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**“Information Aggregation and
Economic Development: The Case
of East Asia”**

**Jose Edgardo Campos and
Hilton L. Root**



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**INFORMATION AGGREGATION AND ECONOMIC DEVELOPMENT: THE CASE
OF EAST ASIA**

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INFORMATION AGGREGATION AND ECONOMIC DEVELOPMENT: THE CASE OF EAST ASIA

Abstract: East Asia's successful leaders recognized that uncertainty and the costs of information were at the heart of the individual and social obstacles to development. Creating political institutions that inspired spontaneous market led growth while at the same time coordinating the aggregation of information needed for long term investment was a central contribution of East Asian leadership to the science of development management. Incentives for firms and individuals to use local information effectively were essential and suggest that leadership in East Asia saw the importance of information more clearly than their counterparts among leaders of the world's poor countries. For example, leadership in Japan, Korea, Malaysia, Thailand, Singapore and Hong Kong, created consultative committees with real input into the policy making process. Councils allow rules governing rent sharing to be explicitly and openly stated so that each participant is assured that regulations allocating shares in the economy are the same for all players. In addition, councils facilitate communication between the private and public sectors by offering inputs into the policy process while providing key players with ownership of the policy outcome. The councils provide: 1) assurances to important sectors that policies governing them will not be capriciously altered; 2) a venue for information about the production and implementation of policy that is available to all players, thus improved transparency; and 3) procedural guidances and precedents for the exchange of views between leadership and the private sector. All this augments accountability. Policies, in turn, are more credible because it can be assumed they are backed by the relevant sectors and thus can be enforced with limited coercion. The importance of councils to government credibility meant that government's were unlikely to change the rules without consulting the appropriate private sector representatives.

1. DICTATORSHIP AND ECONOMIC POLICY

Leadership used extra-legal means to seize power in all of East Asia's high performers except Japan. Although the Asian dictators were responsible for implementing economically responsible policies, this is unusual in world history. Dictators reputed for their economic expertise in policy are rare, they are more likely to have expertise in political manipulation. Once in power, the fear of being overthrown typically drives their choice of policies. Since retaining

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control is a greater priority than the economic outcomes of policy choices, dictators commonly sacrifice the welfare of their subjects to consolidate their hold on power. Thus dictatorship and economic development rarely complement each other.

The dictator's fundamental conundrum is the fear of losing power, therefore he will prioritize the accumulation of loyalty (Tulluck, Wintrobe). Officials may be selected on the basis of their ability to build up a clientele rather than on their technical competence. Control over the economy offers another way to increase regime security. Rather than encourage competition that might reduce costs for consumers, dictators are more likely to assign a monopoly to those business interests who promise to share profits with their benefactor. The dictator thereby builds loyalty by tying the fortunes of those who control economic resources to those of the regime. The monopolies are particularly valuable because the dictator can complement his largess by providing confidential state information, government contracts, and he can manipulate the judicial system to protect the interests of his followers. As the market place is politicized, the growth of firms that do not openly support the dictator may increase insecurity and invite retaliation. Moreover, the leader may decide to reward his followers by taking resources from those who do not profess loyalty or who might have been associated with one of the dictator's rivals. Inevitably economic decisions become embroiled in political machinations and economic rivalry is resolved in the political sphere as insiders use their influence to hinder economic competition. The

privileged insiders will be depicted as patriots so long as they do the leaders bidding, but they know that if they become too wealthy, they too may become targets. Because the ruler lives by threats, even his followers fear their good fortune can be rescinded at any time. Those who benefit from largess today know that the ruler's promise not to harm them in the future carries little credibility. Being above the law, the dictator's promises are not enforceable (Root, 1989, 1994, North, Weingast).

By making the dictator feel admired, subjects can hope to protect themselves from possible censure. Therefore, subjects will provide the dictator only with the information the dictator wants to hear (Wintrobe, 1994). The more power the dictator accumulates, the less subjects will risk disclosing unpleasant information. Nor will state officials risk providing bad news or report activities that contradict the ruler. Lacking a method to hear from those who are targeted about the effectiveness of a given policy, dictators can rarely formulate effective programs.

Overcoming information asymmetry becomes especially acute where the formulation of economic policy is concerned. Dictators have difficulty obtaining information about the economic activities of their followers. Uncertainty about the ruler's future behavior induces firms to be secretive. Because information can be used to confiscate, intimidate or expropriate, economic assets are concealed. Rather than register their assets, firms will hide accounts, and expatriate capital to safe havens abroad. Since investors will hesitate to put their own capital at risk, investments requiring fixed capital will usually

require significant subsidies from public coffers. Hence, resource-based trade will appear more attractive than investments that generate industrial capacity. Another reason for secrecy is that profits of insiders could arouse jealousy and incite unrest. The absence of auditable accounts or reliable information about profits will hinder the development of domestic capital markets. Banks will approve loans on the basis of a client's political connections.

Despite the violent origins of the political authority held by many of the region's leaders, this all too familiar scenario, does not apply to East Asia's high performers. Nevertheless, defining the political origins of East Asian economic success has not been controversial. The success is commonly related to the absence of institutions which constrain government to abide by due process in the choice and implementation of policies. A different hypothesis about the institutional foundations of East Asia's economic success will be suggested.

Unlikely to empower institutions allowing others to contradict him, the dictator has a problem of credibly committing his regime to policies that encourage long term growth. If dictators want information to determine the appropriate choice of policies, they must assure that the disclosure of information does not result in the confiscation of assets. To solve this commitment problem and to institutionalize the flow of information between the private and public sector, Asian leaders traded power with private sector leaders and in effect tied their own hands. The architecture of their institutions limiting

sovereign discretion is rich in implications for the governments of other developing nations, including those governed by democratic constitutions.

The need to gain the cooperation of the economic elites illustrates the importance of institutions which facilitate the exchange of information between the public and private sectors. Each of the high performers had to overcome leadership's credibility deficit in order to win the confidence of those groups having the capability, know how, and/or capital to build a dynamic industrial sector. Leadership had to deliberately craft institutions to induce the economic elites to volunteer expertise and capital in the service of growth.

2. THE DELIBERATION COUNCILS

One critical but often overlooked institutional device to induce cooperative behavior among elites are consultative committees, which five of the successful Asian economies -- Singapore, Thailand, Korea, Japan, and Malaysia -- have used.¹

¹. Although consultation processes have also permeated policy making in Hong Kong they have not been extensively documented. The process of consultation in Hong Kong begins at the level of the executive council, which in 1986 consisted of five ex-officio high government officials -- the governor, the chief secretary, the financial secretary, the attorney general, and the commander of the British forces -- and ten nominated members who do not hold public office. Although formally empowered to override advice given by members of the Executive Council, the governor is unlikely to do so as he depends heavily on the cooperation of non-governmental council members for their contacts among the broader community. The Executive Council as well as the Legislative Council, the Urban or Regional Councils, the District Boards and the many advisory boards and committees appointed by the government all depend on private sector participation. The Legislative Council is an example of government by consultation. The council, which provides advice on the formulation of laws, reserves the largest block of seats for the wealthiest sectors of the commercial, industrial, and financial communities. It meets

To differentiate them from outwardly similar mechanisms in other developing countries, we shall call these committees deliberation councils. Unlike the former, these councils have played an active and often critical role in the formulation of policies, rules, and/or regulations that eventually govern a sector, industry, or in some cases the macro-economy.²

A deliberation council consists of representatives from both the private and public sectors. The particular constitution of its membership depends on the set of policies over which it deliberates. For example, a council formed specifically to discuss, amend, and recommend regulations governing the electronics industry would necessarily include representatives from the biggest electronic firms. If the industry has an active professional association, members of the association would normally act as representatives. It would also include several mid-level and senior level bureaucrats from the ministry of trade

often and publicly debates proposals for future policy and for public expenditure. The Council has the right to question the government about matters of public interest. Any proclamation, rule, regulation, order, resolution, notice, rule of court, by-law or other instrument having legislative effect can be considered by the Council.

Committees form another element of the elaborate system of consultation that takes place between the private and public sectors. The Civil and Miscellaneous Lists of 1989 reported 264 committees, 154 of which were set up by ordinances. But this list seriously underestimates the amount of organized consultation that may draw 'unofficials' into the policy making process. Norman Miners reported 393 advisory committees with a total of 2106 citizen membership. Little is known about the activities of these committees since almost all are closed to the public and papers or minutes are kept confidential.

2. Many of the Japanese councils perform perfunctory roles and do not possess the fundamental characteristics that make a deliberation council effective. Only some (and these tend to be the more important ones) such as the Industrial Structure Council are consonant with our concept.

and industry. On the other hand, a council established to discuss international trade policy would be larger and enlist representation from all major industries and from many government ministries. It may also include representatives of labor and consumer groups and is likely to be chaired by the deputy prime minister, if not the prime minister himself.

Generally the deliberation council has a quasi-legislative authority, and policies cannot be introduced or changed without its recommendation or approval. Unlike a legislative committee, private sector representatives are not chosen (by industry or labor, for example, and not necessarily through voting) and government officials become representatives by virtue of appointment.

The principal task of a council is to assist the government in formulating policies that would enhance the performance of a particular segment of the private sector, if not the private sector as a whole. Within this context, a council is designed to reduce the high transaction costs of coordination; to overcome asymmetric information and rent-seeking; to stabilize the policy environment; and legitimate economic policies. First, it generates a cooperative format to reduce the cost of obtaining and transmitting information relevant to the design and implementation of new or the alteration of existing policies: it facilitates a mutual exchange of information among members of the private and public sectors and thus helps coordinate their responses. Second, it provides private sector participants with a transparent forum in which to bargain over the rules that

determine how rents are to be allocated and thus helps to diminish the importance of patron-client relations and to reduce the need for lobbying. Third, it gives the government a mechanism to instill confidence among investors that policies will not be altered without appropriate consultation and support from the private sector, allowing government to credibly commit to policies that will enhance private sector development. And fourth, it offers private sector participants a forum to express their views on policies that affect their industry (industries) and to have those views incorporated into the formulation or alteration of the policies. Thus, councils create a channel for government to establish the legitimacy of the policies it promulgates and implements.

The specific function(s) of councils vary across the five countries and across sectors within the countries. Several examples each of which will highlight some, if not all, of the functions as well as the economic and political implications of these functions. The National Wages Council in Singapore has successfully fulfilled all four functions.

2.1 SINGAPORE

Singaporean independence was marred by worker and student unrest. Because tensions between labor and government had a long history, leadership understood that resolving these tensions was critical if Singapore was to enjoy the prospect of development. The Peoples Action Party (PAP), which has ruled the country since independence, recognized very early the city state's limitations. The country has two assets, its people and its natural harbor.

To take advantage of these required foreign investment in labor intensive export-oriented industries. Limited by insufficient expertise and short of financial resources, aggressive efforts to attract multinational corporations was the main feature of Singapore's development strategy. Multinationals, however, have generally been hesitant to move their labor intensive operations to countries with an unstable labor regime and/or an uncertain policy environment. The PAP thus focused on facilitating cooperative business-labor relations while stabilizing the policy environment. An important component of the strategy was the creation of the National Wages Council (NWC). The council's was designed to establish political stability by assuring the cooperation of labor.

The NWC is an advisory, tripartite body comprised of government, employer, and labor representatives. Multinationals are heavily represented. Each year, the council reviews the past performance of the economy and evaluates its prospects for the coming year. Based on the findings, members deliberate generally on employment related issues and specifically on the appropriate guidelines for the year's wage increases. A key feature is tying the increases to gains in productivity, estimates of which are based on the past and projected performance of the economy. Meetings are held in the first half of each calendar year. Public views are sought for each year's deliberations, although the deliberations themselves are kept private. Meetings follow two working rules, the Chatham House rule on non-attribution and the decision rule of unanimity.

Under the Chatham House rule, statements and comments made by members are not to be publicly attributed to any specific individual. The rule thus promotes a freer discussion of the issues. Unanimity requires that each of the three groups -- government, labor, and business -- must support the proposed guidelines. Deliberations continue until all three agree to the provisions. Once an agreement is reached, the agreed upon guidelines are announced to the general public. The Council's recommendations are non-binding but, largely because of the unanimity rule, both business and labor have accepted and used them as an impartial benchmark of a reasonable wage settlement and healthy compromise. The government has always automatically accepted the guidelines and usually is the first to adopt them.

The NWC incorporates all four functions of a deliberative council. It has been the primary channel through which government and the private sector share market information, especially valued is information on improvements in productivity and on trends in global markets. Orderly wage increases have resulted from its deliberations: (quasi) rents are allocated transparently and objectively between business (profits) and labor (wages).³ Both labor and business have been granted veto power over wage policy (via unanimity) and thus have had real input into the decision making process. In effect, the council resembles a legislative committee with limited jurisdiction. And finally, precisely because of its veto power, the council has

3. Quasi rents are to be interpreted as gains over and above marginal cost.

helped maintain order and stability in wage negotiations, providing assurances to both business and labor that wage policies will not be reversed arbitrarily or forcefully, e.g. through strikes.

The unanimity rule resulted in the implicit devolution of authority over employment policies by the government to the NWC. Unanimity and devolution have made possible the maintenance of a stable policy environment, a prerequisite for attracting private investment. Unanimity has assured each party that employment policies cannot be altered without their consent. Devolution has provided the credibility that government will not use its coercive powers to alter the council's recommendations. By granting the Council de facto authority over employment policies, the government has imposed on itself a very high cost to changing employment policy "from above." Forcing such a change undermines the growth process since, fearing the onset of arbitrary policy making, businesses may decide to move out and labor may decide to resort to more disruptive expressions of its demands. Should any of the parties take unilateral actions that challenge the council's legitimacy or jurisdiction, they would reduce the future value of the council as an instrument for coordination, consent, and commitment. In short, the council has given the government the capacity to credibly commit to a stable, rational policy making process.

The partnership of public and private sectors began early in Singapore's history. That relationship was institutionalized as early as 1959 with the creation of the Economic Committee

designed to bring all segments of the population together to discuss Singapore's future in the world economy. The consensus which imposed considerable sacrifices represented the participation of all segments of the population in hearings open to all parties that took an interest. The government played its role by allowing the public to scrutinize all available economic and social data. Committee members also had at their disposal evaluations of all the major government policy initiatives. Again after the economic difficulties of 1986 the government institutionalize a public\private partnership in the formulation of the government five year plans. The Singapore case highlights the need for government not to compromise on the need to keep industry open to international competition. A consultative mechanism that compromised competition, liberalization and monetary and fiscal stability would have produced dramatically different results. Consultation is not a substitute for appropriate macro-economic policies.

Where the transparency of information and the quality of the bureaucracy are concerned Singapore tops all developing nations. Despite the consistent collaboration between the public and private sectors (labor and management) in the policy dialogue, that has produced miraculous economic growth and restructuring unparalleled among developing nations, Singapore is faulted in the West for failing to institutionalize the procedural apparatus of multi-party elections. This has led to a debate over whether Western-style democracy is likely to prove more robust in the long-run. Singapore's development suggests that the issue is not

whether democracy has more staying power, but how does a society devise the institutions most suited for its development and survival in a competitive world economy. Lee Kuan Yew's answer has consistently emphasized the need for nations to develop the institutions that are appropriate for their particular stage of development. The choice is not between participatory democracy and authoritarianism, but adopting the appropriate level of participation necessary to articulate a social consensus.

2.2 JAPAN

As a democracy with an elective legislature Japan is unique among the high performers. Whereas, after the War the legislature earned its legitimacy as representatives of the people, the bureaucracy was held over by the occupying forces and lacked a comparable claim to democratic legitimacy. Thus, although a parliamentary democracy Japan's government had a credibility problem. It was dominated by a single party, which had at its service an administrative apparatus which did not have a democratic mandate and yet it could intervene directly in the economic decision making of the private sector. Councils were introduced and were especially important during the first two decades of Japanese democracy as a method for the bureaucracy to break with the past. Vis-a-vis the Diet, councils allowed the bureaucracy to make a claim to being representative of a constituent group. This would inevitably mean that bureaucrats

would have to show the consensus of the relevant council before bringing a policy up for parliamentary approval.⁴

Of the HPAEs Japan's councils were the most well developed and widely recognized. However, they are also the least transparent.⁵ The Japanese deliberation councils included private sector representatives from the large industrial sector and in some cases from labor and consumer groups. There are two categories of deliberation councils that allowed the Japanese government and private industry to cooperate on industrial policy since the late 1940s. The first type is organized along functional or thematic lines, e.g., industrial rationalization, pollution and finance; the second is organized according to industry or sector, e.g., iron and steel, automobile and chemical. The councils are established by a government ministry and are formally associated with specific bureaus within that ministry. Table 1.1 lists the councils attached to the Ministry of Trade and Industry (MITI). The Industrial Structure Council, the Industrial Property Council, the Export and Import Transaction Council, and the Industrial Technology Council are examples of the first type. The Mining Industry Council and the Textile Industry Council are examples of the second. A functional deliberation council is normally divided into special committees.

4. See Ryutaro Komiya, Masahiro Okuno, and Kotaro Suzumura 1984: 16-22.

5. Much of the information is contained in files of MITI to which access is limited. The discussion presented here comes from background papers by researchers in both academia and government and from interviews with Japanese academics and government officials.

The typical process involved in the formulation of policy in MITI is illustrated in Figure 1.1. In the initial stage, MITI calls a hearing and invites various parties to participate. It compiles the data and integrates the results of the hearings into a draft. The draft report goes to the appropriate research group in MITI which then prepares a report for discussion in the appropriate council. In the council, the views of industry officials, academics, consumers, and other interested parties are solicited and incorporated into a plan. The research group then makes changes to the report based on the feedback from council members. The last stage of the process resembles an advertising campaign through which MITI explains to the general public the objectives and reasons for the new policy.

As in Singapore, Thailand, and Korea, a Japanese council is essentially a forum through which government officials and representatives from the private sector -- industry, academia, the press, and in some instances labor - can exchange views on policy matters, discuss trends in markets and products, and more generally, share information.⁶ The councils have provided the government the means to create a consensus on a particular policy matter: when the council does not agree on a policy the bureaucracy is trying to promote, it is unlikely the policy will be approved by the legislature.

Hence, it was important for MITI to achieve consensus within the deliberative council for it is here where success or failure

6. Extensive informal information networks supplement the meetings of the deliberative council.

of a policy initiative was essentially determined. For example, "the plan for the concentration of the automobile industry, which in fact never materialized, were both strongly opposed at the council level. In the end a consensus within the industries concerned was not obtained (JDB/JERI Study, Ch. 2, p.42)." Thrice MITI proposed some version of rationalizing the auto industry. The first was a national car plan which basically gave the rights of production to a single winner. "In 1955, MITI formulated the National Car Project and attempted to execute it, its purpose being concentrated production of low cost, small cars for the general public by a single manufacturer. . . . the Concept concerned a car accommodating (1) four passengers, (2) costing about 250,000 yen, (3) with a displacement of 350 to 500 cc, (4) weighing 400 kg, and (5) with a maximum speed of 100 km/h. Concentrated production of this car by a single manufacturer was proposed (Itoh, 1993, p. 14)." The second was a partitioning of the industry into three groups, each group producing a specific vehicle category. "In May 1961, MITI proposed to split the automakers into three groups of mass production, special passenger cars (high class cars and sports cars), and mini passenger cars, each group consisting of two to three manufacturers (Itoh, 1993, p. 15). " Both times, council members rejected MITI's proposals. And both times, MITI resisted forcing the issue in the Diet. In its third try, MITI managed to obtain a consensus among the manufacturers. The agreement reached was one of import protection in exchange for exporting: every manufacturer could participate (Itoh, 1993). Shortly

thereafter the Diet (the legislature) passed a new automobile industry rationalization law embodying the agreement.

The auto industry example illustrates two functions of a council. First, transparent rules for the allocation of rents among firms were established. Manufacturers agreed to a plan that gave each opportunities to earn rents via protection of the domestic market in exchange for successful expansion into export markets. Second, while providing inputs into legislation manufacturers had veto power. As a consequence, automobile manufacturers could be confident that policies would not be changed without their consent and therefore were relatively durable.

Why does government not overturn those council decisions it opposes and abide only by those it prefers?. The answer is rather subtle. Given that councils have permeated many industries and sectors in the country, by unilaterally imposing its will on a single industry or sector, the government risks undermining the value of councils and thus subverting the whole system of cooperative decision making. This in turn would increase the transactions costs of policy making and thus could retard economic growth.⁷ Should that happen, the legitimacy of the government could be more easily challenged. By institutionalizing councils, the government has limited its

7. This argument is derivative of Grief, Milgrom, and Weingast (1993): tying the fortunes of many groups to the continued use of a particular system raises the cost of altering that system. Hence, the more groups are tied together, the more credible a system becomes. Once again, the idea of coordination costs and irreversibility emerges.

discretionary power over economic policy but in turn has created an environment that has given big business confidence in the stability of those policies agreed upon. .

2.3 KOREA

Rebuilding private sector confidence was a priority for obscure group of officers that in 1961, violently took power in Korea. The officers were willing to place all political bets on economic growth. After first shattering existing old boy networks, they struck a deal with the heads of the big conglomerates they had imprisoned: the private sector would deliver development and, as part of the bargain, confiscated wealth would be released. Consultation played a major role in winning back the support of the private sector. Decision makers in the Korean process the importance of endless meetings with representatives of the private economy. Leadership committed itself to guiding the economic elites by helping to coordinate private sector effort; the actual work was left to the latter.

In Korea from the mid 60's to the early 80's, government and private sector relations were characterized by frequent, regular meetings between leaders of both groups.⁸ These meetings were less formal than the council meetings in Japan or Singapore but they had similar objectives: information exchange; rent

8. Relations were also close and cooperative. Others (especially those in the private sector) would argue that government was high-handed and dictatorial. Although the channels of communication are still operational, the democratization of the polity has led to some chilling of the business - government interface. There is a recognition in many quarters, including business, for the need to reestablish good relations but with more balanced collaboration between the two sectors.

allocation; elite participation in policy making; stability of the policy environment. President Park presided over the Monthly Export Promotion Meetings; his presence gave authority to the meetings. In these meetings, "institutional arrangements and legal and procedural issues for export promotion were brought to the attention of the President and concrete policy recommendations were made. The President allocated follow-up responsibilities to the appropriate ministers. A progress report was made in each meeting by the ministers assigned tasks during the previous meetings. The establishment of this well publicized meeting had a significant effect in exploring profitable markets and in implicitly promising government-wide support for private sector activities designed to achieve those export targets (Chang, 1992)."

The meetings were the barometer for the country's export push and thus critical to its overall economic performance. The ministries were committed to building up the private sector even if that meant bullying it into accepting export markets.⁹ However, bureaucrats did not decide what to produce, rather, they coordinated and assured the sharing of relevant information among all parties that had bargaining power, specifically big business. These meetings and the informal consultations that followed have facilitated early recognition of problems encountered in expanding Korean export markets. The primary focus of these meetings is the joint determination of export targets for various

9. Samsung lost a fertilizer factory when it refused to play ball with Park. This confiscation, however, was conducted according to rules: the stick.

industries by private enterprises and government officials. The Ministry of Commerce and Industry collected information from individual exporters on a monthly, weekly, and sometimes even on a daily basis. It also monitored and analyzed changes in market conditions. Export targets and policies were altered when necessary so that the government and private sector could respond rapidly to fluctuations in world markets. Short term changes in government policies could then reflect world market conditions. The system reduced the risks to private enterprise of engaging in export activity and has helped Korea maintain its sizable share of world markets.

Lower level meetings between middle level managers in private industry, middle level officials in government, and experts/scholars supplemented the Monthly Export Promotion Meetings. Meetings took place in the form of industrial discussion groups. There were basically two types: the functional (e.g., taxation) and the sectorial. The former was centered around the presentation of various viewpoints from known experts on particular topics normally identified and chosen by the bureaucracy, e.g. Ministry of Finance. The experts provide their analyses and opinions; the government bureaucrats normally just listen. Though the final decision is made by the bureaucracy, the policies adopted generally attempt to incorporate all the various viewpoints presented. The second type of industrial discussion group involved representatives from an industry, usually from the corresponding industrial association, discussing their perspectives on a particular issue

with representatives from Ministry of Trade and Industry. At this level, the process is more of information gathering rather than collaborative decision making. Nevertheless, if the industry representatives are vocal enough about the issues, their inputs help shape the final product.

Deliberation councils, in particular the Monthly Export Promotion Meetings, were important in coordinating the export drive. During the meetings, obstacles to achieving competitiveness were discussed and solutions were often recommended and implemented (Amsden, 1989). The meetings presided by Park were devoted to monitoring export targets and solving export related problems. The criteria for access to subsidized credit and to production licenses became more transparent as a result of the councils. Firms seeking credit and/or licenses had to meet Park's basic criterion: "How much have you exported for me lately?" Export performance was used to allocate preferential credit and to determine who would get valuable licenses from the government to produce promoted products, a system Amsden (1989) aptly refers to as reciprocal exchange. It was very clear what the principal function of the council was: to extract the necessary information to formulate better export promotion policies and to allocate rents, i.e. credit subsidies and production licenses, in a systematic, transparent, and objective fashion.¹⁰

10. Exporting, which began in the more neutral environment of the sixties, continued to be a major criterion for allocating credit during the seventies (Export promotion consisted not only of preferential credit but of other policies as well. See Rhee, Ross Larson and Pursell, 1984 for a comprehensive review of

A more subtle and seldom mentioned effect of the reciprocal exchange system was the creation of a dynamic that ultimately made it difficult to alter the country's export orientation. Firms had come to expect significant rewards for success in exporting and thus had oriented their production, management, and marketing capabilities to world markets. Changing the rules of the game would have had serious consequences on firms' operations and thus on economic growth, a specter which would have undermined the legitimacy of the military government. Thus the councils in Korea helped make export policies durable and credible to the private sector. On the one hand, the councils helped coordinate the move from an inward-looking, protectionist trade regime to an outward oriented one. On the other, it helped institutionalize a process which virtually made exporting irreversible.¹¹

Korea's export promoting policies). In credit markets, automatic and highly subsidized financing of exports continued (see table 4.4). Enforce the performance criteria was possible because the government possessed strong leverage over firms: it controlled the sources of loans and the authority over industrial licensing (Haggard, 1990; Amsden, 1989). As Wade (1990) notes, the debt-equity ratio of firms in Korea have been historically higher than in Japan or Taiwan suggesting that much of the firms' initial growth was debt-driven. Since loans often had to be rolled over, the threat of terminating loans could jeopardize the existence of highly leveraged firms. In some cases, the government refused to bail out failing companies unless the firm agreed to changes in the management.

11. Irreversibility is related to the concept of path dependency. Path dependency refers to historical constraints imposed on the trajectory of an economy. For example, Paul David (1975) *Technological Choice, Innovation and Economic Growth*. Cambridge : Cambridge University Press: 1985 "Clio and the Economics of QWERTY." *American Economic Review*, 75: 332-37. The initial development of the typewriter keyboard, the QWERTY keyboard, has constrained the adoption of more efficient keyboards primarily because the former has come to be accepted and used by a very large number of people and establishments.

The Sixth Plan offers an additional example of the role of consultation in Korean development. Transparency and participation were stressed by the authors. tried to make it a story everyone could read. The assistant minister explained, "We wanted to build a popular consensus on the future economic and social course of Korea...So we formed forty three subcommittees to draft working documents, each with two co-chairmen, one from government, the other a private citizen. The drafts were then released to arouse discussion...We got a very big response. The minimum wage was discussed on TV, in newspapers, and at seminars. We also got many letters, so public interest is obviously high."¹² Nevertheless, Korea throughout this period rates poorly on the Freedom House index of democratic indicators. The Korean experience suggests a need to revise such indices to reflect the quality of participation in the policy dialogue itself.

2.4 THAILAND

Prior to 1981 Thai public/private sector relationships were characterized by "a prevailing sense of distrust, and elements of arrogance on both sides. The public sector regarded the private sector as selfish entrepreneurs and thinking only of their personal profits with little sense of social responsibility. The private sector, on the other hand, suspected Government officials of being extremely inefficient corrupt and bureaucratic....The two points of view were rarely reconciled as there was no formal

Changing to a new system would involve an enormous problem of coordination. Irreversibility stems largely from the costs of coordinating a switch.

¹². Cited in Robert Elegant "Pacific Destiny: The Rise of the East" Headline Book, London: 100.

mechanism to bring about more fruitful dialogues (Muscat)."¹³
The sources of the mistrust had deep historical roots. From the overthrow of the monarchy to the late seventies, business - government relations were essentially governed by military - bureaucratic clientelism.¹⁴ The ethnic Chinese business groups were "pariah entrepreneurs", culturally and politically kept on the defensive. "The prevailing forms of business influence were outright bribery or creation of patron-client relationships with the military-bureaucratic leaders, mainly by inviting the latter to join executive boards to hold stock in companies at no cost." (Laothamatas, 1988). The presence of military-political leaders on the boards of twelve of Thailand's sixteen commercial banks in 1972 illustrates the protection racket that placed the private sector at the mercy of well-placed political or military authorities.

In the early 80's to overcome a tradition of mistrust the orchestrators of Thailand's liberalization drive championed the need for better communication between the public and private sectors. Designating the private sector as the engine of growth, the government's Fifth National Economic and Social Plan proposed a mechanism for public and private sector collaboration. That mechanism, high level joint private-public committees: "The National Joint Public and Private Consultative Committee (JPPCC) was established, with the Prime Minister as Chairman and the Secretary General of the National Economics and Social

¹³. Cited in Muscat, 183, from Snoh Unakul,, "Thailand : The Fifth Plan Strategy", pp. 18-27.

¹⁴. See Riggs (1966) for a comprehensive discussion.

Development Board (NESDB) as the Committee Secretary. Other members are the Deputy Prime Minister, ministers and deputy ministers of economic agencies, the Governor of the Bank of Thailand, the Secretary General of the Board of Investment, three representatives from the Thai Chamber of Commerce (TCC), three from the Federation of Thai Industries (FTI), and three from the Thai Bankers Association (TBA). (Samudavanija, 1992, p. 26)."

In Thailand much of the initiative to establish peak industrial associations came from the private sector. Although the government legally chartered these bodies, it did not intervene extensively in their development and management.¹⁵ "As weak as they might have been as interest groups, business associations were at that time (circa 1970) much stronger than any functional group Almost all other groups were created and/or sponsored, and closely controlled by the government for security and agricultural development purposes. By comparison, business associations were largely independent of the government. No public officials sat on the executive boards of business associations. Official control of their operations, internal regulations, and leadership selection, though harsh in theory, was mild in practice. No closures of associations or bans on their functions or leadership selections had been reported (Laothamatas, 1992, p.31)." Hence, in contrast with their status in other corporatist states, industrial associations

15. The impetus for the JPPCC came from the combined efforts of prominent members of the business community with proactive support from technocrats, particularly from Dr. Snoh Unakol, the respected Secretary General of the NESDB during most of the eighties.

evolved more independently of government in Thailand than elsewhere.¹⁶

The industrial associations enabled businessmen and bankers to develop their own networks and to become critical partners of the military-bureaucratic elites in the task of developing the economy. This partnership became evident in the early eighties as Thailand attempted to recover from the impact of the second oil crisis. In 1981, General Prem, who headed the government from 1980 till 1988, sought the assistance of the private sector to help stimulate the Thai economy.¹⁷ The quadrupling of oil prices increased the balance of payments deficit to alarming levels. Prem asked the representatives of the peak industrial associations for help in addressing the external deficit problem. The creation of the JPPCC where development policies could be discussed jointly and openly by high ranking government officials and private sector representatives was their response to Prem's request. With the active support of government technocrats, their recommendation became a reality.¹⁸

Through the JPPCC, information about the impact of regulations, tax measures, and trade policy on the performance of

16. Military-bureaucratic governments often create corporate bodies to represent key sectors of the polity and then controls these bodies by designating the representatives. This is generally referred to in the literature as bureaucratic corporatism (see for instance, Ch.4, Staniland (1985).

17. Laothamatas conjectures that Prem may have given serious thought to creating the JPPCC, which the peak associations had long been clamoring for, in order to establish an alternative base of political support. In 1980 he barely survived an attempted coup by so-called "Young Turks" in the military.

18. The NESDB and in particular, its director Dr. Snoh, convinced the government to establish the JPPCC.

firms and more generally on the economy was transmitted more quickly thereby focusing the government's response to problems. Moreover, various industrial conglomerates were able to express their concerns over trade policy and to have those concerns addressed in a transparent (to members) forum. Hoping to reinvigorate a smothered economy, the Prem government adopted the recommendations of the JPPCC. Big business was incorporated into the policy making process and was given some measure of authority over trade policy.¹⁹ But perhaps the most important contribution of the JPPCC was the reduction of bureaucratic clientilism through the creation of an alternative, more transparent system of rent allocation. The need to minimize the consequences of bureaucratic clientilism was one of the principal motives for the Thai technocrats to actively support the creation of the national JPPCC. The principal sponsor among the technocrats, Snoh Unakol, had a very clear position on this matter. "In Snoh's view, Thailand had been close to the decadent model of capitalism. Government-business relations in the past had served only those few who had massive financial resources or good personal connections with high officials. These relationships created resentment among the business community, as well as the general public. . . . Snoh's proposal for government-

19. In some LDCs where big business dominates trade policy protectionist policies result, e.g. the Philippines. In contrast, in the HPAEs, government has dominated the private sector by controlling the extent to which the private sector participates in decision making. Historical factors are responsible for the difference. See for instance Hutchcroft (1991) and McCoy (1993) on the Philippines, Haggard (1990) on Korea, and Amsden (1979 on Taiwan).

business dialogues was guided considerably by his conviction that a new system must be built in which under-the-table dealings were reduced by the availability of on-the-table consultation, by the government's responsiveness to the legitimate requests of business, and by the deregulation of the economy (Laothamatas, 1992, p. 82).²⁰ Similarly, Robert Muscat explains that the experience "and the whole arrangement based on organizations, issues, and transparency, rather than inside dealings and the pursuit of individual commercial advantage, would promote the "maturation" of the Thai business sector and contribute to the reduction of particularistic or corrupt relationships between business and officialdom (Muscat, 183)". An important component of the business sectors maturation was the acquisition of "a professional capability for open policy discussions". Some of the leading associations commissioned research teams to persuade the government with analytical data. This included contracting with Chulalongkorn University to research the tax structure industries. Field surveys and harvest reports similarly were funded to influence official agricultural policy.²¹

20. In interviews, both a business tycoon close to the Malaysian Business Council and a senior fellow of a local think tank both raised similar points.

21. To protest official policy the Thai Rice Mill association refused to buy paddy from the government in 1982. A group of plant seed extractors took the Revenue Department to court to challenge increasing taxation on their raw materials. A content analysis of summonses issued by the House of Representatives to business associations for testimony indicates an significant increase: between 1984-1987 an average of 4.45 persons a month compared to 0.13 during the 1975-76 democratic years. (Laothamatas, 1988:457).

Only matters of general interest were discussed and unlike the meetings in Korea or Japan, the Thai meetings were open to the press which put pressure on the prime minister to respond to business's proposed reforms. Among the innovations that occurred as a result of the JPPCC dialogue were the development of graduate education in modern business management, incentives for family firms to go public by issuing equity and establishing standards for disclosure. Investment by multinationals was encouraged in joint ventures with Thai firms. The JPPCC was critical in orienting the economy towards manufactured exports. Significant progress resulted towards establishing international competitiveness and modern business practices. In particular, rules, regulations, and tax measures that governed the export of domestically produced or processed manufactured goods were streamlined and rationalized in order to reduce the production costs of manufacturers and to enable them to compete internationally.

Nevertheless, the consultative process in Thailand has been faulted for failure to develop channels for the representation of small farmers and non-unionized labor. The JPPCC does not represent labor, farm or public enterprises. At the least, the councils helped the new professional business sector to establish a foothold in the policy dialogue and to challenge the domination old style sector based on clientelism. It also signaled the government's commitment to professionalism and to the affirmation of international business practices. The blatant exploitation of office holders to obtain privileged access to government favors

by the latter resurged, however, during the Chatichai (July 1988-February 1991) administration (Muscat 257-258). Although that Chatichai government represented the political ascendancy of business, it has less successfully advocated consistent business policies than its predecessor. The pursuit of the spoils of office once again disrupted the dialogue for a coherent policy framework.²²

The shift to an export-oriented economic strategy is perhaps the greatest achievement of the expanded government-business dialogue (Laothamas). But the sources of mistrust have not yet been eliminated. The JPPCC format did not lead to the kind of close collaboration between business and government characteristic of Japan or Korea. Business was unable to impose accountability on the bureaucracy which issues licenses and registers business associations. Measurements of transparency and predictability in the regulatory environment still rank Thailand lower than the first tier of high performers. Robert Muscat explains that lack of transparency diminishes confidence of investors in the state administrative capability. "Most Thai legislation is very brief, limited to granting specified ministries, or departments within ministries, broadly worded empowerment. Legislation typically contains no instructions as to when, when, or to what extent the powers granted must or must

22. Muscat explains that "rivalries among a handful of individual businessmen and groups, then having captured the very mechanisms designed to regulate them and dispense public resources, took center stage"(184). "Decisions on large projects were often made peremptorily without the benefit of NESDB review and without advanced circulation of documentation"(179).

not be exercised. The departments are thereby given wide discretion to apply the law as the bureaucracy sees fit (Muscat: 267).²³ Hence enthusiasm for more government guidance of the economy is weak. That skepticism means Thai Inc. would draw together few enthusiasts. While eschewing guidance, industry does advocate increased government support for export promotion, services, science and technology development (Muscat:261).

The popularity of the national JPPCC led the Prem government to establish provincial Joint Public-Private Consultative Committees.²⁴ The provincial JPPCCs were to be headed by the provincial governor. Since the provinces did not have formal industry associations, except for branches of national federations in some regions, the government required that a chamber of commerce be established before a province could

²³. "Normally, no processes of public or parliamentary review, or limitations on regulatory discretion, are included in the empowerments. Cabinet approval of regulations is normally required, but in practice cabinet members seldom object to a regulation tabled by an issuing minister for formal approval; to do so would invite retaliation when an objecting member tables his own regulations at some future date. Past practice is no guarantee of how any law might be implemented by a future department head. Past applications (e.g., regarding tax liabilities) can be reversed in retroactive administrative determinations. Few laws contain mechanisms for controlling abuse of discretionary powers."Muscat: 267-68.

²⁴. Robert Muscat speculates that the JPPCC declined when the Chatchai business cabinet (July 1988-February 1991) made it unnecessary. "The policy and regulatory framework that is the natural subject of interests to the private sector across the board receded into the background as the rivalries among a handful of individual businessmen and groups, then having captured the very mechanisms designed to regulate them and dispense public resources, took center stage. The further evolution of institutionalized relationships between government and business organizations was put on hold as the individual businessmen/politicians and government leadership became one and the same." p. 184.

qualify to form a JPPCC. This has led to the development of provincial chambers and the proliferation of provincial JPPCCs. Views on their effectiveness vary considerably. Only time will tell whether the provincial offspring can duplicate the success of their parent.

2.5 MALAYSIA

A lack of confidence stymied the collaboration of business with government until the early 1990s when Malaysia too learned about the benefits of formal coordination of information flows. There, business - government relations have evolved through three phases: the free market phase (post independence to 1970); the Bumiputera or New Economic Policy (NEP) phase (1972 to 1985); transition to the New Development Policy (NDP; 1986 - 1990).²⁵ In phase one, the government basically allowed the private sector to function freely and was primarily concerned with infrastructure building. In phase two, in response to the racial riots of 1969, the government introduced the Bumiputera Policy. As discussed earlier, the policy was meant to narrow the wealth gap and enable native Malays to participate in trade and industry by requiring minimum Bumiputera participation in economic activities. During phase three (which roughly coincides with Prime Minister Mahathir's leadership), the antagonism which characterized government-business relations in the second phase was gradually redressed. Firms with less than Malaysian \$2.5M capitalization were no longer subjected to the requirement that

25. The New Development Policy was introduced officially in 1991 as the successor to the twenty year program embodied in the NEP.

30% of its stock be sold to Bumiputeras. The NEP was essentially transformed into the NDP in which big business has been given the primary role of leading the development of the country. This thrust is expressed clearly in Mahathir's Look East Policy. The first sign of a change was the creation of the so-called Budget Dialogue in which captains of industry are called in to discuss the national budget with finance officials. Then advisory groups for certain sectors were formed. Each group includes representatives from industry and government. The members participate in the formulation of policies as well as in the development of strategies for implementation. Finally, the Malaysian Business Council (MBA), which includes 60 members from private industry, some members of labor, several government ministers and deputy ministers, and the Prime Minister who acts as chairman, was established. The MBA facilitated direct communication between big business, labor, and the Prime Minister.

The use of councils actually dated back to as early as 1981. A confidential (government) study of business-government relations in the mid eighties uncovered informal councils tied to government ministries. An informal council basically made evaluations of a ministry's regulations. It was further discovered that a council's effectiveness depended on the participation of individuals from the private sector. Those that had members from the private sector produced output that became useful to the ministries as well as to the private sector groups the latter regulated: rules and regulations were revised to

reduce the burden on the private sector. Those that did not failed to provide useful recommendations to problems they were asked to address. These findings largely influenced the formation of the Malaysian Business Council and the Budget Dialogue Group in which private sector representatives participate as active and equal members.²⁶

It is still too early to evaluate the effectiveness of the MBA and the Budget Dialogue Group and to establish exactly what their functions. Personal interviews with some participants suggest that, like the JPPCC in Thailand, the MBA has helped move rent-seeking from covert, under-the-table dealings to more transparent, over-the-table transactions.²⁷

3. COUNCILS AND ECONOMIC PERFORMANCE

As the preceding examples illustrate, deliberation councils yield economic benefits. A council serves as a convenient channel for collecting relevant information from and distributing it to its participants. It thus improves economic efficiency: it supplements the allocative function of markets by facilitating coordinated responses to changes in economic conditions. A council also helps reduce losses from rent-seeking by reducing the size of the "Harberger" triangles and the magnitude of the "DUP rectangles."²⁸ Furthermore, a council performs a commitment function, binding sovereign authority to a set of

26. Critics point out that labor is not adequately represented in these consultations.

27. See Malaysian Business Council, Institute of Strategic and International Studies, Kuala Lumpur, 1993.

28. See Bhagwati and Srinivasan (1982) for a definition and discussion of Directly Unproductive Profit Seeking (DUP) activities.

rules governing economic policy making. Hence, it helps minimize economic distortions attributable to dynamic inconsistencies.²⁹

3.1 IMPROVING COORDINATION

Although the HPAEs have all established various mechanisms to reduce the (transactions) costs to firms and government of obtaining information about markets, councils stand out as particularly useful mechanisms to transmit information. Changes in world markets, new trends in technologies and perverse effects of regulations domestically and abroad are all communicated to the bureaucracy by private sector agents. In turn, the bureaucracy synthesizes the information and communicates this synthesis through a proposed plan(s). The potential effects of the plan(s) are relayed by private agents back to the bureaucracy for possible alterations. This interactive process continues until a consensus is reached. In short, deliberation councils provide a built-in feedback mechanism that helps the public and private sectors adjust to a changing environment. They "can acquire more information than any one individual (member) for it has each member performing different experiments. Thus, the limitations on an individual industry's or firm's (italics own) capacity are overcome (Lim, 1981, p. 15)." While deliberation

29. See Rodrik (1989) for a discussion of the problem of promises and the lack of credibility within the context of policy reform.

councils cannot substitute for the informational attributes of markets, they certainly supplement them.³⁰

Problems involving synchronization frequently arise in development.³¹ They arise, for instance, in new industries with potentially large scale economies. As Milgrom has pointed out, "economies of scale that are achieved in the manufacture of components of several products increase the need for coordination because the optimal scale of each product is an increasing function of the anticipated scale of the other products that use the same components (Milgrom and Roberts: 106)." From this perspective, consider the following advantages of councils as coordination mechanisms: if a new airport is to be built roads and trains to the airport must be ready by a target date. To induce a company to invest in creating the roads might require assurances that another firm has agreed to construct the airport. Similarly, hotel keepers will invest once they are assured of the behavior of other relevant investors. Information demanded to achieve coordination required for a new airport may not be efficiently conveyed by the price system. Councils offer supplemental sources of information providing decision makers with feedback about how parts toward a large project fit together. They provide a forum to communicate strategy to all members of an industry. When a lack of synchronized behavior may be costly to several parties, the council can be especially

30. In fact, DCs work because they use markets as their guide. The plans developed jointly by the public and private sectors are tested against the realities in the market place.

31. See Gershenkron, 1962.

helpful. For example, the price system does not take into account the true marginal cost of the early introduction of a product. Knowing the number of possible delivery dates requires communication not necessarily conveyed by prices. A council meeting can more easily reveal the marginal costs of a speed-up for each supplier, making it possible to predict the cost of the final product. Councils are thus helpful when inducing private sector actors to make one set of investment requiring assurances that a related set will also be made.

Deliberation councils have helped the Japanese produce goods that require coordination from several firms within an industry. This often involves identifying product potentials of several firms within the industry and agreeing on a program to coordinate production so that the new product can be developed. Councils allow Japanese planners to identify groups of industries or activities that fit together and can also help to avoid the duplication of effort in the introduction of new products. When problems emerge councils permit a centralized response to a crisis within an industry. The industry can then respond more quickly than firms having only decentralized information. Thus, on a number of dimensions councils allow for the coordination of strategic production and distribution decisions.³²

Deliberation councils also help resolve externality problems (which in essence are also coordination problems). For example, an exporter that breaks into a foreign market bears all the costs

32. Councils are not the only means available for firms wishing to coordinate decision making. Japanese business practice includes other methods of promoting cooperation among firms.

while results can easily be copied by firms which did not pay the initial costs of gaining entry.³³ In the council, the costs of learning about new markets are distributed among council membership (World Bank, 1993).

A council might also help distribute burdens from future crises thereby reducing the overall risk of a project (Yamamura, 1986). In Japan, for example, members of a council will shoulder the costs of a collective decision that causes a weaker member to go bankrupt. When downsizing is called for, the biggest firm in the industry may be asked to absorb smaller companies that take the loss.

3.2 TAMING THE RENT-SEEKERS

Whereas an absence of transparency has allowed governments of many developing nations to reserve economic opportunities for their clients, councils have permitted the HPAE regimes to avoid this pattern. In the council, information about the policy environment is shared among all players. Each has access to the same information and information flows both ways. By contrast, in many developing countries, policy relevant information is asymmetrically distributed. Private sector firms do not know what their competitors know and hence are uncertain about what their competitors will do; even announced government plans cannot be trusted. In essence, when the parties have unequal information they mistrust each other and hesitate to cooperate on joint projects.

33. In a discussion of risk sharing, credit markets, and participatory government intervention in Korea and Japan, Cho and Hellman use the tools of institutional economics (1993).

Mistrust creates a strong impetus towards rent-seeking. In the absence of a credible and transparent policy regime governing market competition, pressure groups have incentives to lobby government officials. Lobbying is a defensive measure that often occurs when each group assumes that others lobby to acquire as large a share of the market either directly, e.g. logging concessions, or indirectly, e.g. import quotas. Hence, to protect its turf, each is induced to engage in as much lobbying as can be afforded. Seeking special deals or privileges thus becomes a modus operandi of groups. A council can eliminate this uncertainty and reduce mistrust by making policies transparent to all affected parties: by making information available to all, a council makes it more difficult for individuals or groups to obtain special favors from the government and for government officials to provide special treatment to particular individuals or groups.³⁴ Welfare losses attributable to directly unproductive profit seeking (DUP) activities can thereby be reduced.

In sum, when rules, procedures, and regulations are discussed openly among the relevant parties and input from all parties is encouraged a more transparent and impartial policy environment emerges. This constricts the possible avenues for seeking or granting special favors and raises the cost of and reduces the potential gains from rent-seeking. Councils help

34. Campos and Lien (1994) show that, if firms can reveal information without fear of being taken advantage the level of rent-seeking falls, i.e. firms have less incentives to engage in lobbying.

limit the perverse effects of rent-seeking: members effectively agree to the rules of the game that ultimately determine how rents are to be distributed among them. The rules could directly specify the distribution as in the case of industry downsizing in Japan (Yamamura, 1986) or indirectly as in the case of export performance criteria in Korea (Lim, 1981; Amsden, 1989; Haggard, 1990; Chang, 1993).³⁵ In either case, rent shares are negotiated in an (relatively) open forum making it difficult for individuals or special interest groups to seek special treatment and thus to derail good policies.

3.3 AN IMPLICIT CONSTITUTION: COUNCILS AS COMMITMENT DEVICES

The use of deliberation councils to coordinate economic policy creates a structure of rights and expectations that induces investor confidence. In effect, a de facto constitutional framework to direct economic decision making is erected.

Violating the implied norms imposes costs both on the government and on the private sector operators. To violate the procedural norms or etiquette that governs economic decision making would require altering the rules governing the creation of policy.

Changing the rules imposes costs of its own. The party that forces those changes may ultimately wish for the protection they have abandoned. To avoid procedural changes that may lead to unexpected policy outcomes, officials may decide to stay with the rules already in place. Moreover, an attempt to force a change

35. In the latter case, firm subsidies are based on their export performance and thus on the ability of firms to compete; in the former, the government through the council, determines which firm(s) absorb the less profitable ones in the industry.

in the rules without private sector participation would undermine the future value of the councils as a coordination and rent-sharing mechanism. That in turn would make policy making more difficult.

Ultimately, the councils are commitment devices that restrain governmental discretion.³⁶ By granting authority to deliberation councils the government gains authority. As Okimoto puts it "without industry's willing cooperation, the Japanese state would not be nearly as powerful or effective".³⁷ An agreement from a deliberation council represents unanimity within an industry and increases the likelihood of legislative approval. In effect, the government relinquishes authority to gain the possible consent of the private sector to promote a government

36. It is often argued that Korean business-government relations have been one way with government bribing, cajoling or coercing, private sector firms (Amsden, 1989; Haggard et al, 1990; Lee, 1992). But it should be emphasized that the government has applied the carrot and the stick impartially and consistently. If a firm fails to deliver, it is penalized; if it delivers, it is rewarded. That is, the Korean state has refrained from the predatory behavior so characteristic of many dictatorships.

Of course, the question then is how credible is the state's commitment to impartial and consistent implementation of the carrot and stick? Reputation is critical. If the state's goal is to promote growth, and it depends in part on the private sector help (which was certainly the case in Korea), then it must necessarily obtain the cooperation of the private sector by building a reputation for impartiality and consistency. By contrast, favoritism encourages rent-seeking which results in uncertainty regarding the "rules of the game." This restrains growth by making it difficult to obtain the needed cooperation. In short, the long run cost to the state of ruining its reputation is a disincentive to playing favorites.

37. Okimoto, page 145. "Instead of labeling Japan a strong state, therefore perhaps it would be more accurate to call it a "societal", "relational", or "network" state, one whose strength is derived from the convergence of public and private interests and the extensive network of ties binding the two sectors together".

program. By granting authority to the councils, the government gains credibility that it can implement its programs. This in turn makes the government a more credible player both nationally and internationally. An investor will choose a country where the government has the capability to protect the property rights of investors. The councils provide some of this capability because they imply that policies have the implicit consent of the relevant private sector actors. These rules are an implicit constitution providing guarantees against the imposition of policies detrimental to council members. Revisions of the rules or of policies are subject to the councils purview, thus providing economic actors with assurances against sudden policy shifts. By imposing restrictions on its ability to alter policy, the state makes the property rights of council members more durable.³⁸ Economic entrepreneurialism is encouraged by the knowledge that today's policies will not create the profits for tomorrow's confiscations.

3.4 FROM IMPORT SUBSTITUTION TO EXPORT ORIENTED INDUSTRIALIZATION

38. Economic policy can be viewed as a contract between government and the private sector (Williamson, 1985). However, contracts cannot address every possible contingency. To induce investments in fixed capital assets whose value is greatly reduced in alternative uses, i.e. asset specific investments, the government must be able to commit to not expropriating those investments whether directly through confiscation or indirectly through arbitrary and frequent policy changes, i.e. not renege on ex-ante agreements. But at the same time, the government must also have enough flexibility to change policy when external circumstances warrant. A council can serve as a "flexible" commitment mechanism.

Deliberation councils can play a critical role in facilitating the change toward export orientation from import substitution. By abandoning the relative comfort of the ISI regime, established firms open themselves up to the danger of losing market share by reducing their comparative advantage, e.g. knowledge of the domestic market and control over distribution, to potential domestic competitors. Deliberation councils can be harnessed to reduce this uncertainty and thus to provide better incentives for firms to support the export drive. Through these mediating institutions, information about developments in world markets is shared among all firms, giving each information needed to respond. Subsidized credit can be directed to good performers to reduce the risk of breaking into world markets. In some cases, established firms and the government agree to limit entry in the initial stages. In other words, these institutions help provide the necessary coordination needed to move from a low level equilibrium to a higher level equilibrium: because they guarantee the existing, and often the major, players that none will be disfavored in the fair application of the new rules and regulations. The institutions induce the players to participate more willingly in the new programs; a larger pie and Pareto superior allocations result.

The creation of the JPPCC in Thailand is a good example. "The JPPCC system was also necessitated by the fact that Thailand, in reaction to chronic trade deficits, decided to place an emphasis on export-oriented development. Snoh Unakol, the NESDB secretary-general under the Prem Administration, explained

that the JPPCC system was born out of an observation that 'any country which competes successfully . . . in the international economic arena is also a country with a workable system of government-business collaboration. (Laothamatas, 1992, p. 81)." As discussed earlier, the idea of a JPPCC was initiated by the private sector through representatives of the Thai Chamber of Commerce, The Federation of Thai Industries, and the Thai Bankers Association and supported by Snoh and other technocrats partly because of the need to make business-government relations transparent. In this context, the JPPCC can be viewed as a coordination mechanism designed to help move the Thai economy from an import substitution to an export oriented regime: transparency guaranteed that no firm would have advantages over others in the transition and that everyone would move in the same direction.

Public sources of credit are often necessary to promote an export drive. Private financiers have the means to test the waters in domestic markets but very rarely in foreign markets. Financiers are therefore reluctant to loan for exports and will consistently ration credit in favor of domestic production. Consequently, when domestic bankers combine with large, indigenous merchants, their preferred policy is a secure domestic market characterized by import substitution as opposed to exporting. But government subsidized credit is not sufficient to guarantee good export performance. The carrot, i.e. subsidized credit, without the stick, i.e. penalties, may result in investment without accompanying export growth. Firms may take

advantage of the credit but allocate it to non-export activities (see for example the study of Boyce (1990) on the Philippines). Councils can be especially helpful in providing information that will help the government to direct credit to high performing exporters.

The Monthly Export Promotion Meetings in Korea represent perhaps the clearest example of a council improving information flows and helping identify and finance high performing exporters. As mentioned earlier, these meetings facilitated the setting of export targets based on information provided by both private enterprises and government agencies.³⁹ They also became the forum through which the carrot (rewards such as credit) and the stick (penalties such as withdrawal of foreign exchange privileges) were made credible.

4. THE REGION AS MODEL: INFORMATION AND THE TRANSITION TO A MARKET ECONOMY: OVERCOMING PATRON-CLIENT TIES, A ROLE FOR COUNCILS.

One of the policy assumptions generated by neoclassical economics is that in the absence of interest groups, governments will redistribute resources in a benevolent or unbiased fashion. The assumption that a distributionally neutral state would exist if not for interest group mobilization is particularly unrealistic when applied to developing nations where patron-client networks are the alternative to lobbies of organized interests. Lacking in the neoclassical assumption is an appreciation of the critical role played by institutions. In

39. Chang, 1992.

fact, the East Asian experience with councils suggests that the organization of interest groups is endogenous to institutional design.

Typically developing nations lack institutions that spread information symmetrically between private and public sector players allowing officials to reserve information concerning the regulatory apparatus of the state for the use of privileged regime insiders. One reason for the primacy of patronage is that when organizational activities outside the state are weak, policy making is easily dominated by privileged elites that flourish on clientelistic ties to political leadership. When an opaque legal and regulatory environment allows government officials to reserve economic opportunities for their clients, the regime can control access to the market in order to build a base of political support. When patronage becomes central to the support base of the regime, public and private objectives is widely divergent and mistrust clouds relations between representatives of both groups. Informal contacts between the ministries and government-chosen representatives of the private sector does not overcome that mistrust.

A more formal structure was necessary to reduce the mistrust that characterized the relationships between the private and public sector in all of the East Asian high performers. The extent to which leaders depend on patron-client networks influences their ability to implement market-oriented policies fairly. Therefore, it is necessary to protect ministers from business people who wish to use connections to win exceptions,

privileges, or modifications to rules. The closer an individual's ties to a regime, the more difficult it is for the regime to enforce rules that would alter the individual's behavior.

The creation of formal channels of contact between a minister and those over whom he has tutelage becomes all the more critical when reform packages call for sacrifices from potential supporters. Confronting a close friend, business partner or relative with a demand for sacrifices in the national interest is not easy. When the affected parties are connected to regime officials they may seek relief by gaining special exceptions rather than changes in policy. Thus critical to development is the design of institutions that prevent patronage networks from determining the allocation of economic resources.

The East Asia case highlights the advantages of augmenting the organizational capability of the private sector as a first step in establishing broad based accountability in government. It demonstrates that the design of the state/society interface determines the equilibria relationship that motivates the economic behavior of firms and individual. Impersonal institutions such as deliberative councils, if devised properly and promptly, can weaken patron client ties by diffusing the access to regime officials, thereby strengthening the regime's ability to distribute the benefits of growth broadly.

One objective of councils is to mitigate the effects of rent seeking on growth. The advantage of policies approved by councils is that members will have to accept changes and adjust

to rules that apply to all; their lobbying will quickly become known to other members of the council if they seek exceptions. A second advantage is that when rules and procedures for public/private interfacing are established, the bureaucracy has more authority to resist pressures from powerful individuals. The existence of fixed rules will help insulate the bureaucracy from direct political pressure by powerful individuals or groups. The private sector gains because the design of such institutions will make it costly for the regime to renege upon agreements. Once a commitment device is established, investments that generate a reduced stream of benefits for a guaranteed longer time become more attractive.

The procedural apparatus associated with democracy, most notably multi-party elections, does not eliminate the primacy of patronage in economic exchanges. Even after elections, rarely do organized interests exist to whom political leaders will be accountable. Elections only shift the locus of corruption from an appointed to an elected official. Councils, by contract, allow administrators to make a claim of representing a constituent group and that a consensus of private sector representatives stand behind policies or deals brought before the Parliament for approval. This would make it more difficult for an individual legislature to secretly provide favors.

The constitutions of many new democracies give the bureaucracy primacy over the legislature in the drafting of laws. Although the legislature must approve the laws, the bureaucracy studies, analyzes and drafts the bills. Considering an

administration's lack of familiarity with commercial matters, open and rule bound consultation with private sector representatives is likely to produce more appropriate legislation. This in turn increases confidence among the business community in the regime.

When the process of rule making by the ministers is not generally specified in the new constitutions, it must be made explicit before specific reforms can be crafted. Generally, the constitutions of recently established parliamentary regimes anticipate that ministers will bring regulation to the parliament for approval. Public administrators do not generally possess the expertise to act alone and cannot afford to leave the private sector out of the rule making process. However, the constitution typically does not provide direction for ministries to get the consent and participation of the relevant private sector actors. Nor do parliaments have committee structures to evaluate the regulations they are likely to receive for approval. Before creating effective legislation and regulation, an open method for consulting private sector representatives must be established. The Japanese case is particularly relevant because there ministers worked with deliberative councils on the creation of regulation before submitting it to the Diet. The Parliament was more willing to approve regulations that carried the unanimous support of the relevant deliberative councils. The councils also gave the process of ministerial-legislation drafting the appearance of democratic legitimacy which it might otherwise have lacked.

5. CONCLUSION: THE POLITICAL ROLE OF COUNCILS

The East Asian experience reveals that access to information by all parties is essential for economic development. Information to make effective economic decisions is usually lacking in autocratic governments because the private sector has incentives to dissimulate and deny information to autocrats that can later use their knowledge to expropriate profits, to penalize dissent and to privilege insiders and allies. Information is usually used to maintain power, not to promote welfare enhancing policies. As a result autocrats typically lack information about private sector development and the private sector usually has unreliable information about government programs and intentions. Thus, autocracies have a problem of credibly committing to growth enhancing policies. Dictators are unreliable partners in trade because of their above-the-law status.

The public\private sector interface developed by East Asian leaders diverges from the patterns of information aggregation characteristic of autocratic regimes. The institutions which made this effective aggregation possible are partly responsible for the fact that the level of private sector investment as a percentage of GDP is higher for East Asia than for their developing counterparts among the world's low and middle income nations.⁴⁰

In all the HPAEs, the legislature is significantly weaker than the executive branch. In Japan, the Liberal Democrat Party through the Prime Minister has generally dictated the thrust of 40. Even after one corrects for per-capita income.

policies minimizing the input of debates in the diet. This top-down approach to policy making has earned the HPAEs the reputation as authoritarian states. Modifications to this conception are needed especially if one considers that surveys of democracy typically correlate Asian government with that of Africa as examples of autocratic rule.⁴¹ Because the standard indices of democracy are not sensitive to the participation in policy by consultative bodies, they fail to reflect a fundamental difference between the polities of Asia and those of Africa. Consultative polities differ from autocratic regimes as much as they differ from representative regimes. Councils allow select groups in the private sector (based on function rather than on personal ties) to express their views on economic policies and have those views integrated into the final policy output. This feature gives councils credibility and legitimizes government economic policies: councils grant the private sector participants some influence over the rules that are to govern

41. The Freedom House correlates the political systems of Korea, Malaysia, Singapore, Taiwan, and Thailand at the same anti-democratic extreme as a number of African regimes. The ratings which began in 1973 rank the tigers in the same category, partially free, with Liberia 74-79, 83-88, Lesotho 73-87, Madagascar 73-75, 77-78, 82-90, Senegal 75-91, Zimbabwe 80-88, Zambia 73-87, Tonga 73-91, Uganda 80-91, Cameroon 73, 76, Ivory Coast 79-87, 90-91, Kenya 72-86, Swaziland 72-87. The definition of political rights and civil liberties used in the rankings do not prioritize transparency of the regulatory environment, bureaucratic integrity, equal access to information by private sector operators, consultative instruments, security of property rights, freedom to contract, and the reliability of government commitments. Leaving out the factors contributing to private sector strength and government credibility, the survey does not reflect the conditions that ultimately create a firm foundation for an independent civil society.

their sector and prevent those rules from being altered without consultation.⁴²

In sum, Japan, Korea, Malaysia, Singapore, Thailand and Hong Kong, all developed an effective state/society interface with real input into the policy making process. These consultative bodies induced private sector cooperation with the regime and helped to draw the elites into the process of market-led growth. Councils allow rules governing rent sharing to be explicitly and openly stated so that each participant is assured that the same regulations apply to all players. Similar assurances of consistent private sector input into policy formation are rarely provided by autocratic governments. The same institutions that are designed to win the cooperation of business groups, the deliberative councils, imposed oversight on bureaucratic activity, reducing both patronage and corruption. Administrative oversight, and open lines of information sharing between the private and public sectors, allowed the high performers to provide a level of accountability, transparency and predictability in policy formation that is sometimes found in mature democracies. Nevertheless, observers all too often confound good governance with the type of political regime. East Asia's experience suggests that the foundations of good economic governance, commitment, coordination and consultation, are independent of regime type.

42. It should be pointed out that in the early stages of English parliamentary government, representation was limited to a small privileged group (Root, 1994). The councils are functionally similar to England's ancient parliamentary system.

East Asian rulers gave bargaining power to constituent groups in exchange for information needed to formulate rational economic policies. Thus they were able to overcome the inefficiency of limited communication about policy performance that typically hinders development and assures the survival of ineffective policies in much of the developing world. Being allowed to share in the bargaining surplus induced the private groups to reveal private information.