totally inconceivable that in the context of continued slower growth and growing inequality, such ideological undercurrent may be channeled by a skillful politician into an organized challenge to Neo-Liberalism, although how effective this will be, if it ever materializes at all, is at this stage impossible to predict.

¹⁴ Park is, however, not the only dead person ranking in the poll. In these polls, Kim Goo, the legendary centre-left nationalist politician who was the most respected leader of the "Korean government in exile" in Shanghai during the Japanese colonial rule, despite being dead for 5 decades (he was assassinated in 1949), usually claims his place, although always ranking lower than Park does.

3.4. Theoretical Implications

The rise and decline of the Korean developmental state supplies us with some interesting insights into the process of institutional change. Our discussion on the rise and decline of the Korean developmental state, above all, suggests that institutional change is a highly complex process, involving multi-directional and often subtle interactions between “objective” economic forces, ideas, interests, and existing institutions themselves. This is at one level a very banal statement, but there are too many theories of institutional change which rely almost exclusively on one of these variables (especially economic forces and interests solely defined in terms of such forces) for us not to make this statement.

First of all, our discussion reveals problems with what we call the “simple version of efficiency-driven explanation of institutional change” that emphasizes “objective” economic factors in explaining institutional changes (see section 2.2.1.1). No doubt these factors are often very important in understanding broad historical trends, but they do not allow us to understand all the complexities of the process of institutional changes.

For example, many people argue that the demise of Korean developmental state was inevitable, because, with economic development, the economy has become too complex to centrally coordinate. Even if we accept the argument that economic development necessarily makes centralized coordination more difficult by making the task of coordination more complex, which in itself is a highly contentious proposition¹⁵, the argument still does not explain why such demise happened in Korea at the time when it happened. If it is the stage of development at

¹⁵ Economic development may increase the complexity of the task of coordination, but it also develops the society’s administrative and coordination capabilities both within and outside the

which a particular country is that determines the functionality of a given state form (e.g., developmental state), why did the Korean developmental state go into a decline when the country was at the stage of development similar to where Japan was in the 1960s or the 1970s, when the latter's developmental state was in its prime?

This example shows that, if we are to understand the exact timing and the manner of the demise of the Korean developmental state (and more generally the timing and the exact form of any institutional change), we also need to look at the ideological battles and the changes in interest group politics (and their interaction with each other) that that surrounded the process.

Secondly, our discussion shows that ideas play a much more important role than what is normally suggested in the discussions of institutional change. Social scientists, except those semi-theologians who naively believe in there being “right” ideas and “wrong” ideas, have been loathe to attribute significant role to ideas in the process of institutional change. They like to see ideas as an outgrowth of the material infrastructure of the society (Marxism) or mere vehicles for interest groups to advance their positions (Neoclassical Political Economy). However, the Korean example shows that ideas are much more than these.

For example, the fact that many government bureaucrats in Korea turned against state interventionism – so much so that by the early 1990s some EPB bureaucrats were calling for the abolition of their own ministry – flies directly in the face of what we call the “simple interest-centred view of institutional change”, such as the one found in Neoclassical Political Economy, which, a la Niskanen, predicts that bureaucrats have interests in expanding their bureaux. Unless we understand the influences of Neo-Liberal ideologies, which denies the legitimacy of state government. Therefore, it may, on the whole, make such exercise easier, rather than more

intervention in general and particularly of planning, on these bureaucrats, we will never be able to understand why they campaigned for the reduction of their own power and influence.

Thirdly, having emphasized the importance of ideas in the process of institutional change, we do not wish to give the impression that ideas should be treated as a uniquely independent force that things like interests and institutions are not.

For one example, while ideas are not simply “marketing ploys” of interest groups, it is difficult for an idea to be sustained in the long run without some appeal to important interest groups. The offensive by the *chaebols* and the “revolt” by the upper-middle classes, both of whom were great beneficiaries of the success of the developmental state, against Korean developmentalism in the 1990s that we discussed above are very good cases which illustrate this point.

For another example, while our discussion shows how powerfully ideas can shape the course of institutional change, it is wrong to envisage an one-way relationship between the two. As argued by the most sophisticated versions of both the efficiency-driven and the interest-driven explanations of institutional change (see sections 2.2.1.3 and 2.2.2.3 respectively), institutions affect the way in which people who operate under them perceive the world (what we call the “constitutive” role of institutions). And therefore it is not possible to see them as objects of manipulation by agents with exogenously-formed “preferences”, because the way in which such “preferences” are formed is affected by the nature of existing institutions. To take an example from the Korean case, we may say that the historical association between the

difficult (for a more detailed discussion on this issue, see Chang, 1999).

developmental state and military dictatorship made many people who may not have been otherwise inclined to do so object to developmentalism.

Fourthly, our discussion shows that we need to think more seriously about the importance of human choices in determining institutional changes – not the empty Neoclassical choices, which are more or less pre-determined by “objective” conditions, but genuine choices involving “free will”. Social scientists tend to downplay the role of the choices made by key individuals (or groups of individuals) and happy to leave it to historians, in the belief that this is beyond the domain of “science”, but this is hardly satisfactory.

For example, some people who put emphasis on path dependency in institutional changes (or follow the “sophisticated version of efficiency-driven explanation of institutional change”) argue that Park’s choice for a Japanese-style developmentalism was an “obvious” one, given the institutional legacies of Japanese colonialism (see, e.g., Kohli, 1994). However, when Park came to power, the American model would have been the *more* obvious choice. At the time, many formal institutions of Korea had been already put in their place by the American Occupation Authority, and the tendency towards the American model was further strengthened by what the Rhee regime did (e.g., establishment of a quasi-independent central bank, privatization of banks, American-style spoils system in the bureaucracy). Also, given the country’s near-total economic and political dependence on the US at the time, a Korean leader would have benefited the most by emulating the American model (regardless of the possibility of “success” of this approach, given local conditions). Given all these, it required certain amount of initiative to move away from this “easy” choice of embracing the American model.

For another example, the Kim Young Sam government did not have to go to the extent it actually did in dismantling the developmental state. The easier choice would have been to do what its predecessor, the Roh government, did – namely, to let it wither away slowly. In the above, we argued that there was no compelling “economic” need for Korea to dismantle its developmental state when it did. Moreover, although there were strong domestic and foreign interest group pressures for a weakening of the developmental state, there was no necessity to formally end the 5-year plan, which by the late 1980s already had lost many of its teeth anyway, or to join the OECD, which no interest group was actively asking for. In other words, the Kim government’s dismantling of the developmental state needs to be seen as containing an important element of active choice by its key policy-makers, rather than simply reflecting interest group pressures or “objective” economic conditions.

4. Institution-building at the Global Level: The WTO as an Illustrative Case

For anyone interested in an institutional approach to economic change, the contemporary period is a particularly intriguing one because it is a period of intensive institution building. We are in the midst of the formative stages of the creation of a system of global governance which is likely to become institutionalized and operative over the course of the next 50 to 100 years. Although a great deal of institutionalized governance is already in place at the global level, undertaken by a panoply of international organizations with a wide variety of mandates, the current attempts at global institution building aim to elevate the matter onto an unprecedented plane.

Periods of institution building, like this one, are opportune moments for new research and theorizing. In this case there is obviously much to be learned. Despite the extensive literature on international organizations, we know surprisingly little about how key contemporary global governance institutions function as organizations, how their own structuring facilitates or impedes the possibility of realizing different visions of what the global economy might (or should) look like, or, how modifying their structures might affect the future evolution of the system as a whole. Looking at the formative period of a new set of institutions is also a good opportunity to test our theories of how institution-building works.

In this section, we will focus on only one global governance institution, the newest addition to the Bretton Woods family – the World Trade Organization (WTO). While the WTO is a unique institution in a number of ways, it also illustrates issues that are archetypical of global governance institutions in general. Most importantly it serves to underline the point that, far from being superseded by the shift toward a political economy that is organized more on a global than

a national level, institutional questions gain a new salience as economic actors attempt to “re-scale” the organization of production and exchange.

The WTO (like other global governance institutions) exists because the more sophisticated, internationalist currents in the leadership (including both politicians and corporate managers) of the U.S. and other developed countries realized that a global market requires a complex set of institutional underpinnings. As the “realist” theory of international relations (cf. Waltz, 1979) correctly underlined, a Westphalian world has strong elements of anarchy at the global level. Anarchy does not lend itself to stable market relationships, to say nothing of long-term investments. Reducing the level of anarchy in order to get the stability and predictability necessary for a global economy to operate is the whole point of global governance institutions. Stability and predictability require that the strong as well as the weak accept some level of constraint. Institutionalization involves a tradeoff whereby the strong accept constraint in order to get the more reliable consent from weaker players (as well as from each other) that enables them to do more things (see section 2.1).

The willingness of powerful economic actors to accept institutionalized constraints is in no way predicated on altruism. Sophisticated internationalists like George Soros and Robert Rubin have at least implicitly realized that the current global economy is haunted anew by the “Polanyi problem.” Looking at the rise of national markets, Polanyi (1957[1944]) argued that the socially unsustainable character of “self-regulating” markets generated a natural “protective” reaction on the part of a variety of social groups, including a portion of the elite. Unfortunately, in Polanyi’s analysis this protective reaction was overwhelmed by the inability of the same protective reaction to prevail at the international level. International markets, particularly

financial and currency markets, could not be successfully regulated. First the collapses of the gold standard and then degeneration into the barbarism of Fascism were the result.

In the post-World War II period, the Polanyi problem of reconciling free markets with stable social and political life was taken up again through the construction of a set of international norms and institutions which made possible what John Ruggie (1982) called “embedded liberalism” – international openness combined with social protection and regulated through an interconnected set of powerful nation states. Embedded liberalism helped produce the generation of prosperity in the core industrial countries that is sometimes called the “Golden Age” of twentieth century capitalism (on the Golden Age, see the essays in Marglin & Schor (eds.), 1990).

Gradually, however, the evolution of transborder economic relations undermined this new set of institutions. Embedded liberalism had never been successfully extended to the Third World, and had no good way of dealing with increased Third World participation in worldwide manufacturing production. In addition, its international institutions depended heavily on the foundation of the nation state, whose power was undercut by the increasing speed and magnitude of international transactions. Once again, inability to regulate markets at the international level created social dislocations that seemed beyond the ability of “normal” domestic politics to resolve. The “re-scaling” of the global economy brought the Polanyi problem back to life (see Block, 1999, for further discussions).

As globalization erodes the institutional foundations of embedded liberalism and the Polanyi problem rears its ugly head once again, new institutional structures must be constructed at the global level. Failure to do so would threaten profits as well as the well-being of ordinary citizens, but success can by no means be taken for granted. The difficulty of the task creates new

risk of descent into barbarism. Global governance institutions like the WTO represent a strategy for transcending the Polanyi problem. Unfortunately it is a strategy with serious contradictions of its own, as a closer examination of the WTO in this section will make clear.

Four features of the WTO as an organization need to be underlined. First, and most obvious is its centrality to global economic governance. Second, the surprisingly democratic character of its formal decision-making procedures. Third, the tensions and contradictions between formal and informal realities, both in terms of its governance role and in terms of its decision-making procedures. Finally, and perhaps most important, the political vulnerability of the WTO (and global governance institutions more generally) needs to be underlined.

The formally democratic character of the WTO (in contrast to the IMF, for example) is, at first, surprising. Formally, each of the WTO's 135 member states has an equal vote. Since there is no equivalent to the Security Council, this makes the WTO in theory even more democratic (in the Westphalian sense of one nation one vote) than the United Nations. Its governing "General Council" allows representatives of all major countries (with the notable exception of China and Russia) to participate in relative equality (at least formally) and the WTO ministerial conferences have been accompanied by extensive public debate.

On the other hand, if we turn from theory to practice, the WTO is a classic oligarchy. The precedent, established in the GATT, that all decisions are made by consensus allows the U.S. and other major nations to set the agenda. Nonetheless, informal oligarchy remains in tension with formal democracy and this tension creates some interesting potential for change.

Despite the dominance of the informal rules in practice, the formal rules still provide a basis for political threat. The United States and the advanced industrial countries will be in a

difficult political position if a large block of developing countries were to say, “It is not possible to achieve consensus, this issue must be taken to a vote.” Is it unthinkable that such a threat would prove effective in practice? The recent experience of trying to select a Director-General for the WTO would suggest not. A series of straw votes made it clear that the candidate favoured by the developing countries had enough votes so that – even if the votes would never be officially counted – the developing countries had no reason to back down. The result was an embarrassing stand-off leading to the necessity of appointing an interim Director-General. In the end, a compromise was reached.¹⁶ The fight made it clear that if developing countries decide collectively to fight for something it will not be easy for the US and the EU to simply ignore their position.

The contrast between formal and informal realities also applies to the WTO’s power and centrality to the global trading system, but in a different way. As the organizational embodiment of the GATT, the WTO is the central forum for regulating international trade (see Krueger, 1998). As Ruggie (1998) has nicely underlined, regulating international trade has come to include passing judgement on “trade-related” domestic policies, which can mean anything from environmental regulations to tax laws. This creates the impression that the power of the WTO might even extend inside domestic boundaries. Furthermore, unlike organizations like the ILO, the WTO has the ability to legitimate sanctions if its rulings are not followed. It is, therefore, a legitimate reflection of the general perception of the importance of WTO when a former member of the WTO secretariat (Blackhurst, 1997:533) writes of its “emerging role as the pre-eminent international economic organization.”

¹⁶ Instead of one candidate serving a 4-year term, each will serve a 3 year term.

What is surprising is that if we look at the WTO in formal terms it does not appear to be a very powerful organization. Its formal, legal power is strictly limited. Its founders were very careful to avoid formal threats to sovereignty. The WTO was given no formal power to dictate national trade policies or even punish (directly) countries that refuse to abide by the obligations for openness to that have legally agreed to follow. Its only formal power is to legitimate the right of countries to engage in bilateral trade sanctions **when their interests have been damaged by trade restrictions that violate the WTO agreements.**

If the WTO is seen as powerful, it is because it is viewed as the **embodiment of the interests of the world's major economic powers. The WTO exists because powerful national players wanted to focus the politics of international trade disputes on an international organization whose decisions are likely to be considered legitimate, precisely because it is formally democratic and because those who make individual decisions are bureaucrats not beholden to any particular country. The WTO's informal power then lies in the fact that it is the concrete representation of the informal consensus and solidarity that makes the international trading system work.**

Yet unfortunately for the Michael Moore who runs the WTO and no doubt to the great glee of the Michael Moore whose next movie will probably be about the WTO, this informal consensus and solidarity among the major economic powers around the idea of free trade translates poorly into political support for the organization itself.

In the current political climate, the idea of "free markets" is, without doubt, ideologically hegemonic, but infringements on sovereignty remain

politically problematic. Consequently, institutions that must provide the institutional underpinnings for “free markets” benefit only partially from the ideological hegemony of free markets. As Steven Weber (1999) has pointed out, these organizations, as organizations, attract little political loyalty. The supposedly anachronistic institution of the nation state looks charismatic when compared to the average global governance institution.

The sophisticated internationalism that underlies elite commitment to the WTO is far from universal among key political elites. One of the central reasons for the political vulnerability of global governance institutions is the peculiar ideological character of the nation that is the hegemonic economic, political and military power of this “new world order” – the United States (cf. Evans, 1997). There is a powerful current of elite ideology within the United States that is both profoundly distrustful of any kind of public governance institutions and deeply apprehensive of anything that might reduce the absolute sovereignty of the United States itself. This segment of the conservative political elite is completely supportive of free markets but has little appreciation of the institutional infrastructure necessary to make such markets work, particularly at the global level. Distrust of government in any form combined with deep-seated xenophobia turns any institution of global governance into the enemy. Hostility from traditional conservatives (principally in the United States) who will be hypersensitive to any WTO actions considered to infringe on U.S. sovereignty is almost inevitable.

At the same time, an increasingly active civil society has begun to take a serious and vociferous interest in the politics of globalization. These groups have a global governance agenda that is quite different from the Soros/Rubin agenda. They are interested in governance in the sense of universalistic enforcement of a broad set of democratically formulated socio-

political norms that would reconstruct the market rather than simply expand it. Most of them success of global governance in the Soros/Rubin sense may even diminishing rather than enhancing the kind of global governance that they are interested in. If passivity and defense of its original mission are the WTO's only response to their critiques, frustrated civic groups have every reason to try to get their national governments to withdraw support from the organization. A progressive-conservative alliance of political groups whose only point of agreement is that the WTO should be dismantled is far from fanciful, especially in the United States.

The political vulnerability of the WTO is compounded by the lurking power of the democratic majority – the developing countries. In the Uruguay round the developing countries were willing to accept promises in return for their concessions on issues like TRIPS, finances and services. The power implicit in the possibility of invoking the formal democratic rules was not tested. In Seattle, perhaps emboldened by the willingness of the demonstrators outside the meetings to challenge the status quo, the developing countries drew the line. The Seattle outcome presents a challenge to the sophisticated internationalists. Are they willing to use the WTO to reconstruct global markets in a way that responds to the demands of those disprivileged by the way in which globalization currently functions? Or, will they risk their efforts at global institution-building (and in the longer run increase the possibility of Polanyian collapse) in order to preserve the current definition of what constitutes a legitimate global market?

The vulnerability of the WTO raises the spectre of Polanyian collapse, but it also creates opportunities for institutional change from the perspective of those interested in transforming the current global political economy rather than stabilizing it. These opportunities are perhaps best illustrated by the “core labour standards” issue. “Core labour standards” (CLS) means different things to different people. The most recent ILO version which the U.S. finally agreed to sign up

to is a good example of a minimalist version, but everyone recognizes (some with hope, some with fear) that this is the camel's nose and that ultimately "core labor standards" could come to mean things like protecting the right to organize, which is why the concept is politically interesting. The question then is whether the WTO might provide an arena for getting the camel's nose farther into the tent.

The argument for inclusion of CLS in the WTO's mandate is simple and logical. There is no logical reason why the absence of CLS in a particular country should not be considered a trade-related basis for unfair competition in the same way that absence of intellectual property rights is considered to be a trade-related violation of the rules of fair competition. Not having to pay the wages that labour could demand if it were free to exercise its collective rights constitutes a subsidy to local producers in exactly the same way that not having to pay royalties to Bill Gates constitutes a subsidy to local producers. If the second is a "trade-related" issue, the first is too.

The politics are a bit more complicated than the logical argument. First, there are the politics in the Westphalian sense of positions taken by national governments and then underlying these are the politics of interest groups and organizations (both within and across societies). Then there is the interaction of the two which will determine whether there is any movement.

At the national level, advanced industrial countries with social democratic regimes (i.e., the Nordic countries) have predictably been strong proponents of making the enforcement of CLS part of the WTO's mandate. On the other side, the main opponents of including labour standards in the WTO's mandate are developing countries. Their opposition stems from two different sources.

First, as politicians, sovereignty is important to the developing country leaders, and while Bill Clinton doesn't have to worry about sovereignty, they do, because they don't have the power

in “real politik” terms to resist intrusions that they come to see as illegitimate. In the particular case of the WTO they must remain suspicious that oligarchy will prevail over democracy and that future interpretations of CLS will be used to the benefit of the developed countries. Second, they have economic interests. They see limitations on local firms’ ability to exploit labour as threatening their comparative advantage. Desperate to increase their exports to developed country markets, Third World governments are terrified that the labour standards issue might be used against their exporters. And, of course, as elites within their own countries, normative changes at the global level that might increase the bargaining power of local labour may be seen by many developing country leaders as costs in themselves.

Most interesting in terms of national positions is the United States which has been on the side of CLS (in an ineffectual and wimpy but nonetheless persistent fashion) ever since the formation of the WTO. Obviously we don’t think of the United States government as dedicated to supporting labour. Yet, the “reformist” stance of the U.S. on this issue makes perfect political sense.

From the point of view of the U.S. labour movement, which is a central political constituency from the point of view of the current U.S. administration, institutionalizing global labor standards comparable to those that operate in the U.S., especially in the more economically competitive regions of the Third World, is a bedrock issue. For the administration’s corporate constituency, on the other hand, the issue is less salient. While they are beneficiaries of the absence of labour standards in developing countries, major U.S. transnationals are also aware that the diffusion of CLS would be at most a minor detriment to their global profit rates. From the point of view of the Clinton administration

then, supporting core labour standards in the Third World was a political winner.

This dynamic presents an intriguing opportunity from the point of view of U.S. labour (for further discussions, see Evans, 2000). They are much more likely to be able to succeed when they exert pressure on an issue which carries only minor domestic political costs from the point of US politicians. Trying to get a US administration to support core labor standards beyond its boundaries certainly has more prospect of being a winner than trying to prevent capital from investing abroad or trying to impose general restrictions on the entry of foreign consumer goods into the US.

At this point, however, the peculiar internal organization of the WTO (designed, of course, with a view to solving other problems) changes the calculus. U.S. labor will *never* succeed in getting a level of U.S. support sufficient to trump the Westphalian structure of the WTO as a polity. Without domestic allies within at least the most important developing countries, say Brazil and India for starters, they cannot win – which is to say that nothing is likely to happen unless developed country labour movements can develop more effective alliances with their Third World counterparts.

The argument up to now can be recapitulated briefly as follows:

- 1) An organization is created by governments acting as agents of the more sophisticated elements of transnational capital in order to provide a more politically efficient and effective institutional means of allowing a more stable,

less costly expansion of international openness and increasing the transparency and predictability (and consequently reduce the volatility) of the global economy, thereby reducing the threat of the “Polanyi problem.”

2) Once these aims are embodied in a concrete organization, the organization inevitably becomes the focus not only of the aspirations of those that like the existing mode of globalization and are hoping (through the creation of the organization) to strengthen it, but also of those who are hostile to globalization. Thus seen, on the one hand, we have powerful conservatives interested in recovering an idealized Westphalian past, in which sovereign power was the vehicle of global aspirations rather than being compromised by them, and on the other hand, we have a host of less privileged social actors substantively threatened by the inegalitarian consequences of globalization and therefore hostile to the idea of strengthening the institutional infrastructure of globalization (as long as globalization is defined as “governed free markets”). This inevitable but unintended (and apparently unforeseen) consequence leaves the organization (and its original project) politically vulnerable.

3) The existence and potential power of the organization also change the incentives and potential strategies open to groups harmed and threatened by the existing mode of globalization – in this particular case developed country labor – adding the strategy of imposing a different set of global norms to its traditional (and hitherto relatively ineffectual) strategies of trying to resist globalization through national level strategies aimed at insulation from the global economy.

4) The Westphalian definition of democracy that was (naturally and indeed almost inevitably) incorporated into the internal governance of the WTO forces any group that wants to try to imposing a different set of global norms to find allies within a range of developing countries and do whatever is possible to strengthen the local political position of these allies. Thus, one of the unintended consequences of the creation of the WTO will be to push what has always been a rather chauvinistic labour movement to adopt a more internationalist vision of both its identity and interests and to engage in concrete efforts to strengthen both its ties to third world labor movements and the local political clout of these movements.

While this vignette of the WTO and the core labour standards issue is more a sketch of hypothetical possibilities than it is a recounting of empirical observations, the important role of labor in the demonstrations in Seattle (largely ignored by the media) underlies that the WTO has indeed helped to shift labor's attention from domestic to global politics. The vignette also serves to illustrate several of the propositions set out in our initial conceptual framework.

First, it nicely demonstrates the disarticulation between "objective interests" and institutional agendas. Jesse Helms and Pat Buchanan are as interested in defending free markets as George Soros and Robert Rubin are, but their worldview includes no conception that institutionalized governance at the global level may be a prerequisite for the maintenance of capitalist markets

(or that it is no longer possible to de-link the fortunes of domestic capitalists from the expansion of global markets). In short the road from interests to politics takes a winding path through cultural and ideological assumptions.

Second, it illustrates the way in which the process of institution building generates unintended consequences. The formally Westphalian structure of the WTO is an almost serendipitous by-product of the political complexities of institution-building at the global level. Yet, it may well end up having a profound effect on what kinds of global rules can and cannot be implemented.

Third, it illustrates the way in which institutional constructions themselves can end up reshaping interests. The process of globalization in itself tended to make the AFL-CIO more xenophobic rather than more internationalist. Building institutions to govern globalization has had the opposite effect. Without a concrete organization to serve as a focus for political action, internationalism is too amorphous an agenda to generate much political energy. Given a good target, the politics of internationalism begins to make more sense.

None of these follows from either a functionalist/efficiency model of institution building or an instrumentalist/interest model of institutions. While the WTO may indeed succeed in serving the Soros/Rubin interests that lay behind its creation, it is likely to be able to do so only if it manages to simultaneously speak to the interests of other constituencies. Some of these interests were unanticipated by the WTO's architects. Some of them were at least partially given shape by the very existence of the WTO. In short, to be "efficient", the WTO must end up serving interests that its own existence has helped generate, often unintentionally.

5. Conclusion: Towards an Institutional Approach to Economic Change

Our interest in an institutionalist approach stems in part from intellectual dissatisfaction with the existing economic canon. We are convinced that it suffers from a premature parsimony, one that is achieved at the expense of explanatory power. At the same time, our quest for a better approach to understanding the contemporary global political economy is prompted by dissatisfaction at a more substantive level. Global economic performance leaves a great deal to be desired, and the policy prescriptions that flow from the current canon seem more a part of the problem than a part of the solution. A quick reiteration of the problems will help underline the importance of developing an alternative view.

The most puzzling failure from the point of view of mainstream economics is the failure of the globalized economy to match the record of growth produced by the less open world economy of the Post World War II “Golden Age” of capitalism (roughly 1945-1973). In the ten-year period between 1985-95 the average annual per capital growth rate for lower income and middle income countries was *negative* (excluding China – which has protected itself against full-fledged globalization)(World Bank, 1997).

Another cause for concern is the volatility of the new global financial markets, whose devastating impact on developing economies was demonstrated most dramatically in the 1997-98 Asian financial crisis. The potential fragility of the system is perhaps the greatest source of anxiety for those who are most closely involved in running it (e.g., Soros and Rubin), but they are handicapped in transforming their fears into policy by the inability of the existing canon to provide theoretical foundations for needed changes.

Perhaps most disturbing is the association between increased economic openness and increasing global inequality. The income share of the bottom 60% of the world population has

fallen by more than 40% between 1965 and 1990 (from 9.27% to 5.27%), while the share of the top 20% rose from just under 70% to over 83%. And this trend accelerated at the end of the period, just as globalization accelerated. Growing inequality is, of course, exactly what one would expect from a market which starts from a foundation of vastly unequal endowments and then allows capital and goods to move freely while keeping workers largely trapped inside national boundaries, although this is not what the dominant canon expects.¹⁷ In short, the current canon has not only failed to reduce global inequality but implies policies that are likely to exacerbate current inequities.

Our concern with these practical problems dictated our choice of cases. Between country inequality will only diminish if poor countries can “catch up” economically (i.e., growing at more rapid per capita rates than the developed countries). The developmental state represented in its heyday the institutional instrument *par excellence* for catching-up. Its performance represented an important anomaly for the existing canon, but made sense when viewed through an institutionalist lens. Thus, the developmental state is a critical case for testing the relative explanatory power of an alternative approach.

Initial reactions to the 1997-98 Asian crises included jubilation on the part of the most adamant adherents of the dominant canon because the crisis was seen as negating both East Asian economic success and its institutionalist implications. As we pointed out in section 3, subsequent analyses have shown the jubilation to be not only premature but misplaced (for a review of this literature, see Chang, 2000b). On the one hand, subsequent reflections have increasingly pointed to the key role of hasty and excessive financial liberalization in generating

the crisis. At the same time, the current canon was unlikely to even consider the hypothesis that the domestic roots of the East Asian crisis lay not in the “deviant” institutional character of the developmental state but in the political undermining of this structure – an institutional “regression to the mean” in which the Korean state at least came to resemble more closely the archetypal third world state.

Our argument here not only supports this interpretation but also suggests that the political decline of the developmental state, like its economic problems, had important external bases as well. Ironically, the increasingly more pervasive acceptance of the globally dominant version of the existing canon turns out to be a culprit in the East Asian crisis in two ways – directly as a source of pressure for overly rapid financially liberalization and indirectly as a contributor to the political de-legitimation of the institutional structures of the developmental state itself.

Our analysis of the WTO is more optimistic, perhaps because it focuses on prospective possibilities rather than past performance. The basic argument is twofold.

First, the very existence of the WTO must be seen vindicating the institutionalist position. The most powerful and sophisticated actors in the global economy did not create a new organizational arena fraught with political risks because they were interested in expanding the opportunity for disprivileged nations and social groups to voice their concerns regarding the global economy. They did it because they recognized that markets, especially global markets, do not run themselves and will only continue to run smoothly if they are policed and regulated by some set of quite powerful global institutions and that these institutions will not “spring into being” through some automatic functionalist process but must be created through purposive, and we repeat, politically risky initiatives.

¹⁷ For data and discussion of rising levels of global inequality, see Stewart (1999), UNCTAD

Second, and even more important, efforts to more thoroughly institutionalize global governance have the unanticipated consequence of generating pressure for broader, market-reconstructing definitions of governance. While definitely not created to provide a forum for participatory international politics, global institutions cannot help becoming targets for various “interest groups”, both extant and latent, in international politics. As targets, they focus political energies, define worldviews, generate new agendas that can be pursued in domestic as well as international arenas. And they can even give birth to new “interest groups” by changing the costs and benefits of political alliance and changing worldviews of the actors involved. Whether these efforts can succeed in putting in place policies that will mitigate the inegalitarian character of current global growth remains to be seen, but at least there is a political/institutional process in play which runs counter to the *status quo*.

Putting the developmental state and the WTO together, we have two very different instances with quite different lessons. Both of them are too central to the evolution of the current global political economy to be ignored by the dominant canon. Yet, in both cases, explanation via the dominant canon’s analytical apparatus requires embarrassing contortions, if, indeed, it can be achieved at all. We have, in short, confronted the existing canon with anomalies that it can neither ignore nor dispose of easily.

At the same time, exploration of these cases has proved fruitful in terms of refining and reconstructing the conceptual sketch of institutional dynamics with which we started. Both cases illustrated our basis premise that an adequate theory of institutions must see them as both *constitutive* of interests and *constructed* (or reconstructed) in response to changes in ideology (or

(1997), and Korzeniewicz and Moran (1997), among others.

worldview) as well as in response to changes in interests. But, they did more than this. While the cases were not chosen in order to illustrate the variant ways in which ideas, interests and institutions might interact, they ended up serving this function as well.

In the case of the developmental state, the process whereby social groups that previously formed integral parts of the political foundations of the developmental state came to view their interests as lying in its dismantling provides a nice rebuttal of simplistic theories of interests and institutions. This is most obvious in the case of the bureaucrats who behaved completely irrationally from the point of a Buchanan/Kreuger/Niskanen view of bureaucratic behaviour by calling for their own disempowerment. Their new “free market” attitudes cannot be explained without heavily reliance on a shift in worldview, rooted in turn in new patterns of professional training. The sequence then is one in which worldview rather than position in the economic structure shapes interest definitions.

In the case of local entrepreneurs (the *chaebols*), the logic is more mixed. On the one hand, their objective economic position did shift. Their investments and markets became increasingly international and so their adoption of an internationally prevalent anti-statist ideology makes some sense in economic terms. At the same time, however, it is important to recognize (as became apparent in the aftermath of the Asian crises) that their ability to sustain their own growth independently of the developmental state was, to a significant degree, fictitious. So the shift in their interests was also inseparable from a shift in worldview. The irony here is, of course, that the shift in both worldview and interests was made possible by the success of the developmental state as an instrument of economic transformation. Thus, prior institutional change can be considered to underlie changes in interests and ideas.

The case of the political leadership is also complex. On the one hand, the new generation of political leadership had an ambivalent relation to the developmental state from the beginning, not because of its aggressive pursuit of economic transformation but because of its authoritarian and repressive face. At the same time, they saw the developmental state as guilty of unduly concentrating economic power in the hands of a few *chaebols*. Despite these ambivalences, it is clear that their abandonment of the pro-producer, nationalist elements of the economic policy of the developmental state must be explained in terms of their adherence to a global free-market worldview. This adherence might, of course, represent an interest-based conformity founded on fear that nationalist policies would bring punishment by international financial markets, but the extent of the over-conformity suggests an irreducible element of ideological conversion.

In sum, the developmental state's loss of political support best fits a model in which changing worldviews, more specifically the adoption of the globally dominant worldview on the part of local elites, generates institutional change which, in turn, has negative consequences for economic performance (i.e., contributing to the creation of the Asian crisis).

The WTO case is not inconsistent with the developmental state case but it emphasizes a different sequence. Again, worldview plays a dominant role in generating institutional change (in this case, the sophisticated internationalist Soros/Rubin worldview that recognizes the necessity of creating institutions to govern global markets). The main part of the story, however, leads from the creation of an institutional context to the subsequent redefinition of interests and worldview, with the added twist that the institutional effects are fully decoupled from the intentions of the institution's creators. Concretely, the creation of the WTO provides a stimulus for the redefinition of labour's interests and worldview in an internationalist direction. This

change in worldview and interest definition on the part of a significant set of social actors is, in turn, projected to shift the way that the WTO functions as an institution in the future, and thereby the way in which legitimate global markets are defined.

The most important point here is that the current canon offers little or no analytical leverage on the dynamics of either case. Its basic assumptions prevent it from doing so. “Preferences” (both in the sense of interests and worldviews) must remain exogenous and unchanging. A story in which interests and worldviews are variables shaped by institutional context but also playing a role in causing institutional change is impossible. Premature parsimony has robbed the canon of its ability to deal with these key cases.

Adherents to the dominant canon will, of course, respond to all of this by saying that whatever successes an institutionalist approach may achieve in interpreting individual cases, its explanations remain too complicated and too prone to *ad hoc* improvisations to ever serve as the basis for a satisfying theory of economic change. Encompassing elegance and parsimony, it will be maintained, will always trump superior ability to explain particular cases. The response is clear: A passion for elegance and parsimony is essential to any effort to better understanding of the social world, but premature parsimony can cripple the ability to understand complex realities.

Premature parsimony is fundamental to the theoretical failures of the existing canon. Unfortunately, when it comes to explaining economic change, pressure for premature parsimony is intense. The pressure is intense because the coupling between theory and practice is so uncomfortably tight, ideologically as well as practically.

Powerful social actors care much too intensely about getting clear answers delivered with full conviction to tolerate the kind of complexity that an adequate explanation would involve.

Theories must generate simple rules that enable decision-makers to take prompt action. They must also generate confidence among the decision-makers and ideological hegemony vis-a-vis the rest of society. Elegant, parsimonious theories whose basic premises are at one with the existing, taken-for-granted assumptions of powerful social actors (and to a lesser extent of society at large) and which can also claim broad applicability provide powerful ideological support as well as clear bases for action. Such theories may be incomplete, or wrong, but until the decision-making rules they generate are clearly connected to obviously disastrous outcomes, those rules will prevail. The prevalence of the rules in turn reinforces the legitimacy of the theory, since knowledge of the theory enables prediction of a broad set of important decisions, and makes the theory's predictions to some extent self-fulfilling.

Of course, two additional conditions will have to be met before these rules can become truly "hegemonic". First, the decisions they produce should not imply sacrifice or discomfort to the decision-makers themselves or their most politically powerful constituents. Second, the theories on which they are based should work reasonably well in simple contexts (say short-term microeconomic decision-making in firms) that are salient and valued by decision-makers. As long as these two conditions are met, the contexts in which the theories are applied are likely to be extended indefinitely, despite obvious inconsistencies or illogic and even though their application may lead to immediately deleterious outcomes for the less powerful and raise the risk of crisis and disaster for the decision-makers themselves in the long run.

The contemporary economic canon enjoys all the necessary conditions for sustaining premature parsimony and under current conditions it is unlikely to be unseated by a complex and "mushy" institutional alternative. Even if an institutional alternative could unequivocally demonstrate its scientific superiority, the practical and ideological costs of changing decision-

rules would militate against jettisoning the established canon. And, an institutional alternative is still a long way from such unequivocal demonstrations.

To improve its chances, a more institutionally-oriented alternative canon must do two things. First, it must be able to demonstrate as incontrovertibly as possible that its ability to explain and predict specific events is superior to the existing canon. This means demonstrating that events that are anomalous for the existing canon become comprehensible and predictable once a more institutional view is applied. Given the ambiguities inherent in most social and political outcomes, this is not an easy task, but it is still essential. We would like to think that we have taken a step in this direction with the case studies that we have presented here. Second, while eschewing premature parsimony, an institutional approach must still work in the direction of showing that its explanations are not simply *ad hoc* stories concocted after the fact but are consistent with each other and with some body of general propositions. This is even harder. Our claims to progress on this dimension are more modest. We offer a preliminary step at best.

Even assuming both goals were eventually reached, the possibility of establishing an alternative canon would still depend on the inability of the existing canon to carry on – in short some sort of sufficiently profound practical crises that would rob the existing canon of its ideological charisma. Since such a crisis would likely to be ugly for everyone (not just the privileged), those who would like to unseat the existing canon should probably hope that the occasion of their success never arrives.

This should, however, in no way diminish enthusiasm for trying to contribute to the construction of an alternative canon, for two reasons. First, conquest is not the only form of success. Just as religious dogmas transform themselves by assimilating oppositional positions without ever admitting that the previous orthodoxy was ever in error, intellectual canons can be

substantially transformed without ever appearing to capitulate. Second, the worst of all possible worlds would be to have the existing canon stumble and fall into crisis with no better alternative waiting in the wings to replace it. Anyone who really believes that the premature parsimony of the existing canon has crippled its ability to understand and predict economic change had better be working furiously to construct an alternative view, not because they wish for crisis but because they are terrified of what crisis would mean in the absence of a sound intellectual basis for formulating alternative strategies.

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