Revisiting Industrial Policy and Strategic Coupling Strategy Under the Era of Hyperglobalization

Chean Chung Lee, National University of Singapore, Singapore

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Abstract
In a more independent and interdependent world, it is suggested that in order for states to be successful in economic development, one has no choice but to connect with the world capitalist economy. Although there is no explicit law enforcing this rule, Khong (2018) argues that the experience of the last sixty years provides a clear answer, and even a "tested maxim" that in order for nations to climb the ladder of economic prosperity, the only way is to link up with the world capitalist economy. However, as opposed to "passive integration", it is suggested that "active strategic integration" will be a better option to protect the negative offshoots of hyperglobalization. What level of "activeness" is considered appropriate? How "strategic" should it be to reap the benefits of global economy while not suffering as much from the adverse impacts? This paper aims to provide a critical review on globalization, and further elaborate different strands of "active strategic integration", namely industrial policy, strategic coupling, and counteracting premature deindustrialization.

Keywords: Hyperglobalization, Industrial Policy, Strategic Coupling

INTRODUCTION

Globalization

Globalization which, for economic discussions purpose, often refers to free circulation of capital, labor, goods and technology across national boundaries (Molanovic, 2012). The Institute for Public Policy Research (2012) suggests three categories of globalization: the first stage (First Globalization) between 1870 and 1914, Second Globalization began after World World II until the latest financial crash (1944- 2009), and what we experience now is the Third Globalization.

There is also another categorization coined by Rodrick (2018, p.28): Hyperglobalization. It refers to the phenomena since 1980s on 'extensive economic integration and limited political integration', as well as 'the attempt to eliminate all transaction costs that hinder trade and capital flows'. Hyperglobalization represents a major shift from the Bretton Woods rules to Washington Consensus policies, which gained momentum in the first half of Second Globalization. Under hyperglobalization, trade rules were extended tremendously to cover non-trade areas like intellectual property and sanitary standard that what were previously considered to fall under the domestic policy category. This shift has dramatically increased trade, financial openness and capital flow, but also significantly weakened local governance mechanism and state sovereignty.

One has to be mindful that globalization can be an inter-subjective term as a result of different collective experiences of growth. Piketty (2014, p. 98) reminded this by explaining that "public opinion in different countries varies so widely in regard to commercial and financial globalization and indeed to capitalism in general". It is under this context that, in order to address issues pertaining to globalization (and hyperglobalization) in a meaningful way, we have to discuss the multiple dimensions of globalization, namely knowledge, trade, labor, FDI, capital market, and perhaps others.

Many economists argue for globalization. They claim that free trade and financial liberalization can allocate resources more efficiently, thus reduces overall costs and raises productivity. International trade under the global capitalism system, in essence, has reduced poverty and promoted (and still promoting) economic growth in many developing countries. The proponents also argued that free trade can help create jobs, make companies more competitive, and lower prices for consumers (Collins 2015).

Also on a positive note, Stiglitz (2004, p. 470) opined that globalization of knowledge topped the list as the strongest force for growth in emerging markets. This is because it transfers both technical knowledge and ideas on policies as well as institutions to developing countries. Not so much on globalization on capital flows, he opined. FDI that will stay longer is probably more positive, bringing not only capital, but also technology, institutions, management knowledge, foreign market, and expatriates.

However, the rest of the elements of globalization are far more controversial. Liberalization of short-term capital flow has been the most contentious aspect of globalization. The recent 2008 global sub-prime crisis, and even dated back to the Asian financial crisis, can be attributed to uncontrolled liberalization of capital flow.

Liberalization of trade, while often applauded for bringing growth to developing countries, have serious setbacks. While developed countries enthusiastically pushed for reducing trade barriers, they are often spared from doing the same. At the same time, lowering trade barriers from both sides will give comparative advantages to developed countries in gaining access to commodity and market of the developing countries more easily than the latter do.

Globalization of labour is less discussed. In principle, believers of global efficiency in capital flow should also endorse free flow of labour from areas of low productivity to areas of high productivity. However, the agenda of free capital and goods flows are overemphasized, while the mobility of labour hardly mentioned. 'The fact that the globalization agenda has focused on the free movement of capital, and virtually ignored the movement of labour, reflects in part who is controlling the agenda' (Stiglitz 2004, p. 471). As a result, it is not uncommon to see growing skepticism towards current form of globalization.

After recognizing different dimensions of globalization, now we shall examine how globalization affects growth of developing countries in different ways. Stiglitz (2004, p. 473) argues that mass capital liberalization destroys more jobs in developing countries than creating them. Conventional theory of comparative advantages believe that resources will move from low productivity uses to high productivity uses, thereby making everyone betters off.

However, jobs are not created overnight. It requires a recipe of conducive business environment, low risk and low cost of capital. Globalization and uncontrolled flow of capital will not guarantee a positive climate for business, but aggravate them. Rodrick (1997, p. 4) further suggests that reduced barriers to trade accentuate the asymmetry between groups that can cross international borders, namely owners of capital, highly skilled workers and professionals, and those that cannot. Unskilled and semiskilled workers and most middle managers, who belong in the second category, bear the brunt of globalization. Therefore, removing jobs in protected industries do not necessary creating new and productive jobs, but often lead to unemployment.

Second, globalization results in higher financial and business risks. Indeed, 'the anticipation of risk itself has adverse effects' (Stiglitz 2004, p. 474). As mentioned earlier, higher risks will fetch higher premium in terms of capital cost, thereby adversely affecting job creation and entrepreneur ventures.

Third, capital flows may not translate into more growth. Instead, it will cause the appreciation of currency, and possibly inflation. Cases in some countries where empty properties crowded out real domestic investments, but local people find it harder to survive with higher property cost are some good examples of adverse effect to growth.

Forth and the most important impact - the loss of sovereignty over monetary policy, financial institution and management over social capital. International financial organizations, notably International Monetary Fund (IMF), World Bank and World Trade Organization (WTO), impose non-financial terms and constraints that are lacking political legitimacy. Certainly trade has implications on domestic norms and social arrangements that embody them. 'Globalization becomes contentious when a local workplace practices, legal rules, environmental standards, and social safety nets

are undermined' (Rodrik 1997, p.31). As a result, the solution that is not political sustainable will undermine social cohesion, especially in developing countries where prevailing identity politics is still predominant with existing social cleavages. In long term, that will create political and social instability and further impede growth.

Because of the reasons stated above, globalization is apparently a double-edge sword for the developing countries. On the negative side, globalization has been vilified for increasing poverty, resulting in job loss, and even impeding growth. This relates to our hypothesis: Is participating in global economy the only way out? The answer is self-explanatory: other options are much worse. Just to name a few, South Korea, China and Vietnam were in economically dire situation before the opening up of their economies. North Korea remains so until today.

However, not all countries that embrace world capitalist economy are successful. While central planning evidently fails, unrestrained opening of free market recurrently lead to dismal results. The growth of Argentina and many Latin American countries slowed down after following the liberalization prescriptions of neoliberalism (also known as Washington consensus). In Sub-Saharan Africa, the growth prospect is even bleaker. On the other hand, many East Asian countries, notably Japan, Korea, Taiwan, China and Vietnam managed to integrate themselves into world economy while retaining high growth. It ponders us to ask, what went wrong and what went right? What is the best way to deal with the negative impacts of globalization yet able of reaping benefits from it? Here, three instruments and scenario, namely industrial policy, strategic coupling and the phenomenon of premature deindustrialization will be discussed.

Industrial Policy

Industrial policy is one of the instruments for strategic integration into the world economy. Chang (2003, p. 112) defined industrial policy as 'a policy aimed at particular industries (and firms as their components) to achieve the outcomes that are perceived by the state to be efficient for the economy as a whole'. The impressive developmental stories in Japan, Korea, Taiwan and Singapore can be attributed to deliberate state interventions via active industrial policy. All of them deployed a 'set of policies to deliberately change the market prices and production priorities' (Singh 1998, p. 71), and enabled the 'national champions to overcome their latecomer disadvantages and to achieve economies of scale in domestic and international competition' (Yeung 2016, p. 6).

Chang (2003, pp. 46-52) argued that there are three strands of beliefs on the role of the state: welfare economics, neoliberalism and institutionalism. Welfare economics focuses on the market failure and its inherent consequences: monopoly, externality and inadequate public goods. Standing at the opposite side of welfare economics, neoliberals believe that extending the role of the state beyond its minimal functions of providing basic security, rule of law and support for free market are a form of tyranny. Besides that, state intervention in a complex modern economy is simply impossible and better leave it to the 'spontaneous' order of the market. Also, due to principal-agent problem, state intervention is likely to create allocative inefficiencies, rent-seeking attitude and eventually government failure.

Institutionalism differentiates welfare economics and neoliberalism by explaining that the 'success of an economy depends on an array of economic and political institutions, of which the market is only one, if a very important, component' (Chang 2003, p. 46). While the critique of the neoliberals on welfare economy have provided some important reflections, it has failed to address why some states can be so successful by adopting the institutionalist's industrial policy. Indeed, both welfare economy and neoliberalism strands believe in the institutional primacy of market, which the latter does not. Market is only one of the many economic institutions. Institutionalism explicitly recognizes the role of the state as the 'designer, defender and reformer of many formal and informal institutions, while taking seriously the political constraints on the effective exercise of such a role (Chang 2003, p.52).

Nevertheless, World Bank (1993) claimed that the East Asian miracle was not due to industrial policy, but market-friendly strategy adopted by these countries. However, overwhelming evidence shown that these countries did not follow the doctrine of market-supremacy - taking a hands-off market-friendly approach and leaving prices and priorities to be determined by the market. Ajit (1998, p. 70) listed down a wide array of interventionist instruments used by these countries:

- import controls;
- control over foreign exchange allocations;
- provision of subsidized credit, often at negative real interest rates, to favoured firms and industries;
- control over multinational investment and foreign equity ownership;
- heavy subsidization and 'coercion' of exports, particularly in South Korea;
- a high active state technology policy;
- restrictions on domestic competition and government encouragement of a variety of cartel arrangements in the product markets;
- promotion of conglomerate enterprises through mergers and other government measures (again particularly in South Korea);
- wide use of 'administrative guidance', indicating non-transparency of government interventions.

Obviously, the experience of these countries 'is certainly an argument against laissez-faire; nor does it provide any support for "command" planning of production of the Soviet-type, which in effect supplants the market together' (Arjit 1998, p. 71). This reaffirmed the case of successful industrialization using the industrial policy approach. Rather than stuck into the conventional ways of welfare economics or neoliberalism, elites of these countries focus on the role of the state and how institutions are arranged and prioritized to achieve its economic development goals.

What are the advantages of industrial policy? Chang (2003, p.113) suggests that state can play the role as the manager of conflict and as an entrepreneur. It is argued that new modern industrial economies require large fixed investment, or scale economies. Firms' considerations for competition will result in the case of under-investment (insufficient entry) or over-investment (price war), therefore justifying the needs for state to intervene in ensuring optimal participation. To overcome this, states as the manager of conflicts can use industrial policy tools, such as regulating entry license, providing limit for production and expansion, and offering negotiated exits to keep its production at optimal level.

Of course, it is not easy to arrive at which level is optimal. However, just as there is government failure, there is also market failure. In the modern complex economic system, where the factors of production are 'interdependent in use but dispersed in ownership' (Abramovitz 1986, p. 402), coordinated efforts are ever more desirable to bring effective structural change. It is at this context that state can play the role as central agent in providing a vision for the future – hence the important of state as an entrepreneur.

Under the age of globalization with growing influences of Multinationals Corporations (MNCs) and foreign direct investment (FDI), is industrial policy still relevant? While it is true that FDI and MNCs are playing an increasingly important role under the wave of globalization, it does not mean that states should forego its coordination and entrepreneurial roles under the guidance of industrial policy.

To begin with, what is good for MNCs is not necessary good for the host country. MNCs are investing in a state for profits. The predatory nature of MNCs will cause them to maximize profit extraction and repatriation to their original headquarters, which can be easily done via transfer pricing or royalty payments. MNCs will also tend to keep high-level activities such as R&D in their home country, thus preventing positive spillover effect expected by the host country.

Apart from that, many successful developmental cases using FDI are not as it claimed. A number of countries in East Asia, while not against hosting FDI in certain areas, have had rather restrictive policies toward FDI. Singapore heavily relied on MNCs, but deliberately directed FDI toward government-designated priority sectors (Chang, 2003, p.252). Korea adopted a selective strategy on FDI by only targeting at strategic sector. As a result, as of mid-1980s, only 5% of the MNC subsidiaries in Korea were wholly owned, compared to more than half in Mexico and Brazil (Evans 1987, p.208). At the same time, Malaysia that had fairly liberal attitudes toward MNCs and one of the most favorable destination of FDI in the world, now suffered prolonged economic slowdown. Malaysia is likely to find it difficult to move into more sophisticated industries that will help it sustain long-term growth (Lall 1995, p. 771).

Strategic Coupling

While industrial policy has influenced the growth and development in East Asia countries significantly, it is perhaps more relevant to rethink the role of the state in a more complex, globalized and interconnected world. In the 1970s, it is largely the industrial policy that has driven the growth of state-nurtured firms to become national champion. The success of Samsung, Hyundai, Hon Hai and STC are certainly the results of their states' relentless efforts to promote export-led industrialization. Today, contrary to institutionalists' view, there is a counter-argument that the best time for industrial policy might be over.

Apparently, as these firms have grown to be more international, there were more away from their home states. Starting in 1980s, the firms slowly enjoyed more autonomy and no longer dependent on state support. At the same time, states find it more confined to provide sufficient support to the firms as they grow bigger and more global. Additionally, as another force - globalization began to set in East Asia, big national firms can now connect themselves to the global production networks, which

in turn sustains their growth and expansion. In today's world, firms are no longer necessarily owe their new competitive advantage to policy intervention by their home developmental state.

Therefore, instead of the all-powerful developmental states that were steering growth in the early days, there is a need to reframe this state-centric thesis into firm-specific narrative. National firms are no longer the by-products of the developmental state, but active actors with stronger autonomy, developed organizational and established own decisions.

In view of that, Yeung (2016) argues the developmental state approach is becoming increasingly obsolescent in the post-1990 context. 'Its predominant focus on state initiatives and capacities in early industrialization has rendered itself locked-into a conceptual path dependency premised on seeing the economy and its key agents (firms) through the state and its political choice. Its ability to provide insights into the rise of East Asian firms in the global economy become handicapped by its analytical baggage of state-centrism'. (Yeung 2016, p. 15)

Therefore, to respond to the dynamic articulation of East Asia economies into the global economy, new lens are required to provide new insights. Instead of industrial policy, it is the 'strategic coupling' instrument that these firms have adopted to continue their growth in the age of expanding global production networks.

To untangle this concept, it is referred that 'by '"strategic"', it affords greater analytical significance to firm-specific initiatives, such as technological innovation, capacity building, international market development, and so on. By '"coupling"', it refers to the dynamic relational process through which national firms decouple partially from domestic political-economic structures – developmental states or associated institutions – over time and couple with lead firms in global production network'. (Yeung 2016, p.4)

An example of this is how the global production network of iPhones. In 2015, the contract of assembling 700 million IPhones was given to Foxconn Technology. Hon Hai Precision Industry, Foxconn's parent company is the creation of Taiwan's successful industrial policy. However, most of the production lines of Foxcoon today are situated in Mainland China and not Taiwan. It is harder to tell how Taiwan's developmental policy can benefit Hon Hai today.

On the other hand, Samsung from Korea has shipped more than 837 million phones to users worldwide in 2013-2014 period alone, surpassing Apple to be the largest smartphone vendor in the world. Samsung, the largest chaebol in Korea today, is also a beneficiaries of the domestic developmental state with institutional, political and financial support. According to Yeung, organizationally fragmented and spatially dispersed production networks constitute a new form of economic structure, one that underpins today's complex global economy and its uneven developmental outcomes (Yeung 2016, p. 1). Therefore, it is the strategic coupling, and not industrial policy, that have explained how these firms continue its growth trajectory today.

Phenomenom of Premature Deindustrialization

Here is another thought: Industrial policy might be successful in the past, but it is increasingly difficult in the face of globalization. In the East Asian cases, manufacturing is the main engine of productivity and economic growth. Manufacturing allows rapid economic catch-up because its high-productivity nature and its production technologies are relatively easy to be imported, as compared to the limitation in agriculture and service sectors. Research of Rodrik (2018, p. 80) shown that manufacturing industries will 'close the gap with the technology frontier at the rate of 3 percent per year regardless of policies, institutions, or geography'.

While the discovery on the miracle of manufacturing seems to be a good news for many aspired developing countries, the bad news is, it is more difficult to duplicate the success of the development pattern of these countries using industrial policy today. The predicaments are the effect of globalization and technological progress.

As Rodrik's (2018, p.90) argues, 'rapid global technological progress in manufacturing has reduced the prices of manufactured goods relative to services, discouraging newcomers in developing countries from entry'. The advancement of technology is making manufacturing more capital and skill intensive, and less labor-dependent. These factors, combined with increased trade from China and other exporters to the rest of the world, has suppressed the likelihood of poor countries to develop simple manufacturing. The reason is simple: why produce ourselves as we can get the imported goods cheaper in the market?

As a result of these combined forces, percentage of contribution from the services industry compared to manufacturing has increased over time. However, most of the service jobs created are from the low-end petty services. The development process without going through proper industrialization (which primarily propelled by manufacturing activities) is worrying as it has pulled the overall productivity downward. Premature deindustrialization has affected Brazil's manufacturing employment to peak at only 16 percent and Mexico at 20 percent, far from the early industrialized states of over 30 percent (Rodrik 2018, p. 90).

As more economic growth will come from the service economies, it is clear that it will be more challenging for policy makers to craft the future path of development. Do they have to focus on wider investment in human capital and education so that more quality service jobs can be created? How to have selective industrial policy when growth is now anchored on non-tradable services? Will the recent trade war between US and China unleashes the much needed domestic manufacturing potentials, hence rejuvenates the industrial policy tools?

CONCLUSION

It is not easy for states to win the game of economic development. Strong evidences have shown that in order to enjoy the fruits of development, states have to participate in the world capitalist economy. However, effects of globalization such as free flow of capital, disproportionate comparative advantages, profit-minded FDIs, restrictive movement of labour, and unfair trade practices are detrimental to domestic growth. If you run for help from the Bretton Woods Institutions – IMF, World Bank and WTO,

they will impose policy changes – often to further liberalize market and capital flow, which in turn are leaving states with even limited political and policy choice. In post-1998 Asia financial crisis and 2008 global credit crunch era, states are more aware that unconditional participation in neoliberalism world order will be self-damaging.

In fact, Chang (2014) argues that British and the US, the two strong advocates for free market and free trade, were the fervent users of interventionist industrial policy measures in their early age of development few centuries ago. Started in the fourteenth century, British protected its infant woolen textile industry through import tariffs. The government intervention was even stepped up in the sixteenth century when Robert Walpole, Britain's first prime minister, launched a wide-ranging industrial development program. 'It provided tariff protection and subsidies (especially to encourage export) to strategic industries' (Chang 2014, p. 60).

Likewise, Alexander Hamilton, the first treasury secretary of the US, argued that the government of an economically backward nation, such as the US (at that time), needs to protect and nurture 'industries in their infancy' against superior foreign competitors until they grow up (Chang 2014, p. 62). This protectionist policy lasted the next hundred years, until the Second World War.

History has revealed that both British and the US benefited enormously from their protectionist and interventionist approach of economic and industrial policy. However, once they have attained economic supremacy over others, they liberalized the economy and trade. Not only they have done so, they even impose free trade, liberalization and unfettered globalization to others for their own benefits. Chang (2003) claimed that this is a way of 'kicking away the ladder':

'The historical picture is clear. When they were trying to catch up with the frontier economies, the Now-developed Countries (NDCs) used interventionist trade and industrial policies in order to promote their infant industries'. 'If this is the case, the current orthodoxy advocating free trade and laissez-faire industrial policies seems at odds with historical experience, and the developed countries that propagate such a view seem to be indeed "kicking away the ladder" that they used in order to climb up to where they are' (Chang 2003, p. 13).

It does not matter on whether if it is done intentionally based on naked national interest or misinformed goodwill by some policymakers. Developing states have to be aware of this 'ladder-kicking' exercise, and do not fall into the persuasion and pressure easily. While it is important to connect with the world economy, blindly following the doctrine of neoliberalism policies might not lead to intended results. A mindful, selective and strategic integration that considers socio-political factors are crucial in ensuring better chance of success.

In a nutshell, it is important to allow states to have more maneuvering on policy choices and institution building. To 'win the game' of economic development, at the very least, states need to comprehend different interpretation of globalization, make more informed policy decision, and to have better understanding on the history of economic development.

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Contact email: e0304585@u.nus.edu