CHAPTER 5
THE ROLE OF INSTITUTIONS IN ECONOMIC CHANGE

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Introduction

Institutions are systematic patterns of shared expectations, taken-for-granted assumptions, accepted norms and routines of interaction that have robust effects on shaping the motivations and behaviour of sets of interconnected social actors. In modern societies, they are usually embodied in authoritatively coordinated organizations with formal rules and the capacity to impose coercive sanctions, such as the government or the firms.[1] Everyone recognizes that institutions are fundamental to economic change. Nonetheless, despite a resurgence of "institutionalist" thinking inside and outside of economics over the course of the past 25 years, we are still a long way from a satisfying theory of institutions and their economic effects.

This paper is a modest attempt at pushing forward our thinking about institutions and economic change. Discontent with existing approaches to institutions is one motivation for this effort. The dominant economics canon, bent on conceptualizing economic change in ways that facilitate more elegant mathematical representation, has allowed itself to fall into a false parsimony that cripples its ability to understand major shifts in economic structures. Even conventional "institutionalist" explanations tend to reduce institutions to functionalist consequences of efficiency considerations or instrumental reflections of interests. Our aim is to move beyond this "thin" view of institutions toward a "thick" view, one which recognizes both the key role of culture and ideas and the constitutive role of institutions in shaping the ways that groups and individuals define their preferences.

Another conviction guiding this paper is that a better understanding of major changes in the global political economy is essential for practical as well as theoretical reasons. The current global economy leaves too much to be desired. Despite the paeans of the dominant canon to new "efficiency" of global markets, growth rates have still not recovered to match those of the pre-globalization period prior to 1973. More disturbingly, the growth that is occurring is of a highly inegalitarian sort that divides societies and provides a small minority of the world's citizens with large gains at the expense of social, cultural and ecological assets that are irreplaceable from the point of view of the vast majority. Equally disturbing is the increased volatility of new global markets, especially financial ones.

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[1] It should be emphasized that the market is also an institution supported by a range of formal and informal rules concerning its boundaries, its participants, and the terms of their participation. See Chang (2000b).

Concern over the negative outcomes associated with current patterns of globalization and the intellectual endeavor of replacing thin approaches to institutions with thicker ones are two sides of the same coin. Intellectually inadequate approaches to institutions lead to bad policy and welfare-damaging outcomes on the ground. People are hurt because social scientists and policy makers misunderstand institutions. Only a broadly conceived institutional analysis can provide a basis for theorizing a serious restructuring of globalization. To shy away from the effort to construct such an analysis would seem irresponsible, regardless of how difficult it may be to produce even a modest and preliminary version.

We set out our general conceptual framework in the next section. We argue that an institutional approach must do two things: first, develop a more adequate vision of how institutions shape economic behaviour and outcomes; second, create a more systematic and general understanding of how institutions themselves are formed and change over time. To construct such a vision we must get beyond the traditional view of “institutions as constraints”, focusing attention instead on institutions as devices which *enable* the achievement of goals requiring supra-individual coordination and, even more important, which are *constitutive* of the interests and worldviews of economic actors. Our goal is to move beyond the “thin” economistic models that dominate the current discourse on institutions. Neither a functionalist view in which what is must be “efficient” since otherwise it would not exist, nor an instrumentalist view in which institutions are created and changed to reflect the exogenously defined interests of the powerful are adequate. Instead, we argue for a more “culturalist” (or perhaps Gramscian) perspective in which institutional change depends on a combination of interest-based and cultural/ideological projects (in which worldview may shape interests as well as *vice versa*). Simply put, changing institutions requires changing the worldviews that inevitably underlie institutional frames.

Obviously, our simultaneous emphasis on the constitutive role of institutions and on a culturalist perspective on institutional formation suggests a perspective in which institutions and economic actors are mutually constitutive. This in turn leads to the danger of imagining a self-reinforcing homeostatis: if institutions shaped worldviews and worldviews shaped institutions in some simple way, stasis would result. To avoid this, it is necessary to understand how the process of constructing and maintaining institutions generates tensions and contradictions that force change, and further, how exogenous shocks may set off or redirect such processes. Lacking systematic theoretical leverage on this problem, we rely on our two case studies to give us some purchase.

The remaining sections of the paper present two strategic case studies; these illustrate our theoretical perspective and, at the same time, generate substantive propositions about the causes and consequences of institutional change with applications beyond these cases. The first case study focuses on the national context – specifically, the Korean developmental state. The developmental state provides a classic example of how institutions make a difference in economic change, as it is among the institutions that have most dramatically reshaped the relative national trajectories of economic growth in the late 20th century. Our attention centers not on the well-documented emergence of this state, but on its *fall*. Why should such an obviously effective institution be subject to political attack? And why should such an attack succeed so well in undermining this institution?

Next we present a case study of the World Trade Organization (WTO) in the context of the global political economy. This permits us to focus on how existing organizations of global governance shape the way rules are made and enforced. Our interest in creating more ideal configurations of global rules then leads us to ask: What kind of institution building is required to make the projected rules work, and what is the likelihood that such institutions can be constructed?

The two case studies complement each other and demonstrate the relevance of an institutional approach to the contemporary global political economy. Substantively, the question of what kind of division of labor does and should exist between nation states and international organizations in governing the global economy is hotly contested. The dominant canon has a simple answer: uniform rules, "objectively enforced" are the key to global efficiency; distinctive strategies, such as those created by developmental states, will and should be punished by "the market." Without "buying" this hypothesis we also assume that understanding the global context is essential to understanding the evolution of the developmental state. Conversely, the WTO is, after all, a membership organization whose members are states; its functioning is fundamentally shaped by old ideas of national sovereignty. Theoretically, the developmental state and the WTO provide opportunities for examining very different processes of institutional change: in the case of the developmental state, how established institutions are undermined and transformed; in the case of the WTO, how new institutions are invented.

Having analyzed the possibilities for (and failures of) economic governance in the contemporary political economy, our chapter concludes by returning to more general issues. On the substantive level, we examine the implications of the institutional trajectories we have described for the functioning of the contemporary political economy, and especially for the possibility of more equitable global growth. On a theoretical level, we ask what more general hypotheses about the role of institutions and processes of institutional change. We close with some thoughts on the prospects for building a real institutionalist alternative to the currently dominant canon.

Conceptualizing the Causes and Consequences of Institutional Change

In this section, we set out our general conceptual framework for understanding the nature and the changes of institutions, which will inform our discussions in the following sections. We begin by underlining the limitations conceptualising institutions as *constraints*, and go on to argue that they must also be seen not only as *enabling* but also as *constitutive* of the preferences and worldviews of their constituents. We then go on to critique theories of institutional change that see only efficiency considerations or the realization of interests as driving institutional change and argue for a more culturalist position.

Three Views on Institutions. Mainstream economists do not usually think about institutions; when they do, they see them as "constraints" on free markets that create inefficient "rigidities". The limits of this view are increasingly well known and we do not dwell on them here. What is surprising is that the rhetoric of "institutions as constraints" is also carried by many institutional economists who lean toward the mainstream – the so-called New Institutional Economists (Douglass North, Oliver Williamson, etc.). For example, according to North, "institutions consist of a set of *constraints* on behaviour in the form of rules and regulations; a set of procedures to detect deviations forms the rules and regulations; and, finally, a set of moral, ethical behavioural norms which define the contours that *constrain* the way in which the rules and regulations are specified and enforcement is carried out" (North, 1984, p. 8; italics added).

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

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

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

So shifting our rhetoric to the "enabling" dimension of institutions from the "constraining" dimension does not mean that we are negating the constraining nature of institutions. However, this is an important shift of perspective because we are then implicitly negating the view implicit in the "institutions as constraints" rhetoric that the unconstrained market (if such thing is possible at all) is the "natural" order (or what we call the "market primacy assumption" – see Chang, 1997, 2000a, and 2000b).[2]

However, there is a third and critically important view of institutions, which gets relatively little attention among economists.[3] This view sees institutions not just as enabling or constraining, but also as "constitutive".[4] This is because all institutions have a symbolic dimension and therefore inculcate certain values, or worldviews,

[2] Attributing institutional primacy to the market does *not* necessarily imply endorsing a minimalist view of the state; the question here is *not* where the "correct" boundary between the state and the market should lie. Many economists start their analyses (at least implicitly) from the market supremacy assumption but are keenly aware of the failings of the market and willingly endorse a relatively wide range of interventions, as well as other "institutional" solutions (e.g., Arrow, 1974; Schotter, 1985).

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

[4] Hodgson's essay in this volume denotes this as "reconstitutive downward causation."

into the people who live under them. In other words, as we continue to behave under a certain set of institutions, we begin to internalize the values embodied in those institutions, and as a result to change our selves.[5] This could not happen if human beings took a totally instrumental attitude towards institutions and rule-abiding; if they did, they would only keep the rules which are beneficial to themselves (after due calculation of calculating the changing opportunities for gain and loss as rules are maintained or discarded, etc.). In such a situation, "value-laden" statements and actions could only be regarded as cynical and manipulative "marketing ploys" advancing agents' own interests. And indeed this is what is often implicitly assumed in the mainstream economic literature on institutions, where institutions are seen as products of rational choice by selfish individuals interested only in material gains. However, if we follow this line of reasoning, we cannot really explain why institutions exist at all.

To begin with, if everyone is a selfish rational individual with an instrumental attitude towards rule-keeping, then there will be inordinate amount of cheating and shirking around. If this is the case, no institution will be sustainable, because then the cost of monitoring the possible deviations and punishing them will be truly prohibitive. Moreover, in this situation, it is questionable whether any monitoring and sanctioning mechanism against rule-breaking can exist at all. This is because the monitoring/sanctioning mechanism itself is a public good (in the sense that people who have not devoted their efforts in monitoring and sanctioning deviants can also benefit from the improved behavioural standards as a result of such activities), and therefore no selfish individual will find it "rational" to spend his/her time and resources in maintaining the monitoring and punishment mechanism.[6]

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

Needless to say, all the above should *not* be interpreted as meaning that people's motivations are more or less determined by the institutional structure. If we are not to lapse into an unwarranted structural determinism, we need to accept that individuals also influence the way institutions are formed and run, as it is typically done in the NIE models. However, our approach differs from that of the NIE in that it postulates a two-way causation between individual motivation and social institutions, rather than a one-way causation from individuals to institutions, although we believe that in the final analysis institutions as at least "temporally" prior to individuals (Hodgson, 2000).

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

Formation and Change of Institutions. Whether one sees institutions as constraining, enabling or constitutive, the question of how they change is crucial. The strong element of legacy, inertia, and path dependence in the determination of institutional forms must be acknowledged at the start. Even new institutions are built

[5] Of course, the "original" selves are themselves products of the existing institutional structure.

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

out of the raw material of existing institutions – the developmental state out of old bureaucratic traditions, the WTO out of GATT and so on. Formalistic models that don't take institutional inheritance seriously and fail to recognize that new institutions are likely to be first and foremost adaptations of prior institutions will miss the mark. Nonetheless, institutions do change and we need better theories of how and why they change. If we want to understand how and why particular institutions decay, or what conditions create opportunities for renovating or reinventing institutions, we must begin from a general perspective on how institutions are created and change.

We can broadly divide the different approaches to the origins of and changes in institutions into two groups, namely, the efficiency-driven approach and the interest-based approach, with sub-approaches in each group, each with very different theoretical and policy implications.

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

It is clear that in this simple form, the view is untenable for both theoretical and empirical reasons. Theoretically, when bounded rationality[7] is one of the important reasons that we have institutions, it stretches our credulity to argue that individuals who are not even capable of doing the standard optimization exercise involving only resource costs is capable of engaging in a "meta-optimization" exercise involving both resource costs and decision-making costs (or transaction costs). Empirically, we simply observe too many examples of inefficient institutions, whose persistence does not really serve anyone's interest.

As a result, some of those who hold this vision acknowledge that, at a given point of time, there may exist inefficient institutions, but they argue that these institutions will be "selected against" in an "evolutionary" process in the long run (Alchian, 1950, is the classic example).[8] However, even this more sophisticated evolutionary version has an obvious limit. The problem is that institutions are, by definition, not easily malleable (a perfectly malleable institution will be as good as no institution), and therefore that typically "the rate of change in the environment will exceed the rate of adjustment to it" (March & Olsen, 1989, p. 168). If this is the case, there cannot be any presumption that institutional evolution is moving in an optimal direction (see Chang, 1995, for further discussion).

In a more sophisticated version of the efficiency-driven approach to institutions, it is admitted that that not all institutional changes are of efficiency-enhancing kind and therefore that many of them will not be optimal even in the longer run (so, the

[7] The term is due to Herbert Simon. Simon (1983) is the best exposition of this view.

[8] For a comprehensive discussion of evolutionary approaches in economics, see Hodgson (1993).

simplistic “evolutionary” argument is rejected). The reason for this, according to those who take this approach (such as Brian Arthur, Paul David, and Joel Mokyr), is that the evolution of institutions involves path dependency.

In this view, certain institutions (say, technological regimes) may be chosen over others, not because of their inherent efficiency but because of certain irreversible “events” in history. The best example in this regard is probably that of “network externality”, which gives the first-movers a selection advantage through the frequency-dependent definition of “evolutionary fitness” (e.g., the competition between different computer operating systems). For another example, if certain irreversible investments have been made in certain physical, intellectual, and relational “specific assets” (the concept is due to Williamson, 1985) assuming the presence of particular institutions, the relative efficiency of the existing institutions vis-à-vis alternative institutions will have been enhanced, as the holders of these assets will have vested interests in preserving the existing institutions (see Chang & Rowthorn, 1995, for an elaboration of this point).

This perspective has allowed us to better understand the process of institutional changes. However, at least in its present form, it remains very “economistic” in that the process of institutional change is driven basically by technological factors, and in that individuals are seen as operating on the basis of purely “economic”, rational calculations (even though it is admitted that rational calculations by individuals do not necessarily amount to a socially optimal outcome). The essential problem with this approach is that there is no room for human agency in the sense that what people believe (instead of what they “should” believe, given the technological imperatives) does not make a difference to the process of institutional change. [9]

The most sophisticated version of efficiency-driven approach extends the argument to the “cultural” dimension in the sense that the worldviews possessed by human agents matter. The proponents of this view start from the assumption that human agents have bounded rationality (a concept to which Williamson and other more “purist” efficiency-driven theorists give lip service to but do not really adopt in practice) and argue that institutions make the complex world more intelligible to them by restricting their behavioural options and also by confining their scarce attention to a truncated set of possibilities.

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

Some of those who espouse the “culturalist” version of the efficiency-driven approach go one step further and argue that what worldview people hold is not independent of the institutions under which that they have been operating – or that there is “endogenous preference formation” (see for example, Hodgson, 1988, and

[9] Chang & Rowthorn (1995) attempt to combine this approach with what we call the “culture-based structured-interest approach”.

Bowles and Gintis, 2000). The argument is that institutions embody certain “moral values”, and by operating under certain institutions for a period of time, it is likely that people begin to internalize those values (this is what we called the “constitutive” role of institutions).

Note that even with these “subjective” elements (such as moral values and worldviews) thrown in, the approach is ultimately driven by efficiency – only that the definition of efficiency now takes on a subjective dimension. And in this sense, we can still call this a version of the efficiency-driven approach, however different it may appear from simpler versions of efficiency-driven institutionalist theory that we discussed earlier (see section 2.2.1.1).

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

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

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

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

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

In his famous discussion of the emergence of the capitalist factory system, “What Do Bosses Do?”, Stephen Marglin (1974) argued that existing (capitalist) property relations determined the way in which capitalist-style firm organization was chosen over worker-managed firms, when the latter did have efficiency advantages (but see Williamson, 1985, for a critique of this argument from an “efficiency” point of view). Robert Brenner, in his famous discussion on the revival of feudalism in Eastern

Europe, argued that the same exogenous shock of rising grain prices led to the demise of feudalism in Western Europe whereas it led to its strengthening in Eastern Europe because of the differences in their existing institutions (Brenner, 1976; see Aston & Philpin (eds.), 1985, for the subsequent debate). Sam Bowles and Herb Gintis, in a series of recent articles, have emphasized that the "contested" nature of exchange relationships in credit and labour markets make the market outcomes dependent on the existing power relationships (e.g., Bowles & Gintis, 1993, and 1996).

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

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

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

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

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

In this case, "context" is actually a complex nesting of contexts, especially in a globalized world. The worldviews of individual agents are nested composites of the immediate culture of communities and organizations, national ideologies and, as we will see in the discussion of the developmental state, an increasing pervasive global culture. Having admitted the cultural construction of interests, political economy should also have a theory of culture, which obviously is a tall order. Nonetheless, introducing even a primitive theoretical consideration of ideology and worldview into the discussion of institutional change allows for qualitative improvement over simple efficiency and interest-based theories.

The (Rise and) Decline of the Korean Developmental State

Introduction – Why the Developmental State? In the post World War II period, a small set of countries in East Asia stands almost alone in having significantly improved their position in the world hierarchy of nations. During the post-war period, per capita income growth rates in Japan, Korea, and Taiwan have been in the region of 5-6% per annum. By contrast, per capita income growth rate in the major now-advanced capitalist countries during the Industrial *Revolution* (1820-1870) was about 1% per annum.[10]

This unprecedented growth involved a fundamental transformation of East Asian economies from poor exporters of primary products to sophisticated producers of high value-added manufactured goods; even in Japan, silk and silk-related raw materials were the biggest export item until the 1950s. Flying in the face of western advice that they should stick with those products that reflected their "natural comparative advantage," these countries constructed new bases of comparative advantage. Starting from economic levels comparable to the more prosperous countries of Africa in the 1950's (even Japan's per capita income during the 1950s was lower than that of South Africa), they had moved to European income levels by the mid-nineties. Further, all this was accomplished in countries whose Confucian cultures had been derided in the West and whose elites had seemed hopelessly corrupt and ill-suited to anything beyond agrarian exploitation or tax-farming.

Conventional growth models that depend on individual entrepreneurs responding to market signals did not predict and could not explain the kind of transformation that occurred in East Asia. Only dramatic institutional innovation can explain it; and to the chagrin of neo-classical theories, there is a consensus that the state played a critical role in this unprecedented process of economic and social transformation. It is for this reason that these states were dubbed "developmental states."

Without recapitulating the voluminous writing on the developmental state,[11] it is

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[10] This figure is the arithmetic average of per capita output growth rate figures for the US, Canada, Japan, the UK, France, West Germany, and Italy. The same figure for the subsequent periods were 1.4% in 1870-1913 and 1.2% in 1913-1950. The figure was "only" 3.8% even during the "Golden Age of Capitalism" (roughly 1945-73). See table 8.1 (p. 117) in Armstrong et al. (1991). If sustained over time, small gaps in growth rates have huge consequences. if a country's per capita income is growing at 1% per annum (this is the case of Argentina during the postwar period), per capita income will double in 70 years – not the 12-15 years that it took Korea or Taiwan to do it. A country with per capita income growth of 0.3% per annum – the case of Bangladesh until the 1980s – would require 230 years to double its per capita income.

[11] The concept originated with Johnson's (1982) analysis of Japan in the 1950's and 1960's. See Amsden (1989), Wade (1990), Chang (1993), Evans (1995), Akyuz, (ed) (1999), and Woo-Cumings (ed.) (1999) for subsequent elaborations. World Bank (1993) and World Bank (1997) also grudgingly acknowledge the fundamental role of the state.

worth underlying some of this literature's basic postulates. At the root of these changes was a revitalization of centuries-old bureaucratic traditions and their redirection, for a variety of ideological and geo-political reasons, toward the accumulation of industrial capital. This permitted relationships with local private sector elites, combining support, protection, and discpline, that fostered these elites' willingness to invest in risky industrial ventures. The transformation of the state fostered a transformation of the capitalist class into a singularly effective variant of the classic industrial *bourgeoisie*.

All of this makes the subsequent decline of the developmental state a fascinating puzzle from the point of view of institutional analysis. With the recent economic crises in the region conventional theorists were quick to try to wipe out the troubling "developmental state anomaly" by claiming that the crisis demonstrated that the developmental state had been a charade all along. Unfortunately for their quest for parsimony, this interpretation does not stand up to even minimal scrutiny. First of all, whether or not the recent crisis is due to the "failure" of the developmental state, the economic and social progress achieved by the developmental states over the last half century or so in the region cannot be erased from history. Secondly, the recent crises in the region are the result of the decline, rather than the persistence, of developmental state (see below and also Wade, 1998, Singh, 1999, Chang, 2000c). Thirdly, the developmental state is a threatened institution not primarily because it was economically ineffectual, or even because its potential economic efficacy has been undercut by globalisation. The problems of the developmental state lie first of all in domestic politics and in the domestic political consequences of economic success.

While this analysis applies in varying degrees to the full range of East Asian developmental states, the Korean case stands out as the most interesting. When it was in its ascendancy, it was the most dramatic, if not necessarily most effective, specimen of this species; and its subsequent decline was the earliest and most comprehensive. The transformative projects envisaged and implemented by the developmental states of Japan and Taiwan during the postwar period were not as comprehensive and forceful as that of Korea. In the case of Japan, its longer history of industrialization not only required less state involvement in the transformative project, but also necessitated a more consensus-oriented approach in the state's dealing with the private sector. In the case of Taiwan, Kuomintang's position as an "occupation authority", as well its allegiance to the semi-socialist ideals of Sun Yat-sen's Three People's Principle, implied that the transformative project could not be as ambitious or as well-integrated with the activities of the private sector as that of Korea.

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

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

The Rise of the Korean Developmental State. The Korean developmental state emerged from a most unpromising environment. While the legacies of the proto-developmental state that existed under Japanese colonial rule were important (Kohli, 1994), the enormity of the destruction of the colonial institutional fabric after 1945 (the end of Japanese rule) cannot be underestimated. For one thing, the end of Japanese colonialism in 1945 unleashed political turmoil, which wreaked havoc on the institutional structure the Japanese left behind. The American occupation of what eventually became South Korea until 1948 increased the nation's institutional turmoil, as many American-style institutions were grafted onto this Japanese institutional structure. Needless to say, the Korean War (1950-53) exacerbated social and institutional dislocation even further.

The regime of Syng Mahn Rhee that ruled South Korea from its birth in 1948 until 1960 was fundamentally anti-developmentalist. Its only stab at developmentalism was the establishment of the Ministry of Reconstruction in 1955. This Ministry, however, acted primarily as a liaison with aid donors; it did not even formulate a development plan until 1959, and this plan was never implemented. The bureaucracy was nominally organized along meritocratic lines; but between 1949 and 1961, only 336 passed the High Civil Service Examination, far fewer than the 8,263 who got government jobs through "special appointments" (Cheng et al., 1998, p. 105). The quality of the bureaucracy was such that, until the late 1960s, Korean bureaucrats were being sent to Pakistan and the Philippines, among other places, for extra training.

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

What is often ignored is that these institutional changes also resulted in a critical "ideological" or "worldview" change. The institutional changes made by the Park regime in the early days embodied a nationalistic, pro-industry (vs. pro-finance), pro-producer (vs. pro-consumer) outlook, which emphasized capital accumulation, innovation, and structural transformation – namely the ideas associated with developmentalism. This outlook contrasts with Anglo-American market liberalism with its emphasis on consumer welfare, price competition, and allocative efficiency – all emulated, if poorly, by the Rhee regime.

These institutional changes formed the basis for a cascade of changes in the behavior of the private sector, which in turn produced an extra-ordinary transformation of the Korean economy. From a backward exporter of tungsten and ginseng, Korea became first an exporter of labor-intensive manufacturer goods (e.g., textiles, shoes, wigs) and then a world power in capital- and technology-intensive exports. In steel, an industry in which western advisors were uniformly convinced that it had no comparative advantage, it was able to make profits while selling at half the U.S. list price (Amsden, 1989, p. 317). In semi-conductors, an even more improbable area for investment, the Korean output surpassed that of the major industrial powers of Europe (Evans, 1995). All of this, of course, makes explaining the subsequent decline of the developmental state a particularly crucial task for any institutional theory of economic change.

The Decline of the Developmental State. In a sense, the Korean developmental state was challenged from the beginning – in the 1960s, by the conservative, pro-democratic alliance led by Yoon Bo Sun, and in the 1970s by the pro-democracy, center-left opposition forces led by Kim Dae Jung (president, 1998-2003) and (to a lesser extent) Kim Young Sam (president, 1993-8), since the 1970s. However, the fundamental challenge came from the Neo-liberal forces, which began to crystallize from the late 1970s onward in an alliance among the "liberal" faction of the bureaucracy, the majority of the intellectual community, and the increasingly powerful business conglomerates (the *chaebols*).

Neo-liberal forces made a critical breakthrough after the assassination of General Park in 1979 by his intelligence service chief. Initially, the political vacuum left by the death of Park seemed to open a space for the pro-democracy center-left forces led by the two Kims. However, these were soon crushed by the two-stage military coup (1979-80) staged by the "new military," led by General Chun Doo Hwan, and culminating in the Kwangju massacre (May 1980).

General Chun was by no means a Neo-liberal, but he allied himself with Neo-liberal bureaucrats and implemented a series of institutional changes signaling the start of a Neo-liberal offensive against the developmental state. He adopted the anti-inflationary rhetoric of Neo-liberalism in a bid to deal with the inflationary pressures created by the second oil shock and the subsequent world recession exacerbated by the monetarist macroeconomic policies of major industrialized countries. He privatized a number of banks and partially liberalized the financial market in 1983. He also introduced the 1986 Industrial Development Law (IDL), which shifted the country's industrial policy in a "functional" (as opposed to a "selective") direction.

By no means, however, did changes under Chun's rule make the subsequent demise of the developmental state inevitable. While its force was somewhat diminished, developmentalism still remained the overarching ideology of the regime, and proved formidably effective in certain areas, such as information technology industries (Evans, 1995). Many of the formal institutional changes in Neo-liberal direction made under Chun, such as financial liberalization (Amsden and Euh, 1990) and the IDL (Chang, 1993), were limited in scope Their effectiveness was curtailed in part by the inertia built into more-slowly-changing informal institutions such as bureaucratic convention and business practices.

Massive pro-democracy protests in the summer of 1987 triggered a more fundamental shift. Huge public actions protested Chun's attempt to use the rigged electoral college system to hand the presidency over to General Roh Tae Woo, his chosen successor and erstwhile collaborator. These protests succeeded in forcing the military to capitulate to public demands for a democratic presidential electoral system (Roh did manage to win the subsequent election held in late 1987).

The consequent political discrediting of the military rule led to a rapid weakening of the legitimacy of developmentalism, because it was seen (in our view mistakenly) as the former's Siamese twin. What was decisive in this process was the increasing conversion of the intellectual elite, especially the bureaucratic elite, to Neo-liberalism. An increasing number of elite bureaucrats and academics earned advanced degrees in the US at the height of its Neo-liberal revolution; the return of this cohort to Korea meant more and more people inside and outside the government who were convinced of the virtues of free market, and who regarded developmentalism as a "backward" and "mistaken" ideology.[12] In this ideological battle, the Neo-liberals were critically helped by the ideological dominance of Anglo-American academia and media at the world level. Neo-liberalism thus established itself as the dominant ideology among Korean elite circles, including the elite bureaucracy, in the late 1980s and early 1990s.

Many of the bureaucrats, however, still had instinctive attachment to developmentalism. This is readily seen in the intellectually-confused policy documents of the time, wherein Neo-liberal pronouncements on overall policy direction make an uneasy fit with developmentalist policies in particular areas. However, the conversion of many bureaucrats to Neo-liberalism was wholehearted and even dogmatic. For example, by the early 1990s, one frequently encountered bureaucrats from the Economic Planning Board, which somewhat paradoxically had become the home of Neo-liberalism in the Korean state at the time, calling for a radical retreat of the state and especially for the abolishment of their own ministry on the ground that planning, if it ever was desirable, was no longer feasible due to the increasing complexity of the economy**.**[13]

Moreover, since the late 1980s the *chaebols* increasingly viewed the Korean state as more of a liability than an asset in their competitive struggle in the world market. The many spectacular successes they had had in export markets, such as memory chips and automobiles, which were previously regarded as the exclusive domains of more advanced economies convinced them that they could now stand on their own. Their confidence was corroborated by the approval they started gaining in the

[12] Alice Amsden (1991) first highlighted the potential danger to the Korean economic model of the rapid increase in the numbers and intellectual ascendancy of what she calls the ATKEs (American-educated Korean economists). In the annual listing of economics Ph.D's published between 1987 and 1995 in the *Journal of Economic Literature*, Korean names constitute approximately 9.7% of all listed names (776 out of 8,040). This is an astonishing statistic, given that Korea accounts for about 0.75% of world's population (and that very few of these names represent Korean-Americans). An overwhelming proportion of these economists subsequently returned to Korea, steering university economics education increasingly in a Neo-liberal direction. In addition, many elite bureaucrats, increasingly educated along Neo-liberal lines in Korean universities, were sent to the US for advanced study; most eventually returned to their old jobs in the Korean government.

[13] It is interesting to speculate on why the "planning" ministry became the home of pro-market Neo-liberal thinking in the Korean bureaucracy. One possibility is that, not tied to particular "clients" as were other economic ministries, the EPB had traditionally behaved more "ideologically", whatever the ideology in favor. Another is that the EPB, as the top economic ministry, always recruited people with top scores in the economics section of the High Civil Service Examination; this meant that its bureaucrats were likely to do better in graduate studies in the US, and hence to earn more prestigious degrees.

international capital market. By the mid-1990s, the leading *chaebols* were considered creditworthy enough to float bonds in advanced-country capital markets. Their rapidly growing foreign ventures also started to weaken their identification with the nationalistic outlook of developmentalism.[14]

By the mid-1990s, the *chaebols* had become staggeringly aggressive in calling for the withdrawal of the state from economic management. "Owners" and the top managers of leading *chaebols* made public pronouncements against state intervention at every conceivable opportunity. The *chaebols* also set up a small but extremely well-funded research institute called Korea Centre for Free Enterprise, which churned out numerous documents with a Neo-liberal flavor, translated classical works in the Neo-liberal tradition (such as Hayek and Buchanan), and invited well-known American Neo-liberal thinkers to give high-profile talks in Korea.

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

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

A further push towards Neo-liberalism was provided from the late 1980s onward by insistence of the US and other advanced countries that what was now regarded as a developed country should abandon the "unfair" protections provided to their industrial and financial enterprises and thus give these nations' firms better access to an increasingly attractive market. When the Kim Young Sam government decided in 1993 to join the OECD, opening up markets became more imperative, as this was a conditions for membership.[15]

The resulting changes leading to the dismantling of the Korean developmental

[14] By the mid-1990s Korea was one of the largest foreign investors in a number of developing and transition economies, not just in Asia but also in Europe (e.g., Indonesia, Vietnam, Poland, Uzbekistan). It was also one of the largest investors in the UK electronics industry.

[15] Korea was accepted as a member of the OECD in 1996.

state and (in our view) subsequently to the current crisis, have been documented elsewhere (see Chang, 1998, Chang et al., 1998, and Chang & Yoo, 2000, for further details). The dismantling of industrial policy, the hallmark of the developmental state, had its tentative beginning in the late 1980s, and was completed by the mid-1990s. Financial liberalization, including capital account liberalization, gained momentum after 1991, but accelerated in 1993, when Korea signed a bilateral agreement with the US for financial market liberalization and opening. Most symbolically, the 5-year plan was terminated in 1993; and in that same year, the Economic Planning Board was abolished (as some of its own members had wished for some time) and merged with the Ministry of Finance to form the Ministry of Economy and Finance in 1994. Although certain residues of developmentalism could still be found in places (e.g., supports for R&D in certain high-technology industries), the dismantling of the developmental state was effectively finished by the middle of Kim Young Sam's presidency (say, 1995).

As is well known, the subsequent financial crisis contributed to a further decline of the developmental state. At the ideological level, the discrediting of the developmental state model has become even stronger. Neo-liberal forces inside and outside the country have managed to blame the current crisis on the developmental state, despite the fact that it was already effectively, if not completely, dismantled before the crisis – various models identifying industrial policy, cronyism, and the so-called "logic of too big to fail" as the main cause of the crisis are examples of such efforts (see Chang, 2000c, for some detailed criticisms).[16] And as a result, subsequently many additional institutional changes have been made by the current Kim Dae Jung government, sometimes willingly and sometimes under IMF pressure, that further destroyed the foundations of the developmental state.

The additional liberalizations of financial markets, of international trade, and of foreign direct investments that were implemented in the early days of the current crisis under IMF pressure are well known by now. Less well-known is the rewriting of the central bank constitution to give it both independence and a single-mindedly focus on inflation control, both features that are contrary to the pro-industry (and anti-finance) outlook of developmentalism (for further details, see Chang & Yoo, 2000). Even less known, however, are the changes in the organization of the government.

After the crisis, the head of the Ministry of Economy and Finance (MOFE) was demoted from the position of a deputy prime minister to a simple minister. Control over the government budget, which had given the MOFE such clout in earlier days, was transferred in May 1999 to a new small ministry, the Ministry for Planning and Budgeting; this new ministry was also given the (perhaps largely symbolic) oversight of "government reform". The Ministry of International Trade, Industry, and Energy (MOTIE) saw its crucial trade-related functions transferred to the Foreign Ministry and as a result becoming the much weaker and demoralized Ministry of Commerce, Industry, and Energy (MOCIE).

[16] Of course, this is not to say that the Korean developmental model was without flaws. There were some obvious weaknesses, such as the excessive concentration of even high-tech export industries in commodity-type products (specialisation in DRAM rather than custom chips), which made the country vulnerable to international demand cycles. However, it is not entirely clear how much of this was due to the Korean developmental state per se. The lopsided character of Korean industrialization, and the emphasis on scale economies (DRAM chips) over niche markets (custom chips), for example, are responses to the technological and organizational obstacles associated with breaking into the more sophisticated segments of export markets. In any event, the lopsided specialization of Korean industries only intensified with the state's abandonment of investment coordination across sectors and firms (see Chang et al., 1998).

These changes in government organization symbolize a fundamental shift in the role of the state in the economy. The reassignment of the EPB's former functions between the MOFE and the MPB, along with the demotion of the MOFE minister, implies that whatever remains of the government's planning function no longer requires concerted efforts and serious inter-ministerial coordination. The new central bank constitution eliminates the pro-industry bias in macroeconomic management. The transfer of trade functions to the Foreign Ministry means that trade policy is now seen as a part of diplomacy and not an integral part of industrial policy.

Another important post-crisis development is the weakening of the elite bureaucracy itself.[17] As many people attributed the recent crisis to the *dirigiste* model of development, the elite bureaucracy as its protagonist naturally came under severe criticism. The criticism did not simply involve criticisms of particular policies. Now the very legitimacy of the institution of bureaucracy itself was, with the help of the Neo-liberal "government failure" rhetoric, being undermined. At the same time, the Kim Dae Jung government has been keen to weaken the elite bureaucracy, which it sees as representing the corrupt and inefficient *ancien regime*, and imbue more "entrepreneurial" and "service-oriented" ethos into the bureaucracy by vastly expanding, and indeed setting up a quota for, mid-career "special appointments" through a competitive recruitment process open to those who are not career bureaucrats – in other words, it has started the process of destroying the Weberian bureaucracy that was so critical in its development and moving to a more "American" model of bureaucracy.

All these have led to an unprecedented demoralization in the elite bureaucracy; when combined with aggressive head-hunting by the private sector, this has led to an unprecedented hemorrhaging of personnel from the elite bureaucracy. For example, since the crisis, dozens of high-flying young bureaucrats between their mid-30s and mid-40s in the elite ministries, especially the Ministry of Finance and Economy, have moved to *chaebol* firms – something such people would have never have done before the crisis.[18]

Despite these "*gestalt* shifts" and formal institutional changes that followed the recent crisis, the imperatives of crisis management have paradoxically re-activated some of the developmentalist policy devices that were laid to rest during the mid-1990s. For example, the Kim Dae Jung government implemented various programmes of state-mediated industrial and corporate restructuring, a staple of the Korean developmental state – such as the so-called "Big Deal" programme of "voluntary" business swaps and mergers among the leading *chaebols*, on the one hand, and the state-led restructuring of Daewoo and other bankrupt *chaebols*, on the other hand. For another example, the MOCIE in late 1999 introduced a programme of promoting "star firms" in parts and materials industries and stepped up export promotion measures. Further, in autumn 2000, the Kim Dae Jung government restored the post of the Minister of Finance and Economy to its former status at the Deputy Prime Ministrial level. Without how long-lasting or effective these "revivals" of

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

[18] Prior to the crisis, elite bureaucrats would have moved to the private sector only later in their careers, after exhausting their career possibilities within the government, via a process known in Japan as *amakudari*.

developmentalist policies will be, these trends show how some patterns can recur even in times of a most radical institutional overhaul.[19]

Theoretical Implications. This analysis of the rise and decline of the Korean developmental state supplies us with some interesting insights into the process of institutional change. It shows that institutional change is a highly complex process, involving multi-directional and often subtle interactions between "objective" economic forces, ideas, interests, and existing institutions themselves, unlikely to be captured by simple application of efficiency or interest-based models.

Simple efficiency-driven explanations of institutional change (as per section 2 above) perform poorly when applied to this case. For example, many people argue that the demise of Korean developmental state was inevitable, because, with economic development, the economy has become too complex to centrally coordinate. Even if we accept the argument that economic development necessarily makes centralized coordination more difficult by making the task of coordination more complex, which in itself is a highly contentious proposition[20], the argument still does not explain why such demise happened in Korea at the time when it happened. If it is the stage of development at which a particular country is that determines the functionality of a given state form (e.g., developmental state), why did the Korean developmental state go into a decline when the country was at the stage of development similar to where Japan was in the 1960s or the 1970s, when the latter's developmental state was in its prime?

If we are to understand the exact timing and the manner of the demise of the Korean developmental state (and more generally the timing and the exact form of any institutional change), we also need to look at the ideological battles and the changes in interest group politics (and their interaction with each other) that surrounded the process. For example, the fact that many government bureaucrats in Korea turned against state interventionism – so much so that by the early 1990s some EPB bureaucrats were calling for the abolition of their own ministry – flies directly in the face of what we call the "simple interest-centred view of institutional change", such as the one found in Neoclassical Political Economy, which, a la Niskanen, predicts that bureaucrats have interests in expanding their bureaux. Unless we understand the influences of Neo-liberal ideologies, which denies the legitimacy of state intervention in general and particularly of planning, on these bureaucrats, we will never be able to understand why they campaigned for the reduction of their own power and influence.

Having emphasized the importance of ideas in the process of institutional change, we do not wish to give the impression that ideas should be treated as a uniquely independent force that things like interests and institutions are not. While ideas are not simply "marketing ploys" of interest groups, it is difficult for an idea to be sustained in the long run without some appeal to important interest groups. The offensive by the *chaebols* and the "revolt" by the upper-middle classes, both of whom had been great beneficiaries of the success of the developmental state, against

[19] Support for developmentalism may remain at the grassroots level as well. While many Koreans regard Park's developmentalism as the root cause of the current crisis, 20 years after his death Park consistently ranks in the top 10 in various opinion poll rankings of individuals who are most influential in running today's Korea.

[20] Economic development may increase the complexity of the task of coordination, but it also develops the society's administrative and coordination capabilities both within and outside the government. Therefore, it may, on the whole, make such exercise easier, rather than more difficult (for a more detailed discussion on this issue, see Chang, 1999).

Korean developmentalism in the 1990s that we discussed above are very good cases which illustrate this point.

For another example, while our discussion shows how powerfully ideas can shape the course of institutional change, it is wrong to envisage a one-way relationship between the two. As we argued above, institutions affect the ways in which people who operate under them perceive the world (the "constitutive" role of institutions). And therefore it is not possible to see them as objects of manipulation by agents with exogenously-formed "preferences", because the way in which such "preferences" are formed is itself affected by the nature of existing institutions. To take an example from the Korean case, we may say that the historical association between the developmental state and military dictatorship made many people who may not have been otherwise inclined to do so object to developmentalism.

Another point that emerges from our discussion is the need to think more seriously about the importance of human choices in determining institutional changes – not the empty Neoclassical choices, which are more or less pre-determined by "objective" conditions and fixed preferences, but hard-to-predict choices involving a complex process of balancing ideology and interests. For example, some people who put emphasis on path dependency in institutional changes (or follow the "sophisticated version of efficiency-driven explanation of institutional change") argue that Park's choice for a Japanese-style developmentalism was an "obvious" one, given the institutional legacies of Japanese colonialism (see, e.g., Kohli, 1994). However, when Park came to power, the American model would have been the *more* obvious choice. At the time, many formal institutions of Korea had been already put in their place by the American Occupation Authority, and the tendency towards the American model was further strengthened by what the Rhee regime did (e.g., establishment of a quasi-independent central bank, privatization of banks, American-style spoils system in the bureaucracy). Also, given the country's near-total economic and political dependence on the US at the time, a Korean leader would have benefited the most by emulating the American model (regardless of the possibility of "success" of this approach, given local conditions). Given all these, it required certain amount of initiative on the part of Park and his key aides to move away from this "easy" choice of embracing the American model.

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

Finally, the rise and especially the decline of the Korean developmental state demonstrate the way in which the "nesting" of worldviews shapes processes of institutional change. Kim Dae Jung government's identification of both *chaebol* and the state bureaucracy with anti-democratic militarism represents an ideological view generated by Korean experience and political debates. The convictions of American trained economists that the developmental state could not possibly work, on the other hand, represent the impact of global worldview on Korean institutional change. The increasing importance of global institutions and worldviews in shaping the evolution of national institutions like the developmental state is one of the reasons that it makes sense at this point to turn our attention to institutional change at the global level.

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

Having been the central public actors in the definition of economic policy for hundreds of years, states' powers are now challenged by the construction of global institutions. While modern states have always had to share power with private transnational actors, during the past 50 years a set of public organizations have been established that can be considered the embryonic embodiment of global governance institutions. It is not completely fanciful to suggest that they might eventually come to play a role at the global level analogous the role that states have played within their national territories over the last 400 years.

This contemporary period of intensive institution building is then particularly intriguing from the viewpoint of an institutional approach to economic change. For despite the extensive literature on international organizations, we know surprisingly little about how key contemporary global governance institutions function as organizations, how their own structuring facilitates or impedes the possibility of realizing different visions of the global economy, or how modifying their structures might affect the future evolution of the global system. Looking at the formation of these new institutions thus provides an opportunity to develop and test theoretical ideas concerning how institution-building works.

Global institution-building also has implications for institutions at other levels, including the developmental state. Global institutions both embody and re-shape global norms and worldviews, which in turn are incorporated into the worldviews of actors at the national level. Global institutions are also a constraining and enabling context for institutions at the national level, making it harder to maintain some institutions and easier for others to emerge. At the same time, the relationship between global institutions and nation states is anything but one-way [was: zero-sum]. Global governance institutions depend fundamentally on the capacities of nation states to execute their goals, even while they may enhance the capacities of nation states in certain areas by providing political clouts and technical assistance. Looking at global institutions is a powerful reminder that institutional change is a multi-level process.

In this section, we will focus on one global governance institution, the newest addition to the Bretton Woods family – the World Trade Organization (WTO). While the WTO is a unique institution, it illustrates some archetypical features of global governance institutions. Examining the WTO will permit us to underline the point that institutional questions are not superseded by the shift toward a political economy organized on a global instead of a national level, and to the contrary gain a new salience as economic actors attempt to "re-scale" the organization of production and exchange.

The WTO (like other global governance institutions) exists because the more sophisticated, internationalist currents in the corporate and political leadership of the U.S. and other developed countries realized that a global market requires a complex set of institutional underpinnings. As the "realist" theory of international relations (cf. Waltz, 1979) correctly underlined, an international system of independent sovereign states (commonly referred to as a "Westphalian" system) has strong elements of anarchy at the global level. Anarchy does not lend itself to stable market relationships, to say nothing of long-term investments. Reducing the level of anarchy to get the stability and predictability necessary for a global economy to operate is the whole point of global governance institutions.

Institutionalization involves a trade-off wherein the strong accept certain constraints to get more reliable consent from weaker players (and each other), enabling them to do more (see section 2.1). It is by no means an uncontested trade-off. Opting for the benefits of institutionalization instead flies in the face of a worldview, constructed over the course of hundreds of years, in which sovereignty is politically sacred. Even developing countries – India for example – are fiercely defensive when they see international norms infringing on their sovereignty. The point is that, as Steven Weber (1999) has pointed out, global governance institutions, as organizations, attract little political loyalty. The supposedly anachronistic institution of the nation state looks charismatic when compared to these institutions.

Within the U.S. political class, the "bilateral *real politik*" version of global governance, in which economic and political threats against less powerful nations replace invocations of international norms, is a very attractive alternative to the compromises involved in trying to institutionalize governance norms at the international level. In short, while prerogatives of sovereignty have unquestionably been eroded, political worldviews built on the foundation of sovereignty continue to be very powerful and to make the construction of global governance institutions into a very uncertain task.

Support for global governance institutions requires a sophisticated sense of the long-term dangers of normlessness and a corresponding appreciation of the returns to institution-building. Sophisticated internationalists like George Soros and Robert Rubin have at least implicitly realized that the current global economy is haunted anew by the "Polanyi problem." Looking at the rise of national markets, Polanyi (1957[1944]) argued that the socially unsustainable character of "self-regulating" markets generated a natural "protective" reaction on the part of a variety of social groups, including a portion of the elite. Unfortunately, in Polanyi's analysis this protective reaction was overwhelmed by the inability of the same protective reaction to prevail at the international level. International markets, particularly financial and currency markets, could not be successfully regulated. First the collapses of the gold standard and then degeneration into the barbarism of Fascism were the result.

In the post-World War II period, the Polanyi problem of reconciling free markets with stable social and political life was taken up again through the construction of a set of international norms and institutions, including the "Bretton Woods" institutions at the global level, complemented by an understanding of the importance of continued regulation (especially of capital flows) at the national level (Hveem, 1999). This made possible what John Ruggie (1982) called "embedded liberalism" –

international openness combined with social protection and regulated through an interconnected set of powerful nation states. Embedded liberalism helped produce the generation of prosperity in the core industrial countries that is sometimes called the "Golden Age" of capitalism (on the rise and the fall of the Golden Age, see the essays in Marglin & Schor (eds.), 1990).

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

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

There are, of course, different ways of transcending the Polanyi problem. The goal of the U.S. Treasury and the international financial community is to provide an institutional foundation for the universalistic enforcement of narrowly defined market norms. The political base for this form of transcendence is very powerful but equally narrow. Embedded liberalism went well beyond this conception and it is not at all clear that the narrower view is politically viable.

Another quite different view of building global governance institutions is the vision that was adumbrated in the formation of the United Nations, and is epitomized in efforts to enforce universal norms around issues like human rights and environmental sustainability (cf. Keck and Sikkink, 1998; Evans, 2000). This vision of globalization aims at the universalistic enforcement, not of a narrow set of market norms, but of a broad set of democratically formulated socio-political norms. For holders of this view, global institutions that only enforce narrow market norms, even if they do so universally, may easily be judged worse than no global institutions at all. This was probably the position of the majority of the protestors in Seattle in December 1999. An alliance between supporters of this view and nationalist adherents to the bilateral real politik view could be politically potent.

Such an alliance would also draw the support of a fourth group – believers in a romantic version of a decentralized political economy, organized not around sovereign states but at the local level. John Zerzan, intellectual leader of the "black block" anarchist faction that drew major headlines in Chicago represents this view[21], but its adherents are spread widely across the left-right spectrum. Any kind of global governance is an anathema to this group. For them, the Polanyian collapse is part of

[21] For an interesting discussion of Zerzan's "anarcho-primitivist" ideology, see *The Wall Street Journal*, Dec. 6, 1999, A17.

the solution.

All of this is to say that building global governance institutions is a delicate business. Interests remain important, but worldviews are even more so. Definitions of what is “efficient” for whom are slippery. Individuals whose apparent interests would seem to be identical may have diametrically opposed positions and alliances among people who define their interests in completely different ways are equally likely. All of this can be illustrated by looking at the brief and tumultuous life of the WTO.

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

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

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

Despite the dominance of the informal rules in practice, the formal rules still provide a basis for political threat. The United States and the advanced industrial countries will be in a difficult political position if a large block of developing countries were to say, “It is not possible to achieve consensus. Therefore, this issue must be taken to a vote.” However, recent experience -- in particular the recent struggle over delecting a WTO Director General and the collapse of the Seattle “Millennium Round” – demonstrate that, on the one hand, it will not be easy for the US and the EU to simply ignore developing countries when they decide collectively to fight for something, but on the other the impact of such political threats on outcomes is not clear.

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

In formal terms, the WTO does not appear to be a very powerful organization.[22] But the WTO is seen as powerful because it is viewed as embodying the interests of the world’s major economic powers. The WTO exists because powerful national players wanted to focus the politics of international trade disputes on an international organization whose decisions are likely to be considered legitimate, precisely because it is formally democratic and because those who make individual decisions are bureaucrats not beholden to any particular country. The WTO’s informal power then lies in the fact that it is the concrete representation of the informal consensus and solidarity that makes the international trading system work.

Yet at the same time, the formal aspects of the WTO regime remain a potentially important source of support from smaller countries looking for relief from the world of bilateral real politik, in which they are relentless bullied by the “great powers” (most obviously the United States). The “dispute settlement mechanism,” which interprets rather than formulates policies, is more formal and transparent. While informal oligarchy is still not irrelevant, Costa Rica may occasionally prevail in a case against the U.S., which is not likely to happen in a world of bilateral real politik. The dispute settlement mechanism is, in fact, a good example of how universalistically enforced norms help bring weaker parties on board, even if they have little effective say in the formulation of the rules themselves, and even if the general content of the rules does not reflect their interests. Apparently transparent and objective governance features, like the dispute settlement mechanism, are fundamental to the ability of organizations like the WTO to claim international legitimacy, but they are obviously no help *vis a vis* U.S. politicians interested in avoiding any limitations on the hegemon’s sovereignty.

Curiously, organizations like the WTO may be more vulnerable to attack from the hegemon that pushed for their creation than from the poor nations that are excluded from the informal oligarchy that shapes their policy. The unusual ideological character of the United States makes it peculiarly unsuited to play the institution-building role that one might expect the global hegemon to play (cf. Evans, 1997). There is a powerful current of elite ideology within the United States that is both profoundly distrustful of any kind of public governance institutions and deeply apprehensive of anything that might reduce the absolute sovereignty of the United States itself. This segment of the conservative political elite is completely supportive of free markets but has little appreciation of the institutional infrastructure necessary to make such markets work, particularly at the global level. Distrust of government in any form combined with deep-seated xenophobia turns any institution of global governance into the enemy. Hostility from traditional conservatives (principally in the United States) who will be hypersensitive to any WTO actions considered to infringe on U.S. sovereignty is almost inevitable.

At the same time, an increasingly active civil society has begun to take a serious and vociferous interest in the politics of globalization. These groups are either interested in governance in the sense of universalistic enforcement of a broad set of

[22] Its only formal power is to legitimate countries’ right to engage in bilateral trade sanctions when their interests have been damaged by trade restrictions that violate WTO agreements.

democratically formulated socio-political norms that would reconstruct the market rather than simply expand it, or they are hoping to re-establish some political and economy autonomy at the local level. The success of global governance in the Soros/Rubin sense of universalistic enforcement of narrow market norms would be a defeat for both groups. Unless organizations like the WTO can convince the first group that it can somehow serve as an instrument in promoting the broader set of socio-political norms, something at least along the lines of embedded liberalism, frustrated civic groups have every reason to try to get their national governments to withdraw support from the organization. A progressive-conservative alliance of political groups whose only point of agreement is that the WTO should be dismantled is far from fanciful, especially in the United States.

The political vulnerability of the WTO is compounded by the lurking power of the global democratic majority, which is to say the developing countries. In the Uruguay Round, the developing countries were willing to accept promises in return for their concessions on issues like TRIPS, finances, and services. In Seattle, perhaps emboldened by the willingness of the demonstrators outside the meetings to challenge the status quo, they drew the line.

For developing countries, universal enforcement of narrow market norms (as in the case of the dispute settlement mechanism) may represent a marginal improvement over the bilateral bullying of a real politik world, but as long as the mandate is narrowly defined and the content of these narrow rules is determined by an oligarchy of rich countries with advice from private firms, global governance is only a marginal improvement over Westphalian anarchy for them.

Developing countries want, and need, a set of rules that not only resuscitates the social protections of embedded liberalism, but expands embedded liberalism beyond the OECD countries. They also need rules that don't simply reinforce the privileges of the firms and countries that currently control global markets, but provide some support for efforts to "catch-up." If global governance is to gain their reliable political support, it must go beyond narrow market norms. Are the sophisticated internationalists who have the most to gain from a stable institutionalized global system willing to use the WTO and other similar institutions to reconstruct global markets in a way that responds to such demands? Or, will they risk their efforts at global institution-building (and in the longer run increase the possibility of Polanyian collapse) to preserve the current definition of the legitimate global market?

If institution building were simply a question of efficiency and interests, the outlook would seem hopeful. Transnational capitalist elites are much better off if global governance organizations enforce some broader norms while providing stability and predictability, than they are if global governance founders for lack of political allies. Even in the short run, having to abandon an organization like the WTO would be a major shock to investor confidence in the predictability of global political economy, something that sophisticated internationalists must avoid at all costs. The bargain is not all that dissimilar from the one that produced the welfare state and embedded liberalism, except that it must be constructed at the global level.

Unfortunately, the process of institution building is more complicated and less predictable. If we could count on global elites making rational choices, the world would be a more pleasant place than it is. If experience is any guide, elites are unlikely to accept "rational" compromises unless they are under political pressure sufficiently intense to jar them out of business as usual. Opportunities for more progressive trajectories of institution building at the global level depend not just on the responsiveness of elites but on the formation of complex alliances among groups with disparate interests as well as common ones.

The complexities of building such alliances are well illustrated by the "core labour standards" issue. "Core labour standards" (CLS) at their most basic are epitomized by the recent ILO version, which the U.S. finally agreed to sign up to, is a good example of a minimalist version, but everyone recognizes (some with hope, some with fear) that this is the thin end of a wedge and that ultimately CLS could come to mean things like protecting the right to organize, which is why the concept is politically interesting.

The argument for inclusion of CLS in the WTO's mandate is simple and logical. The absence of CLS in a particular country can be considered a trade-related basis for unfair competition just as the absence of intellectual property rights is considered a basis of unfair competition. Like the privilege of not having to pay royalties to Bill Gates, not having to pay the wages that labour could demand if it were free to exercise its collective rights constitutes a subsidy to local producers.

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

First there is always the sovereignty issue. Third World leaders see CLS as giving the WTO one more excuse to intrude on their internal affairs. Second, they see limitations on local firms' ability to exploit labour as threatening their comparative advantage. Desperate to increase their exports to developed country markets, Third World governments are terrified that the labour standards issue might be used against their exporters. And, of course, many developing country leaders may see normative changes at the global level that might increase the bargaining power of local labour as a bad thing for their local business allies.

U.S. labour movement, which is a central political constituency from the point of view of the current U.S. administration, sees institutionalizing global labor standards comparable to those that operate in the U.S., especially in the more economically competitive regions of the Third World, is a bedrock issue (See Palley, Drake and Lee, 1999).[23] For the administration's corporate constituency, on the other hand, the issue is less salient. While they are beneficiaries of the absence of labour standards in developing countries, major U.S. transnationals are also aware that the diffusion of CLS would be at most a minor detriment to their global profit rates. For U.S. labour, then trying to get a US administration to support core labor standards beyond its boundaries certainly has more prospect of being a winner than trying to prevent capital from investing abroad or trying to impose general restrictions on the entry of foreign consumer goods into the US.

To make progress on this issue, however, international allies are essential. U.S. labour must have significant allies within at least the most important developing countries. Again, logically it would make sense for Third World labor to support CLS,

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[23] In principle a similar logic applies to European trade unions, but for these unions the question of labor standards within the EU takes political precedence, leaving U.S. labor unions as more salient actors on the issue.

even if national political leaders did not. Being able to threaten both employers and national politicians with international sanctions if local labor rights were not respected could be a powerful new bargaining tool. Yet, so far there are no visible examples of public political support for trade-enforceable international labour standards by major Third World trade union movements.[24]

The reasons for the lukewarm response of Third World trade union movements are not hard to understand. For decades the international position of U.S. labor has combined opposition to the most militant Third World labor movements on grounds that they might be Communists with unabashed protectionism. Not surprisingly then, Third World labor sees the support of U.S. trade unionists for CLS as motivated less by international labor solidarity than by the desire of privileged Northern workers to deny Southern producers access to Northern markets and thereby avoid sharing the returns from global productivity increases with their brothers and sisters in the South – in short protectionism (c.f. Amsden, 2000, p. 14).

For U.S. labor then, trying to use the WTO to improve global enforcement of labor rights means completely renovating its relationships with Third World labor movements, building concrete ties and demonstrating solidarity. Old attitude in which Third World workers are dangerous because they are "willing to work for too little" have to be replaced by a new vision in which Third World labor is a key political ally that must be supported.

In short, the core labor standards case provides a very nice illustration of how institution-building efforts can play a constitutive role, pushing groups to redefine their interests in interesting and unexpected ways. The argument can be recapitulated briefly as follows:

1. An international organization is created by governments acting as agents of the more sophisticated elements of transnational capital, to provide a more politically efficient and effective institutional means of allowing a more stable, less costly expansion of international openness and increasing the transparency and predictability (and consequently reduce the volatility) of the global economy, thereby reducing the threat of the "Polanyi problem."

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

[24] In some cases (e.g. the Indian National Trade Union Congress), the response has been consistently and strongly negative (Haworth and Hughes, 1997). In other cases (e.g. CUT in Brazil, COSATU in South Africa), the response has been ambivalent at best.

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

4. The one-nation/one-vote definition of democracy that was (naturally and indeed almost inevitably) incorporated into the internal governance of the WTO forces any group that wants to try imposing a different set of global norms to find allies within a range of developing countries and do whatever is possible to strengthen the local political position of these allies. Thus, one of the unintended consequences of the creation of the WTO was to create an additional incentives for the U.S. labour movement to redefine its interests in a more internationalist direction and to engage in concrete efforts to strengthen both its ties to Third World labor movements and the local political clout of these movements. The important role of labor in the demonstrations in Seattle (largely ignored by the media) underlies the WTO's role in helping to shift labor's attention from domestic to global politics.

Regardless of how the core labor standards issue ends up playing out, the case of the WTO serves to illustrate the necessity of taking an institutional perspective to understand economic change at the global level. It reinforces our initial argument that institutional change cannot be explained by functional/efficiency or instrumental/interest logics but must also take into account the independent impact of worldviews and ideologies. Likewise, it validates our contention that institutions must be seen as constitutive of the worldviews as well as being shaped by them.

Conclusion: Towards an Institutionalist Approach to Economic Change

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

At the same time, exploration of these cases has proved fruitful in terms of refining and reconstructing the conceptual sketch of institutional dynamics with which we started. Both cases illustrated our basic premise that an adequate theorization must see institutions as both *constructed* (or reconstructed) in response to changes in interests and ideology (or worldview), on the one hand, and *constitutive* of interests and ideology, on the other hand. But, they did more than this. While the cases were not chosen to illustrate the variant ways in which ideas, interests and institutions might interact, they ended up serving this function.

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

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

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

In sum, the developmental state's loss of political support best fits a model in which changing worldviews, more specifically the adoption of the globally dominant worldview on the part of local elite, was more important than shifts in their "objective" economic interests in generating institutional change which had negative consequences for economic performance (i.e., contributing to the creation of the Asian crisis) and, therefore, negative consequences for the "objective interests" of the key actors who formulated and implemented the decline of the developmental state.

The WTO case is not inconsistent with the developmental state case but it emphasizes a different sequence. Again, worldview plays a dominant role in generating institutional change (in this case, the sophisticated internationalist Soros/Rubin worldview that recognizes the necessity of creating institutions to govern global markets). Likewise, in the event that the current project of global institution-building collapses, conservative ideologies which exalt the privileges of sovereignty and the short-term advantages of bilateral bullying are likely to play a major role.

The main part of the story, however, leads from the creation of an institutional context to the subsequent redefinition of interests and worldview, with the added twist that the institutional effects are fully decoupled from the intentions of the institution's creators. Concretely, the creation of the WTO provides a stimulus for the redefinition of labour's interests and worldview in an internationalist direction. This change in worldview and interest definition on the part of a significant set of social actors is, in turn, projected to shift the way that the WTO functions as an institution in the future, and thereby the way in which legitimate global markets are defined.

Our analysis also strongly reinforces Block's (1999) admonition that it is a grave mistake to think of the global political economy as a "natural" system in which each element is logically and "organically" connected to the others so that tinkering with any part of it will disrupt the functioning of the whole. We have tried, as Block (1999, p. 10) suggests, to "reconceptualize international capitalism as a constructed system." We have shown how the rise and demise of the developmental state reflected a complex process of individual agency, changing worldviews and shifting political alliances, not some "inexorable economic logic" of the global system as a whole. The WTO demonstrates even more clearly the extent to which the global political economy is a system under construction with the economic logic of the resulting system dependent on the outcome of the process of institution building.

The juxtaposition of the two cases also illustrates the benefits of thicker institutional analysis. Obviously, the emergence of the WTO and the decline of the developmental state take place in the same global arena. Thin institutional analysis often sees their interrelation is simple "zero-sum" terms – as a competition over a fixed amount of total sovereignty in which increasing global governance is locked in struggle with the national economic strategies of Third World governments. Our analysis suggests a very different picture. The complicated political dynamics of the decline of the developmental state had little to do with governments being forced by the WTO or other global governance organizations to give up nationalist political strategies. Conversely, among the myriad threats to the institutionalization of the WTO, the nationalist economic policies of Third World governments hardly feature. The implications of our analysis for the inter-relation of the two cases reinforce the basic point: thin institutional approaches lead to misleading conclusions regarding institutional dynamics.

The overall point is clear. Our analysis illustrates the reasons for our discontent with the dominant canon. The false parsimony of its non-institutional view offers little or no analytical leverage on the dynamics of either case. Its basic assumptions prevent it from doing so. "Preferences" (both in the sense of interests and worldviews) must remain exogenous and unchanging. A story in which interests and worldviews are variables shaped by institutional context but also playing a role in causing institutional change is impossible. False parsimony has robbed the canon of its ability to deal with these key cases.

Unfortunately, when it comes to explaining economic change, it will take more than an intellectually plausible overall framework combined with superior ability to explain particular cases, even very important cases, to displace the institutionally anaemic, dominant approach.

In addition to the "QWERTY" sort of "path dependency" advantages that the dominant canon has, simply on the basis of longevity and "network effects," the nature of the coupling between theory and practice gives the particular kind of false parsimony that the dominant canon has developed a tremendous advantages. Powerful social actors care much too intensely about getting clear answers delivered with full conviction to tolerate the kind of complexity that an adequate institutional explanation involves. Theories must generate simple rules that enable decision-makers to take prompt action. They must also generate confidence among the decision-makers and ideological hegemony vis-à-vis the rest of society.

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

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

The contemporary economic canon enjoys all the necessary conditions for sustaining false parsimony and under current conditions it is unlikely to be unseated by a complex and "mushy" institutionalist alternative. Even if an institutionalist alternative could unequivocally demonstrate its scientific superiority, the practical and ideological costs of changing decision-rules would militate against jettisoning the established canon. And, an institutional alternative is still a long way from such unequivocal demonstrations.

To improve its chances, a more institutionally-oriented alternative canon must do two things. First, it must continue to demonstrate that events that are anomalous for the existing canon become comprehensible and predictable once a more institutionalist view is applied. Given the ambiguities inherent in most social and political outcomes, this is not an easy task, but it is still essential. Second, while eschewing false parsimony, an institutionalist approach must still work in the direction of showing that its explanations are not simply *ad hoc* stories concocted after the fact but are consistent with each other and with some body of general propositions. This is even harder.

Despite the difficulties involved, the prospects for the rise of an alternative, institutionalist view are not as bleak as this discussion makes them appear. First, conquest is not the only form of success. Just as religious dogmas transform themselves by assimilating oppositional positions without admitting that the previous orthodoxy was ever in error, intellectual canons can be substantially transformed without ever appearing to capitulate. Positions that might have seemed blasphemous thirty years ago – e.g. the important role of increasing returns – are already accepted by the more innovative practitioners of the conventional canon. Such changes create useful building blocks for the construction of an alternative canon.

At the same time, the aim is certainly not to "reinvent the wheel." Manufacturers trying to calculate the costs of making widgets in a given organizational and institutional need the kinds of tools that standard microeconomics has developed. We also need to take advantage of the immense amount of work that has been put into techniques of calculating national incomes, estimating changes in the money supply etc.. It would be foolish not to take advantage of all the work that has been done on these issues under the aegis of the conventional paradigm. Such tools become misleading because they are used without the acknowledgement of their institutional assumptions. The problem with conventional economics is that it would prefer to ignore the fact that changes in the institutional context are both possible and can dramatically change the implications of the numbers they interpret.

As North and others have pointed out, it is precisely the "taken for granted" character of institutions that makes them invaluable to individuals and societies that don't have the time or ability to optimize. It would be foolish to suggest that consideration of the full range of institutional alternatives should be a part of all day-to-day decision-making. Nonetheless, ongoing preoccupation with the question "How might existing institutions be organized differently and what would happen if they were?" is not just healthy but essential. The current hegemony of the dominant canon cuts off that question and that is what makes it dangerous.

Both an accurate assessment of the possibility that an institutional perspective might gain more sway and a strategy for achieving such an end must obviously depend on political as well as intellectual factors. The ascendance of an alternative canon is unlikely to happen in isolation from the mobilization of social actors that see their interests harmed by the policies generated by the dominant canon. Thus, anyone interested in the intellectual project of developing an alternate canon must be equally interested in the political project of empowering those most prejudiced by the logic of the existing canon.

There is, of course, an uglier scenario for the creation of a political base for new ideas – a traumatic economic crisis. A sufficiently profound practical crisis would rob the existing canon of its ideological charisma, but it would wreak havoc in the lives of everyone (not just the privileged). Those who would like to unseat the existing canon should hope that this kind of occasion for their success never arrives, which is not to say that aversion to a traumatic crisis should diminish enthusiasm for working toward the construction of an alternative canon. First of all, infusing existing policy debates with some alternative perspectives is probably the best way to diminish the possibility of such a crisis. Second, if a crisis cannot be avoided, the worst of all possible worlds would be to have the existing canon stumble and fall into crisis with no better alternative waiting in the wings to replace it. Anyone who really believes that the false parsimony of the existing canon has crippled its ability to understand and predict economic change had better be working furiously to construct an alternative view, not because they wish for crisis but because they are terrified of what crisis would mean in the absence of a sound intellectual basis for formulating alternative strategies.

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