Review: Explaining the Flexible Rigidities of East Asia

Henrique Grazziotin

Ha-Joon Chang. "Explaining 'Flexible Rigidities' in East Asia". In: CHANG, Ha-Joon. *The East Asian Development Experience: the Miracle, the Crisis and the Future*. Penang: TWN; New York: Zed Books, 2008.

Palavras-chave: Leste Asiático, Desenvolvimento, Estado Desenvolvimentista

Key words: East Asia, Development, Developmental State

The economic development of the East Asian countries since the 1950s is certainly one of the most relevant phenomena in the world economic history of the post-Second World War period. With the leadership of Japan, the first country in the region to accomplish structural transformations on a great scale, and then followed by South Korea, Taiwan, Hong Kong, Singapore and China, this period witnessed considerable improvements in the standard of living of the population with elevated income growth *per capita*. This process transformed productive structures, leading to a global reorganization of production with direct impacts on Western Europe and North America. With spectacular success in export markets through the technological transformation of its productive matrix, this phenomenon is even more surprising for the Asian countries since they are countries that share the characteristic of low endowment of resources and a high population density.

Success in the industrial sectors of high technology, such as electronics and automobiles, is a consequence of the rapid capacity of structural transformation acquired in this period as well as the capacity to adjust to the external shocks of the 1970s and 1980s. Many scholars in economic history have offered interpretations of the success of East Asia in the post-war period with little consensus regarding the causes. Our objective in this review is to summarize some of the considerations of Ha-Joon Chang on this process, focusing on the idea of "flexible rigidities" in East Asia and exploring the relation between flexibility and rigidity in the market and its impacts on development. The explanation for this relation is present in the chapter "'Flexible Rigidities' in East Asia" in his book *The East Asian Development Experience: the Miracle, the Crisis and the Future*.

Chang belongs to a series of economists influenced by the singularity of the experience presented in the East Asian countries who began to study regional development through an historical perspective focusing on the developmental policies of states. Among this group of authors, we may also highlight Chalmers Johnson (1982), Peter Evans (1995), Alice Amsden (1989) and Robert Wade (1990), who have sought to understand the different spheres of the relations between state, society and economic environment, stressing the elements which allowed the state, or not, to impel great structural transformations. Their studies are relevant not only to understand the specific historical experiences of the Asian case, but also as a lesson for other countries currently undergoing development to accomplish similar transformations. The influence of theorists of the developmental state is growing in regions such as Latin America, and despite the recognition of the unique and specific character of each experience of economic development, their studies are essential to better understand the relations between state and society.

It is worth emphasizing that the development of East Asia is above all a phenomenon of great complexity that involves many elements that are directly interconnected. These include, among others, the class structure of each national society and the correlation of forces existent in society, the capacity of the bureaucracy of the different states, the international insertion of each country in political and economic terms and the technological capacity developed in industry. Therefore, its explanation requires an ample research effort to demystify the process. *The East Asian Development Experience* is a collection that aims to contribute to this effort. It includes articles published by Chang in the 1990s and 2000s, exploring diverse explanatory factors for Asian development. The book also offers a wide-ranging discussion on the Asian financial crisis and the future of the region in the post-crisis period.

For Chang, one of the principal reasons for the Asian "miracle" is the existence of "flexible rigidities", an explanation that runs against the policies proposed by conventional economics. Chang's perspective focuses on the actions of the state and private sector agents in the creation of rigidities that in the neoliberal vision would supposedly hamper the efficient allocation of economic resources. Yet he concludes that such actions are a crucial factor in explaining the success of these countries. Based on the notion of dynamic efficiency, Chang argues that although they reduce flexibility in the short term, restrictions on the mobility of economic factors (rigidity) may lead to a greater flexibility in the long term due to the greater economic growth that results.

Chang begins his exposition with the neoliberal interpretation of the causes of economic development in East Asia.[1] This conception attributes the Asian success to free-market policies, based on the idea that the more flexibility in the allocation of factors of production, the more efficient the productive process will be. In these terms, the neoliberal argument posits that all rigidity will impede the efficient allocation of resources and is synonymous with economic inefficiency,with the action of the state one of the principal causes of market rigidity and allocative problems. Consequently, the flexibility generated by a "minimum non-intervening state", following the neoliberal logic, allowed resources to freely follow the signals of market prices in the search for the most lucrative allocation. Therefore, the case of development in East Asia in the post-war period is interpreted by neoliberal economists as a result of the full flexibility of the free market.

In reality, Chang affirms that many of the rigidities associated to economic problems by the neoliberals existed in East Asia with some created by state action and others by the very behavior of the private sector and that these were not necessarily damaging to development, but actually beneficial. For example, there was the strong application of an industrial policy applied to specific sectors with strong restrictions on the entrance to and exit from markets, changes in productive capacity, price changes and the choice of productive techniques. There was also ample banking and financial regulation with state banks utilizing credit to direct to strategic sectors, thus controlling the entrance and exit of capital from the country. In the labor market, there was the utilization of income policies and "protective" labor laws for the worker.

Not only the state is capable of creating certain rigidities to market activity; private sector actors also display this behavior. Some consumer markets, for example, presented difficulties for the entrance of new competitors due to the high degree of consumer loyalty. Industrial organization itself, created through networks of subcontractors (the *just-in-time* organizational model) showed a high degree of rigidity since a company within this arrangement maintained preferential suppliers through long-term contracts, relinquishing possibly higher profits in the short term by contracting lower-cost suppliers. Another common

[1]Chang characterizes neoliberalism as the "profane alliance" between the neoclassical and Austrian schools of economic thinking. The former would be responsible for providing mathematical and analytical instruments to the neoliberal vision, giving it a "scientific character" while the latter would be responsible for the ideological and political character in defense of the "minimal" state. For more details, see Chang (2002).

practice of the private sector that created rigidity was the maintenance of cartels organized byindustrial associations in moments of strong growth or recession with the objective of preserving the profits of producers or blocking new competitors from entering in the market. It is worth emphasizing as well the fact that in the Japanese labor market, the existence of lifelong jobs was a common practice as well as salary determination by length of service and not by effort or qualifications as is required in "flexible" labor markets.

East Asia, therefore, contained many of the rigidities condemned by the neoliberal vision, necessitating a distinct theoretical reflection to understand how rigidities influenced the Asian economies in the long term. Chang argues that, assuming the existence of a limited rationality, rigidities, in the sense of limitations, are an essential part of human life without which no complex human system could be efficient: "agents with limited rationality need some behavioral rules that limit the flexibility of their actions in order to deal with the complexity of the world" (p. 117). Thus, a certain degree of rigidity is an essential part of life and, consequently, of the functioning of any economic system and not an "artificial" element created by the government or interest groups as in the neoliberal conception.

What Chang aims to demonstrate in this work is that restrictions to the free mobility of economic factors through market rigidity may be beneficial for the long-term development of a country. The reduction of flexibility of such factors in the short-term may lead to greater flexibility in the long term to generate innovative technologies. In an analogous form, the reduction of individual flexibility may amplify the flexibility of the national economy as a whole since it may maintain the factors of production in the country, avoiding capital flight, for example, and generating growth in production.

The historical experience of countries like Japan, South Korea and Taiwan corroborate the ideas of Chang. With the intention of obtaining more technological capacity for the national economy, national states intervened in the transformation of the economic structure, focusing on high-technology industries. To accomplish this, the state frequently had to reduce the short-term flexibility of the market. Cartels were created to defend certain sectors in Japan based on the idea that obtaining technological capacity was directly related to the learning process of a determined productive activity, requiring a stable environment for innovation. Another example is the protectionist policies to promote infant industries. These policies were forms of temporarily suspending the market mechanisms of prices to obtain technological capacity. Chang stresses that the cartels and protectionist policies were gradually removed as companies acquired such capacities, obtaining technological competitiveness: "These policies provided the time and the resources for the firms of these industries to accumulate technological capacity through learning, which proved critical in their posterior incursion in world markets" (CHANG, 2008, p. 126).

Another important form of state action in East Asia is related to the control of capital and the importation of technology. Chang affirms that the East Asian countries adopted a systemic vision of flexibility, rejecting the idea that maximum individual flexibility signifies maximum flexibility for a country as a whole to deal with economic problems. Thus, the state restricted capital mobility in such a way as to avoid the flight of capital and controlled the importation of technologies in accordance with the project of national development.

Lastly, Chang argues that the developmental states did not deny the fact that markets are fundamentally political, differently than the neoliberal ideas that markets should be "depoliticized". Therefore, the processes of structural change on a large scale were discussed and resolved politically without relegating such a process to the "natural" forces of the market. One example is the program of industrial restructuration in South Korea in which the state and the industrial sector negotiated agreements to overcome problems of profit generation.

Although he is capable of describing only a part of the complex phenomena involved in Asian development, Chang has developed a heterodoxical approach very different from the conventional interpretation. He shows how restrictions to the free mobility of the market may be important in the long term for nations. A reading of Chang leads us to believe, as Shakespeare put it in *Hamlet*, that "There are more things in Heaven and Earth...than are dreamt of in...[neoclassical] philosophy". Authors who have studied the historical experience of East Asian development have frequently put these questions on the agenda. Reading them is thus very relevant in our days.

BIBLIOGRAPHY

AMSDEN, Alice. *Asia's Next Giant*. New York: Oxford University Press, 1989.

CHANG, Ha-Joon. "Rompendo o modelo: Uma economia política institucionalista alternativa à teoria neoliberal do mercado e do Estado". In: ARBIX, Glauco et alii (eds.) *Brasil, México, África do Sul, Índia e China: diálogo entre os que chegaram depois*. São Paulo: UNESP, EDUSP, 2002.

CHANG, Ha-Joon. "Explaining 'Flexible Rigidities' in East Asia". In: CHANG, Ha-Joon. *The East Asian Development Experience: the Miracle, the Crisis and the Future*. Penang: TWN; New York: Zed Books, 2008.

EVANS, Peter. *Embedded autonomy: States& industrial transformation*. Princeton, Princeton University Press, 1995.

JOHNSON, Chalmers. *MITI and the Japanese Miracle*. Stanford: Stanford University Press, 1982.

WADE, Robert. *Governingthe Market*. Princeton: Princeton University Press, 1990.