

The Long(term) and the Short(term) of the Asian Financial Crises

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INTRODUCTION

The Asian and Emerging Markets financial crisis of 1997–98 was the most serious global financial crisis since the Mexican default in 1982. Like Credit Anstalt’s bankruptcy in 1931, the collapse of the Thai baht triggered a chain of bank failures and currency collapses that threatened the stability of the entire international financial system. The panic culminated in the 1998 Russian bond default and the associated collapse of the hedge fund Long Term Capital Management. LTCM had roughly \$1 trillion of other people’s money under its management – \$1 trillion that included deposits from some of the same global banks that already had \$360 billion exposed in Asia and another \$480 billion exposed in other Emerging Markets. By way of contrast, in the 1982 Mexican default, developing country debt totaled only \$578 billion (in 1998 dollars), and the crisis never surged upward into global capital markets. Only successful crisis management by the US Federal Reserve Bank and other central banks unfroze the global financial system and prevented something like the global financial crisis that followed Credit Anstalt’s collapse.

The crisis was – and is – also serious for Asia and particularly the Asean group. The 1982 debt crisis caused a so-called lost decade of growth in Latin America, in which per capita incomes substantially declined. Immediately after the 1997–98 crisis it looked questionable whether growth would resume in Asia; now prognostications are more sanguine and the question is whether high-speed growth can resume. Still, this “rosy scenarios” suffers from a deficit of historical perspective. It also overlooks the ways in which the crises were both an outcome of increased nationalism in Asia and a cause for increased nationalism in Asia.

A comparison with the period 1890–1930 suggests that this is just the second (or third) in series of Asian booms and busts, booms that naturally raise incomes but do not markedly close the relative gap between the rich OECD countries and *most* Asian economies. This historical record also suggests that we should not expect a return to high-speed growth, understood as growth consistently at or above the 1980s–90s trend, at least in the medium term. Instead, a comparison suggests that rapid spurts in Asian growth have occurred when the developed economies are shifting from one set of leading sectors to another. During this shift, declining industries move offshore – most recently to Asia – while the emerging leading sector creates rising demand for new inputs. The barriers to entry in the production of declining industries’ products are low,

which means that much offshore growth is extensive, the probability of a financial crisis is high, and the prospect for sustained long-term growth is small. Historically, Asian producers have tended to crowd into similar product lines, leading to falling prices, financial crises, and slower growth. In the long nineteenth-century, colonial governments enforced this crowding, provoking nationalist responses from local elites and peasants who first resisted these transformations and then suffered from falling prices. In the late twentieth-century, nation building local states have driven this process, but with much the same outcomes.

This chapter thus presents a stylized comparison of the underlying causes for the 1997–98 Emerging Markets financial crisis, and compares it to the similar crisis at the end of the 1890–1930 period. Then it will assess the differing political environments driving Asian growth and industrialization in order to assess the medium term prospects for continued Asian growth. Asia at century's start and end displays eight superficial commonalities that rest on top of three broader structural similarities. These structural similarities generated both the prior and present crisis.

EIGHT COMMONALITIES

Both the current financial crisis and the earlier one have eight common superficial features.

- The general economic environment is one of rapidly rising world demand for new goods based on new technologies.
- The states managing Asian economies, whether colonial or independent, are determined to boost output and exports to capture part of this growing demand, so they borrow foreign capital directly, they mobilize local capital, and they encourage private actors to borrow capital from abroad. Despite this widespread desire for growth, only a handful of developing economies are actually successful: 9 countries represented 75 percent of Emerging Market exports both in 1913 and in 1997; Asian economies accounted for 47 percent of EM exports in 1913 (raw materials only) and 64 percent (manufactures only) in 1997.
- In the successful countries large scale foreign investors (large in terms of investment, large in terms of scale and modernity of production, large relative to local firms) stimulate thousands of local producers to begin producing as well,

sometimes as suppliers, sometimes simply by bringing into being the service networks firms need to produce and to export.

- The combination of foreign and local investment allows local production to supply a good part of rising world demand, leading to rapid expansion of Asian exports. However, unlike the rest of the “Emerging Market” economies (which also increase exports), there is also a high component of ‘intra-Asian’ trade, leading to deepening economic integration via a modest increase in intra-industry trade.
- A flow of migrants both complementary and consequent to the rising intra-Asian flow of goods begins. This rectifies labor shortages in new production zones, but also produces rising ethnic tensions between established populations and newcomers.
- Part of this flow is a flow of Chinese persons *and* capital. This flow provokes local hostility towards Chinese populations and often a de facto apartheid.
- Overlaying these economic flows is a decade or longer long ideological and real (that is, investment-based) struggle between the Anglo-economies and Japan over what constitutes the proper growth model for Asia, particularly in terms of how China shall be integrated into world markets. As for China, it represents a rising but fragile power.
- Finally the proximate cause for the crisis is overproduction of Asian goods, leading to falling prices for those goods in world markets, difficulties servicing public debts, default on some private debts, and a severe contraction of Asian imports of goods from the rest of the world as capital inflows temporarily cease.

Now this is a broad brush picture, so it could be argued that at this level of generality maybe the strokes are so broad that everything looks alike. However, these broad similarities reflect the operation of three similar fundamental structural conditions in each era. One economic and one political structural condition each derive from the difficulties of late industrialization. Late industrializing economies require sustained increases in exports to generate the sustained increases in productivity needed to catch up with more developed economies. Late industrialization thus has also always required local states that were willing to coordinate investment by local firms and

solve some of their collective action problems around the skills formation for workers, the acquisition of new technologies and their entry into new markets. These states have historically always justified this intervention on nationalist grounds. The third structural condition derives from the differing opportunities for export created by the political organization of global markets by the current hegemonic power; put simply, some hegemonic powers historically have been more open than others to large export streams from developing economies. The first two differed somewhat in each era, but the third diverged considerably.

STRUCTURAL FEATURES

How did these three structural conditions generate the common features of these two financial crises?

Long-term development in late industrializers requires above average increases in productivity. Historically, sustained development with rising *relative* incomes has only occurred for countries that generated large export streams. Successful late development almost always requires large export streams because, as Verdoorn's law tells us, high rates of productivity growth generally emerge from rising rates of growth of output as firms struggle to overcome bottlenecks and limiting factors, and in doing so learn more efficient production techniques (Kaldor 1996). Exports allow a developing economy to overcome the barriers to large-scale production presented by a small domestic market. If late developers export goods with only average increases in rates of growth of output (and thus often of demand) those late developers will experience only average increases in productivity. As a result the economy more or less stays in the same place relative to everyone else. This is not a bad thing, but it is not the kind of huge leap taken, for example, by Japan, or even South Korea, both of which generated enormous increases in exports that in turn forced the reorganization of the production process and generated massive increases in productivity and income (Amsden 1990).

Large increases in productivity are a prerequisite for sustained growth. If you export goods with low barriers to entry at average rates of growth of both production output and productivity, you face declining prices, because others can enter your markets with equal ease. By definition most late industrializers will export goods with low barriers – otherwise how could

they jump into the market?¹ Consequently, the substantial increases in exports associated with late development tend to be fratricidal: it is impossible for everyone to experience success, because the very existence of successful countries creates less successful ones stuck in low-value-added, commodity like exports. Thus in the nineteenth-century Japan's rapidly growing exports of silk and tea constricted Chinese exports of the same products. It did not displace them, but it slowed their rate of growth, and thus limited the contribution China's two largest exports could make to growth. Japan's rapidly rising silk exports, in contrast, spurred innovations in silk processing and sericulture, and in service industries linked to silk.

Second, local political structures also tend to generate crises. Historically successful late industrialization has required massive state intervention to concentrate capital for investment. This can be done unpleasantly, as when the state squeezes the peasantry through taxes and rigged markets, or more pleasantly, as when the state loans its creditworthiness to local, otherwise uncreditworthy borrowers. Historically, would be late developing states in nineteenth-century Europe and Japan and twentieth-century Asia and Latin America channeled this capital to productive investments; protected local markets from foreign firms; acquired production and product technologies; and marketed local production abroad. There is not much difference between the two centuries except the rising degree of intervention and the sophistication of the tools. The goals and activities of the nineteenth-century Prussian state firm, the *Seehandlung*, are virtually indistinguishable from those of modern trade promotion organizations like KOTRA or CETRA. Similarly, the tools predatory colonial states in Indonesia, Korea or Indochina used to squeeze peasants did not differ much from those used by independent governments in Taiwan and South Korea later in the century, even if the reasons for squeezing the peasantry differed.

Late industrialization thus typically involves considerable risk of overcapacity as the state encourages businesses to pursue economies of scale and the use of the latest, most efficient production equipment through various guarantees on investment in capacity ahead of existing demand. But this mobilization of investment capital by the state, and the implicit guarantee that the state will bail out investors who get themselves into trouble, means that much investment takes place that will not be validated by the market. Losers from fratricidal battles over market shares in world markets thus tend to be saddled with excess capacity and a low rate of profit, which further depresses growth prospects and future investment. It also threatens the capital that

has been invested in these export sectors and the service sectors that support them. This tends to create overcapacity, falling prices, and rates of return too low to sustain future investment. While states can overcome these tendencies by offering even greater investment incentives, this simply magnifies the risk that unsustainable levels of capacity will be created.

Why would states persist in the pursuit of excess capacity? Historically, states attempting late industrialization have done so for geopolitical reasons, and because they have strong support from extant or would-be industrialists in their economies. External threats and domestic actors seeking concentrated benefits (that is, rents) are sufficient explanations for late industrial strategies.

The sacrifices that these strategies entail are also almost always justified by appeals to nationalist and/or progressive visions of the future – indeed they almost always blend both elements into an allegedly “unique” local pathway into modernity (Gerschenkron 1964). These appeals are a necessary part of the development process, because the counterpart to the mobilization of capital is the mobilization of peasant populations as a new industrial labor force, the mobilization of peasant savings for investment in industry, and a reduction of landlords’ control over both peasant bodies and peasant savings. Not surprisingly peasants and landlords everywhere have responded to these efforts with hostility, open rebellion, and appeals to ‘traditional’ national values. Japan, after all, endured nearly 200 peasant uprisings and five samurai rebellions after the Meiji restoration, and participants on both sides justified their actions with reference to traditional national values. In other Asian countries the state’s mobilization of savings has also had as one of its goals the creation of what is perceived of as a “truly” national bourgeoisie, that is, one that is not composed of immigrant entrepreneurs. Thus the Malaysian and Indonesian states have tried to forge a bumiputra elite in the process of creating a local capacity for growth. Nationalism – understood first as a quite reasonable fear of foreign occupation or economic colonization – is thus a spur to and justification for economic transformation at the same time that traditionalism is a response to the dislocations of industrialization. But both forces lead states to pursue industrialization at all costs, including the creation of overcapacity.

Finally, external politics also creates structural conditions that reinforce the tendency towards excess capacity and financial crisis. Late developers have always depended on growing

external markets. While expanding Asian markets did historically help industrialization in Asia in the nineteenth-century, the ultimate motor of growth was located outside Asia in the developed countries. Can twentieth-century Asian markets as a whole substitute for a rapidly growing Japan, US, European market? The historical record suggests not, especially for China. The problem with this reliance on external demand is that the large export streams associated with late development tend to provoke protectionist responses in the developed countries that by definition must absorb these exports (because they have the money). By limiting potential demand, protection tends to depress world market prices in the face of supply surges.² Lower prices and smaller volumes in turn depress growth rates in late developers, and again, threaten the capital that has been invested in production and in infrastructure to support production.

Now let's go back and look at each episode of rapid economic growth in Asia to show that Asian growth is likely to remain at trend, rather than continuing to be "miraculous."

THE LONG NINETEENTH-CENTURY BOOM

New leading sectors and export demand

At the end of the nineteenth-century the European and US economies began a period of relatively rapid growth based on the emergence of a new set of leading sectors clustered around industrial chemicals, bicycles (and later the internal combustion engine), and the electricity industry, and on the consolidation of the prior wave of growth based on steel and standardized machine tools. The expansion of these new leading sectors in European economies also spurred expansion of Asian agriculture and industry two ways.

Rising demand for raw materials directly linked to the new industries was the first spur to expansion. The emergence of the electrical industries and of bicycling massively increased demand for rubber for insulation and tires. In Malaysia alone, the number of hectares planted under rubber bounced from 2400 in 1900 to nearly 220,000 in 1910. Roughly the same processes occurred because of food canning (an electrically driven continuous flow processing industry), which required tin, sugars and standardized vegetable oils, and through continued urbanization, which required more petroleum for domestic lighting. Later the motor industry would consume enormous volumes of petroleum and rubber. The increasing volume of continuously run

machinery itself required more lubrication, which palm and mineral oils provided.

Urbanization constituted the second spur to expanded Asian exports. The workers filling northwestern Europe's new cities had tenuous links to the countryside. Their diet shifted towards imported foods and drugs. Sugar already provided an estimated 20 percent of the average Briton's calories by 1900, and this diet spread to the rest of Europe. Consumption of tea, margarine (generally made from palm and coconut oils), coffee, tobacco also boomed. By 1913 roughly half of Asian exports were raw materials of one sort or another, much of which went to Europe.

Most of these new Asian exports to Europe came from plants introduced to or transplanted within Asia. Rubber in Malaya, tea in northeast India (Assam) and Sri Lanka (Ceylon), and (some) systematically cultivated palm and coconuts almost always occurred in new monocultural production zones, with Indonesian sugar being an important and salient exception. New mining ventures, such as tin in Malaya, also tended to occur at some distance from traditional areas of settlement. Even old crops grown for export, like rice, generally came from newly pioneered areas, like Cochin China in Indochina, or the plain east of Bangkok. This is not to say that settled peasants did not add some crops to their portfolios, but that these exports predominantly came from new lands.

Because new production zones involved large investments to create infrastructure and tide producers over until production came on line, they tended to be developed either by vertically integrated European firms engaged in plantation agriculture (for example, Unilever or Lipton), or by Chinese capital dominating newly settled peasant producers. In the former case, the scale and organization of export production dwarfed earlier imperial efforts. The latter case presents more continuity. In both, however, the speed at which new supply emerged was historically unusual.

Labor migration

Because these exports came from newly pioneered areas, they also involved substantial migrations of both labor and capital. Labor for these new production zones came from displaced peasants turned into indentured or migrant labor, and from migrants trying to turn themselves into freeholding peasants. About 50 million Indians and Chinese moved in the nineteenth-century. Tamils went as indentured servants to Ceylon and Malaysia; other Indians went to frontiers in

northeastern India, Africa and the Caribbean. Southern Chinese went to Vietnam, Indonesia, Africa, Malaysia and parts of the new world. About 1 million Japanese and perhaps as many Filipinos went as indentured labor to Hawaii, the US and Latin America. Vietnamese migrated south to Cochinchina, displacing Chams. At least 360,000 Javanese went as indentured labor to the outer islands, and as many as another 5 million voluntarily migrated to pioneer the coasts of Sumatra and Borneo.

Chinese Capital

Chinese also migrated as “capitalists,” or more precisely as merchant intermediaries between peasants in the new production zones and wholesalers in areas of new demand. Thus in Indonesia, Indochina and Thailand, Chinese lenders financed new rubber and rice production, while also handling marketing of the harvest. Chinese lending and control over distribution naturally enough evoked peasant hostility, except where Chinese migrants themselves constituted a substantial portion of the new peasant settlers, as in Thailand. Elsewhere this hostility allowed colonial governments to segregate the Chinese for their own “protection,” assuring continued hostility. In the Dutch East Indies, for example, the Chinese population rose from roughly 340,000 in 1880 to 1.2 million in 1930. Over one-third of this population was engaged in commerce, and another fifth in skilled occupations (Furnivall 1944: 240-242, 408, 412). Chinese merchants were particularly important in funding timber and sugar production outside Java, as well as rice production in Cochinchina.

Intra-Asian trade

These migrations in turn created a rising internal demand for Asian exports of foods and manufactures for the proletarianized labor forces that provided most of the commodities exported to extra-Asian markets. Ex-peasants and new settlers working full-time for money incomes turned to the market to buy food and manufactures they previously had made for themselves or in subsistence economies. New rice production zones in Thailand, Vietnam, and Bengal emerged, adding to demand for manufactures by enlarging incomes there. Rice imports into the Dutch East Indies grew from fl.12 million in 1880 to fl.104 million in 1929 (Korthals Altes 1991: 118, 127). Thailand’s rice exports tripled from their average 1870s levels of 163 million tons to 487 million

tons by the 1890s, and tripled again by the 1920s to 1,345 million tons; Burma's rice exports rose from about 29 million rupees in 1872-73 to 218 million rupees by 1926-27. Virtually all of this rice went to other Asian countries, including the emerging cities of Singapore and Hong Kong, as well as new production zones for tea, tin, palm and rubber in India, Ceylon, Malaysia and Indonesia.

Rising intra-Asian demands for consumption goods also spilled over into manufactures. Consequently, the Japanese, Indian, and Chinese textile and garment industries all expanded to satisfy this demand, although local industries also supplied a substantial portion of demand. Thus, again, in the Dutch East Indies, cotton goods imports grew from fl.36 million in 1900 to fl.100 million in 1925, while local production was minimal until the 1930s. In Burma, by the 1920s, roughly 38 percent of imports were food, clothing, and household goods for the local population, and these came almost exclusively from Asian sources. Another 25 percent were capital goods, corresponding to European imports (Furnivall 1948: 189-91).

When all was said and done, roughly half of Asian exports remained inside Asia – and for some countries, the proportion of exports going to other Asian destinations was substantially higher than it is today. Parts of this expanding Asian market remained the preserve of European firms: capital goods like rail and oceanic transport, colonialists' own consumption, bibles, etc. Nonetheless, a huge market segment remained untouched by European producers.

This segment catered to local consumption and involved goods that European firms could not profitably produce in Europe for Asian markets. Asian producers, particularly the Japanese, jumped into this market segment. One Japanese scholar precisely marks the divide between the European and Asian textile markets as cotton textiles with thread counts above about 25 and those below (Kawakatsu 1986). Higher thread counts denote fineness and quality. European, especially British textile producers in search of higher profits, systematically moved up-market into higher thread counts at the end of the nineteenth-century. They abandoned the lower ranges of the market to Asian producers in textiles and other household goods.

When "European" firms competed in this product range, they did so by locating production in what we would now think of as "export processing zones" (EPZs). These emerged first in India and then in China. In both countries production was highly concentrated. India's "modern" textile industry was located primarily in Bombay, where cloth output seems to have

increased by 7.7 percent per year from 1897 to 1913. China's was located in Shanghai, where 48 percent of spindles and 56 percent of looms were foreign owned by 1936. Most of this production occurred inside "concession" areas governed by European law. Only Japan developed a substantially locally owned cotton textile industry, although its growth lagged India's at 7 percent per year. This industry was able to subordinate Asian production of raw materials to its own needs, absorbing a significant proportion of India's output of cotton yarns and investing in the Shanghai "EPZ" by the 1920s.

This intra-Asian demand for manufactures did spur broad industrialization in Asia, and distinguishes Asian export led development from contemporaneous export led development in Latin America, Africa and most of Eastern Europe. India's large-scale industry (centered on cotton textiles, jute, wool, paper, beer and iron) expanded at about 4 to 5 percent per year. By 1914 India had the fourth largest cotton textile industry in world by weight, because of the predominance of coarse cloth. Similarly, foreign capital industrialized China and especially Shanghai. By 1936 half of Chinese coal output and one-third of financial capital was foreign owned. Total foreign production amounted to approximately 2.5 percent of GDP, and foreign direct investment (FDI) amounted to \$2.6 billion in 1936, or roughly \$50 billion in 1998 dollars. Elsewhere, industrial growth largely occurred in sectors backlinked to agricultural exports. Thus sugar refining dominated Indonesian industry until the crisis of the 1930s spurred local textile and metals production.

Export volumes grew rapidly because European demand for Asian exports dynamized *intra*-Asian trade, and because the barriers to entry for most of intra-Asian trade were quite low. In many cases peasants could simply shift production from one crop to another; and when they didn't, European and Chinese capital was willing to coerce/induce them to shift. In Indonesia, peasants rapidly displaced plantation production of rubber, sugar, and tobacco in the 1900s, and Burma and Thailand family farming peasants grew rice for export. These peasants achieved quite high rates of growth of output. In Indonesia, where all export production rose about 5 percent per year, 1893 to 1928 (and 4 percent per year, 1893 to 1938), peasant production grew even more rapidly at 7.5 percent per year (and 6.6 percent). This permitted the peasant share of export production to triple from 12 percent to 37 percent (Booth 1989: 83). Because peasants were particularly responsive to high prices, and because barriers to entry were low, any upswing in

prices induced peasants to commit thousands more acres to production, leading to soaring production, which soon produced falling prices. The biggest jumps in Indonesian smallholder rubber output occurred just after the 1907 and WWI price peaks - and these big increases in supply then contributed to price declines.

States and the economy

Local states, including the colonial ones, abetted and encouraged this increased production. A mixture of benign and malign motivations drove them to increase investment in social overheads that agriculture needed. Like peasants, states also interpreted rising prices as an opportunity to harvest gains from export expansion. States pursued mercantilist policies designed to generate ‘internal’ sources of supply of strategic or marketable goods, like petroleum, tobacco, sugar and rubber. Ready markets for these goods meant they could directly and indirectly generate revenue that offset trade deficits that metropolitan economies ran with other developed economies, particularly the United States. In 1929, for example, Europe and Japan had a total merchandise trade deficit of \$1350 million with the United States. They partially offset this with the cumulative \$610 million merchandise trade surplus that their colonies had with the United States. To take an earlier year at random, 1906, India, Ceylon and the Straits Settlements had a \$63 million merchandise trade surplus with the United States. The importance of India in Britain’s balance of payments is well known, but Indonesia occupied an even more important place in Holland’s. And both before and even more strongly after World War I, colonial governments began pursuing “ethical” policies designed to damp down rising nationalist movements by spending more on education and infrastructure. Investment designed to expand and upgrade tropical production increased the public debt imposed on Asian economies by their colonial governments (Table 1 presents data for the end of period).

Table 1 Public Foreign Debt Outstanding as a Percentage of National Income and Exports

National Income		Exports	
Early 1920s	Late 1930s	Early 1920s	Late 1930s

Indonesia	23	47	79	174
India	14	21	128	208
Japan	9	5	71	46
Thailand	–	7	68	28
For comparison:				
Argentina	–	10	37	77
Egypt	–	48	159	263
Canada	01	14	64	85
Australia	54	70	288	397

Source: Anne Booth, “Evolution of Fiscal Policy,” in Booth 1990: 237.

Debt and prices

At the same time, virtually all peasant producers were indebted to Chinese and other middlemen or to land speculators (for example, chettyars in Burma). Data on informal lending by Chinese and similar middlemen is not available. But formal institutions lending to agriculture in the Dutch East Indies expanded their paid up capital, and one must presume lending, from fl.72.1 million to fl.274 million 1900 to 1930, matching the increase in export production (Furnivall 1944: 335). In Burma, about £50 million had been advanced to agriculture by the 1920s. Peasants thus were vulnerable to any downswing in prices, especially since they typically borrowed at the peak of the price cycle. This made them more likely to try to borrow and be permitted to borrow more than was prudent. There were several such small price cycles in the period 1870-1914, with the largest being the upswing in prices from 1890 to 1905, but World War I produced a massive upswing in prices that in turn produced an equally massive fall in prices in the 1920s.

Peasants could have ridden out these price falls if they were able to rapidly increase productivity. But what is striking about the massive increase in peasant output is how limited productivity gains were; most growth was extensive. For example Thai and Javanese rice output per unit of land was fairly static through the late nineteenth and early twentieth centuries. Rubber output per unit land in Thailand, Ceylon and Sumatra – all peasant cultivation – was also fairly static. Indonesian sugar output per acre doubled from 1870 to 1900, and Indonesian per capita incomes seem to have risen about 2 percent per year from 1900 to 1930. This is not bad, but it is not exactly miracle growth. The contrast with export production, which grew at twice the rate, is

striking and suggests that much of the increase in output came from extensive growth – bringing wasteland into cultivation, shifting from swidden agriculture to settled cultivation, and working more hours.

Low barriers to entry and soaring, state sponsored production left local producers vulnerable to falling prices for their goods. And prices did fall, fairly consistently from the late 1890s onwards. By 1913 most tropical exports were down about 10 percent from their nineteenth-century highs. From 1913 to 1925, terms of trade fell for Indonesia, Ceylon, Taiwan, and the Philippines (though less severely there than for the others). Since so much of the population was involved in exporting (in outer Indonesia, for example, 20 percent of peasant income was from export crops), these price falls certainly hurt the peasantry, particularly as colonial governments tried to block the import of cheap consumption goods (primarily from Japan). Peasants thus were squeezed between falling prices and fixed debt in the 1920s and 1930s.

The Depression drove prices down even farther, producing a 21 percent drop in export and import values across Asia. Some commodities, like rubber, suffered 90 percent declines in price despite only small declines in volume. Falling export revenues meant falling customs revenues for states that had modernized their tax base away from product monopolies and crude land taxes in kind, towards customs and revenues from state infrastructure enterprises. Like peasants, states suddenly found themselves with large debts at very high real interest rates. Virtually all Asian economies were run by colonial governments that would not permit defaults on public debt (though what happened to private debts owed to Chinese lenders is unclear). These governments simply increased tax pressure on their subject populations. In Indonesia the state took over responsibility for 90 percent of exports – and prioritized imports from Holland to the detriment of cheaper Japanese imports. The same occurred in India. In both countries this hurt local producers, for whom falling prices all round might have canceled out some of the effects of the depression. Ultimately only wartime inflation eliminated both debts and (temporarily) the problem of falling prices for raw materials.

Can we tell a similar story for the more recent financial crisis?

THE LATE TWENTIETH-CENTURY BOOM

The Asian economic boom of the late twentieth-century presents the same features and dynamics and the earlier one. As in the nineteenth-century, rising demand for Asian produced goods in the United States and, to a lesser extent, Japan, pulled Asian economies along. The interaction of very intrusive Asian state policies supporting industrial development with the particular kind of trade protection the US state offered to its threatened domestic industries rapidly dispersed industry across Asia. In this respect, state policy bears more on the ultimate outcome than it did in the long nineteenth-century. The rapid expansion of industrial production in Asia induced an equal rapid influx of foreign capital. This influx was magnified by changes in US monetary policy taken with an eye towards domestic concerns. Nonetheless, as with nineteenth-century agriculture, the expansion of Asian industrial output largely created a capacity to produce low-value-added, commodity-type goods. Prices for these goods fell through the 1990s, putting pressure first on China, then on Japan, and finally on the Asean economies to devalue their currencies so as to maintain macroeconomic balance. Devaluation of the Thai baht, of course, proved the proximate trigger for the crisis. But the underlying problem of overcapacity in core Asian exports was already visible in the early 1990s. How did US and Japanese production models interact to expand and disperse industrial production in Pacific Rim Asia?

New leading sectors and export demand

The emergence of both a new leading sector – electronics – and a new production model for the old mass production, assembly line leading sectors – the Japanese combination of just-in-time production and state investment coordination – pushed US firms overseas in search of cheaper labor than they could find at home. US-style assembly line production and its associated unions of semi-skilled workers created very tight labor markets in the US, which both pushed up wages and compressed wage structures through the late 1960s. Labor-intensive industries like garment assembly and textiles found themselves unable to compete against new producers in low wage areas, whether those new producers were in Japan or in the newly industrializing US South. Textile and garment producers adopted a two-pronged strategy to deal with their declining profitability. They dispersed themselves to the south, and they sought trade protection from

Congress.

At roughly the same time, the newly emerging electronics industry also found itself unable to compete for low-skill workers. But because its production process was easily segmented in time and space, it voluntarily went offshore to low wage production zones in Mexico and Asia. Later in the 1960s, as Japanese firms began to penetrate US markets for low-end electronics, this industry also pressed for trade protection.

Both industries had high wage costs relative to productivity when compared with Japan. But both industries also misdiagnosed their problem as one of very low Japanese wages, rather than rapidly rising Japanese productivity. Neither industry therefore opted to revitalize their own production process, and instead both pursued protection and dispersion. Their pursuit of protection interacted with the Japanese production model to spread new industries across Asia.

The Japanese state's coordination of investment and suppression of consumption are more important to our analysis than the just-in-time aspects of the Japanese production model. From the 1950s on, much as in any other late developing economy, the Japanese state deliberately suppressed domestic demand and used the financial system to channel capital to industry. Deliberate use of capital controls to maintain low interest rates combined with meager public pensions to induce very high levels of private savings. The state directed these savings into targeted industries, inducing investment by offering over and covert forms of protection. Protection and directed investment then induced Japan's *keiretsu* (business groups) to over-invest in targeted sectors. Because each *keiretsu* sought market share in the sectors the government targeted, they all rushed into each sector with massive investments. Given a constrained domestic market, over-investment created overcapacity, which naturally poured into world markets as exports. These exports surges tended to focus on the US market, which then, as now, was *relatively* open to imports.

Because the Japanese state protected domestic markets, sopped up domestic savings, and controlled the exchange rate against the dollar, the accumulation of dollars and of trade surpluses by the end of the 1960s did not produce a corresponding rise in the yen or in Japanese imports. Instead, the Japanese government sterilized its rising hoard of dollars by turning them into US Treasury bonds. This was a sustainable policy only so long as the US accepted a rising bilateral trade deficit with Japan. For domestic political reasons this proved periodically untenable, and the

US then set limits on specific Japanese exports to its market.

If low wages pulled some US firms to Asia, the US limits on Japanese exports pushed Japanese industry to disperse to Asia. In order to comply with the ban on bilateral quotas in the General Agreement on Tariffs and Trade (GATT), the US requested voluntary export restraints (VERs) from the Japanese. These VERs set very detailed limits on the volume of specific commodities exported from Japan to the United States. For example, the first VER in 1955 limited Japanese exports of cotton garments. Naturally enough, Japanese firms and their state sought to evade the quotas in legitimate ways. They pursued three avenues. First, since exports of cotton garments were limited, they upgraded their production to synthetics and wool. Second, since exports of cottons from Japan were limited, they shifted production to nearby low-wage export platforms, like Hong Kong, Taiwan, and South Korea. Finally, since exports to the United States were limited, they exported more to third party markets.

Dispersion then created a self-sustaining dynamic. As cotton garments flowed from the new production sites in the first tier of Asian newly industrializing economies, the US imposed VERs on their exports, forcing further dispersion, upgrading and diversion. This created the so-called ‘flying geese’ pattern, whereby lead goose Japan developed and then shed steel, consumer electronics, cars, and DRAMs to follower geese Korea and Taiwan, which in turn shed clothing, shoes and low-end consumer electronics first to Asean and then to China. Tables 2 and 3 show how the newly industrialized countries are specialized into these various products.

The flying geese pattern contained an internal tendency towards over-investment and over capacity. Because VERs forced industries to relocate before they fully depreciated their capital, VERs created multiple production complexes. Also, the most promising sites for investment were economies in which the state deliberately emulated the Japanese model of late development via state coordination of investment. However, US policy choices over inflation and the dollar’s exchange rate aggravated this pattern. When the Reagan Administration engineered the fall of the overvalued dollar in 1985, this placed Japanese policymakers in a difficult position. One-third of Japanese economic growth in the 1980s had come from exports

Table 2 Shares of exports of specific products in total merchandise exports of selected NICs, 1997, percent

	Automotive	Textiles	Garments	Office	Agricultural	Total
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				machines & Telecoms	products	Merchandise exports, \$ bil.
Argentina	7.1	—	—	—	53.1	25,516
Brazil	9.2	1.9	—	2.0	34.5	52,987
Mexico	18.0	1.6	3.9	15.6	—	110,432
China	—	7.6	17.4	11.8	8.6	182,697
Taiwan—	10.4	—	32.5	—	—	121,850
South Korea	9.0	9.8	3.1	24.9	—	136,164
Hong Kong	—	6.0	34.2	18.9	—	27,306
reexports	—	8.1	8.6	20.2	—	160,889
Singapore	—	0.3	0.6	57.5	—	72,411
reexports	—	1.9	2.0	43.8	—	52,584
Czech Republic	9.1	4.4	2.7	2.3	—	22,775
Hungary	5.6	—	5.9	15.7	16.0	19,100
Poland	5.1	2.5	8.6	3.2	14.7	25,750
Spain	24.9	—	1.1	3.3	15.9	104,277
— insignificant						

— insignificant

Source: WTO 1998.

Table 3 Share of Selected World Exports by Commodity (SITC code), %, 1997

	China	Indonesia	Korea	Malaysia	Philippines	Taiwan	Thailand
Baby toys (894)	24.9		1.4	1.0	0.5	8.0	1.5
Crustacea (036)	5.2	7.2			1.2		12.9
Footwear (851)	22.2	4.0	2.0		0.5	2.0	2.0
Radio receivers (762)	18.7	2.8		9.1			
Rubber (231)		28.9		20.4			35.7
Synthetic Fabrics (653)		8.5	2.8	19.5	1.4		9.9
Transistors (776)	1.0		10.1	7.5	4.5	6.3	1.9
Vegetable oils (422)		26.7		44.8	8.3		
Veneers (634)		21.6		11.7			

Source: International trade Center database, <http://www.intracen.org>.

to the US. Unable to continue their traditional export-led growth model, Japanese policymakers were forced to choose between doing nothing and suffering recession, or, as the Maekawa report urged, opting for some kind of domestically-led growth model. They naturally opted for the latter, and the central bank allowed interest rates to fall to 2 percent. But this policy choice did not produce a US-style, consumer led, domestically oriented economy, per Maekawa, because none of the fundamental institutional structures were changed. Rather than consumer-led growth, low interest rates generated company and investment-led growth. Emboldened by low interest rates and rising consumer spending, companies embarked on a huge investment spree. Locally this produced the “bubble economy,” as equity and land prices quadrupled in six years; the accompanying construction boom encouraged even more investment and speculation. Japanese firms also went overseas, creating production complexes in the United States and, to a lesser extent, Southeast Asia. Because of the bubble, they did not shut down production capacity in Japan. So these new investments magnified the overcapacity already created by US VERs.

Labor migration

Labor flows in the late twentieth-century were more modest than in the nineteenth-century. Nationalism, decolonization and the ethnic tensions produced by prior waves of migration made governments more sensitive to large inflows while deterring many would-be migrants. Nonetheless, a massive internal migration occurred in China, with as many as 80 million workers flowing first into new production zones in Guangdong province and other special economic zones, and then into cities more generally. Production workers also flowed from Indonesia into Malaysia and Thailand, and within Indonesia into EPZs in areas proximate to Singapore. In 1994, for example, a Malaysia amnesty for illegal immigrants registered nearly 500,000 migrants, suggesting that the real level of migration was much higher (UNESCO, 1997).

Chinese

The salience of Chinese capital in the Southeast Asian boom also need not be elaborated much. As early as 1986 to 1990, 30 percent of FDI in the Asean economies came from the Asian Gang of Four – Hong Kong, Taiwan, Singapore and South Korea – as they offloaded industries facing VERs onto lower-waged Asian economies. These countries maintained their share in the

1990s, although the use of Hong Kong to disguise the return of capital originating in mainland Chinese complicates the picture. By 1990, local ethnic Chinese accounted for as much as 65 percent of private capital in Malaysia, 40 percent in the Philippines, 80 percent in Thailand, and 80 percent in Indonesia (Hatch and Yamamura 1996: 82).

Intra-Asian trade

As in the nineteenth-century, all this investment created dense networks of intra-Asian trade, although again as in the nineteenth-century demand from outside the region energized this trade. Quite complex industrial production networks emerged on top of traditional flows of foods and raw materials. By the early 1990s 40 percent of Asia's exports of manufactured goods went to Asian destinations, exclusive of Japan, which absorbed an additional 10 percent. In any case the so-called "China circle" of production links is probably denser than it was in the nineteenth-century (Naughton 1997; Hatch and Yamamura 1996).

States, the economy, and Nationalism

As in the nineteenth-century, local states abetted the emergence of overproduction. Appeals to national pride, "Asian values" and a general sense that Asia's century had arrived glossed over substantial dislocation of peasant populations. These appeals justified the targeting of industrial sectors perceived as especially salient to the development process or especially important for establishing that an economy had arrived in the ranks of the developed economies. Everyone thus pursued textiles, toys and household goods exports as an easy way to generate foreign exchange to pay for the capitalization of the more impressive automotive and electronics sectors. The relative success of the Japanese model, which involved the deliberate creation of overcapacity, legitimated these state activities despite pressure from US dominated policy institutions like the IMF and World Bank. Thus the Malaysian and Indonesia governments actively expanded local automobile production, while the Thai government acquiesced in new or expanded factories by six multinational automobile firms. Little of this increased production was able to generate export sales outside the Asean region. Asian governments funded this investment by committing a huge share of domestic production to fixed capital formation: 43 percent of GDP in Thailand 1992-1995; 36 percent in Singapore and 37 percent in Korea.

Paradoxically, Asian states' ability to finance this investment dramatically increased after the bursting of the Japanese bubble. The Japanese investment boom from 1988 to 1990 created excess capacity equal to between 30 and 50 percent of projected consumption in core Japanese industries like semiconductors and electronics. Overcapacity increased Japanese firms' desire to protect their domestic market while pouring excess production into world markets. Car, semiconductor, and color TV exports all rose about 16 percent 1989 to 1992. But this export drive ran headlong into a US administration elected on economic issues, and a Federal Reserve Bank trying to save the US financial system from the effects of recession. Consequently the Clinton administration allowed the dollar to fall to historically low levels against the yen in order to blunt Japan's latest export drive. The Fed abetted this fall, dropping its discount rate to 3 percent in 1992/93. By 1995 the dollar bought between 80 and 90 yen, rather than the 150 it had bought in 1990. This second *endaka* (high yen shock) certainly had its intended effect on Japan's exports of cars, home electronics, cameras and precision machinery, which all fell by roughly half between 1992 and 1996.

Because Southeast Asian currencies were pegged against the dollar, the falling dollar made it more profitable to export from Southeast Asia than Japan. Despite overcapacity at home, Japanese firms increased their investment in Southeast Asia. This produced booming economies, which drew in more US and then European capital. And as US interest rates fell, the Southeast Asian central banks had to lower their interest rates to keep their currencies pegged against the falling dollar. The money supply began expanding in the Asean economies at 25 to 30 percent annual rates, following export growth rates of 20 percent per year. Falling interest rates, 25 to 30 percent annual increases in the money supply, and the increased attractiveness of Southeast Asian sites for exporting to the United States set off an extraordinary investment boom both in Southeast Asia and the other emerging markets. Asian fixed investment, net of that in Japan, went from 6 percent of total world investment to 18 percent 1990 to 1996. A good quarter of that, on average, came as foreign investment, through private foreign direct and portfolio flows totaling \$420 billion. Where investment in Southeast Asia nearly tripled in those six years, investment in Japan and the United States grew only 40 percent and in Europe only 10 percent. Overall, private capital flows to the emerging markets nearly doubled, 1993 to 1996, from \$175 billion to \$328 billion.

There were three problems with this investment. First, while Southeast Asian states largely agreed with the principles of the Japanese growth model, they deviated from its practices. States proved unable to *consistently* direct investment into productive capacity and to *consistently* discipline local firms into upgrading production. Instead, especially in the MIT economies (Malaysia, Indonesia and Thailand) and Hong Kong/south China, states let local banks (often run by cousins or political allies) borrow in foreign currencies and relend the money in local currency terms to investors in property based ventures like hotels and office buildings. In the MIT economies roughly a third of foreign funds went into this sort of venture. These projects carried enormous *potential* foreign exchange risks because by their very nature they could only earn local currencies while their liabilities were foreign currency denominated. But because everyone believed that these states would maintain their peg against the dollar, they were willing to also believe that this risk did not exist; if pegs held, and the continuing inflow of foreign cash seemed to imply they would, then the local currency earnings of these speculative ventures could always be turned into dollars for repayment. This delusion took extreme form in nationalist *folies de grandeur* like Malaysia's PETRONAS Twin Towers, or the Suharto government's decision to license a joint venture in automobile production between Hyundai and the politically well-connected Bimantara Citra Mobil Nasional. The second problem was that much of the portfolio investment occurred as short-term loans. Short-term loans exceeded foreign reserve holdings in Korea (by a factor of 3:1), Indonesia and Thailand, and were 60 percent of Malaysia's. These loans could be easily rolled over if money kept flowing in, but if it did not, it could easily provoke a financial collapse.

Third, most important, this investment largely produced only extensive growth; that is, the Southeast Asian economies, and to a lesser extent Korea, simply generated massive overcapacity in basic industries, turning not only textiles, toys and household goods into low-price commodities, but also low-end electronics, cars, and car parts. As production ramped up across Southeast Asia, especially China, from 1990 on, terms of trade apparently fell for all countries except Singapore and Taiwan. Here China appears to have played a critical role in depressing terms of trade by 20 percent for the MIT economies. In short, nationalist drives for industrialization had turned into a three cornered fight between Japan, China and Asean as a whole. Like their nineteenth-century predecessors, these brave new industrializers needed to

export greater and greater volumes of goods to pay back a given volume of debt and thereby validate both their investments and their political regimes, but greater exports only drove prices further down. And if these basic productive enterprises could not earn enough cash to handle their loans, how much would be left over for ventures earning only local currency?

Debt and crisis

As in the 1920s, all that remained was for someone to light the fuse on this explosive mix. China lit that fuse in 1994 when it devalued its yuan by 32 percent, and the fuse burned down to a stick of dynamite in Thailand by July 1997. China's devaluation triggered great concerns in the United States about Japan's economy, and in 1995 the Clinton Administration reversed course, allowing the yen to fall 28 percent against the dollar in two years. The administration hoped this would allow Japan enough time to deal with the estimated \$600 billion of bad loans in its banking system.

Devaluation increased China's exports and Japan's direct exports, but at the expense of the MIT economies. Japanese firms, faced with a fratricidal choice between producing at home and producing abroad, naturally favored home production. China's emergence as the largest exporter of clothing (18 percent of world exports) and toys (roughly a third) displaced exports from the MIT economies. Moreover, FDI inflows swung decisively towards China and away from the MIT economies, with China attracting three times the inflows of the MIT group and the Philippines in 1997 after starting from rough parity in 1992 (Thomsen 1999: 15). Thus after racking up successive years of double-digit export growth after 1990, MIT export growth fell to virtually nothing (see Table 4), and their current account deficits expanded. Meanwhile the bilateral US trade deficit with China doubled to \$30 billion, a clear indication that the Chinese had won the competitive struggle with the MIT economies for dominance of export markets.

Table 4 Asian Emerging Market export value and growth, 1990-1997

	<i>Value, 1997, \$ billion</i>	<i>Annual percentage change</i>	
		<i>1990-97</i>	<i>1997 only</i>
China	182,000	17	21
Korea	136,200	11	5
Indonesia	53,540	20	7
Malaysia	78,445	14	1
Thailand	57,385	24	3
Taiwan	121,900	9	5
World	5,305,000	7	5

Source: WTO 1998: 33, 50, 65.

This in turn confronted the MIT economies with quite difficult choices. Consistent with the Mundell-Flemming model, they could pursue only two of the following three policy choices: monetary policy autonomy, free capital flows, and fixed exchange rates. Their policy stance in 1995 was free capital flows and fixed exchange rates (the peg to the dollar). From 1995 to 1997, the rising US dollar and the inflationary effects of capital inflows combined to price their exports out of world markets. Doing nothing would simply erode export competitiveness as local wage and land costs rose, and cause foreign capital to shift to cheaper locations. If they raised interest rates to damp down inflation, and thus kept their export prices in line with China's, they would also have to impose capital controls to prevent even more inflationary inflows of capital attracted by high interest rates. But capital controls would slow investment, and make highly indebted firms go bust, particularly in the property sector. Slower investment would also disadvantage them in what was essentially a race to expand production before anyone else did. Finally, they could devalue, matching China's devaluation. But doing this would certainly push local firms with foreign currency debts into bankruptcy, because their borrowing was premised the ability to exchange local currency earning into foreign exchange at fixed parities. In short, every policy choice available to the MIT states would have involved inflicting pain on powerful local interests. Consequently the MIT states dithered, allowing currency speculators to force devaluations when it became apparent that current account deficits were depleting Thailand's foreign exchange reserves.

The Thais devalued the baht, throwing their local banking system into crisis as nonperforming loans reached about one third of GDP. From there the devaluation and banking crisis spread to all the emerging markets, partly for tangible economic reasons — they all were still essentially exporters of commodities whose prices could only fall — and partly for rationally irrational reasons — given that some investors would panic, it was better to anticipate panic and divest as quickly as possible.

The story here has of course stressed the tangible economic reasons for panic: falling prices for commodity exports, including undifferentiated, low-value-added consumer goods. This is why the medium term is unlikely to bring neither an end to Asian financial problems, nor a resumption of high-speed growth. While the US government organized bailouts for some Asian economies, most notably South Korea's, this simply prevented the short-term panic from cascading into a replay of the 1929-1932 catastrophe. This certainly was a good thing. But it does nothing to resolve the underlying long-term problems. The 2001 US economic slowdown immediately affects growth prospects in Asia, because so many Asian economies rely so heavily on exports to the US, because the Japanese economy is likely to continue stagnating, and because to the extent that there is growth in China, it will not translate into increased exports from Asean and indeed may translate into displacement of Asean exports from third party markets..

Over the long-term, all three conditions for sustained late development that the earlier discussion highlighted seem unlikely to reoccur. Rapid export growth leading to rapid productivity growth, government orchestration of the capacity to invest productively, and foreign markets to absorb all that production are very unlikely to be present for most Asian economies. And indeed, only in Taiwan did the average growth rate 1998-2000 exceed half the average growth rate 1992-97. The Asean economies, by contrast, averaged negative growth in the latter period.

First, the massive overhang of productive capacity is still in place in most countries, even if domestic demand recovers. So downward pressure on prices continues and this means that foreign debt service will constrain capacity for domestic growth and reinvestment. China also faces a serious problem of internal deflation. In 1999 it engineered a second, but invisible, devaluation of the yuan by removing some taxes on exports, and in 2000-2001 it embarked on a gradual escalation of tensions with the US in a effort to divert domestic attention away from the

faltering economy. Finally the Japanese economy, which constitutes around two-thirds of Southeast and East Asian GDP, remains mired in recession. The much-touted recovery of late 1999 did not bring annual growth rates over 2 percent, and by 2001 the continued depression of equity and property markets threatened to bring the entire financial system to its knees. In the long term it is hard to see how Japan could have substantially higher growth without making politically painful and socially wrenching changes to the entire institutional structure of the economy.

Second, the price for IMF bailouts was a reduction in the capacity of states to coordinate investment and mobilize capital and labor to get growth. The sale of banks and industrial firms to profit minded foreign firms removes the government's ability to coordinate investment. For some countries this is probably a good thing – vide Indonesia. But for South Korea it is the end of the model for high-speed growth. Malaysia remains a difficult case, because while on the one hand it avoided reconstruction along IMF lines, on the other it has a host of unprofitable and unproductive state firms. In all these countries the dismantling of state directive capacity redirected nationalist sentiment in anti-US, anti-Western, and anti-IMF directions. In multi-ethnic Indonesia and Malaysia the end to high-speed growth also increased communal tension, which played out in Malaysia as an effort by Mahathir to quell Anwar's implicit promotion of Chinese business and in Indonesia as anti-Chinese riots, regional separatism and violence between Javanese colonists and indigenous populations in the outer islands.

Third, external markets pose a powerful constraint, not opportunity. As noted above, Japan remains the key to problems of insufficient demand in Asia and elsewhere, because it is a massive global creditor with a developed economy. By all rights, Japan should be a bigger importer than it is. But consumption power is locked up in bad bank debt, its own overcapacity problems, and the way that consumption is constrained by local credit markets and distribution networks. Japan typically runs trade surpluses with Asean. Meanwhile in the United States, the Federal Reserve Bank sees the rising US current account deficit, 25 percent of which is with China, as both a symptom and cause of excessive demand in the US economy. It used the current account deficit as a reason for one of its interest rate hikes in 1999-2000. While every Chinese manufacturer may dream that each American parent should buy one more beanie baby for her child, these hopes, like Lancashire's dream of an extra inch on every Chinese shirt, are unlikely to

be fulfilled. Finally, although China, Taiwan and Singapore, are also sitting on large foreign exchange reserves, using those reserves to absorb excess export production Asia would undermine their own nationalist drive to build up their own economies.

All this suggests that the rapid growth of the 1980s and early 1990s will not reemerge for some time, even if Asian economies “recover.” The long-term prognosis for Asia thus is not grim, but is not going to be a story of rapid growth like the recent past. And since government legitimacy in Asia is premised on rapid growth and rising living standards, what then for nationalism? If the historical record in both Europe and Asia suggests anything, the collision between the nationalist sentiments deliberately unleashed by states seeking to accelerate industrial growth and then reinforced by the sudden deceleration of growth in the crisis of 1997-98 is highly likely to leave blood spilled on the road to continued economic development.

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¹ Rather than present an elaborate explanation about why this should be so, I refer the reader to chapter 4 in Schwartz (2000) for a brief synopsis of the arguments, and to Gerschenkron (1964) and Waldner (1999) for more extensive treatments.

² Note that in developed country markets protection will raise final market prices, by limiting the supply available to local consumers. However, this will not raise world market prices, because limits on the absorptive capacity of developed country markets will create an oversupply in supply countries. The gap between high prices in developed country internal markets, and low world market prices creates an opportunity for arbitrage. The structure of distribution channels determines who captures this opportunity. Generally, in the nineteenth-century, developed country multinational firms or their states captured this rent. In the twentieth-century developed country retail chains, some of the wholesalers associated with them, and various brand names subcontracting offshore have captured it.