

Dissertation

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Quo vadis, developmental state?
A comparative analysis: Japan and Croatia

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To my mother and my very best friend, who made me believe that “there’s no such
place as far away”

Preface and acknowledgements

Although I am a graduate in economics, I have always been interested in political science and international affairs. After having graduated in June 2007, I was admitted to Diplomatic Academy of Vienna. Moreover, during summer 2007, I first considered enrolling into a doctoral programme in political science in order to broaden my knowledge in international politics and international relations. Still, I have never wanted to write exclusively about a subject in the field of political science, but rather, my wish was to link the dissertation subject to the knowledge of economics I had already acquired.

Actually, political economy caught my interest during my undergraduate studies. I heard about the notion of developmental state for the first time while studying for a *Magister* in economics, during a class on international economics and development. I knew immediately that I wanted to know more about it. At the same time, I started learning Japanese in 2006 and was absolutely fascinated by the language, and, generally, by Japan's politics, economics and culture. Hence, for my dissertation topic I decided to merge all subjects I am passionate about in a unique study: political science, economics, Japan, and finally, my own home country, Croatia.

Therefore my expression of thanks goes firstly to Professor Ulrich Brand, who did not hesitate to accept the supervision of my doctoral thesis, although I was new at the Institute of Political Sciences. Professor Brand's valuable advice, helpful assistance and very detailed comments were of great help for me. Moreover, I want to thank Professor Minoru Sawai from the Department of Economics, Osaka University, who was at my disposition for all information I needed during my doctoral research in Osaka in summer 2008. Of course, I must not forget the Japan Foundation in Kansai that selected and fully sponsored me during a two-month programme for young researchers in summer 2008. Both the Japanese language course and the assistance for the doctoral research offered by the Japan Foundation were unmatched and superb. Additionally, I want to mention the Paris Dauphine University, where I spent an exchange semester in 2008/09, and where I was gratefully given permission to use a library designed for the Dauphine master and doctoral students only.

Finally, if it had not been for the constant moral and financial support of my mother, I would have never learned what I know today, I certainly would not have seen as much of the world as I did, and, consequently, I would have never written this doctoral thesis.

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INTRODUCTION

“Just as the state has no money of its own, so it has no power of its own. All the power it has is what society gives it, plus what it confiscates from time to time on one pretext or another; there is no other source from which state power can be drawn. Therefore every assumption of state power, whether by gift or seizure, leaves society with much less power. There is never, nor can be, any strengthening of state power without a corresponding and roughly equivalent depletion of freedom.”

Albert Jay Nock

“The modern state, no matter what its form, is essentially a capitalist machine, the state of the capitalists, the ideal personification of the total national capital.”

Friedrich Engels

“A binary opposition is a pair of opposites, thought by the structuralists to powerfully form and organize human thought and culture. Some are commonsense, such as raw vs. cooked; however, many such oppositions imply or are used in such a way that privileges one of the terms of the opposition, creating a hierarchy.”

Claude Lévi-Strauss

It must not have been Albert Jay Nock, an American libertarian¹, or Friedrich Engels, a German Marxist, whose statements were available for the opening of this thesis. I might have equally taken dozens of similar affirmations of politicians, lawyers, economists and business people, writers, journalists, actors

¹ Libertarianism is a concept used in the political philosophy, defined by the Stanford Encyclopedia of Philosophy as a philosophical movement whose authors hold “that agents initially fully own themselves and have moral powers to acquire property rights in external things under certain conditions”. Although it is sometimes, mostly by political scientists, thought as a completely anarchistic, left-wing movement, or oppositely, by others, mostly economic scholars, as a right-wing, pro-capitalist school, Stanford Encyclopedia of Philosophy available online distinguishes between the left-wing and the right-wing libertarianism. I will employ the word by implicitly understanding the latter economic concept, thus libertarianism allowing the unlimited use or appropriation by individuals (radical right-wing libertarianism) or, in its slightly milder but abstracter version, the one arguing that no individual be made worse off by the use or appropriation of a resource compared with non-use or non-appropriation (Nozickian right-wing libertarianism, named by the philosopher Robert Nozick).

and scientists. Although the argumentation may be absolutely opposite (such as in the libertarian and Marxist case), the *leitmotiv* is always the same: the state is a predatory instrument of the elites who merely seek their self-interests. Consequently, these elites will ruin the rest of society, the non-elites. A few decades ago, we were powerlessly exposed to the state, a monster; we used to be bound to it economically, politically and ideologically.

Today, however, all those who were so eager to see the end of the state, claim to be living their five minutes of fame. The name of their weapon is globalization, which is seen by them as a saviour of liberties and thus as a destroyer of the useless state. The only missing link in the concept is: what is to be done once the state is really abolished, if this time has come? Are we going to become “free at last” – free of economic burdens of taxes and contributions, free of nationalism, free of borders?

The attack on the nation-state, or at least the frustration with and the fear of it is, contrary to many wide-spread beliefs, not any spectacular news. Karagiannis and Madjd-Sadjadi (2007: 99) remind us that the nation-state has been under attack for more than 400 years: first it had to survive the era of colonialism (1500-1775), than imperialism, and finally it has found itself in the period of multinationalism, internationalism and globalization.

However, the financial crisis which started in 2007 and culminated with the global economic crisis of 2008, having proportions last time seen in 1929 during the Great Depression, overshadowed the concept of self-regulation, and returned some credibility to the state. But, in principle, the debate is a classic. The state-passionate argue: “Do not panic, the good old state is here to solve all your problems, just give it its old role back.” Others, who count in George W. Bush himself, warn rather: “Just do not over-regulate again.”

The first are completely wrongly and mistakenly declared Marxists, since, as we can read out from the above Engels quotation and as we will see in the further course of this thesis, associating the concept of the strong state with Marx is the example of contradiction *par excellence*. The second group, not accidentally related to George W. Bush, has lost its credibility due to their

questionable economic, social and foreign policies. Now whom should average citizens, every day bombarded with the information on the unprecedented proportion of the crisis, finally trust?

This thesis aims to serve as a defence of the state, but in a manner slightly different than many propositions offered today. As the third quote for the opening, I chose the one by a French anthropologist Claude Lévy-Strauss, who argues that the human mind obviously very easily falls into the trap of making binary oppositions. For many, it is either black or white, religious fundamentalism or atheism, love or hate, communism or liberalism, globalization or North Korea, Chavez or Bush, a total state or no state. Is this not absolutely devastating? Precisely, the basis for any extremism lies in such binary oppositions, and we all claim to be afraid of extremism.

In this line, this thesis wants to argue why the state is required today, as an answer to all those who argue, like libertarians or Marxists, that the state should be rendered powerless. If it gains any power, they say, it will always and unexceptionally abuse it, either against our general liberties (libertarianism), or against our pocket (monetarism), or against the poorest among us (Marxism).

Part I of this thesis is therefore dedicated to reviewing the present scholarship on economic role of the state. These theories will be reviewed in chapter 1. As an answer to their criticism, one can point to the concept of developmental state, a very successful state model, in particular of the 1950s and 1960s, which was launched in Japan and recognized as exceptional by Chalmers Johnson in 1982. Johnson's work, which has meanwhile become a must for any student of international political economy, irrelevant of their political orientation, triggered off a number of publications and authors concerned with the concept of developmental state. This concept and its partisans insist on the power, or capacities, of the state, and argue that the state, if certain conditions are fulfilled, does not have to act as a *persona non grata* in present debates. Such modern approaches will be elaborated in the second part of chapter 1 of this thesis.

Differently from classic statism, though, the thesis will also insist on the relation of the state with other social groups, associations and agents. It will argue, in a rather neo-pluralist tradition, that the state is not monolithic, but rather fragmented. Moreover, it will attempt to show that, although the state is indispensable, it cannot function properly without the input of all other social agents, such as the private sector, labour unions, non-governmental organizations, and so on.

Therefore, in chapter 2, after investigating the traditional role of developmental state, as perceived by the aforementioned literature, this thesis will try to make a brief '*pro-con* list', thus it will name the most important arguments in favour and against the concept of developmental state. In so doing, it will also briefly review the case of Argentina, which clearly is a case for a developmental state. On the other hand, the modern times we live in, marked by the increasing democratization and participation of different groups in all kinds of social activities, urge for a rethinking of the traditional concept of developmental state. This thesis will also review this argument.

Furthermore, it will attempt to step further and to dismiss the scheme in which the state and the market are the only actors to observe. As we shall see, bureaucracy and politics are significant, and the interest groups from the business sector are doubtless very important, but both of these "blocks" (the state and the business) can function only partially without the non-governmental organizations, the media, and minorities – briefly, without society in general.

Therefore, as I will argue, the state needs society, and society is also in an urgent need for the state. A proverb from the Democratic Republic of Congo has it: "*mukalenga wa bantu, bantu wa mukalenga*" which can be translated as: a power without the people to impose it on, is no power; however, the people upon whom no power is exercised, are no people, and there is no society, but a chaos.

Part II, a case-study part of the thesis, will depart with the case of Japan, a pioneer of developmentalism. Although an enormous number of writers have

worked on its economic model, this thesis aims to synthesize the most important findings so far, in order to be able to use them for further discussion. Therefore, Japan will not serve as an axis of the thesis, but rather as a good example. Since I do not believe that economics or political science are ahistoric sciences, in chapter 3 I will therefore first sum up the course of the Japanese economic history. Its developmental state model will then be looked at in the second part of chapter 3, all the way with criticisms from different kinds of schools of thought (in order to prevent the thesis from binary thinking).

However, in my view the biggest novelty of the thesis is the fact I want to use the Japanese model to rethink the economic development of a post-socialist, transition country, Croatia, in chapter 4. In my knowledge no publications, except a short contribution by a Croatian economist Vojmir Franičević², have been written on this subject so far. Normally, the developmental state model has been applied in the case of Latin America, rare are those in Eastern Europe, but none to Croatia. As many other ex-socialist countries, Croatia faces a dilemma of either fully embracing capitalism or hating it and wishing for socialism to be back.

It is often forgotten how citizens of former socialist states are affected by capitalism, in particular by its crises such as the one of 2008 and afterwards. The dilemma of these countries is, in a way, similar to a small child brought into a theatre to see a show with its parents. The child, similarly to most of its peers, hates theatres, mostly because it has to sit quietly for two hours without understanding a word of what is going on. If well raised, the child will obey and sit quietly hoping for an end. However, if it is spoiled, an *enfant-roi*, it will mess around, make noise, and finally force the parents to bring it home.

In either case, however, there is a positive scenario: the child will eventually be able to go into its room, it will be free to play, to speak loudly, to do whatever it wishes, of course under the supervision of its parents. And then,

² See Franičević, V. (2003): Between Market and State: Developmental States in South East Europe?, in: Globalization, Democratization and Development. European and Japanese Views of Change in South East Europe. Ed. by Vojmir Franičević and Hiroshi Kimura, in association with the wiiw. Zagreb, Massmedia 2003.

suddenly, there comes the bad part: the child has to go to sleep. It had spent two hours of sitting in the theatre, it had dreamt of its room full of toys, and now it finally has it all – but, after another two hours in the room, it has to go to sleep, and it cannot object, because the parents have the final say.

Of course this is an oversimplification. Transitions from socialism to capitalism and from the one-party system to democracy are a way more complicated, painful and destructive process than a mere tell-off of a child. Moreover, the newly introduced capitalist system in former socialist states provokes, besides its unquestionable positive consequences, also some effects fairly outreaching just simple going to sleep: indeed, there is inequality, foreign pressures and influences, consumerism and pauperisation, and intellectual backwardness. For, being given more choice does not necessarily imply a happier person.

Suddenly however, there emerges a crisis such as the one of 2008, and the average citizen of a post-socialist country asks a crucial question in a simple vocabulary: “Should we have maintained socialism?” All of a sudden, the perpetual debate is revived: *Then*, everyone was more or less equal, and *now*, everyone can find himself or herself without a job and on the street in the blink of an eye... Paradoxically, many citizens of ex-socialist and communist states find that their state has become even more repressive in times of capitalism, than it had been during socialism.

This thesis will argue that, in dilemmas such as these, the state is too easily misconceived. Underlining the negative connotations of state power and phantomizing its authority often leads to exaggerated and false conclusions. Part III will, in this sense, offer a revised theory of the developmental state. In chapter 5, I will attempt to directly confront Japan and Croatia of *today*, and, bearing in mind their complex histories and societies, I will try to summarize what Croatia could learn from Japan, not only as a role-model, but also from Japan’s mistakes after the Second World War.

Finally, the revised concept of the developmental state, to be elaborated in chapter 6, will refer primarily to developing and transition states. It will

introduce a state that cooperates with the private sector and in the same time attributes a very important role to its civil society. By departing from certain theories dealing with social relations within the state, it will be argued that, given the political and civic will, there can exist the state that does not forget its industries but also not its poor, simply because it will not act alone.

It will certainly not be omnipotent, and I am not pretending to find and offer a Holy Grail. However, this theory will provide some material to reflect upon. The basis is to think in terms of different groups, which justify the point that states are neither altruistic nor predatory. Rather, if one takes into account more than just an economic analysis (by “more” I understand the history and the complex social structures), something overlooked by most classic state theories, the state will hopefully be seen in a much clearer way.

Finally, before embarking upon my analysis, I have to emphasize once again that I do not prefer any specific school of thought. Many of them change completely when applied in the real world. For instance, Marxism is in transition countries seen, quite understandably and due to their historic experience, with a mixture of disregard and fear. Socialism is in most minds related to a hideous totalitarianism, a single party one had to worship and a single dictator who was always right. A single way of thinking was allowed and every divergence was considered dangerous. Of course, this is fatal to development and, from today’s perspective, it is clear that such an approach is rather short-lasting. Still, I cannot help but remark how, on the other side of the coin, some neoliberal theorists can also be unbelievably arrogant with their binary oppositions. Sometimes, if they are not able to explain things by themselves, they simply blame Marxists, such as in this view of the Japanese developmentalism:

Japanese story is not a story about interventionist policy at all. (...) [Rather,] Marxists ran the Japanese social science departments. Predictably, they told tales that suited their doctrinal requirements: markets fail, planning works. (Miwa and Ramseyer 2006: 146)

The good news for all the citizens of post-socialist countries is however: there can be a way to escape extremist neo-liberalism without going back to totalitarian socialism. In fact, there could be no ideology at all.

PART I: SUMMARIZING THEORIES OF THE STATE

CHAPTER 1

DEMYSTIFYING THE STATE

1.1 THE MAIN CLASSIC THEORIES OF THE STATE

There are so many interpretations of the purpose, causes and consequences of the state intervention in the economy, that it would certainly not be possible to squeeze them in a single chapter. Nevertheless, the aim of this thesis is not to search for the ‘right’ theory, nor does it pretend to do so. Rather, in this chapter I want to briefly review the role of the state discussed by several most important (and controversial) theories of the state.

To start with, let us choose a rather philosophical definition: Steinberger (2004: 146) sees the state as “omnicompetent in scope, absolute in authority, and organic in function.” Omnicompetent in scope means simply that its purview is unlimited. Absoluteness in authority implies that there is no external source of appeal: civil disobedience to the state does not endanger, but on the contrary, underline the presence of the state. Bartelson’s (2001: 186) argument goes into the same direction: “The truth of the state is a truth whose validity resides in being taken as a lie; it is only as long as the state is seen as a “deception” that it can continue to exercise any authority”.

In other words, as long as there is an implicit understanding, or conscience, of state authority, as long as it is discussed, questioned or disputed – it will exist. One never disobeys the state, but rather what may be thought of as an invalid or faulty attempt to express the state’s demands, i.e. one disobeys the government rather than the state (Steinberger 2004: 186). Finally, by “organic in function” Steinberger understands the idea that the state is and must remain an organism (“an organism in which whole and part are deeply bound together in a relationship of utter mutual dependence”, (322)). Thus, the state is more than simply a government: it is a structure of interdependent und mutually

coherent propositions about how things in the world really are (ibid). And here lies the apple of discord: is the state an instrument of someone or something? Is it autonomous? Is it a beast, or a rather benign creation?

In this chapter I will briefly review the most frequent contemporary theories of the state. Sections 1.1.1-1.1.4 will offer short overviews of the perspectives of the new right, elite theory, Marxism /neo-Marxism and pluralism/neo-pluralism. Then, in sections 1.2.1 and 1.2.2, I will follow the argumentation of theorists of developmental state, notably Linda Weiss, in order to get into the notion of state capacity and of diverse recent approaches to the functioning of the state. Finally, section 1.3 will be concluded by combining the classic theories of the state with the work of the developmental state theorists, such as Peter Evans, Linda Weiss and Robert Wade, to name only a few. I will then suggest the link for which the evidence will be sought in chapters on Japan and Croatia, and in the final chapter of the thesis.

What makes the state so special? Dunleavy and O'Leary (1997:2) embark upon their elaboration of state activities by enumerating the principal five characteristics, which, put altogether, give a first impression of the role of the state. First, the state is a separate institution of set of institutions, different from the rest of its society because it is able to create public and private spheres. Secondly, the state is sovereign, the supreme power and the ultimate authority within its territory. Thirdly, the state extends to all the individuals within a given territory and applies equally to all. Fourthly, the modern state's personnel are mostly recruited and trained in a bureaucratic manner. Fifthly and lastly, the state has the capacity to extract monetary revenues (taxation) to finance its activities. However plausible or even banal these criteria might seem, they are surprisingly often overlooked. Without that negligence, many works on the subject, including this thesis, would not have needed to be written.

Hay and Lister (2006) claim that the origins of the state lie in Mesopotamia, and that in these initial stages, the state was largely despotic and coercive in the manner in which it exercised power over a population. They trace the origins of the modern state to Western Europe. In this area, it started

with an absolutist state (Bourbon France, Habsburg Spain and Tudor England), thus the state which had a centralized bureaucracy and tax-raising capacity, a standing army, a system of diplomatic relations with other states and, had clearly delineated and commonly accepted territorial borders. It is however also to Western Europe that the rise of a different state concept, the welfare state, can be traced.

The first step towards the genealogy of the concept of the state was taken by Machiavelli and his *Il Principe*, where the state became synonymous not only with the prince himself, but also with the character of the political regime, the geographical area over which sovereign authority was claimed and maintained, and the institutions of government entitled to preserve that authority (Hay and Lister 2006). The Weberian definition of the state is valid as long as “its administrative staff successfully upholds the claim to the monopoly of the legitimate use of physical force in the enforcement of its order” (Weber 19...54).

Hay and Lister (2006) see the state both as institutional contextualization and as historical contextualization. The first implies that the state provides, both functionally and organizationally, a context within which political actors are seen to be embedded and with respect to which they must be situated analytically. In Bob Jessop’s words: “The bias inscribed on the terrain of the state as a site of strategic action can only be understood as a bias relative to specific strategies pursued by specific forces to advance specific interests over a given time horizon in terms of a specific set of other forces each advancing their own interests through specific strategies. Particular forms of state privilege some strategies over others, privilege the access of some forces over others, some interests over others, some time horizons over others, some coalition possibilities over others” (1990: 10).

The second concept, the one of the state as a historical contextualization, implies that to understand the capacity for governmental autonomy means to assess the extent of the institutional, structural and strategic legacy inherited from the past, thus to understand the dynamics between state and governmental power over time (Hay and Lister 2006: 12). As a logical pursuit of

this argument, we might ask ourselves what kinds of roles the state may exercise. Dunleavy and O'Leary (1997) define three models, depending on how the strength of the state and the analogical strength of its environment are seen in a liberal democratic state.

Cipher models stress that the state is above all a passive mechanism controlled from outside the formal political sphere, and that ultimate power lies with groups in civil society, business sector or dominant elites. State institutions require an exogenous leadership input to operate effectively; otherwise they are powerless, uncoordinated and useless. This stems from the fact that the state as such is weak, its environment being very powerful instead (Dunleavy and O'Leary 1997:327ff).

The *guardian image* (ibid: 329) of the state sees it as an autonomous institutional force capable of rebalancing the social pressures acting upon it. The scope here is either to make the state's environment fit in with the state personnel's view of the social interest, or to achieve the public policy configuration which is appropriate for long-run overall societal development. In this model, the state is strong, and its environment is either weak, balanced or segmented, depending on the theory.

The *partisan image* (ibid: 331) sees the liberal democratic state as equal to any other social actor, advancing the institutional interests or personal welfare of the organisations and individuals that compose it. However, the state is constrained since its environment is equally strong. Hence, the state has to bargain with other social forces to achieve favourable outcomes for public agencies or officials. The state acts on its own behalf, rather than striving for public interest outcomes or operating in line with a functional logic of the guardian model.

For the purpose of this introduction, I am going to try to see the economic role of this abstract unity called the state, by means of four different pairs of glasses: the new right (1.1.1), elite theory (1.1.2), Marxism and neo-Marxism (1.1.3) and pluralist and neo-pluralist theories (1.1.4). Afterwards I will make the

point on why I believe all these approaches are oversimplified and sometimes even superficial.

1.1.1 THE NEW RIGHT

Generally, the new right is said to favour little economic and high judicial intervention. Whereas the old right (conservatives) was principally against the state (preferring a medieval feudalism), the new right today gathers a wide range of thinkers, from libertarians to reactionaries (Dunleavy and O'Leary 1987: 72 ff). I am going to mention briefly only some of them.

Let us start with a rather brutal question: should the state exist? Monetarist Milton Friedman (1991: 25) is clear in this context: "However attractive anarchy may be as a philosophy, it is not feasible in a world of imperfect man." As tempted as one might be after reading this statement to conclude that Milton Friedman's real position has been misinterpreted, this would be a great mistake. In fact, having summarized several state intervention types in the United States that are in no case approved if seen from the liberal perspective, (such as agricultural subsidies, tariffs, control of output, rent control, minimum wage rates, regulation of industries, social security programs, public housing etc.), Friedman (ibid: 35 ff) concludes: "The list is far from comprehensive." The monetary system should also be "free from irresponsible governmental tinkering" (ibid: 51).

Even if Thatcher and Reagan's legendary policies were a great inspiration that eventually evolved into orthodoxy, the new right thinkers are not united in their considerations of the role of the state. By seeing state as gradually fainting from neutral until practically non-existing, the liberal school essentially acknowledges three different approaches towards the state (Dunleavy and O'Leary 1987:126), quoted as follows.

According to scholars such as Brennan and Buchanan, the state is a Leviathan. It will always try to exploit its citizens, but there are however some mechanisms available for limiting the government revenues. State should intervene only in the regulation of public goods. Citizens can also control the

government by adopting constitutional rules that limit the government taxation base.

In a second new right theory, rational or public choice, a starting point is a rational egoistic individual. Public choice authors like Buchanan and Tullock go on to argue that before a constitution is drawn, people will be completely uncertain as far as their future is concerned (which corresponds roughly to the famous Rawls' veil of uncertainty). Therefore, all the individuals will choose a democratic social order within the constitution. The latter will then grant them individual liberties and secure their private capital ownership.

Moreover, as we shall see later in chapter 2, this school developed theories of bureaucracy and politics that actively use the economic framework to interpret the behaviour of the electorate. In the opinion of Hindmoor (2006), this theory is crucial because it changed dramatically, and not only interpreted the world. It equipped the new right politicians, such as Ronald Reagan and Margaret Thatcher, with a convenient language to dismiss the state and to propose alternative policy recommendations.

Finally, radical libertarians like Robert Nozick combine the findings of the Austrian school (mostly, the market liberalism) and the public choice theory (uncertainty and maximization of the overall social welfare). Libertarians champion for the minimal state with its only function being to protect the natural rights. The minimal state is established by rational individuals and under uncertainty. This school has never been taken really seriously due to the predominance of the public choice theory. Moreover, as Barry (2004: 18) notes, there is an important point which distinguishes the minimal statist's view of liberty in relation to classical liberals. These latter believe in the symmetry of claims to liberty so that all aspects of freedom are equally important. Thus, economic liberty is on a par with familiar civil liberties. Minimal statist, on the contrary, claim that these liberties should be separated and that there is a connection between liberty and private property.

Why does the new right dislike the state so much? There are numerous reasons, only some of which will be stated here. Anyone who has read Friedrich

Hayek, is aware that he as a representative of the Austrian school, distinguishes between a legal framework provided by the state on the one hand, and the central authority with a principal role of planning on the other (1949:135). Although Hayek's work on *Individualism and Economic Order* is mainly a discussion about socialism and central planning, we can read out from it his general attitude towards state intervention. He sums up his colleague's Ludwig von Mises and his own argument: "In our opinion well-accepted analysis shows that it [state intervention] does not provide an alternative which can be rationally chosen or which can be expected to provide a stable or satisfactory solution of any of the problems to which it is applied" (ibid: 134).

As it is well known, the new right regards individual property with a combination of admiration and reverence. Concerning income distribution by the state, Milton Friedman emphasizes above all the inviolability of private rights of individuals and therefore affirms: "The unwillingness of the rich Robinson Crusoe or the lucky finder of the \$20 bill to share his wealth *does not justify the use of coercion by the others*" (1991: 165, emphasis added). In chapters on poverty alleviation and social welfare, Friedman's standpoint is once again clearly stated: a liberal distinguishes between equality of right or equality of opportunities on the one side, and the material equality or equality of outcome on the other side (ibid: 195). This is why the (welfare) state is seen as unnecessary.

Returning to Dunleavy and O'Leary, (1997: 108 – 123), I will quickly note their three models of the new right, which are interesting because they view the state as a purely responsive machine. The first one is the cipher model, here called the *demand-side model*. Here, significant obstacles to citizens' abilities to direct state policy-making are introduced. They are a result of imperfections of the political system, such as bidding up voters' expectations, manipulating the political-business cycle, or log-rolling.

The new-right variant of the guardian state is an abstract *welfare-maximizing model*, rather a theoretical than an empirical possibility. It is important to contend that welfare maximization need not entail social and

economic redistribution. Why is this? Interventions are perceived as merely lowering aggregate social welfare because they stifle incentives to work hard, to invest and innovate. Consequently, the state intervention only takes place to correct distortions in the individual exercise of rights.

Finally, the new-right's *supply-side model* offers a simpler version of the partisan state, centring on budget maximization by government agencies. The partisan state overrides citizen preferences because self-seeking bureaucrats manipulate information and resources. The usual results are over-regulation of private sector operations, the over-supply of public services, increased deficit financing and growing public debt.

Most new right theories are mathematically precise, as they believe that human behaviour is rational and can be therefore reduced to mathematical formulas. Obviously, these theories do not account for diversity of humans, or diversity of states for that matter, since their methodological individualism does not allow for it. Clearly, this is a gross methodological mistake.

1.1.2 ELITE THEORY

According to elitism, our reality is as simple as it can only be: there are the ruling and the ruled. Anyone struck by the similarity to Marxism should however know that every resemblance ends right here. Classical elitists (notably Vilfredo Pareto and Gaetano Mosca) claim that Marxism has limited power in explaining domination. Additionally, they do not believe in a classless society that Marxism promises (Dunleavy and O'Leary 1987: 138 ff.).

Mark Evans (2006) reminds that there are two groups of elite theorists: classical elitists (such as the above mentioned Mosca and Pareto, or Robert Michels) and modern elitists (C. Wright Mills, Jeremy Burnham, and later Michael Mann and Theda Skocpol, only to name some). According to the traditional elitism, the rulers of society constitute a socially cohesive group, which is territorially based within a nation state. Moreover, the ruling elite is

'closed-off' from the ruled, and its members are selected by virtue of their economic political or ideological resources.

Dunleavy and O'Leary (1987: 143) note that elites consist of excellent, trained, chosen individuals. They are able and authorised to lead, to regulate and to govern. It is not only a positive statement, but also a normative one. Democracy stands not for liberty, equality or participation, nor for social welfare. Rather, it filters the elites and creates elite pluralism. Elite theory therefore took over some basic arguments of Weber's bureaucracy theory.

Very interested in the role of political leadership, elite theorists attempt to explain the phenomenon of bureaucracy. For instance, democratic elitists adopt Weber's notion of hierarchy, impersonality and recruitment of officials on the basis of merit, and they also acknowledge the notion of rational policy-making. In this sense, the elitist position completely differs from the new right, but also from the Marxist perspective of bureaucracy.

Power is seen as a universal feature of human existence. Elite theorists therefore argue that the crucial characteristic of most social relations is the exercise of power, because elites always try to rationalize their rule, both to themselves and to maintain the masses in a quiescent condition. Authority is in fact the mask of power. However, the dominated are not given the voice to express their position, and so it can be easily overlooked and such power relationship therefore might never be observed (ibid :49ff). This resembles the views of some Marxist authors, notably Gramsci.

More recent elitist approaches offer a slightly different picture (Evans 2006: 39ff): the rulers of society are engaged in an ongoing process of competitive elitism. While this group remains territorially based within a national state, due to global imperatives it will have linkages and/or membership of global elite networks in order to maintain its power base in society; the ruling elite remains 'closed-off' from the ruled, and, finally, the power bases of its members are selected by virtue of a broader range of resources-economic, political, ideological or technical.

Modern elitists are concerned with management, notably C.Wright Mills (1956), who had the most impact on the modern elite theory, in *The Power Elite*, and James Burnham, in *The Managerial Revolution* (1943). Theda Skocpol explicitly treats the state as autonomous and thus implies that state and civil society co-exist as two separate entities, which is highly questionable. On the other hand, Michael Mann's principal methodological task lies in investigating the interest of state elite. He distinguishes between two types of state power. As Evans (2006: 48) notes, the first, despotic power, relates to the range of actions which the elite is empowered to take without traditional negotiation with civil society and the second, infrastructural power, refers to the capacity of the state to actually penetrate civil society and to implement political decisions.

With the impact of globalization, the elite theory has also expanded to new areas (Evans 2006: 50ff), of which four categories are worth noting. At *the international level*, elite governance manifests itself in the epistemic community approach. I will come back to the governance theory in chapter 6. At this point, it should be mentioned that epistemic communities (policy-making elites which are comprised of natural, social scientists or individuals from any discipline or profession with authoritative claims to policy relevant knowledge), play a key role in processing policy ideas to member states.

As noted by Adler and Hass (1992) these communities have a limited number of participants, common interests, and engage into an ongoing process of bargaining. Their membership and values persist over time and all participants share a consensual knowledge base. Moreover, all members have knowledge resources in an exchange relationship and are all highly dependent on the intelligence-gathering skills. Finally, the view of policy makers ultimately determines the influence of an epistemic community and its status of acceptance.

As for elite governance *at the macro level*, the statecraft approach prevails. The group of political party leaders and civil servants has its own interests, which are distinct from the rest of society. This theory then claims that such a group can often successfully pursue these interests. At the *subsectoral*

level, on the contrary, other groups are more potent. Some elite theorists emphasize the importance of policy networks. General policy-making is seen as the outcome of the interaction between policy networks, hierarchies and markets. These policy communities are the most common form of networks.

Modern elitists claim that policy communities constitute an elite system of governance, notably within the EU today, to which I will revert in chapter 6. Finally, several elitists use the case of urban regimes in order to explain elite governance at the city level. Decisions are taken by business in which government plays no role, and this is what obviously links this theory with Marxism, but also with the theory of Charles Lindblom, who was himself a neo-pluralist.

The elite theory in general recognizes five aspects of state organization (Dunleavy and O'Leary 1987: 164). It stresses the role of political leaderships in liberal democracies. Moreover, it emphasizes, as already mentioned, the predominance of bureaucracies in shaping policy-making. Elite theory also tries to identify reasons for fragmentation (or centralization) of governmental tiers and sectors. Additionally, elitists analyze the role of law as related to power and authority. Besides that, they are eager to find out the nature of strong policy connections between government activities and major economic interests.

Again, elitist models can be divided into three categories, depending on what role for the state they foresee (Dunleavy and O'Leary 1987:185 – 197). The state is seen as a cipher in the *external control model*. This model implies external control of the state by socially or economically dominant elites. Elite theorists see only a one-way flow of influence in market societies, with a few economically powerful, high status groups differentially organized and resourceful in manipulating the liberal democratic process. Not only business elites, but also the whole managerial strata of modern advanced industrial society belong to elites, according to different social closure models.

The elite theory image of the *guardian state* is the liberal corporatist view, which argues that a closed process of accommodation between government, business and other institutional elites directs strategic policy in line with a

shared conception of this order to create the conception of national interest. Liberal corporatism, as elite theory sees it, produces a coherent ideology, stressing national economic success against foreign competition and a restrictive conception of social order, which major interest blocks help the government to enforce.

The elite theory's *autonomous state model* (partisan model) offers a picture of complex and many-sided preference structures that politicians and policy-makers may have. Where the goals of state personnel conflict with those of external social interests, internal state preferences prevail in policy-making. Interestingly, however is the case where such differences are muted. Because the state is rather independent, public officials' preferences nonetheless design the policy in detail. In conclusion, elite theory is a rather dispersed theory, ranging from classical elitists who restricted themselves to a very narrow definition of state elites, all the way to modern elitism that attempts to explain (and justify) statism, international networks and policy communities. Here, I offered only a brief overview of this complex set of theories.

1.1.3 MARXISM AND NEOMARXISM

Dunleavy and O'Leary (1987:203ff) argue that the core Marxist system of ideas draws principally on three early 19th-century influences: British economics, German philosophy and French revolutionary experience. While the debate on the economic part of the theory is not going to be elaborated in this thesis, it is interesting how the lack of consensus between Marxists has grown more significant. What all Marxists, however, do have in common are several basic ideas: the nature of the ruling class is defined by its ownership and control of the means of production; mechanisms that tie this class to the state are socialization, interpersonal networks, connection; state policies further the general interests of the capitalist class (Hay 2006: 72).

Some Marxists have also abandoned the attempt to detect a class struggle between the exploiters and the exploited within advanced capitalism.

Instead the focus of class struggle is displaced from the national level to the world level (e.g. Wallerstein). As Hay (2006) sums up, there are in principle four ways Marxists see the state. According to the first view, the state is seen as the repressive arm of the bourgeoisie (mostly based on Lenin's work *The State and Revolution*); the second view emphasizes that the state is an instrument of the ruling class (this is what is similar to elite theory); the third perspective sees the state as an ideal collective capitalist (see as the best example Altvater (1973)); finally, the state is seen as a factor of cohesion within the social formation (in Poulantzas' (1980: 24ff) words, "the unity and cohesion of a social formation by concentrating and sanctioning class domination").

Nicos Poulantzas emphasizes the role of state ideology in his last and very important elaboration on *State, Power and Socialism* (1980: 17) by stating that "the political field of the State (as well as the sphere of ideology) has always, in different forms, been present in the constitution and reproduction of the relations of production." Nevertheless, "economic functions (...) occupy the *dominant place* within the State...*The totality of operations of the State are currently being reorganized in relation to its economic role*" (ibid: 65, italics in original). As there are different forms of capitalist states, different modes of production and also different "social formations," Poulantzas argues: "A theory of the capitalist State can be elaborated only if it is brought into relation with the history of political struggles under capitalism" (ibid: 25).

Poulantzas (1980: 203-247) also discusses authoritarian statism in detail. There are five main features of it. First, there is an obvious decline of parliaments and the strengthening of executive power. Second, the separation of powers doctrine, meaning the loosening of institutional connections between the executive, the legislature and the judiciary, contributes to the creation of authoritarian statism. Third, in many countries there is only one single party which is dominant, providing for its inviolable authority. The fourth characteristic is that the executive dominates the media. Lastly, there are parallel networks which cross-cut the formal or official organization of the state and cause a concentration of powers to accumulate at the very top of the executive.

Another neo-Marxist legacy is the famous Miliband – Poulantzas debate. Whereas Poulantzas accused Miliband of instrumentalism (since this latter saw the state as neutral and dependent on the capitalist class), Miliband answered by reproaching structuralism to Poulantzas (since he was decisive to investigate the structure, form and function of the state itself, seeing it not merely as an instrument of economic elites, but also the co-bearer of capitalism). Later, the fruit of this debate was a rephrasing of positions by both protagonists: Miliband embraced the idea of Block, where the state is seen as a custodian of capital, and Poulantzas started something which would be formulated as the strategic relational-approach by the probably most influential contemporary Marxist, Bob Jessop. Jessop's well-argued analysis challenges non-Marxist theories with the force unmatched among the Marxists.

Jessop makes a significant contribution to the theory of the state, notably in his recent works (Jessop 1990, 2002, 2006). Bob Jessop's approach in his book *The Future of the Capitalist States* (2002), influenced notably by the regulation school and the theory of the state by Gramsci and Poulantzas, analyzes the shift from the post-war Keynesian welfare national state and Western (Atlantic) Fordism, to the post-Fordist accumulation regime which he dubs in this book a 'Schumpeterian competition state'. Jessop focuses on various subjects: on the restructuring of the welfare state but also on interconnections within the knowledge-based economy, on the increasing importance of economic policies to the detriment of social policies.

Marxist thinkers have also tried to answer another question, as elaborated by Dunleavy and O'Leary (1987: 231-233): how have the dominant classes or fractions in capitalist societies managed to enforce sufficient control to restrict class consciousness? Some neo-Marxists emphasize that working-class political mobilization confronts special difficulties. Hierarchical organizations are more unified, creating constant pressure upon proletarian movements to imitate their modes of organization. However, hierarchy is capable to erode the important "collective identity" of the working class on which all the possibility of the effective collective depends. Moreover, the capitalists

and their class allies (such as the petite bourgeoisie and controllers of labour) are much better organized than proletarian movements. Capitalists are able to withdraw resources more incrementally, with restricted implications for their own immediate welfare. In the similar vein, they can usually redeploy means of production in other localities, regions or countries if faced with large-scale disruption. No wonder, then, that the dominant classes have survived for such a long time.

Besides that, Marxists emphasize the production of a dominant ideology, which is a set of ideas about political and social questions which not only privileges capitalist interests, but also protects the status quo from criticism by making existing social arrangements appear completely normal and inconspicuous. Dunleavy and O'Leary: "Direct capitalist control of influence over the communication of ideas (mass media, publishing, universities) and capitalist influence over the available ways of understanding are systematically skewed towards representing the social system, and its conflicts in ways which do not threaten the hegemony of capital" (ibid: 232).

In this last line, it is also important to note the importance of Antonio Gramsci, whose explanation of the dominant class is one of the most quoted among the neo-Marxists. The dominant class, in order to maintain its supremacy, must succeed in presenting its own moral, political and cultural values as societal norms, thereby constructing an ideologically-engendered common sense (Hay 2006: 69).

As far as state organization is concerned, three models are again proposed (Dunleavy and O'Leary 1987: 236-258): a cipher, guardian and partisan one, or, in the Marxist case, instrumentalist (cipher), functional (guardian) and arbiter (partisan) approaches. What is more, the state is seen as relatively autonomous of the capitalist class in the cipher and arbiter (class balance) models, and it is relatively autonomous of the capitalist mode of production in the guardian approach. Marxist instrumentalists put forward a similar cipher model to the external control model of elite theory. However, most instrumentalist accounts locate power more specifically than elite theory,

identifying only capital (economic) ownership as the critical basis for control over state policies.

All Marxist accounts of the state as a guardian use functionalist explanations. Public policies which concede social redistribution are interpreted as functional for the survival and development of capitalism. State agencies have quite a lot of autonomy from direct control by capital which is attributed to either the separation between economic, ideological and political structures with their own dynamic of development. The Marxist view of the state as partisan is provided by the arbiter model, generalized from Marx's original conception of Bonapartism as a transition period from capitalism to socialism.

The modern arbiter model sees a general role for a strong, relatively autonomous state capable of organizing different fractions of capital behind a strategy attuned to the needs of the dominant fraction of capital (TNCs). Therefore both the state and its environment are autonomous. Authoritarian statism is considered to be able help to revitalize other classes and thus achieve faster economic development.

Lastly, it worth emphasizing that, although the Marxist theory of the state is probably more fragmented than any other theory, their sharp and potent critique of capitalism often remains non-responded. Some claim that the Marxist approach is the only one to consider "society-made states" and not merely "state-made societies" in its analysis (Piersen 1996). The weakest point of Marxism is, however, its limitation to a purely theoretical criticism of the (capitalist) state. As for Marxism in practice, this thesis will take a closer look at Yugoslavia, whereby many practical shortcomings will become clearer.

1.1.4 PLURALISM AND NEO-PLURALISM

The distinction of pluralism in relation to liberal democracy on the one hand, and elite theory or Marxism on the other, is that the power is not exclusively in the hands of the electorate, nor possessed by an (economic or political) elite. In other words, no social or economic agent is seen as omnipotent. The pluralism

sees the power as something changing: it is the result of the changing access to both monetary and non-monetary resources.

Martin Smith (2006: 21ff) retells an interesting story of pluralism, which formally appeared in Britain in the first half of the 20th century. The notion is in itself really pluralist, because it can be linked to a range of ideological thought including that of anarchists, socialists, Whigs and Conservatives. The founding were that liberty should be most important political value, groups should be regarded as “persons”, and that ideas of state sovereignty should be rejected. Thus, in its early phase pluralism was actually anti-statist, but this is due to historical circumstances. Namely, the period between 1914 and 1945 effectively destroyed the liberal state form that existed in Britain. The British state nationalized the pluralistic delivery of public goods so that the services delivered by the voluntary sector, private business and local government were taken over by the central government. This is why the pluralist authors of the time contested the absolute sovereignty of the state.

Hirst (1993) gives more detail on British pluralism, which in his opinion analyzes corporate personality, associationalism, develops a powerful critique of sovereignty and of representative democracy, and, finally, investigates the principle of function. As for this last, we can find more proof in the work of one of the leading thinkers of the English pluralism, G.D.H.Cole, *The social theory* (1920). The principle of function is, as he states: „[A]s the purpose or object behind an association or institution must be specific and in some degree intelligible in order to have the power to call the association or institution into being, so the functions of all associations and institutions, however they may change and develop, are, in the last resort, also specific.”

The notion that distinguishes Cole from the liberal mainstream is important in this context: he implicitly rejects the notion of methodological individualism. Whereas functions of institutions (therefore also of the state) are specific, if we choose to focus on the individuals, things are different: “Every individual is in his nature universal: his actions and courses of action his purposes and desires, are specific because he makes them so; but he himself

is not, and cannot be, made specific, and therefore cannot be expressed in terms of function" (Cole: 1920/1993: 61). On the very same page, Cole concludes: "An association is not, and cannot be, in any real sense, a "person", because it is specific and functional, and not universal. The individual becomes "functional" or rather "multi-functional" only by limiting himself; the association is functional and limited by its very nature. "

Since "the state is an inclusive territorial association, ignoring differences between men and compulsorily taking in everyone who ordinarily dwells within its area" because "it is not concerned not with their differences, but with their identity," it is clear that "the state must exist primarily to deal with things, which affect all its members more or less equally and in the same way (Cole 1920/1993: 20).

And while the other British pluralist Joseph Figgis believes that the "state is a synthesis of living wills" (Figgis 1920/1993: 126), his contemporary Harold Laski adds: "Government may be strong, but if it is to be human it cannot have the tentacles of an octopus" (1920/1933: 180). Crucial in this sense is that the monolithic state cannot exist, since "we are forced to the admission that the parts are as real as primary, and as self-sufficing as the whole" (ibid). Contemporary movements, especially trade union movements, are "driving us towards an effort at the partition of power"(ibid: 190).

Paul Q. Hirst (1993) notes that there is a difference between the American and the British pluralist thought. He claims that American pluralism focuses on the necessity and the strength of associations as a counterforce to the state and the corporate sector. This, however, is only one of the characteristics of the American pluralism. It is widely known that the writers such as Dahl, Lindblom, Galbraith or Connelly introduce economic theory, political philosophy and political economy into their analysis, and that they focus on a variety of groups within society.

In the 1960s the classical pluralism was challenged. With the emergence of economists such as John Kenneth Galbraith, the thesis of an enforced corporate power became increasingly more present. William Connolly's (1969) *The Bias of the Pluralism* was in fact the groundbreaking work that led to the creation of neo-pluralism. Neo-pluralism sees the state as a rather autonomous actor which is able to pursue its own interests, but it emphasizes also that political programmes are to a considerable extent oriented towards corporate interests.

Two writers who take the credit for the rise of the American pluralism are Robert Dahl and Charles Lindblom, both belonging to the Yale School. In his study *Who Governs? Democracy and Power in an American City* (1961) Robert Dahl shows that the policy-making in the United States is not monolithic. The same was confirmed by Charles Lindblom, who in his later phase came closer to Marxists, since he argued that there were many groups which shared the power among themselves, but there was however one group which had more power than the other: the business.

Unorthodox economists who are today seen as neo-pluralists examine the role of business as a special set of interest groups. John Kenneth Galbraith, similarly to other unorthodox economists, is strictly Keynesian in his macro-economic approach. They believe that government is necessary involved in fostering economic growth and smoothing out the peaks and troughs of the business cycle. They stress the role of the government intervention in sustaining large corporations, even though many of them emphasize and praise the importance of private sector. Similarly, the apparatus of welfare state is of critical economic significance (Dunleavy and O'Leary 1987: 275 ff).

It is important that neo-pluralists by no means assume that change in economic situation bears direct consequences in political and social relations within a particular country, which clearly distinguishes neo-pluralism from neo-Marxism. In the similar vein, technological progress is no guarantee for a predetermined development path. Hence, a strong preference for multi-causal

explanation to cope with the analysis of contemporary trends is also a hallmark of neo-pluralism (Dunleavy and O'Leary 1987: 285-288).

The neo-pluralist version of a cipher state view, the *deformed polyarchy model*, (Dunleavy and O'Leary: 288-300) argues that the cleavage between the formal political equality of liberal democracy and the obvious inequalities of power typical for capitalism as a socio-economic system is seen as creating a *dual polity*. The state is in part genuinely controlled by electoral competition, interest group lobbying and mass media, and representative institutions have a reduced by still not negligible role in exercising authority. Business influence in this dual polity is quite largely confined to economic issues directly touching on corporations' interests. Moreover, there have been important variations in the mechanisms for integrating business democracy (e.g. Japan, France).

In the second, guardian model, the *state is professionalized*. Professions bring a much more concentrated and formalized expertise to bear on the tasks of government. Profession training is closely integrated with the higher educational system and places stress on analytic skills and technical knowledge. Moreover, professional education places a good deal of stress on people conforming with a code of ethics stressing respect for the public interest. Finally, the professionalization of policy-making involves transferring power, especially over the implementation of public policies, to professionals themselves. Very often, the external control is provided by locating an agency in a network of interacting bodies (the best example is Japan, as we shall see later). In this manner, the active agreement of other actors has to be secured before policy can proceed, and different agencies defend different aspects of the public interest and related client groups (ibid: 305-311).

In this context, it is again worth mentioning Galbraith. The model of professionalized state overlaps to a certain extent with the famous notion of technostructure, introduced and discussed by Galbraith in his work *The New Industrial State* (1967). How to explain the technostructure? "This is a collective and imperfectly defined entity (...) It includes, however, only a small proportion of those who, as participants, contribute information to group decisions. (...) It

embraces all who bring specialized knowledge, talent, or experience to group decision-making. This, not the management is the guiding intelligence – the brain – of the enterprise” (Galbraith 1967:71).

Now how can such a strong technostructure cooperate with the state? Will it swallow it? Will it push in the background the essential role of the state? Galbraith does not think so: “The relationship of the technostructure of the mature corporation to the state is the same. The state is strongly concerned with the stability of the economy. And with its expansion or growth. And with education. And with technical and scientific advance. And, most notably, with the national defence. These are *the* national goals; they are sufficiently trite so that one has a reassuring sense of the obvious in articulating them. All have their counterpart in the needs and goals of the technostructure” (ibid: 309). This confirms the neo-pluralist thesis that the business is indeed a privileged group among many.

Recent pluralist developments, as argued by Smith (2006), are sometimes very heterogeneous. Whereas the theory of governance argues that the central state has completely lost power in the midst of power transfers to the international level, another theory, that of social capital (which I will elaborate in more detail in chapter 2, as a complement to developmental state theory), investigates the networks within and beyond the state, but to the state itself it reserves a rather limited role. In sum, pluralism and neo-liberalism explain the roles of the state with its environment, but they fail to problematize the state itself. Whereas, in the beginning many pluralists feared the state (for a critique see e.g. Bartelson 2002), others, mainly neo-pluralists see it the state as a benign institution. Here again we see the whole problematic of the binary oppositions, or the ‘either-or-thinking’: within a single school, the alternatives are to hate the state or to worship it. Luckily, neo-pluralists have begun to realize the flaw of such thinking, and they attempt to adapt their theory to the world we live in.

1.2 ENDOGENIZING STATE POWER

Having conceptualised the most present theories of the state within their approach to state intervention, I will elaborate at this point why these theories demonstrate considerable deficits in explaining the reality. But beforehand, what is actually our reality? No matter what we think about it, it is globalization. Globalization promotes economic cooperation and technological sophistication, but unfortunately it is also prone to crises, because it is very hard to manage the world under a single economic system. The word is present in various papers and discussions, connecting people and alienating them, enriching the ones, impoverishing the other.

Attacking globalization helps to enlighten its weakest points, but it does not tell us at all how to manage it. Joseph Stiglitz is a good example of a scholar who had turned from a general enemy of globalization to someone rather proposing how to handle it while it is here. One should only note his two books and the change in their titles (the first one being entitled *Globalization and its discontents*, the second, more reconciliatory and optimistic one, *Making globalization work*). Now, is there a way to make globalization work? We should undoubtedly begin with the state and its inner structure. To neglect the state means to neglect reality, since states are, in words of Stanley Hoffmann, rather “obstinate” than “obsolete”.

Ordinary citizens are quite baffled by the trade-off of different normative theories and the practice. Why does it come to this cleavage? The generally accepted truth is that theories and models are simplified versions of reality. If one invests certain effort to implement them, they can serve merely as *guidelines*, for the fact that reality is considerably more complex. For this reason, seeing state in its relation to the economy as a “black box”, or as a simple unit, is the root of all misunderstanding. Think of neoliberal principles: the state involvement in the economy is generally seen as unnecessary, even harmful. Statements such as the one by Milton Friedman, extensively enumerating the undesired state actions and then remarking that “the list is far from comprehensive”, is the best example.

In fact, this is also how radical liberalists (libertarians) see it. The ideology of market failure allows the state to intervene only if the market is not capable of bringing matters in order. The new right, irrelevant if thinkers are radical or not, is generally very sceptic about the role and the abilities of the state. They believe that globalization is and will yet prove to be an executioner of the state, this useless agent that unnecessarily intervenes in free markets and spoils everything it can.

Although he belongs to a different (and quite opposite) school of thought, neo-Marxist Poulantzas, by the same token, talks of authoritarian statism as a manner of confining basic democratic rights. Moreover, Antonio Gramsci's core concept was the state hegemony accompanied by a tacit consensus of the ruled. Generally speaking, the neo-Marxists concentrated on the notion that the state is merely to be seen as an instrument of bourgeoisie, and that the time is ripe for its disappearance.

Contrary to that, elitists welcomed the selection of *crème de la crème* that creates a state apparatus, controls society and business, and makes policy decisions. These elites are not merely economic ones, as argued by some Marxists, but also encompass political and social areas. In other words, elite theorists are, along with neo-pluralists, broadly not the adversaries of state intervention. Neo-pluralists emphasize the role that state has when controlling large corporations which have meanwhile become very powerful.

Still, today these theories lack preciseness because the issue *whether the state intervenes* is not the primary matter anymore. Any state, as we all well know, intervenes in the economy. Be it the United States, any member state of the European Union, Japan, emerging economies such as China or India, Latin American countries or any non-EU European states, it is obvious that the state is not deprived of its influence. In the similar vein, Kozul-Wright (1995), debunks the myth of Anglo-Saxon capitalism by demonstrating that the state has played a crucial role in the development of both countries.

The real question lies in the *extent and diversity* of the modes of intervention. Only if the US does not have a well-developed health system, this

does not automatically imply that the American state does not engage in some other policy areas, such as industrial policy. Analogically, even if the Nordic countries have the best social system in the world, this does not necessarily mean their innovation sectors are keeping pace with that successful system. In any case, the state is there and no one can deny its existence. Otherwise, the nine previous WTO trade rounds would certainly have borne some more fruit by means of more liberalisation, less protectionism and more famous national treatment.

Note that all of the theories presented above regard the state intervention as an independent variable. The scope of this chapter is to redefine the concept of state power by endogenizing it. The notion of state power is not an innovation: already Peter Evans, Linda Weiss, Ben Fine, Robert Wade and many more have made significant contributions in this field. The statist school originates from the notion of *Bringing the state back in*, which was the name of the book by Peter Evans, Dieter Rueschemeyer and Theda Skocpol (1985). They argued that the importance of the state has long been overlooked and that the whole notion of state power should be reconceptualized.

All these theories in favour of bringing the state back in, in fact rest upon Max Weber. Although, according to Kelly (2003: 74), Weber was not actually interested in providing a theory of the state, as we might understand that today. The state represented for him a cultural problem. Still, we can define a Weberian notion of the state as the one of a final, 'sovereign' authority with respect to the society and economy within a given territory (Greven 2000: 31). As Offe (2000: 64) reminds, Weber distinguished between the political community with its *Gemeinsamkeitsglauben* (a belief in community) and the *Gemeinsamkeitsgefühle* (feelings of belonging to a community). The proposal I will offer in chapter 6 will, in a way, also follow the classic Weber's vision of the state.

One is tempted to think that since Weber, nothing has changed. Still, as demonstrated by Schmidt (2006), there have been also some evolutions in the importance of institutionalism. It started with rational choice institutionalism,

which mainly explained the existence of institutions, thus also the state, by claiming that different interests push their creation forward. It was static and based on game theory and principle-agent theory, and it was very present in the public choice theory, as we have seen it previously.

On the other hand, historical institutionalism emphasized the path dependency. It was static, contenting itself to tracing varieties of capitalism in different countries and deriving the importance of historical roots of institutions. Similarly, sociological institutionalism argued that norms and culture had to take the credit for the existence of institutions. This kind of institutionalism explained thus almost the whole institutional complexity by cultural appropriateness. Its flaw was again its static. Unlike these various types of institutionalism, discursive institutionalism, to which Schmidt (2006) claims to belong herself, is said to be explained by communication, ideas and discourse among institutions, with an emphasis on change and continuity, and above all constructivism. This makes this kind of institutionalism dynamic.

Therefore the state also has to be demystified in the course of a dynamic analysis. This present section aims to synthesize the most important progress concerning the endogenous concept of state intervention (primarily based on the work of Linda Weiss) and then to offer its own input in further chapters.

1.2.1 STATE CAPACITY OR STATE CAPACITIES?

To start the analysis, Weiss (1998) reemploys the notion of “social caging” by Michael Mann, and understands it as a phenomenon where “with the nationalization of social life, much of the activity and social relations that were previously constituted at local or supra-national levels came to be regulated through the nation-state, hence depending increasingly on the latter for its existence” (Weiss 1998: 11).

As far as government failure is concerned, Weiss, in line with the “bringing the state back in” school, identifies two neo-classical premises that she refutes. The first is the one of the predatory or rent-generating state. The main starting point is that bureaucrats do not pursue collective goals, but only

their own ones. This is why they have a kind of arbitrary power. However, the institutional view is able to offer a different picture. Namely, not the simple presence of institutions, but the degree and type of institutional depth (insulation) and breadth (embeddedness) plays an important role in determining and delimiting this arbitrary power of bureaucrats (ibid: 18).

The other neo-classical assumption is that markets are generally more efficient than governments. In other words, government failure is the main reason to think that state is generally incompetent. Weiss offers an alternative view by arguing that in those states with a mainly or completely liberal regime, their relatively weak domestic capacities to respond to economic change would appear to be due less to endemic or insurmountable problems of rent-seeking and information gaps than to an historically formed regime predisposition hostile to government coordination and public-private cooperation (ibid: 20). The most challenging issue of Weiss' work (1998, 2003) is obviously to show why states are not always merely predatory and inefficient market substitutes.

First, let us turn to the linguistic, but also semantic, notion of state power. Linda Weiss notices: "(...) there can be no such thing as state capacity in general (...)" (Weiss 1998:4). According to her, we should be talking about many *state capacities* instead of only one, since the state can arguably be successful in some areas and less successful in the other, as already stated above. State capacity can only be defined if one takes into account that states are not unitary or monolithic structures. There is no particular crystallization that can ultimately determine the overall character of the state (ibid: 15ff). Thus, it can help to differentiate capabilities as between the domestic and international spheres. It makes little sense to speak of state capacity in general. One must always ask: Capacity for what?

Taking a closer look at the East Asian countries, Linda Weiss (1998) defines the sources and outcomes of state capacity. She seeks to show how the government-business cooperation can be accommodated in a theory of state capacity. The forms of cooperation have adapted over time to the changing tasks of transformation (ibid: 43). Historically and geopolitically formed

regime orientation of the state is highly interlinked with its bureaucratic attributes and government-industry linkages. Through its capacity to adapt to external shocks and pressures by generating new means of governing industrial change, the state can then design and implementation of strategic industrial policies. This is done by resource coordination, selective intervention and disciplined support. The outcomes are dynamic internationally competitive industries (ibid: 44).

Weiss then goes on and divides states into those that are mainly concerned with output and growth (developmental states), the ones that redistribute the present resources (welfare states), and the third category of states that either do not do anything of the above, or try to do both. She concentrates on the last group, namely the states that try to do both, adding that “state capability has today become an important advantage in international competition” (Weiss 1998: 5) because state coordination encompasses “coordinating complementary investment decisions, organizing the specialization of smaller firms (...), promoting the sharing of information as well as technological acquisition, learning, and diffusion (ibid: 6).

“Transformative capacity” is the ability to coordinate industrial change in order to meet the changing context of international competition (Weiss 1998: 7). States with very high extractive capacity (Sweden) exhibit little of the transformative capacity of a low-taxing state like Japan. One false belief is that, the more open or internationalized an economy, the weaker the state’s capacity to govern industrial change. This coincides with a general belief that globalization will destroy the state. In this case one would predict for Sweden, which is a highly integrated nation state, relatively weak state capacity. This is not true, since the state as such is not the sole source of its transformative capacity – the latter depends very largely on the nature of the state’s domestic linkages (ibid: 8).

Weiss also talks about the limits of the distributive state. The Swedish problem is not so much its famous system of public compensation for labour, affected by economic change, as the absence of public inducements for

industry to pursue quantitative change. The Swedish system has been quasi-Keynesian with regard to labour, but *laissez-faire* with regard to industry (ibid: 113).

As states do not behave in a uniform manner, Linda Weiss presents four principal hypotheses to explain cross-national differences in state capacity.

a) The first places most emphasis on *social bargaining, or corporatism* – often seen in a negative context, as oligarchism, elitism and sometimes even fascism. The tripartite version of corporatism involving power-sharing arrangements among business, labour and the state, has often figured in comparative analysis as the key to state capacity (but compare Olson 1971 on the one hand, or on the other hand Jessop 1990). The state facilitates corporatist bargaining via legal recognition of organized interest and provision of policy resources as a quid pro quo – industry negotiations over wages. Second, corporatist bargaining underpins the state's macro-economic efforts to control inflation. However, Weiss believes that this thesis is merely concerned with social organization and not the organization of the state itself (Weiss 1998: 24 ff).

b) The second thesis is the one of coercion, or the *strong-state thesis*. A strong state is generally understood as “the national political executive and the bureaucracy which serves that executive office” (ibid: 26). The existence of such state is tested on the basis of three capacities: the ability to formulate policy goals and evolve strategies for implementing them independent of societal pressures; the ability to alter the behaviour of important domestic groups in order to further its policies; and the ability to restructure the domestic environment (property rights, industrial structure) in pursuit of its goals. This coercive sense of capacity is often emphasized, or the thesis of “leading” and “following”. Therefore Weiss concludes: “(...) state power has been conceptualized in a way that makes it virtually impossible to apply to modern states” (27). Her critique (28 ff.) consists of four arguments.

First, states are not monolithic. The arguments of “strong” and “weak” are general ideal types. Secondly, strength or autonomy is a poor predictor of policy orientation. It is important to distinguish the question of transformative capacity and developmental effectiveness from that of “strong” versus “weak” states. A strong state is not necessarily a highly interventionist one, while a weak state may well be interventionist (socialist states). The third argument is that strength should be seen as autonomy, and effectiveness as capacity, and that those two should be distinguished (if a state is autonomous, this autonomy does not have to be fruitful for the society in general). Lastly, when talking of “statism”, one should bear in mind the difference between the notions of “power over” and “power to”. In the first notion, the state *acts against* particular dominant classes (as emphasized by Marxists). The second idea is, however, to emphasize the state’s capacity to *cooperate*.

c) The third strong state thesis, in addition to corporatism and authoritarianism, is the one which stresses the role of *policy instruments*. It is important once again to distinguish the state’s ability to formulate its goals from the capacity to devise and implement strategies to achieve them. The question is then to ask whether state structures can insulate political elites from the demands of powerful lobbies. State insulation derives from the mode of recruitment of the national civil service, the degree to which power is centralized and the extent to which the political executive has autonomy from legislative scrutiny (Weiss 1998: 31).

Consequently, Zysman (quoted in Weiss 1998: 32) tries to establish three categories in order to find the connection between the character of a country’s financial system and the capacity of the state to intervene effectively in the economy. “State-led” systems are those typical of France and Japan, where credit-based, price-administered finance allows bureaucrats to coordinate the flow of investments. “Company-led” models of change occur where there are extensive capital markets and therefore minimal means of state-coordinated change, as in Britain and the US. Finally there is a third

pattern, the “negotiated” or tripartite-bargained adjustment, typical for the former West Germany, where the financial system was led by banking institutions.

d) Numerous authors, for instance Evans (1995, 1997), propose the fourth category of the state explanations, the notion of capacity as *embedded autonomy*. They argue that the capacity also depends on the organization of groups in society. Peter Evans affirms that states which are more effective in achieving their transformative goals tend to be not only merely sufficiently autonomous to formulate their own goals, but also sufficiently *embedded* in particular industrial networks to implement them. In other words, autonomy is not sufficient if goals are to be implemented successfully. For that to occur, autonomy must be embedded in specific social ties. This is, says Evans, an example of “Weberian bureaucratic insulation” (Evans 1989). Weiss, however, argues that embedded autonomy, although it pertains in all states, illuminates the transformative capacity of some states. “*While all (or most) industrialized states have developed a generalized insulation and embeddedness, only some states have developed these features also in a form and degree of particular benefit to the industrial economy*” (Weiss 1998: 36, italic in the original).

Although many studies suggest that the East Asian capacity for coordination has an institutional basis, Linda Weiss develops this proposition into a further and a novel one: the institutional arrangements results in a distinctive kind of government- business relationship, referred to in her work as *governed independence* (GI), different in her view from all other approaches, including *governed market theory* by Robert Wade (1990, revised in 2004).

Governed market theory proposed by Wade departs from the notion of strong state, which is capable to develop strategic industrial policies, resulting in the high level of investment and internationally competitive industries. In the absence of some form of coordination, there is no guarantee that savings and investment will be channelled towards productive rather than speculative activities. Wade, who is generally interested in the role of the state in East Asia,

reveals in a short study (Wade 1995: 126-130) what factors have been crucial for such an immense boom. In his opinion, the availability of information provided and coordinated by the state for its officials influenced the developmental path of these countries. Also education, trade policies and organization of pilot agencies that exercise foresight and strategic planning, as well as stable state-society relations, have all contributed to East Asian development.

In Linda Weiss' opinion, many studies fail to pay sufficient attention to the possible importance of cooperation to a theory of state capacity. Cooperation is usually seen as a sign of the diminution of state power (Weiss 1998: 45). Governed independence is not seen as "power 'over' society that one associates with authoritarian government; it is power 'through' society, which is much more potent in developmental terms" (ibid 49). Vartiainen (1995) invokes that the state (such as Finland, but also in the East Asian case prior to the Asian crisis) very well coordinated investment. Late industrializers, moreover, have a bureaucratic tradition based on meritocracy – an important point for the further discussion.

The GI theory identifies the major risks firms are exposed to without the state-business cooperation: raising capital, developing new product technologies, finding new markets and training skilled engineers (Weiss 1998: 47). The results are institutional capacities for industrial transformation, being the best explanation on how Japan and the "Asian tigers" of the 90s succeeded to build up strong and speedily growing economies. In accordance to the theory of GI, Weiss argues that the notion of 'embedded autonomy' by Peter Evans does not encompass the relation of the autonomous and therefore insulated bureaucracy with its broader political environment.

Four main forms of GI are (Weiss 1997: 71-79): disciplined support, public risk absorption, private-sector governance and public-private innovation alliances. In Wade's view, only leadership (urging or prodding industry to do something that it would otherwise not do) counts as making a real difference to investment and production patterns. He suggests that the government can

intervene as a leader or as a follower. Following the market means that the government assists the projects that private business people want to undertake, and leading the market means that the government initiates these projects (Wade 1995: 133).

However, Weiss (1998) argues, is it really so that if the state is seen as leader, industry has to be seen necessarily as follower? Concentration (social corporatism) applies where the state is moderately insulated and the social group is highly organized in a robust negotiating relationship, but where domestic linkages are broadly constituted (Sweden). The last category, proposed by Weiss herself, is the one of governed interdependence, where both state and social groups are strong. In other words, the state is insulated and industry is highly organized in a strong negotiating relationship, but where domestic linkages are relatively narrowly yet tightly constituted (post-war Japan) (Weiss 1998: 37). Her concept of GI (governed independence) denies that, suggesting a simultaneous initiative but both the state and the business. This is visualised by presenting three types of GI.

The first type of GI, disciplined support, exists where performance conditions (outcomes) apply in exchange for support. Disciplined support is not simply a guard against rent-seeking behaviour. It is also a way of monitoring and measuring the attainment policy goals and of establishing public accountability. Japan has also used protection as a creative discipline. The second major type of GI involves public initiatives. The public sector absorbs most or all of the risk, often mediating between producers and end users in the domestic market. The third type, private-sector governance (PSG) is an unusual kind of state capacity in that it involves teasing out of economic society the capacity for self-governance. It can be seen as a system of state informed coordination in which the state acts as coordinator of the last resort. The final type of cooperative coordination is increasingly associated with policies for acquiring, developing, upgrading and diffusing technology. The proliferation of innovation or technology alliances is a good example. Public-private networks

discipline capital and build in public accountability through performance conditions set by the state.

GI is therefore a state-informed system. Such system does not happen entirely by chance (the importance of historical legacies and situational circumstances notwithstanding). The organization and participation of business is indeed fundamental to its evolution and success; but if a state and its wider political elite are not imbued with the sense of a transformative project, they will not seek to build such capacities or to secure their institutional supports over time (Weiss 1998: 80).

In other words, GI suggests, different from Wade's or Evans' propositions, that both the state and society be strong and cooperate *without one being somehow superior to the other*. Bureaucracy apparatus consists of high-quality bureaucrats, whose merit-based recruitment and promotion, rather than political appointment, have tended to minimize political manipulation of the bureaucracy. The second feature of East Asian success are the core economic ministries, 'pilot agencies' (MITI in Japan, EPBs in Korea, ITRI in Taiwan), which own the particular capacity for marshalling and analysing economic information in-house (ibid: 50). This in-house information-oriented capacity equips state agencies with competence in areas normally left to private sector, and it nurtures bureaucratic independence vis-à-vis sectoral interests. Pilot agencies are again completely insulated. For instance, MITI's horizontal agencies (such as the Industrial Policy Bureau, responsible for overall industrial policy) develop and coordinate policy across industries.

However, even the most perfectly structured civil service can have little economic impact if political leaders do not share growth agenda. State-industry linkages, or 'domestic linkages' as referred to by Linda Weiss, include the array of institutional ties, policy networks, deliberative councils and the like, which link government and industry in the information-exchange and policy-making process (Weiss 1998: 55). Institutional linkages are important because they are about state doing things not in isolation from the private sector, but in concertation with industry. Bureaucracy therefore needs to be closely

connected with organized industry. Public-private cooperation is more institutionalized in East Asia than in most other countries.

As far as the organization of industries is concerned, it is worth mentioning that close ties between government and industry are not, in themselves, an explanation for state's effectiveness. Cooperation seems to work well only if the state is sufficiently insulated, so that it retains a definite capacity for social goal-setting and for coordinating policies and resources to that end. In short, GI requires a state that is, paradoxically, both distant and close. State connectedness without insulation is likely to breed rent-seeking and distributional coalitions that can smother vitality. By contrast, insulation without connectedness may widen information gaps that encourage policy failure.

1.2.2 STATE CAPACITY IN VIEW OF ECONOMIC TRANSFORMATION

Today many are claiming the death of the developmental state, arguing that if business is strong, the state must be weak. It is however important to be aware of how the term was first applied to capitalist economies. Chalmers Johnson reserved the term 'developmental state' for a state which was willing and able to pursue a transformative project. The state might encourage and support the industry's self-governance (interwar Japan), it might prefer to act through unilateral, top-down measures (World War II) or it might institute a more cooperative approach to decision-making (since 1950s) (Weiss 1998: 65). Panić (1995) stresses that such a decision-making method shown its fullest effect after the World War II, whereas after 1973 the situation has significantly changed for the worse in some countries.

Weiss (1998) proposes that there has been a transformation in the basis of state autonomy (i.e. from autonomy to embedded autonomy, from an insulated state taking many top-down decisions to one which has embedded its autonomy in a range of economic institutions). This transformation of state capacity is most highly developed in Japan and, as the tasks of the modern industrial economy have changed, so the changes in the basis of state capacity

have become more rather than less congruent with a transformative project (ibid).

There are several types of economic transformation. The first one is a revolutionary transformation which involves breaking with an antecedent economic system (socialist states). Historically, this type of transformation has required breaking the power of the dominant class. The type of state power here is insulated from, but not embedded in, the dominant economic groups hence a strong state in the sense of despotic-coercive capacity. Ellman (1995) reminds in this context that these countries have very little experience with normal market behaviour. Officials are not given sufficient incentive, so that they often leave public administration for the private sector.

The second type Weiss (1998) proposes is a structural transformation. In other words, it is the transformation from an agrarian base to an industrial one. This task appears to demand a strong state, as in type 1, detached from the dominant (landed) class and able to impose reforms and redistribute resources. The third type is sectoral (industrial-technological) transformation involves the creation of new branches of production the shift to new products, the adoption of new technologies, and the diffusion of innovation. Japan is the exemplary case. This type of continuous transformation demands not a 'strong' state in a coercive sense, but a more finely tuned, 'catalytic' state. In that context, a 'strong' state, understood as one with the capacity to act against private interests, is important in one sense only: when the private interests in question are inimical to, or in conflict with, a project of economic transformation (Weiss 1998: 66ff).

Catalytic states seek to achieve their goals less by relying on their own resources than by assuming a dominant role in coalitions of states, transnational institutions and private-sector groups. Weiss suggests that the most important power actors in these new inter-state coalitions will not necessarily be those initiating them, but those who participate in them on the basis of a position of domestic strength (Weiss 1998: 211). The Japanese and German cases suggest that not all capital is equal and that there is a hierarchy

to the integration process. The hierarchical aspect of integration is one that has a basis in strong transformative capability and hence is supported by robust domestic linkages between government and industry.

The state engineering a major economic transformation encourages entrepreneurship and creates a system of coordination, as emphasized by Chang and Rowthorn (1995: 36-38). Not only does such an undertaking require a consensus of different actors within the society, but it also needs a vision provided by the state. This vision is referred to by Chang and Rowthorn as institutionalization, meaning again that bureaucracy can play a significant role in informing agents of the creative potential of the state. This enables the transfer of “power” from the state over to business, making them equally represented. Holton (1998: 101) confirms that strong multinational enterprises (MNEs) also need strong states and stable societies, which requires giving governments a certain autonomy of those MNEs. This autonomy, again, is not to be interpreted as a rigid form of dirigisme.

In a nutshell, there are several categories we can identify. Statism applies where the state is “strong” (goal-oriented, insulated from pluralist pressures) and the social group is fragmented or weakly organized, making domestic linkages difficult or unstable. It results in top-down decision-making, relatively frequent information failures and implementation blockages. State corporatism applies where the state is “strong” and the social group is highly organized, yet is more an instrument of public policy than a negotiating partner – a situation conforming most closely to the notion of “embedded autonomy” (interwar Japan, 1960s South Korea).

In this line, Weiss (1998: 119ff) compares Germany and Japan and debunks the myth of Japan as an exclusively developmental, and Germany as an exclusively welfare state. Rather, they both combine the elements from each category. Such dualistic states are strong, with response from their business and civil sectors being equally potent. Indeed, Germany is not only a welfare state as it is thought to be. Private-sector governance (PSG), a congenial alternative to state activism, became the principal means through which the

German state was able to affect its developmental goals. German state was very extended in the 90s, and its withdrawal was highly desired (Sontheimer 1995: 28).

In Germany, PSG is however far from being state free: it is by and large a state-sponsored and state-informed system of coordination. In Japan, the same applies to the famous ministry, MITI, the role of which will be also recalled in this study. The Japanese state is also distributive and not merely developmental, in the sense that it supports its agricultural policy (rice farmers), its sunset industries (declining sectors), small businesses and not least, its employees (Weiss 1998: 119ff).

1.3 CONCLUSION: THE STATE, GLOBALIZATION AND THE FRAMEWORK OF NEO-PLURALISM

In the wake of the global financial and economic crisis of 2008, one might assert that globalists have definitely overplayed the degree of state powerlessness. At the same time, the state response to crisis is not uniform. It seems that the basic state hypothesis is inspired largely by the EU experience, but it would be far too easy to conclude from the mere existence of the EU that differences in state-economy relations and policy regimes have been ironed out with increasing rounds of integration. This issue will also be more discussed later. For now, the notion of state adaptivity is also worth mentioning. The East Asian experience has shown that there is much more to governing the economy than only macro-economic policies. There is also the industrial policy, which must be creative.

In her other, more recent work *States in the Global Economy: Bringing Domestic Institutions Back In*, Linda Weiss (2001) contends that globalization, although seen as a constraint, is not such a peril as suggested, if there is interdependence of domestic institutions with the rest of the population and with the rest of the world. In this manner, the constraints are well delimited. Even the

effectiveness of contemporary welfare states, as shown by Swank (2001), is not damaged by globalization if domestic political and economic institutions are efficient. Michael Loriaux (2001) confirms the same for one of the most known European pioneer developmental states, France. Hence, both state forms have a future, and, if we follow the line of argumentation of Linda Weiss (1998), they have a future if combined as well. Even if exposed to criticism after the Asian crisis, the East Asian model, which I will analyze on the Japanese case, is seen by many as the one that has a great future with the right institutions to monitor its development (Woo-Cumings 2001).

Production and investment are not subject to a strong globalization tendency whereby an open world market displaces institutional and locational constraints; the same cannot be said of finance. Many economic historians, such as Opello and Rosow (2004), precipitate themselves to assert that the state is challenged today, given its historical evolution, its ups and downs and its amount of power now and then.

We are witnessing changes in state power, but these changes have to do not with diminution but with reconstitution of power around the consolidation of domestic and international linkages. Linda Weiss (2001: 316) talks about post-developmental states with new roles proscribed, and stresses that the most important change today is “the transformation from absolute, dirigiste, statist, or rigidly arm’s-length types of rule” such as the one in post-socialist states, “to one based on either increased infrastructural state power (China) or new forms of governed interdependence”.

Can we, and if the answer is positive, then *how* can we, link the concept of embedded autonomy (Evans), governed market theory (Wade) or, finally, governed interdependence (Weiss), all very resembling to each other and attempting to explain the East Asian growth, to the most important theories of the state presented in section 1.1 of this thesis? If we decide to agree with the findings of Evans, Wade and Weiss, implying that the Asian model was so successful because the state was insulated, but not authoritative, we might ask

whether any of the group of theories presented in section 1.1 came closer to such an understanding of the state.

Once again, these were the assumptions of the scholarship presented in this section:

a) State power is not singular and not monolithic. While up to now there have been observations of *one single state capacity* (to intervene in the economy), this literature strange presents the state as agent equipped with *many capacities*, one of which is to coordinate the market.

b) The state is an initiator of economic policy, not merely concerned with macroeconomic data, but also with a comprehensive and well-organized industrial policy.

c) The state is sufficiently embedded (Evans), governing the market (Wade) at the one hand, but at the same time allowing the market to stay creative, by means of governed independence (Weiss).

d) Such a state might also, such as in the Japanese case, include a welfare policy which is not incompatible with the welfare state such as Germany. Thus, emphasizing the industrial policy does not provoke a cleavage of such an approach with the approach of welfare state.

Classic British pluralism did not refute the state completely, as pointed out by Bartelson (2001). It simply put forward the idea that the state is not the *only actor*, and that it is not at all homogenous. Unlike liberal theories, the British pluralist Cole refuted methodological individualism by showing that the institution and the individual cannot be equalized, since the individual cannot be reduced to a function, which is the case of associations and institutions. Although the state does have a function, it is very complex since the state, here again, is not monolithic. Moreover, neo-pluralist scholars (especially the unorthodox economists among them) very well predicted and described the developments within what was to become the East Asian developmental state, which I am going to elaborate in chapter 2.

As we shall see in chapter 3, the developmental state in Japan has been shaped by almost all of the characteristics of the *New Industrial State* by John Kenneth Galbraith, or what Marxists in particular refer to as Fordism: the state was highly professionalized and the powerful business technostructure counterbalanced the equally powerful bureaucracy. Industrial planning was a normal element of the industrial policy, and the state was still a capitalist one.

Clearly, education was also given a significant value. What is different from the analysis of the neo-Marxist theory, and similar to the elite theory, is obviously the fact that the elites were carefully selected on the basis of merit and technical excellence (the model is still existent, but not only in Japan; also in France there is a prestigious *grande école*, *École nationale d'administration* or ENA, the institution that yearly selects and educates the best French bureaucrats-to-be). Moreover, the objective of these elites was not indoctrination, but professionalization of the society. Different from the elite theory is however the understanding of power. As Weiss, Evans or Wade observe the East Asian miracle, they argue that the state strength was not in a power to manipulate, but to transform and to successfully shape industrial policy.

It is important to stress that the strength of the state in Japan, Korea, Taiwan in the 70s, 80s and 90s, as well as in Finland, France or even Germany in the 90s, was not challenged by the strength of industry. In fact, the private and the public were a perfect complement for each other. Politics and bureaucracy on the one hand, and business on the other, found the common ground and cooperated successfully. This is the fact that again makes the set of explanations presented in this section closer to the neo-pluralist theory.

For all these reasons, this thesis will attempt to argue that the partisan model on the neo-pluralist state, the one in which the state cooperates with society (which is as pluralist and as fragmented as the state itself) and is equally strong to it (or equally weak, considering their interlinking), is in fact the logical improvement of the East Asian developmental state.

CHAPTER 2

FROM THE DEVELOPMENTAL TO THE POST- DEVELOPMENTAL STATE

The capacity of the state to shape industrial policies by intervening to a “right” extent, not being too authoritative but also not too *laissez-faire*, is an art which only a few are able to master. The developmental state perspective argues that such a strategy is however possible, and that it is also the only advisable one for any state wanting to enhance its competitiveness in today’s global world. Besides the market intervention, the developmental state too had two important attributes: social and welfare policies (the features it borrowed from welfare states) and its ability to adapt to a changing environment, as well as to manage economic and financial crises.

Therefore, section 2.1.1 will summarize the most important theoretical findings on bureaucratic and political decision-making developments and try to place these into a specific category within the concept of a developmental state. In section 2.1.2, I will then turn to the issue of state-led development – the industrial policy and the ability to change. Section 2.1.3 will mark the transition to the modern approach to the developmental state, thus in brief presenting the theory of social capital. After that, section 2.2 will attempt to demonstrate the necessity of reforms for the developmental state and the reformulation of the concept into the notion of the post-developmental state.

I will then review the arguments which enforce the necessity of having a creative and active state. The most obvious among these cases is the failure of neo-liberalism itself, something that has become clearer than ever during the 2007/08 economic crisis. However, due to the fact that the crisis is still ongoing in the time of writing this thesis, it is not still too early to critically judge it. Hence, I will turn to the (in)famous Washington Consensus (2.2.1) and its

consequences, notably the case of Argentina (2.2.2), which then led to the reformulation of the concept into a notion of Post-Washington Consensus (2.2.3). However, this concept was too vague to last, and with the global crisis of 2008, it failed again.

Moreover, I will briefly sketch the critique of the concept of the traditional developmental state: on the one hand, it is true that the strong state (in particularly its bureaucrats) can be a source of corruption due to powerful interest groups from the business sector – something referred to in Japan as ‘iron triangles’. On the other hand, the concept has overlooked any other social relation except that between the state and the business, and any other policy except industrial policy. This will be dealt with in section 2.2.4. Finally, in section 2.3, the most important social actors and groups from, on the one hand, the traditional developmental state concept, and on the other hand, according to their today’s role and importance, will be summarized.

2.1. DEVELOPMENTAL STATE: THE NOTION

“Like most human institutions (the family, the village, the city, the state, customs, laws, the nation) developmental state was born long before anybody thought of naming it. Indeed there were developmental states long before economists, political scientists or historians recognized them as such, and that not all developmental states, as conventionally labelled, have been true members of the select club of developmental states” (Bagchi 2000: 398)

This chapter aims to summarize the most important characteristics of the developmental state. As already mentioned in chapter 1, the developmental state represents the concept in which is the state is oriented towards economic growth and development, and in which it acts in a rather entrepreneurial manner in order to attain these goals. The name was coined by Chalmers Johnson in his work *MITI and the Japanese Miracle: the Growth of the Industrial Policy 1925-1975* (1982), where the author analyzed the Japanese economic growth, with the emphasis on the period after the Second World War. Johnson

(1982: 315-319) defines elements of the state which would be ready to follow the Japanese model: a small, elite bureaucracy, a political system in which the bureaucracy is given sufficient scope to take initiative, the market-conforming methods of state intervention, and finally, pilot development organizations such as the famous Ministry of International Trade and Industry (MITI).

According to Bagchi (2000: 399), the first DS in our sense was that of the northern part of the Spanish Netherlands in the 16th century which finally evolved into today's Netherlands in 1568. The state was run by the elites, thus by merchant princes and manufacturers. The second factor which contributed to shaping a developmental state out of the Netherlands, was the intense patriotism of the Dutch. Their nationalism was, however, intensely practical. While they were for instance ready to combat Spanish aggression, they would make peace whenever the oligarchs considered it profitable to consolidate their gains rather than squander their resources.

A third notable characteristic of the Dutch developmental state was its religious tolerance. While Calvinism was declared the state religion in several of the states, there were very few conflicts between the Calvinists and the dissenters. The fourth characteristic was a deliberate attempt to create institutions and habitats which would facilitate clean living and growth (400-402). However, as Bagchi continues, it is important to note that all these innovations presupposed a ruling class which was literate and often highly educated. The Dutch ruling class encouraged education and the useful arts and founded academies or training institutes for advancing them (2000: 403).

The recognition of England, and later on, the United Kingdom, as a developmental has been delayed, but it does not change anything in the fact that Britain had some traits of a developmental state (ibid: 404). Although by the beginning of the eighteenth century Britain had emerged as a state with all powers of national policy-making centralized in the Parliament, it operated a highly decentralized state apparatus run by the property-owners in the counties, provincial cities and towns. This decentralization changed, and the Keynesian

economic policies after the Second World War until the arrival of Margaret Thatcher in the late 1970s were very in accordance with the logic of developmental state.

Germany, too, used to be a developmental state. The economic unification of the German states, the abolition of internal tariffs, customs and serfdom, and massive investments in railway networks by Prussia and other German states from the 1830s led to a vigorous expansion of the domestic market. The state apparatus was manned by the powerful bureaucrats and nobility with roots in the *ancien regime*. But the state effectively pursued goals of capitalist development, partly as a means of enhancing its military power and partly, of course, with the objective of enhancing the standards of living of all Germans.

Authoritarianism of the German state acquired a nationalist rationale under Bismarck with his successful pursuit of a policy of Prussian imperialism. Since a successful developmental state actively encourages learning from foreigners, adaptation of technologies and organizations to local conditions and introduction of productive innovations, Bagchi concludes that in that respect, even small German principalities and states were heading towards the model of a developmental state long before Germany was unified (ibid 410ff).

The Japanese developmental state, as we shall see in more detail, also evolved over time until it assumed its mature form in the late 1950s. The beginning of modern Japanese development is generally assigned to the period of the Meiji Restoration, and by and large this chronology is right. However, some preconditions for the construction of a developmental state had been laid down before 1868. These included freedom from foreign rule; in spite of the unequal treaties imposed on Japan after the arrival of Commodore Perry, the Japanese attained a high degree of national autonomy in policymaking. Other factors included the intense nationalism of the Japanese ruling class and its demonstrated ability to learn from foreigners such as the Chinese who had better technologies of production or war, or useful principles for organization of the state and society (ibid: 413 ff).

Finally, South Korea also fulfilled one important characteristic of a developmental state, namely a strong and realistic sense of nationalism. Syngman Rhee, the first president of South Korea and a dictatorial ruler who ruled from 1948 to 1960 and was utterly dependent on U.S. military and economic aid. But he led a very clever policy: he played on American fears of the resurgence of communism and his threat to invade North Korea in order to extract more aid. Later on, South Korea developed in a similar way as Japan: very strong relations of the state with large industrial conglomerates, *chaebols*, were the axis of economic growth (ibid: 423).

Becker (2002) attributes the beginning of the developmental state, which would correspond to Johnson's perspective of the concept, to the inter-war period. Developmental state reached its absolute flourishing after the Second World War and lasted until the 1970s. Among other countries, many Latin American countries focused on the model of import substitution in combination with the construction of the welfare state. In the words of Perry Anderson: "Mercantilism was precisely a theory of the coherent intervention of the political state into the workings of the economy, in the joint interests of the prosperity of the one and the power of the other" (quoted in Woo-Cumings 1999: 5).

This thesis will distinguish between *the developmental state* (understood generally as the East Asian state model), *the post-developmental state* (referring to East Asian countries after the Asian crisis) and *the developmental society* (a term used by Linda Weiss (1998)) but not explained quite in detail). In other words, while the notion of developmental state was used in both positivistic and normative ways (as an experience of Japan, South Korea, Taiwan, and, to some extent, of Malaysia, Singapore, Hong Kong and India, and as an ideal concept for other countries to follow), the notion of the post-developmental state is rather vague.

This is firstly due to a relatively short period of the usage of the term, and, secondly, to the impreciseness of the notion itself. For, what is a post-developmental state? The concept tells us that the old idea has been rendered

old-fashioned and overcome, but it does not tell us what it consists in. It informs that the developmental state has been reformed, but it lacks an explanation *how* this was done. Similarly, the notion of a developmental society has not at all been discussed at all. One could guess that the idea is the insulation of the state into society, making both inseparable from each other. If the state is seen as one of the actors within society, i.e. if society is seen as superior to the state, then the notion of developmental society is justified. I will discuss this all the way through this thesis.

Let us go back to the initial concept of developmental state. Woo-Cumings reminds that what we understand today by a developmental state was already to find in the writings of early development economists, such as Gunnar Myrdal, Paul Baran, P.N. Rosenstein-Rodan, and Simon Kuznets. But why did it all start precisely in East Asia? Woo-Cumings (1999: 7) reminds that revolutionary nationalism in East Asia grew from war and imperialism and manifested itself variously. In China and North Korea it evolved into communism, and in Japan, South Korea and Taiwan it became the capitalist developmental state.

As for these countries, Chalmers Johnson argues that it was state control of finance that was the most important aspect of developmental state, followed by other aspects such as labour relations, autonomy of the economic bureaucracy, the combination of incentives and command structures. Therefore developmental state „actually exists in time and space in East Asia and also exists as an abstract generalization about the essence of the East Asian examples. It is both particular and generalizable“ (Johnson 1982: 34).

As already discussed in the first chapter of this thesis, the role of the state in the regulation of national economy as well as its general interaction with the market has represented a bone of contention for a very long time. Moreover, the debate does not seem to cease, especially in 2008, because due to the global crisis, the return of the state has become a subject of many public discussions. Therefore, the re-examination of “state capacities”, as suggested

by Linda Weiss, or its “embedded autonomy”, as proposed by Peter Evans, is indeed necessary.

Generally, the primary argument of the development state scholars and partisans is the efficiency of the state-led industrial development. The role of the state in shaping its own industrial policy is for many authors of developmental state school absolutely crucial. I believe that the traditional concept of developmental state should be analyzed from two different angles: one explaining the relationship of the state, business and the broader society, and the other one analyzing the state itself, i.e. its bureaucracy and politics. Hence I will briefly discuss these two features of developmental state, which in Eastern Asia resulted in high growth, high rates of savings and investments, and imply high investment in innovation, research and development, as well as the general preference of production over speculation.

2.1.1 THE STATE: BUREAUCRACY AND POLITICS

To start with, let us turn to the state itself. A traditional analysis of the developmental state concept includes the assessment of bureaucracy, as policy initiator, and politics, as policy executor. In the 1960s, 70s and 80s there was much discussion about bureaucracy and authoritarian political regimes. In Japan, bureaucracy and politics were seen as two angles of “iron triangle” (the third angle was, expectedly, business). Today, however, globalization and democratization borne a positive fruit of political activism of different parts of society, foremost the civil society and non-profit organizations.

Precisely out of this reason, the governance today needs competent politicians and competent bureaucracy, but not in the manner as of the 1960s and 1970s. Our age requires a transparent, cooperative and creative bureaucracy, and equivalent politicians. The emergence of non-profit organisations and the civil society are able to force the old “iron” bureaucracy and corrupt politicians to adapt. But how did the East Asian developmental

states manage to be “corrupt” and “iron”, as many reproach them, and on the other hand, so productive and creative?

In order to analyse the East Asian bureaucracy, we need a little theoretic background. Garson (1993: 14-17) analyzes a theoretical view of bureaucracy by three dominant schools concerned with it: neoclassical, Marxist and institutional. According to Garson, neoclassical economies seldom look back to Weber for inspiration. They base their analysis of bureaucracy on the work of Coase.

Some of the work inspired by Coase has recently proven fruitful in the analysis of other forms of organization, including bureaucracy in governments. The core of the neoclassical approach is individual decision making. Literature on this subject assumes maximization by individuals of utility, and by firms of profit. In other words, the approach is a typical *homo oeconomicus* one. The scholars of public choice theory are the most interested in this line of argumentation. Two of them, William Niskanen and Anthony Downs, are the most prominent. Although their approaches are indeed very similar to each other, Dunleavy (1991) argues that Niskanen is to be seen as the representative of the new right and Downs rather of the pluralist theory.

Niskanen's (1974) aim was to show what exactly a typical bureaucrat's behaviour looks like. Bureaucrats aim to enhance their budget maximand due to their rational behaviour. Any bureaucrat aspires to maximize his budget in the form of salaries, offices, power, patronage or output of the bureau. Downs (1967) also assumes that there is individual motivation of each bureaucrat: power, income, prestige, convenience, security, personal loyalty, pride due to proficient performance, but also the desire to serve the public interest or commitment to a specific programme or action (Downs 1967: 84 – 87). What sets apart the Downs' model from the Niskanen's is that Niskanen takes one single objective of bureaucrats (i.e. obtaining his budget maximand), whereas Downs presumes many bureaucrats' goals.

However, it is necessary to distinguish between the function and motives of a bureaucrat. Schumpeter formulates it in the following way: "It does not follow that the social meaning of a type of activity will necessarily provide the motive power..." (Schumpeter 1950:82). Put differently, the motive why someone carries out a function may be unrelated to the function itself. This is, I believe, a very useful statement for any further analysis. In other words, it is not the existence of bureaucracy that is problematic; it is rather certain individuals who render it like that. So before it is dismissed in its totality, it should be seen from a different angle.

The Marxist analysis has as its most fundamental characteristic an emphasis on the role of social classes. In a capitalist society, in addition to any other conflicts that may occur between or within these and other classes, workers and capitalists are in a fundamental conflict. As it is broadly known, this conflict is based on production by some (workers) and their exploitation by others (capitalists). The focus of attention is on who produces, who gets what is produced and how the latter get it away from the former. Garson (1993) asserts that due to the fact that Marxists tried to keep everything in a two-class, labour-versus capitalist framework, this gave them rise to dismiss bureaucracy as a mere tool of capitalist society.

Chattopadhyay (1993: 39-42) follows this argument by stating that in Marxism bureaucracy is conceived as a general form of organization of administrators hierarchically arranged from the top downwards. Chattopadhyay is however more concerned with the relation of bureaucracy and the class. He argues that Marx considers the relation of bureaucracy to class to be rather historical, and not as something fixed independently of social evolution. In Marx's earlier works, bureaucracy was regarded as a class (*Stand*) on its own.

It appears that Marx later reformulated his view and concluded that bureaucracy is not independent. Rather, he contended that the ruling bourgeois class totally subordinated bureaucracy. Moreover, Chattopadhyay reminds that Marx did not see bureaucracy to be directly related to the material conditions of

production. The debate on whether Marx saw bureaucracy as a class or not is still vivid today, because Marx never actually made it clear. However, Marxists still regard bureaucracy with bitterness, not anymore as a mere capitalist tool, but as an inherent structure co-shaping capitalism (see for instance Altvater 1973, Poulantzas 1980, Jessop 1990, 2002).

The third approach did not dismiss bureaucracy as the first two. Garson (1993) considers institutionalist approach to be probably the smallest approach used. In a sense, it is also the one for which an exploration of bureaucracy is most natural, because it stresses the importance of economic institutions and their structure in determining outcomes. DeGregori and Thomas (1993: 54) define the institutional economic theory of technology and institutions as a model that seeks to understand the complex relationships between technologies and the institutional rules that govern human behaviour, including skilled activity.

The fact that many within this group look back to Weber and Veblen has encouraged them to examine bureaucracy as a phenomenon, given Weber's paradigmatic studies of this subject. A major feature of this approach is emphasis on the normative aspect of economics as opposed to the positivist emphasis of the neoclassical school. A major difference between institutionalism and the other approaches is, in Garson's words, that "institutions are perceived as having a life and a logic of their own" (1993: 17).

Having summarized the view of bureaucracy by the neo-classical (liberal), Marxist and institutionalist analyses, it is time to ask to which of these school had it right as far as East Asian development states were concerned. Aoki (1998: 547-549) examines the bureaucracy of Japan, which influenced the bureaucratic organization of other East Asian developmental states, and argues that it may be considered to be pursuing the maximization of its own political stock which is roughly defined as the capacity to extract fiscal resources, recruit able human resources to its own machinery and regulate activities of private

actors to its own advantage. From this point of view, the neo-classical analysis was the closest to reality.

The military-led Japanese bureaucracy failed miserably in setting as a goal the building of an empire, and the externally enforced post-war reform democratized the political context of the bureaucracy (ibid). To sustain its viability, the Japanese bureaucracy formed a coalition with the ruling political parties and big businesses, and reformulated joint “national” goals as the rebuilding of economic power. This was a “bureau-pluralism”. In this game, pluralist interests of various social interest groups are mediated by competing bureaux within the bureaucratic process. In this sense, a pluralist version of institutionalism is the one best explaining the bureaucracy within the developmental state.

Nevertheless, in developmental states, as we will see on the Japanese example later, bureaucracy was often perceived rather negatively due to its autonomous power. Of course, authoritarian bureaucracy may become a source of corruption and vested interests. Of course, bearing in mind that Weber’s bureaucracy is an ideal type, and that many dysfunctions are indeed probable and possible, as examined by Crozier (1964), Marxists do make a point by stating that, if they narrowly cooperate with business for their own purpose, bureaucrats contribute to the maintenance of capitalism as universal economic system.

However, adhocracy as an opposite of bureaucracy would provoke either anarchy, or traditional or charismatic domination, to use Max Weber’s terms. Hence, in Weberian sense, the efficiency and organization of bureaucracy can outweigh its costs. The Japanese example will show that the axiom about bureaucrats wanting to enhance their self-interest (not only in the form of profit, but also of self-esteem, reputation etc.) actually contributed to the economic boom and social wealth, due to the formulation of “national interests,” as stated above.

The Japanese example will show that the neoclassic view of greedy and corrupt officials *without exception* does not necessarily have to prove right. Neither does the Marxist model: the assumption of bureaucracy as an instrument or a tool of the bourgeois and capitalists to exploit the labour did not hold in East Asian developmental state, since the income equality and favourable work conditions were characteristic features of this system. Moreover, the model of self-government in Yugoslavia, as a textbook example of the Marxist socialism, evolved into a huge bureaucracy itself. However, it was for most of the time an inefficient, biased and corrupt bureaucracy, as we shall see in chapter 4.

Therefore, although all the theories briefly reviewed here are right to some extent, the closest to developmental state model *as a whole* is probably the institutional view of bureaucracy, explaining bureaucracy on the social, traditional and cultural level at one hand, and on the technological and corporate level on the other. Again, it should not be forgotten that the world in the 1960s until 1980s was completely different from today: it was living the birth of decolonization in the middle of the Cold War, it was still marked by apartheid and communism, and in Asia, it was the time of a shy opening.

A complex analysis of the Asian mentality and tradition could probably also well explain the importance of particular bureaucracies in East Asia. However, this thesis is interested in another analysis, that of powerful business-state relations after World War II until 1990s since these relations can explain, on the technological level, the necessity and the results of strong bureaucracy networks during that time. Bureaucracy was probably the most efficient in what Johnson called “pilot agencies”, thus institutions with a developmental character in charge of enhancing competitiveness and supporting economic growth.

The best example of a pilot agency is definitely MITI, the functioning of which was thoroughly described in Johnson’s (1982) major work. Wade (1990: 371) analyses pilot agencies of the “economic general staff” as the bureaucratic elite which is selected further from already very carefully selected bureaucrats

by means of extremely competitive examinations, with the aim to employ it in this core section for achieving significant economic growth. Such pilot agencies have a rather small number of staff (MITI having only 200 employees in the 1960s). In Japan, but also in South Korea and Taiwan, the small number of such “pilot agencies” was generally preferred. In the aftermath of the Asian crisis, the question was posed whether the different reaction of different East Asian countries to the crisis was the outcome of their different institutional quality.

A significant number of scholars, such as Park (2006: 40ff) argue though that the quality of institutions prior to the crisis was not so good as it is believed. The technocratic elite of East Asia’s strong states was not always insulated from political pressures and they often succumbed to the pressures of intervention by various interest groups. In South Eastern Asia, government officials forged close ties with private entrepreneurs to pursue their own interests. These ties made them, as expected highly susceptible to corruption.

As an answer, Park (2006: 100) suggests that the institutional reform should be directed to building legal, social, and political institutions for governance indispensable for the working of an effective democratic political regime, i.e. “Western rules and institutions”. However, this type of advice has a significant deficit: East Asia is not the West, and, even more important, it is only relatively recently that it has opened towards that same West.

In both Eastern and South-Eastern Asia, the process of democratization assumed a linear characteristic, with Taiwan being the most exemplary case. Political developments in most of these countries proceeded from being an under-institutionalized autocracy to institutionalized autocracy and to new democracy (Pei 1998). However, the democratization of East Asia did not occur in light of and in harmony with standard socioeconomic values of the West (Friedman, ed. 1994). From a comparative perspective, the transition from weak democracies to authoritarian rule in many countries of East Asia (excluding Japan) in 1960s and 1970s, differed fundamentally, Pei (1998) claims, from the similar trend in Latin American countries.

In Latin America, the emergence of bureaucratic authoritarianism was mainly caused by the exhaustion of the import-substitution industrialization and unsuccessful populist policies there. East Asia, on the contrary, although most its “soft authoritarian” regimes indeed shared many characteristics of bureaucratic authoritarianism, it is important to note that the factors bringing about their ascendance were different. The chief cause was the underdevelopment of critical political institutions (parties, bureaucratic institutions, judiciary), while the economic factors played in this case rather a minor role (Pei 1998: 43).

Interesting is however, as Pei describes, the development of institutionalism within these countries. While in most of these countries (Japan, Hong Kong and Singapore) the authoritarianism was present, it still remains a puzzle how private property remained protected by the rule of law, how the radical parties of the Left hardly gained power (with obvious exceptions of China, Indonesia under Sukarno, Burma-Myanmar and Vietnam). In these countries, the self-destruction of the radical Left was very costly: from the Great Leap Forward and Cultural Revolution in China, Vietnam’s absolute isolation until the 1980s, the bloody elimination of Sukarno’s regime in Indonesia to Burma’s three decades of radical isolation (Pei 1998: 46).

Pei goes on to claim that, on the contrary, in Malaysia, Singapore, Hong Kong, South Korea and Taiwan, but of course the same can be said for Japan, the government ruled by the Right first successfully destroyed the Left as a political force, and then wisely adopted certain equity policies of the Left.

In Malaysia, the communist insurgence was defeated under the British colonial rule; in Singapore, the communist party experienced an internal split and was confronted with the government which destroyed it in a short period; in Thailand there was no nationalist revolution to which the communism could act as a counter-balance, so it never established itself; in South Korea, the Korean War destroyed the Left for obvious reasons of authoritarianism in neighbouring North Korea; finally, in Taiwan the Left was exposed to Kuomintang’s constant

repression so it never actually could expand itself (Pei 1998: 46ff). All these countries had their own path of democratization, both through formal and informal policy-making (on democratization in general see for instance Schaeffer (ed. 2005), on informal politics in East Asia see Dittmer, Fukui and Lee (eds. 2000)).

Finally, as this thesis will argue in chapter 3, Japan's Liberal Democratic Party (LDP), formed in 1955, never really offered a chance to the socialist party to establish itself, the only exception being in 1994/95 when socialist were incumbent (Junnosuke 1992). The way *how* the LDP did it is interesting, mostly because Japan is a democratic country (and has been formally such since 1947, thus it has over 60 years of democracy in store).

Rather, the LDP's self-imposed rules, which deliberately restricted its power, helped it to gain and maintain political trust. Moreover, the LDP seems not to have been so "iron" as many suggest, due to the counter-strength of bureaucrats, whose force again could not prevail because ministries had in many cases rather diverged interests, so the picture of the state as composed of corrupt bureaucrats and unscrupulous politicians should be dismissed in its radical variant. Of course there were *some* politicians with vested interests (Tanaka Kakuei in Japan being the most obvious example), but to claim the state as a totality functioned in this way would be completely untrue and inappropriate.

2.1.2 STATE-LED INDUSTRIAL DEVELOPMENT

Now that we reviewed the structure of the state, we should turn to the state-business relations as presented by the traditional developmental state view. Karagiannis and Madjd-Sadjadi (2007:8) contrast in their recent book the neoliberal and developmental state perspectives concerning eternal debate 'the state vs. the market'. As it is well known, neoliberal analysis draws heavily on

the First and Second Theorems of Welfare Economics. The First Theorem states that competitive markets produce Pareto optimal results, although the results of that competitive market may not be to the liking of individuals: markets may distribute goods in a manner that produces large-scale disparities in wealth. The Second Theorem of Welfare Economics states that it does not matter that competitive markets produce disparities in wealth because these can be corrected by altering the initial endowments that everyone has.

Obviously, such an approach is a very naïve one: if the market creates disparities, it will automatically fix them, so there is absolutely no reason to worry over recessions or even to change economic policies. Looking at this from the 2008 perspective, one cannot help being sceptic: the financial, and then also economic crisis all over the world has lasted for over a year, global bourses are constantly breaking down and unemployment is increasing, accompanied by the sluggish growth; the market did not seem to react automatically. If the argument is: “It eventually will”, then its target group are only those extremely patient.

As we will see on the Japanese and East Asian examples, the state can intervene in the industrial sectors in several ways: it can regulate the industry by laws and legal regulations; it can intervene by means of public enterprises, or it can create development agencies and through these cooperate with industrial clusters and individual companies. Particular cases when state intervention should displace the market are if (Samuels 1987: 426):

- the targeted industry is fragmented vertically or isolated horizontally from other sectors,
- the state is highly centralized either vertically, vis-à-vis local and regional governments, or horizontally, with a consolidated national bureaucracy,
- the economy is undergoing late development or reconstruction, especially when this involves a concentration of financial resource,

- the targeted industry is vulnerable in world markets,
- the ruling is narrow and unstable, or if
- there is an 'administrative tradition' of state intervention.

Apart from this last argument, which is rather debatable (an 'administrative tradition' in the past justifying intervention in the present without any further explanation leads to rather circular arguments), I believe other described situations summarize very well the most important reasons for state interventions. In the matter of fact, the first, second, third and fourth arguments are typical for developmental states in their early phases.

Additionally, the fourth argument represents a typical "infant industry argument", as proposed by a German economist Friedrich List. Many liberal economists contend that determining an infant, i.e. new and vulnerable industry is a political, and not an economic decision. However, I believe this has less to do with politics than with strategic planning: if the government is not only able to determine its comparative advantage, but also to develop it further, then it is an active government. Citizens usually want such a government.

As far as public enterprises are concerned, Karagiannis and Madjd-Sadjadi (2007:10ff) list their advantages in comparison to purely private incentives. Clearly, if we take as an example a country in which capital markets are incomplete or underdeveloped, the domestic private sector may be unable to undertake investments that would be necessary to develop the local industry to a sufficient extent. Karagiannis and Madjd-Sadjadi however do not partisan regulation in all cases. Economically seen, in case of a natural monopoly, the choice is often between regulation and ownership. They argue that in some cases ownership, if properly managed, may be economically preferable to natural monopoly. One could add that models of private-public cooperation, often to be found in developmental states, combine well both regulation and ownership.

Through cross subsidisation, public enterprises can achieve important public policy goals and help to achieve policies that would have otherwise left numerous individuals incapable of bettering their lives. Furthermore, the public enterprise can serve as a “window on the industry,” in words of Karagiannis and Madjd-Sadjadi, allowing an access to information for the government during its policy-setting. Importantly, when there are significant externalities, a public enterprise can respond in a socially desirable manner, as it does not need to be a profit-maximising enterprise. Social goals are then superior to private ones. One could add at this point that in many developmental states, such as Japan, Korea or even China, public-private cooperation was and still is a very important feature of economic development. Thus, these models successfully combine the best of both sides.

Does national planning always have to invoke socialism? Absolutely not, because, in fact, when public investment is a part of national planning, it is possible to take into account all kinds of effects, which would not be possible with only private investments. Without strategic planning, the developmental state actually loses its *raison d'être*. The government can look ahead of the market to draw up long-term parameters of a developmental intervention that does not deny the importance of the market system operating within this overall strategy. What is required is that there should be a fairly comprehensive state investment plan for industrial development, and the state should be capable of giving effect to this plan, through the “administrative guidance” of the privately owned firms. This was the case in Japan, where many firms were domestic and not foreign-owned firms (Karagiannis and Madjd-Sadjadi 2007:12ff).

Finally, public enterprises and generally state-led industrial development can help alleviate coordination failure out of all the reasons mentioned above. Generally, through its capacity to adapt to external shocks and pressures by generating new means of governing industrial change, the state can then design and implement strategic industrial policies. This is done by resource coordination, selective intervention and disciplined support. The outcomes are,

as we have already stated in chapter 1, dynamic internationally competitive industries (compare Weiss 1998: 144).

This leads us to the crucial point, namely to the decision-making within the enterprise. In capitalism, managers' compensation is not necessarily tied to their performance and may even be tied to goals that are contradictory to profit maximisation (for instance, the sales growth). Managers of public enterprises usually are closely monitored by one or at most a handful of individuals and as a result their compensation is not only a matter of public record but also public scrutiny (Karagiannis and Madjd-Sadjadi 2007:13ff). A pure *laissez-faire* can result in a problem referred to by many economists as the principal-agent problem.

One should not forget, still, that not only the standard capitalism suffers from the problems of coordination. In what he dubs his "work of a lifetime" (1982), i.e. in a comprehensive economic and political analysis of the political economy socialism, a Croatian-born Yugoslav economist and the candidate for the Nobel Prize in this discipline, Branko Horvat proposes a socialist economic system, his interpretation of Marx, for which he, as so many others, believed to be the only right one. He offered the view of firstly a state-limited, and then eventually a fully stateless society. Self-management, on which I will come to talk more extensively in the chapter dedicated to the Croatian economy within Yugoslavia, is Horvat's alternative to the state. It is absolutely crucial to understand this in the context of developmental state, because the goal of self-management is actually an argument *in favour* of the state-business relations. In fact, Horvat's analysis was in my view one of the rare quite *concrete* alternatives Marxists proposed to the capitalist state.

Why is Horvat's ideal model of socialism touched on precisely at this point and in the context of the state-led industrial development? The answer lies in the necessity to juxtapose two completely opposed schools, which however have one point in common: the state and industry do not belong together according to both *laissez-faire* and Marxism. In liberal capitalism, public

companies are considered to be redundant, and economic national planning recalls of socialism. The Marxist socialism does not attack planning, but it does make various reproaches against the state, since the state should not be the one being in charge of planning. In socialism, it is society, i.e. the workers, who organize the production, and who should also be responsible of planning.

If we suppose there were no state, but simply workers deciding about themselves and their economic activity, could this imply a perfect coordination in any industry? Horvat (1982: 252ff) himself is aware of many possible difficulties that could arise in the model. Quite banal, but very true, is the fact that among the workers who should organize themselves, they will probably waste much time in discussions instead of working, because the participatory management is characterized by what might be termed “the unanimity syndrome”. In Yugoslavia after the Second World War, this was often present.

Horvat goes on to auto-criticize his theory by stating that in the socialist model the distinction between legislative and administrative work is not clearly perceived, nor is responsibility transparent. Moreover, there is a spontaneous tendency to interfere with the day-to-day- administration of the enterprise. The general manager of an enterprise (which belongs to the workers), as we shall see, is elected in such a system directly by the workers. Thus, it is not really workers who decide in the first place.

The problem which arises is a typical principal-agent one, paradoxically. A passive or incompetent manager can easily avoid any responsibility by letting the workers’ council (one of the most important bodies within the self-governing system) assume all risks. A demagogue will build his position on his apparent willingness to obey always and unconditionally – regardless of the damage caused by inappropriate decisions. Finally, a manipulator will let the workers’ council decide on rivalities or on issues requiring technical competence that the council members do not possess in order to make them rubber-stamp his own decisions. A truly dedicated and potentially efficient manager may be accused of usurping self-management rights (Horvat 1982: 252ff).

Thus, the substitution of the state by the society of workers who at the same time constitute the industry *and* the body which supervises this same industry, could indeed have negative consequences. Moreover, the Federation, which is by Horvat seen as a supreme body (as he thought in terms of Yugoslavia and its republics), is conceived as an extensive bureaucracy, although Horvat refuses to believe this, as we shall see in chapter 4. Development state, on the contrary, proposes the state to cooperate with the industry. In the pioneer developmental state works, such as those by Chalmers Johnson or Robert Wade, the state was still seen as an authoritarian coordinator. However, today's challenges envisage something beyond this rather superficial statement. In communist states such as the former Soviet Union, the etatism was strong and economy politicized.

On the contrary, from its very beginning, the concept of developmental state proposes the state entitled to make economic and welfare-enhancing, and not regime-oriented or party-related decisions. In Horvat's vision, the self-governing principle is in fact a root of bureaucratic organization which *a priori* supervises the self-government (which, then, ceases to be a real self-government). Put differently, if a self-governing organization is seen as a source of development but if it is incorporated into a comprehensive bureaucracy which makes sure that self-government works, then bureaucracy is, again, seen as a source of growth itself. In developmental state, politics and bureaucracy are seen rather as a tool, and not as a source, of economic development. In my view, this is what distinguishes the developmental state from both capitalism and socialism.

Okazaki (2006) shows on the Japanese example how it firstly came to the cooperation between the government and the private sector. I will return to the Japanese industrialization in the chapter foreseen for it, but here the scope is merely to emphasize the circumstances which led to the state-led industrialization. Analogically to Japan, in South Korea or Taiwan the process was rather similar.

Following Okazaki (2006), we could assert that in the first half of the 1950s, the Japanese economy resumed capital accumulation and re-established the heavy industry base. When the Japanese economy was in transition to a market economy following the Dodge (American) plan of 1949, heavy industries were faced with the problems of high cost and small scale. This in turn impeded investment for rationalization, and the Japanese economy became mired in a vicious circle. Complementarity among industries, economies of scale and incomplete information brought about this failure in coordination. Then, the state had to make a move.

Coordination by the government played an important role. The Council for Industrial Rationalization was a body through which cooperation between government and private enterprises could create a path to escape the vicious cycle. The path was formulated and developed into the plans for simultaneous investment in related industries. Briefly, this was a coordinated experiment by the government and private enterprises. There were also many technical officials in MITI (Ministry of International Trade and Industry) as a legacy of the war economy and therefore MITI itself had the ability to evaluate the technology and technological capacity of the enterprises. Third, in policy implementation, the government made use of the ability of the financial institutions (ibid: 132).

The Japanese business cartels *zaibatsu* (later *keiretsu*) or the Korean *chaebols* represent the prototype of industrial organization within the early developmental state. Chalmers Johnson (1982: 114) writes that in the 1920s, the MITI leaders of industrial policy were led to attempt an approach of direct state control of the economy, that carried them to disaster. "The bitterness of the era of the Yoshino-Kishi line was more than enough to warn those who managed both the state and private enterprises after the war that catastrophes could occur if they did not transcend both self-control and state control in favour of genuine public- private cooperation," Johnson (1982: 114) concludes.

Today, the role of the government is rather a cooperative one. In Japan, the reformed MITI, since 2002 METI (Ministry of Economy, Trade and Industry),

also tries to describe its new approach to industrial policy as one in which the government tries to facilitate positive spirals, i.e. interactions between supply and demand at the micro- and macroeconomic levels (Vogel 2006: 88).

Cooperation and positive incentives of the state for business are not equal to the politically or ideologically based support of economic elites provided by the state. If the state limits itself to the second variant, as many non-East Asian examples demonstrate, for instance Yugoslavia, or many Latin American countries. Pínglé (1999: 175ff) describes the case of Venezuela in the 1960s by arguing that the state was not autonomous from the dominant economic interests. It became more focused on responding to the pressures, needs, and requests of influential groups and individuals, than on managing economic development.

This decreased its capacity to implement policies and make decisions aimed at serving the population as a whole. Pínglé (1999) therefore contends that strong and unified industry associations, or the presence of non-contractual relations between the state and the conglomerated and other industry actors, might have indeed prevented this. They were, however, missing. A similar case was to find in India, a failed developmental state. The industry associations in India were concerned primarily with bargaining with the state for benefits and privileges. The absence of the developmental ensemble explains to a substantial extent that nation's recent performance. Yugoslavia was not very different from this situation, as we shall see in chapter 4.

The developmental state is, as already argued, not a static concept. In today's globalized world, a moderate regionalization of industrial production might well be needed. Dieter Ernst (2004: 34) argues in his survey on the Japanese production networks in the electronics industry that industrial (electronics) sector of Japan now "critically depends on the region, not only as a global export production base but also as a major and increasingly sophisticated market for its products, services, and technology".

Developmental states are all characterized by high saving, high investment and high growth. Karagiannis and Madjd-Sadjadi (2007: 240ff) also argue that without continuous investment, economies not only have their potential for growth curtailed. Besides that, improvements and increases in infrastructure, capital equipment and research & development do not occur overnight. Not only regional restructuring, but also local economic restructuring is needed (decentralization). Instead of placing emphasis on consumption spending and transfer payments only, the state should also consider government investments as very important (ibid: 242).

Clearly, one final goal for every modern developmental state to enhance its industrial sector is its investment into education. Only in this manner will the development of a new local economy based on high-technology industrial sectors, the modernization of existing mature industries and firms through the application of new production technologies and new product development, be possible. Therefore, the government has to invest in the upgrading of skills and technical qualifications of the labour force through various workplace-experience programmes, reskilling, education and training. Hence, not only the improvements and/or extensions of physical infrastructure and business infrastructure, but also of social infrastructure are of course needed (ibid: 251).

In theory, the developmental state should adapt, but never renounce its industrial growth model. In praxis however, East Asian countries succumbed the overall global trend of liberalization and the Washington Consensus in the 1990s. To their misfortune, some of the East Asian countries were successful in partially applying the neoliberal model into their economies. This is what, in view of some scholars, brought about the Asian economic and financial crisis of 1997/98. Other (above all neo-liberal authors, but also several Marxists, see e.g. Burkett and Hart-Landsberg (2000)) argue that the developmental state itself was the root of its own destruction. In that sense, the Japanese case is to be analyzed in detail in the next chapter.

Van Hoa (2002: 12) analyses the Asian economic and financial crisis of 1997/98 in general and maintains that the governments of East Asian countries did not have an appropriate and effective management plan to deal with economic and financial crises. Moreover, the external help from international institutions was completely misconceived. As for all countries except Japan, the international organisations such as the IMF, the World Bank and the Asian Developmental Bank assisted them in crisis management. Van Hoa maintains that the cures and remedies proposed or imposed by these international organisations on Asian crisis economies seem to have been inappropriate and ineffective.

For Japan, which had both maintained its old neo-Keynesian (budget deficits) and adopted in some areas orthodox monetary policies (e.g. zero interest rates), Van Hoa also believes that its economic and financial crisis management had not been appropriate. Hellman, Murdock and Stiglitz (1998) show in their financial restraint theory that the financial deregulations introduced in the early 1980s eliminated the incentives that ensured prudent monitoring. In other words, the neo-liberal reforms of the 1980s are seen by these theorists as one of the principal causes of the crisis.

After the Asian crisis, both liberal and developmental state theorists stepped into the breach for their arguments. Obviously, liberal authors were triumphing over the fall of East Asian giants. Developmental state was proclaimed dead, not only by neoliberals but also by declared socialists. On the contrary, developmental state theorists, such as Chang and Grabel (2005), Onis and Senses (2005), or Fine (2006), maintained that it were precisely neoliberal reforms that overshadowed the brilliant path of developmental states. They certainly needed some inner restructuring, but not in a way proposed by the West. Hence, some reforms were proposed.

Ben Fine in 1999 drafted a paper asking whether *Developmental State is Dead –Long Live Social Capital?*, which led him to the publication of the book questioning the importance of social capital in international political economy

(*Social Capital versus Social Theory: Political Economy and Social Science at the Turn of the Millennium*, 2001). The last concept of social capital, which will be discussed in section 2.1.3, originally aimed the conflict state-market with the mix of New Keynesianism and social relations as the engine of growth. Fine is sceptic against this notion, arguing that the concept is so vague that it has been overused and misused (in particular by the World Bank). Social capital within agents however can co-exist with the state, which this thesis will try to demonstrate.

2.1.3 THEORY OF SOCIAL CAPITAL

After the Asian crisis, the development state theory encountered numerous critics and it was often discredited for its strong state which, in the eyes of many scholars, was not able to manage financial and economic crises. In response, apart from diverse attempts to complement the existing theory, such as by introducing the developmental state as such (Johnson 1982, 1986), governed market theory (Wade 1990), the embedded autonomy of the state (Evans 1995), or governed independence (Weiss 1998), there was also an independent theory which evolved at the beginning of 1990s. It was the theory of social capital, and many developmental state scholars have still been working on creating a nexus between the developmental state and the notion of social capital.

By evoking the theory of social capital, anyone at least superficially aware of its propositions will instantly think of the Harvard professor Robert Putnam. He investigated the notion (without really introducing the term, which had been present for a while) and then concluded, bringing a later very often quoted definition: “Social capital (...) refers to social connections and the attendant norms and trust” (Putnam 1993: 665).

The application of social capital in the context of public policy had been shown in the classic example by James Coleman (1988). Coleman describes the New York wholesale diamond market. In this market, merchants trust each other so much that they hand over bags full with diamonds to other merchants

without any thought of trumpery or fraud. This is why transactions such as this one are conducted without insurance or formal agreement. Any outsider is perplexed by this trust, but the point is right there: there is a strong cohesion between the insiders of the group.

As a pioneer work on social capital, Robert Putnam did research (1993) on Italian North and South which led him to the conclusion about the utmost importance of reciprocity, social trust and civic association for economic development. Theoretical foundation of Putnam's findings can clearly be found in the works of many important social scientists. Alexis de Tocqueville for instance wrote in his *Democracy in America*: „Nothing in my view more deserves attention than the intellectual and moral associations in America. American political and industrial associations easily catch our eyes, but the others tend not to be noticed“ (1969: 517).

In the similar vein, a French sociologist Émile Durkheim showed that the suicide was far more common in societies and groups characterized by social dislocation and loose social bonds. Another French sociologist Pierre Bourdieu also argued that economic orthodoxy was artificially limiting itself to the study of a narrow band of practices that were socially recognized as “economic“ and in so doing, they overlooked the fact that capital was in fact economic, cultural and social.

Francis Fukuyama was another important figure in the context of social capital. He emphasized that economists had underestimated the importance of social capital in general and trust in particular. For him, social capital denotes a cluster of specific characteristics of social life, norms and customs, which support cooperation and solidarity (Fukuyama 2000). Social capital is often defined as a characteristic of social structure, being characterized by two main features.

It is thought as civic participation or density of relationships among the members of community (its first feature), which is characterized by widespread mutual trust, collective actions and respect for mutually shared norms (its

second feature). This theory can be useful in analyzing power distribution within society, and this is why some prefer to see in it the community governance (Bowles and Gintis 2002). By means of two variables, i.e. social trust and civic participation, Štulhofer (2004), similar to many other country analyses, demonstrates the position of social capital within the Croatian society.

One of the basic reasons for the popularity of this theory in social sciences is its positive impact on economic development in its view of society, and not the state, as social capital has become a synonym for positive influence of informal norms and institutions on growth and development. Social capital has been interpreted as a resource which makes communities economically more prosperous, socially more stable, more creative, healthier, safer as well as more content (Štulhofer 2004). In recent years, the importance of social capital has been empirically confirmed in the transitional context as well, both in terms of social capital with economic growth (Glaeser et al. 2002, Dasgupta 2002), and pointing out the deficit of civility and civic participation in the post-socialist societies (e.g. Rose et al. 1997).

However, the model of social capital has also been subject to a series of criticisms (above all Fine 1999 and 2001, Grix 2001). These critics reproach it an excessive scope, ahistoricism and decontextualisation, as well as conceptual vagueness. Rubio (1997) analyzes the criminal milieu of Colombia and demonstrates that it is also organized in forms of well-established networks. Therefore a question can be asked whether there is a line between a *positive* and a *negative* sort of social capital.

Many scholars observe as well that the theory of social capital completely ignores the role of the state (Foley and Edwards 1999, Maloney et al. 2000, Hospers and Van Lochem 2002; Mihaylova 2005). Fine (1999: 12) adds that the main reason why the World Bank was so eager to deploy the concept of social capital is that the theory allows the Bank to “broaden its agenda while retaining continuity with most of its practices and prejudices which include the benign neglect of macro-relations of power, preference for favoured NGOs and grassroots movements, and decentralized initiatives.”

On the other hand, Grix (2001) points out methodological problems related to the measurement of fundamental dimensions. He questions the empirical validity of generalized trust, the problematic aggregation of civic organizations and similarly problematic generalizations used for measuring trust in institutions. In other words, what is measured by trust? Given the complexity of institutions, how should we measure an aggregate trust in them? Which institutions shape their social relations more than others? Such questions have challenged the theory of social capital, although many (such as Halpern 2005) still hold that the basic principle of the theory could be useful for further research in many social disciplines. I will return to this suggestion in chapter 6.

2.2 THE POST-DEVELOPMENTAL STATE

As we have seen, the concept of developmental state dates back as early as to the 17th-century Netherlands. However, developmental state established itself in the modern sense of the word in East Asia after the World War II among the late industrializers. The scholar who is the father of the concept is Chalmers Johnson who, much later (in 1982) dubbed this type of state organization 'the developmental state'. Since then, the debate has been constant, expanding itself to the general ideological controversies of the state and the market.

After the Asian crisis of 1997 and 1998, many neo-liberal (thus, not all liberal, but mostly monetarist) economists exulted since their theory of market deregulation seemed to win over the developmental state theory. Yet in 2008, many hold that the state should be *brought back in* again (recalling the Evans, Rueschemeyer and Skocpol 1985 book title), due to the unprecedented financial and economic crisis brought about by deregulation, the only crisis nearly matching its proportion being the 1929 economic crisis. On the other hand, most Marxists dismiss both neo-liberal and developmental state views, by arguing that not the model variant, but instead the whole model, should be changed.

In the following pages my scope is to sum up the most important arguments of either side: on the one hand, the arguments of the developmental state scholars, and on the other hand, arguments who point out the reasons why the (developmental) state is generally not a solution. By doing so, I will try to show how the concept of the developmental state evolved into a debate on the post-developmental state. But has the post-developmental state been sufficiently modernized, in the sense that it can match the needs of today's globalized society? Section 2.2 will try to provide an answer.

2.2.1. THE NEOLIBERAL WASHINGTON CONSENSUS

The best argument for the existence of developmental states is certainly the fact that market can fail (and therefore also the theories of market asymmetries, incomplete information and uncertainty). Market failures often cause crises and recessions, such as the subprime mortgage crisis of 2007 and global recession of 2008. Its causes and consequences will be debated for a long time, although everyone is aware why it in fact started. The US subprime mortgage crisis evolved into a global financial crisis, which then led to general recession. This crisis is acute and nobody knows how long it is going to last. To judge it critically, apart from saying that the *laissez-faire* of financial markets and irresponsible financial policies in general were responsible for it, would be impossible at the moment, because the crisis is far from over.

The Asian crisis (1997/98) was its precedent in terms of impact. However, as far the causes of this crisis are concerned, economists are not so unanimous about them. Everyone knows it was because of a financial bubble, but why was the bubble created in the first place? Hellman, Murdock and Stiglitz (1998) argue that the guilty in charge was deregulation of financial market, thus *laissez-faire*, introduced in the states which had been clearly developmental up to that moment. On the contrary, Hanazaki and Horiuchi (2004) for instance, argue the reason lies in *too little* deregulation. But, financial crises are only an introduction, as they often evolve into broader and more general type, into

economic crises which do not only affect financial markets, but also the real economy. The 2008 crisis is a clear example.

There is an economic crisis which affected both financial markets and the real economy and almost everyone is unanimous about its causes. It is the Latin American crisis which took place in the 1990s and at the beginning of the new millennium, hence after the emergence of the Washington consensus. This was the crisis for which the 'sketch', to express myself in a bit exaggerated way, was laid down in advance. It is probably every economic analyst's dream to have a clear case like that: after the crisis' outbreak, everyone is able to point into one single direction, because it is known who and what policies are to blame. On the contrary, for Latin American countries and Argentina in particular, the impact of the Washington Consensus was far from dream.

In 1989, the economist from the Institute for International Economics, John Williamson, first coined the term Washington Consensus for a package of solutions, a written SOS plan addressing the biggest problem of Latin America, its massive indebtedness. The Washington Consensus policies were designed to respond to very grave problems of Latin America, and at the time of their emergence made considerable sense for many Latin American countries. In the 1980s the governments of those countries had often run huge deficits. Losses in inefficient government enterprises contributed to those deficits. Loose monetary policy led to inflation running out of control (Stiglitz 2002: 53).

Hence, in 1990 in Washington, a conference was held and indebted countries of Latin America accepted the invitation, following the recommendation of the written version of the Consensus. The "Ten Commandments" were: (1) fiscal policy discipline; (2) redirection of public spending (3) tax reform, (4) liberalization of financial markets and market-determined interest rates, (5) competitive exchange rates, (6) trade liberalization, (7) liberalization of foreign direct investment (8) privatization of state enterprises, (9) deregulation and (10) protection of property rights (Naim 2000: 527).

However, this was not as easy as it sounds. Joseph Stiglitz (1998:1) argued at the time of full implementation of the Consensus that the ten recommendations simply could not save Latin America: „[T]he policies advanced by the Washington consensus are hardly complete and sometimes misguided. Making markets work requires more than just low inflation, it requires sound financial regulation, competition policy, and policies to facilitate the transfer of technology, to name some fundamental issues neglected by the Washington consensus.”

Naim (2000: 509-511) argues that a “consensus” had actually never existed among the economists, because some were constantly attacking Williamson and neo-liberal policies in general, while the other claimed the Consensus to be the right cure for every kind of problem. Ten recommendations were grouped in “easy” and “difficult” ones to implement. Surprisingly, those in favour of a single currency, dismantling the obstacles for FDI or financial markets liberalisation were considered to be the easy ones. No attention was paid to institutions, which were absolutely unready for the liberalization boom (Naim 2000 : 513).

An aspect of which the sight was also completely lost was the economic backwardness and underdevelopment. It was simply assumed, although never confessed, that all the countries share the same extent of development. The Washington Consensus implicitly assumed the overall international economic stability and the ability of countries subject to reforms to implement these promptly. Moreover, the Consensus did not consider institutions as important for change, emphasizing only the necessity for savings.

It did not pay attention to social inequality in the countries which were to follow its recommendations. Furthermore, it seems the Consensus did not notice how weak the public sector of the Latin American countries really was. Finally, and probably the most important feature simply ignored by the Washington Consensus was a different ideology within many post-socialist

developing countries, absolutely not ready to be substituted by neoliberal ideas (Naim 2000: 523 – 526).

Numerous authors, Gore (2000), Chang and Grabel (2004) or Santiso (2004) investigate the same problem: why have the reforms of the Consensus failed in so many countries? Chang and Grabel (2004), the prominent post-Keynesianists, criticize the entire neoliberal background of the Consensus. They also quote in their paper several myths which appeared after the failure of the Consensus and which aimed to justify its collapse. Policies such as the free market under any circumstance and by all means, the pullback of the state and the general belief that the Anglo-American economic model is applicable everywhere are examples of such myths (Chang and Grabel 2004: 276-279). An unconditional and quick financial market liberalization and the absolutely free trade for Chang and Grabel also stay out of question. Moreover, a sudden shift to ahistoric perspectives without any consideration of social and cultural structure of every country is regarded as a further mistake of the Consensus (Gore 2000: 796).

Santiso (2004) analyses an interesting question: whether the Washington Consensus was really inadequate and incomplete for the very beginning, or if it was rather the failure of those who were supposed to follow its instructions, but were not capable of doing it. Santiso summarizes therefore three different perspectives: the one by Kuczynski and Williamson (both from the Institute for International Economics, which was in the sense the *alma mater* of the Consensus), another by Fine, Lapavistas and Pincus, and the third one represented by the IMF-economist Anne Krueger.

The first perspective analysed is one by Fine et al., who all argue that the Washington Consensus was doomed to failure from its very beginning. An aggressive neoliberal approach was too narrow for the countries that were supposed to follow it. Not only do they support the argumentation of the type Chang and Grabel, but they also add some more similar to those of Stiglitz, i.e. about the information asymmetry and incomplete markets (Santiso 2004: 834).

Opposed to this is the perspective of Anne Krueger. Krueger and her like-minded colleagues content that the Consensus was not at all falsely formulated. However, due to the lack of capability of those who were supposed to implement it, it had to fail. This is an optimist camp: in their view, as soon as there are more capable actors, there will also exist the “right” Washington Consensus (Santiso 2004: 835 -837).

The last string of literature includes J. Williamson, the drafter of the Consensus himself. His opinion is that the first version of the Consensus was really very imprecise and thus doomed to failure. Santiso seems to be sceptical about such a moderate view of Williamson (Santiso 2004: 838). In an often quoted chapter of a book he co-edited, Williamson (2003: 323-331) tries to explain the failure of the Washington Consensus by adding some *mea culpa*. He argues that the first document concerning the Latin American debt crisis, *Toward Renewed Economic Growth in Latin America* by Balassa et al. (1986) initially had a very frosty reception in Latin America. This was because it called for upheaval in the region’s traditional approach to economic policy. But opinion started to change quite quickly, and by the time of the Brady Plan in 1989, a number of countries were implementing the sort of reforms that the above work had advocated. This is why they also accepted the Washington Consensus.

Furthermore, Williamson (2003: 328ff) then offers his three explanations why the Consensus failed. The first reason is the series of crises that emerging markets have suffered, starting with that in Mexico at the end of 1994. The other reason is that the reform was incomplete, similar to Krueger’s explanation quoted above. The problem lay not in too much, but in too little implementation of the reform. Finally, the third reason was that the objective of the Consensus was excessively narrow: it consisted in accelerating growth without worsening income distribution. It therefore overlooked many other important aspects of the reform. The results were catastrophic.

Barkin (2001: 185) sums up these results: “Neo-liberalism is exacerbating the polarization of society in all of its dimensions. Structural

adjustments, with their programme for international economic integration and public-sector austerity on the domestic front have radically reduced the possibilities for equitable growth and the satisfaction of social needs. For most Latin Americans, this neoliberal opening is a nightmare. Falling real income, increasing unemployment and the accelerated withdrawal of social safety nets leave us with few alternatives.”

At the time when Barkin was drafting his paper, Argentina was experiencing exactly what had been predicted in that paper: a nightmare. Following section will select the most important causes and consequences of the Argentine crisis, aiming to show why the neo-liberalism was not well-suited for this country and why the developmental state would have been a much better choice.

2.2.2 A FAILURE OF THE CONSENSUS: ARGENTINA

Argentina is a country of mysteries. Its economic misfortune is still a great riddle. Della Paolera and Gallo (2003), for instance, contend that although the country was, and is, a country with outstanding economic potential, during its *Belle Époque* (roughly 1820 -1929), it somehow missed the opportunity to design the right institutions that would secure sustainable growth and insulate the society from the voracity of politicians and rent seekers. It was based on prosperity of incomes, not of institutions. In 1800, it reached the income level of the United States and Europe, and in 1987 its income amounted to only 43% of income of the OECD countries (Della Paolera and Gallo 2003: 5).

Argentina was faithful to its import substitution policy until the 1970s. This policy proved to be right at its very beginning, but eventually it contributed to the Latin American debt crisis and the 10-year stagnation of the entire continent in the 1980s, the period which is known in the literature under the name “lost decade”. Debt crisis provoked a massive inflation. The problem was not so much in import substitution, had it been combined with export strategies and

powerful institutions, which are the characteristics of developmental state. Argentina, on the contrary, was subject to numerous unrests, massive unemployment and increasing poverty and inequality.

The Washington Consensus seemed to be the right cure: it promised an anti-inflation policy at the one hand, and it also guaranteed protection against incapable politicians and the state on the other (Stiglitz 2006: 59). This is why Argentina saw its salvation in it. Privatization and liberalization were seen as the right path, chosen in 1989 (Menin and Cerda 2006: 2). The Argentine peso was pegged to the US-dollar. Argentine President Menem was constantly praised by the IMF and put forward as a prime example and the role model for all other countries. Argentina was unfortunately so successful in implementing the reforms that the IMF soon ranked it among the best practices. It also obtained an overall score of A+ by the IMF. Only a couple of years after, in 2001, the whole Argentine economy crashed (Stiglitz 2004: 7).

The IMF saw the reasons for the crash in Argentina's inner economic problems. Mussa (2002: 9) describes the situation in the following way: "If Argentina had a more flexible economic system, especially in its labour markets, its economy would have been more able to adapt to the rigors of the Convertibility Plan, unemployment would have been lower, fiscal deficits smaller, and interest rates would have been lower because creditors would have more confidence in the capacity of the Argentine government to service its obligations. Moreover, if the dollar had not been so strong in recent years, Argentina would have had a more competitive exchange rate vis-à-vis its important European trading partners."

Blustein (2006: 4ff) emphasizes however the other side of the argument, similar to those of Stiglitz or Santiso, namely that Argentina really prided itself on following free-market, economically orthodox policies during the 1990s. The Argentine government vigorously pursued the Consensus and as a result, the Heritage Foundation, a conservative think tank that evaluates countries according to an 'Index of Economic Freedom' rated Argentina in 1999 as tied

with Chile for the best policies in Latin America, and almost equal to Australia and Taiwan.

Blustein therefore concludes that two sets of actors were in fact responsible for the Argentine crisis: the IMF and the US government, the Fund's dominant overseer. Both of them ignored the crucial factor, the modern system of globalized financial capital. "This engine is remarkably powerful but volatile," concludes Blustein (2006: 5). It indeed is, as the current global financial crisis (2008) confirms.

Williamson (2003: 327) is not convinced, even after the bankruptcy of the Argentine economy. He decisively defends the Consensus: "In acknowledging disappointment in the outcomes, let me emphasize that I am not agreeing that the Washington Consensus was responsible for the tragedy in Argentina. Argentina undertook many good reforms, but it also made two fatal errors: it nailed its mast to a currency board that resulted in its exchange rate becoming grossly uncompetitive, and it failed to follow the strict fiscal policies that would have been needed to give the currency board a chance to work. Both run directly counter to the policies recommended in what I meant by the Washington Consensus, so it is unambiguously wrong to blame the latter for Argentina's tragedy."

However, this can be challenged without too much effort. Fanelli and Frenkel (1999) published their paper on the Argentine economy at the time *before* the collapse of 2001. As early as in 1999, they warned that the Consensus could have many negative repercussions. They describe the Consensus: "In the Argentine case the application of Washington Consensus recommendations was almost a laboratory experiment. It was *rapid, integral* and *structural* in the true sense of the word: it embraced almost all markets and radically dismantled the institutions of 'statism' and 'protectionism'" (Fanelli and Frenkel 1999: 79, italics added). The biggest gap between the expected and the observed results of the Consensus was the one associated with the evolution of unemployment. Argentina was hit by a real typhoon of market fundamentalism.

Although the country has stabilized its economy in the meanwhile, although the new President Cristina Fernandez de Kirchner is ex-President Nestor Kirchner's wife and shares overwhelmingly his economic policies (which are neo-Keynesian), the new economic crisis is threatening the fragile economy again.

2.2.3 FROM THE POST-CONSENSUS TO THE NEW ECONOMIC CRISIS

With Argentine bankruptcy, the Washington Consensus had to retire. What is then its heritage? Are we living in an era of the Post-Washington Consensus (dubbed so by Joseph Stiglitz)? Until 2008, perhaps we did. However, the 2008 crisis changed the world, again. And, ironically, on 15 November 2008, the G-20 world leaders met, again in Washington, to save the world. This time, however, the creation of a new Breton Woods was discussed, thus a policy diametrically opposite to the Washington Consensus of 1990. So is there a paradigm shift?

Gore (2002) offers an interesting analysis. His idea is precisely to demonstrate such a "paradigm shift" in the concepts of economic development after 1990. He proposes two categories of frameworks: the normative and the explanatory one. Moreover, he suggests that both of these frameworks be regarded on two levels: on the national and the global level. Hence his grill offers a theory of four different combinations in total (Gore 2000: 792).

The Washington Consensus and the Liberal International Economic Order (LIEO) are to be placed in the field described by "global normative framework, national explanatory framework". This implies that the scope of the Washington Consensus was to be *implemented globally*, and that in order to do so, it had the precondition to be *explained on the national level*. In Asian developmental states and the Latin American neo-structuralism (a critique of neo-liberalism) the model is completely reverse: the model should be *implemented on the national level* only if it can prior to that be *explained on the*

global level (Gore 200: 798). Therefore, the shift is obvious from global to national as far as the implementation of the model is concerned. Nevertheless, I believe that the Asian developmental model had never had an ambition to be explained on the global level, which I will try to elaborate in the final chapter, chapter 6 of this thesis.

Yet what was, if there was ever such thing as the Post-Washington Consensus, its difference in relation to the original? Önis and Senses (2005: 276) think that the Post-Washington Consensus more emphasized the role of institutions and of a transparent state than its predecessor. However, their critique is oriented towards the total neglect of globalization in the Post-Washington Consensus (Önis and Senses 2005: 279). In their opinion, it again ignored an inner structure of countries and potential conflicts (Önis and Senses 2005: 286).

The Post-Washington Consensus did not offer a clear alternative to the previous Consensus, because it only criticized it without proposing anything new (Fine 2001: 5). It is also in no way pro-interventionist – it simply had no courage for that and was looking for some middle ground (Fine 2001: 13). Thus, no real alternative was proposed by it.

Then came year 2007, and along with it also the American subprime mortgage crisis. The Bush administration did not succeed in managing the United States house prices bubble. Subprime mortgages, i.e. loans to not really trustworthy clients who were not able to offer down payments, exploded in 2005-2007. The bubble burst in 2007, and expectedly, this crisis first expanded to industrialized nations and American partners. Bourses started crushing. After that, 2008 brought economic recession in almost all industrialized nations, including Japan. The result is still unclear, since the 'new Bretton Woods' has not been achieved, and many countries still do not have a slightest inkling how to combat the crisis. They agreed on more financial regulation in Washington in November 2008, but the concrete measures are still vague. The new president

of the United States, Barack Obama, brought a new hope. However, the world is very well aware that one person is not able to change the global economy.

2.2.4 ARGUMENTS CALLING FOR A NEW REVISION OF THE CONCEPT OF DEVELOPMENTAL STATE

Even if Obama certainly will not be able to reverse the global system, Asian countries have meanwhile regained self-confidence. Their old model could last in the current era, they now think. But they have to adapt, and, as we have seen in section 2.1, one of the traits of developmental state is ability to learn and to quickly adapt to new situations. In this section, I will review two sets of criticisms against the traditional statist view of developmental state scholars: the first one is the rigidity of the state- business connections, and the second set of arguments points to the lack of non-state actors in the model, and the negligence of such as environmental policy.

Moreover, in this same section I will emphasize the innovations of the post-developmental state (which emerged in the 1980s and 1990s) which brought more democratization and transparency, but which also embraced neo-liberal reforms in some sectors, notably the labour policy, provoking massive discontent. In effect, neither the traditional developmental state nor the post-developmental states are ideal models. The chapter will be concluded with a summary of both types, offering a basis for further discussion.

A. 'IRON TRIANGLES'

As already discussed in the chapter on state intervention, neither neo-liberals nor Marxian economists and state theorists regard the role of the state in economic activities with approval. However, both schools quote completely different reasons when supporting their attitude. If we reduce the state

apparatus to bureaucracy, which is of course false but at this point very helpful, the concept of developmental state can be criticized from both sides.

Liberals like Mises and Hayek, or monetarists such as Friedman, always insisted on free markets. Finally, libertarians like Nozick and Rothbard emphasize individual liberty issues and decisively demand for a minimal or practically non-existent state. One of the explanations of the New Political Economy, a neoclassical discipline trying to link governance and economy, is the existence of rent seeking. As we have seen earlier, writers such as Downs or Niskanen claim that bureaucrats are self-interested agents who only want to maximize their own profit.

Krueger (1974) invented therefore the notion of rent-seeking, denoting the rent for which businesses compete. The same concept can be applied to bureaucrats and politicians. Their rent (reputation, social connections, or even bribes) demands a fierce competition. During such a competition, they will forget about the national interest or social goals and put themselves in the centre.

Buchanan (1980: 52) suggests the neoclassical concept as the universal cure against rent-seeking: "So long as governmental action is restricted largely, if not entirely, to protecting individual rights, personal and property, and enforcing voluntarily negotiated private contracts, the market process dominates economic behaviour and ensures that any economic rents that appear will be dissipated by the forces of competitive entry." In other words, the minimal state will not be tempted to waste its resources on corrupt bureaucrats and politicians.

As already stated, the Marxists regard the state and its bureaucrats as an ideal collective capitalist (Altvater 1973). The state is assumed to form basic preconditions for capitalism and therefore it is also never class-neutral. Jessop (1990) believes that the state and state power must assume a certain role in capital accumulation, which then results in "complex, contradictory effect of

class struggles” (Jessop 1990: 100). Therefore, the Marxists see the state apparatus as a source of conflicts due to different interests and therefore these state apparatuses and their economic intervention can never be neutral. This also implies that state intervention has inherent limitations and is always subject to inevitable influence of various class and popular-democratic struggles. Its extent will vary depending on political forces (Jessop 1990: 101).

In the similar vein, a Croatian Marxist who did not neglect the market, but indeed shared the above views, Branko Horvat (1982: 198-200) enumerates inefficiencies of a strong state organization. Thus, on the theoretical level, a serious shortcoming of bureaucrats and politicians within developmental state are their status and privileges to which the rest of the society does not have access. This then creates social stratification and the elites that will tend to do anything in their power not to have to abandon their position. An infamous ‘iron triangle’ in Japan is a good example. Such structures regularly last very long and are resistant to any kind of reform. Analogically, politically conform bureaucrats often engage in vested interests and corruption.

Moon and Prasad (1998: 11-15) analyze developmental states of East Asia in practice and come to the conclusion that the concept lacks many elements. First, the conceptualization of the state itself appears overly simplistic. The model fails to uncover the complex and dynamic internal workings of the state structure by depicting the state an internally cohesive, unitary actor. There were some responses to this fallacy, i.e. the work of Peter Evans, Robert Wade or Linda Weiss, where all of them tried to depict the dynamics within the state. I believe that the work of Linda Weiss is the most comprehensive one, however it leaves many questions behind. The most important one is: how should the bureaucracy really work in the modern developmental state? Idem: what is the role of politics within such a state organization?

However, as Moon and Prasad (1998: 11) emphasize, the general developmental state model also commits the fallacy of reductionism by equating the state with bureaucrats. As they rightfully add, state structure is not a

coherent and unitary entity, but is composed of several distinguishable dimensions: executive leadership, executive-bureaucratic nexus, intra-bureaucratic dynamics and bureaucratic constituents. The cohesion, unity and dominance of state structure depend on the combination of these dimensions.

As far as executive leadership and the prominent Chalmers Johnson's statement that in Japan "politicians reign and bureaucrats rule," Moon and Prasad believe it is unrealistic to assume that political leaders including the chief executive simply reign by creating space for bureaucratic manoeuvres. They not only reign, but also rule. Hence reducing politicians to puppets of bureaucrats and businesses is unrealistic. Politicians' ruling or reigning depends on their leadership style, political calculation and institutional constraints.

Moon and Prasad then make a remark that in Korea, General Park Chung Hee subjugated bureaucrats under his grip and dictated virtually every policy detail, while Chun Do Hwan delegated power to bureaucrats. In Japan, on the other hand, strong prime ministers such as Yoshida, Sato and Tanaka practiced both reigning and ruling but weak prime ministers (Hatoyama, Kishi, Miki), delegated the ruling function largely to bureaucrats. In Japan, the factional politics of the leading Liberal Democratic Party and sometimes even the legislative slowed down the crucial decisions of the executive. In Korea, the Party-Executive Consultative Council also often impeded the executive branch (Moon and Prasad 1998: 11).

It is rightly believed that the bureaucrats in the East Asian developmental states are technically competent and highly convergent in their goal orientation. However, they observe a problem equal to all East Asian developmental states: despite similar cultural traits, close school ties, and congruence with national goals, bureaucratic agencies in developmental states are not unitary, but reflect organizational complexities with diverse and often conflicting ideologies, preferences and interests. Inter-agency rivalries, compartmentalization and sectionalism are the rule, as in any other bureaucracy (ibid).

No matter how much the Asian bureaucrats are special, they do share common problems related to any other bureaucracy in the world. Despite that, it would be false to state that developmental states all have similar bureaucratic systems, as it is implicitly assumed in many works. Moon and Prasad conclude that Japan, for instance, has a deep bureaucratic fragmentation, whereas Korea is an example of a clear vertical bureaucracy. Taiwan is somewhere in-between.

Thus, the failure to elucidate the internal organizations and interactions of state structure has led to an incomplete conceptualization of state-society relations (Moon and Prasad 1998:12). Clearly, bureaucratic agencies are not organizational islands, but are beholden to corresponding social groups and obliged to protect their interests and solicit their support! Moreover, as Okimoto (1982) reminds, there are no uniform patterns between developmental states as far as state –private sector interlinking is concerned. He claims that in Korea these links are vertical and selective, while in Japan they are more horizontal and consultative.

Furthermore, the efforts of the developmental state paradigm to trace the causal linkages between institutions and economic performance seem also problematic (Moon and Prasad 1998: 13ff). Several basic assumptions underlying the argument that developmental states promote superior economic performance are easy to challenge. One of the premises is that insulated bureaucrats create rational policies in the “national interest”, which can, but also may not be the case if economic policies are politicized. A second assumption is that state policies are highly competent and effective, whereas in, for instance, South Korea and Taiwan despite the major success failed (heavy-chemical industry in Korea, steel sector in Taiwan). Finally, the developmental state paradigm assumes that state policies provide the major determinant of economic performance and outcomes, overlooking different fluctuating patterns.

Park (2006: 34ff) quotes four failures of the East Asian political system. The first was benign neglect of the inherent conflicts between East Asia’s governance mechanism, on the one hand, and the democratic polity and market liberalization on the other. Another failure was the inability to restructure the

financial system. A third failure of the system was the closed and non-transparent corporate sector that did not fare well with market liberalization and opening. Briefly, the system was slow in accepting global norms. Finally, the fourth failure of the East Asian model according to Park was its fixation on an export-led development strategy, which was at the same time the most successful feature of the East Asian development model and. This argument is disputed, because many authors, as mentioned earlier, claim that for instance in Japan there was *no export-led fixation*.

Following the argument, this section seems to leave us with three conclusions:

a) the bureaucrats and politicians in the developmental state are not perfect, and thus also not spared of vested interests, corruption, rivalry and even elitism, often leading to the stratification of society into those having the access to information and those who do not have such access.

b) There is no single “developmental state bureaucracy,” since the bureaucratic systems in different developmental states can be distinguished from each other.

c) Despite the common belief, bureaucracy is not the most important feature of the developmental state apparatus, because it is often fragmented itself and dependent on politicians, businesses, and increasingly also the non-state actors; this is clearly overlooked in the assessment of the developmental state model.

B. STATE AND BUSINESS AND... WELL, THAT'S IT

But is it really all in the single relation between the state and the market, at last? What did the developmental state theorists and practitioners forget when boosting about the strong state? They forgot that the state is not homogenous, and that it depends on a series of other actors, who, thanks to globalization,

quickly recognized their role and are eager to engage in a series of issues. Japan was often criticized by the West for its lack of democratization as far as the presence of non-governmental organizations, civil society, women participation in politics, and so on are concerned. Moreover, other developmental states were not spared of such criticism. The emergence of new priorities, such as the boom in environmental issues (primarily the relation between industrial growth and ecology), was also not tackled in the initial concept.

Nevertheless, let me point out here that the Western critique is often unjustified. Sometimes it really seems that the West simply could not stand the fact that East Asia, especially Japan, was growing rapidly. Reproaching to Japan the lack of democratization in the 1960s (the high-growth era) is, to put it mildly, strange. One should bear in mind that, in the same period, in the United States its president Kennedy as well as a pastor Martin Luther King were assassinated; Europe, especially France, reacted to undemocratic processes and poverty with the 1968 protests and revolutions; the entire world rose against the Vietnam war, but remained unheard. This is not to justify Japan's masculine politics or certain corrupt politicians, but rather to emphasize the hypocrisy of the industrialized nations when it comes to criticizing those who dare to be in some way different.

Nevertheless, East Asia had to adapt, not because the West told it to do so, but for its own sake. It engaged in regional integration, global partnerships, trade, development aid, environmental negotiations, and a number of other issues which were not a priority during the period between 1950 and 1980. In this vein, Pekkanen (2004) contends that civil society has always been an unrecognized element of developmental state story, both in its success and its decline. Yet, the very success of developmental state brought Japan to a new level of affluence and led to the increasing prominence of civil society organizations. Pekkanen concludes that, although small in scale compared to the United States, the activities of these groups are corrosive to political insulation.

Today, there is no room for iron triangles, since the world has become a different place. The existence of civil society has contributed to the overall increase in democratization. East Asian states simply had to adapt to this new circumstances. Therefore they started preparing conditions for the civil society to develop. As Yamamoto (1999) notes, non-profit and non-governmental organisations active in the field of human development and welfare are a very recent phenomenon in many countries of East Asia, because in the past they have been discouraged by authoritarian regimes.

Moreover, all the NGOs remain heavily dependent on external sources for funds, notably official overseas aid organisations, the US philanthropic funds and Japanese corporate funds. Similarly, in Korea, the *chaebol* (industrial conglomerates) have generated philanthropic corporate funding to an extent unknown in the other countries (Gough 2000:11). This is a good example that the industry may not only cooperate with the government, but also with the non-governmental sector.

In the miracle period, the social partnership in the shape of wage negotiations, similar to that of Germany or Austria, regularly took place. *Shunto*, the annual “spring offensive” in which management and trade unions conducted wage negotiations throughout the country, came into being in the late 1950s. This has now in Japan been eroded, due to neo-liberal reforms of 1980s and especially 1990s, as chapter 3 will argue.

And not only in Japan are the consequences serious. Joon Yoon (2005) argues that Korea has adopted the Japanese labour model: industrial peace unparalleled elsewhere implying fostering worker-management cooperation (company unionism, no temporary layoffs, synchronized annual contracts, seniority-based wages, and the bonus system). Yet the labour relations in Korea have been turbulent for the last 15 years, with its strike intensity exceeding that of any industrialized country during most of that period. Joon Yoon is convinced that one of the most important reasons for this labour militancy is due to abrupt decontrol of labour relations in 1987.

Thus, similarly to Japan, Korea simply overtook the model of labour market liberalization, which it did not need and for which it was not ready. Similarly to the above argument of Japan, this is not to argue that Korea needs a dictator such as General Park Chung Hee who was practically alone to rule the country. Neither does it need non-transparent politicians and bureaucracy. It, however, does need the state besides the market – it needs its previous labour model (adapted to today's global conditions, of course, but not 'neo-liberalized') as it is starving for social equality.

2.3 CONCLUSION: DEVELOPMENTAL STATE - ACTORS AND THEIR POWER, NOW AND THEN

As we have seen in this chapter, the roles of the state (its politics and bureaucracy) and the business have very much changed in the course of previous decades. Moreover, civil society and numerous associations have emerged, rendering the assumption about the state as a single actor rather questionable. The traditional developmental state concept has overlooked globalization, not in the sense that it overestimated the role and the capacity of the state, but rather because it neglected other social actors and groups in the economic life. Table 1 contrasts the role of different social actors in East Asia in the high-growth phase with their roles today. As it is obvious, some of them had only a little significance in, say, the 1960s. If we want to apply some tenets of the traditional developmental state today, we have to rethink it from today's perspective. This is the objective of the following table, as it introduces us to the next part of this study: the case studies.

Table 1: Social actors/groups and their roles within and outside developmental state, now and then (East Asian developmental states)

social actor /group		Role 1950-1970	role in 2008
STATE	BUREAUCRACY	Administrative organization of economic activity; rather autonomous, often vested interests ("iron triangle" of bureaucrats, politicians and business)	Administrative organization of economic activity; reform into a transparent, more flexible and cooperative apparatus
	POLITICIANS	Regulation of economic activity; often one dominant party, dependent on bureaucracy	Regulation of economic activity; relatively to bureaucrats, more power than before but rather unstable majorities in their respective governments
PRIVATE SECTOR		Engine of growth – production and exports in the centre; interlinked with bureaucracy and politicians	Still powerful, but lost its importance due to the 1997/98 speculation bubble and the recent global crisis; moderate liberalization, but still regulated
INSTITUTIONS	NATIONAL	A few "pilot agencies" in Japan, Taiwan or Korea, very significant for growth; later led to democratization	Numerous "pilot agencies" with none in the centre; reforms, with states more prone to coordination ("social capital") and not only regulation

	REGIONAL, INTERNATIONAL	Regional integration not seen as particularly important, dominance of Japan; international cooperation very limited	Regional cooperation and integration envisaged and supported, especially after the 1997/98 crisis; internationally still rather protectionist, participation in the WTO minimal; emerging donors in the IMF and the World Bank (the only non-emerging, Japan, being the most important Asian donor)
LABOUR UNIONS		Important; labour negotiations very important, social income equality among the world's highest	1990-2005 decreasing importance; since then attempts of revival; growing discontent of labour (e.g. Korea)
CIVIL SOCIETY AND NGOs		Rather dispersed and rare, due to rather authoritarian regimes; non-organized protest groups	Emergence, but still not as present as in Europe or the US; cooperation of NGOs with the private sector - increasing importance

PART II: CASE STUDIES

CHAPTER 3

JAPAN, *DOKUJI NO MODERU*

The previous two chapters served as a theoretical perspective on the role of the state. Whereas the first chapter recalled the classic state theories, the second focused on the concept of developmental state. I identified the present state of the debate, and besides that also the shortcomings of the traditional developmental state theory. Rapid reforms, I argued, resulted in the post-developmental state, which coincided with the Post-Washington Consensus. It again was a response to the outside pressure.

Old developmental states opened quickly, became politically relatively more liberal and tolerant as civil society emerged. However, the part of the “package” was also the quick privatization of state enterprises and liberalization of financial markets, and a decline in labour negotiations and massive layoffs. Luckily, the consequences were not similar to those in Argentina, but still, these state have not completely recovered from the Asian crisis. Moreover, the global financial crisis of 2008 only made matters worse. Hence, the post-developmental state in that form is again not acceptable.

For the revised theory of the old developmental state, we first need to review what was good and what was not so good in the pioneer developmental state, Japan. The following chapter will remind the reader of the Japanese social and economic history, the advantages and shortcoming of the Japanese economic model, and it will conclude by determining whether the role of the state in this model was sufficient. It will not, however, analyze in detail the current situation in Japan, since this will be done in chapter 5.

3.1. BIRTH OF THE JAPANESE DEVELOPMENTAL STATE: A SHORT HISTORY

At this point we need an insight into a contemporary political, economic and social history of Japan. How did it come to the Japanese miracle? History can provide us with answers. This section will thus review the Tokugawa period (3.1.1), the Meiji Restoration (3.1.2), the interwar period (3.1.3) and the period from the American occupation until today (3.1.4).

3.1.1. THE TOKUGAWA (EDO) PERIOD (1603-1868)

As noted previously, the Japanese economic development was not at all spontaneous or the product of some magic force, no matter how mystically powerful the hills above Kyoto might seem; nor was it simply the person of Meiji Emperor who transformed the country from a self-sufficient island to an astonishing global role model of economic development. It was, as one might rightly assume, a set of different factors that were Japan's driving force. One of these factors, clearly, is the history itself. Recalling the Japanese history in brief is not a very difficult task, since there are plenty of authors who rose to the challenge.

For instance, Tsutsui et al. (2007) offer an intensive investigation into the totality of the Japanese history, Meyer (1993) gives a rather concise but still a very informative overview, McClain (2002) thoroughly investigates the period of the Japanese history including and after the dynasty of Tokugawa (after 1603), whereas Flath (2005) or McCargo (2004) offer rather short summaries of the Japanese economic history after 1603. Though I am myself more interested in the period after 1868, I will briefly summarize the most important events which had led to the Meiji era, to remind that this latter one only triggered off what had been prepared long in advance.

Sabouret (1995: 74-78) follows the commonly accepted line of literature and divides the history of Japan into 5 main periods: the prehistory (8000 BC - 600 AD), the ancient period (600 – 1185), the Middle Age (1185-1573), the period of premodern Japan (1573-1867) and the contemporary Japan (1868 up to now). All of these periods are then divided into further time sequences, some of which will be mentioned in the course of this chapter. While the first three epochs are characterized by constant struggles of numerous dynasties for power, in 1603 something crucial and utterly different will happen: the monarchy will disappear and the shogunate (shogun's office, in Japanese *bakufu*, 'the house of the general') will be established. Although the first shogun title was conferred by the Emperor already in 1192 to Minamoto Yoritomo, more than four centuries had to pass until the shogunate became the only form of governing force in Japan. How did it come to that?

As noted by Flath (2005: 31), the Japanese feudal system was somewhat different from that in Europe. In the late 15th and early 16th centuries, there gradually emerged locally powerful rulers known as *daimyo* (literally meaning "great names"). First, their area of influence was very restricted, but eventually they started exerting control over more extensive territories. As their authority became more secure and encompassed a wider region, they disposed over different policies that had long-lasting benefits and enabled them to draw resources away from neighbouring rivals. By the middle of the 16th century, the *daimyo* had come to assume all functions of government within their respective domains called *han*. They had an army of their own samurais, but their total power did not extend their own *han*.

Nevertheless, Tokugawa Ieyasu (1543-1616), the founding father and the first shogun of the Tokugawa shogunate (*bakufu*), was different. He simply did not want to restrict himself to an area as limited as *han*. Gradually, he took over the whole country (reunified during his predecessors) and in 1603 he became a shogun. Although notionally subordinate to the Emperor, the shogun was indeed effectively a ruler. By defeating their rivals militarily, the

Tokugawa family achieved hegemonic control of Japan, bringing under their control the numerous local feudal lords (McCargo 2004: 15).

Tokugawa Ieyasu conferred to himself alone certain rights, including the right to establish foreign policies and national standards of measurement, the right to issue national currency, and the right to remove other *daimyo* who were suspect for threatening the hegemony of the shogunate or offenses of the shogun. During the two centuries when Japan was a relatively closed country, real political power laid in the hands of the Edo shogun (“generalissimo”), while the Emperor lived in seclusion in Kyoto (McCargo 2004: 16).

All *daimyo* including the shogun were dynastic in character. As a general rule, each *daimyo* was succeeded by his eldest son. Moreover, during the Tokugawa era, the Japanese population was stratified into social castes by shogunal decree. The priests of two most important religions of Japan, Shinto and Buddhism, and doctors, were outside the caste system, but nearly everyone else fell into one of four groups: samurai, farmer, artisan, and merchant.

Hérail (1986: 318) notes that the neo-Confucian tradition took the credit for this stratification, the principle of which was the natural order. If such an order was established in the nature, it seemed evident that that order should find its equivalence among humans. Investigating the life of peasants and, on the other hand, of the town residents in the 17th –century Japan, Hérail (1986) comes to the conclusion that, although the latter enjoyed certain privileges and liberties reserved only for them, they were also not spared of stratification in their professions. Apprentices had to wait a long time in order to be able to climb the professional ladder. Finally, those who exercised professions considered ignoble, such as squaring or tanning, were secluded from the rest of society, although they had a theoretical possibility to be conferred their status back (Hérail 1986: 327).

Daimyo had the obligation to always stay well informed about the central administration in Edo. Notably, the policy of *sankin kotai* (alternate attendance) is to mention in this context. This policy required each *daimyo* to periodically change residence, therefore to spend a certain amount of time in their own *han*, and then to stay in Edo (today's Tokyo), the capital, for a while. This system established the responsibility of the *daimyo* before the shogun (Flath 2005: 33).

Although the *daimyo* were the sovereign rulers of their respective *han*, having independent powers to set taxes on their subjects, there also existed a system of collecting land taxes that was quite uniform throughout Japan, referred to as the *honbyakusho* (original farmers') system (Flath 2005: 24). Despite the fact that Edo Japan is often loosely termed "feudal", a combination of central military power and local devolution to the *daimyo* amounted to a "feudal-central hybrid" (McCargo 2004: 16). At this point, let us stress that this form of government, a mixed model combining centralization and the *daimyo han* rule, will later form an important characteristic of Japanese bureaucracy.

As for international trade before the 17th century, one can say it existed in its most rudimentary features. In 1642, however, the third shogun and the grandson of Tokugawa Ieyasu, Tokugawa Iemitsu, issued an order for the closing of the country. The Dutch were the only European country that was allowed continued contact through the southern port at Nagasaki, but they were not allowed free transit within Japan. Under the policy of national isolation, the Tokugawa also expelled Christians from Japan (McCargo 2004: 15). Hérail (1986: 330) estimates there were about 300 000 Christians forced to leave Japan in 1613. In 1616, only the ports of Nagasaki and Hirado were open to foreigners. Nevertheless, in 1623 the English were definitely expelled from Japan, following the Spaniards in 1624 and in 1639 the Portuguese (Hérail 1986: 331ff).

Despite such unilateral Japanese acts, the image of Japan as a "closed country" is said to have been somewhat exaggerated. In practice, the foreign trade taking place throughout this period was substantial, especially with China

and Korea, and notably through the Ryukyu Islands (today Okinawa). Western books other than Christian tracts were allowed to circulate in Japan after 1720, and Japanese experts in “Dutch studies” (representing for the Japanese the synonym for the knowledge about the West) were engaged in translating and assimilating information from abroad, especially material concerning technological and scientific progress (McCargo: 16). Although some authors insist that Japan remained closed all the long until the Meiji Restoration, others, such as Hérail (1986: 333) assert that Japan never completely broke ties with the West. It is only in the 20th century, though, that the country will reach the peak of export production (Flath 2005: 26).

Japan achieved significant industrialization and rising per capita income only after the precipitous demise of the Tokugawa regime and the dismantlement of the *baku-han* system in the mid-nineteenth century. Many scholars of Japan’s economic history remain divided on whether the draconian economic and political controls of the Tokugawa era, notably centralization and trade controls, retarded Japan’s economic development or hastened it (Flath 2005: 18).

This discussion overwhelmingly reminds of the debate on the Japanese economic growth after World War II, as we shall see later. Pratt warns of generalizations. “There is no doubt that the lives of Japanese changed in very important ways over the course of Tokugawa, and that terms like ‘immerisation’ are woefully inadequate in characterizing their lot” (2007: 96). However, historians cannot ignore the questions of who benefits from economic growth. But precisely the most remarkable transformation took place in the countryside, since farmers produced more for the market, and they also bought more from that same market (ibid: 97).

In any case, from the founding of the Tokugawa dynasty by Ieyasu in 1603 until the Genroku era (1688-1704), the apogee of Edo culture, the economy of Japan grew significantly. The population increased from about 20 million in 1600 to about 30 million in 1700. The great cities, particularly Edo,

grew and prospered. The extensive growth in the 17th century derived from the more secure and durable rights of the samurai class to the taxable output of the economy (Flath 2005: 26). However, it also gradually had the effect of shifting power away from the samurai towards the emerging commercial sector. The city of Osaka was at that time and remains today one of the principal trading cities. But, engaging in commerce in Japan was traditionally considered with significant disregard, because trade itself was not capable to generate any new value (contrary to agriculture or manufacture), so its volume was gradually reduced throughout the 18th century (Hérail 1986: 353).

The Edo government was eagerly looking for justifications of its authoritative mandate in the Chinese political philosophy, the basis of which was contained in the principle of obedience and loyalty of the inferior towards their rulers (Hérail 1986: 336). Under the *baku-han* system, *daimyo* were secure in their exclusive rights to levy taxes on the lands within their own *han*. In sum, the historical record of the late Tokugawa era affords evidence of both technical change and capital accumulation (Flath 2005: 27).

Many historians argue that the prominent discussion on *Nihonjinron* (literally: theories about the Japanese people) also dates back to Tokugawa period, although it was coined after the Second World War. *Nihonjinron* is a set of theories encompassing sociology, psychology and philosophy, but also linguistics and general history. All have in common to claim that the Japanese people are unique, that their identity is distinct with relation to any other. Some traits of *Nihonjinron* border with racism, claiming that the Japanese race is absolutely unique or sometimes even superior to other. However, put aside this extreme view of *Nihonjinron*, there are also many arguing the speciality of the Japanese language, economics and culture when compared not only to the West, but also to other Asian countries.

The Tokugawa period, or the period of seclusion, was definitely a fertile ground for *Nihonjinron*, and the forced opening in the 19th century only lighted the fire of it towards the West. The *bakufu* was politically a stratified society, as

noted above, consisting of shogun, the priests, the *daimyo*, the *samurais*, and poor peasants. How did come to the transition of political to economic stratification? In this period, the economic change was absolutely rapid.

This pace of change however produced numerous reasons for social discontent. The samurai became jealous of higher incomes of merchant families, whereas it was clear that social classes alone no longer determined wealth. Moreover, there were numerous peasant protests over taxing policies which made clear that the Tokugawa did not have a long period ahead. The Edo bureaucracy is said not to have been meritocratic, but it did reserve higher positions for the well-born, blocking career prospects for lower ranking but more able young samurai (McCargo 2004: 17).

Nosco (2007:111) shows however, that by the end of the 17th century merchants and other non-samurai commoners figured prominently among the student rolls of private academies as they increasingly availed themselves of forms of knowledge to which they or their ancestors would have been excluded as recently as a century earlier. In this way knowledge became a socially valuable commodity. Hence, the result of the change was not always pauperisation, and this is similar to the arguments of the theories of *Nihonjinron*. In other words, the Japanese transformation is seen as different from, say, the abolishment of feudal system in Europe.

While the reforms of the second half of the 17th and the whole 18th century (notably the reforms of the Kyoho, Kansei and Tenpo eras in the fields of agriculture, industry and government) hardly bore any fruit, the trigger of the real change was the arrival of the American “black ships” under Commodore Matthew Perry in 1853. Perry wanted to re-establish trade relations of the United States with Japan. *Bakufu* did not have much choice, given its problematic political situation and the experience of its neighbours with the West, notably China. Since the Tokugawa did not want something like the Opium Wars to repeat on their territory, and given the powerful fleet of Commodore Perry, Japan formally opened for trade in 1854 (Sabouret 1995:

80). Moreover, Japan also accepted to sign “unequal treaties” with the United States in 1858. This opened the way to signing similar treaties with Great Britain, Russia, Holland and France immediately afterwards (Gravereau 1993: 23).

After the conservative *daimyo* leader Ii Naosuke, who negotiated the opening of Japan, was assassinated in 1860, the policies towards the reunification of the Emperor and shogunate failed. Conservative *daimyo* from the South, hostile to the regime, quickly formed an alliance against the shogunate in 1866 (Hérail 1986: 378). Too weak to resist the attacks, the last shogun, Yoshinobu, was therefore forced to give back the power to the Emperor. In 1867, the old- new monarchy was finally restored, and this was the beginning of the Japanese renaissance.

3.1.2. THE MEIJI RESTORATION (1868-1912)

The significance of the Restoration today is contested: while some historians see it simply as an elite manoeuvre on the part of a small group of ambitious samurai, the more recent scholarship has supported the view that the Restoration reflected a growing social movement for revolutionary change (McCargo 2004: 17).

The Meiji Restoration was indeed crucial in many aspects. Immediately in 1868, the newly proclaimed ruling council of government, the *dajokan*, acted quickly to consolidate its authority. At first, the Meiji leaders usurped the position previously occupied by the Tokugawa *bakufu*, continuing both to collect rice taxes and to pay samurai stipends, and allowed *han* governments to do likewise (Flath 2005: 26). Young emperor Mutsuhito, aged 14, became a symbol of national unity. He reigned until 1912 under the name “Meiji”, meaning “the enlightened reign”. After 1868, the Emperor was no longer a political marionette: the significance of his role began to grow (Gravereau 1993: 23).

A period of rapid modernization followed, as Japan sought to catch up with the West. Moreover, missions were sent to study Western states and

societies (such as France, Britain, Germany and the United States). The aim was to identify models that Japan could apply. This demonstrates an astonishing feature of the Japanese collective psychology: a high level of readiness to adapt models of other countries despite the fact that these latter actually *broke into* Japan's territory and imposed their values there. During the early Meiji period, Japan established a wide range of new institutions, including a British-style navy and postal system, a French-style police and judicial system, American-style banking and primary school system, and a German-style army (McCargo 2004: 20).

This meant that, from the earliest phase of its modernization, Japan had the quality that every state should possess: the ability to learn from other countries that are especially successful in a certain area, regardless its political relations with them. Yet learning from others does imply a random imitation of other systems, but thinking through what models would be optimal for one's own country given its social, historic political and economic context.

Among the Japanese new leaders there were many open to change. Why? McCargo argues: "Japan benefited from a relatively young leadership, and, importantly, the ruling elite were urban-dwellers who derived their power from their formal positions, not from landed estates" (2004: 20). The result was that during the Meiji period, Japan emerged as the first non-western industrial power. *Shookusan ko-gyo* (*Establish and develop the industry*) was the devise of the Meiji government, which itself inherited from the shogunate a very poor financial situation (Abbad 1992: 18ff).

Various steps, taken in order to forge a more powerful and effective state, and to establish a strong sense of national identity, brought about this rapid industrialization. The monarchy was seen as an important symbol of the nation. School textbooks, at first controlled and then also directly written by the Ministry of Education, and came to emphasize moral themes, such as loyalty to the throne (McCargo 2004: 21). The Japanese nationalism was boiling, before exploding between 1926 and the end of the World War II.

In 1869, the turning point in the political reorganization of the country happened: the *daimyo* handed their fiefs back to the state and were made state officials or bureaucrats (Sabouret 1995: 80). In the same year, the new social hierarchy, along with its four new classes, was established: the nobility (*kazoku*), unifying the aristocracy of the Court and the ex-feudal owners; warriors of the higher order (*shizoku*) along with the samurai; warriors of the lower order (*sotsu*); and finally, the rest, “the ordinary people” (*heimin*). The governmental policy aimed to abolish the *sotsu*, which could not be easily differentiated from the *heimin* anymore (Abbad 1992: 16).

Moreover, in July 1871 the Meiji government abolished the *han* in a promulgation known as *haihan chicken*, and replaced them with new political units, three *fu* and 302 *ken*, both corresponding to prefectures in English (Flath 2005: 28). Economically, the country also experienced major changes. Prior to Meiji Restoration, the main sources of revenue both to the *bakufu* and to the *han* governments had been rice taxes. Flath (2005: 31) point out that in July 1873 the government moved to replace the rice tax with a monetary land tax. Besides acting to consolidate sources of revenue, the Meiji government also aimed to curtail expenses, whereby the major government expense early on was the payment of stipends to the samurai or warrior caste.

In 1873, the Meiji government amassed a largely non-samurai force armed with modern weapons. The government divested itself of the major drain on public finances, the samurai stipends. Therefore it introduced the first voluntary commutation of stipends, and then the suspension of all pension payments (ibid). In order to keep pace with the West, the tradition of which it met so abruptly, Japan decided in 1880 to liberalize numerous small public enterprises, favouring thus the birth of industrial bourgeoisie (Sabouret 1995: 80).

The country also seemed to be ready for the introduction of the Western democracy. Hirobumi Ito, the first prime minister of Japan, boasted that Meiji had brought Japan not only “prosperity, strength and culture”, but “an equal

footing in the family of the most powerful and civilized nations of the world” (Huffman 2007: 143). Three leading figures of the Restoration, Takayoshi Kido, Takamori Saigo and Toshimichi Okubo, died within a year of one another in 1877/78 leaving the future direction of Japanese politics unclear.

Then, in the famous political crisis of 1881, the finance minister Okuma proposed the early establishment of representative democracy and was soon driven from office. Masayoshi Matsukata was appointed Minister of Finance in October 1881. As Vice Minister of Finance, Matsukata had been one of the architects of the land tax reform, and after an observation tour of European capitals had advocated a number of further reforms (Flath 2005: 33).

The early establishment of a convertible currency under Matsukata comported perfectly with a prominent political slogan of Meiji Japan “rich country, strong army”. Japan indeed became rich: the *Matsukata deflation* completely reversed the previous situation inherited from the *bakufu*. Although it initially induced a business recession in the 1880s, it however raised the real value of the land tax receipts, unburdened the government of the annual losses which the government factories had invariably sustained, and restored fiscal balance (Flath 2005: 34). The Matsukata reform had spectacular effects in the budget, but however those who bore the burden of it were mainly peasants, workers, small entrepreneurs, merchants and artisans (Abbad 1992: 24).

After a series of revolts, mostly initiated by lower classes that demanded a more democratic decision-making, Japan finally became the first Asian country with its own constitution and parliament. The most significant political development of the Meiji period was therefore the promulgation of the 1889 Constitution, which symbolized the forging of the first modern nation-state in Asia (McCargo 2004: 21). The Meiji Constitution had provided for a bicameral assembly (the Diet), including an elected Lower House and non-elected House of Peers. Moreover, to prevent the prime minister from becoming too powerful, ministers of state were made responsible not to him, but to the Emperor. That

made it difficult for the prime minister to ensure cabinet unity and it weakened the cabinet as a whole (Large 2007: 159).

Therefore, although most essential powers of government reposed in a prime minister, nominally appointed by the Emperor, but in actual practice selected by the Meiji oligarchs themselves, both extra-legally as *genrou* (elder statesmen) and in their formal capacity as an advisory council to the Emperor (*sumitsuin*, the Privy Council) (Flath 2005: 27). Therefore, even though the Constitution was the one imposed from above and despite its definition of the Emperor as the sovereign source of supreme authority, in practice the real power belonged to a group of influential leaders and oligarchs (McCargo 2004: 21).

The government was dubbed *hanbatsuseifu* (meaning literally “provinces- fractions –government”) implying that the future political leaders of Japan could be selected from only some provinces (formen *han*) of Japan, such as Satsuma, Choshu, Tosa or Hizen. These provinces had a historical importance. Vié (1971: 14ff) warns however that the denomination “oligarchs” deserves to be clarified. The ruling fractions during Edo had always needed support from the elite of the *ancien regime*, and analogically, Meiji oligarchs could also not govern without the help of an extensive bureaucracy.

Besides that, ruling fractions were not necessarily formed on a regional basis: in Satsuma fraction, for instance, there were many fraction members not originally from that region. Large (2007) asserts that that, although in theory the Emperor stood supreme in all civil and military affairs, the oligarchs in fact anticipated that the emperor would reign over, but not rule, Japan. However, they could not unify the government.

Foreign expansion was one further preoccupation of the Meiji oligarchy. In 1876, two decades after Japan’s own forced opening by Perry, the Japanese leaders coerced Korea into opening three of its ports to Japanese traders. From this point, Japan was a rival to the Western powers in pursuit of Asian empire,

even though, ironically, its very own waters encompassed trade ports established by unequal treaties (Flath 2005: 36-37). After the victory in the Sino-Japanese War of 1894/1895 and the acquisition of Chinese concessions of Pescadores, Formosa (later Taiwan) and the Liaotung Peninsula, the Shimonoseki Treaty will give the chance to the Japanese to renegotiate the unequal treaties. Japan's territorial expansion was just about to begin, and its power in Asia grew significantly. The 1904/1905 Russian-Japanese War, then, gave a new imperialistic force in the battle of wills between Japan and his neighbours. Korea will be the first victim, annexed in 1910 (Sabouret 1995: 81).

As the end of the nineteenth century approached, the Japanese economy underwent a permanent transformation. The industries that mechanized and grew first were cotton spinning and silk reeling. Textiles carried a much greater weight in Japan's foreign trade than in its output. Cotton yarn and raw silk, together, accounted for about half of Japan's exports in the last decade of the 19th century. Raw cotton accounted for a third of Japan's imports. However, Meiji Japan's direct gains from foreign trade should not be overstated, because it was more oriented towards domestic production. Moreover, the Meiji government actively encouraged the infusion of foreign technology. Under the slogan "increase production, encourage industry", the Meiji government hired foreign advisers to set up model factories, including mechanized cotton spinning factories and silk filatures (Flath 2005: 35).

The light industry began to flourish after the Sino-Japanese, and the heavy industry after the Russian-Japanese War. During the Meiji era also the agricultural production increased, not due to agricultural revolution, but simply to the amelioration of the existing agriculture (Hérail 1986: 431). Industrialized Japan however, as it was also the case in Europe and the US, had to cope with certain by-products of industrialization, some of which were pauperisation and the renewed stratification of the society.

All the socialist parties in Japan were banned throughout the interwar period. However, the restlessness of the extreme left will persist, and the secret

movements of the socialists will multiply. Nevertheless, this party was again subject to repression. The party which is present and active in Japan today, the Social Democratic Party of Japan, was finally founded in 1945.

Explaining the roots of the Japanese capitalism, Vié (1991: 50ff) emphasizes the importance of the dual economy of the Meiji time: small artisans and agricultural properties were to find next to huge factories and modern technologies. Flath (2005: 51) however reminds that there are many scholars claiming that in such dual economy, only one of the two sectors, the modern sector, exhibited a sensitive response to economic incentives. According to this line of thinking, Japan's small firms belong to a backward sector of its economy, in which sentimental attachments to traditional ways of living have attenuated the pursuit of economic gain. In the similar vein, the Meiji era is marked by the birth of *zaibatsu*, or financial cartels, which we will approach in more detail later on. Therefore, the industrial part of the dual economy is generally regarded as the pillar of modernization.

After the death of the Emperor Meiji in 1912, though, everything in Japan will go downhill. When he learned about the death of the Emperor, the general Nogi, celebrated for his victory in Port Arthur during the Russian-Japanese War, committed suicide (Sabouret 1995: 81). A great crisis was to take place, both economically and politically. Before passing on to that rather obscure part of the Japanese history, we should conclude by emphasizing once again the importance the Meiji Restoration for further Japanese development. In Flath's words (2005: 45), the change was drastic: "As the Meiji era closed in 1912, Japan's economy exhibited many features that would have struck an Edoite of a hundred years earlier as completely alien but would be familiar to a Tokyoite of today."

3.1.3 FROM THE MEIJI INTO THE WARS: 1912-1945

However, it was not only the economy that changed. The government organization became after the death of Emperor Meiji at first more democratic, and later it fell into the hands of the military. The first period, Taisho democracy, corresponds to the reign of the weak and mentally ill Emperor Taisho (1912-1926). This was the time when political parties grew in importance and there was also greater political freedom than previously.

In the First World War, Japan will take the side of Entente, and will therefore be able, as one of the victors, to accede to the League of Nations in 1919 (Sabouret 1995: 81). From 1918 to 1932, political parties were more powerful than ever, and prime ministers were generally selected from among the party leaders. Nevertheless, the political parties that existed were mostly elite organizations, and party politicians were obliged to work in close collaboration with the court, the bureaucracy and the military (McCargo 2004: 23).

An important political change occurred in 1925, when universal male suffrage was introduced. The heritage from the Meiji leadership was also the strong army, since the Meiji placed considerable emphasis on military. Two victories in two wars, against China in 1895 and Russia in 1905, were a major turning point, greatly emboldening Japan's leadership for the pursuit of further imperialist adventures. The rise of militarism in Japan during the 1920s empowered the armed forces at the expense of other political institutions, leaving the military in a strong position (McCargo 2004: 23).

During World War I, Japan enjoyed an unprecedented economic boom. Nevertheless, half of the nation's labour force continued to work as self-employed farmers, and another fourth of the labour force as small shop-keepers, independent craftsmen, and the like. Japan had accumulated massive foreign debt to finance its 1905 war with Russia, which exploded later (Flath 2005: 45).

The Japanese accumulation of foreign assets during World War I had implications for Japan's exchange rate and industrial structure. Cumulatively, very small firms employed far more Japanese workers in 1920 than did large firms. Agriculture was still the occupation of roughly half the workforce in Japan of the 1920s and 1930s and these were overwhelmingly self-employed. Turning from agriculture to manufacturing, the persistence of small firms in Japan in the 1920s can be attributed to the extreme refinement of traditional handicrafts (Flath 2005: 51).

In the decade after World War I, Japan joined Britain and the US in the arms limitation agreements, diplomatic treaties and pursuit of an open world trading regime, anchored by the gold standard. Nevertheless, the 1923 Tokyo earthquake drained government resources and ultimately led to a severe banking crisis in 1927 (Flath 2005: 61). This crisis will announce the sound of the death knell for the economic prosperity of Japan prior to the World War II.

The rise of militarism from the 1920s culminated in 1931, when the Japanese Army used an event of an insignificant explosion to invade the whole of Manchuria and establish the puppet state of Manchukuo. The Japanese military occupation of Manchuria marked an abrupt departure from Japan's policy of conciliation of the Western powers, referred to as "Shidehara diplomacy" after Shidehara Kijurou, foreign minister from 1924-27 and 1929-31. Until its August 1945 surrender, Japan attacked China, the US Navy at Pearl Harbour (1941), invaded and conquered most of Southeast Asia, and fought a brutal war against the Allies (McCargo 2004: 24).

Hence, Japan's "Fifteen-Year War", as the period of Japanese imperialism (1931-1945) is referred to in the literature, was definitely one of the darkest periods in the entire Japanese history. Japan, subject to an overall international criticism, quit the League of Nations in 1933. After its alliance with Hitler's Germany in 1936, massacres of Nankin in 1937 and the creation of the axis Berlin-Rome-Tokyo, Japan was caught by the final military madness.

What should one hold of Japanese imperialism? Numerous historians encourage a vivid discussion, the result of which are always two poles. As McCargo (2004: 24) stresses, there is a group of (mainly Japanese) scholars that claims that the aim of this Japanese imperialism was in fact liberalisation, designed to free Asia from colonialism and establish a 'Great East Asian Co-Prosperity Zone'. The other side argues that there was nothing altruistic in invading Manchuria or prohibiting the teaching of Korean language in schools in Korea in 1941, as pointed out by Sabouret (1995: 82). It is certain that the military was in this period largely beyond the reach of civilian control. The prime minister and foreign minister often found themselves reacting to situations over which they had little control or influence. Therefore, the tenure of civilian leaders was usually short-lived: there were 13 cabinets and 11 prime ministers between 1932 and 1945 (McCargo 2004: 25).

Economically, the 1930s were, unlike almost everywhere else in the world, not caught in a trap of overall recession. This is not to say that Japan lived its economic boom. However, finance minister Takahashi marked the scene of this time. As Nanto and Takagi (1985) suggested, Takahashi had seemed to have read and assimilated Keynes pre-*General Theory* writings, because he very exactly implemented Keynes' policies in Japan before the famous book was even published. In any case, Takahashi asserted in the manner of Keynes, that, by deficit financing and accommodative monetary policy, the government could stimulate private economic activity. The Japanese developmentalism was in its infancy.

Whether because of Takahashi finance or the natural resiliency of Japan's market economy, the economic malaise was rapidly overcome. However, the assassination of Prime Minister Inukai in 1932 effectively ended government by the political parties. Takahashi, too, was killed in a plot organised by young military officers, in 1936. The Inukai coalition was immediately succeeded by two coalition governments headed by admirals not

affiliated with political parties (Flath 2005: 61). Thus, bad politics slowed down the promising economic growth and development.

Between 1931-1945, however, most characteristics of the contemporary Japanese economic system appeared. The state emerged as the economic general staff, and its capacity in economic intervention was strengthened enormously. Meanwhile, various nonmarket governance structures developed to restrain market forces. A very characteristic form of contemporary Japanese management, consisting in permanent employment, the seniority-based wage, and the company-based union, also developed. Many elements of these institutions had existed before the managed economy was created. Nevertheless, they were institutionally recomposed into a coherent economic system in 1931-1945. Although all major industrialized countries were confronting both the Great Depression and World War II, it is today known that Japan, along with Germany and Italy, demonstrated a pattern considerably different from the responses of both liberal capitalism and socialism (Flath 2005: 64).

In order to sustain the military adventure, this ideology gave production top priority in industrial policy. Flath (2005: 65ff) holds that the ideology of the managed economy, incorporating ideas from various sources, not only became the framework for the industrial policy practised by the Japanese state in 1931-1945, but also laid out the general principle for Japanese developmentalism in the long run. Contrary to that, many historians and developmental state scholars believe developmental state was born during the Meiji era.

In the military era, Japan put its economy forward. The military supported control by the state bureaucracy and the efforts to militarize the national economy. Although the military supported bureaucracy, its leaders also recognized that their goals could not be achieved without support from business. Therefore they had to admit the principle of capitalism. In contrast, the private sector had no excuse for opposing the managed economy because support of business was perceived as the highest priority of the nation at that time (ibid).

It is interesting here to point out the fact that when Japan was under strong international pressure, communists abandoned their Marxist beliefs and stood on the same side as management and the state for the first time in modern Japanese history. In the meantime, the claims for individual interests and shareholders' profits were strongly rejected. As Flath (2005: 66) puts it: "Marxist ideology coexisted with fascist and liberal ideologies, in order to formulate the strategy for the managed economy."

The American decision to drop atomic bombs on the Japanese cities of Hiroshima and Nagasaki was doubtless one of the most controversial of the Second World War. Despite the fact that the rest of the world has generally regarded Japan as an aggressive power during the 15-year period of 1931-45, within Japan there is a dominant perception of Japan as a victim of war. This is a rather delicate issue, since there is also a considerable denial of guilt for atomic destruction on the side of the United States.

Within Japan however, not only was Japan uniquely victimized as the target of two atomic bombs, but also the Japanese people saw themselves as the victims of the Japanese militarism. Blame was shifted away from the nation as a whole, onto the military and their elite supporters, especially the 28 leaders judged at the Tokyo War Crimes Tribunal (McCargo 2004: 27). Such a view among the Japanese continues to persist today, due to the nation seeing itself as a double victim, both of the regime and of the American bombs. As in most such issues, there is certainly a truth there, but it does not excuse Japan for its militarism and imperialism in the interwar period.

In the similar vein, the role of the Emperor Hirohito (1926-1989) during the war remains highly contested: some scholars see him as a rather peace-loving man, the others as a war criminal (McCargo 2004: 26). Gravereau (1988) is one of many scholars who are interested in the era of this Emperor who marked the entire 20th century. He contends that Hirohito, like the Japanese nation in general, is seen by some as a marionette of the military regime during the Japanese "Fifteen-Year War".

Gravereau describes the Japan of the 1930s and mid-40s as a society which is “under control” (1988: 68). Similarly to Orwell’s 1984, Gravereau asserts that everything, even one’s own thoughts, were subject to surveillance. Large (2007: 165ff) reminds that although historians debate the question of fascism in Japan of this time, there is however a consensus that it was driven by the impact of the economic depression on rural and urban Japan, the uproar over the disadvantageous terms for Japan in the 1930 London Naval Treaty and the crisis of the Manchurian Incident. Abbad (1992) however speaks more of duality, not only concerning the economy as it was mentioned previously, but also the duality of policies, institutions, even people. Ancient and new, modern and traditional, conservative and radical: this was Japan of the prewar time. And, no less, it is also Japan of today. In order to understand it and to learn from its past, these discrepancies should never be overlooked.

3.1.4. AMERICAN OCCUPATION (1945-1952) UNTIL TODAY

At the end of the war, Japan was deeply in the state of *kyodatsu* (despair, demoralization) and some scholars assert that much of the initial energy and optimism for its reconstruction therefore came from outside. Yet the Americans in fact demanded that the Japanese shoulder many costs of the occupation. In allied circles, there was considerable disagreement over how Japan should be treated. In the United States the debate was especially strong. There is an argument United States favoured an extremely limited intervention, and that this is precisely the reason why, in 1946, General Douglas MacArthur was assigned the task of implementing post-surrender arrangements and introducing a system of “democratic self-government.” Ironically, he himself had a very limited contact with Japanese people (McCargo 2004: 28ff).

The initial postwar period witnessed great problems in the economy, as shown by Pilat (1994). The economy had to assimilate six million expatriates, there were shortages in food and energy, threat of large indemnities from the

former occupied countries, strong inflationary pressures, and on top of this the country lay partly in ruins. Surprisingly, high unemployment did not arise after the war, probably because people could simply not afford to be unemployed.

The agricultural sector assimilated a large part of the labour surplus, whereas many others fled into the informal economy. In the first two years the economy suffered from great food and energy shortages, similar to many European economies. It seemed also that the occupation authorities would ask for large indemnities and that a large part of the remaining production facilities would be moved to the United States. This situation did not materialize, Pilat (1994) goes on, because with the outbreak of the Cold War the United States saw greater purpose in strengthening the Japanese economy.

In 1948 this American policy shift became clearer, when a number of restrictions on Japan's economic policy were lifted and the occupation authorities started planning for economic stabilisation and reconstruction. Up to 1950 the recovery of the economy progressed only slowly. A large, and much needed impulse to the recovery progress was given by the outbreak of the Korean War. This led to a worldwide economic boom, and affected the economy favourably. A combination of increased exports, partly for United States military purposes, and additional income from expenditures by United States military personnel in Japan, led to a large increase in foreign currency inflows. This was used for increased imports of foreign technology and large investments in capital goods. By the end of the Korean War the economy had been put firmly on the rapid growth path (Pilat 1994: 16ff).

The American-drafted 1947 constitution was a matter very different from the Meiji constitution. There was an intensive debate in Occupation circles concerning the future of the Emperor. Eventually he was stripped of all powers and designated the "symbol of the state" rather than "head of the state". Sovereignty now rested with the Japanese people, who elected a parliament (Diet) to which the Cabinet was responsible. Women's suffrage was introduced for the first time and local autonomy was adopted as a central principle for local

and prefectural government. Japan moreover renounced the sovereign right to wage war. Left-wing parties regained the right to be politically active. Education was also reformed from the ground. Trials and forced retirements of individuals held to have been important supporters of the war took place (McCargo 2004: 30).

The most important subject to debate is why the Japanese embraced a constitution so different from the previous (1889) one. McCargo (2004: 31-33) sums up the debate: while some contend that Japan's political development, especially in the Taisho era (1912-1926), resulted in enforced democratization, and that the new constitution was a logical continuation of the path started in 1889, the other reproach the new constitution its inability to break with the past, i.e. with the evolution of business conglomerates (the *zaibatsu*, although dissolved in 1945, evolved into the new cartels, *keiretsu*) and extensive bureaucracy.

Flath (2005: 171ff) believes that the American policy toward Japan was one of the most important structural factors in explaining the discontinuities of the wartime legacies in 1946-9. On the one hand, the United States was the major initiator of change. Its democratic reforms considerably changed Japan's economic and social structures. On the other hand, the US policy also created a favourable environment for many elements of the wartime system to continue. It indeed demilitarized the Japanese economy. At the same time, however, it strengthened the position of bureaucrats in policy making and enabled the state to break down the barriers of bureaucratic sectionalism.

As for the economic reform introduced by the 1947 Constitution, the changes were remarkable. An extensive land reform was implemented: no individual was allowed to hold more than about 7.5 acres of land, which had the effect of bringing rural landlordism to an end. However, due to the outbreak of the Cold War, the US policy towards Japan completely changed, which is notorious today as the "reverse course". MacArthur's initial enthusiasm for building up countervailing left-wing forces against the nationalist military in

Japan now faded. The US new top priority in Japan was forging an economically strong and self-sufficient nation, the task overseen by the American banker Joseph Dodge (McCargo 2004: 29).

After the signing of the Treaty of San Francisco in 1951, by which it was confirmed that Japan would renounce all its territories conquered after 1854, the Occupation formally ended in 1952. However, Japan still bears the stamp of laws and regulations enacted during the period of the Occupation (Flath 2005: 192).

Although he believes that the Dodge line was crucial for the further economic development of Japan, Flath himself (2000: 171) argues that the seriousness of the economic crisis and the perception of national isolation in the early postwar period also helped the developmental ideology to prevail in state industrial policy. Despite strong challenges from Western individualism and Marxist class analysis, the nation-state remained the unit of analysis in Japanese economic thinking and the state-centred ideology prevailed in policy debates. This pro-state orientation was strengthened by the perception of Japan's national isolation and by the distrust of the American policy concerning Japan postwar reconstruction.

The same author finally makes a significant comment on the interaction of the state and the private sector. Especially after the World War II, the private sector not only depended on direct bureaucratic intervention, but it also encouraged the development of nonmarket governance structures. Clearly, in the ideology of the managed economy, the profit motive of private companies was thought to conflict with national goals. The state concentrated on how to make individual companies function better as part of the entire economic system under the guidance of the state, rather than on how to help them make profits. This is an important facet of the early Japanese developmentalism, which I will approach in the next chapter.

As for the last 55 years after the Occupation, Japan's political history has been less turbulent (from 1989, with the new Emperor Akihito, started an era of Heisei, i.e. "peace everywhere"). A brief overview of the modern Japanese history in a very instructive work by Sabouret et al. (2005: 378-413) informs that, quickly after the entering into force of the 1947 Constitution, a military group of sympathizers of communism was excluded from an official service. Soon, these will form a terrorist group, the "Japanese red army."

Since Japan accepted, by means of its new Constitution in Article 9, never to wage war anymore, its security depended entirely on the United States, with which it signed a treaty on mutual security. In 1955, socialist party reunited. Moreover, in the same year, the most important and powerful Japanese political party, Liberal Democratic Party, was created and immediately gained power. It has been incumbent since, with the exception of 1994/95, when the socialist government was shortly in power. The merger of two conservative parties to create the LDP thus marked the beginning of a period of one-party dominance which lasted almost four decades, this period being known as the 1955 system (McCargo 2004: 38).

When in 1989 Emperor Hirohito died, Akihito inherited the throne as the 125th Emperor of Japan and the Heisei period started (*peace everywhere*). In this context, it is important to mention that during the previous 50 years, Japan has tried to normalize its relations with China. These are now still far from ideal, but the progress, although slow, has been visible. For instance, Japan signed a treaty on commerce with China in 1974. In 1978, Deng Xiaoping visited Japan and two countries ratified a Treaty of Peace and Friendship (Sabouret 2005: 412). During the incumbency of Prime Minister Koizumi, however, in 2005 the relations again deteriorated due to the revisionist policies concerning the history textbooks (especially concerning the 1937 Nanking massacres). Many fear that the incumbent prime minister Taro Aso will contribute to a new deterioration of Sino-Japanese relations, despite the efforts made by his predecessor Yasuo Fukuda.

Christensen (2007: 288) points out that while today it is relatively to reject arguments of Japanese uniqueness (*Nihonjinron*), it does not give the researchers the right to ignore Japan's indeed special political circumstances. Japan is the first non-Western state to achieve levels of political and economic development equivalent to those of Western Europe and North America. Japan is also the only democracy with completely free elections to have had one dominant political party over a fifty-year period. Its media is arguably much more docile than the media of any other advanced industrialized state.

So, in conclusion, we could say that the course of Japanese history made the country indeed special (not in a negative connotation of *Nihonjinron*, but in its neutral meaning, implying simply a difference). Japan was in many ways not comparable to "standard" Western models of politics, social organization, economic systems and society in general. To confront the riddle of economic growth in a society which is so complex, one undoubtedly has to be aware of the historical context of its economic development. Having recalled it, and this is unfortunately what many scholars do not do, now we are ready to embark upon demystifying the Japanese economic model. It is, obviously, the consequence of the complexity of societal relations in Japan, and not merely of isolated motives such as imperialism, or greed, or catching-up, or rationality, or whatsoever.

3.2. JAPANESE DEVELOPMENTALISM

In this section, will proceed in the following way. Section 3.2.1 will first sketch and compare several perspectives towards Japanese developmentalism (the neo-liberal, Marxist and Chalmers Johnson's) in relation to its qualities, its shortcomings and its future potential after the Asian crisis and the crisis of 2008. Section 3.2.2 will then recall the traditional elements of the Japanese developmental state, that is, the roles of bureaucracy, politics and business. Section 3.2.3 will conclude the chapter by assessing the traditional (Chalmers

Johnson's, or, what some call revisionist) view of the Japanese developmentalism.

3.2.1. APPRAISAL OF JAPANESE ECONOMIC DEVELOPMENTALIS

Japanese developmentalism was based in a national belief in the importance of catching up with and surpassing the advanced economies of the West. Yamamura and Streeck (2003) argue that the crucial tenet of Japanese developmentalism is the high long-term performance of the economy which can be most effectively maintained by increasing exports of successively more advanced manufactured products. Such a model basically assumes three relations of cooperation: the relation between government (and bureaucracy, in Japan primarily MITI) and industry; long-term, intensive and multifaceted relations between firms (keiretsu); and labour-management relations within large firms (Yamamura and Streeck 2003: 5ff).

This view is rather common – it is a standard perspective. On the other hand, it is disputed by certain authors as far as the importance of export-led growth is concerned (Stiglitz 1996, Lawrence and Weinstein 1999). Others deny the importance of business conglomerates (Miwa and Ramseyer 2006), and some question the positive role of the bureaucracy and politics (Trevor 2001, Beason and Patterson 2004). Some scholars (e.g. Burkett and Hart-Landsberg 2000, Schoppa 2006) doubt that the managers of Japanese firms really cooperated with the labour during the high-growth era.

After 1973, growth in Japan has slowed sharply, although the average growth rate of 3.5 percent per year up to the early 1990s exceeded that of other industrialized economies (Kokko 2002). As 1990s began it became evident that the bubble boom had in fact been the twilight of Japanese developmentalism, and the Asian crisis seemed to have the final impact. Nevertheless, although significant erosion and adaptation have taken place, the core characteristics of the Japanese institutional configuration are still intact. Vogel (2003) holds that

the future of Japanese developmentalism depends on technological and societal shifts yet to come. Japan is adjusting to new challenges, by reorganizing rather than by dismantling.

In order to understand Japanese model, we have to understand its components. The following section will hopefully shed some light on the notion: it will compare the Anglo-Saxon capitalism with Japanese developmentalism (3.2.1.1); it will then point out the critique of Marxism towards Japanese developmentalism (3.2.1.2); finally, it will present the notion as seen by its founder, Chalmers Johnson (3.2.1.3).

3.2.1.1. ANGLO-SAXON CAPITALISM VS. JAPANESE DEVELOPMENTALISM: THEORY AND PRACTICE

In fact, how alternative has Japan been? Certainly, its development has been regarded as a great economic challenge to Western countries. Still more profound challenge, however, is intellectual, because the Japanese developmentalism represents a different tradition in the history of economic thinking. Gao (1997: 64-66) regards the Japanese experience in economic development as one which has demonstrated an alternative path of industrialization to the Anglo-Saxon experience. The Japanese developmentalism takes historic facts into consideration, unlike neoclassical school, which is ahistorical.

Besides that, Gao emphasizes one further difference: neoclassical economics focuses on a particular aspect of virtually all human behaviour and investigates facts and discovers truths about them. In contrast, the Japanese developmentalism emphasizes the concrete processes of production, distribution, exchange, and consumption of goods and services in the Japanese industrialization. The Japanese developmentalism rejects neoclassical economists' claim that economic laws are universal and insists rather on the relativity of economic theories.

Japanese economics (*Jissen-ha*) is different because its theoretical propositions were derived through induction. They were based on empirical studies of economic reality and were concerned with the timely issues confronted by the Japanese economy. Moreover, The Japanese developmentalism treats economic phenomena institutionally, emphasizing how the nation-state increases its wealth through promoting the power of production by employing a state industrial policy, business networks and management (Gao 1997: 64-66).

Although they have different theoretical roots, the *Jissen-ha* and the neoclassical economics had their paths crossed. The Japanese developmentalism underwent a drastic transition in the 1950s in the new environment defined by liberal capitalism. According to McCargo (2004), in this transition two dynamic forces were at work. On the one hand, the Dodge Line (1949) ended the era of the managed economy. It raised the issue of efficiency, forcing Japanese industrial policy to change the wartime version of direct bureaucratic control over the distribution of materials and prices to a new form of state intervention that could not only allocate resources strategically, but also strengthen the production efficiency of Japanese companies to survive in the international competition. All these characteristics listed by McCargo contributed to what I call in this chapter a *dokuji no moderu*, or Japan's own model.

On the other hand, the Korean War (1950-1953) not only provided the Japanese with an opportunity to survive the stabilization panic caused by the Dodge Plan and to accumulate capital, it also demonstrated the possibility of continuing the military version of developmentalism in one way or another. Ironically, the outbreak of the Korean War provided however a much-needed boost to Japan's economy, producing huge orders for uniforms and equipments. Japan itself was not involved in the War because it was not allowed, according to its 1947 Constitution. By this manner it was able to reap considerable economic benefits from the existence of diverse wars in Asia (Korea, later Vietnam) (McCargo 2004: 37).

Japan was overwhelmed by the choice between these two alternatives, i.e. market liberalism and developmentalism, in the 1950s. In response to these challenges, two strategies were formulated. Prime Minister Yoshida Shigeru presented a corresponding political strategy. He claimed that, by allying with the United States, Japan would not only receive economic reconstruction, but also political protection. The “Yoshida doctrine” assured that Japan relied on the United States to provide for its national security needs, concentrating instead on economic growth and national reconstruction (McCargo 2004: 38).

On the other hand, Japan also formulated its economic strategy. Schumpeter’s theory of innovation changed the way Japanese economists understood the dynamics of long-term economic growth. It also reformulated the Japanese definition of comparative advantage in international trade in terms of production technology (Gao 1997: 222). In 1955 Japan also joined the newly-established GATT, which helped it to gain access to export markets. The membership in the International Monetary Fund helped Japan to obtain secure supplies of raw materials for its industrial output, given its limited domestic sources of raw materials. Although highly vulnerable to external pressures, Japan’s exports increased by an average of 17 percent from 1953 to 1965 (McCargo 2004: 41).

Under the new definition of dynamic comparative advantages (i.e., the state should not wait until comparative advantages arise, but it should create them itself), the wartime focus on the development of heavy-chemical industries obtained new significance in state industrial policy. After the state revised the antimonopoly law twice, former *zaibatsu* companies began to organize themselves into *keiretsu*. The business groups, sustained by the main bank system, began to dominate the market again. Meanwhile, cartels also became legal again to combat the economic recession and to rationalize the industrial structure (Gao 1997: 222ff).

Gao (1997: 224) then goes on to show that in the 1950s, labour and management were still far from working out a mutually accepted institutional

solution that would embody the developmental vision. Finally, although the state changed the means of intervention, the economy was still heavily controlled. Market forces began to improve the competitiveness of Japanese companies, but foreign products had not joined the competition in Japan's domestic markets.

What has been constant throughout the history of the Japanese developmentalism, though, are high saving rates, as shown by McCargo (2004: 43). Saving rates in Japan are exceptionally high, with a variety of explanations provided, such as cultural interpretations, deficiencies in the social security system, the bonus system, tax incentives, high housing prices etc. Be that as it may, net household saving as a percentage of disposable household income have been at least twice higher than in the United States or the United Kingdom.

3.2.1.2. MARXISM VS. JAPANESE DEVELOPMENTALISM

Marxists explain the Japanese developmentalism in a slightly different fashion. Burkett and Hart-Landsberg (2000) offer a Marxist approach to East Asian development and crisis of the 1990s. Such an approach recognizes that the region's competitive successes involved not just effective management of production, investment, and macroeconomic policies, but also effective extraction of surplus values from workers by (state and private) capital and its effective conversion into means of expanded exploitation and monetary accumulation. The conclusion is that as individual enterprises, nations and regions are more or less successful in appropriating social resources and applying them to the exploitation of workers, the resulting capitalist development is necessarily uneven.

The non-Marxist perspectives, say Burkett and Hart-Landsberg (2000: 45), all suffer from faulty conceptions of Japanese capitalism and its international expansion. Unlike Marxism, neo-liberalism and structural institutionalism both focus on national development-policy options within a given international context. As a result, each provides at most a partial understanding

of Japan's crucial influence on East Asian development as a regional whole (ibid).

Furthermore, Burkett and Hart-Landsberg (2000:46) criticize what they call a left-liberal consensus (LLC), which in fact broadly corresponds to what developmental state scholars understand as the Japanese developmentalism. The LLC, Marxist authors assert, sees Japanese capitalism as superior to US capitalism because of its greater rate of savings and more efficient allocation of labour-management relations, more cooperative and efficient allocation to labour-management relations, and more humane and efficient approach to structuring international economic relations. Burkett and Hart-Landsberg criticize, however, that the LLC failed to examine this investment regime in terms of the basic class relations of the Japanese economy (2000: 49).

They claim that the high Japanese savings rate is due to the extremely high housing costs faced by Japanese workers. High savings have also been a response to the country's relatively small welfare state. The tradition of high Japanese household savings in reality "represents a consistent long-term policy for a specific form of high capital accumulation" (Halliday 1978: 231, quoted in Burkett and Hart-Landsberg 2000: 47).

As for, according to many, the most impressive feature of the Japanese economy, lifetime employment, two Marxist scholars argue that in fact it has never covered more than 30 percent of all workers in Japan, with a concentration of male workers in large private firms and the government (Burkett and Hart-Landsberg 2000: 52). Even for the permanent workers in the big Japanese corporations, lifetime employment normally ends with a forced retirement between the ages of 50 and 60, followed by many additional years of full-time labour in smaller subcontracting enterprises, contingent corporate positions or self-employment (Takashi 1997, quoted in Burkett and Hart-Landsberg 2000: 52ff).

Their further reproaches are that developmentalism or, as they call it, LLC, employed an ahistorical and nonholistic approach. LLC-type analyses derive development visions from the requirements of capitalist competition rather than from critical engagement with popular struggles against the exploitation and social costs built into this competition. LLC makes in their opinion international solidarity difficult if not impossible to build (Burkett and Hart-Landsberg 2000: 58).

Burkett and Hart-Landsberg further claim to show how Japanese capitalist model that promoted a concentrated and privileged industrial core, stressed production for export, captured overseas markets through military and then economic power and maintained its competitiveness through the exploitation and repression of its workers, worked. Their analysis suggests that Japan's current economic difficulties do not involve any crisis of socialism or even a relatively egalitarian capitalism. Rather, they represent the exhaustion of the world's most efficient and exploitative version of export-driven capitalism.

They pinpoint that "Japan's export-oriented scrap-and-build accumulation was a highly competitive variant of capitalistic creative destruction" (Burkett and Hart-Landsberg 2000: 121). Following the argument that by installing more advanced technologies that reduce unit labour costs, firms expand productive capacity beyond the extent of the market. This explains why capitalist competition takes the form of a struggle for export markets in which firms from different countries compete for shares in the total value added. Finally, the state disposed with bureaucracy that actively intervened in the economy to promote an externally oriented accumulation process at the expense of working people in Japan and the rest of Asia (Burkett and Hart-Landsberg 2000: 78).

In conclusion, Marxian analysis wants to distinguish itself from other approaches (compare e.g. Bramble 1994, Radice 1999). Neo-liberals, they say, have aimed to demonstrate that Japan's planning agencies had shown themselves incapable of managing Japan's movement toward a high-consumption economy. Statists and developmental state theorists, again, think

that Japan's economic problems had been overestimated and country's planning apparatus is still quite effective. Marxists say that both claims are not true, since the Japanese capital and its state are unable to utilize society's tremendous potential surplus for human-development ends (Burkett and Hart-Landsberg 2000: 149).

However, Komiya (1993) criticizes this scheme by defending the Japanese developmentalism in three points raised by the Marxists. The first is the Marxist claim whereby the government and capitalists collaborate to exploit workers and the public at large. Komiya admits that ownership and management of firms are probably more thoroughly separated in post-war Japan than in most other countries including the US. Generally, salaried executives rather than capitalists in the Anglo-Saxon implication of the word, dominate the management of big business. These salaried executives pay less attention to profits and lay more emphasis on growth of the firm than managers in other countries, so long as the profit rate is higher than a certain minimum considered as acceptable to the industry.

Second, most industries where the government has intervened extensively (iron, steel, shipbuilding, shipping, petroleum refining, chemicals, petrochemicals and electric power) have been characterized by a low rate of profit throughout the high growth period. These industries and firms have grown and their wage rates have risen rapidly, but their profit rates have remained relatively low.

Third, Japan's ruling Conservative government has been closely associated with the interests of big business and the relatively rich, and has done many things which are considered to be favourable to them and little if anything which was opposed by them. However, the functioning of the highly competitive market mechanism of the post-war Japanese economy is such that big businesses cannot retain for themselves all or most of the benefits of industrial policies which are supposed to be favourable to them (Komiya 1993: 309).

Moreover, there is an additional argument in favour of Japanese development, which is that Japan's growth was not primarily export-led. As already stated, authors such as Boltho (1996), Stiglitz (1996), Lawrence and Weinstein (1999, 2001) suggest that Japanese growth was not primarily export-led, but that it was propelled by domestic production, and that imports were also very significant in the post-war growth. Thus, the Marxist thesis about the exploitative growth seems to be exaggerated. Moreover, the statement that the Japanese developmentalism is a model which impedes international cooperation and solidarity, since Japan is characterized by high rates of official developmental assistance for poor countries, as it will be mentioned later. Finally, Marxists also missed the point by referring to capitalist destruction, since the model is one of the most creative so far. I will elaborate it in more detail in section 3.2.2. For now, let us how the Japanese developmentalism was seen by the man who recognized it first, Chalmers Johnson.

3.2.1.3 CHALMERS JOHNSON AND HIS “SCHOOLS OF THOUGHT”

The pioneer of the discussion on the Japanese developmentalism, Chalmers Johnson, goes beyond the usual neo-liberalism vs. Marxism debates. Johnson is not interested in what both schools have to say, but simply in why the miracle in Japan occurred. He claims that the development of the post-war Japanese state had its roots in the economic initiatives of the 1930s.

In this sense the experience of the 1930s and the 1940s was not by any means totally negative for post-war Japan; these were the years in which the managerial tools of developmental state were first tested (Johnson 1982: 308). Hence he distinguishes between three directions in which the debate on developmentalism goes. The first school assumes, simply as it is, a miracle. Charles Kindleberger refers to a “riddle” of how Japanese “produced Keynesian policies as early as 1932 without a Keynes” (Johnson 1982: 6).

A second set of explanations belongs to the socioeconomic school, or what Johnson called “anything-but-politics” approach to the “miracle” research. This school includes four major types of analysis:

- the “national character – basic values – consensus” analysis, which Johnson holds for overgeneralized;
- the “no-miracle-occurred” analysis, which rejects the notions of “industrial structure”, “coordination of investment”, “public-private cooperation” and the whole notion of developmental state;
- the “unique-structural-features” approach (unusual Japanese institutions), which emphasizes “three sacred treasures” – the lifetime employment system, the seniority wage system and enterprise unionism, and
- the “free-ride” analysis, which argues that Japan is the beneficiary of its postwar alliance with the US due to its lack of defence expenditures, ready access to its major export market, and relatively cheap transfers of technology (Johnson 1982: 13-15).

Final school, in which Johnson places himself, is the one that stresses the role of developmental state in the economic miracle. Why? “It always seems to raise difficulties in the Anglo-American countries, where the existence of developmental state in any form other than the communist state has largely been forgotten or ignored as a result of the years of disputation with Marxist-Leninists. Japan’s political economy can be located precisely in the line of descent from the German Historical School - sometimes labelled ‘economic nationalism’, Handelspolitik or neomercantilism...” (Johnson 1982: 17).

Rather than “plan-ideological”, developmental state of Japan after the Second World War was “plan-rational” (ibid). As we have seen in the chapter introducing the notion of a developmental state, Johnson holds that precisely this path was crucial for the further Japanese economic development. In the similar vein, Gao (1997: 64) asserts that this tradition competes with the

tradition of neoclassical economics, because *the Japanese developmentalism treats industrialization, and not capitalism, as its subject.*

3.2.2. ELEMENTS OF THE JAPANESE DEVELOPMENTAL STATE

Despite all the research conducted on it, do we know the real truth about the Japanese economic growth? “Sometimes the *honne* (genuinely felt) element could emerge (...). But when we speak to foreigners, often we still speak *tatemae* (false front),” Jun Eto from the Tokyo Institute of Technology said once (quoted in Trevor 2001:41). This, again, proves that the Japanese developmentalism goes beyond the economy. This section will however restrict to economy and attempt to investigate what happened during the post-war growth. In chapter, 6 the thesis will then try to exceed the limits of growth explanations.

Although the Meiji system already provided for the institutional basics of the future economic growth and development, the economy before the World War II at the same time possessed many characteristics of a classic market economy. Okazaki (1998) emphasizes that Japanese corporations operated under a system of corporate governance that resembled the classic joint-stock corporation. The main actors in this system, namely the conglomerates or *zaibatsu* and prominent private investors, also played an intermediary role in the relationship between the government and the private sector.

The economic mobilization that accompanied the Second World War upset and changed Japan’s economic system insofar as the government introduced planning and control systems to manage the wartime economy. The Japanese market economy can therefore be considered unique because, although it is certainly a market economy, certain key elements of its systemic foundation were introduced under a planned and controlled economic system (Okazaki 1998: 29).

Japan has made two great strides forward internationalization in the modern era according to Gibney (1998). The first era brought the dynamic of the young Meiji reformers. In less than two decades, in a 19th century cultural revolution that ranks with the 18th century American and French revolutions, the Japanese successfully turned a declining and semi-feudal shogunate into a modern nation-state. In the end, however, the high ideals of Meiji were subverted by military nationalists, who led the nation into a disastrous war.

Next came MacArthur “democratization” and its aftermath. This time, however, instead of the implicit threat of Commodore Perry’s offshore gunboats, there marched in the Military Police and Constitution-makers of American military occupation. The Japanese people welcomed General MacArthur as readily as they had canonized Emperor Meiji (Gibney 1998: 12).

But, then, what is the Japanese engine of growth? And how did the Japanese manage to combine two at least in theory completely irreconcilable components? Trevor (2001) is sceptical and sticks to the “iron triangle” of Japanese power. What he sees in a rather negative context, namely as power holders who simply can not be dethroned, we can also see as the pillars of the Japanese developmental state: bureaucrats, politicians and big businesses. On the contrary, Johnson (1982: 315-319) names all of these as a source of growth. Let us take a closer look at each of these elements in following sections.

3.2.2.1. JAPANESE BUREAUCRACY

In his essay “Japan: Who Governs?” which had appeared 7 years before his first famous book was published, Chalmers Johnson asserts that the bureaucracy did not rule in a vacuum in Japan, but it held an ascendant position and was likely to continue to do so (Johnson 1975). He was not wrong. Bureaucrats and politicians in Japan are considered to constitute two different types of elites (Muramatsu and Krauss 1984). Both elites have recognized roles and influence in the policy-making process, although there are still some

differences in those roles and a rather large difference in the styles in which they approach and perform those roles.

The difference lies in the following: bureaucrats are often seen as stabilizers and politicians as energizers. In the late 1980s, there was some evidence that well-established interest groups relate mainly to bureaucratic agencies, while newer groups turn to political parties (Campbell 1989). Johnson (1982) also sees the bureaucracy as the source of energy and change: the LDP's function, for instance, was often to distribute government support largely to social groups who do not benefit directly from economic growth policies (small businesses, farmers).

Campbell tries to explain his argument about stabilizers and energizers. First, different communities have different characteristics: politicians might play an energizing role in agriculture and a stabilizing role in industrial policy. Second, in Japan it appears that politicians are more likely to be energizers in the general arena. Bureaucrats are still considered to be the main force of change in more particular policy communities, although this started to change with democratization reforms (see e.g. Mari 2008).

But why are politicians and bureaucrats in Japan so different? Johnson (1982) is concerned to explain why the discrepancy between the formal authority of either the Emperor (prewar) or the Diet (postwar) and the actual powers of the state bureaucracy exists and persists and why this discrepancy contributes to the success of developmental state (1982: 35). He also makes the distinction between *tatemae* and *honne* (unlike Trevor (2001), Johnson does not explain these concepts as “false front” and “true face”, but by the notions of “principle” and “actual practice”. In this section, I will firstly try to explain the negative and weak points of the Japanese bureaucracy after World War II. Then, I will go on by showing, on the example of administrative guidance and pilot development agencies, the brighter side of the Japanese bureaucracy.

A. BUREAUCRACY AS THE PART OF AN “IRON TRIANGLE”

Bureaucracy in Japan has been always regarded from a certain distance. The common term for governmental authorities is “those above” (*okami*). It is also said that Japanese do not normally question the authority of the government because they respect its “samurai sword” (*denka no hoto*) (Johnson 1982: 40). In the era of high growth, ministries were the most important bureaucratic institutions. Even after 1965, after which many scholars agree that the control of the Ministry of International Trade and Industry (MITI) actually diminished, the presence of bureaucracy is far from gone. Actually, as Trevor (2001: 138) quotes, between 1985 and 1991 most ministries increased the number of types of licences under their control.

In 1991, the Ministry of International Trade and Industry (MITI) had 1916 licences, the Ministry of Finance (MOF) 1210, and the Ministry of Health and Agriculture, Fisheries and Food (MAFF) 1315, the Ministry of Health and Welfare (MHW) 1106, down to the Ministry of Education with 312 licences (*ibid*). Trevor therefore concludes: “Under the guise of protecting the public (from what?), preventing “disorder in the market” or disorderly marketing and guiding the economy in the public interest, the bureaucrats act to preserve cozy cartels in business, which the established companies and their managers certainly appreciate.”

Moreover, Trevor criticizes the fact that officials in the top ministries (MOF, MITI), are recognized as the elite of the elite, produced by the grinding examination system and that their power and influence give them a prestige in the wider society seldom found in other industrialized societies. Japanese officials have the power to make laws, in a way that gives themselves the maximum amount of power in their enforcement (*ibid*).

After the high-growth phase ended, in the late 1970s and the early 1980s, Japanese inflows of foreign direct investment fell, with little prospect of appreciable change in sight. In this context neither MITI’s administrative

guidance nor America's official pressure could alter the pace and magnitude of that investment. Rather, control over timing and substance of liberalization remained in the hands of Japanese oligopolists, who proved reluctant to respond to any economic pressures initiated (Encarnation and Mason 1990). Naoto Kan, leader of the Democratic Party of Japan, an opposition party of the incumbent Liberal Democratic Party, in 1998 summarized the problem. "Bureaucrats", he said, "are like an airplane put on automatic pilot. When Japan was in the middle of high economic growth, their pursuit of a pre-set goal worked well. But now, we cannot afford to fly automatic pilot any more" (Gibney 1998: 11).

Bureaucrats are in this view not only the marionettes of the system, they are also dependent on politicians. In this context, Grimes (2001) argues that the abilities bureaucrats have in competition with politicians they do have are based on real, institutional factors that define the constraints of both bureaucracies and political parties. Inevitably, that means considerable variance in the power balance among competing actors, depending both bureaucracies and political parties. Inevitably, that means considerable variance in the power balance among competing actors, depending on the issue area (Grimes 2001: 221ff).

In the similar vein, Ramseyer and Rosenbluth (1993: 122) argue that bureaucrats in Japan are not independent. The Japanese Diet maintains effective control over the processes of policy making and implementation by forcing bureaucrats to "write the bills that will best promote the LDP electoral odds, and administer them in ways that will best lead to the same end." Bureaucrats have no choice because, if they oppose, "LDP leaders will not pass the statutes they write, will legislate against the regulations they promulgate, and may do what they can to see that their careers go nowhere."

Another problem with bureaucrats in Japan, and almost everywhere else, is corruption. The immanent example of corrupt bureaucrats is doubtless the saga of Tanaka Kakuei and the Lockheed bribery that has rocked Japan since 1976. Tanaka Kakuei was a controversial prime minister famous because he

had never completed any university education. He was found guilty for being bribed by the American company Lockheed, but he was never accused since he died during his trial in 1990. His case pointed to corruption and vested interests in Japan's bureaucratic circles. In his essay describing the case of Kakuei Tanaka, Chalmers Johnson concluded that the old bureaucratic structure of Tanaka's time has not disappeared. However, Japan learned much from this case. In Johnson's opinion, just as the Japanese owe their postwar foreign policy primarily to Shigeru Yoshida and their economic achievements primarily to Ikeda, they owe their belated democratization of the political system primarily to Tanaka Kakuei (Johnson 1986: 28).

Another, this time Japan-specific case which has been criticized by many, is the phenomenon of *amakudari*. An *amakudari* is a former government official who, after retirement from long years of civil service, is reemployed in the private or quasi-private sector and begins a "second life" in which he draws heavily on the expertise and the personal relations that he accumulated in his "first life" as a bureaucrat (Schaede 1998: 160). *Amakudari* means literally "descent from heaven".

These officials create elite personnel networks of senior bureaucrats, top business leaders, and politicians. Moreover, the members of these networks have a homogenous outlook based on their education at the University of Tokyo. Finally, there is a clear stratification or hierarchy in the networks based on the ministries' participation in these *amakudari* networks. To sum up, network relations are negotiated, mutual, and reciprocal relations between the government and various segments of society (Colignon and Usui 2003: 80).

The *amakudari* system is based on three different sets of incentives by the three parties involved. The government aims to ensure the implementation of regulation. The government official aims to increase his lifetime employment income by assuming higher-paying positions after early retirement. Finally, corporations pursue three simultaneous goals: to ensure access to, to ensure

intermediation in times of clashes of interests with the government, and to lobby under the framework of encompassing regulation (Schaede 1998:167).

Besides that, Colignon and Usui (2003: 55ff) add in this context that *amakudari* is a personnel system that is shaped by and part of the dynamics of politics among the ministries and the public and private sectors. Bureaucrats are more than self-interested individuals – they constitute a status group. *Amakudari*, the end point of a bureaucrat's career, is institutionalized – it connects a matrix of organizations across a number of institutional spheres. *Amakudari* is also the product of competition among ministries that exemplifies the development of sectionalism, an often criticized feature of the Japanese bureaucratic system. Ministries and agencies responded to the shortage of administrative resources and to a series of administrative reforms by extending their administrative and regulatory control and creating new networks of *amakudari*.

Colignon and Usui (2003:54) then go on to enumerate four key features that helped compose or combine the different conceptions of *amakudari*. First, *amakudari* positions define a formal and codified territory of positions for the ministry. Second, the responsibility for the placement of and the coordination of the placement of ex-officials is a more or less formally centralized responsibility of a specific office of the ministry. Third, there are certain cultural norms and expectations that surround *amakudari* movements involving appropriate placement and procedures for placements. Fourth, these *amakudari* personnel provide tangible benefits to private organizations' abilities to compete in a regulated economy substantially driven by government grants and contracts. *Amakudari* creates a linkage between the most powerful segments of the bureaucracy and the more established segments of the private sector.

However, *amakudari* are not the only Japanese particularity, yet they are most often discussed in the literature. Analogically to the reemployment of *amakudari* in the private companies, *yokosuberi* is the postretirement path of high-ranking bureaucrats to public corporations. Finally, *wataridori* are the

officials reemployed subsequent to the first reemployment position after leaving the ministry (i.e. second or subsequent *amakudari* or *yokusuberi*). The examination of *wataridori* provides a description of the structure and process of serial reemployment of top-level bureaucrats. (Colignon and Usui 2003: 27ff). Having said that, it becomes clear that the process is multifaceted and interlinked.

Contrary to widespread assumptions, the phenomenon of government Old Boys, or *amakudari*, in large Japanese firms has increased, and not declined, in the 1990s. This contradicts the notion that the regulatory system of developmental state is slowly disappearing. Schaede (1998) concludes therefore that the management of regulation model shows why government and business interact in the process of public and corporate strategy formulation (1998: 167).

Given the assumption that *amakudari* relations are strong and resistant to any societal changes, Colignon and Usui (2003: 27ff) ask themselves about the future of the *amakudari* phenomenon and power structures, whereby they define a power structure as a network of roles and organizations within a society that is responsible for maintaining the general social structure and shaping new policy initiatives. The crucial questions that persist include for them the breadth, extent and structure of *amakudari* networks and how they change over time. A complex network of social relations maintains elites in their top positions in the key positions of society. The two scholars' conclusion is that the domination component of the elite policy networks is the subordination of electoral politics and subgroups (the masses) to the cohesive alliance of the various institutional elites.

Nevertheless, there are also somewhat more positive interpretations of the *amakudari* phenomenon. According to Sakakibara (1998:80), competition between ministry-based networks has worked to maximize the resources within a particular ministry and inter-ministry competition has pushed aggressive policy implementation. Bureaucrats created industry associations and public

corporations and widened their networks. This was useful because through this the bureaucrats “created “legs and arms” through which they can exercise their influence rather than creating new intra-ministry organizations or adding personnel” (Sakakibara 1998:80).

Interestingly, Sakakibara also connects the persistence of *amakudari* today with the advent of an extreme variety of individualism in the 1980s (dubbed “me-ism” in Japan) and a rigidly classical form of *laissez-faire* policy that would leave everything in the hands of the market. The pursuit of self-interest and money-worship became more pronounced than ever in that time. *Amakudari* are no exception – and given the tradition, why not go on? However, given their tradition and longevity that both well exceed the advent of neo-liberalism, I am rather sceptical about the *amakudari* flourished due to neo-liberal reforms. They have their roots deep in Japanese state organization.

B. BUREAUCRACY AS PILLAR OF PILOT AGENCIES

Yet, as always, there is another side of the coin. In his list of “market-conforming methods of intervention”, Chalmers Johnson particularly emphasizes administrative guidance (Johnson 1982: 318). Bureaucracy is an important means of interpreting law. The Japanese generally draft short and highly generalized laws. They give concrete meaning to these laws through bureaucratically originated cabinet orders, ordinances, rules, and administrative guidance.

Beason and Patterson (2004: 16ff) interpret Johnson’s argument as revisionist. They add that revisionists have found basically three reasons for the importance of bureaucracy. The first is rooted in the ongoing influence of the Japanese history and culture, specifically the notion that Japan’s political past is one of authoritarianism where elected officials were hardly the dominant class. The second reason of the revisionists concerns the conditions that prevailed during the Allied Occupation of Japan and, specifically, how these conditions

helped increase bureaucratic power at the expense of Japan's politicians. The third reason finally concerns how certain actions taken by bureaucrats in the Occupation and post-Occupation periods helped advance their power and diminish that of Japan's elected Diet members.

Inkster (2001) traces the beginnings of the powerful bureaucracy back to the Meiji period. Government activities then included social control, modelling factories and project construction, stipend commutation which clarified social position and produced financial resources, infrastructural, especially transport, developments which reduced private sector costs and extended markets, labour force education and training which reduced costs and induced further organisation innovations (Inkster 2001: 86).

Let us take a closer look. Has the dominance of bureaucracy always been necessarily bad? The best help with answering this is a pilot organization like MITI. This ministry was charged with organizing and steering economic growth, and it had all the power to do so. The problem with such pilot organizations, as quoted by Johnson, is to find the mix of power needed by the pilot agency without either giving it control over so many sectors as to make it all-powerful or so few as to make it ineffective (Johnson 1982: 319).

Ministries were and are not almighty. While investigating the Japanese trade policy, Mikanagi (1996) analyzes the structure of Japanese bureaucracy. She shows that, despite its centrality, the bureaucracy faces a number of constraints placed on its ability to liberalize markets. Most importantly, the bureaucracy is not a unified actor that single-mindedly pursues economic growth. It is a complex mosaic of various ministries with diverse goals which the Japanese government must satisfy. Each ministry has varying degrees of autonomy and ranges of policy instruments which may further constrain its ability to carry out market liberalization.

Mikanagi (1996) defines the autonomy of a ministry i as the degree to which it can make decisions on its own without intervention by actors external to

the ministry. Inter-ministry conflicts could be grouped into two kinds of rivalries. The first rivalry emerges when the issue is fairly new, complicated and the jurisdiction is not established, so the ministries compete for it. In the second case, when more than one ministry has legal jurisdiction, each of them will try to prove that it has the power.

The relation between ministries and the private sector is far from a classical top-down approach. Rather, it can be promotive (in case of new industries), post-promotive (in case of established industries), restructuring (in case of troubled industries) and regulatory (in case of public enterprises). Although this last remark might seem surprising, in Japan regulation does not mean state intervention in the market, but state intervention in an industry which provides public goods (Mikanagi 1996: 32).

But let us turn back to MITI. MITI is the descendant of one of the original ministries dating back to 1881, and it is certainly a “welfare community”, but it also has several characteristics that distinguish it from the other economic bureaucracies. In the post-war Japan, it was the smallest of the economic ministries in terms of personnel (only about 200 officials), and it controlled the smallest share of the general account budget (Johnson 1982: 79).

The wartime Munitions Ministry, which had reverted to its pre-war title of the Ministry of Commerce and Industry, and in 1949 adopted the name Ministry of International Trade and Industry (MITI). This Ministry was given wide-ranging authority and comprehensive responsibilities (Kokko 2002), for industrial planning, financing, enforcing mergers, setting production quotas, rationing foreign exchange, and sourcing and allocating foreign technology to individual firms.

The first phase of modern Japanese industrial policy seems was far from predicting economic miracle. Then, the things changed: economic crisis gave birth to industrial policy. The long recessions following World War I and the panic of 1927, led to the creation of Ministry of Commerce and Industry (MCI)

and to the first attempts at industrial policy. Analogically, the need for economic recovery from World War II, accompanied by the deflation panic of 1949, led to the creation of MITI and to the renewal of industrial policy (Johnson 1982: 114).

The approach in the long-term planning of the economy was in some ways similar to that in socialist economies, with one important distinction: in Japan, competition was fierce although MITI attempted to restrain it. Moreover, the government was not directly involved in manufacturing, which was the exclusive domain of private firms that were strongly motivated to increase their profits and prestige (Kokko 2002).

The role of MITI has been especially strong in the shaping and directing of industrial policy, often in close consultation with private enterprise. The purposes of industrial policy have changed over time. In the period directly following the war its aim was reconstruction and the achievement of economic independence. After 1965, MITI has become less interventionist and its policy focus has gradually changed to structural adjustment and technology policy. Apart from MITI, the Ministry of Finance and the Bank of Japan have played an important role, for instance in their targeting of investment funds (Pilat 1994: 70).

In 1949, the Allied powers introduced the Foreign Exchange and Foreign Trade Control Law. This was the main legal instrument for MITI's action. Moreover, MITI controlled investment funds, both in the government budget and in specialized credit institutions (such as the postal savings bank). These instruments gave MITI complete control over private industry through the allocation of credits and foreign exchange for imports. MITI focused on 44 "strategic" industries (including steel, shipbuilding, coal, and chemicals) which were expected to stimulate demand and production in other sectors. MITI provided the investment capital, foreign exchange, and technology needed to upgrade production (Kokko 2002: 5).

In addition to the formal groups in MITI, there were also numerous informal brainstorming institutions. Japanese analysts usually characterize the

basic outlook of MITI officials as “nationalistic” (Johnson 1982: 80). A significant part of the MITI perspective is its impatience with the Anglo-American doctrine of economic competition. After the war MITI had to reconcile itself to the occupation-fostered market system in Japan, but, as Johnson (1982: 81) stresses, it has always been hostile to American-style price competition and antitrust legislation.

The period between 1952 and 1961 was the ministry’s golden age. However, the degree of official intervention was not the same for all industries and in all periods. So, until 1955, industry was essentially operating under MITI orders, during the period between 1955 and 1960, control was managed through credit allocations, and from 1961 onwards, firms were allowed to prepare their own investment programs with “guidance” from MITI officials (Kokko 2002: 5). Okimoto (1982: 400) supports this statement. Although the degree of intervention and selection of policy instruments varied by industry, MITI intervention tended to include an extensive involvement during the early stages of an industry’s life cycle when market demand was still small.

The intervention then fell off significantly. Later however, as the industry loses comparative advantage and faces the problems of senescence – saturated markets, the loss of market share, and excess capacity, the intervention was again stronger. Okimoto depicts a number of high-technology industries clustered at their early stage – data processing, computer services, biotechnology, space, ocean development, and nuclear energy. It is then visible that administrative guidance was at its highest during the early and late phases of the industrial life cycle (Okimoto 1982: 400).

Finally, I have already indicated that bureaucrats should not be generally and necessarily put into relation with corruption. In Japan, the case of Tanaka (who, by the way, was a politician and not a bureaucrat) is so infamous that it became the only thing many Western critics point to. Komiya (1993) observes however that there have been very few cases in Japan in which high officials *in charge of industrial policies* were involved in bribery. There are two reasons for

this. For one thing, acceptance of bribes is severely punished. Another reason is that although their salaries are surprisingly low, government officials are under the lifetime employment scheme, and high officials can take prestigious and well-paid jobs after retirement from the civil service, *amakudari* (Komiya 1993: 314ff, footnote). Thus at some point, the *amakudari* system may be seen as a cure against corruption. Though one might be extremely sceptical (as I am myself) about whether this could work in any other country, obviously, in Japan, it somehow manages to work.

3.2.2.2 THE JAPANESE POLITICIANS

“Japan has first-rate industries; and tenth-rate politicians”. This is how Trevor (2001) starts his chapter about Japanese political decision-making. Moreover, he adds that what the Japanese prime minister says in the international arena is severely limited by his dependence on the special interest groups and the bureaucrats (Trevor 2001: 180). Can the role of the Japanese politicians really be reduced merely to complying with what lobbies and bureaucrats say?

As Johnson’s famous postulate “The bureaucrats rule and the politicians reign”, has been employed in virtually any context, it is always repeated that the special interest groups need the help of the politicians in lobbying for contracts, subsidies and protection from competition. Ultimately the Diet passes the legislation, although this, too, can be managed by means of the ministries issuing administrative guidance, which is for Trevor (2001:181) nothing but “a means of camouflaging what the government is doing and of preserving ‘harmony’ in the Diet.”

In order to support his critique of Japanese political system, Trevor (2001: 210) quotes Kazuo Nukazawa, the managing director of the Keidanren (the Japanese business association), who said in 1993: “We Japanese feel we have been pretty successful. Why should we change? Others who are doing worse than us should change, not us.” In other words, according to Trevor,

Japanese are sending only one message to the world: "We must change in order to remain the same." This is why Japan will never change: neither in its power structure, national economy, bureaucracy or ideology (Trevor 2001: 229).

Tiberghien (2007:127) similarly states that the appearance of bureaucratic power in Japan is deceiving since bureaucrats are not able to shape the overall agenda. Institutionally, power rather lies in the hands of politicians. Clearly, some countries and individuals are obviously frustrated about this dilemma. In the previous section I showed that bureaucrats are sometimes seen as the marionettes of politicians. In this chapter, I offer a reverse argument. In fact, none of the arguments is originally my own, and both should illustrate the state of debate about the Japanese developmental state. But we might ask whether Japan should change at all. The answer we could give for now is: Japan should adapt. However what about the real change, from the ground? This remains to be seen in this chapter.

Initially, Johnson (1982: 317) argued that the key for development is the political system in which the bureaucracy is given sufficient scope to take initiative and operate effectively. In other words, the government according to Johnson must stand ready to intervene in the work of the bureaucracy and to restrain it when it has gone too far. Still more important overall function of the government is in Johnson's view to fend off the numerous interest groups in the society, which if catered to would distort the priorities of developmental state. Johnson asserts that this is precisely what made Japanese politics different from that in Argentina, Brazil or Chile of his time. In these countries the government was rather bureaucratic-authoritarian at the time of publishing his book, in 1982.

"Japanese policymaking today involves far more complexity and far less coherence than it displayed two decades ago. If there was ever much reason to give credence to the notion of Japan Inc., there is no reason to do so in the 1980s," believes Pempel (1987: 23). He adds that in the 1980s there was already far more division within Japan over the central directions in foreign

policy, economic policy, and defense policy than had been the case when high economic growth and close ties to the US served as unifying policy umbrellas for virtually all members of Japan's conservative camp. Thus, already 20 years ago Japan started some political changes.

Two of the most important aspects of political parties are organization and ideology. Some of the opposition parties in Japan, such as the Socialists and the Komeito (Clean Government Party) emphasize membership and ideology, while the organization of the dominant party, the Liberal Democratic Party (LDP), experiences a considerable division and factionalism within the party. The importance of ideology for the LDP is minimal (Hayes 2005: 69). Probably this factor has helped it to govern over 50 years with only one interruption. From 1955 to 1993 the LDP formed coalitions with other parties when it lacked a majority of votes in parliament. But a coalition formation is not a dominant feature of Japanese parliamentary politics, in contrast to other multiparty systems (Hayes 2005: 70).

Founded in 1955, the LDP has been a predominant party from its foundation, in cycles of dominance from 1958-63, decline from 1967-76, resurgence 1979-1990, crisis in 1994-96 and a new upheaval up to the present. Generally, through the past the party disposed with vote shares from 56,6% to 35,1% (Beason and Patterson 2004: 161). Hayes (2005) notes that the key of the LDP's success is its favourable record in promoting economic prosperity. Moreover, its opposition is far from viable, and, once again, it does not mobilize voter support on the basis of its ideology or policy preferences. Rather, its prosperity is linked to the close personal bond that is maintained between voters and local political organizations (*koenkai*).

These organizations are not party mechanisms but are directly associated with the individual Diet member, who along with *koenkai* serves as a link between the voter and party factions (Hayes 2005: 70ff). The LDP embraces a conservative political philosophy although it is far from doctrinaire. The LDP divided into factions immediately upon its formation. Inter-factional

competition within the LDP is very important, because leadership selection in the LDP has traditionally involved a process of factional bargaining.

The opposition parties have, on the other hand, fairly distinctive ideologies, which they do not have to defend against competitors and have therefore been rather ideologically consistent (ibid). The Japan Socialist Party (JSP) was created in 1945, under the English name the Socialist Democratic Party (SDP), in fear not to provoke the Occupation authorities who were suspicious against the left forces. The Clean Government Party (Komeito), is the only party in post-war Japan with links to a religious organization, sponsored by Buddhism. On the other hand, the Japan Communist Party (JCP) was founded as early as in 1922, financed by the Soviet Union, is quite marginal, and so was the Democratic Socialist Party, which collapsed in 1998 (Hayes 2005: 89-02).

Politically, the LDP has often had problems with obtaining majority in both chambers. According to the 1947 Constitution, the House of Representatives or the lower house (*shugiin*), is the more powerful chamber. It selects the Prime Minister and the House of Councilors, whereas the upper house (*sangiin*) has almost no power at all to prevent the lower house in its choice. If both houses propose a Prime Minister or if the House of Councilors fails to designate a candidate within 10 days of House of Representatives' decision, then the lower house can make a final decision. The LDP often does not obtain majority in the lower house, and this is why its cabinets are frequently forced to resign.

Unlike many other Western scholars, Beason and Patterson (2004) do not think that the Japanese politics has always been rotten: "There is little to dispute that, during the period of high growth, Japan looked like a very different country than it was in the last decade. As a result, it is not unreasonable to think that, in the last several years, something has gone wrong with Japan's political-economic system" (2004:4). In fact, they find it specifically curious how the same bureaucrats, who ostensibly played a central role in Japan's post-war

economic miracle, have been unable, at a very minimum, to keep the current crisis from continuing as long as it has. The first answer Beason and Patterson provide us with is: the LDP used the tools of economic policy throughout the post-war period to serve its electoral interests.

There are many features of Japanese politics that arguably make it distinctive but perhaps most notable is the pattern of single-party predominance that defined election outcomes throughout most of the post-war period. Beason and Patterson (2004: 26) therefore give us a second possible cause of the present situation in Japan by arguing that, even if bureaucrats initiate some policy through administrative action, politicians can simply enact legislation that counters it if that is their collective desire. In the Japanese case, there seems to be a gap between what the LDP politicians expect bureaucrats to do and what Japan's bureaucrats actually do.

In my opinion, the unsuccessful crisis management in present Japan corresponds rather to this second explanation addressed by Beason and Patterson, i.e. that there is a lack of coordination between politics and bureaucracy, than in the fact that the LDP used economic policies for being re-elected. At the end of the 1960s, Diet played almost no role in setting industrial policy. The bureaucracy drafted almost all laws, and those that the government sought to have passed in general went through successfully, without amendment. The policy setters differed: from the mediating bureaus and pilot agencies (MITI), industry associations, to policy councils (*shingikai*), consultative bodies whose deliberations are referred to in the process of policy formation and whose principal members are private individuals, including former bureaucrats (Komiya 1993: 303-305).

In the 1970s and after, the trend was changed and it led to the increasing importance of the horizontal bureaus within MITI relative to the vertical bureaus. This is also when the influence of the ruling LDP and its members over industrial policy increased (*ibid*). The signs of looming trouble in Japan's political-economic system were there in the 1980. Responding to outside

pressures, Japan started introducing neo-liberal reforms and experiencing its economic downhill. The LDP reacted swiftly.

George (1981) shows how the LDP supported rural areas. Notably, the agricultural policy-making in Japan was regarded as a highly ritualized process in which an established group of participants reached a predictable schedule of decisions guided by a fixed set of party-political, organizational and bureaucratic objectives. As for businesses, the LDP helped smaller and medium-size firms in the area of access to finance, taxation and of trade (protection) (Beason and Patterson 2004: 111). However, the LDP efforts failed because the party simply did not succeed in halting the loss of support that contributed to its secular decline throughout the postwar period.

Beason and Patterson observe as a result a gap between bureaucrats and politicians. This gap may become particularly wide when the interests of politicians direct their attention to rather generalized matter, i.e. things other than the detail work of specific policies that is generally the provenance of bureaucrats. On the other hand, this gap will become very narrow when the interests of politicians behave them to focus on how bureaucrats put together and implement specific details of programs of concern (Beason and Patterson 2004: 26ff).

Differently from this rather pessimistic view, Tiberghien (2007: 106) focuses on the Asian crisis and the post-miracle period and asserts that entrepreneurial politicians, as he names them, played a key role in saving Japanese economy. The Japanese crisis of the 1990s was actually an unusual type of crisis, because it was slow and protracted. It was visible on certain indicators (non-performing loans, deflation, economic growth), but not on others (huge current account surplus, very low long-term bond interest rate, limited unemployment). The intensity of the crisis and its perception among citizens were low on average and variable from year to year.

In the post-miracle period, Tiberghien asserts, the process of reforms could only be slow and gradual. However, the political entrepreneurship of leaders such as Ryutaro Hashimoto, Koichi Kato, Taku Yamasaki, Kaoru Yosano, Keizo Obuchi and Junichiro Koizumi tipped the scale toward some of the most significant regulatory reforms. At the same time, their ability to act has been constrained due to lower political autonomy. Nevertheless, irrespective of the political moves they made, their active role showed that individuals could be heard and remarkably powerful in a system such as Japanese, for which most believe it is iron and resistant.

Different prime ministers obviously disposed of different power: as for their strategic political autonomy, Tiberghien (2007) claims it was low when the LDP had a minority in the upper house. Their ability to be successful in strategic bureaucratic delegation was changing too. The lack of direct cabinet control over the legislative agenda has often been underestimated in academic analyses of the Japanese political system, partly because of the long period of LDP dominance until 1993. Therefore, the Japanese politics really is to some extent hidden, or *tatamae*, to the outsiders. But this does not imply it is necessarily bad. It is simply different, and disposes in certain elements of efficiency many other nations can only dream of.

3.2.2.3. BIG BUSINESSES AND THEIR RELATION TO LABOUR

Finally, it is time to take a better look at the Japanese business sector, often criticized for forming powerful interest groups. Prior to the Second World War, each *zaibatsu* (property agglomeration) was a set of interrelated and interlocked commercial enterprises, closely held by the same family. The four most prominent *zaibatsu* – Mitsui, Mitsubishi, Yasuda and Sumitomo – had various origins, but the founding families of each acquired existing enterprises and established new ones throughout the Meiji era, all the while maintaining close

ownership and ultimately consolidating controlling-share interests in a family-owned holding company (Flath 2005: 47).

Mitsui specialized in banking and brokerage of international trade, diversifying its production later in mining, textiles, iron and steel. Mitsubishi specialized in shipping, later then in shipbuilding and mining, Yasuda's field was banking and insurance. Sumidomo specialized in copper mining and than, later on, in banking, coal mining, steel and copper (ibid).

The distinguishing features of the *zaibatsu* were their diversification and their close control by the founding families. By these criteria, there existed *zaibatsu* other than the four major ones: these include Furukawa, Asano, Okura, Suzuki, Nomura, Fujita, Yasukawa, Kawasaki, Iwai and Kuhara (ibid: 48). The Japanese business sector was innovative, different and special in many ways.

Primarily, the organisation of production was specific. Japanese businesses taught the rest of the world about how to use scarce resources in a lean production, they introduced just-in-time-delivery, quality circles, continuous product improvements and the system of subcontracting (Pilat 1994: 73). Moreover, Japanese firms and the Japanese state constructed a development model based on the steel industry as a generative sector that drove Japan's economic ascent. These strategies were overtaken by the world: organizational innovations in the use of long-term contracts and joint ventures in raw materials industries (Bunker and Ciccantell 2007).

Moreover, the ownership system of *zaibatsu* contributed to its success. The advantages of close ownership reside in the superior economic incentives to monitor managers. This monitoring benefits all shareholders in proportion to their holdings. Small shareholders have little to gain from actively aligning the interests of corporate managers with their own interest, and they rationally defer to large shareholders who have more of their own wealth at stake. *Zaibatsu* enterprises prospered because they were closely held firms (Flath 2005: 49).

As impressive as the *zaibatsu* empires became, they never employed a very large fraction of Japan's labour force. Cumulatively, very small firms employed far more Japanese workers in 1920 than did large firms. Agriculture was the occupation of roughly half the workforce in Japan of the 1920s and 1930s and these were overwhelmingly self-employed, many of them share tenants. Turning from agriculture to manufacturing, the persistence of small firms in Japan in the 1920s can be attributed to the extreme refinement of traditional handicrafts (ibid: 51).

After the state revised the antimonopoly law after the Second World War, former *zaibatsu* companies began to organize themselves into *keiretsu*. The business groups, sustained by the main bank system, began to dominate the market again. Meanwhile, cartels also became legal again to combat the economic recession and to rationalize the industrial structure (Gao 1997: 222ff).

There were six *keiretsu*, i.e. four *zaibatsu* mentioned above plus two newcomers, Daiichi Kangyo and Sanwa. They were assumed to have easier access to credits, since each *zaibatsu* possessed its own bank. However these banks were often demanding higher interest from the company with which they were together in a *keiretsu*, so that the *keiretsu* are often said to have had a lower profitability than they actually should have earned. Some opinions, especially Miwa and Ramseyer (2006), are rather extreme: they argue that the *keiretsu* have never actually existed. The argument, as strange as it sounds, is that the *keiretsu* were invented by the Economic Research Institute of Japan and have lived in Japanese economic history ever since, without actual existence.

Johnson (1982: 310ff) identifies three forms of state-business relationships in Japan. *Self-control* means that the state licences private enterprises to achieve developmental goals, by means of state-sponsored cartels, in which the state authorized cartels in strategic industries, but then left to the enterprises themselves the task of fashioning and operating the cartel, enabling the competition. The form of government-business relationship by means of

self-control is the one typically preferred by big businesses, and applied in particular industries in 1930s until 1960s.

The other type was a direct *state control*. It refers to the attempt to separate management from ownership and to put management under the state supervision. It was typically the form of the relationship preferred by the bureaucrats of the late 1930's and by the whole state bureaucracy during postwar reconstruction and the early stages of high-speed growth. Sometimes, this form of a state-business cooperation had a negative impact on competition. In this context, a strong tendency for an organization called *genkyoku*, whereby each industry fell under jurisdiction of a certain ministerial bureau, division, or section (Komiya 1993: 298).

The third, and the most important and successful category, is the one of public-private cooperation. Although all three types of models were employed in Japan during its pre-war, interwar and post-war period, this model brought the best results. Its principal feature was that it left the ownership and the management exclusively in private hands, while the state could focus more on the social goal-setting while not impeding competition.

The chief mechanisms of the cooperative relationship are the selective access to governmental or government-guaranteed financing, the targeted tax breaks, the government-supervised investment coordination in order to keep all participants profitable, the equitable allocation by the state of burdens during times of adversity, the governmental assistance in the commercialization and sale of products, and the governmental assistance when an industry as a whole begins to decline.

Moreover, the Japanese business has always been very well organized. Trade associations have been an important actor in the Japanese economy. Schaede (2000: 256) shows that initially, trade associations arose to fulfil the basic economic need of establishing markets. Over time, these activities expanded into rule-setting and self-regulation became a core activity of

associations. Japan's modern trade associations grew out of the *za* which emerged in the 12th century. The *za* organized and maintained markets in fixed locations. During the Tokugawa period, trade associations became more sophisticated.

However, around the end of the 19th century, as companies started to differentiate by size, large firms began to establish their own associations and enforced their negotiation position, which is why Japan is often criticized for corporatism. In this context, it should be maintained that perceptions of international weakness have rather consistently pushed for corporatist solutions in Japan, both at the level of the national political economic sectors and the state. The specific forms and the relative inclination towards or against such solutions have, of course, differed over time and from sector to sector (compare Pempel and Tsunekawa 1979).

Having sketched the most important features of the Japanese business, let us turn to Marxist criticism, which always, at least indirectly, touches the labour. The Japanese labour market is known for several distinct features, including lifetime employment, seniority wages, and enterprise unions, all said to be unique to Japan. Japanese enterprise unions are typically organized within each firm across different job specifications (across blue-collar or white-collar workers).

Moreover, blue-collar workers are treated in a more egalitarian manner to white-collar workers in Japan than they are in the US. The Japanese economy demonstrates longer work hours, but its unemployment rate is low and inflexible. Finally, there are severance payments upon retirement. Thus, Japanese workers tend to change jobs less often, to stay in a company longer and to have a steeper wage profile in comparison to Americans workers. Semi-annual bonuses amount to 15 -30 percent of annual income of Japanese workers. Another feature of the Japanese labour market is *Shunto*, the annual, synchronized "spring offensive" for contract negotiations (Ito 1996: 210-213).

The Japanese developmental state did not exist to the detriment of the welfare state. Similarly to the analysis of Weiss (1998: 119 ff) discussed in the first chapter, Manow (2001) believes that the German (a typical welfare state) and Japanese (a typical developmental state) post-war experiences and their welfare and wage regimes have developed in close correspondence with each other. While companies could stabilize their workforce by offering more favourable provisions as compared to the public schemes, the state continued to regulate company welfare tightly, to force uniform standards upon the larger part of the industry and to lend credibility to the private promises of business.

Following Komiya's analysis (1993: 159-189), a well-managed major Japanese firm in each field has developed as a carefully built organization consisting of managers at various levels, engineers, skilled workers, and other personnel, and having managerial and technological expertise in its specialized field. Most of the members of the top management of a large Japanese firm are selected from among those who have served for a long time as regular, core employees of the firm. The typical Japanese firm considers its employees, rather than shareholders, as its primary constituents.

The management of typical large Japanese firms may be conceived of the representatives of the regular core employees of the firm, rather than of the shareholders. Thus large Japanese firms come to possess certain characteristics similar to those of the "labour-managed firm". With the lifetime employment and seniority promotion systems it is advantageous for the regular, core members of a firm, that the firm continue at least to exist and to grow at a fairly rapid rate if possible. Some of the aspects of Japanese firms' behaviour are best understood in this context of the pressure from the inside towards the continued existence and a high rate of growth.

Another point which can be raised here, is that the income distribution in the post-war Japan has been relatively equal. Although reliable statistical data on income distribution are scarce, and international comparison of income distribution is extremely difficult both in practice and conceptually, it appears

that income is more nearly equally distributed in Japan than, say, West Germany or France. This is due to the land reform, *zaibatsu* dissolution, and the once-for-all-capital levy enforced immediately after the war, on the one hand, and on the other high progressive income as well as the inheritance taxation in the post-war years (Komiya 309 ff).

3.3 CONCLUSION: JAPAN, MISUNDERSTOOD?

After our discussion on the effectiveness of administrative guidance, a rather controversial claim by Chalmers Johnson leaves us with many questions: “The power of administrative guidance is rather like the grant of authority to a military commander or a ship captain to take responsibility for all matters within his jurisdiction. Administrative guidance is a perfectly logical extension of the capitalist developmental state, with its emphasis on effectiveness rather than legality” (1982: 273).

In other words, does the Japanese developmentalism conflict with democracy, as remarked in chapter 2? Does it produce a society of the elites and the governed? As many critics claim, and as we have seen in this chapter, it indeed does. Still, one should always bear in mind that a part of Western criticism (particularly from the United States) came due to their collective puzzlement with the Japanese model.

They could simply not understand how everything they were eagerly fighting against could actually exist in a country, but without a Japanese Stalin, Tito or Castro. Japan has been a democratic country since 1947, and the first Asian democracy in general. Its one-party dominance is by no means a product of dictatorship, but of a rather complex combination of circumstances. Its business sector was less oriented towards profit and more to industrial goals, and despite an orientation towards production it still reached a very high level of social equality.

Still, it would be mistaken to say that the criticism is completely unjustified. The Japanese iron bureaucracy and powerful lobbies are still today an object of contempt among the Japanese people. But, a combination of the foreign pressure and the new generations of more open and more globalization-prone Japanese, have pushed for strengthening of social groups different than merely bureaucrats and businessmen, as I will discuss in chapter 5. Hence, if we assume that one of the central characteristics of developmental states is, as stated in chapter 2, its ability to adapt and to learn from others, however without changing its own successful features, then we can assert that Japanese the developmental state is facing a real challenge today.

CHAPTER 4

CROATIA, RELIQUIAE RELIQUARIUM?

Many people around the world heard about Croatia for the first time in the early 1990s, while the country, struck by the bloody war of independence, was calling Europe and the world for help and compassion. The world was confused, for it could not identify what precisely was going on in the Balkans. Many followers of the war only had a vague idea of how the Balkans was the “barrel of gunpowder”, as the saying goes. The world had a picture of something similar to African tribes killing each other in the middle of their desert, as the notion is referred to today, rogue states. And precisely, if there is anything the Croatian people hate, it is certainly pushing them into a drawer of an unidentified Balkan tribe who suddenly decided to argue with its neighbours.

Croatia is a Central European country situated between the Pannonian Plain and the Adriatic Sea. Some claim it is geographically in the Balkans, others say it is in Central Europe. Since I am not a geography specialist, I will claim that Croatia has *culturally* and *historically* always been the part of European tradition. When the early humanism and renaissance were extremely popular in Italy, Croatian art was immediately and profoundly influenced. When Vienna decided to impose an enlightened absolutism, Croatia had to follow, and when that same Vienna was under siege of the Ottoman Empire, Croatian soldiers defended it.

Similarly, when Napoleon was at his peak, the French abolished the Republic of Dubrovnik, but also brought their revolutionary spirit to Croatia. In 1848, Europe was overwhelmed by revolutions and Croatia was no exception. I could go on, but the point is merely to assert that Croatia was never on the margin of what was happening in Europe. The point is not in patriotism or nationalism, but rather in knowing one's history well.

Croatia is bordered by Hungary to the north, Slovenia to the west, and Serbia and Montenegro and Bosnia and Herzegovina to the east. The southern border is formed by the Adriatic Sea which separates the country from Italy. The main regions are Slavonia in the East, Zagorje and Međimurje in the North, Lika and Gorski Kotar in the North- and South-West, and there are two regions on the maritime coast, the Istrian peninsula in the West and Dalmatia in the South. Administratively, Croatia consists of 20 counties and the capital city of Zagreb, and has a population of approximately 4,5 million (census 2001).

Why would that small and only recently democratized country be of interest when rethinking the concept of developmental state? For several reasons, as I will argue in following chapters. Let me point out here only the fact that developmental state addresses precisely those countries which did not industrialize along with developed nations, or whose industrialization was abruptly interrupted. Croatia, as we will see, initially followed the path of its more developed neighbours, but then the history played its crucial role as Croatia opted for an alternative way, socialism within the People's Federal Republic of Yugoslavia (from 1963 the Socialist Federal Republic of Yugoslavia).

However, as I will try to show, it would be an oversimplification to say Croatia either voluntarily accepted socialism or that it was forced to accept it. Rather, complicated historical circumstances had pushed the country into a system that it had initially accepted, because it thought there was no other alternative. Later on, Croatia regretted its choice, because it realised that there were other possibilities to choose from.

Since the starting point of this thesis is to rethink the link and relations between politics and economy, this chapter will, after reviewing Croatian modern history up to the present moment (section 4.1), go on to sketch the model of Yugoslav economy, the part of which Croatia was for more than 40 years (section 4.2). In section 4.3 I will briefly recall the conditions and achievements of Croatian transition to capitalism after 1990. I will not describe the present situation in Croatia in too much detail since the intention is to do so

in chapter 5. Finally, section 4.4 will conclude by asking what Croatia could learn from its social and economic past.

4.1 SHORT REVIEW OF THE MODERN HISTORY OF CROATIA

As a country of a very turbulent history, Croatia was ruled by different rulers for centuries. This is the fact with which any analysis of the Croatian history and society should commence. Each of these rulers imposed something new, different and characteristic for their culture and mentality. Far from being a self-sufficient society for centuries as it was the case of Japan, and analogically, far from having any imperialist ambitions, the country was struggling with different types of hegemonies imposed from the outside world. This section compactly reviews the modern Croatian history, until the First World War (section 4.1.1), in the interwar period and the first Yugoslavia (section 4.1.2), in the second Yugoslavia from 1945 to 1990 (section 4.1.3) and, finally, from the Homeland War 1991-1995 until today (section 4.1.4).

4.1.1 CROATIA UNTIL WORLD WAR I

Long time ago, Croatia seemed powerful. Under King Tomislav in the 10th century, the early Croatian state reached its zenith. Tomislav united Dalmatia with Pannonia and upgraded his title from that of duke to king with the permission of the Pope. As a result he became lord of a substantial state, roughly covered by modern Croatia, Bosnia and the coast of Montenegro (Tanner 1997: 9). When Tomislav died, a crisis began, along with civil wars that did not stop until the end of the 10th century (Goldstein 1999:18).

Under King Petar Krešimir IV, the Croatian crown recovered much of the authority it had enjoyed under Tomislav. However, the neighbouring Hungary saw its chance in Croatia, when Croatian gentry started to disunite. Kalman, the new Hungarian king was a resourceful statesman who was determined to gain through diplomacy what could not be obtained by force. Having defeated the

last Croatian native king, Petar Svačić, Kalman embarked on negotiations with the gentry.

The result of Kalman's negotiations with the leaders of the twelve largest clans of the south was a historic agreement in 1102 signed in the northern town of Križevci and called the *Pacta Conventa*. Under the terms of the pact, the great Croat families recognised Kalman as king. In return he granted Croatia a virtual self-government under a *ban* (Croatian noble title) (Tanner 1997: 14). All the lands that made up the Croatian state (comprising what are today Northern Croatia, Dalmatia, duchies of Neretva and Slavonia) were now united under the reign of Arpad dynasty (Goldstein 1999: 21).

The independent kingdom of Croatia as in times of the famous king Tomislav therefore came to an end. For the next eight centuries Croatia was to be ruled as a part of the kingdom of Hungary, albeit under the Habsburgs from 1527. While the other cities of Dalmatia suffered from constant battles between Venice and Hungary-Croatia, the city and Republic of Dubrovnik grew rich undisturbed, exploiting its position on the crossroads between the West and the half-barbarous kingdoms of Bosnia and Serbia (Tanner 1997: 25).

When king Ladislav of Naples sold his rights to the Croatian city of Zadar and its surroundings to Venice in the early 15th century, it seemed that Croatia would wait long too reunite again. Indeed, even when Dalmatia and Slavonia were reunited under the Habsburgs in the nineteenth century, they were not permitted to unite into one administrative territory. Reunion had to wait until 1939, and the formation of the autonomous Croatian *banovina* (province) in royal Yugoslavia (Tanner 1997: 27)

Croatia is often called under historians the Ramparts of Christendom, being a Roman Catholic country which defended its neighbours at many occasions against the Turks. Under the Ottoman siege, Croat hopes of recovering large tracts of the country with the aid of the Habsburgs were disappointed. From 1527 to the 1590s however, Croatia continued to lose

territory. What began as a political dispute between the Croatian parliament, *Sabor*, and the Habsburg over the Military Frontier in Croatia (*Krajina*), a region encompassing today's regions of Lika, Kordun and Banija, over to Slavonia, soon assumed additional ethnic and religious overtones. In fact, the *Krajina* was settled on the invitation of the Habsburgs with Vlachs or Morlachs as they were also known, most of whom belonged to the Serbian Orthodox Church although a minority were Catholic. Serb scholars have usually insisted that the Orthodox Vlachs were ethnic Serbs, in order to boost the claim that the *Krajina* should be attached to a Serbian state, as in the 1991-1995 war (Tanner 1997: 39)

The dispute between Emperor and Sabor over the *Krajina* was one reason why relations between the Habsburgs and the Croats deteriorated in the seventeenth century. Another was disappointment over the Habsburgs' failure to recover any territory from the Turks. Historians often talk, when referring to this period, about the *Reliquiae reliquiarum*, the remains of the remains of Croatia. Nevertheless, by the 1600s, the power of the Turks was visibly weaker and the great Croat noble families, the Frankopans and Zrinskis, were becoming impatient with the Emperor's unwillingness to push the Ottomans back (Tanner 1997: 50).

The failure of the Ottoman siege of Vienna in 1683 marked a great turning point in the history of Central Europe and the Balkans. After the siege of Vienna collapsed, the legend of Ottoman invincibility was broken (Tanner 1997: 53). In 1700, therefore after the liberation of the most of what is today's Croatian territory from the Ottoman Empire, with the liberated area being absolutely devastated and the population spread all over Europe, Croatia counted a total of 644,500 within its today's borders. This has probably been the smallest population in Croatia since the beginning of the 10th century (Gelo 1998: 22).

In 18th century, as a result, the country was choking with poverty. After the reforms and the enlightened absolutism of Maria Theresa and Joseph II, in the latter half of the eighteenth century, Dalmatia was even forced to import

agricultural products to keep the local population alive, draining precious supplies of money to Venice and Italy and worsening the province's trade deficit. For the most people, the only solution seemed to emigrate. Therefore, in 1780 the authorities reported that many people emigrated from Dalmatian cities (Tanner 1997: 63).

The new storm broke after the Empress Maria Theresa's death in 1780. In 1785, in one swoop, Croatia was virtually abolished. The post of *ban* was rendered redundant; Zagreb was merged into one part of Hungary, and eastern Slavonia into another. Some signs of the French revolution appeared in Croatia soon after 1789. In 1794 the first Jacobin agitators surfaced in Zagreb (Tanner 1997: 67).

Many Jacobins were in fact Hungarians who themselves were complotting against the Habsburg Monarchy. Some Croats, who could not endure the pressure of absolutism, joined them voluntarily. During the notorious common assembly from 1790 to 1792, an extensive independent reform programme of the development of Hungary was drafted. Immediately after that, and in the context of the conspiracy of Hungarian Jacobins, preparations for an open political confrontation with the Vienna Monarchy absolutism followed. In 1795, this conspiracy was revealed and the conspirators killed (Karaman 2000: 78).

In 1797 large numbers of Croatian soldiers from the Military Frontier had been employed in fighting the French in Italy. The war ended in failure for Austria, and Napoleon and Francis immediately agreed to exchange Habsburg-ruled Lombardy, which the French had seized, for Venice's possessions in Dalmatia (Tanner 1997: 68). In 1808, French soldiers entered the city of Dubrovnik. The French regime in Dalmatia crumbled rapidly in the aftermath of the disastrous campaign in Russia in which, ironically, also many Croatian soldiers from the *Krajina* fought with distinction (Tanner 1997: 67-71).

Obviously, Croatian territories were for centuries exchanged and sold among the leaders of more powerful nations. Therefore, the country did not have a real chance to start its economic development, since it always had to accept some new rules, leaders and impositions. However, an astonishing fact is that Croatia always somehow managed to move forwards. Igor Karaman, a prominent Croatian economic historian, offers a thorough analysis of the Croatian economy in the 19th and 20th centuries (see Karaman 1972, 1991, 2000). He describes the establishment of modern capitalism in Croatia in detail, which dates from the mid-19th century.

As Karaman reminds, the principal factor for the establishment of capitalist relations or capitalist features of production organisation and techniques is the merchant bourgeoisie. This stratum of Croatian society developed due to the intensive commerce of cereals in the late 18th century. After 1820, the trade in wood and wooden materials gained some importance. In the same time, at the Croatian coast the shipbuilding industry flourished (Karaman 1991: 44ff). However, an administrative and political fragmentation of Croatia, and the subjection of its territory to different outside factors, led to a struggle of different forces within the Monarchy. Consequently, the Croatian issue culminated during the Illyrian movement and the Croatian national revival.

The Illyrian movement began in the 1830s as a reaction to Hungarian political and cultural pressure. Illyria was originally a region dating back to the period of Ancient Greece, inhabited by the tribes called Illyrians. Using the name, Napoleon called his possessions in Dalmatia the Illyrian provinces. In the 19th century, the name was also popular as a root of a new idea of Pan-Slavism, which will later be replaced by Yugoslavism, thus the union of the Slavs against non-Slavic hegemony. As Tanner (1997: 81) rightfully remarks, the initial idea of Illyrism could flourish only in the minds of intellectuals and their aristocratic patrons. The average Croat and Serb peasant certainly never came to think of himself or herself as Illyrian, and Illyrianism faded in the era of mass politics, when the peasants got the vote.

Soon, faced with Hungary's apparent determination and cultural pressure to reduce Croatia to the status of a province, it had seemed logical for the Serbs and Croats of the empire to unite against their joint enemy. Thus the notion of Illyrism was reformulated into the South Slavism (Yugoslavhood or *jugoslavenstvo*). However, the Serbs were playing a slightly different game. What is still today by far most discussed policy document of that time, Ilija Garašanin's *Načertanije* (Plan), outlined the new country's foreign policy goals, creating an enlarged Serbian state at the expense of the Ottoman Empire. His ambition was for Serbia to expand south to Kosovo and then on to Thessaloniki. The union of South Slavs, or the notion of *jugoslavenstvo*, were for Garašanin absolutely irrelevant as such, but they served as a tantamount for the real Serbian intentions (Tanner 1997: 102ff).

In the mid-19th century, Croatia seemed to wake up from a long hibernation. This was the time of the Croatian national revival (1835-1875). As a student, young Ljudevit Gaj had been irritated by his education because the language of instruction was Latin, the ethos was Hungarian and nothing was taught about Croatia, or in Croatian. In 1832 there were first fist-fights in the academy at Zagreb between Hungarian and Croatian students, following an attempt by one of the professors to give lectures in Croatian. Ljudevit Gaj introduced a number of linguistic reforms. Growing Hungarian pressure divided the Croatian Parliament and encouraged the formation of parties.

As for national economy during the Revival, there were many plans for establishing important institutions necessary for the development and functioning of any modern society. Because of the forming of the capitalist economy and industry, it was particularly necessary to initiate the building of transportation system in order to encourage the formation of a single market. It was also of the utmost importance to organize a credit business, whereby a corresponding national economic policy was formulated (Karaman 2000: 91). The 1860s and 1870s are therefore regarded as the era of the initial formation of the modern capitalist economy in Croatia. Industries and factories

were established in many sectors, both in Northern Croatia and at the coast (Karaman 2000: 109).

The 19th century was also the period in which lived a great Croatian personality, Ante Starčević. His belief in Croatia's independence was absolute: he preferred any kind of isolation to compromises with Austria or Hungary. Other, such as bishop Josip Juraj Strossmayer, on the contrary, were dreaming about Zagreb and Croatia being at the centre of the new southern Slav entity, free of Austria and Hungary. Their wish was fulfilled, with a single modification: Zagreb and Croatia were never in the centre of a new union of South Slavs, as we shall see.

The revolutions of 1848 propelled Croatia into a state of wild excitement. On 25 March 1848, a national assembly met in Zagreb. The demands included the unification of Dalmatia and Slavonia, annual meetings of the *Sabor*, the call for the Military Frontier (*Krajina*) to be abolished, the exclusive use of Croatian in educational and governmental institutions and the establishment of a Croatian army, or at least of army units that would serve only in Croatia. The assembly also demanded the appointment as ban of a popular officer from the Military Frontier, Josip Jelačić. He helped to defend Vienna by pushing back the Hungarians during the Revolution of 1848 and he also abolished the serfdom in Croatia (Tanner 1997: 83).

The first significant attempts of establishment of a modern state system of Croatia are to trace back to the mid-18th century. This system aimed to transform existent social relations in the spirit of enlightened absolutism (Karaman 2000: 113-127). Upon his appointment, Josip Jelačić formed the *Ban committee* (a central administrative institution). High officials served in the liberal-conservative spirit, thus promoting two higher classes, i.e. landowning gentry, interested in trade, and the merchant bourgeoisie. They saw the future of the Northern Croatia only with Hungary. Therefore, the core of the modern industrial society in their understanding could be located only in Northern Croatia.

In the period of Jelačić's administration, not only the constitutional framework was built, but also many other institutional and structural elements necessary for the full development of a modern society. The appearance of an active core of the industrially oriented middle bourgeoisie opened many possibilities provided that there was free interaction of newly formed class forces of bourgeoisie. This would at the same time imply a gradual limitation of the role and the influences of state apparatus, i.e. bureaucratic officials and intelligentsia (Karaman 2000: 127).

The Austrian –Hungarian compromise of 1867 marked the rebirth of the Habsburg Empire as the Austro-Hungarian Dual Monarchy. The Croats again attempted to squeeze capital from the struggle between Vienna and Budapest only to emerge completely empty-handed. As a result of another agreement, Croatian-Hungarian Compromise of 1868 (*Hrvatsko-ugarska nagodba*), Croatia was handed over to Hungary. A new *ban*, Levin Rauch, was appointed to oversee the working out of Croatia's autonomy inside Hungary under the Compromise. Dalmatia remained in Austria. The Croats retained the post of *ban* as the president of the Croatian government, the *Sabor*, the supreme court, the Croatian Domobrani (Home Guard) and the right to use Croatian as the language of administration and education (Tanner 1997: 98ff).

But the deal was worse than it sounded: the *ban* was to be appointed on the recommendation of the Hungarian government rather than the Croatian Parliament, *Sabor*. The fiscal terms of the *Nagodba* were not generous either. 55 % of Croatia's revenues were allocated for the use of the joint treasury, leaving 45 % for the domestic budget. In a further blow, Rijeka and the Međimurje region were detached from Croatia and reincorporated into Hungary, reversing Maria Theresa's decision of 1776 (ibid). Imre Tkalac's (1852) report offers a good insight into the economic situation in Croatia of the 19th century. What he was especially unhappy with was the agriculture: despite the fact that Croatia possessed all the preconditions for wealth, it stayed a poor country, not being able to feed its own population.

The largest proportion of the population in Northern Croatia had the basis of their existence in agriculture. The area of Istria was reorganized under the Austrian government since 1815 (after the downfall of French reign). Regency in Trieste covered the Istrian peninsula and the area around Gorizia. The Austrian reign was established over the territory of Dalmatia and Dubrovnik (after the abolition of the Dubrovnik Republic). There was a strong agricultural production in all these areas (Karaman 2000: 147-152). From the mid-19th century in Croatian territories countries under the Habsburg reign it was evident that the change of the existent institutions of traditional society (such as peasant house cooperatives) was absolutely necessary (Karaman 2000: 163).

Albeit the fact that, after the breakdown of feudalism, landowners and big merchants in the Military Frontier area (*Krajina*) did their best to adapt to the new capitalist system, their main interest stayed however in the peasant labour force, as numerous and as cheap as possible. Due to such intentions they were actually trying to conserve the institution of peasant house cooperatives, exclusively in its traditional role. Similar trends were obvious especially under the *ban* Khuen Hedervary regime. In 1881, the Croatian-Slavonian *Krajina* was however definitely abolished, being itself the only feudal creation that had survived so long.

In Northern Croatia, the orientation towards the peasant communities was exactly the opposite: the scope was to abolish house cooperatives as quickly as possible. The partisans of this idea were themselves modernizers "from above". During the neo-absolutist regime, such doctrines were mainly result of the Monarchy. However, in the period before and during the *Nagodba*, domestic partisans of modernization shared the same attitude: high officials and liberal intelligentsia (especially from the circle of Chancellor and *ban* Ivan Mažuranić) (Karaman 2000: 181).

The example of Imre Tkalac shows that Croatia was also on the path of industrialization, following its more developed neighbours. Notably, what is common to all Tkalac's reports is a liberal approach to economy, not unusual for

his time. Following his mentor of economic policy from Heidelberg, K.Rau, Tkalac was the partisan of a free market, and he was consequently against the feudal, medieval limitations. He supported a free market competition, and only in some exceptional cases he could tolerate interventionist measures (in manufacture, for instance).

Karaman (2000) asserts that, although the formation of capitalist economy and bourgeoisie was slower in Croatia after the revolution of 1848/49 than in Austria or Hungary themselves, the Monarchy could benefit from Croatian developed areas. Revolutionary cycle of the transformation period in the constitution of the bourgeois-capitalist society in Croatia encompasses mainly a high time of the Croatian National Revival, thus the period from the reform of the social and political system (1848/49) until the end of the establishment of the modern bourgeois institutional structure at the end of the 1870s. During the first years of the *ban* Ivan Mažuranić (especially in 1874 and 1875) a necessary transformation of social and political system was conducted through a set of legislative directives. In the same time, the institutional structure was established (Karaman 2000: 36-41).

The period of the economic history of Croatia starting in the mid-19th century is beginning of a new era, of the creation of a modern capitalist economy (Karaman 2000: 192). All around Croatia, railroads were built and the modern banking system established. However, Croatian territories often did not share the same economic policies and interests: Dalmatia and Istria were under direct rule of Austria, the town of Rijeka under the exclusive, and Northern Croatia under the significant rule of Hungary, while the rest of the Military Frontier was exposed to a conflict of interests between Vienna and Budapest.

In the middle of this industrialization process, many Croatian countries were increasingly dependant on foreign factors (1880s and 1990s). This was then the opportunity for stronger and better organized Hungarian, Austrian or any other foreign capital jumped in and determined the paths of Croatian industrialization and development. Of course the primary goal of foreign

investments was always the foreign profit, and not Croatian (Karaman 2000: 223).

Although the fierce competition in the shape of modern production technologies from Western parts of the Monarchy impeded the shaping of textile industry as early as at the manufacture level (until 1848), the domestic economy started to grow slowly in the 1850s and 60s in some other sectors, above all in the food industry (Karaman 1991: 101). In 1860s, factories were zealously built, capital accumulated and transportation system modernised. A general crisis due to various conflicts within the Dual Monarchy was also brought about by the heating-up of the economy and because of the early form of speculative activities.

Unfortunately, for Croatia this implied the persistence of a general long-term stagnation for the domestic economic forces due to unsatisfactory economic policies both in Austria and Hungary. In this way the national economy was deprived of any progress in the course of industrialisation, capital accumulation and general modernization, all the way until the end of the 19th century. Moreover, the development of Croatian urban areas as potential centres of a capitalist society in the making was limited (Karaman 2000: 236). More favourable circumstances reappeared in Croatia only in the final years of the 19th century, during the period of strengthening of different areas of the economy. It was then that, after almost two centuries of stagnation, the economy experienced a real revival.

The entrepreneurship was far more active in the 19th century than in the era of absolutism. Partly favourable general conditions of economic development as a consequence of the boom of capitalist economy in the Monarchy and especially in its Hungarian part influenced the mobility of economic forces also in Northern Croatia. A significant share of this economic boom in Croatia was due to a temporarily more favourable economic policy of the Hungarian government towards Croatia since the political crisis of 1873 (i.e.,

since the partial recognition of the system established by the Croatian-Hungarian Settlement by Croatian political leaders) (Karaman 1991: 164).

Therefore, the subordination of the Croatian territories to the governments in Vienna and Budapest (and consequently, their social, economic and political dependence), deprived the citizens of Croatian territories of any support in building up of the modern industrial economy. Despite these mainly unfavourable conditions for the development of industrial sector under the Austro-Hungarian reign, many creative industrial initiatives can be observed until the First World War in today's Croatia. These initiatives took place particularly in sectors that were related to the use of natural resources or to a favourable geopolitical location.

Initial support for the raising of manufacture industries at the higher level of industrial processing came from domestic entrepreneurs as early as in the mid-19th century. However, these attempts failed due to a general weak political and economic position of Croatia in the Monarchy. Generally, the growth of smaller enterprises can be observed from the end of the 19th century. These investments considerably expanded and enriched Croatian industrial policies by introducing a factory production into processing industries, something which had been put aside until that moment. (Karaman 1991: 239 ff).

As it is well-known, the Austrian-Hungarian Monarchy did not last. The Dual Monarchy established in 1867 was intended to be a short-term, interim solution, which in fact it was not, given that it lasted for more than 50 years. However, no one thought that after 50 years, in 1918, the Monarchy will definitely disappear, in any form whatsoever. It survived the First World War, but it could not survive its consequences. The assassination of the Austrian emperor Francis Ferdinand in 1914 in Sarajevo by a Serb militarist triggered off the War, after which Austria, as one of the conquered nations, had to give up many of its territories. After centuries of the Habsburg rule, Croatia saw its chance which it simply had to take, because it naively believed it would find its political and economic freedom within the new Kingdom. In words of a

prominent historian Ivo Banac (1988: 115): “In the aftermath of the Sarajevo assassination, South Slavic politics were thrown into a state of flux. The changing international situation opened for the solution of the South Slavic national question. The search for the solution, however, was characterized by often divergent political programs.” Unfortunately, these divergences did not matter at the time. Later, they did, and very much indeed.

This is why finally, in 1917, the Croats and the Serbs agreed in the Pact of Corfu to work for union and a “constitutional, democratic and parliamentary monarchy under the Karadjordjević dynasty” (Tanner 1997:117). Following this, the National Council of Slovenes, Croats and Serbs was formed under the rule of the Serbian dynasty Karadjordjević. On 1 December, Serbian Prince Regent Alexander formally proclaimed the existence of the Kingdom of Serbs, Croats and Slovenes. Croatia headed from one trouble straight into the other.

4.1.2 CROATIA IN THE FIRST YUGOSLAVIA UNTIL THE WORLD WAR II

The Croats did not find what they were looking for in the new Kingdom. Seemingly, the new monarchy guaranteed equality for all the three flags (Croatian, Serbian and Slovenian), all the three names, all the three religions (Roman Catholicism, Orthodoxy and Islam), and the Latin and Cyrillic script (Goldstein 1999:110). However, this was far from true. The Croats should have probably listened to the famous Croatian politician and the founder of the Croatian Peasants' Party Stjepan Radić who warned Croatian people not to rush into union with Serbia “like a bunch of geese in the fog”.

Radić was known to general public from 1895, when he was one of the protestants against Hungary who burned the Hungarian flag (Goldstein 1999: 100). The Serbs, however, heard him and were very intimidated by such speeches. As a consequence, Radić was shot by the Serb Punisa Račić in the middle of the National Parliament in Belgrade in 1928, and he died of the consequences of this attack less than two months after.

This scandalized the Croats who were increasingly louder in their disapproval of the Kingdom's politics. After the death of Radić and as a response to it, Ante Pavelić formed an illegal underground paramilitary organisation, the *Hrvatski Domobrani* (Croatian Home Guard). A day after the King suspended parliamentary government on 6 January 1929 and therefore again reduced any possibility to protest against current politics, Ante Pavelić set up the Ustashe Croatian Liberation Movement in Zagreb (the word *ustaša* being derived from *ustanak*, meaning uprising, in the sense of resistance) (Tanner 1997: 125).

The new Kingdom's economy was very weak at the beginning. The principal instruments used by the state to encourage the development of industry were protective import duties, state credits, opening of state mines, granting of mining concessions, developments of transport by the use of public funds, and subsidies for industry. In the immediate post-war period there was a rapid growth of new industries. The state also took a direct role in the export trade partly through a state-owned limited company. In addition, a department of the Ministry of Commerce and Industry controlled the exports of most other agricultural products (Singleton and Carter 1982: 60).

Karaman (1991: 281) finds that first years after the unification of Yugoslav peoples and countries were marked by economic instability, scarcity and social conflicts. During the 4-year-war destruction, countless human lives were lost and material goods destroyed. Besides that, the new Yugoslav community encompassed and gathered within its borders the areas with different economic and social characteristics, shaped during the previous separated periods under different foreign reign. Thus the building of a unique economic system on the whole Yugoslav area was an extensive and difficult task which could be solved only gradually and with many troubles.

State regulation of the economy increased in 1930s. In 1939, partly under pressure from the military, state control was established over the production and export of all minerals. In January 1941, a Ministry of Food was

established, with powers to control prices and to regulate the distribution and exports of food. The tendency towards state intervention, which was present from the early days of the kingdom, was conceived partly with the intention of stimulating native industries and protecting them against foreign competition (Singleton and Carter 1982: 61).

Moreover, gestures were made in 1921 towards the idea of free trade amongst the Danubian states, and a conference to this end was held at Portorož in November 1921. The failure of Yugoslavia to ratify this protocol has been explained on the grounds that it was too weak to abandon its control of the foreign trade (Singleton and Carter 1982: 62). Hence, the 1st Yugoslavia was indeed a very protectionist state. Foreign investments were the greatest in the non-ferrous metal industry, fuel and power production and shipping. The usual pattern was that the foreign-owned company employed Yugoslav workers to extract the raw materials that were then exported in raw or semi -finished form to a more developed industrial country where the finished goods were manufactured (ibid: 64ff).

The collapse of the Habsburg and Hohenzollern Empires at the end of the war provide an opportunity for French, British and Swiss capital to move in where previously Austro-Hungarian and German economic interests had predominated. The Kingdom inherited the public debt from the ruined Austro-Hungarian Empire and from the independent states of Serbia and Montenegro. In addition to these old debts, the new government incurred further loans to finance industrial development, and in particular to improve the railway network (ibid: 67).

At many levels, the economy of the Kingdom of Yugoslavia was influenced and even controlled by foreigners. The state borrowed heavily abroad; large parts of industry were either under direct foreign ownership on their activities were circumscribed by agreements with foreign cartels; and finally, the predominance of Germany after 1935 as the principal trading partner

gave that country and its Nazi rulers an overwhelming influence on Yugoslavia's economic development (ibid: 69).

There were several business cycles within the first Yugoslavia according to Singleton and Carter (1982: 73ff): the post-war boom from 1918 to 1925 (due to the great demand for building materials in order to repair the damages of war); the period of stabilisation from 1925-1930 (overheated economy, where many small businesses failed); the great depression and its aftermath 1931-1935 (manufacturing industry slumped, fall in agricultural prices, iron and steel output fell) and the post-depression recovery from 1935 to 1940 (export-led recovery coincided with the German rearmament drive and the later economic consequences of Europe's preparations for war).

Yugoslavia had an overwhelmingly rural population of about 44,4% of total population. In 1919 a land reform was concluded, with an interim decree stating that land should be distributed to those who have no land at all (Singleton and Carter 1982: 82). The agriculture contributed to 45 % of the national income in the period 1923- 1925, and a decade later the proportion had fallen only to 42,9% (ibid 1982: 89). Moreover, food exports accounted for between 50 % and 60% of total Yugoslav exports during the inter-war period (ibid: 90).

Actually, the first Yugoslavia started in 1918 as an economically underdeveloped country and it remained so until the Second World War. With its average growth rate of 1,9% from 1923 until 1939, 0,15% per inhabitant, Yugoslavia maintained all the characteristics of an economically underdeveloped country with a dominant extensive agriculture (Sirotković 1996: 46).

Rudolf Bičanić, a Croatian economist who lived both in the first and the second Yugoslavia, prepared in 1938 a very precise study about the economic position of Croatia in the Kingdom of Slovenes, Croats and Serbs (the first Yugoslavia). He calculated that in 1937 Croatia and Dalmatia accounted for

overwhelming shares in Yugoslav economy: 28% in agriculture, 30% in cattle-breeding, 38% in forestry, 30% in manufacture, 27% in commerce, 33% in industry and 49% in total banking of Yugoslavia (Bićanić 1938: 51). Serbia, on the contrary, brought into new country as much as 80 times more debt than other countries added together (ibid: 67). Bićanić asserts that the Serbs completely rebuilt their country after the First World War with Croatian money. As for taxes in this period, he observes a soaring inequality: Croatia had to pay twice, Slovenia thrice, Vojvodina five times taxes more per inhabitant than Serbia (ibid: 84)

Situation for the Croats was not better in the central administration. Until 1937 (1918-1937), none of 35 governments fell transparently in Parliament, but each and every of them was removed “off stage” (ibid: 90). Of a total of 350 000 functionaries and officials, there was a clear Serbian hegemony over all other peoples in bureaucracy. Due to such centralism, the number of mainly Serbian officials was constantly increasing as they were nominated by the central government, whereby many Croats were forcefully retired (ibid: 51).

Most of these Serbian officials were not qualified for their posts and did not have any experience or knowledge of Croatian laws. Bićanić believed that Serbian bureaucracy governed by mistrust, violence and corruption. Again, as we have seen before, many Serbs knew that in the name of Serbia alone they could not rule Zagreb. This is why they used the notion of *Yugoslavhood*. The carriers of this ideology were therefore the official circles and bureaucracy (ibid: 99ff).

In the upper state government in 1937 there were 88 Serbs and as little as 9 Croats, and in some other bodies, such as the Ministry of Finance, the situation was not much better: 150 Serbs and only 15 Croats (ibid: 103). The position of Croats in the state administration was even worse than their number. There was a tremendous suppression on Croats who were forced to give up their national feelings (ibid: 115).

The central administration of Yugoslavia was a fertile ground for corruption. The bureaucratic apparatus was “enormous, sluggish, lazy, indifferent, desperately formalistic, slow, unpractical, irrational and ignorant, and above all terribly costly” (ibid: 113). This was due to the fact that its activity was induced only through personal protections and personal/party revenges. The government is concentrated in Belgrade, and this is why the Serb officials explained that all corruption was coming “from the outside” (ibid: 115).

As for the public expenditure on infrastructure, dotations and general investment, Bićanić finds that there were always more financial means in store for Serbia than for other countries. Croatia had no influence on the management of the royal army. Besides that, the Serbian propaganda was constantly trying to present the army in Yugoslavia and abroad as a non-politic organism, which was a delusion (ibid: 152).

Moreover, there was a financial dictatorship of state banks. The monetary policy upon which 15 million people were dependent was led in the interest of the biggest shareholders of the National Bank in Belgrade. When the Bank gave out its cheap loans almost 50% went to Serbia (ibid: 211). Yugoslavia also disposed of an agricultural bank giving privileged loans. Croatia obtained one-ninth of all the loans that Serbia received (ibid: 223). The State of Yugoslavia served as an important economic factor: it was the biggest employer, entrepreneur, buyer, merchant, organizer and owner of transportation, the biggest accumulator of capital, the biggest regulator of transportation and organizer of domestic and foreign trade (ibid: 228).

Finally, the University of Zagreb was impeded in its development, due to the lack of loans available for education. The states of Yugoslavia had a fictive autonomy, but were in fact very limited in their development. In only one city, Belgrade, the amount of investments equalled to that which could have revived the whole country. Bićanić ends his bitter prologue by maintaining he would not be heard, because if at any point the Croats dared to raise their voice, the

Serbs would refute everything by simply saying that the Croats were separatists (ibid: 245-250).

This was the situation in which Stjepan Radić's successor at the top of the Peasant's Party, Vladko Maček, was trying to negotiate a better position of Croatia within the Kingdom. Finally, he and the Serb Cvetković reached a *Sporazum* (agreement) on 20 August 1939, which was approved by the Regent. According to this agreement, the Croatian *Banovina* (the name invoked the previous Croatian title of *ban*, the governor, and implied a territory of Croatia with more autonomy than before) included all the Northern Croatia, Dalmatia with the addition of Dubrovnik and the bay of Kotor, about the one-third of Bosnia and a large part of the Srijem region.

The new *Banovina* was to have a unified parliament and the post of *ban* was to be restored, not to the joint parliament in Belgrade. Foreign affairs, foreign trade, the army, the post, the railways and certain key main roads remained the responsibility of Belgrade. Outstanding disagreements concerned the new *Banovina*'s budget and the police, who remained under the auspices of both the military in Belgrade and the direction in Zagreb (Tanner 1997: 133).

The *Banovina* might have solved the crisis in the relations between the Serbs and the Croats that had threatened to wreck the Yugoslav state since its creation. However, the outbreak of hostilities between Germany, France and Britain in September 1939 confronted the Regent Karadjordjević with a terrible dilemma. His sympathies lay with Britain. However, the Croats' ties were with Austria and Central Europe, who were on the opposite side. The Regent simply did not see the reason to preserve the agreement (Tanner 1997:134).

On 6 April 1941, Germany declared war on Yugoslavia. Ante Pavelić's Ustashe movement aligned with Germany. In 1945, the establishment of the *Nezavisna Država Hrvatska* (Independent State of Croatia) was proclaimed, known generally by its abbreviation NDH. Unfortunately for Croatia, the new state was a carbon copy of Nazi Germany. The Germans did not care for it, and

the Italians wanted to keep it weak. Soon, in the Treaty of Rome of 1943, Pavelić handed to the fascist Italy almost the whole Dalmatia.

The new state, NDH, was definitely not what the true Croatian patriots, from the 19th century, such as Ante Starčević, would have wanted. Starčević dreamt of the free and independent Croatia, with all its inhabitants living in harmony. On the contrary, Pavelić's regime in line with the Nazi ideology was responsible for the killing of many Jews, Serbs and other foreign nationals. No one knows the exact number of victims. Later on, Communist authorities claimed that about 600 000 people perished in the notorious camp Jasenovac, whereas Croatian president Tuđman, a historian, came up with the number of 60 000. Modern Croatian historians, such as Ivo Banac, a former Professor at Yale University, concluded that both numbers were incorrect. Whereas 600 000 is almost generally seen as exaggerated, the number of only 60 000 seems to be a serious underestimation. Banac calculated that there were about 120 000 people killed in Jasenovac.

Tanner (1997: 160) finds that the right wing and the clerical were held back from opposing the NDH by their conviction that the Croatian independence was a good thing, even if the form that it took under Pavelić was obviously not. The left was less restrained. Quickly, the persecution of the left-wing intellectuals hastened the flight of the Intelligentsia away from the Ustashe, so that the NDH were soon fighting against the organized anti-fascist left-wing rebels, known as Partisans.

The Partisans staged their first big wartime congress in 1942. The Anti-Fascist National Liberation Council of Yugoslavia was supposed to be a leading anti-German resistance in the region. Josip Broz Tito, the future Yugoslav leader who would reign for almost 40 years, emerged as the leading personality. Soon, Pavelić was informed that Germany was about to surrender and was given command over the remaining Axis forces in Croatia. He and his family slipped into Argentina. This was the end of the NDH, this dark period of Croatian history. Pavelić and his like-minded abused the original desire of many

Croats to have their independent country by transforming that same country into a theatre of monstrous crimes, succumbed to the Nazi Germany.

Many Serbs were meanwhile very eager to join the Partisans, and the Partisan response to the end of the NDH was cruel. As a group of Ustashe and other Croats and Slovenes was to escape the new regime, the British stopped them and handed them back over to the Partisans. In May 1945 the confrontation came to a head when the Croats attempted to cross into Austria at Bleiburg. The Partisans killed as many Croats and Slovenes as they could. Here again, the numbers vary considerably, from 30 000 to 200 000 dead, depending on the source (Tanner 1997: 170).

Soon after this tragedy, on 29 November 1945, the monarchy was abolished and Yugoslavia proclaimed a people's republic (People's Federal Republic of Yugoslavia). It encompassed Bosnia and Herzegovina, Croatia, Macedonia, Montenegro, Serbia, Slovenia and the province of Kosovo. The Karadjodjevic dynasty lost the throne as the Communist party overtook the power. Its leader, Josip Broz Tito, born in Croatia, was the first prime minister. In 1953, Tito was then named president of Yugoslavia, and in 1974, president for life.

4.1.3 CROATIA IN THE SECOND YUGOSLAVIA

In January 1946, the Constituent Assembly ratified the first of four constitutions to which Tito's Yugoslavia was ruled. The new bicameral National Assembly became the supreme organ of state authority. The Federal Council was unitary, based on one deputy for every 50 000 citizens much like the parliament of the 1921 constitution. The Council of Nationalities was a federal body: each republic had thirty representatives, and the provinces of Vojvodina and Kosovo 20 and 15, respectively (Lampe 1996: 230).

Party propaganda attempted to rally popular support around the ideology of Yugoslavism rather than federalism or socialism, and at first it succeeded. The 1946 constitution itself enshrined “brotherhood and unity” (*bratstvo i jedinstvo*). The new regime was particularly popular among rural youth (ibid: 232). The celebrated break with the Soviet block in 1948 made Tito’s Yugoslavia unique in Eastern Europe and eventually led to better relations with the West among any of the Communist regimes (ibid: 237).

The Croats had many reasons for discontent due to economic, social and political position they had in the new country. As we shall see further on, economically Yugoslavia was oriented towards the redistribution of wealth from the richer republics to the poorer ones. Croatia itself was, after Slovenia, economically the best-off republic, and it was systemically impoverished due to obligatory transfers to underdeveloped regions. Serbia itself constantly accentuated its underdevelopment. Politically, the Croatian language suffered the constant suppression to the benefit of an artificially created language, Serbo-Croatian. Many politicians who were Communists, but who opposed to Tito (such as Andrija Hebrang) were persecuted and assassinated. Croatian intellectuals and media were constantly subject to censorship.

Moreover, two dilemmas bothered Croatia. Economists in Slovenia and Croatia concluded that federal institutions like the Belgrade General Investment Fund favouring heavy industry and investment in the less developed republics and regions, were working to their disadvantage. Secondly, despite the fact that the investment policy favoured the less developed republics, low price ceilings for energy and other raw materials that were their major sectors did not (Lampe 1996: 277).

The culmination of Croatian discontent was the Croatian Spring in 1971, the massive student demonstrations. It was initiated by the Croatian Writers’ Club, in the shape of the Declaration Concerning the Name and Position of the Croatian Language of 1967. The background was a row over a new Serbo-Croat dictionary between two Serb and Croat cultural organisations (Matica

srpska and Matica hrvatska). The Croatian Spring affected three main areas of public life: the Party itself, deeply reforming some Croatian communists; Matica hrvatska, Croatian cultural organization, and Zagreb University (Tanner 1997: 190).

Nevertheless, for the Croats the result of the Croatian Spring was disappointing: Matica hrvatska was shut down, many intellectuals and politicians imprisoned (among them the future first president of Croatia, Franjo Tuđman) and some expelled from the Communist Party. The atmosphere between the Serbs and the Croats was definitely poisoned by the events of 1971. Repression was so efficient and opposition so splintered that Croatia appeared uncommonly calm from the early 1970s to the mid-1980.

Yet, under the calm surface of the “silent republic”, as Croatia was nicknamed in the Yugoslav media in the early 1980s, there were disturbing trends. The Party in both Croatia and Slovenia was contracting in size and getting old. Tito’s death in 1980 will then finally excite speculation in the Western press about the possible break-up of Yugoslavia, predictions of the revival of Croat nationalism and of ethnic tension between the Serbs and the Croats (Tanner 1997: 204).

In 1974, a new federal (the fourth and the last) Constitution was ratified, according more autonomy to the individual republics, thus basically fulfilling the main goals of the Croatian Spring movement. One of the provisions of the new Constitution was that each republic officially had the option to declare independence from the federation, subject to certain constitutional regulations. Moreover, the new Constitution conferred a similar status to two autonomous provinces of Yugoslavia, Kosovo, a largely ethnic Albanian populated region of Serbia, and Vojvodina, a region of Serbia with Serb majority, but with large numbers of ethnic minorities (Hungarian, the Croats). This opened way to the soon breakdown of Yugoslavia, the split of Serbia and Montenegro in 2006, and finally the proclamation of the Kosovo independence in 2008.

In 1987 Slobodan Milošević emerged as a political force in Serbia. Until then Milošević displayed no particular concern for the plight of the Serbs in Kosovo or in Bosnia and Croatia. Then, however, he suddenly encouraged the demonstrations of Kosovo Serbs against Albanians.

As Ramet (1999: 26) notices, the Serb-Croatian conflict was always at the centre of political strife in the country and in the fragile conditions associated with the rise of Slobodan Milošević in Serbia, re-emerged as the pivotal conflict in Yugoslavia. Immediately, Croatian politicians accused Serbian leader Slobodan Milošević of Stalinist and unitarist tendencies and charged that Serbian politicians were trying to destabilize and neutralize Croatia. In the course of 1989, Milošević tried to create a base of support among non-Serbs by talking about a program of anti-bureaucratic revolution. This campaign was widely viewed with a combination of distrust and cynicism outside Serbia (in Croatia in particular). Serb nationalists were raising awkward issues (Ramet 1999: 35). They tackled the economy, politics and, of course, the history.

All of a sudden, the Serbs began to talk about the large-scale transfer of industry from Serbia to Croatia and Bosnia in the years 1945-1951, a transfer which had been part of an effort to move factories away from areas that might fall rapidly to Soviet control in the event of a Soviet bloc invasion, but that the Serbs now said had been intended to weaken Serbia. Moreover, the Serbs now talked of the "Orthodox origin" of Dalmatian Croats. They revived a long latent claim that Montenegrins were actually Serbs. Furthermore, the Serbs, stoked by the Serbian Academy's incendiary Memorandum, attacked the entire legacy of Tito, arguing that it had been above all anti-Serbian, and suggested that it was time to weed out the confederal elements introduced by Tito (such as the veto system).

All this led to a large-scale conflict. Finally, Milošević even told an enthusiastic crowd of one million Serbs at Kosovo Polje on 28 June 1989, at the six hundredth anniversary of the battle which had led to medieval Serbia's precipitous decline and ultimate conquest by Ottoman Turkey, that Serbia was

engaged in a new battle and that armed conflict might not be far off (Ramet 1999: 55ff).

Having seen the political position of Croatia within Yugoslavia, we now turn to the economic situation. Was it better than in the first Yugoslavia? Sirotković (1996) emphasizes that the economic position of Croatia after the World War II was based on the common Yugoslav economic policy and the unique economic system. After Tito's breakup with Stalin in 1948 and the adaptation to the new situation, the concept or strategy of development in Croatia changed considerably, while the concept of self-management was proclaimed to be the new social standard aiming to create the new economic system. Such expectations, however, did not materialize.

With its average growth rate from 1948 to 1989 of 5%, i.e. 4,2% per inhabitant, Yugoslavia ranked among rapid- growing economies. In the same period, Croatia had a somewhat slower total growth, and higher growth per inhabitant (ibid). Nevertheless, in the 1980s this growth slowed down. In 1981 stagnation broke out, resulting finally in the decrease of production even before the armed attack on Croatia. The causes for this recession should be searched for in the past and in the functioning of the system which was considerably different from what the proclamations of constitutions had laid down.

Moreover, as Sirotković (1996: 11) adds, no reform in the period from the 1950s to the 1990s enabled a thorough change of the system. Thus the positive consequences of single reforms were always very short-lasting. All the social problems reappeared and were increasingly more difficult to solve, the same being true for democratic processes which were highly limited and the market constrained through the powerful state control. The policy of economic development was predominantly loaded by a doctrinarian, pragmatic conception of faster development of economically disfavoured areas, which inhibited total development, therefore also the development of Croatia.

Seen in the long run and in absolute terms, Croatia indeed did realize during its Yugoslavian time a significant increment in its economic potential. Its level of development increased from 1955 to 1989 by approximately 4.5 times (in terms of GDP) and 4.8 times (per inhabitant). These growth rates of the total GDP were however slower than the Yugoslav average (Sirotković 1996: 12). However, the redistribution of this growth, as well as different economic policies Croatia would have envisaged for itself, made this period economically unfavourable for Croatia in the long run.

The emphasis of the Croatian development policy was placed on industrialization. Very high growth rates of the industrial production were achieved, thus making industry dominant in the structure of total production. Economic development of Croatia as well as of Yugoslavia as a whole shows some oscillations in shorter periods, and also some significant discrepancies. Such distortions were evident in almost all social relations after 1979: GDP was reduced almost to a stagnant growth rate, while the employment and basic capital showed a significantly slower increase, however showing a multiple growth as related to GDP. What is characteristic for Croatia is its lower share of investments in GDP than the Yugoslav average, which stems from the outflow of capital accumulation from Croatia, but also from the relatively low degree of utilisation of supplementary foreign capital accumulation (Sirotković 1996: 14).

Yugoslavia had generally low labour productivity and technological progress in comparison to the OECD economies. Economic growth of Yugoslavia was realized through an extremely low efficiency of investments and very cheap labour force. Since the economic system was unique, this also encompassed Croatia. Due to the very fast development, it was necessary to increase the expenditures. A high increase in employment which was brought about by such policies, required also a corresponding increase of monetary means for personal revenues and other necessary expenditures (Sirotković 1996: 15).

A breakup with Stalin and the introduction of self-governing economy at the beginning of the 1950s were connected to various changes in the economic system, leading to decentralization and independence of business in the sense that the control over very strictly controlled inner and outer markets was loosened. The accent was placed on the relationship between the central, federal government and economic organizations. In that sense, the role of single Yugoslav republics was marginal.

The adoption of the Constitutional Law of 1953 in which the self-governing economy, about which I will talk a little later, was institutionalized, resulted in a polarisation in decision-making: investment decisions were mainly function of federal state bodies, while the self-governing bodies decided about the redistribution of personal revenues, however still in the given global framework (Sirotković 1996: 20). At the same time, large transformations in the political system were carried out, aiming to complete a self-governing social transformation, whereby all social decisions, starting with municipalities, over republics to federation, were to be founded on self-governing decisions. New Constitutions of 1953 and the 1965 did not move much forward in this regard.

All this was an introduction to a large crisis, so political decisions were to be made. The constitution was again amended in 1971, and the new constitution entered into force in 1974. During this period (1971-74) various features of economic system were improved. The national accounting system was normalized, liquidity problems partially solved, the economically rational amortization system was established, the problems of financial means dedicated to manufacture were finally approached, and the inner market was mature for the price liberalization and fulfilling all the conditions for the establishment of a global and structural imbalance (Sirotković 1996: 23).

The whole system had a clear effect of impoverishment of the economy after 1974. At the same time this system had a negative impact on the regional redistribution, to the detriment of Slovenia and above all Croatia. Net-contributors were exclusively Croatia and Slovenia. The redistribution was

conducted through the Fund for Economic Investment and through the Federation for General and Common Expenditure. Besides that, there were contributions for «supranational» federal institutions, such as federal army, police, foreign affairs, the Yugoslav National Bank and the customs service (Sirotković 1996: 27).

Important segments of the economic system were dominated by the central state organs of Yugoslavia, particularly in the areas of pricing, investment, in a monetary, credit and foreign exchange affairs (Sirotković 1996: 28). The administration, especially federal, used a very well-known trick, employed in the practice of many etatist and bureaucratic systems. Since state institutions had to be financed in a stable way, there had to exist a social plan for the year ahead. This plan supposed the real increase of GDP, prices, exports and imports, and according to that plan the expenditure for bureaucratic apparatus was determined in advance (Sirotković 1996: 30). Hence, the simple fact that the plan used the estimates and not the real data, leads us to the conclusion that GDP was generally overvalued, which brought to bureaucrats much more than actually necessary. The economic position of Yugoslavia reached its lowest point in 1990 due to its insisting on the redistribution system, despite the crisis it found itself in.

The Memorandum of the Serbian Academy of Sciences and Arts (SANU) of 1986 asserted that Serbia had a problem of economic backwardness, blaming other republics for it. It also mentioned a disaster, the possible breakup of Yugoslavia. In the eyes of the SANU drafters, Slovenia and Croatia were responsible for all the bad outcomes of the Yugoslav economic policy, due to the dominance of their politicians in decision-making (the Slovene Kardelj, and of course Tito who was Croat). They estimated that the influence of these two countries was exercised to the detriment of Serbia and other countries. Finally, the 1974 constitution was nothing but a disaster for the SANU, since it opened the way for the fall of Yugoslavia (Sirotković 1996: 37).

Analogically to Bićanić for the period of the first Yugoslavia, Sirotković (1996: 57) shows how important Croatian economy was, within the second Yugoslavia. Croatian share in the production in 1983 amounted to 24,48% and in 1987 it remained almost the same at 24,44%. In both years, its share in total GDP was 25%, thus one-fourth of the total Yugoslav production! As for imports, in 1983 it accounted for 28,6 % and in 1987, for 22,25% of all Yugoslav imports. On the other hand, its export volume amounted to more than one-fourth (28,76%) of total Yugoslav exports in 1983 and a little less in 1987 (25,55%). It is clear why the Serbs considered the dissolution of Yugoslavia a disaster.

4.1.4 FROM THE HOMELAND WAR TO THE EU-CANDIDACY

In Croatia, the decision was final. In 1989, the future president of Croatia Franjo Tuđman founded the Croatian Democratic Union (HDZ). This party was the first to win the first multiparty elections in Croatia in 1992, after decades under one single party within Yugoslavia, the Communist Party. Franjo Tuđman became the first president and, as he is often called, the father of modern Croatia. Soon it was clear that the days of Yugoslavia were counted off. In May 1991, a referendum was held with a question on whether Croatia should remain in Yugoslavia or become independent. 94% of all the citizens of Croatia voted in favour of independence. The war in Croatia, in Croatia known under the name the Homeland War, started soon after.

After the confiscations of much of their Territorial Defence weaponry, Slovenia and Croatia were in desperate need of armaments and turned to foreign sources. Both countries faced a serious obstacle. In spite of early expressions of sympathy from the German and Austrian governments, the states of Western Europe held back from offering diplomatic recognition of support to these two republics. On the contrary, the US, the Soviet Union, China, France and other countries issued statements supportive of Yugoslav unity and hostile to Slovenian and Croatian secession. Nevertheless, Slovenia

and Croatia unilaterally declared their independence on 25 June 1991. By the mid- January 1992, Croatia was recognized by all EC member states and in May 1992 it was admitted to the United Nations

The Serbian aggression started immediately, and it was disastrous. Aside from Vukovar, which by October 1991 succumbed to Serbian siege, Serbian militias backed by the former Yugoslav National Army (JNA) also laid siege to Osijek, Dubrovnik, Petrinja, Glina, Okučani, Vinkovci. Other cities, notably Zagreb, Karlovac, Slavonski Brod and other were subject to constant aerial bombardment. In the midst of the fighting, paradoxically, Serbian President Milošević accused Croatia of trying to pursue a “policy of genocide” (Ramet 1999: 67).

Although the formal armistice between Croatia and Serbia was signed in 1992, significant parts of Slavonia and the ex-Military Border (*Krajina*) regions were under Serbian occupation until 1995. However, in military operations Flash (May 1995) and Storm (August 1995), Croatia restored all of its territory with the guaranty of the peaceful reintegration of all the Serbs who inhabited these areas. The war ended by the Dayton-Paris Agreement (the talks were held in Dayton, Ohio, and the treaty was concluded in Paris in December 1995).

However, the new Croatian Democratic Union (HDZ)-government soon proved to be less patriotic than it had tried to look like. First, it used the strong desire of the people to have their own and independent country at last, by proclaiming itself the champion of Croatian statehood, and Croatian military victories served it to confirm this. Ottaway and Maltz (2001: 376) hold that the HDZ leadership exploited Tuđman’s and the party’s image to eviscerate the political opposition, branding opponents as traitors rather than accepting them as legitimate political adversaries.

This corresponds to a foreign image of Croatia in the 1990s, and that projection is true. Economically, this government helped to stratify and impoverish the nation, and it deluded it definitely. However, despite the moral

decline of the HDZ, the importance of the personality of Tuđman for the Croatian history remains uncontested, since, whether it is accepted or not, he was the person who had the courage to lead the nation into independence, of which it had dreamt for hundreds of years. This is often forgotten.

After Tuđman's death in 1999, the HDZ soon found itself in the middle of crisis. The catastrophic results of the market liberalization and privatization in Croatia enlarged the gap between the extremely poor and the new rich. The HDZ soon lost the elections of 2000, and the 6-party coalition formed the new government. The biggest and the most significant among these 6 parties was the SDP, the Social Democratic Party. Its president Ivica Račan became the new prime minister.

The new left-wing government, however, was also a disappointment, because it was reluctant to restructure the public and the private sector after the unsuccessful economic transformation. Investigating and prosecuting offices proved weak, incompetent, and sometimes complicit (Ottaway and Maltz 2001: 380). The presidential system was weakened and the role of prime minister gained on significance. The newly elected president was still incumbent Stjepan Mesić, who had also been the last President of the Presidency of the Socialist Federal Republic of Yugoslavia and the first Croatian prime minister after the free elections of 1992. As the left-wing coalition government did not achieve what the electorate had expected, in 2004 the HDZ restored its power and has been incumbent since, with the Prime Minister Ivo Sanader as the government leader.

In 2003, Croatia applied for the accession to the European Union and in 2004 it became an official candidate. Due to a dispute with the International Criminal Tribunal for the Former Yugoslavia (ICTY) in The Hague, which accused Croatia of the lack of will to extradite its general Ante Gotovina (suspected by the ICTY for war crimes during the military operation Storm of 1995) the beginning of the Croatian EU-negotiations was postponed until 2005. Nevertheless, in October 2005 the negotiations were launched, and in

December 2005 the fugitive general was captured and transferred to The Hague. His trial is still in operation.

Croatia has so far opened all the chapters of the European *acquis communautaire*, and closed only some of them, the biggest issues being with the reform of judiciary system, agriculture and economic adaptation. The accession date of Croatia to the EU has not been determined, but the main belief is that this should happen by 2011 at the latest. I will return to the Croatian EU-candidacy and prospects in chapter 5.

4.2 ECONOMY OF YUGOSLAVIA, 1945-1990

In the previous chapter we had seen how the Japanese post-war economy was conceived. Japan chose developmental state model for its post-war recovery. Yugoslavia, which became officially a socialist country in 1963, but in reality, it was socialist from its very beginning. Led by one party and an authoritarian leader, to some extent it came close to developmental state organization, but, as it is my aim to show in this section, there were considerable differences. In section 4.2.1 I will briefly recall the history of the Yugoslav model, while section 4.2.2 will inform about three most distinct features of this model: political framework, bureaucratic social planning and the self-management.

4.2.1 SHORT HISTORY OF THE YUGOSLAV ECONOMIC MODEL

The new federation emerged in 1945 was a complex unity. As Branko Horvat (1982:3) writes, "Yugoslavia may be described as one country with two alphabets, three religions, four languages, five nations, six federal states called republics, seven neighbours and eight national banks, and the population of 21 million." Bearing this in mind, it is clear that the economic model had to be constructed to satisfy all the republics. This section investigates whether it was successful in this enterprise.

In his 1976 book about the Yugoslav economic system, Branko Horvat describes the beginning of the second Yugoslavia as a peasant country. He argues that it was peasants who participated in the National Liberation War en masse. In Yugoslavia, numerous landowners lost their land without compensation. The next crucial move, undertaken in 1946, was nationalization of private capital in industry, mining, transport, banking and wholesale trade establishments. In 1948, nationalization was extended to retail trade and catering and in 1958 to residential buildings with more than three apartments. About one-half of the Yugoslav economy, outside agriculture, was owned by foreign capital (Horvat 1976: 7).

In the very beginning, the new country was supposed to be modelled on Stalin's Soviet Union. The land reform of 1945 stated: "The maximum agricultural holding to remain the property of the farmer cultivating it with his family shall be established by provincial laws, with the proviso that that it may not be under 20 nor over 35 hectares of cultivable land" (Singleton and Carter 1982: 103). The largest group of beneficiaries from the distribution were ex-Partisans and their families from poorer regions.

Following the Soviet model, a system of compulsory deliveries of surplus food to state agencies was introduced in 1945. Prices were fixed at levels far below what the peasants could have achieved on the open market, and delivery quotas were often set at unrealistic levels by bureaucrats who had no knowledge of local conditions (ibid). This collectivization drive did not succeed since it was exposed to strong resistance. As Horvat (1976: 14) claims, in 1952 and 1953, several laws were passed regulating the formation, operation and termination of business enterprises. The enterprises could be set up even by a group of citizens. In agriculture, the collectivization drive increased the number of peasants' work cooperatives, but with its compulsory deliveries, administrative controls and the rest, it depressed the output.

Yugoslavia sought for alternatives (Singleton and Carter 1982: 109). The general agricultural co-operative did not attempt to change property relations. It

bore some resemblance to west European farmers' cooperatives. The peasants remained the owners of the land, but were encouraged to join a cooperative which organized the purchase of seed, fertilizer and machinery, and might also be involved in providing an advisory service, credit and marketing facilities. Another form of agricultural organization was the agro-industrial combine, involving a worker-managed enterprise which processed and marketed agricultural products, owned land of its own, but also entered into contracts with private farmers to supply the combine with some of its raw materials.

As mentioned by Horvat (1976: 88-102), there were three stages in agricultural reform. The first was the period of etatist collectivization (1945-1953). In fact, during the first post-war period, agriculture was treated as a source of capital accumulation and the peasants as a social group of small property and potentially capitalist elements that should be re-educated by administrative measures and included in the socialized that is, state, sector of the economy. After 1948, such an etatist pressure led to stagnation, and even to a fall in production.

The second phase is the one of the cooperation and the duality of agriculture, between 1953 and 1964. During these years, new ways of organizing agriculture were sought. The peasant work cooperatives were gradually dissolved. The prices of agricultural products continued to be relatively low. In order to stimulate the producers, in 1952, federal subsidies were introduced. The notion of duality implied that individual farms were to be found mainly in the developed regions, while collective farms were mainly located in underdeveloped regions. Thus, the ways of cooperation between individual and collective farms were needed.

The third and the last period was the time of economic reform and attempts to achieve a *laissez-faire* market, after 1964. The rival of Yugoslavia, the Soviet Union, organized its agriculture by means of *sovkhozy*, state farms, and *kolkhozy*, collective farms. They were separated from each other. On the contrary, in Yugoslavia after liberation state agricultural estates, agricultural

machine stations, and peasant work cooperatives were organized. There were also other cooperatives, but they were considered to be transitional forms. There were also many individual peasant farms, but that was considered a reflection of the initial stage of socialist transformation of the village.

Soon, Tito broke up his ties with Stalin and the Cominform in 1948, and this is why he soon abandoned hard-line policies he had forced on the country in 1945. Yugoslavia was excluded from the conference which led to the founding of the Council for Mutual Economic Assistance (COMECON) in Moscow in 1949. Since the Soviet economic blockade threatened Yugoslavia with collapse, Tito turned to the West for help and accepted loans. In return Tito had to tone down his anti-Western propaganda and stop supporting the Communists in the civil war in Greece.

At home, the fear that peasant resistance to collectivisation might spark off a rebellion that would give Stalin an excuse to invade forced him to slow down, and eventually abandon, the whole policy (Tanner 1997: 1984). The various drawbacks of the Soviet model, plus the desire to repudiate its publicly, still pushed Tito's Politbureau toward a new theory of decentralized socialism. Specifically intended to replace the first, Soviet-style, Constitution of 1946, the second Yugoslav 1953 Constitution embodied the new theory (Lampe 1996: 229).

Soon after the breakup with the Soviet Union, Tito started receiving a generous Western help. The largest UNRRA (United Nations Relief and Rehabilitation Agency) delivery to any European country was dedicated to Yugoslavia, whereby the sum was double the 1938 value of Yugoslavia's imports. UNRRA replaced almost the entire pre-war fleet. The largest part of UNRRA not surprisingly came from the United States, undamaged by the war and its economy in high gear (Lampe 1996: 236).

The Communist leadership had in fact begun to explore ways of distinguishing Yugoslav from Soviet practice as early as 1949. More importantly,

their innovations would proceed at a slower pace and have less to do with the market mechanism than many Western observers assumed. The arrival of the Western aid also facilitated the primary feature of the new Yugoslav road to socialism – the decentralization of continued the Communist political control over industry (Lampe 1996: 250ff).

According to Lampe (1996: 253), the economic renewal was well under way, and party membership was mushrooming. Also, Yugoslavia had just signed a series of bilateral trade agreements with the Soviet Union, its East European clients, and pre-war partner Czechoslovakia. A significant supply of agricultural aid began in 1950, soon joined by a US military mission and joint venture with Britain and France to shore up the growing imbalance of payments in Western trade.

The severe droughts of the 1950 and 1952 obliged the Tito regime to seek emergency food shipments from the US. Further shipments from the West European accumulation under the Marshall Plan, by then the Economic Cooperation Administration, and other sources increased the 1951 and 1952 totals towards 100 million dollar apiece. The US also provided a variety of military assistance to the Yugoslav National Army (JNA), but not much armament (Lampe 1996: 254). The problem was however how to export enough to Western Europe and the US, with the Italian market still restricted because of the Trieste dispute, because someone had to pay for the imports that the Soviet bloc would have provided and that would accounted for rapid industrialization (Lampe 1996: 255).

The American answer was to press Tito personally in 1952 for a more competitive and export-oriented economy. In sum, the initial American assistance to Yugoslavia allowed the Communist regime to continue starving the agricultural sector in favour of the heavy industry and defence. Against these liabilities, however, we must balance the preservation of Yugoslavia's independence from the Soviet bloc. Tito's Yugoslavia had the chance to make

its Western economic ties and domestic commitment to decentralization work to its unique advantage (Lampe 1996: 256).

Yugoslavia maintained its Third World connections with the Non-Aligned Movement. Clearly, the movement remained Yugoslavia's best forum for propagating the theory and practice of workers' self-management. Official missions to a long list of countries, from Peru to Indonesia, promoted general support for its positions in the UN. This experience also combined with the Yugoslav promotion through the SUNFED and the UNCTAD to ease access to some \$ 4 billion in World Bank loans from 1960 to 1990. Such prolonged support also owed something to the \$ 1,75 million in grants, soft loans and dinar sales that the US provided to Yugoslavia between 1953 and 1964 (Lampe 1996: 268).

The United States continued through the 1980s to play the role of Yugoslavia's lender of last resort. After that, West Germany and then Italy of Western Europe came forward as the most important partners. Together, their equipment and consumer goods provided high quality imports meeting high standards that no member of the Soviet bloc could match (Lampe 1996: 271).

Yugoslavia's economy grew at a faster pace from 1953 until 1961 than most others in the world, including those of the Soviet bloc. The value of industrial production led the way with an average annual increase of 12,7 % by official statistics, reduced insignificantly. However, heavy doses of capital and labour outpaced gains in productivity. Investment was high and consumption low. Still, from 1954 forward, Yugoslavia had witnessed a discussion of how to disengage from this top-heavy mechanism for investment (Lampe 1996: 273 ff).

There was definitely something different about Yugoslav economy: it did not dismiss the market. On the contrary, as Branko Horvat writes in 1971: "The present Yugoslav economy is truly a market economy and very different from the rigid, semi-administrative economy of ten years ago, not to mention earlier periods. But it appears that this has not been noted, and old conceptions,

bureaucratic approaches, intuitive and ad hoc solutions, short-run pragmatism, and neglect of scientific economic research continue to burden Yugoslav economic policy. A market economy is like a precious machine, highly productive but sensitive. A skilled worker can attain exceptional results with it. When there is inept leadership, waste and breakdowns occur" (Horvat 1971: 190).

Still, Yugoslavia was not capable of combining the market and its very own self-government practices. In fact, with the second international oil crisis in 1979, Yugoslavia experienced a massive decline. Registered unemployment reached 16,3 % in 1985. Aggregate inflation for 1979-1985 exceeded 1000 % (whereas the European average at that time was less than 50%). Yugoslavia had a political crisis, too, with federal-republic relations deadlocked, especially after Tito's death in 1980 (Lampe 1996: 293). Even after Tito's death, when Yugoslavia was unable to service the interest on its loans and the country experienced a severe balance of payments crisis, the Party always refused to admit there was a crisis. It was only in the autumn of 1981 that a federal commission was set up at last to examine the crisis. By that time inflation had soared from the pre-1976 level of about 15 per cent to over 50 per cent (Tanner 1997: 201).

The commission recommended big spending cuts, which were carried out after agreements were signed with the International Monetary Fund in 1983 and 1984. In spite of that, inflation reached a record of 70 per cent in 1985. The debt crisis which was made worse by the rise in oil prices in the mid-1970s, forced Yugoslavia to agree to stand-by arrangements with the IMF, which insisted on repeated devaluations of the dinar as a condition for assisting the federal government with servicing a gross debt (ibid: 207).

As they say, the rest is history. The downward spiral caused soon the collapse of labour productivity. As a result of a general apathy, about 500 000 of Yugoslavia's 5,5 million workforce were absent each day, while the others worked an average of less than five hours a day (ibid: 208).

Singleton and Carter (1982:179) emphasize however that the Yugoslav economy was chronically unstable, and not only after oil shocks. There was always an absence of tools to deal with inflation, which was a natural consequence of high growth. Moreover, Yugoslavia had a deep-seated unemployment problem. Real product per worker declined gradually: in the period between 1960-1970 it amounted to 4,3% average change per annum, between 1970-1979 it was only 2,8%, and in 1979-1985 it collapsed to the negative value (-3,6%). Besides that, Yugoslavia's trade problem was caused by its seemingly inexhaustible demand for imports.

Finally, Ramet (1999: 50) asserts that the Yugoslav economy was, by 1988, in extreme crisis. In that year, the national income declined 2 percent, inflation reached 160 percent, and the foreign debt had reached an all-time high of \$ 20 billion. All six republics experienced economic decline in 1990. Political instability and talk of civil war and military coups of course scared off investors. But, this was only a consequence of a deeper system instability, which we are going to analyze now.

4.2.2 CHARACTERISTICS OF YUGOSLAV ECONOMY

A. POLITICAL AND LEGISLATIVE FRAMEWORK

As it has already been mentioned, the first Constitution of 1946 proclaimed the Federal People's Republic of Yugoslavia. After his famous "No" to Stalin, Tito had to invent a new economic architecture, a socialist but not the Soviet-Union-type socialist system. The second Constitution of 1953 spoke of decentralization and other departures from Soviet practice, but its specific provisions did not point in that direction. By this Constitution, the republics lost their rights of secession and sovereignty, granted in 1946.

Sovereignty now reposed with people, vaguely defined as the unified Yugoslav working class. Their single, socialist consciousness would create a

single Yugoslav one to replace the various nationalisms that had been discredited during the Second World War, by the unique idea of Yugoslavhood. Its Communist sponsorship, however, could not help the idea to survive the Tito era. Nevertheless, it is important to stress that the Constitution of 1953 gave birth to the self-governing principle. Another very important innovation found its place: it became known as the principle of the fusion of political and economic sovereignty of the working people (Horvat 1976: 15).

Economic discussion before 1952 was therefore dominated by two themes: planning for fast growth and the search for an authentic socialism. Preparation for the New Economic System, as it was called, started with the Law on Management of Government Business Enterprises and Economic Associations by Workers' Collectives enacted in July 1950, and ended with the Constitutional Law on Principles of the Social and Political System of Yugoslavia, passed in 1953. The New Economic System became operational in 1952. It was transitional in character and lasted until 1960 exhibiting very high economic growth (Horvat 1976: 12ff).

In 1951 the government was busy dismantling the central planning apparatus, with its ministries, directorates, and administratively fixed prices. A new Law on Planned Management of the National Economy replaced detailed central planning of production by planning of the so-called basic proportions. In 1951 there existed a large number of categories of market and planned prices. This was replaced by a single price structure which, with certain exceptions, was to be regulated by the market (Horvat 1976: 13).

The last phase in Yugoslav post-war socioeconomic development was prepared by a series of political, economic and constitutional reforms between 1958 and 1963. Thus, the Yugoslav variant of socialism appears to imply social ownership, self-management in the economy, and the absence of non-labour income and exploitation (Horvat 1976: 20). The period from 1963 to 1966 witnessed the most intensive political debate over economic reform in the history of the second Yugoslavia. The third Constitution of 1963 renamed the

country from people's into the Social Federal Republic of Yugoslavia. It offered a reform advocated more political representation, but hardly resolved the issue of how that reform might proceed. The major opponent of this market reform, Aleksandar Ranković, used political pressure behind the scenes to deter it and was disgraced in 1966 (Lampe 1996: 277).

The 1965 reform encompassed (Lampe 1996: 282ff) the combat of inflation, import increase and hence, a drastic reduction in the number of banks. Their capital and direction would come from changing their principal enterprise and institutional depositors who now became shareholders. The new banks would operate on a commercial basis, providing long- and short-term credit to the borrowers most likely to repay their loans.

The rest of the reform included 5 provisions: (1) Taxes on the turnover of goods were reduced and made more uniform. (2) The Fund for Accelerated Development of Less Developed Republics and Kosovo received significant resources. (3) Aiming for the goals of full GATT membership by 1966, Yugoslav currency *dinar* was again devalued. (4) Agricultural and raw material prices were still controlled, but increased in order to bring them closer to world level. (5) Finally, peasants working private land were allowed access to bank credit to purchase the tractors and other agricultural equipment they needed to shore up their lagging productivity (Lampe 1996: 287).

This reform was comprehensive, but it was rather *laissez-faire*-inspired and it could not last, since even before Tito's death, the country entered a severe crisis, as we have discussed above. As a result, in a few months a group of experts produced a report, popularly called the Yellow Book. It found that inefficient planning resulted in economic instability.

The last Constitution of 1974 was, as already remarked, more important for political than for economic reasons. Although further bank reform was envisaged and the new Law on Associated Labour adopted, Yugoslavia found itself in a severe debt crisis in the period 1979-1985, which contributed to its

definitive end. In sum, it remains to be said that all the four Constitutions of Yugoslavia encompassed various reforms of the economic life, but they did not include a long-term economic policy. Rather, many discretionary measures were proposed and the government seemed more to fight fire than to prevent it. And all this, despite the fact it actually *had* a system of planning.

B. BUREAUCRACY AND SOCIAL PLANNING

This powerful relation between the state and economy is the most obvious if one decides to analyze the industrial planning, as Galbraith (1967: 25ff) puts it: "As viewed by the industrial firm, planning consists in foreseeing the actions required between the initiation of production and its completion and preparing for the accomplishment of these actions. And it consists also of foreseeing, and having a design for meeting, any unscheduled developments, favourable or otherwise, that may occur along the way. As planning is viewed by the economist, political scientist or pundit, it consists of replacing prices and the market as the mechanism for determining what will be produced, with an authoritative determination of what will be produced and consumed and at what price. It will be thought that the word planning is being used in two different senses. In practice, however, the two kinds of planning, if such they may be called, are inextricably associated."

Yugoslavia was initially proud of its planning system, as one can read out in the publications of the economist Branko Horvat. He participated in the preparation of the report called the White Book in 1970, where it was concluded that Yugoslavia needed decentralization. Also, the authors of the White Book maintained that the state apparatus as authority is not the only possible solution, and that something had to be done in this respect. However, the state remained authoritarian until the end.

The state apparatus is defined by Horvat as the organ supposed to carry out coordinative and informative functions, to perform services for the

population and work organizations, and to use force only exceptionally (Horvat 1976: 29ff). The existence of very important economic problems that should be solved on the federal level did not, in Horvat's opinion, necessarily imply the framework of the state apparatus and a bureaucratic way of solving these problems. Thus, he concludes that the state apparatus should be left with only a minimum of essential functions, and for decisions on the Yugoslav level to be made in bodies that also include other social elements. On the other hand, there was a contradictory dilemma whether the authority should be given to the Federation or to the states in general (Horvat 1976: 30).

However, and it is important to emphasize this, none of these Horvat's claims materialized in Yugoslavia. Aspirations to reach a level of socialism not seen anywhere else in the world, actually did not match the real Yugoslavia and its actual authoritarianism of the state apparatus. In other words, Yugoslavia was very organized in a very etatist manner, a condition Horvat and the Marxists neither foresaw nor welcomed. Moreover, the authority was given to the Federation, but the states were ironically, to employ the Marxist jargon, the mere instruments of the system. In 1976, Horvat did not recognize it, and Yugoslavia had already been 30 years old.

So what was then the role of the state in Yugoslavia? The Federation, thus the Yugoslav state, was in charge of planning. As already noted, Yugoslav social planning started in the Soviet spirit. The First Five-Year Plan covered the period from 1947 through 1951. It proclaimed four main goals: to overcome economic and technological backwardness, to strengthen the economic and military power of the economy, to strengthen and develop the socialist sector of the economy, and to increase the general welfare of the population. Consumption was taken care of, but it was last in the order of priorities (Horvat 1976: 43-48).

Although Horvat (1976: 8) praises the First Five-Year Plan, stating that it was ambitious and seen as the foundation for the future industrialized and developed Yugoslavia, and successfully carried out in the first eighteen months,

other authors (Singleton and Carter 1982, Lampe 1996, Sirotković 1996) deny that. After all, the plan is said to have been successfully completed in 4 years, but in reality many claim it had been abandoned.

Horvat (1976) argues that the plan encountered difficulties due to a complete economic boycott by the Soviet Union, as a consequence of the Tito-Stalin split. Lampe (1996: 238) argues on the other hand that Yugoslavia's first Five Year Plan was by all accounts a spectacular failure. It is important in this context that the regime proclaimed an agricultural land reform that redistributed land from eight categories. Although maximum holdings of private land were now limited, and the considerable backlogs of peasant debt was also cancelled. The Communist leadership believed that these gestures would draw peasant voluntarily into the General Agricultural Cooperatives that it created in 1946 to replace the pre-war networks. They were quickly disillusioned, since the peasants were never really fond of Communism (Lampe 1996: 240).

Due to the failure of the First Plan, in 1952, rigid central planning was replaced by "planning by global proportions". The measure were a minimum use of output capacity and the corresponding wage fund, profits as a percentage of the wage bill, basic capital formation and taxes and allocation budgetary resources (Horvat 1976). The year 1956 was used to prepare the Second Five-Year Plan for the period 1957-1961. In that plan, the increase of consumption already ranked third among the five main goals, but it was not really successful.

The Third Plan for the period 1961-65 endeavoured to accelerate the growth of output even further. Personal consumption ranked second among the goals. But the plan was hardly launched when the country found itself in the middle of a recession. Due to incorrect estimations, the plan had to be abandoned as early as in 1962 (Sirotković 1996: 22). When the Fourth Plan 1966-70 failed, the task of the Fifth and the last Plan 1971-75 was to repair the damage. It envisaged an acceleration of the investment and the rate of growth, structural changes in favour of industries that were lagging behind, faster

increase of productivity, and a substantial slowing of price increases. The period after 1960 may therefore be described as a crisis in Yugoslav planning. The Sixth (1976-1980), Seventh (1981-1985) and Eight Plan (1986-1990) were not especially fruitful since the country had already been hit by a severe crisis.

The economic reform of 1965 proclaimed as its primary goal the financial and social enforcement of self-governing positions, being itself a precondition for independence and responsibility, rational management and business on the domestic and international markets. However, during the first unfavourable economic situation in 1967, it was evident that the reform and its crucial elements were not system-compatible, and this is why that period was a turning point with a tendency of reversing back to the pre-reform state. The priority and monopoly of statist decision-making was held (Sirotković 1996: 22).

However, the central planning period was seen only as introduction to the self-governing phase, which was *a posteriori* proclaimed as the final goal of socialism. In the post-revolutionary economic development, three distinct phases can be observed (Horvat 1976: 48): the central planning phase immediately after the war; (1947-1952); the transformation phase or decentralization (1952-1964); and finally the self-governing phase in which economic organization assumed more permanent forms (1964-1980). After that Yugoslavia entered into a grave political and economic crisis.

In the central planning period, collectivization caused stagnation of agriculture until 1953, when collectivization was discounted and reversed. Consequently, a low rate of growth was seen for the entire period. The economic boycott of the Cominform countries depressed foreign trade, and exports, in particular. As a result of both factors, investments could expand only slowly, and the overall pace of development was not impressive. The rapid expansion of unemployment was an indication of the inefficiency of economic organization (Horvat 1976: 49).

In the second period, the unfettered economy was in full swing in all spheres. Foreign trade expanded faster than output, and exports faster than imports. Prices were stable except in agriculture, where the disparity from the first period had to be corrected. Personal consumption and real wages were rising as fast as one could wish. The overall performance of the economy set a standard against which alternative economic policies could be evaluated. Unemployment was very low, and economy was growing incredibly (ibid).

In the third period trends were reversed and the performance dropped to the standards of the central planning phase. The dismantling of the federal investment funds reduced the growth rate of investment to less than half of what it had been before. This, together with poor coordination of activities and poor economic policy, reduced the rates of growth of output. As a result, employment possibilities were drastically reduced, and the rate of employment growth dropped to almost one-third of what it had been previously (ibid).

However, as Družić (1998: 113) remarks, the planning system resulted already at its very beginning in a suboptimal allocation of resources and, besides that, also in the underemployment of factors (non-sufficient utilization of capital and a very low productivity of the labour force). An autarkic development and a plan distribution of resources on consumption and savings, instead of a free market at which demand and supply are the principal resource allocators, resulted according to Družić in a long-term multilayer imbalance.

The first layer was an imbalance between the aggregate supply and demand which manifested itself in planned economies at the same time as a deficit and a surplus in demand and supply. A planned production of an unmotivated state sector of the economy resulted in out of date, bad quality products, and they were produced according to planning tasks, and not according to a real market demand. The final outcome were increasing reserves of a productive capital and of consumption goods, for which there were no buyers, i.e. oversupply. On the other hand, the population accumulated monetary means, creating thereby the demand for long-lasting and temporary

consumption goods, which could not be satisfied by the existing production structure, i.e. over-demand.

The other layer was a structural imbalance between the most important services. The technique of planning priorities brought to the long-term disproportions between the industry, agriculture and infrastructural services (transportation, housing and communal services etc.) By means of the policy of “price scissors”, in which the prices of agricultural products were, as a part of the plan, held on a low non-economic level, the prices of industry goods were, again according to the plan, held at a high non-economic level, a mechanism of a revenue spillover was created, and it had a devastating impact on the use of scarce resources. In the agricultural sector, low prices and missing resources resulted in low productivity, technological backwardness and a low level of production. In the transportation sector, low freight rates resulted in non-developed, hardly leaky routes and an old-fashioned vehicle fleet with high maintenance costs and frequent breakdowns.

The third layer was the sectoral imbalance. This imbalance was due to a policy of forced industrialization, which imposed the priority of ferrous metallurgy, of iron and steel industries, and machine engineering. Such objectives of an accelerated industrial development through capital investments brought about the imbalance between heavy and light industries, between the production of industrial and consumption goods.

The fourth layer consisted in a foreign trade imbalance, characterized by permanent deficits in foreign trade exchange of the ancient planned economies with developed markets. The formed planned economies were increasingly less developed, exporting mainly the products with a low or a very low proportion of R & D (Družić 1998: 115).

C. SELF-MANAGEMENT

Self-management (also referred to as self-government, or as a self-governing economy) was undoubtedly the most significant characteristic of Yugoslav economic institutions. Yugoslav social scientists were unanimous in the belief that, without self-management, socialism was impossible. The system was however not a Yugoslav invention. It had been invented at the beginning of the 19th century, and used since the Paris Commune (Horvat 1982: 156ff).

The principle was based upon the socialist belief that the workers, and not the managers, should manage companies they work in. Moreover, the ownership of these companies was conceived as social, and not state ownership. In this sense, Yugoslav economy was a mixed economy, combining the state planning, social ownership, and workers' self-management. All workers and employees of a firm constituted the work collective. This collective was responsible for electing a workers' council by secret ballot. This council then further elected a managing board as its executive organ. The director was the chief executive and is an ex officio member of the managing board. By re-reading the previous sentence, the reader will be probably a bit perplexed: how did it happen that there was a director? Was self-management not meant to serve as *workers'* self-management?

Exactly. Many Yugoslavian economists, Horvat included, quickly realized how incompatible the role of director was in this context. Nevertheless, they also realized that the workers couldn't really be self-managed. Some asserted that the director had to rely on the college of executive heads, which was his advisory body, but this body was aimed to be subordinated to him. In 1959, a new development began with the creation of economic units in order to bring in further democratization. The enterprises were subdivided into smaller units with a score or several scores of workers. Soon, economic units were transformed into work units (Horvat 1982: 159).

The introduction of self-management in 1950 implied the dissolution of the centrally planned, administratively run economy. The enterprise was to become independent and autonomous. Nevertheless, individual enterprises needed some guidance and coordination. Therefore, higher business associations were set up to replace former state directorates and to preserve continuity in the organization of the economy. The governing councils of the new bodies were composed of representatives of workers' councils of the constituent enterprises (Horvat 1982: 168).

However, the notion of self-management never really resolved its ownership controversy. The initial question, "If state ownership fails to promote socialism, what is a feasible alternative?" was promptly answered in Yugoslavia with: "Social ownership." But then, no one could really define social ownership, and it was attempted to relate the notion to the one of self-government. A general disagreement went on. The main objection to the concept of social ownership is the unknown title of that ownership. In that sense, social ownership established itself as a form of a self-directed economy, which was nowhere else to find.

In Družić's view (1998: 117), without a transparent proprietary relationship by which the ownership is defined as either private or public (state) ownership, it was not possible to motivate the mobility of capital towards profitable projects. Furthermore, in such a model there was no stimulation of a function of entrepreneur, nor the motivation for the rational conducting of business, because there was no natural relationship between the owner, employees, administration and entrepreneurs. Hence the crucial problem of social ownership is its lack of motivation.

Lampe (1996: 270) also notes several difficulties of the Yugoslav enterprise system: that Yugoslav industrial enterprises soon became large and started to dismiss workers. Second, too many directors were not just political appointees but were men selected by the communal council because of their wartime credentials (minimally educated peasants who had joined the Partisans

as teenagers). Third, retained earnings remained severely limited: after taxes and contributions, only less than a half of earning stayed with the enterprise. Singleton and Carter (1982:146) add in this context that after 1965, the unwillingness of the federal government to intervene except in times of acute crisis arises from a deep-rooted conviction that the system of self-management should be allowed to tackle such problems without state interference.

Self-management has evolved during the 1970s in two major ways. Firstly, attempts have been made to decentralize decision-making within enterprises by breaking down large enterprises into smaller-self-management units, each of which would be semi-autonomous in its decision-making. Secondly, there has been an attempt to extend the direct influence of enterprises or associated labour upwards in order to widen the role of the worker in the decision-making process in the community at large (Singleton and Carter 1982: 155). None of these attempts bore some fruit.

Soon it was clear that this system did not work, although it had a positive influence on economic movements, acceleration of production, consumption and productivity. The system implied abandonment of the Stalinist concept of economy and transition to rational planning with an accent on the increase in living standard of the population. In the period of introduction of self-governing this transition was however slowed down by introducing the concept of communes. Hence, the self-governing economy was limited to business, and municipalities had no possibility to become self-governing themselves. It was clear that self-governing did not establish itself as the main social relationship (Sirotković 1996: 20).

Self-management implied, in Branko Horvat's words (1982: 237), the equality of producers. He understands by this the following: in the self-managing economy, every member of society has the right to work, every member of society has the right to compete for any job and every member of society has the right to participate in the management on equal terms. In his most comprehensive work, *Political Economy of Socialism*, Horvat (1982:239-

259) went so far to develop the imaginary system of self-governing economy which eventually replaced the state. In the following pages, I will briefly show what he devised.

Horvat starts with the Yugoslav reality that he later on modifies into a normative model. The participatory organization is, and Horvat admits it himself, more complicated than the traditional hierarchical organization. In the self-governing economy, the basic organizational unit is not the enterprise but the work group. This latter one does not stand merely for a group of workers but also a definite subsystem in the production system known as the enterprise. In this capacity, the smallest functional unit is an economic unit. Work units are federated into a work community, economic units into an enterprise. Whenever the decisions of a work unit affect substantially the interests of other work units, the right of decision-making ought to be delegated to the next higher level.

This is the justification for establishing a workers' council as the second-level decision-making body. Horvat sees the implementation of decisions as a matter of professional competence, not of democracy. In the self-governing economy, policy decisions should be legitimized by political authority, while executive and administrative work, on the contrary, should be overseen by professional authority. However, since political and technical decisions cannot be neatly separated, and neither can work units be made perfectly homogenous nor the entire work community sufficiently small, there is always a possibility for individuals and groups to abuse the power. In fact, in Yugoslavia the bureaucracy was never depoliticized. Quite on the contrary: the Communist Party was omnipresent and its power was absolute.

In principle, Horvat argues, almost all decisions were to be made always at the lowest possible level. In this respect he again moves off from the Yugoslav reality. He argues that only when decisions affect the interests of other work units will they be made at the level above the work unit. Most of the decisions that affect the daily lives of workers can be made at the work unit level. Other policy decisions may be delegated to the central legislative organ,

the workers' council. Nevertheless, vitally important decisions, the notion remaining imprecise in Horvat's text, were to be made only by the entire work community at a general meeting or by referendum.

One of the most important goals of Yugoslavia was the full employment, and this was the root of its popularity among the working class. After the Second World War, many found a job which was usually low-paid, but, however, they had an employment and this was the only thing that counted for them. Until the oil shocks, inflation was controlled. Moreover, the state was generous: it distributed free apartments to the workers, organized their summer holidays, their free time and generally their lives.

The only condition was joining the Party, which so many did without thinking twice about it. Actually, the Party claimed it was not the state, but the Communist society, who cared about the labour. Everything was socially owned. However, it soon became clear that this method provoked an extremely low labour productivity, as mentioned above. Logically seen, if a worker is *a priori* guaranteed a fix job and all the possible benefits, and if this is not related to their performance, what could then be their motivation to work? In this sense, there was a popular joke in Yugoslavia, thought as an address of the worker to his superior, which perfectly reflects the situation: "You cannot pay me as little as I can actually work".

When preparing his 1982 work, Branko Horvat was clearly influenced by the theory of associated labour which was extremely popular at his time. The theory stems from Tito's most important aide, the Slovene Edvard Kardelj. According to such organization of labour, the right of a worker to decide within his company and to share profits depended on his investment in labour. Similarly to Horvat's ideal self-governing economy, in organizations of associated labour workers united into enterprises, and those latter then formed associations of associated labour, *de facto* large companies.

When new workers joined the enterprise, they signed a social contract whereby they associated their labour with that of the rest of the work community under existing constitution and ordinances. Work units took their decisions in plenum. Moreover, they elected a chairman, who represented their units during the workers' council. But, as Horvat further notes, worker management can function only if it is fully public. Consequently, prompt and adequate information regarding everything that was going on was vitally important. Again, in reality, transparency was not one of the highlights of the Yugoslav policy making.

For conflicts, Horvat foresaw a grievances commission dealing with the conflicts of first type (whereby an individual may be harmed by an action of the collectivity), and a work responsibility commission dealing with conflicts of the second type (the interests of the collectivity may be impaired by the irresponsible behaviour of an individual). The chairmen of these two commissions were in fact also members of the supervisory committee, which was planned to become an organ of workers' control and supervised all managerial activities. The council of reference should be the body a combination of a constitutional court and an arbitration board (for arbitration, new rules etc.)

In conclusion, Horvat saw no reason why only business firms should enjoy the privilege of self-management. He claimed that in a socialist society, whenever individuals associate their work in order to earn their living, they form a work organization based on self-management. The hierarchy should be replaced by cooperation. Thus, self-management should extend to all types of groups and associations and into all spheres of living.

As noted above, it failed to do so as far as decentralization and local autonomy was concerned, and it failed to do so in any other area. Why was it? Horvat (1976: 58) gives an answer himself: "Full autonomy might in some cases not be desirable." In fact, no one in Yugoslavia was able to know where the normative line between self-management and political repression really was, simply because that line had never existed. Self-management was combined

with discretionary politics, and was often used more for political propaganda than for the workers' benefit.

As for potential problems of the system, Horvat himself indicates several which were later crucial for the collapse of the system. Self-management naturally implied control of all managerial activities. It was then thought among its implementers that control is exercised most efficiently by direct participation in all decisions, including administrative, professional and routine decisions, which led to impossible decision-making.

Moreover, there was a divorce between decision-making and responsibility. In the similar vein, since managers were likely to be better educated than workers and better informed about the firm's affairs than anyone else, they in fact held more power than some other groups. Furthermore, with an enterprise treated as a federation of economic units, internal organization was very complex and required much experience and professional knowledge in order to be handled appropriately.

Otherwise, the conflict between all the decision-making bodies described in the previous pages risked to multiply, and individuals and groups in furthering their private interests were prone to misuse the system. This was often the case. Finally, there were also the dangers of inefficiency and etatism. Instead of solving their problems by themselves, there was a risk that managers might ask government to intervene, and that, according to Horvat, was fatal.

It is interesting to observe how in 1982, thus in the very last decade of Yugoslavia, Horvat treats all these deficiencies of the self-managing system as merely *potential*. In reality, they very much corresponded to the truth: there was an extreme conflict in decision-making within enterprises, the government often intervened into all spheres of economy and life in general, and the Communist ideology, and not the workers (as the theory said), had the final say.

And how then, finally, despite all its flaws, was the self-management of Yugoslavia supposed to replace the old state? Since his book dates back to the

period shortly after Tito's death, Horvat became very much aware of the new weakness of the Party. As already mentioned above, in the 1980s the Yugoslav governments were even trying to gradually separate themselves from Communism as the authority of the Communist Party was fading away.

Thus, for his model of Yugoslavia of the future, Horvat foresaw an Assembly which would be made of the House of Citizens and the House of the Economy. Citizens would elect their representatives for the House of Citizens, and the producers for the House of the Economy. There would be the Executive Council elected by the House of Citizens, and the Constitutional court elected by the House of the Economy, although the citizens would be able to review the decision of the producers (Horvat 1982: 304).

In the context of Yugoslavia, Horvat also thought in terms of federation. There would be only four federal basic institutions: the Planning Bureau, the National Bank, the Development Fund and the Arbitration Board for Incomes and Prices. Each formal state within the federation would be in charge to provide for its own social services. However, the federation would be a supreme instance with three basic tasks: equalizing the conditions of economic activity, ensuring market equilibrium and ensuring economic growth (Horvat 1982: 353). Note how similar this reformulation of goals is to what we saw in the previous chapter on Japan.

It remains to ask ourselves: In what foreseeable period was such an ideal system envisaged? Horvat asserted that not so much time was to pass, because he held that the workers would eventually press for self-management. "We are bit interested merely in the destruction of the existing system; our fundamental aim is to build a new, socialist system," Horvat (1982: 470) writes. However, so far, the only destruction in this context was the one of Yugoslavia.

4.3 ECONOMIC TRANSFORMATION OF CROATIA AFTER 1990

In the course of this chapter, I have underlined the particularities of the Yugoslav system, which, as we have seen, was a system of a mixed economy, combining the state planning on the one hand, and the social ownership and worker's self-management on the other hand. Thus, all the republics inherited such an economic structure after the fall of Yugoslavia. Different to other socialist planned economies, notably those of the Soviet Union, the particularity of the Yugoslav economy was a common (social) ownership instead of a socialist state ownership.

As stated in this chapter, Yugoslavia had a higher degree of market openness. It resulted in social ownership as a special form of proprietorship, which implied that the employees were more interested in the business of their company. Although the influence of the state and the political structure on the market was large, the companies were relatively free to decide upon the volume and the structure of production, respecting at the same time the market signals, and especially upon the revenue distribution on production and savings. Družić (1998: 117) however points out that the categories of social ownership had a different impact in different companies, depending on their size.

In fact, large companies dominating the economic structure were highly influenced by different state and political factors and they practically functioned as a state ownership, with the minimal influence of the companies themselves and their employees on the development and business policies. Thus there was no higher identification of the employees with the company they worked in.

Small and middle enterprises enjoyed a higher degree of market freedom. The employees were relatively free to create the business policy and to distribute the achieved revenue. The employees there were willing to invest into their future or into expanding production by refraining themselves from current consumption, which led to income redistribution. This again contributed to the

better identification of the workers with their company, than it was the case of large companies.

Croatia, similarly to other Yugoslav economies, experienced a shock provoked by the dissolution of Yugoslavia. Besides that, Croatia had to confront the war initiated by the Serb aggression. Družić notes that 70,6% of the Croatian economy was partially or completely ruined. After the end of the war in 1995, the economy had to find its way into recovery. In this sense, Croatia entered into the phase of transition right after the war, which many other ex-socialist countries did not have to suffer (Czechoslovakia, Poland, Hungary, etc.).

Transition countries opted for different ways of conducting the market privatization and transformation. The dilemma lied in whether it was necessary to transform the former socialist economy into the market economy by a gradual approach, or rather by a shock therapy, implying instant transformation. So for instance, in Hungary, the “case by case” method was applied. In Poland, a mixed model was employed (combining different kinds of privatization: by coupons, sell-out to the employees, or by insolvency). The new countries that emerged, Czech Republic and Slovakia, used the coupon privatization, and Slovenia a compromise mode whereby each step was negotiated between the state and the private sector. All of these countries obtained a different degree of success in their privatization and transformation processes.

In Croatia, the project of ownership transformation is today perceived to be a large failure. It comprised about 3600 ex-socialist enterprises in 1991 and the estimated value of these enterprises amounted to approximately US \$ 20 billion, excluding the shipbuilding, agricultural and oil industry sectors (Družić 1998: 120). The transformation of social ownership, as a special interim period of the Croatian ownership transformation, started in the mid-1991, by the adoption of the Privatization Law. The reasons of such transformation were identified by referring to economic and general economic backwardness in the years prior to transition.

This transition therefore aimed to control rational management and at the same time take care of the value growth of the proprietorship. This implied a huge step: an economic transformation from a non-defined form of social ownership, in which there were no owner's titles, to a strictly defined form of ownership. This motivated the Croatian government of the time, very eager to embrace capitalism as soon as possible to offer shares for sale, and not merely to distribute them among the citizens. Many reasons served as a motivation for this principle, as noted by Družić (1998: 120): the government claimed all of a sudden that everyone had to pay for any service, or otherwise the already high budget deficit would deepen still more. Moreover, the government reminded that it had had to finance a defensive war and that therefore the mid-1990s had to serve to development priorities and settling of social costs of transition (indemnities to unemployed, health and social security).

In general, there were four variants of a transformation model (Družić 1998: 121ff). The first was the buyout of companies. That was a pure version of transformation, whereby the buyer concluded a treaty with the Agency for Restructuration and Development, paid an estimated amount, became the owner and then transformed an enterprise into the limited liability law company or a corporation. The second model was the one of recapitalization, i.e. the capital investment in the company. Unlike that, the third model was the transformation of debt into investment. The fourth model consisted in the transfer of shares and dividends into state funds.

In the process of privatization, it was planned that the process of ownership transformation would be finalized and the market economy established. This implied that owners' shares of which the Croatian Fund for Development disposed, were supposed to find their real owners – entrepreneurs, who would attribute them an efficient economic function by increasing the value of these shares. The privatization stage also encompassed the privatization of the large industries which did not participate in the first transformation stage (oil industry, shipbuilding).

During this transition period, the labour market found itself in a difficult situation. The commitment of Croatia to the market concept of development also determined a new approach to the employment policy. Unlike the concept of full employment during Yugoslavia, Croatia had to determine a new policy consisting in the efficiency principle. Therefore, this implied the reduction of labour force (Barić 1998: 207).

A dominant role of one single party certainly contributed to circumstances in which privatization was conducted by taking political suitability in consideration, and in turn by neglecting the criteria of increasing production and employment on the basis of general restructuring of management and capital accumulation. A special role here was played by manager loans. This was the foundation of the tycoon privatization, as it is dubbed in Croatia, denoting the new rich (tycoons) who acquired everything they possess today precisely in the period of privatization and economic transformation. This stratified the Croatian society in a small number of politically privileged and rich, and on the other hand, plenty of those who were impoverished and without more significant rights (Veselica and Vojnić 2002: 979ff).

Veselica and Vojnić (2002) also quote the wrong policy of stabilization during the period of privatization, by means of the exchange rate of the newly introduced Croatian dinar (HRD) and the German mark (DEM). The initial exchange rate of the HRD in relation to the DEM was 4,444:1. Croatian currency was visibly appreciated already at the beginning, but later on it was even more appreciated until the level where the enterprises were ruined, and new tycoons were constantly emerging. Bankruptcies and insolvencies became everyday news, and unemployment grew to unrecorded levels. Industrial production was doubled and the foreign debt exploded.

Numerous critics warned that instead of privatization and denationalization, this process resulted in the re-etatization of 1998/99. Surprisingly, the government seemed to envisage precisely that: to maintain the control over the national resources and over the choice of future owners and managers, i.e. the

new political and economic elite. The Privatization Law from 1991 recognized the rights of employees and offered them many incentives to buy shares. It seemed that this model really gave preference to insiders.

In practice, however, this did not mean that the employees and workers, but their ex-socialist managers, were given preference. In first two years, managers were successful, together with the employees and workers, in buying major shares in companies. However, in 1993 the policy was again reversed and the limit of only 50% of total company shares for the insiders was introduced. Those who benefited from such an approach were employees in the public sector, war veterans, pensioners and those whose property had been confiscated and nationalized in Yugoslavia (Franičević 2002: 19).

At the end of privatization, 640 000 small shareholders were registered, but this number was significantly reduced during the re-etatization of 1999. Privatization of many companies failed and therefore after 379 000 cancelled contracts with small shareholders the process of deprivatization and, de facto, re-etatization was initialized in 1998 and 1999 (Franičević 2002: 20). War profiteers and new tycoons had already taken everything they could. Many banks were controlled by the state and often not at all transparent. The Croatian Privatization Fund sold shares to company outsiders (domestic and foreign), the process which itself was a disappointment for many in Croatia. A relatively small group of powerful outsiders created about ten huge holdings and took control over hundreds of companies in the sectors of industry, trade, services, the media and banks.

In a survey of 1998 (quoted in Franičević 2002: 21), about 47% expressed themselves as entirely discontent with the privatization, 22 % partially discontent, and only 1% was completely satisfied with it. 65% requested a total revision of all the privatization transactions, 19% found that the revision was necessary only in cases where illegal transactions had already been confirmed, and only 4% was against any revision. Today, even mentioning the privatization provokes bitter sentiments. In chapter 5, I will talk about Croatia

today and indicate some more consequences of the 1990s privatization and transformation.

4.4 CONCLUSION: NEITHER SELF-MANAGEMENT NOR WILD CAPITALISM?

The economic transformation in Croatia was well beyond the economy. It encompassed a profound social change, and, above all, it had a large moral dimension (compare Franičević 2001 and 2002), something which is often overseen. In this sense, speaking about the introduction of capitalism in Croatia in mere terms of numbers and statistics is a mistake. Moreover, combining morality with former and present ideologies is even more dangerous. Unfortunately, both practices are common in today's Croatia.

This chapter aimed to show how well or how bad Croatia fared within Yugoslavia. It is interesting, as it had been stated for several times in the course of this study, that Yugoslavia was not a typical socialist economy, if the Soviet Union is understood as the measure of typical. Right after its creation, Yugoslavia broke away with Stalin, and hence also with his economic ideas. The result was a rather specific model with many advantages, but also many disadvantages, as summarized in Table 2.

As Table 2 demonstrates, the system was generous and perceived as fairer than many others, but it lacked the long-term perspective and precision of the key terms it employed. Moreover, it was highly politicized and its biggest failure was its inability to motivate its labour, not to remain Party-members (because there, it was undoubtedly very successful), but to contribute to a general economic and social development of their country. After the breakup of Yugoslavia, it became clear to which extent the industrialized world was actually ahead – not merely economically, but also politically and technologically.

At this point, it is also useful to compare the growth rates of labour productivity and of technological progress in Japan, Yugoslavia and the Socialist Republic of Croatia within Yugoslavia. For example in the period 1960-1987, Japan had a labour productivity growth rate of 5,4 %, Croatia of 1,7%, and Yugoslavia of only 1,5%. As for technological progress in Japan, in 1973 it amounted to 6,3%, in Croatia to 2,7%, and in Yugoslavia 2,4% (Sirotković 1996: 15). It is therefore clear that although Yugoslavia claimed to be productive and different than other socialist countries, it lacked both motivation and innovation.

While postulating against individualism and selfishness, the Yugoslav model actually supported both of them, because today, many people who are nostalgic about Yugoslavia are actually nostalgic about a panoply of free opportunities they had during Tito's 40 years, such as 'social apartments' they were attributed or symbolic loans for all purposes they were granted by the state. They were ready to forget the politics and the Party manipulation, they were also ready not to have an opinion about anything. And this is where the morale jumps in. Suddenly, such people woke up one day, and they were simply told: "From today on, forget Yugoslavia."

On the other hand, the post-Yugoslav time did not promise them any compensation. Some of them suddenly became very pro-Croatia and anti-Part, others stuck to Yugoslavhood. Yes, it was nice to witness a dawn of a new country, but clearly, the patriotism does not pay bills, it does not feed one's children and it also does not promise a fix salary without too much work. On the contrary, the new era was extremely uncertain, firstly because of a hideous war and all its repercussions, and secondly because it demanded a profound society transformation.

In such an environment, many discovered the magic of private ownership and used the privatization period to become shamefully rich, and they abandoned their socialist beliefs immediately. Others were not that lucky, so they became reluctant and started to hate a new country and the wild capitalism in general, and, even worse, they started regarding the two as a bundle. The

third and the fewest, rare honest patriots who did not search for any immediate material wealth, decided to wait patiently for better times. Obviously, this last group was and remains the most disappointed one.

All this being said, it is legitimate to ask: is there a model for Croatia? As I have argued in this chapter, in today's circumstances neither the return to self-government, nor the re-embrace of a 1990s-type-capitalism, is an option. In several years, Croatia will inevitably enter the European Union, where, contrary to what many politicians claim, not everything will be rosy. Consequently, Croatia will have to have a competent government, a skilful bureaucracy, a sane business sector, and, above all, stable and strong social relations within a motivated population, in order to keep pace with Europe of which it dreams so much. This is going to be elaborated in more detail in the next chapter.

Table 2: Advantages and disadvantages of the Yugoslav economic system

	Why was it good in Yugoslavia?	Why was it bad in Yugoslavia?
State social planning	rationalization of production, possibility of optimal results preparing for economic shocks visibility of different progress in different sectors and ability to act in accordance with economic backwardness	extremely politicized (already the first plan was started in the Soviet tradition, but it was reformulated in 1948, leading to instability) no long-term economic policy or orientation (planning was seen as a temporary phase, but it lasted all the way until the end of Yugoslavia) bureaucrats and politicians were practically one (precondition for a successful career was the membership in the Communist party) the imperative of industrialization

		implied the gradual destruction of peasants and agriculture; the Party did not really know how to handle them, so they were treated by means of a “carrots and sticks” policy
Social ownership	the concept regards neither the state nor the private sector, but the society, as its starting point high social cohesion social equality in the period 1950-1970 relatively high	the notion of social concept seemed and still seems extremely vague, as no one could determine the limits of society; this is why the Party abused the concept and it was the state that decided in all the major points lack of individual motivation, since no individual property lack of motivation for research and innovation (resulting in mediocrity and backwardness); no systemic support for talented ideology instead of society determines the outcomes
Self-management and associated labour	unique system where the labour should play a crucial role and decide for itself management of companies by workers, while property belongs to society (thus not to the state) low unemployment until the 1970s	the labour did not decide for itself: there were managers, bureaucrats and Party politicians instead low productivity, lack of workers' motivation no individual responsibility, hence corruption

PART III: RETHINKING THE DEVELOPMENTAL STATE

CHAPTER 5

AND HOW ABOUT TODAY?

Having analyzed the economic history of both Japan and Croatia up to this moment, as well as the elements of the Japanese developmental state and the Yugoslav planned and self-managing economy, we are now ready to investigate the present developments. In other words, this chapter aims to compare Japan and Croatia in their current and future developmentalist perspectives. However, unlike Part II, where we focused on their economic models of the past, in this chapter we will examine specific actors and their present roles.

As we will see, apart from the state and its economic policy (section 5.1), enterprises and trade associations (5.2) and the regional and international institutions (5.3), this chapter will also take a look at labour unions (5.4) and civil society (5.5) of both countries. In section 5.6 (conclusion), I will reflect upon what a small transition country like Croatia should and should not learn from the pilot developmental state, Japan.

5.1 STATE AND THE ECONOMIC POLICY

In chapter 3, I mentioned how many authors had repeatedly demanded the traditional Japan to change. Meanwhile, has Japan really changed? There are different perspectives in this regard. Calder (1988) defines the Japanese state as a reactive state. In such a state, the impetus to policy change is typically supplied by outside pressure, and that reaction prevails over strategy in the relatively narrow range of cases where the two come into conflict.

On the other hand, Tiberghien (2007: 12) asserts that today, the effect of corporate foreign direct investment inflows remains lower than that of equity

inflows. Moreover, he observes weakening trends since the volume of investment in Japan by financial institutions and corporations is actually diminishing. However, the rising actors are, surprisingly, individuals. In sum, on the one hand the volume of foreign direct investment is decreasing in Japan in the era of globalization, and on the other hand the Japanese state is sometimes seen as passive, needing to be pushed to follow the mainstream. Clearly, there is a paradox there.

Vogel (2006: 214) describes in his book *Japan Remodelled* how the Japanese remodelling really happened. Yes, Japan did remodel, however not into what Vogel dubs a Liberal Market Economy (LME). Although some measures were indeed liberal, such as wage restraints, labour and management collaborate to raise productivity, nonrenewal of non-regular workers and an increase in the share of non-regular workers, others were everything but that. There was a strong shift in lifetime employment guarantee from company to corporate group.

Many main bank ties were renegotiated, and there was a significant shift from lending to universal banking and the effort to restructure the main bank relationships around reorganized corporate groups. A full government regulation was replaced with a new concept: private-sector governance (whereby, again, *laissez-faire* was out of the question). The Japanese government ministries have also converted new roles. The major ministries, especially MITI, have demonstrated a remarkable knack for reinventing themselves. MITI officials helped to orchestrate the bureaucratic reorganization in 2001 that gave them a new name (METI) and broader responsibilities, including the right to contribute to overall economic management by absorbing functions from the old Economic Planning Agency.

In the similar vein, Vogel (2006: 217ff) also reminds that METI (MITI) moved from classic industrial policy to espousing deregulation, cultivating Japan's market infrastructure, and facilitating corporate restructuring. It also developed a new approach to industrial policy itself, i.e. one that seeks to

upgrade certain technological capabilities rather than to sponsor specific sectors or firms, to promote joint ventures and strategic alliances rather than to organize consortia, to revitalize troubled companies with new financial techniques rather than recession cartels and to spur innovation by triggering private investment rather than guiding it directly. Nevertheless, it should not be forgotten or overseen that METI retains in fact the essence of the old MITI: a commitment to promoting Japanese industry, a tradition of working closely with the private sector, and a fierce determination to preserve its own authority.

However, the phenomenon of *amakudari*, or “the glue of the iron triangle” (Prestowitz 1988: 117), persists. From the analysis of Colignon and Usui (2003: 56-80) results that the Ministry of Finance (MOF) remains a central point in the path of *amakudari* to the private sector. Moreover, today *amakudari* are associated with larger, *keiretsu*-affiliated firms, firms located in the Kanto area, and firms in the banking, insurance, and service industries with expanding proportions of employment. The dominant ministries place their ex-officials among the most powerful and well-situated corporations in the private sector. Finally, the METI, but also the ministries of education, transport, the National Police Agency, and the Okinawa Development Agency operate by considering the *amakudari* logic completely normal (Colignon and Usui 2003: 80).

Schaede (1998: 167ff) holds that this phenomenon will not disappear as long as administrative guidance prevails. Actually, she argues that there are two structural factors that constitute a clear obstacle for abolishing the system. The pension system for civil servants is critically underfunded, so that from the government’s perspective the *amakudari* system remains its best substitute. Furthermore, without the *amakudari* system, Japanese ministries and government agencies will be unable to attract the best young students from the nation’s leading universities into civil service. Hence, abolishing the *amakudari* system would require a complete reorganization of the political economy and the regulatory system of Japan.

In the view of Colignon and Usui (2003: 55ff), this phenomenon of placing the former civil servants into business, but also the phenomenon of the iron bureaucracy in general, will indeed continue because Japan is a regulatory society. Besides that, Japan is an economy in which private corporations, as well as public ones, use *amakudari* personnel to increase their information and gain grants and contracts dispersed by the government. Moreover, *amakudari* personnel become what Colignon and Usui call “hostages” for private and public firms when these latter are dealing with government ministries. These hostages may be used to insulate or shield the organization from political or media attack. Finally, *amakudari* provide a basis of information and coordination that reduces significantly transaction costs of companies.

Should the bureaucracy of Japan today be reformed? Yasuhiro Nakasone, former Japanese prime minister, thinks that steps indeed must be taken in this direction. He believes that bureaucrats should be selected and dispatched to various ministries by the central authority (the cabinet), hence that the ministries should not pick their own personnel. Moreover, for promotions to the rank of head of division (*kacho*) or above, the candidate should be required to have served in two other ministries for a certain number of years (Nakasone 1998).

These two measures would help to ensure that bureaucrats focus their loyalty on the nation or the civil service as a whole rather than one particular ministry, and thus reduce the inter-ministry rivalry. However, I hold that Japan could also reconsider a French model, by which candidates indicate their ministry preferences during their final examination at the prestigious École Nationale d'Administration (ENA), and then become the post according to their results. A third reform proposed by Nakasone would be to have a significant percentage of mid-level and senior bureaucrats, such as bureau chiefs, counsellors and administrative vice ministers, be political appointees recruited from outside the civil service, not only from the political world but from business as and academia as well (Nakasone 1998: 52).

In its government-business relations, Japan has already changed to a certain extent. As Tiberghien (2007) argues, 1999 was a crucial year when a major of corporate restructuring swept through the economy. Whereas we cannot be certain yet about the current prime minister Taro Aso, who is also the grandson of Shigeru Yoshida (the prime minister whose smart political doctrine contributed to the post-war miracle), Aso's predecessors Obuchi and Koizumi were indeed what Tiberghien calls "entrepreneurial politicians". Obuchi government clearly announced its support of supply-side reforms and took direct action, such as the Industrial Revitalization Law (August 1999) to induce corporate restructuring. Most of the corporate-related reforms passed in 1999 and 2000 emerged out of the Industrial Competitiveness Council (ICC), and advisory council set up by Prime Minister Obuchi.

According to this Law, many Japanese companies could apply for the government support in the form of tax incentives, exemptions of commercial law requirements regarding administrative procedures, low interest loans etc. By arguing that the reforms emerging from the ICC were not driven by labour unions, nor from the United States, nor from the organized interest groups (Keidanren), Tiberghien shows that Japanese politicians are today less dependent on iron triangles and foreign pressures. However, significant layoffs brought about neo-liberal reforms have to be dealt with very soon, and this is where the Japanese have to recall their past. I will tackle the current state of the Japanese labour policy later on.

In the meantime, let us investigate the role of the state in Croatia today. Moore and Vamvakidis from the IMF (2008) base their report on Croatia by stating the business environment needs to be improved through further measures to reduce the administrative burden, legal uncertainties, and corruption. Crucially for the further argument of this thesis, they urge for reforms to reduce the role of the state in the economy through fiscal consolidation and faster privatization.

Ten years ago, Croatian economists Crkvenac and Kovačević (1998) suggested an export-led model for Croatia. It should consist of a policy of stimulation of entrepreneurship in different companies, which would then trigger off diverse incentives for the business climate of an unfettered interaction of human resources. As they noted, the range of supportive state actions is very broad, starting with a duty-free import of goods aiming to serve in the industrial production, preferential bank loans for starting or encouraging of the existing export-orientated programmes, different tax reliefs to international business partners during their starting-up of export-orientated production., a free transfer of the profit of foreign companies abroad, the stimulation of technology transfer, duty-free zones for the export production etc. (Crkvenac and Kovačević 1998: 281 ff). However, Croatia did not choose similar policies.

Contrary to that, Kesner-Škreb, Pleše and Mikić (2003) argue that state aid to enterprises in Croatia, in their paper examined for year 2001, is absolutely too high and mainly directed to certain industries, primarily transport, shipbuilding and tourism. Therefore, during its negotiations for the EU accession, they claim that Croatia will have to gradually reduce the size of state aid. Their proposal is to redirect the state aid to horizontal objectives, or those that are common to all enterprises, such as research and development, small and medium-size enterprises, training and employment, environmental protection. Finally, they say, the arbitrariness in the allocation of state aid should be minimized and the process of its allocation rendered more transparent.

Jović and Kesner-Škreb (2006) add that the state-aid-to-GDP ratio is four times higher in Croatia than in the European Union, state aid being mainly targeted to particular industries. They suggest for Croatia to reform thoroughly or reduce its sectoral aid to shipbuilding, transport (especially the railways) and the steel industry, as well as aid to rescuing and restructuring firms in difficulty. Why do many insist that much that the state aid is generally bad? Since the introduction of a capitalist economic system, Croatia has been trying hard not to be associated with the strong state. It was one of the countries that were eager

to follow the prescriptions of the Washington Consensus on good governance. In this line, Dragičević (2007) reminds that the bad governance in Croatia is a consequence of low efficacy and rampant corruption as well as of a lack of strategic and creative governance. Luckily for Croatia, the result of the Washington Consensus implementation was not fatal as in other countries (such as notably Argentina).

However, bearing in mind that the Washington Consensus was very superficial in its estimations, some other authors, such as Radošević (2004), propose the development model for Croatia based on the hypotheses of the Post-Washington Consensus, preserving the role of the state to the moderate extent. Nevertheless, since it was argued earlier in this thesis that the Post-Washington Consensus was also quite imprecise and vague in its policy proposals, it should undoubtedly be thought about some other directions. In the meantime, the EU and many Croatian authors criticize notably the size of the Croatian public administration.

The Croatian public administration disposes of 15 ministries, and in addition there are many state administration organizations, offices of the Government and legal entities with public authorities (such as the Agency for the protection of market competition, the Agency for Supervision of Pension Funds and Insurance Companies, the Directorate for supervision of insurance companies, the Central Register of Insured Persons, the Telecommunications Council etc.)

In terms of size, many authors claim that the Croatian civil service should be big enough for the implementation of the planned measures. Between 1991 and 2002 the number of units of local and regional government rose from 104 to 560. In Croatia the general government bill comes to 11.1% of GDP. Expenditure for general public services came to 2.9% of GDP in 2002 (Boromisa 2004: 189).

Therefore, Mervar and Nestić (1999) claim that a smaller public sector which would be more stimulating for the economic growth could be achieved through reducing some non-productive categories of spending (administration, army, and police), through the increase of cost-efficiency of public projects and through the strict control of further growth of transfers. As they add: "Government intervention should be limited to establishing the 'rules of the game' and to the fields where the market is not able to accomplish its role. It is necessary to create an institutional infrastructure for the functioning market economy" (Mervar and Nestić 1999: 138).

Following the similar trend, some scholars conclude that the institutional infrastructure is one of the greatest barriers to an intensification of entrepreneurial activities, namely (Singer et al. 2003: 37): inefficiency of institutions of the legal system, the Government, and the Parliament, i.e., institutions which are the stronghold of legality, social order, and business conditions in general, as well as overly complicated and lengthy administrative procedures, especially procedures related to obtaining entrance visas and work permits, as well as procedures related to land (acquisition of land, registration of land, and building).

What can we conclude from all these claims? Firstly, that the Croatian state is not creative, innovative or cooperative. It is perceived as generally corrupt as it succumbs to interests of powerful interest groups. Basically, no one trusts it. Secondly, we can read out from all the above claims that while not trusting the state, Croatian scholars are very much confident in the outside world. In other words, everything that is appreciated in the European Union or in the United States seems also to be a perfect cure against all Croatian troubles.

While the foreign pressure for reforms, as I had mentioned it earlier, is in cases very desirable, Croatia's own model construction should be envisaged and aspired to. Just as Japan after the Second World War inevitably had to open, Croatia today has no choice in this regard, because the autarchy and isolation are absolutely not an option. Nevertheless, just as Japan created its

own economic model, out of nowhere, from death and destruction, Croatia also has the obligation towards its citizens to find its own best economic model. Following from this, the state has to be present, since it is only under the guidance of the state that such a model has a perspective. Note that I do not claim that the state should be the only agent to carry out the reforms: all social groups, starting from civil society, the private sector over to labour have to participate in this project, *guided by the state*.

The future of industrial policy is certainly, among other things, in the ability of the state to support innovation and invest in research and development. Japan is indeed the best example: from a technologically underdeveloped country, its R&D share reached in the 1990s that of the US and Germany (Saito 2000: 250). Whereas in Japan this conscience has been present for a long time, Croatia ranks well by European standards in comparison to other CEEC, in particular Bulgaria and Romania, according to Aralica and Bačić (2005), but has not made a significant progress in its innovation potential and policy with respect to the EU and other industrialized nations.

In the similar vein, Švarc (2004) contends that Croatia has failed to make the necessary shift from the standard research and industrial policies towards an innovation policy leading to a knowledge-based economic growth. Moreover, many authors plead today for a complete market liberalization of financial markets. However, Vujčić (2003) holds that although capital controls are not a long-term solution, they indeed could be a useful additional instrument for restricting short-term capital flows. In particular, Vujčić adds, in a small and post-socialist country in which capital flows can be particularly volatile and in which the instruments of indirect monetary control are insufficiently developed, capital controls can, if not misused, have a useful role to play.

In a nutshell, if we remind ourselves how the role of MITI in Japan was first rather authoritative and strong (until 1960), and how it then gradually weakened, we might learn some lessons for Croatia and any post-socialist country in general. But, as Komiya (1993) underlines, a condition for Japanese-type

industrial policies to succeed is the existence of a bureaucracy capable of planning, implementing, and administering complicated policy systems. There must be an abundant supply of honest, intelligent, and dedicated bureaucrats. Croatian readers are now certainly sceptic, because they doubt that “honest” and “bureaucrat” might stand together at all. But, as I will argue further on, if bureaucracy and politics are depoliticized, and if none of the actors within the state is predominant, it is possible to attain that goal. Here, the civil society jumps in, and this is what I will elaborate in more detail in section 5.5 and in chapter 6.

5.2 BUSINESS AND TRADE ASSOCIATIONS

In this section, we will ask what is left of the dominant Japanese business, and what is the perspective of its still underdeveloped Croatian counterpart. For Lincoln and Gerlach (2004), the potent conglomerates or *keiretsu* have withered away. The authors conducted an in-depth econometric analysis of 259 firms in Japan, and came to the conclusion that relationships remain central to the Japanese way of business, but they are much more subordinated to the competitive strategy of the enterprise than was true of the network economy in the past.

Others say that today the concept is modernized, due to constant Western critiques of Japan's industrial conglomerates and cartels. However, industrial clusters addressed by Sonobe and Otsuka (2006:4) could be the future of the industrial organization of Japan. The industrial cluster is the geographical concentration or localization of enterprises producing similar or closely related goods in a small area. In view of a historical perspective, it is interesting to find in Japan and Taiwan that industries tend to be born and nurtured in large cities but they tend to be relocated to suburban areas in later stages of the industrial development. Sonobe and Otsuka (2006: 59) further believe that such revolutionary changes in the location of enterprises and the

division of labour among them should be regarded as an integral part of the process of industrial development, as the efficiency of industrial production is likely to require changing industrial locations and production organization over time.

We could identify three most important features of such a concept, taking in consideration the clusters and their relation to the state (Sonobe and Otsuka 2006: 200-202):

- Like *zaibatsu/keiretsu* in Japan, industrial clusters imply non-market institutions that require the government support for construction of marketplace and industrial zones aiming to organize production.
- Furthermore, industrial clusters require the state to provide sufficient training for its future entrepreneurs.
- Finally the government has to set up industrial parks and induce enterprises producing similar products and intermediate inputs to move in so that industrial clusters are formed.

The importance of the state's role is still there. However, Saito (2000) describes how the Japanese economy found itself in the middle of depression at the beginning of the new millennium. In 2008, it again entered into recession. In Saito's opinion, the state the Japanese economy found itself in during the 1990s and after 2000 was due to misinvestment of large funds in land and securities, the delay of government expansionary policy which was in harmony with neoliberal policies implemented at the time, and the delay of monetary policy (due to the previous deflation, lowering the interest rate was impossible because it had already been already very low).

On the contrary, Schaede (2000) believes that the shift from developmental state to a system dominated by industry self-regulation is needed and in fact happening. She holds that the reshaping of power structures, whereby the bureaucrats should become merely advisors of the businesses, will match an increase in private process regulation, or self-regulation (Schaede

2000: 5ff). Under self-regulation she understands a process by which a trade association, comprised of the leading firms in an industry designs rules of trade for that industry and enforces those rules through self-designed sanctions. Schaede (2000: 7) also predicts that the scope and depth with which Japanese associations pursue self-regulation will be more significant than in other countries.

Self-regulation implies the greater influence of trade associations, which have been consistently present in Japan since the earliest times, as we have seen in chapter 3. Japanese trade associations (*jishu-kisei*) have formed basic core units around narrowly defined industry segments for effective industry governance. These core groups unite in several layers of regional and topical intermediate umbrella organization, which in turn link up under large national umbrella federations that lobby for political representation. Due to this multilayered structure, today there are an unusual number of trade associations in Japan (Schaede 2000: 67). As a result of the increasing importance of trade associations, incumbent firms now effectively govern many Japanese markets, in particular in terms of restructuring the distribution system. The record of post-war antitrust enforcement reveals that Japan's antitrust system considers most activities of self-regulation as acceptable (other than price-fixing).

However, Schaede's analysis is far too simplistic and one-sided. Precisely the current global financial and economic crisis of 2008 is the best proof that the market and the system of self-regulation failed. On the contrary, the state is moving toward playing the role of a more independent, neutral agent (Archardoguy 2005). Although the state still manages markets through regulations that bolster domestic firms, support employment and minimize bankruptcies. It is thus premature to conclude that the state has fundamentally altered its role. Firms also recognize the need to allow market forces to determine corporate success and failure much more than in the past. Economic action in Japan is still primarily social action. Archardoguy concludes that Japan

is far from becoming the United States, and that its aspirations do not go in that direction.

In which direction is the Croatian business going? After the war, Croatian recovery was slow but constant. On the monetary level, the economy normalized itself relatively quickly, and as Payne (2002) shows, inflationary dynamics in Croatia between 1992 and 1999 indicated positive correlation with the wage growth and currency depreciation. However, Croatia also faced a series of problems, notably a soaring foreign debt and the rise of unemployment, which in 2008 amounted to \$ 53.3 billion, and 14.8%, respectively.³

In the similar vein, Novotny (2008) notes that the public debt of Croatia amounted to 40,93% of BDP in 2006, and the foreign debt reached 85,3% in the ratio foreign debt / BDP and 171,3% in the ratio foreign debt/exports (2008: 371). Thus, the results are alarming. Croatia is at the very top of comparable countries of the foreign and public debt into the GDP and the foreign debt and export income ratio. But the government focuses rather on export promotion than on enterprise restructuring, as if the exports would produce themselves automatically and independently. This is why, again, the healthy relation between the state and the private sector is of utmost importance.

According to a large survey conducted by Singer et al. (2003), in 2000 only 1% of all Croatian firms were really large firms (Singer et al. 2003: 30). Despite of several smaller reforms in the meantime, insufficient allocation of funds for education, high tax incidence on new businesses, ineffective labour market with high cost of adaptation of employees to the demands of production certainly do not contribute to the entrepreneurial activity of the country. There is no stimulation for the engagement of non-formal sources of financing of start-up business projects, Singer et al. conclude. Professional infrastructure of support (trainings, consulting, networking...) is in its infancy and there is no

³ See the CIA World Factbook section on Croatia, <https://www.cia.gov/library/publications/the-world-factbook/print/hr.html>

standardized quality of service. The lack of education focused on entrepreneurship is the most important factor that negatively impacts the level of entrepreneurial activity in Croatia.

As Singer et al. further note, new enterprises with a potential of high growth, i.e. ones that use the new technology, which expect to create new markets with their products, which anticipate an intensive growth of the number of employees and the launch on the international markets make up a smaller section of entrepreneurial ventures around the world. The number of such enterprises is higher in countries that invest above average sums in research and development. This is why Croatia should also choose that path. Moreover, women in Croatia take part in entrepreneurial activity less often than men (Singer et al. 2003, Barković and Borožan 2004). In Croatia, the ratio of female entrepreneurs is 33%. In the developed countries this ratio is more in favour of women.

As I have already emphasized, the export promotion is only a phase two, because the first step is obviously to reorganize the domestic industry. In that sense, it should be noted that the first minister of MITI, Inagaki Heitaro, made a speech at the time of MITI's inauguration in 1949. He emphasized that an increase in production, the rationalization of enterprises, and the raising of the technical level of industry were all prerequisite to an expansion of trade (Johnson 1982: 193). In other words, contrary to what some argue, Japan was not primarily export-oriented, it was production-oriented. Export growth came out as a natural consequence.

Given the fact that only 1% of Croatian firms are large, it would be irrational to expect that some Croatian version of *zaibatsu* or *keiretsu* decide to overtake the market. However, what the state can support is certainly the creation of industrial clusters as described above. If an example *par excellence* of cooperation should be found, then this is definitely it. The state provides infrastructure, technical equipment and training, and the business elaborates its

own structure. Hopefully, this and future governments in Croatia will come to the same conclusion.

5.3 REGIONAL AND INTERNATIONAL INSTITUTIONS AND COOPERATION

Japan has always served as a role model to its neighbouring countries. After the Asian crisis, it has continued being a country all the other countries look up to, despite the fact that Japan itself was also touched by the crisis. Yoshimatsu (2003) gives the example of the Japanese reinforcement of its development model not only within its borders, but also at the regional level, and even after the Asian crisis. In its efforts to assist industrial restructuring in Thailand, the Japanese government made its Thai counterpart acknowledge the necessity of state intervention in fostering small and medium-sized enterprises.

Besides that, Japan sought to transfer experiences of institution building such as the advisory council system, the policy finance system and industrial development coordinated by trade associations. Thus, the Japanese government maintained and partially intensified developmental state approach in its cooperation with industrial restructuring programmes after the crisis.

Beyond this, Japan is today one of the largest providers of the Official Development Assistance (ODA) for undeveloped countries. Its three institutions (the Japan International Cooperation Agency, the Exim Bank and the Overseas Economic Fund) are the main pillars of Japanese foreign aid. In 2007, Japan was the 5th largest donor in absolute terms, with US\$ 7.7 billion⁴. Moreover, In 2008, in the middle of economic crisis and its own recession, Japan offered US \$ 100 billion to the IMF in order to assist countries especially hit by the crisis. Cynics could remark that Japan would not do any of these actions if it were not

⁴ See the homepage of the OECD,
http://www.oecd.org/document/8/0,3343,en_2649_201185_40381960_1_1_1_1,00.html.

for its own interest, but the fact is that many other countries have been extremely ration with the ODA and the crisis management funding, claiming their own scarce resources.

As maintained by Ito and Patrick (2005), Japan's foreign economic policy has long been founded on its comprehensive security, political and economic alliance with the United States. Japan also committed itself to an open, globally multilateral trading system under the GATT the WTO. This is why it has embarked on a new trade policy, one of bilateral cooperation under free trade or economic partnership agreements. Traditionally, Asian countries have not formed significant preferential trading arrangements.

This being said, the ASEAN Free Trade Area is a regional trade agreement, but the lowering of tariffs among its 10 Southeast Asian members has been slow. Japan, Korea and China were the only three outliers, as they had not joined new regional preferential agreements. Japan's first free trade agreement, with Singapore, became effective in 2002. In the fear not to become isolated from other regional cooperation institutions, such as the EU, NAFTA and ASEAN, Japan has recently become more focused on the region.

The strongest opponents to free trade in Japan, as noted by Urata (2005), are the powerful domestic protectionist forces and lobbies particularly in agriculture, fisheries and other labour-intensive sectors which are Japan's most economically inefficient industries. The conflicts between these sectors and other business and industrial interests have become increasingly open and pronounced, in part due to the negotiation realities of free trade agreements. Japan needs a fundamental reform in its approach to these inefficient sectors whereby Urata suggests shifting to a system of guaranteed income subsidies for existing farmers combined with free imports and acceptance of world prices that will benefit consumer welfare.

The economic history is extremely dynamic, and the adaptation to the current situation is a necessary requirement for any country that wants to

prosper. The adaptation does not have to imply a 360° change, though. In Japan the goods liberalization was overwhelmingly accepted already in the 1960s, but the capital liberalization was regarded with an absolute terror. Johnson (1982: 267) notes for instance that in 1967, MITI introduced a set of rules concerning foreign investment, such as the 100 % liberalization of only those industries in which foreign competition was unlikely, the limitation of direct investment in other industries to joint ventures with at least 50% Japanese participation, etc. Today, such restrictions are not pursued and also not envisaged by Japan. After the Asian crisis, Japan came down to Earth as it realized that following the Anglo-Saxon model, even partially, was not an option. Today, to maintain that Japan or South Korea's capital markets are fully liberalized would be nonsense, as demonstrated by numerous authors (see for instance Archodoguy 2005, Voegel 2006).

Therefore we can conclude that although Japan is today more open to regional and international economic cooperation and despite its adjustment to globalization, it did not renounce the basics of its traditional model. As one can imagine, it is a real art to combine a successful economic cooperation with an inner economic stability. Although itself hit by a global recession, its financial-debt-to-GDP-ratio (debt of financial institutions, not to be confounded with the national or public debt, which is a total debt of all agents within the country) is incomparably lower than that of the US or the Eurozone. This implies that, as many predict, Japanese economy will be less vulnerable and will recover from the recession more easily.

The Croatian economy, on the contrary, is very vulnerable. In spite of the presence of war, break-down of trade with a number of former Yugoslav republics, sharp drop in the trade with the region, restrictions on exports of strategic commodities introduced by the domestic authorities as well as certain degree of imports control introduced by the European Community, the share of goods exports reached 50 percent of the GDP in 1992-93 (Mervar 1994).

Unfortunately, it has stayed at the same level since, while the imports reached over 57% of the GDP.

As a possible remedy, some scholars suggest that Croatian macroeconomic policies should define autonomous export growth; in particular, the increase of “export per capita” as well as the increase of “relative shares” of Croatian exports in the total world trade. This, again, should be a product of cooperation of the state and business. The economic diplomacy has a primary goal to enable low costs of market access to the new markets or/and increase of relative market shares in the old markets for Croatian exporters, removing political barriers and non – commercial (political) export risks. On the other hand, Croatian exporters, with the guidance from the state, should be able to secure competitive advantages for entry into the international market (Radošević 2002).

But, as it known, the foreign trade liberalization is not the only form of the international economic cooperation. While there is a relatively low level of foreign direct investment (FDI) in Japan, Croatia has a relatively high level of FDI per capita, but its structure of international trade and sector specialization is not satisfying (Buturac et al. 2004). In the last years there have not been any significant improvements, as the structure of Croatian trade has an increasingly similar export structure with the countries with much lower levels of the GDP per capita.

Very criticized in the Croatian media and by the general public is the fact that during the privatization period practically all Croatian banks were sold off to larger foreign banking groups. Although Galac and Kraft (2000) maintain that the entry was slow and foreign banks were cautious in their approach to the Croatian market in the late 1990s, there is a widespread sentiment in the Croatian public that Croatia had lost much of its financial and economic independence through the sell-out of domestic banks to the foreigners.

Galac and Kraft (2000) and later also Kraft (2002) argue that foreign banks have cheaper funding sources, possess approximately equal knowledge of the

local market, and employ better cadre than local banks. They add that the foreign banks have channeled funds to domestic banks during the hard times of the 1998-99 banking crisis in Croatia. Finally, they conclude, the arrival of the foreign banks represents substantial foreign direct investment in and of itself. However, in times of financial crises and global recessions such as the one of 2008 and afterwards, it is very difficult to maintain that the overwhelming presence of foreign banks is absolutely beneficial for Croatia.

A considerable share of the EU-scepticism in Croatia derives from the sentiment that the Union will, similarly to foreign banks, limit the Croatian economic *marge de manoeuvre*. As Mihaljek (2003) warns, the free movement of capital and the right of the EU residents to acquire real estate in the EU member states, is decisive during Croatia's EU accession negotiations. It will also affect its real estate market, the tourism industry and the national economy. Again, Mihaljek's conclusion is that Croatia will benefit in the long run from foreign investment in the property sector.

Bearing in mind a number of reasons, Mihaljek proposes rather a gradual approach to the opening-up of the real estate market to non-residents. Such reasons are the potential lack of legislation limiting property speculation, potential spillovers of price increases from the market for secondary residences onto the local housing market, costs of the adjustment in the housing market and construction industry to a sudden large increase in demand for secondary residences, loss of competitiveness in the tourism industry if there should be violations of building regulations and the resulting overdevelopment of coastal areas, and macroeconomic pressures arising from large and sudden capital inflows.

The relationship with regional and international economic institutions is in Croatia not similar to that of Japan, since Croatia obviously is still not in the position to act as a donor or as an important regional player. Croatian relations with Bretton Woods institutions (the International Monetary Fund and the World Bank) have been stable, and in the previous 15 years Croatia has benefited

from different loans, funds and support from them. Despite that, both institutions are often regarded with scepticism and criticism in Croatia.

For instance, Maršić (2004) argues that the structural accommodations demanded by the World Bank have been designed primarily with the criterion of economic efficiency in mind, while the social aspects have constantly been overlooked. To conclude this discussion, however, let me note at this point that, with structural programmes of the Bank and the Fund being far from ideal, Croatia should nevertheless pay more attention to its domestic economic policy, and not merely wait for the rest of the world to intervene in times of crises.

5.4 LABOUR UNIONS AND SOCIAL WELFARE

As we had already noted in chapter 1, contrary to the generally widespread belief, Japan's welfare spending has not been as low as it is often portrayed. In Japan, the developmental state and the welfare state were one and the same. Though other factors were also at work, public welfare helped the state to win democratic support for its developmental policies (Kasza 2006).

In his comprehensive analysis, Kasza (2006) refutes the thesis that Japan is a unique welfare society in the realm of pension policy or health insurance. Japan's programs resemble those of other industrialized nations. Social insurance is similar to that of other countries: young people finance their future pensions by contributing to a collective insurance fund. Moreover, the young finance the old through the pay-as-you-go system, pensions are earnings-related, pensionable age amounts to 60-65, and there are also pensions for unemployed spouses. As for public health, Japan has universal public health insurance for citizens and a comprehensive social insurance. Thus, the Japanese welfare state is as present as it is the case with different industrialized countries.

Unlike health and pension policies, Kasza (2006) shows that Japan's employment programs support a divergence theory of the welfare state. The types of policy instruments, again, are similar to other developed countries: unemployment assistance, vocational training, agricultural policies, etc. However, the extraordinarily aggressive work policies in inefficient economic sectors set Japan apart from other welfare systems. Meanwhile, some elements of this policy have changed in Japan. As shown by Vogel (2006), the labour market has become more vulnerable as it was exposed to external pressures of liberalization.

In 1999, the Japan Institute of Labour published a volume in which it tried to clarify some issues of the Japanese labour market. As it has often been claimed, the most important features of the Japanese labour market are the lifetime employment, the seniority wage and early-retirement schemes. Many economists (Ito 1995, Saito 2000) show however that the lifetime employment is only to find in large companies and that almost exclusively men benefit from it.

The Japan Institute of Labour demolished another myth: that the seniority wage implies the wage rise according to an employee's age and/or length of the service irrespective of a managerial post or individual capabilities. This is most certainly not true, since the efficiency and the achievement determine the wage, and not merely the age of an employee. The Institute also denotes some innovations of the labour market: the early-retirement schemes with better arrangements, increasing temporary transfers (*shukko*) to an affiliated company, the increase of non-lifetime employment, and the increase in mid-career hiring.

At present, things look a little less rosy. Schoppa (2006) contends that the post-war Japanese system ensured lifetime employment for male workers, but also that it refused the government support the private (female) provision of care for children and the elderly. Schoppa claims that two social groups bore a particularly heavy burden in providing for the social protection of the weak and dependent: large firms, which committed to keeping their core workforce on the

payroll even in slow times, and women, who stayed home to care for their homes and families.

Japan's best hope for transforming this system and to create new opportunities for both dissatisfied groups (large firms and women) is to re-channel their frustration in the political process. In 2001 many hoped that the new Prime Minister Koizumi might play this role. Keidanren (Japan Federation of Economic Organizations) leaders as well as many women voters welcomed his leadership. Koizumi however disappointed many of these hopes as he ended up doing little to help women balance work and family (Schoppa 2006: 210).

But trade unions were also disappointed. Weathers (2008) shows in this context that *shunto* (spring labour negotiation offensive) in Japan until recently played an important role in linking wage raises for low-end earners to those of major firm employees, thus promoting social equity. However this system of wage linking mechanisms broke down at around 2000 due to the Japanese economic recession. Unions are presently seeking to revive with diverse campaigns on behalf of small-firm and non-regular workers, and efforts to make wage and compensation demands more flexible. However, up to now they have failed to do that.

Following this discussion, Miura (2008) concludes that despite the fact that Junichiro Koizumi's neoliberal reforms require stronger labour movement, the unions did not manage to revitalize *shunto*. The central thesis of Miura's article is that politics of productivity, being characteristic for developmental state, disappeared in the mid 1990s and was replaced by 'the politics of consumption'. In the course of such politics, workers are treated as consumers or clients, which results in existing labour laws and employment protection becoming outmoded and irrelevant.

According to Miura, the balance of political power was shifted away from bureaucracy toward politicians and the Diet, which might be taken to imply that

democracy in Japan is today healthier than ever. What Miura (2008) however argues, is that the breakdown of *shunto* was due to the Japanese “iron triangle” of business, bureaucrats and politicians. She adds that in order to revive the labour movement in Japan, the country needs above all a stabile political democracy.

This does not seem completely logical knowing that Japanese “lost fifteen years” (from 1990 until 2005) were precisely the time of the attempts to apply neoliberal methods into some areas of the economy, above all the labour sector. Is therefore only political reform needed? Hardly, because Japan’s labour movement until the implementation of neoliberal reforms was more active and efficient than afterwards. In this area, such as in many others, Japan needs an element of its all model back. It does not need authoritarianism, but it does need the state to steer up the cooperation of all participating economic agents.

Croatia also needs the state, because with its unemployment rate of 11,8% in 2007, the country has a big unemployment problem. There are many roots of this problem. Pološki Vokić and Frajlić (2004) conducted a research to find out that Croatian employees are simply not competitive. The findings indicate that the average employee in Croatia is in his/her 40s, undereducated, not mobile and not additionally trained. These findings are in contradiction with Croatian managers’ perceptions about the characteristics of a competitive employee, who should be educated, willing to learn, hardworking, persistent, ambitious and, above all, young.

Moreover, there are not sufficient incentives offered for the highly educated. There is no motivation for educated people to work in the public sector, since relatively low-paid workers benefit more from working in the public sector than high-paid workers do. Moreover, the premium decreases with the education level. Conditional wages of the employees in education sector show that they are the worst positioned among public sector industries (Nestić 2005a).

Politicians often justify their support for non-increasing of wages by arguing that high costs of labour reduce competitiveness. This does not always correspond to the truth, as demonstrated in the work of Švigir (2004). He shows that the growth in exports in specific sectors in Croatia does not correlate with the dynamics of labour costs in that sector. Moreover, the radio, television and telecommunications equipment production sectors, and the food and beverage production sector, which exhibit the highest wage growth, actually represent a *source of export growth*.

Rather, Švigir argues, for manufacturing industry export competitiveness certain non-cost factors are crucial: investment in technological development, an efficient system of distribution, successful marketing campaigns, superlative design and product quality, a flexible management structure, good acquaintanceship with new markets and consumer needs, as well as a pay system that provides incentives for employee creativity – generally, all the factors taken care of by the state. Therefore, no matter which economic agent or sector we decide to analyze, we always conclude it by stating that in Croatia, the state is absolutely necessary.

But above all, Croatia seems to have forgotten about the importance of education. Bejaković (2004: 5) argues that despite the formally acquired educational qualifications, Croatian workers still seriously lag behind the EU member states and some of the Central and Eastern European transition countries. The percentage of highly educated persons is still below the European average, and the same can be said of the effectiveness of schooling and university-level study. Adult education, which is practically the most dynamic sector of lifelong learning throughout the world, is the most neglected area of Croatia's educational system.

Lowther (2004) supports this opinion and adds that the main characteristics of Croatia's education financing are chronic under-funding, lack of equity and transparency in budgetary allocation, unbalanced structure of the education budget in terms of categories of expenditure and source of funds,

and lack of synergy (legislative, professional and institutional) for system change.

Yet not only unemployment, but also income inequality is Croatia's urgent problem. Nestić's (2003) and (2005b) studies show that overall income inequality decreased in the 1973-1983 period, and increased afterwards. The mild increase in inequality was specially observable during the 1998-2002 post-privatization period. Moreover, the income share of the poorest has shrunk due to their lower share in wages and pensions. This is a clear proof that Croatia should restructure, and not dismantle, its welfare state, as many wish it to do that. Here again, it should be noted that Japan is a good example of how a productive state and a welfare state can coexist, and how, if such a state suddenly tries to switch from its old model to a completely different, neo-liberal model of welfare, it will encounter grave difficulties.

In the framework of the Croatian welfare policy, there are the pension system, the health-care and educational systems and, possibly the provision of social housing. Also, there are programmes of social insurance and social assistance. Bejaković and McAuley (1999) argue that Croatia faces more demands than many former socialist states as far as welfare policy is concerned. Both the demands of transition and of post-war reconstruction, which will last for years, due to a high number of veterans, invalids, war widows, and persons with war trauma and psychological disturbances provoked by the war, call for an increase in the level of investment in the welfare state.

Puljiz (2004) has three proposals in this context. The first one is a partial privatization of the social security systems, the second one is the establishment of basic universal rights, as well as of the social protection net, while the third one is the 'individualization of social rights' i.e. the inclusion of the marginalized individuals and groups into society, which means the adjustment of social intervention to the specific needs of the user. All of them are practical, but one should never forget the role that the state should play in this context, because an immediately privatization of a social security system in a country which

should restructure – economically, politically, socially and morally, would definitely be a bad move.

5.5 CIVIL SOCIETY

In this section I will tackle the civil society, a category which is normally not elaborated in the traditional developmental state theory nor in neo-liberal theories of the state. Florini (2002) names several reasons for the rise of importance of civil society today, such as the increased importance of education, information technology and the expansion of the middle class. But, also challenges today have gone global with stronger democratization, which has led to a necessity to face them on a global level. This level, clearly, is not constructed only out of states, but of a variety of different agents. Karlson (1993) reminds similarly that the agents of civil society act both in markets and communities as a counterbalance to the state by forming the long-lasting informal groups. Nevertheless, these

While the previous sections, as well as chapters 3 and 4, focused on the economic history of Japan and Yugoslavia, later Croatia, their economic models, and finally, their present situation, this sections aims to examine briefly the groups of actors ‘in the making’ within both countries. Interestingly enough, although one of the countries described is economically developed (behind the United States, Japan is the second most developed country in the world), and the other is a transition country, both Japan and Croatia have one more thing in common: a relatively underdeveloped civil society.

Japan is making progress though. The scholarship that relates the weakness of civil society to the existence of developmental state is relatively loud. So Pekkanen (2004) for instance concludes that by and large most interest groups and civil society organizations were constrained in influence over policymaking in Japan’s developmental state, and its ‘administrative guidance.’

It should not be overlooked that, due to precisely administrative guidance, the lives of the Japanese had been transformed from the poverty of the 1930s and the death and destruction of the 1940s to some of the highest levels of per capita income on earth (Johnson 1982: 304). During 1970s, under weakened, but still present administrative guidance of MITI, Japan's economy had also mastered two oil crises and emerged in stronger condition, despite the fact that Japan remained the most vulnerable of the world's economies to commercial interruptions.

Johnson's conclusion is therefore that administrative guidance will not disappear in the nearer future. Its extent changed, but it is still there. Many claim that the political insulation demanded in a developmental state also depends upon the insulation from civil society organizations or interest groups. However, it would be erroneous to believe that civil society in broader sense in Japan has emerged only recently.

Vosse (1999) reminds of various labour union protests in the 1950s, opposition movements against the Japan-US Mutual Security Treaty and Tokyo Narita airport, the students' movement in the 1960s, or the environmental-, peace-, or women's movements. These were clearly very significant factors in expanding a social stratum of socially or politically interested and active citizens. In the 1960s, Vosse argues, it seemed as if one were witnessing the formation of an efficient civil society that could provide a social balance against the dominance of the bureaucracy- based political power structure and one-party rule. In the similar vein, Pekkanen (2004) shows in his paper that civil society organizations are proliferating in Japan.

Moreover, Japan's civil society becomes more pluralistic, particularly with groups that emphasize their independence from the bureaucracy. Finally, civil society groups are beginning to forge a new relationship with political parties. This is why, according to Pekkanen, Japan's civil society sector cannot be thought of simply as weak. Rather, a dual structure radiates throughout the subsectors. Interestingly, Japan's particularity is a plethora of small, local groups and, on the other hand, a paucity of large, professionalized groups. One

of Japan's particularities are the neighborhood associations (NHAs), quite plentiful in Japan (Pekkanen 2000). On the contrary, large advocacy groups, or in general a professionalized civil society in Japan, is especially scarce.

Non-profit and non-government organizations have seen a boom over recent years. Yamamoto (1999) describes that in 1995, the government's mishandling of rescue operations in the aftermath of the devastating Kobe Earthquake exacerbated popular dissatisfaction with the central government. On the contrary, the effectiveness of voluntary activities by private non-profit organizations and individuals in the immediate post-earthquake period put the concept of civil society in a positive light. This is why the passage of the NGO Law in Japan was the result of an alliance between the NGOs and politicians, many of who had started to distance themselves from the bureaucracy.

Most of the growth has been precisely in these "new" types of organizations, known variously as "citizens groups" or non-profit organizations, both of which are the Japanese parlance for groups that specifically prize their independence from the bureaucracy, rather than referring to a particular type of group. Moreover, the left-leaning opposition can take the credit for the passage of the NPO law. Eventually, even the leading LDP has recognized benefits of civil society, since it helps it to oppose itself to bureaucrats. Pekkanen (2004) therefore holds that the political picture of Japan now is considerably different than in the 1960s, and that although the unprofessionalized civil society groups still dominate, the move forward is more than obvious.

On the other hand, in Croatia, many foreign NGOs emerged during and after the war. Scholars (see for instance Stubbs 1996) noted that many NGOs operating at that time in Croatia were in the fields of aid, health, and psycho-social provision. Major sources of funding of these NGOs were foreign donors, including governments (e.g. USAID), regional bodies (such as the European Union), and global bodies (for instance UNHCR). Both during and after the war, co-operation with foreign organizations continued. These foreign organizations thus initiated the establishment of a number of associations in Croatia, and

provided these associations with much needed technical support (Bezovan 2001).

Civil society, mostly in shape of associations, also played a significant role in solving war-related problems, assisting in overcoming crises related to refugees and displaced persons, as well as providing for war victims. At that time there was a high level of solidarity among citizens. However, in the mid-1990s this solidarity began to decline and citizens formerly engaged in civil organizations began to withdraw, focusing instead on solving their personal problems. The citizens' withdrawal and declining sense of solidarity was exacerbated by escalating economic crisis and a focus on family problems, leading to a standstill in civil society's development (ibid).

What is characteristic of the post-war period in Croatia is the emphasis on relief models rather than on social development in projects dealing with refugees and displaced people in Croatia. It is clear that 'relief models' are more containable and less likely to lead to a politicization of aid. Instead of social development and community work approaches, heavy emphasis was placed on psycho-social programmes and, in particular, on dealing with war trauma (Stubbs 1996: 9).

There is limited tradition of civil society in Croatia. As Bezovan (2001) rightly observes, its development has been hindered by half a century of communism and totalitarian ideology coupled with a lack of experience with the concept of freedom of association. Citizens' civil engagement, for solving both individual and community problems, has never become really a common practice among the vast majority of citizens in Croatia. Most citizens consider the government and the state responsible for solving their problems.

In Croatia, the term 'civil society organizations' (CSOs) refers to associations, foundations, public benefit companies with private status and labour unions. The links between businesses and CSOs in Croatia are poor (Bezovan 2001: 8), unlike Japan, where, as noted before, this sort of

cooperation has imposed itself as one of very important society relations. Companies almost never support the role of their employees as activists in CSOs. Following the experiences of socialism and privatization of the economy, the business sector does not see any reason for supporting civil society.

However, there is a relatively small number of companies tend to support health institutions, schools, sports and recreation organizations, the church and in rare cases, some small CSOs. On the other hand, some large companies have recently started inviting public tenders for granting donations. The social responsibility of companies concerning problems in their respective communities, as well as their responsibility for public welfare, is thus a serious issue for civil society development in Croatia (Bezovan 2001: 9).

As for the role of the European Union in this context, as noted by Vidačak (2003), the biggest problem is that there is no clear list of priorities and demands on the basis of which it might be possible to monitor the progress made in this area by a candidate country. In the context of foreign pressure, as underlined in multiple occasions in this thesis, this is not very helpful. Although in several countries, via the PHARE programme resources, foundations have been set up for the development of civil society, there is no concrete support by the EU in terms of propositions, models and mechanisms (Vidačak 2003). This is a clear indicator that civic participation in Croatia, thus one of the elements of social capital, should increase and the activist groups multiply. In other words, here, besides the state which ensures the background, citizens themselves are needed.

5.6 INSTEAD OF A CONCLUSION: WHAT CAN CROATIA LEARN FROM JAPAN?

For a country that had been for decades indoctrinated by one and only totalitarian party, comrade Tito's superb personality, the self-governing

economic system and the omnipresent Yugoslavhood for which everyone had a different interpretation, the 1990s came too early and too late at the time. They came too late because many non-socialist countries developed much more rapidly and had lived the phase in which Croatia found itself in 1991 some forty to fifty years before the Croatian independence. However, the 1990s also came too early since Croatia, similarly to all other post-socialist countries, was simply and virtually shocked by the force of capitalism, democratization and liberalization.

In 1991, a grand opening happened to Croatia. It was in a way an opening similar to that of Japan after the Second World War, when the country found itself suddenly exposed to the world. It is however worth repeating that Yugoslavia was a far more open country than its socialist counterparts. Particularly, and in opposition to, say, citizens of Romania or Poland, Yugoslavian citizens were allowed to travel and work abroad (Germany and Austria in particular welcomed many Yugoslav *Gastarbeiter* working as cheap labour force). Japan, too, did not open in 1945 for the first time, since we have seen that already the Meiji Restoration brought its profound modernization. Nevertheless, for both countries a war (the Second World War in Japan and the Homeland War in Croatia) implied a turning point and a new beginning in their political and socio-economic histories.

However, at this point the resemblance abruptly stops, since the two countries chose very different paths. Different? But both of them chose capitalism! Indeed, they both chose capitalism; however at this point it should be talked about many “capitalisms,” since the Japanese “developmental capitalism” of the 1950s and 1960s and the Croatian “post-socialist capitalism” of 1990s had little in common. Even today, as presented in this chapter, many differences persist.

One further point is, as demonstrated in chapter 4, that Yugoslav socialism and Japanese capitalism diverged in many important points, but were also somewhat similar. Some go even so far to claim that Japan was in fact *more socialist than socialist countries*, in the sense that it really applied the

original socialist guiding principles which, on the contrary, had been lost in numerous socialist countries due to their powerful indoctrination and ideologies. Tadashi Nakamae said in that context: “Japan has had a more socialist economy than, say, the Eastern Europeans. Our ruling philosophy has been the convoy system, which means that every company must grow together at the same pace, without true winners or losers” (quoted in Lincoln and Gerlach 2001: 211).

Yet again, the question about what capitalism really is and, on the other hand, what can be really understood as socialism, is not so easily answered. Yugoslavia was more similar to Japan than to the Soviet Union as far as the organization of enterprises was concerned; still, Yugoslavia was more similar to the Soviet Union than to Japan in the context of planning. Although Japan also planned its industrial production, this production was planned without any political connotations in the framework of a long-term strategy. Yugoslavia, on the contrary, always chose shorter periods with goals that were literally impossible to reach. If an economic crisis emerged or came from the outside, these plans were quickly remodeled, redone or retired, if they could not be rescued. This is why these five-year plans were in fact never completely carried out, as I had showed in chapter 4.

Where does today's Croatia stand? After the process of privatization and liberalization, which is almost unanimously proclaimed a large failure (see Družić 1998, Franičević 2001 and 2002, Veselica and Vojnić 2001), and during the EU-candidacy and screening process, Croatia must determine its long-term strategy. If it fails to do it now, its position within the European Union might be very uncertain. Although some Croatian authors (see for instance Dragičević 2007) are still in favour of a full implementation of the Washington Consensus, it is reasonable from today's perspective not to wish to Croatia the destiny of, say, Argentina, as we have seen in chapter 2.

Moreover, the global economic crisis of 2008 is a real test for Croatia as it should rethink its economic policies over again. Maršić (2006) makes the point by arguing that the Croatian negotiation structure with the EU is streamlined in

order to match ambitions to complete negotiations in a very short time, rather than to undertake profound reforms. This institutional set-up concentrates one-dimensionally on executive expertise and reinforces problems on the domestic level.

But, as I have repeated for several times in this thesis, the state is very important, but it is not omnipotent. The state should in no case be ripped its power off, since, as noted previously, state power does not necessarily render it a vicious authoritarian. Nevertheless, this thesis urges that, *besides the state and the business*, civil society, and broader, state's own citizens should not be forgotten. Japan showed that the model of developmental state, if applied consistently, really works. However, Japan is also a proof that if a country chooses an abrupt modernization and liberalization (in Japan's case it has been limited, but it cannot be denied), then its most fragile part of population, i.e. its labour and its poor, will suffer.

Therefore, let us recapitulate the Japanese lesson for Croatia. Franičević's (2001) main argument is that neoliberal approach to post-socialist economic transformation and development seriously misinterprets the role of the state. For any government wishing to transform the state-dominated societies into market societies it does not suffice simply to decompose the state because, as Franičević rightly remarks, the process of market constitution is *per se* very political (2001: 66). Hence, in order to change from the ground an economic system, a different type of political institutions must be constructed, and for this, the state is absolutely needed. In this sense, any "stateless" alternative for the post-socialist countries like Croatia would be fatal.

Some authors (e.g. Boromisa 2004) focus on the reform of the public administration in Croatia as a part of negotiations with the European Union. Surely, something is rotten in the Croatian administration, given its size that does not match its efficiency. Boromisa proposed to clarify the institutional framework, to lay down the organization of the public administration, to reduce the number of ministries (which has meanwhile been done, from 19 to 15 ministries), determine performance criteria and relate institutional budgets to

them, to gradually introduce budgeting in terms of activities, to monitoring reforms in all phases in implementation.

However, I believe that the reform of bureaucracy in Croatia should be more profound and more concrete than merely reducing and coordinating the institutions of public administration. Actually, I consider that a reform *within bureaucracy*, organized similarly to the Japanese and French systems, would be crucial. No, Croatia does not need an iron bureaucracy, nor does it need something similar to *amakudari*. In Japan, the *amakudari* system serves as a compensation for the relatively low wages at the beginning of one's career. This is a wrong incentive for a country in transition. To motivate the young by employing them in the public service with relatively low wages, with the promise that they would be later transferred into the business sector, is undesirable because it would result in inefficiency of both sectors, and would not reduce corruption.

Rather, Croatia should take Japan, or also France, as a model in its initial selection of bureaucrats. Bearing in mind that entering into Croatian public service does not require any comprehensive selection process, it becomes clear why it does not score very high in anti-corruption rankings. A priority for Croatia is de-politicizing its bureaucracy by means of setting up, or building on, demanding university programmes, which would aim to educate professional bureaucrats.

In other words, similarly to Tokyo University in Japan or École nationale d'administration (ENA) in France, Croatia should indeed establish (a) prestigious institution (s) which would form country's professional elite. The state should furthermore stipulate brilliant individuals, irrespective of their educational, social and financial background, who are able to pass a very selective entrance examination at the beginning, and final examination at the end of their education at this unique institution.

At the end of their education, young people should be granted a position in a selected ministry for which they obtained specialization. Such a selection would lead to motivations and incentives other than merely a pure profit, since

the reputation of a prestigious institution would, again like in Japan or in France, certify for one's individual quality, thus increasing their self-esteem and a competitive spirit. By investing considerably more in education and research in general, the state can also be helped, as Vuk-Pavlović's (2001) paper demonstrates, by a large Croatian expatriate scientific community.

Moreover, the number of institutions would not have to be dramatically reduced, if the number of individuals who are employed in these institutions is itself not very large. If we recall that MITI had not more than 200 employees at the peak of the rapid growth period, it is clear that it is not the number of persons, but the quality of institutions that counts. Again, the number of institutions should itself be sufficiently big, since the diversity of areas covered is also increasing.

Concerning the remuneration of public officials, Croatia should organize its bureaucracy according to a seniority wage increase system (not only in the sense of age, but of efficiency). The issue is now raised whether this bureaucracy will be immune to vested interests and business lobbying or rather prone to corruption, as a large proportion has been up to now. Unlike Japan, that scored 7.5 out of 10 in the Transparency International index of corruption perception (whereby 10 means a highly clean, and 0 a highly corrupt society), Croatia scored only 4.2 in the Transparency International Corruption Perception Index Report 2007⁵.

In this sense, Croatia needs a certain amount of what the Japanese call *gaiatsu*, or foreign pressure, in order to combat corruption and to reform its judiciary system. During the EU-negotiations, it became evident that one of the negotiation chapters that would be most difficult to close will be the chapter on judicature. This proved to be right. Although the current government is doing its best to show to Brussels that Croatia is making progress, its problem is precisely that it focused more on *making impressions* than to thoroughly

⁵ See <http://www.infoplease.com/world/statistics/2007-transparency-international-corruption-perceptions.html>.

changing the system. The EU, on the other hand, is sceptical, because its quite negative experience with letting in Bulgaria and Romania, both very corrupt states, leads it to the conclusion that it should rather not rush.

However, the date of the Croatian EU-accession is, contrary to what many think and are obsessed with, not important in comparison with reforms Croatia has to undertake. For its own sake, it should enforce the politics of favouring industrial policies and moderate state intervention *before and in the early phase after* the EU-accession, because later on within the Union, say in 10-15 years, it will be quite restricted in this sense.

It is well known that the EU has very strict rules on industrial competition. Nevertheless, the EU is not, and not should be understood, as a holy cow: during the present recession, it has not so far found a common solution how to combat the crisis, and it most certainly will not, since countries have very divergent interests. Nevertheless, the Croatian state must have a multiple function, since it should promote its industries without leaving behind a comprehensive agricultural policy. Croatia has considerable agricultural resources and neglecting them would imply a significant impoverishment. Hence, Croatia should not commit a socialist error by investing everything into various industries and on the other hand letting its agricultural population live on the edge. Japan focused mainly on industry because in agricultural terms, this country has only very limited resources.

Different EU-states, such as France, the Netherlands or Germany, are not willing to step back from their principles of supporting agriculture, and when the EU-agricultural budget is voted on, this is very clearly seen. Croatia should transform its resources into a benefit, and not into a burden. Its tourism is certainly very important, but it is not the only industry Croatia has. In other words, in selecting industries it wishes to support, the state should indeed be developmental: it should recognize its potential in *all possible sectors*, and then develop its strategy according to this. On the contrary, elaborating a strategy without a real insight into one's potential, just for the sake of *having a strategy*

which the EU and the world could like, is an error which Croatia is not deprived of.

Contrary to what eurosceptics in Croatia fear, and they are numerous (see e.g. Štulhofer 2006), foreign pressure and foreign incentives do not necessarily imply a foreign hegemony. Clearly, in a country like Croatia, with a turbulent history and with a predominant pattern of foreign rule, it is very difficult to convince the people about the advantages of foreign pressure. But, think again of Japan. During the American occupation, it was forbidden to spend more than one percent of its GDP on military expenditure, which released substantial amounts for productive investments. Furthermore, although the Japanese had lagged behind in the technological advances, they caught up very fast (Pilat 1994:15ff).

The occupation had another favourable effect, Pilat (1994) reminds, because it allowed the Japanese to build up close ties with the United States, at that time the technological leader and one of the few major economies which was not in ruins after the war. External military security was assured by the United States in a security treaty, a huge export market for Japanese products was opened up, as well as the integration into the international economic community. At a time when other markets were often closed to Japan, this relationship was of great importance.

No, the European Union does not plan to occupy Croatia, and I am by no means implying that. Rather, I want to emphasize that a relatively small and up to its opening irrelevant country can actually reap benefits out of foreign pressure, of course *if a country's leadership and organization are sufficiently clever*. In this context, a national aspect of the traditional development state plays a crucial role, because it is able to distinguish between the international cooperation and its own priorities.

Put differently, if there is a sufficient political and citizens' will and determination, Croatia can make significant progress well *before* its EU-

accession, be it scheduled for 2011 or 2031. On the one hand, the country is forced to adapt its structure and to eradicate its vices inherited from the socialist era (such as corruption, nepotism, lack of transparency in all spheres of public life). On the other hand, being a candidate country, Croatia can benefit from numerous EU-accession funds, by means of which it can then finance its projects, not so much for the sake of the EU, but for its own good.

As well remarked by Strpić (2000), from the historically based Croatian point of view, a possibility of integration of Croatia into the world center was always in founding a world market “niche”, and never, unlike Japan, in making its own mini-empire. Croatia, as a small European country, has no choice but to pursue its integration by following the Central European and Mediterranean cultural and political traditions.

However, it does have a choice *how* to pursue that integration, and only if its leaders decide to dedicate themselves more to the content than to the impression of the picture Croatia sends to the world, Croatia will actually be able to benefit from globalization and international integration. Otherwise, if they limit themselves to ideological fights, or to borrowing literally everything they see outside without any reflection on Croatia’s social and historical particularities, the worse will happen: the globalized world will swallow Croatia.

Therefore, the best measure against euroscepticism is improving the credibility of *one’s own* national institutions, as Štulhofer (2006: 155) contends: “Measures that increase professionalism, effectiveness and transparency, measures that clearly identify responsibilities and entail concrete sanctions against the government employees who break the laws and rules of professional conduct are an important part of the strategy of reducing euroscepticism. An increase in trust in the national institutions should result in a reduction of distrust in the EU institutions.”

It is certainly very positive to have precise economic goals, such as that in the paper by Mihaljek (2001), to double economic growth in Croatia in the next

15 years. This, however, does not bring us any further, since basically all countries aim to increase their growth. The content of policies, i.e. the way by which a developing and transition country should achieve growth, is crucial, though.

Croatia has a big unemployment problem, and many groups of society are pushing for its solutions. As Bejaković and Gotovac (2005: 217-219) note, for the sake of the improvement of employability and the reduction of unemployment in the Republic of Croatia, it is necessary to carry out a review of the entirety of the labour and social legislation and make changes wherever necessary. Activities related to professional orientation, whole-life education and qualification, professional development and the increase of the total stock of knowledge in society ought to be enhanced.

Moreover, as Bejaković and Gotovac go on, active labour market policy measures must be more strongly directed to persons between 15 and 24 years of age, among whom the rates of unemployment are the highest. They add that “collective negotiations and agreements of employers and workers’ councils should be looked at within the context of sustainable economic growth, and not only as a means for protecting the interests of those currently employed”. This is, I think, a crucial point in this context.

Put differently, it is not only the state, albeit it is in principle its primary task, to solve this problem. It should be helped out by the broader society, i.e. by different groups which constitute it. In order to facilitate the convergence of human capital in Croatia toward the level of human capital in developed countries, it is necessary to act in several directions. First, in future decision-making on wage policies in public services and state-owned companies, the state could take care to adjust wage premiums for educated workers to match prevailing practices in the private sector (Šošić 2004).

With the new strength of non-state and non-business actors, the Croatian society will, similarly to Japan, indeed become much more pluralistic, and

precisely due to the dual relationship between the state, the market and the rest of society, i.e. their cooperation and competition at the same time, all of the actors will have to search for allies in other agents. This will lead to the fact that policies should be on the one hand developmental, as far as economic growth and industrial production is concerned (primary task of the state and the business, with a say by society in broader sense – trade unions, non-governmental organizations, non-profit organizations, civic groups), but on the other hand also human, in the domains such as labour, social welfare and civic rights (primary task of all three groups of agents). I will go in more detail to explore this in chapter 6.

CHAPTER 6

TOWARDS A REVISED THEORY OF DEVELOPMENTAL STATE WITH EMPHASIS ON POST-SOCIALIST STATES

Up to now, I have tried to build up the basis of a comprehensive puzzle: I first offered a review of the existing theory of the developmental state and its critique, and then I produced a comparative analysis of Japan (as an eminent and pioneer example of developmental state) and Croatia (a post-socialist state with, in my opinion, quite unclear ambitions). I concluded this analysis in chapter 5 by asking what Croatia could learn from Japan in the domain of its economic, but also social development.

However, in order to complete the puzzle, I should at this point propose my own view of developmental state on the theoretical level. This view will not be a purely theoretical one though, since I do not believe in the Washington-Consensus-alike approaches, which prescribe certain rules purely normatively, and then expect the global actors to fully adapt to them in given delays. Quite on the contrary, I believe, similarly to the *Jissen-ha* (Japanese economics), that there has to be a strong empirical foundation in order to be able to construct a theory. Moreover, and contrary to any classic theories of the state, I do not hold that any single theory of the state can explain the global phenomena. In line with that, I hold that the social structure within and beyond the state could indeed help us to build a better, more comprehensive theory for developing countries, be it late industrializers or countries that are currently in the middle of economic transition and transformation.

In order to do that, I shall proceed by investigating in section 6.1 to what extent the theory of social capital and a neo-pluralist political and economic theory in general could be useful for further analysis of what I will refer to as 'developmental society'. Section 6.2 will offer basic assumptions of my revised

theory, with important lessons for *post-socialist states*. This section will argue that we do not only need to analyze the actors such as the state, civil society or the private sector from within, but that their inner structure will determine their interdependencies, to which the scholarship should also focus.

With the scope of presenting the revised theory of the developmental state, applicable to post-developmental states, the following two sections will decompose the analysis by investigating in section 6.2.1 the relation of the state and the market, in section 6.2.2 the relation between the state and society. Section 6.2.3 will explore the role of governance in the context of developmentalism. Finally, section 6.3 will conclude the chapter.

6.1 BASIC ASSUMPTIONS

As the first step of this reconceptualization, I will lay down the basic assumptions of the revised theory of the developmental state. In order to do that, I will first distinguish between state authority and its capacities. Unlike many other writers, I will argue that the two notions are not the same. In one next step, I will define, in a fashion similar to pluralist and neo-pluralist tradition, that there are many social groups *within* and *outside* the state, which will render the state structure more complicated than it is usually pictured. Finally, using several findings from the theory of social capital, I will attempt to define the relations between different actors. All this will serve for my analysis of state-economy and state-society relations.

6.1.1 DEFINING AUTHORITY AND CAPACITIES

In my view, the apple of discord is hidden in the question: is the state an instrument of someone or something? Is it autonomous? Is it a beast, or rather a benign creation? To start with, let us choose a rather philosophical definition, which is in my view the most precise one I was able to find. Steinberger (2004: 146) sees the state as “omnicompetent in scope, absolute in authority, and organic in function.”

Omnicompetent in scope means simply that its purview is unlimited. In what I will later refer to as social trust, this notion of omnicompetence will be pivotal.

Absoluteness in authority implies that there is no external source of appeal. Despite the presence of international institutions and organizations, they cannot (and should not) dispute the authority of the state. Moreover, Steinberger argues civil disobedience to the state does not endanger, but on the contrary, underline the presence of the state. Bartelson's (2001: 186) argument goes into the same direction: "The truth of the state is a truth whose validity resides in being taken as a lie; it is only as long as the state is seen as a "deception" that it can continue to exercise any authority".

In other words, as long as there is an implicit understanding, or conscience, of state authority, as long as it is discussed, questioned or disputed – it will exist. In fact one never disobeys the state in the sense of its authority, but rather what may be thought of as an invalid or faulty attempt to express the state's demands, i.e. one disobeys the government rather than the state (Steinberger 2004: 186). Finally, by "organic in function" Steinberger understands the idea that the state is and must remain an organism ("an organism in which whole and part are deeply bound together in a relationship of utter mutual dependence", (322)). Thus, the state is more than simply a government – it is a structure of interdependent and mutually coherent propositions about how things in the world really are (ibid).

In order to avoid confusion, I should at this point offer my own definition, which to a certain extent coincides with Steinberger's and Bartelson's definition. While the literature for the most time mentions "state power", we should consider our starting point a theoretical distinction between state authority in the sense of Steinberger, the notion of state power, and the notion of state capacities in the sense of Weiss (1998). In other words, state authority is an abstract notion which concretizes itself through the choice of the state to act, whereby the notion of legitimate authority becomes the notion of power.

I would define state authority as a legitimate authority of the state within its physical borders, similar to Rousseau's Social Contract, because there is a general will and a general trust of citizens towards concepts such as common judicature,

common army, common market, common education system, and so on. State authority implies legitimacy, but also duties and obligations of the state. Claus Offe (2000:66) noted in this sense: “Geography and history are not the end of the story. The political community of a demos is also defined by a third dimension – a duly constituted authority of state.” According to Rosenau (1999), the spheres of authority differ in form and structure because authority is relational. There have to exist the superior and the inferior, and both sides have to acknowledge their position in order to constitute an authority relation.

In newly created states, in particular those having emerged from Yugoslavia, the ideal of state authority is especially visible, since it has been, as we have seen in the case of Croatia where it was bundled together with the sovereignty aspirations, the guiding principle of the people throughout the centuries. No other institution, or structure, was considered above the independent and the free state. For the Croats, Yugoslavia and its governing structures did not come up with their expectations. So in other words, although Croatian citizens have always wanted to have a Croatian administration instead of a Yugoslav one, they have never questioned the existence of an abstract category of government in general.

Generally, citizens may be seen as a source of trust. Steinberger has a point by claiming that no citizen objects to these concepts on a purely theoretical level. In fact, anarchists do, but I will put them between parentheses here. Anarchy, the entire human history has taught us, rests utopian because anarchy implies primarily uncertainty and distrust. Rather, citizens object the way in which these ideal concepts are institutionalized through **state power**. State power transforms state authority into institutions, which offer only a framework to be precisely defined by agents of state power. Along with its legislative and judiciary powers, agents of state power encompass the executive: a legally elected government, and a bureaucracy, which both carry out the institutionalization of state authority. We should remember Foucault’s argument in his lesson on the governmentality (*la gouvernementalité*), distinguishing the notions of state and government: the state is “like nature, has its own proper form of rationality”, whereas the government

“must find the principles of its rationality in that which constitutes the specific reality of the state” (Senellart 1993).

In dictatorial regimes, state power implies a violent transformation of state authority, because the state denies the right of the ensemble of its citizens, i.e. its source of trust, to express themselves freely. In such circumstances, the example of which is again Yugoslavia in particular in its latest phase, the ideal trust materializes into a concrete distrust, which again, eventually, could even evolve into an ideal distrust. This leads us to the conclusion that, in the long run, dictatorial regimes and anarchies in fact very much resemble each other.

Besides that, the notion of general civic trust does not necessarily have to imply democracy. In dictatorships and totalitarian regimes, this trust is replaced by ideologies, which however have a limited date, as history has shown. Dictatorships do not last eternally, since it may happen the person of dictator dies and the entire dictatorship falls apart (Yugoslavia after Tito's death), or that opposing forces from within (e.g. Prague Spring in 1968, Croatian Spring 1971, Ceausescu's decapitation in Romania), or, in recent times, also from without, intervene and topple the dictator. This was the case in practically all post-socialist European states. Undoubtedly, general civic trust cannot be ever replaced: many have tried, but they did not succeed.

On the other hand, in liberal democracies, the institutionalization of state authority is conducted in such a way that institutionalized state power should not move away from the ideal concept of state authority. This is planned by the agents of state power, i.e. a legitimately elected government, and carried out by state bureaucracy. However, at the point where the citizens do not trust their government anymore, they are entitled to elect another one. In case they perceive all opposition parties as equally bad to the incumbent government and hence if they feel restricted in their choice, they can take initiative and engage in political life themselves. In this way, the libertarian objection that the state serves against personal liberties and democracy is rendered very questionable.

Still, citizens change the politicians within the government, and never the institutions of bureaucracy and government *per se* (again with the exception of anarchy). Thus, persons entitled to represent these institutions are replaceable (for instance, they may not be re-elected or re-appointed in democracies; or for example they die, are assassinated, or eventually abdicate, in monarchies, dictatorships and totalitarian regimes). However, institutions of state power are constant because they are a materialization of the ideal state authority, which is absolute, since it cannot be abolished or amended by any individual, group or institution.

State capacities, in harmony with what has been said in chapter 1, form the ability of institutionalized agents of state power to shape different policies by *cooperating with and responding to demands of* all social groups within physical borders of the state (traditional state) and beyond them (the state in the globalization era). The notion of state capacities is therefore a very dynamic concept. State capacities are different policies that are exercised by agents of state power, and co-shaped by different national and international social groups. We however suppose that the shift in state capacities cannot provoke any change in state authority as an ideal concept, but only in its institutionalization. This discussion is summarized in Table 3. I have taken two examples in order to enlighten my proposed concepts

If power is defined as something pernicious, then the whole perspective points to the same direction: the power renders those who possess it necessarily mean, and they will certainly misuse and abuse it. However, if we distinguish between the authority, power and capacities, this rather one-sided perspective becomes necessarily clearer. Moreover, none of the extreme schools arguing against the state has really explained who or what will the object of trust in the absence of state, be it politically, economically or socially (given the inevitable imperfections of any social order, which result from the imperfections of humanity itself). And, without trust conferred to a particular legitimate authority, who or what will be able to trace the lines of responsibility?

What we can finally conclude from the separation of these three central notions is that the ideal concept of the state is not perceived by the citizens as state authority, but that state power, and especially the capacities of the state vary considerably from one state to other. Moreover, the economic role of the state can be seen as one of the numerous institutionalized creations of the abstract state authority (whereby the state is ideally conferred the authority to ensure the social welfare). Nevertheless, it should not be forgotten that it is also heavily influenced through the interactions with other social actors. Agents of state power may initiate different policies concerning the market, and thereby also shape different state capacities, but they can never act completely alone. This is why the economic intervention of the state is indeed required and desirable, but it should never be carried out without the non-state actors.

One of the forms of such an intervention is, for instance, the industrial policy. It does not consist in the power of the state to intervene in the market, because it the capacity of the state which only forms or initiates a policy; still, either as a reaction to this policy or in form of their own concurrent proposals, different social groups have a capacity of pressure. Consequently, state policies are reviewed or agents of state power dismissed. One could argue that this interaction could block some very useful policies in their initial stage. Yet, without such a dialogue, the price to pay is extremely high: the civic trust risks to be stemmed or even to disappear.

In non-democratic states, institutions of state power may more easily disappear because they had not been well constructed in the first place. However, my proposal presupposes a developmental state which has a government and state apparatus (which most of today's states have), and in which the formation of different social groups and civil society is not proscribed (which, again, is true in almost all countries of Asia, Eastern Europe and Latin America). Russia and China do not fully fit into this scheme, as do not some countries of Africa and the Middle East. There, state authority is existent, but state power and state capacities are not sufficiently elaborated.

Hence, my elaboration mainly refers to 'the old developmental states' of Asia, to Eastern European and Latin American countries. I do not pretend that my theory is globally and universally valuable, and I have already noted on several occasions that it restricts itself to apply some features of the traditional developmental state model in the transition or post-socialist states. Many African countries would need a more comprehensive theory in the domain of state power (institutionalization), since obviously state power is a precondition for state capacities. It is clearly beyond the scope of this thesis to elaborate such a case of developmentalism, but I hope this will constitute a comprehensive research subject in the future.

Table 3: State authority, state power and state capacities in an ever-changing process

STATE AUTHORITY (ideal, invariable):

WHAT DO WE EXPECT?

Example No.1: Trust that the state will protect its citizens against any kind of violence.

Example No.2: Conviction that the state is in the position to offer a decent work to every person.



STATE POWER (concrete, constant in its framework but variable in content, representatives are dependent on general trust):

WHAT ARE PRECONDITIONS FOR OUR REALITY?

Example No.1: Institutionalization of the judiciary system and the current legislation framework.

Example No. 2: Institutionalization of labour conditions, workplaces and enterprises, systems of remuneration, etc .



STATE CAPACITIES (concrete, variable, since dependent upon cooperation of representatives of state power with other social groups):

WHAT IS OUR REALITY AND TO WHAT EXTENT DO WE AIM TO CHANGE IT?

Example No.1: Current government anti-violence policy (state capacity 1) is seen as well thought, but not comprehensive. Hence, pressures by civil society groups in case of increase in general violence, cooperation with labour unions in case there in an increase in violence at workplace, etc., result in the revision and better implementation of judiciary decisions on violence protection (state capacity 2).

Example No.2: Current government labour policy (state capacity 1) is seen as insufficient. Hence, social response/pressure in the shape of labour unions on the one hand, and trade associations on the other; the increase of informal sector; cooperation with different NGOs, etc., result in the revision of general labour conditions (state capacity 2).

6.1.2 DEFINING THE ACTORS

For the start, let us recall chapter 1. Different from Marxists, who base their analysis of power mainly on class domination which is a result of an economic appropriation, or elitists who claim that power should belong to a rather small and closed group; different from neoclassical political economy which depicts politicians engaged in a constant struggle for power and constantly modifying their programmes according to their voters' preferences; different but still reuniting many state theories, the pluralist and neo-pluralist thinkers see the power as dispersed and shared between different social groups. My proposition in the previous sections was pluralist to the extent that it presupposed many social groups. Otherwise, state capacities will remain a static category and eventually evolve into some kind of totalitarianism, as it was clearly the case in former socialist states.

Power, as neo-pluralists rightly argue, is determined by the access to resources, but these do not necessarily have to be monetary resources. Rather, they can be determined by charisma, or historic legacies, or ideologies. In this sense, the Marxist vision of power is highly limited, since it focuses on a single relationship between capital and power. In Yugoslavia, we have seen, money was not at all a primary source of power, since initially it was a historic legacy (Partisans' victory over the Ustashe), the rise of anti-fascism and its transformation into communism, successful attempts of the Communist Party to make a charisma out of Tito, and the economic revival in the first 15 years of Yugoslavia.

Moreover, contrary to the assumptions of the public choice theory, after the breakdown of Communism in Croatia, politicians did not merely strive for votes and they did not adapt their programmes to their voters' preferences, because there was no strong alternative to the incumbent party (HDZ) and its president (Tuđman). The Socialists were discredited and did not have any say because of their Communist past, and other parties were simply too small and overshadowed by the credit of leading Croatia to independence that the HDZ

took. This definitely contributed to the outcome of privatization as described in chapters 4 and 5.

Generally seen, the state is a rather complicated structure in this globalization era, because it is pluralistic within its borders, but the field of interest of social groups constituting it, may again cross its physical borders. In that sense, it would be rather simplistic to claim that the state is an instrument of any single group. States are seen as constructed of social groups which cooperate with international social groups (associations, media) and hence these groups, besides the obvious impact of foreign governments, international institutions and globalized markets, constitute a certain peer pressure for the state in question. The presence of all today's global actors, as already discussed in chapter 2, is a clear proof that the post-socialist and generally all states, wishing to model their economic development according to Japan's example, have to take the plurality of actors and the international pressure as their starting point.

Many post-socialist countries are now either in the European Union already, or are waiting to be accepted, such as Croatia. In order to accede or to become a candidate, all these countries have had to undertake various reforms, of which the economic ones are not always well-suited to them; but in turn the reforms of judiciary, anti-corruption measures, education, cultural cooperation, and so on, are a typical example of a necessary foreign pressure. Otherwise, it is rather questionable when, and if, they would have been carried out at all. The EU has become a sort of Orwell's Big Brother for all these countries.

In this sense, it would be rather erroneous to affirm that in Croatia, as in other post-socialist countries, democratization has not already taken place. As already mentioned earlier, there are several important civil society organizations, associations and, above all, numerous labour unions. The media have also become a lot more transparent than in the 1990s. On the other hand, the Croatian people are very negative and sceptic towards any type of autonomous leadership, given the obvious lessons from the past. However, although the

incumbent coalition government (where the HDZ is a principal party) is not at all weak in relation to opposition, it is far from Tuđman's HDZ.

Hence, it is logical to conclude that today's Croatia, similar to other ex-socialist countries, cannot become the traditional developmental state of Japan from the 1960s. Clearly, the time framework is completely different, historic legacies have resulted with a fear of the autonomous state, and social actors have mushroomed in the last 15 years of democratization. And, obviously, many other factors have to be taken into consideration, apart from merely state-business relations.

Surely these relations constitute the most painful experience of all post-socialist countries, but precisely because they should go on, these countries must not forget the rest of their society. Yet if they are willing to do so, they still have the chance to become an improved developmental state within an improved developmental society. One might call these post-developmental state and post-developmental society, but it is not really the name one should be worried about.

6.1.3 DEFINING THE LINKS

Having described the basic notions of authority, power and capacities, and having defined the actors, I now turn to the notion of relations between these actors. Although numerous objections have been raised against the theory of social capital, as we have seen in chapter 2, the theory is still vividly discussed and defended. Social relations within different and multi-faceted networks of social life had too long been neglected by economists, as noted by Pierre Bourdieu. While there are many questions about the precision and the contextualization of the theory (Fine 1999, 2000), about the measurement of social capital (Grix 2001, Halpern 2005) and about its overuse and the 'cover-all' approach, especially by the World Bank, the theory does still have some merits.

As Halpern (2005: 10ff) notes, social capital consists of a network (network members), of norms, values and expectancies, and of sanctions (formal and informal). Already Woolcock (1998) made use of analyzing social ties when trying to explain state capacities. He decided to use two variables, linkage and organizational integrity, to compare different types of states. As a result, he argued that states with high linkage, thus with a high level of state embeddedness (in the sense of Peter Evans (1995)), and high organizational integrity (thus referring to state's institutional coherence, competence) are developmental states, and that for instance socialist states of the Soviet Union were characterized by high linkages (a very autonomous, bureaucratic state) and low integrity (weak institutions, corruption). While such an analysis is certainly very interesting, it restricts itself to the state, which, for our analysis here, is not sufficient.

Linda Weiss (1998) noted that there is a tendency to move towards a 'developmental society', and not merely to talk about the state. In order to understand the society, we need to be aware of many factors besides its state organization and its economy: history, identity, cultural conflicts and traditions. Both liberal theorists and Marxists have restricted themselves in their political economy merely to bureaucracies, voting systems or markets. On the contrary, as I have tried to show, the shift in the analysis should also encompass *historic and cultural components* of economic and political systems. Only by doing this, a theory can be less abstract. In contrast to many, I do not think it is necessary that we have a global approach by which we would be able to explain every single development, every single war, every economy or every history.

However, as argued by this thesis, the state and the market must not be dismissed because they are the necessary institutions in the time of openness and invisible frontiers. While the market serves as a bond and the background for openness, the state, alone and in cooperation with other states, has a dual function. Its first goal is to provide the necessary economic, institutional, legislative and social background for its interaction with other social groups, and

on the other hand to enable the interaction of social groups *independent of the state*. The second objective of the state is to prevent the abuses of the business sector against other social groups.

Let us start with Halpern' s (2005) approach towards social capital because it offers an interesting insight because the approach is multisided and multifunctional. It does not use just one, but three different levels. Halpern departs from the individual, goes over the meso-level of groups, to end up finally at the macro-, or state and inter-state level. These levels do not stand in a strict hierarchy to each other; rather, the relations between the agents of different levels are similar to each other.

Roughly, one can divide these relations into 'bonding', 'bridging' and 'linking' (Halpern 2005: 26ff). *Bonding* designs close relationships (such as between parents and their children), *bridging* stands for social ties (such as those between friends and social acquaintances), whereas *linking* denotes social links to those with more and less power and resources. On the other hand, Halpern also uses categories of networks, norms and sanctions to explain bonding, bridging and linking on different levels. The micro-level is obviously an individual level, the meso-level stands the community level, and the macro-level denotes the interstate relations. The result is a three-level, multidimensional analysis:

Table 4: Micro-, meso- and macro-levels of social capital

Micro-level

	<i>Networks</i>	<i>Norms</i>	<i>Sanctions</i>
<i>Bonding</i>	Parents	Love and care	Withdrawal
<i>Bridging</i>	Friends, social acquaintances	Reciprocity	Shame and reputation

<i>Linking</i>	Links to powerful	Generosity	Shaming and formal sanction
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Meso-level

	<i>Networks</i>	<i>Norms</i>	<i>Sanctions</i>
<i>Bonding</i>	Neighbourhood or workplace	Community customs	Exclusion
<i>Bridging</i>	Links between communities	Out-group understanding	Group conflict
<i>Linking</i>	Link between strata	Mutual respect	Enforcement

Macro-level

	<i>Networks</i>	<i>Norms</i>	<i>Sanctions</i>
<i>Bonding</i>	Nation or race	Diplomacy and war	International law
<i>Bridging</i>	Patriotism and trust	Treaties	Human rights aid
<i>Linking</i>	Honours and law	E.g. trading links	E.g. United Nations

Source: loosely adapted from Halpern (2005:27)

According to different studies quoted by Halpern, social trust (and thus an abundant social capital) is associated with more effective and less corrupt governments. This is how the concept is understood also by the World Bank: the social capital is measured by means of numerous and extensive surveys, which then result with rankings comparing different countries according to their level of social capital (social trust and civic participation).

This approach is praiseworthy since it can act as a means of pressure among different countries. However, it is far from sufficient. Clearly, such an analysis is severely limited, because social capital, a variable originally not seen as a strictly economic one, is again transposed into a bunch of numbers, statistics and graphs. Let us take an example of an imaginary state in order to show the importance of relations between different social agents. In that state, which is imagined to be democratic, citizens form communities at work, during their spare time, in neighbourhoods, etc (*bonding* and *bridging*). Of course, the citizens alone decide upon their lives, but the feeling of security is indispensable in this context, and they are not powerful enough to ensure it themselves. This, again, is a basis for an abstract state authority.

This is why the citizens will confer the general issue of security to the representatives of state power. This is an example of *linking*. The state will undertake various steps so that citizens can feel safe (for example, by preventing violence in their neighbourhood or by making sure the work conditions are satisfactory, thus by its guidelines for the public and private sectors), thus it will link back. On the basis of this, citizens will trust the representatives of state power and this trust will be a pre-condition for their further evaluations. By the same token, if an enterprise sees that the state will ensure a positive climate for business transactions, it will trust the representative of state power in the future. This is a passive side of the social capital approach.

Although the state has a number of capacities which do not have to result in predatory or elitist undertakings, I am not claiming that these capacities

will never result in bad policies. Therefore, on the active side of social capital, citizens can amend the policies of the state by participating in various civic organizations. Moreover, in such a society the term 'social strata' is rendered flatter if one keeps in mind that politicians, bureaucrats and powerful business are subject to control by the society itself, and that they accede to their posts only by personal merits and results. Utopia?

Not necessarily, because even if the state has failed to hear one group of agents, if it protects the business due to its lobbying but forgets about the labour, the civic participation will lead to a society in which the groups will be more able to defend their rights (bridging and linking). The state and the lobbyists will have to back out, and the trust in the state in general will be reduced. In a future cycle, governments may be reversed; numerous bureaucrats and CEOs put to trial and plead guilty for bribery. This again may lead to a rise in social trust.

What can we learn from such a cycle? First, that social capital will vary, as any other type of capital, and that hence, relations can weaken and strengthen; the state is more developmental in some periods than in the other ones (Japan is here again the best example). If individuals grow up with different norms, rules and regulations in the circle of their families and communities, it is normal to expect that they will replicate this understanding of trust, norms and sanctions in the 'real world'. They will elect their government, work as public servants themselves, or protest against the government – it does not matter how they interact with the state, but their relations are so diversified and pointing to so many directions, within and beyond the borders of the state, that the notion of an arbitrary power is eventually softened.

Secondly, a precondition for all these relations, irrespective of their strength, is trust, and, as its consequence, responsibility. Anyone arguing that the state is always predatory, corrupt, elitist and discriminatory, should try to imagine the society without it. In the socialist vision, it is argued that linking between those with less and more power is in fact redundant and harmful at the same time, since if we abolish the state and the capitalist system, the cleavages

between more and less power will simply vanish. In the post-socialist countries, the problem is considerably more profound.

In the communist era, the vision of all society members sharing the same amount of power was, as described in chapter 4 for Yugoslavia, far from truth. The problem of linking was solved by adhering to 'them', i.e. to the Communist Party. In Yugoslavia, this was particularly visible: those simply wishing to live a peaceful, but very simple and obedient life, were allowed to choose not to belong to the Party. However, all those who wanted to advance in their careers or who aimed to be socially active, were forced to join. Moreover, workers were only formally entitled to self-government, and Yugoslavia was completely centralized. The political and economic centre was in Belgrade, leaving other republics with clearly less power.

After the end of communism, however, old power structures were suddenly erased, but the new ones grew quickly: new parties (still with the majority of old politicians), new tycoons, and the new international code of conduct. In Croatia, the destructive war resulted in thousands of killed, invalids and refugees. Society, irrelevant of its economic breakdown, was physically on the brink of anarchy. New power structures had to be urgently formed. Some of them were less altruistic than the other, but eventually they have in previous 15 years transformed into modern, socially accepted, power structures. Abolishing them would imply a serious concern, irrelevant of their overwhelmingly capitalist nature, because this would bring back these countries *psychologically* 15 years back. Again, not everything can be explained by capital-power relations.

Thirdly, this is not to argue that the legitimate state power cannot be misused – far from that. However, if one realizes and accepts that the inter-agent relations weaken the power of the supreme authority (seen as one of the state in authoritarian regimes), and that the unique combination of bonding, bridging and linking makes the entire process of decision-making more transparent and less hierarchical, then it is easy to conclude that these same various social networks are able to dismiss any abusive state apparatus.

Moreover, they are able to produce a new one, as a response to wrong and failed policies. This again can have various applications in different areas of social life, which I will elaborate in more details in further sections.

Thus, the power can be a repression, but it can also imply enhancing of capacities. The state as a static and ahistoric structure should generally be dismissed, since its action is the product of different, pluralist initiatives. In ex-socialist states, the state must be rendered dynamic and responsive to social needs, because it has to restore its capacities to correspond as more as possible to citizens' expectations (ideal state authority).

6.1.4 DEFINING THE ENVIRONMENT: GLOBAL GOVERNANCE OR SOCIAL CLOSURE?

As I have already mentioned on several occasions in the course of this study, it is fairly difficult to speak of social agents as a precise and a geographically limited groups. Open borders complicate such aspirations to a large extent. Yet as Hewson and Sinclair (1999: 5) rightfully remind, today the myth is being spread about the world market leveling states to produce a 'borderless world'. I hope, and it has been my intention for this thesis, to respond from a different angle to claims like that one. I still do not argue that proposals such as that of, for instance, Zürn (2006: 237): "The national boundedness of traditional governance and the unique or decisive role of the nation state are increasingly challenged under conditions of globalization or societal denationalization," should be completely dismissed, but a borderless world should not be overplayed either.

Apart from an explanation about the open, but still not erased borders, there are two other perspectives, as Hewson and Sinclair (1999) remind. First, there is a more sophisticated view, i.e. that the internationalization of markets has more direct implications for coalitions of domestic interests than for states. Yet another explanation is that global markets are neither new nor that they form a

single integrated world economic space, and so there is no substantial tilt away from the significance of autonomous national policy. An American political scientist James Rosenau used the term 'global governance' in order "to appreciate the ways in which global change is an encompassing phenomenon involving relocations of authority across multiple levels and areas" (Hewson and Sinclair 1999: 5).

In particular, Rosenau used the term global governance in order to emphasize the implications of a widespread reorientation of individuals' political skills and horizons. We can understand the concept as denoting an encompassing trend of authority being relocated in multiple directions (ibid: 6ff). In fact, the global governance does not imply any world government. Rather, it suggests that although the bulk of decisions is made on the domestic level, states often encounter various problems which they cannot solve in any other way but by cooperation.

Guy Peters and Pierre (2006) classify four different models of governance. First, there is an etatist model, with obviously a very strong state and almost non-existent societal agents (dictatorships of the past and the present). In a second, liberal, state type, there is again a state-centric perspective, but societal actors have some autonomous sources of legitimacy, and some claims for involvement, such as for instance corporatist bargaining (Japan in its high growth phase).

Thirdly, there is a 'Dutch model' (Kooiman 2003), in which networks become central, but the state retains capacity to make autonomous decisions and steer from a distance. Finally, there can also exist governance without government, because networks and markets become completely dominant. Both extremes being excluded, most contemporary societies slide constantly between the second and the third model. This dynamics can be explained by numerous factors, but the basic reason in my view is the change in social relations and social trust, which are historically conditioned.

Doty (1996) similarly argues that the term global governance encompasses governance by, with and without government at a transcontinental scale: intergovernmental governance (governance with governments), supranational governance (governance by one single government which contradicts the notion of state sovereignty) and transnational governance (governance without governments, but with transnational and non-governmental organizations). Due to the fact that supranational governance is to a large extent rejected by the national state, intergovernmental governance (to some extent present in the EU) and transnational governance (e.g. the UN) are more common today. In both cases national sovereignty is limited by the considerable levels of delegation in a number of policy areas, whereby private and public governance are often mixed (Doty 1996, Hall and Biersteker 2002).

Hewson and Sinclair remind that, apart from Rosenau, there are also other academic theories trying to conceptualize global governance. So for instance, there is a strand of literature that arose in the context of international regime theory, which had had a significant impact on scholarly thinking in the 1980s. However, the scholars of international regime theory seriously neglect global change and global organizations (Hewson and Sinclair 1999: 11-13).

One second usage of the global governance concept invoked by Hewson and Sinclair is the one pointing out that global change has transformed the environment of the world organizations. This is at the same time the most prolific and widespread strand of literature. But from where we stand today, both scholars conclude, there is still much to be done: "More inquiry is needed into shifts in the political horizons of individuals, into the increasing power of the transnational elites of the global political economy, into the emergence of a global civil society, and, especially, into the rise of global informational elites" (ibid: 18).

Others, again, like Sassen (2002) are trying to rethink governance and therefore speak of an intermediate zone where private authority and state authority meet. She argues that the relocation of national public zones to

transnational private areas lies also inside particular components of national states.

We have already discussed the emergence of a global civil society in both Japan and Croatia earlier in this study. While states have to delegate a portion of their competencies and duties to other bodies, civil society itself, although its particular members may restrict themselves to a specific geographical area, has gone global due to a degree of universality in world issues. So for instance, both in Japan and in Croatia and although these countries have culturally not so much in common, labour unions exist, women claim more engagement at top positions, environmentalists have become more active recently, etc.

Such world issues surely are beyond the borders, but could we really contend that they destroy them, not so much because the state has become weaker (since its *authority cannot weaken as long as there is social trust*, I have argued in this chapter), but *because civil society has become more powerful and more borderless*? Has the internationalization of the state emerged thanks to the internationalization of society? Partly, my answer is yes. I have shown earlier that with a plentitude of social agents, state capacities (and not so much state power, to re-use the vocabulary of this chapter) may be questioned, modified or even initiated by the non-state agents. Due to the global pressure (a generalized version of *gaiatsu*), both the governmental and the non-governmental agents have to negotiate and delegate their tasks. This is the clear-cut governance, as defined above.

However, the newly emerged concept of governance (and together with it the internationalization of the state and of civil society) does not imply the weakening of state authority as a category, and also largely not of state power (supranationality being often rejected in, say, the EU). And so long state authority and state power are present, state capacities can be globalized, partly delegated, amended or even privatized – but never *completely* taken away from the representatives of the national state power (its executive and legislative) and the national civil society. Again, I am not denying the internationalization of state or

society. What I am denying, still, is the affirmation that they are absolute and complete.

In this vein, Palan (1999) rightfully identifies the social closure as the greatest obstacle for global governance. He analyzes the closure of the state and society. The national state experiences closure due to the spiritual unity and the duty of collective organization of its citizens, which had produced that state in the first place. On the other hand, society will also always tend to achieve some kind of closure. It is always some quest for political order, regional national, international, or global, which is implicit. In other words, there is always an attended quest for boundedness and closure (Palan 1999: 64). So despite the internationalization of both the state and civil society, none of them can ever be fully globalized.

Consequently, scholars such as Latham (1999) express their criticism towards the concept of global governance. It is unclear, they argue, what kind of a governing agency would be possible on a global scale. How is governance to be distinguished from, for instance, resistance, command, and contest (Latham 1999)? Moreover, what are the political dimensions and implications of projects of global governance, who would be winners and losers of the process, and, finally how could such outcomes be contested regarding particular systems of governance?

In my view, all these questions can be responded to only by taking into consideration not only the closure of the national state, but also the closure of different societal types and non-governmental actors. I am not arguing that the states or societies are fully closed, but rather that the governance as described above could become global only by consensus, and that such a consensus will very probably lack in the future. Within a national state, even for its non-governmental actors, the national issues will have a clear priority over the world issues, if these do not coincide with each other. As Offe (2000: 65) puts it: "Borders are not barriers, but rather filters or membranes, which can be selectively opened from within..."

Since the subject of investigation of this thesis is the developmental state model application in the post-socialist states, in particular in Croatia, a perfect example for supranational governance in this case is the European Union. All post-socialist countries have had clear-cut aspirations to become the members of the EU. Some of them have already achieved this goal, while others (Croatia among them) are still standing in line for the accession. To what extent can a small country with the socialist past become a developmental state and at the same time embrace its new European future?

Here it is necessary to hearken back to the idea of state sovereignty. The notion of state sovereignty, as a product of Rousseau's 'public will' (*volonté de tous*), is closely tied to the concept of state authority as laid down in the course of this chapter. I argued that state authority is an abstract, but still very present category. If we criticize the government of our state, it does not imply we want to have the very existence of the state abolished. Rather, the state as a regulatory community always holds its implicit, ideal authority, and whereas various governments come and go, this authority is persistent. In this vein, along with such an authority (or the common trust in the state, as I named it earlier), individuals render the state a sovereign.

According to Greven (2000: 41), a democratic polity is constituted out of and by citizens only who together form its artificial body politic and are the last and only source of sovereignty. Put differently, the state will retain its sovereignty in the globalized world as long as its own citizens confer their trust to their elected representatives. Doty (1996: 141) defines sovereignty as "the construction of the inside versus the outside of nations is a function of a state's discursive authority and power, that is, its ability to fix meaning and identity in relatively stable ways." Moreover, sovereignty is a contingent political effect suggests that the social construction of sovereignty is a never completed project. Thus, the necessity for sovereignty is always renewable.

Now how can we link the notion of global governance with that of the developmental state? And, in concrete terms, how can we associate a potential

post-socialist developmental state within its broader environment in this discussion? In the case of Croatia, as I have argued in chapters 4 and 5, the broader environment, or a higher level, is the European Union. In a way, the European Union may be a perfect example of a *peer pressure*, thus of global governance in the sense of no direct government, but rather as a body that suggests socially and politically desirable policies. Moreover, the social trust within a nation state is, according to Halpern (2005) and as discussed in section 6.1.3, an example of bridging, thus of the links between actors that are close and befriended.

But on the other hand, the problem with the EU is that its relationship with nation states cannot be defined by any of relationship types laid down by Halpern. Neither is this relationship entirely what Halpern calls bonding, due to the different national cultural and social inheritances within the EU (something individuals are 'born with'); nor is it entirely an example of bridging, due to patriotism and the feeling of belonging to a certain nation (something that individuals can to a certain extent influence); nor is it completely the case of linking, since linking is a type of relationship with agents holding more power than oneself, and the power of, say, the EU legislation, has been often contested and thus not absolute.

The problem here is, in the first place, the fact that for many, bridging and especially bonding are a direct obstacle to linking within the EU. In fact, in order to obtain some kind of EU-citizenship, one would require a feeling of a belonging to a unique nation, thus to bleach out the bonding and bridging relations of individuals to their own nation state. But as far as this linking is concerned, could it ever exist without creating at the same time some kind of the EU citizenship? In other words, how could the EU hold more power than the nation state? It is a classic debate. For Greven (2000: 46) the EU is an independent source of governance because it effectively and legitimately establishes political aims and policy programmes and reinforces their implementation through its own competencies, resources and instruments. He argues that the EU is a polycentric, multilevel political regime, because today each member state operates on at least three levels of government

(the EU's centralist institutions and competencies exist alongside national governments and local authorities) (ibid: 47). But is the EU a sovereign?

According to Weber's famous definition of a modern state, a "monopoly over the legitimate use of violence" is a necessary element of sovereignty. As Greven (2000: 48) maintains, the EU does not possess military or police forces of its own to enforce its authority in the face of national resistance. However, the practice of opting out and thereby allowing for different speeds and intensities of integration within the EU has proved to be a good means of reinforcing integration in the medium and long terms). But, importantly for Greven, if the EU-supranational elites were to be put under great pressure in their respective national policies by the demands of citizens for a more democratic political process, their room for maneuvering on the European level would be reduced. This would endanger even the elitist approach to European unification. Thus for Greven, the EU cannot become a democracy by following the road thus far taken (ibid: 55).

Offe (2000: 71ff) argues that every provisional solution between the two extremes of full nation-state sovereignty and European supranationalism inevitably violates two key reference values: the protection of the social welfare system and the severing of democratic legitimation. As an alternative he suggests a transfer of the ability to act back to the nation-state, or forward to the EU. While I hold that this is a very realistic approach and that the status quo is not satisfactory at all, I also think that this is a great opportunity for small states wishing to transform themselves in a kind of a creative developmental state.

On the same subject, Zürn (2000: 102) holds that there are immense democratic deficits of the EU. For him, the process of the European integration is not a deliberative process. Thus, all participants do not have to justify their concerns as a matter of public interest, by arguing and by not bargaining. Rather, he claims, the EU is an aggregative democracy, where everyone tries to assert their interest unconditionally. Zürn also concludes that this is not sufficient to constitute a democracy within the EU. In the vocabulary I have been using all the

long, I would put it in the following way: there is a lack of civic trust, and hence also of the ideal authority of the EU, and this is why it is contested very much.

Grande (2000: 117) contends, on the other hand, that the EU can become an extension of the national state. In his opinion, the EU exhibits some state like features such as institutionalization, its member states all have democratic constitutions, the political elites of the EU's member states have shown a strong commitment to democratizing the EU, and finally, the economic and social prerequisites for the establishment of democracy are already satisfied on the respective national levels. Hence, the EU is according to him to an opponent of the welfare state. Nevertheless, McCormick (2007) discusses in this context that the important German sociologist Jürgen Habermas overestimated the accomplishments of the *Sozialstaat*. Therefore, Habermas may have too readily accentuated the feasibility of the EU as a *Rechtsstaat* and a *Sozialstaat*. What McCormick suggests, on the contrary is, a feasibility of a *Sektoralstaat* within the EU, since its various policy sectors bring about its horizontal differentiation.

Still, Grande holds, applying the majoritarian model of representative democracy to the multilevel system of European policy making, creates at least three structural problems: the emergence of structural minorities and the greater sociocultural heterogeneity of the EU, the lack of political accountability and control, and the underdeveloped responsiveness of supranational institutions to the preferences and interests of European citizens. The EU is very heterogeneous. Hence its decision-making cannot be based mainly on majority rule (Grande 2000: 132). Having said all that, I can only conclude that the EU, and global governance in general, will always require the healthy state on one hand, and for most issues a consensus on the other hand. Unfortunately, the one is often a contradiction of the other. Still, the role of civil society and the multitude of agents is to soften that contradiction and reconcile the differences that arise among the national and the multi- or international levels.

6.2 STATE CAPACITIES AND SOCIETY

In this final step, I shall analyze state capacities as described in the previous sections within the context of society. The scope of Part II of this thesis was not to merely present two case studies, one of Japan as the 'old' developmental state and a potential developmental society, and on the other hand, one of Croatia, the post-socialist state and society, which has now entered a new phase of its historic development.

Rather, the aim was to confirm the importance of the role of the state in both types of societies, but also to emphasize the role of society which has to interact with the state. Any attempt of reconceptualization must therefore focus on two types of relationships (Camilleri 1995): between the state and the market on the one hand (section 6.2.1) and between the state and society on the other (section 6.2.2). In this time of global change, it is very significant to be aware of the space this change occupies, as well as of its norms and principles, global architecture and the presence of many agents with international practices.

6.2.1 THE STATE AND THE ECONOMY

It is well known what Karl Polanyi had to say about the state-economy relations. However, it is never redundant to recall it. In his *Great Transformation*, Polanyi distinguishes between two periods of state-economy relations. In the first phase, the market is self-regulating and the state's primary task is that of enforcing the rules of the market. However, as the self-regulating market becomes more destructive, the state is obliged to intervene. In Japan, as we have seen, the process was rather reverse, but this does not endanger Polanyi's thesis. The process described in *The Great Transformation* is repetitive and circular.

The goal of industrial growth can, on the other hand, have a strong ideology nexus, and lead to totalitarianism (as in Yugoslavia or China, or Hitler's Germany). Therefore, today a balance between the state and the economy is a

priority. In this globalized era, the state may choose either delegation of authority (transfer of power to international institutions, in form of global governance discussed above) or reassert its authority by a degree of reregulation and the revival of trade protectionism. It can also leave all to the market, which is fatal, as the recession of 2007/08 and after demonstrates.

So which is the right proportion of the state control of the economy? No one can tell that exactly, but two conclusions can be made. First, it is important not to underestimate the omnipresence of an ideal state authority. Economically, it is an authority based on the trust in welfare. Not only are the citizens ready to establish the relations of bridging among themselves and their communities, or to act in solidarity, in order to obtain welfare. They are also ready to link, i.e. to enforce relations with those with more power or more social relations. The power is therefore not only understood in a classical Marxist sense, as an access to monetary power.

Second, the market participates in political processes. Franičević (2002) points out that demolishing the state and enforcing a free market would imply a political process *per se*. This is the very reason why the process of privatization in many ex-socialist countries failed. Its main objective was to instantly get rid of the state, whereas the history of these countries was precisely a counter-argument for such an initiative. Reacting as if there had been absolutely no history, and undertaking reforms as if, for instance, the year 1990 were the year zero, is the biggest mistake of any Washington-Consensus-type could commit.

But, an attentive reader will now argue, if the state and the market were both very political in socialism, and if their interaction remains political still today in a largely neo-liberal era, then what is the difference? If the analysis in section 6.1 is estimated as correct and if we consider that state capacities, and thus also policies, are created and modified only in cooperation of different social groups including the business sector, then the market is a co-shaper of a political process. These attributes render the market a political institution.

However, the line between cooperation and ideology is often opaque, or even invisible. Only after a certain period of time does it become clear whether the benign cooperation has been replaced by totalitarianism, in which the state and the market become one and the same. And this is a crucial difference between *now* and *then*: today, although without totalitarianism, we risk economic crashes such as the one of the current global financial and economic crisis, attempts to make the state monolithic would be equally fatal. Japan of the 1950s and 1960s was not a monolithic state, and it was not led by any type of particular ideology. It might have not recognized the role of broader society, but the state and the business cooperated closely. Differently than in Yugoslavia, Japan recognized the importance of public *and* private ownership. It never attempted to claim that everything was simply *socially owned*.

As Pierson (1996: 97) stresses, the contemporary state is indeed an owner. Actually, modern states, at both the national and local level, are often society's largest landowners. Furthermore, in the last instance, most states in claiming to be sovereign actually retain certain special rights of ownership throughout their jurisdiction, which they may evoke in times of national emergency. Though frequently under-considered, it is important not to neglect these important property rights vested in the state.

But state is not merely an owner. It is also a producer and an employer. In other words, its task is the provision of public goods. On the other hand, many critics insist that rights to certain forms of welfare provision are an aspect of our shared citizenship and should not be subject to the logic of the market. Hence, as argued by Pierson (1996: 104), the broad pattern of change is more one of the commercialization rather than privatization of the government's welfare activity. While this process is leading to a reduction in the state's economic role as an employer, it also leads to a wholesale increase in its function as a regulator.

For Marxists, notably Bob Jessop, the welfare state can last only temporary, which is a paradox of the capitalist state. As Jessop (2002) claims,

the capitalist state destroyed the welfare state by means of its own “bureaucratism, the juridification of social relations, political-empire building, centralization, clientelism and the intensification of personal dependence” (2002: 87). This is also the reason and the root of what Jessop dubs ‘Offe’s paradox’. In fact, Claus Offe had argued that “while capitalism cannot coexist with, neither can it exist without, the welfare state” (Offe, quoted in: Jessop (2002): 275).

Jessop claims in this context that this Offe’s statement is actually a harsh reality of the capitalist state. The welfare state can be consolidated, but it can never be permanently existent (Jessop 2002: 276). Whereas the argument motivates the further reflection, I have to remark at this point that this statement is as ahistoric as the assumptions of monetarism, for instance. For, I fully agree with Jessop on the temporality of the welfare state, but I do not contend that this is only an issue within a capitalist state.

Yugoslavia was a very successful welfare state in its very beginning, but as soon as it was struck by the oil shocks and its own indebtedness, it ceased to be a full-employment society. In other words, any state with any economic system reacts to its environment, be it again socialist or capitalist. Yugoslavia, as we noted, cooperated with the United States, but it was also one of the co-founders of the Non-Aligned Movement, where the economies were everything but capitalist.

In fact, if we accept that state authority is permanent, but that the representatives of state power and state capacities change in time, due to different historic and socio-political challenges, then, as I pointed out earlier, *any state is more developmental, or more welfare-oriented, at some stages than at others*. The change depends on the amount of trust and social relations among different agents. Obviously, if there was a strong outside pressure, Japan responded by restructuring its developmental state to the extent that it did not change much of its industrial policy, unfortunately however to the detriment of its labour policy. Consequently, this had political consequences

(both Prime Minister Koizumi and Abe had to resign), as well as contributed to the restructuring and strengthening of civil society.

Analogically, Croatia was necessarily founded as a welfare state because it had to take care of its war invalids, widows and refugees, and despite its horrendous privatization which corresponds to a textbook definition of crony capitalism, it remained a strong welfare state which has started only recently to reflect upon the reducing the state participation, motivated primarily by the EU candidature. In other words, the amounts of 'developmentalism' and 'welfarism' are socially and politically, and not only economically, conditioned. And, since the political framework changes, and since the society is never constant, the state capacities which shape developmental and welfare policies also change.

Now the most absurd conclusion would probably be something I will dubhere a 'Rostow-type-conclusion', whereby W.W. Rostow was an American economist and theorist, proposing a theory of economic development in stages. In other words, by claiming that the state is developmental and welfare-oriented in different cycles, one is tempted to produce an analysis by which a universal theory of stages *each* country has to pass in order to be economically well-off. This, I am very convicted, is fully and completely erroneous.

Similarly, my theory of the state-society cooperation might be applicable in Croatia, but not in China, Romania, Chile, or Burkina Faso. There is also no universal cycle of capitalism, socialism or even of what is in German "der dritte Weg". Rather, by proposing the model of developmental state I want to show that an ideology-free model of developmentalism and welfare state is feasible. Put differently, the post-socialist countries are in fact not facing any dilemma; they have choices they have never dreamt of. I am not claiming that developmentalism can work in Croatia identically or even as closely as in Japan. But, as argued in chapter 5, some elements of the Japanese developmentalism should certainly be reflected upon in Croatia.

Generally said, one can go only so far to claim that the majority of today's states have dual policies: they are reactive on one hand, and entrepreneurial on the other. The Japanese state is not an only reactive state, as criticized in the 1980s. All states are at times reactive, because no state is isolated from others. Even North Korea has to cooperate with South Korea, sometimes, to some extent. Therefore, all states sometimes, whereby the frequency depends on their size and power, face a certain foreign pressure, or *gaiatsu*. Even the United States, being the most powerful and wealthy country in the world, faced enormous foreign pressure due to its policies in Iraq, Afghanistan, or the lack of economic regulation which led to a subprime crash. Anti-Americanism is at its highest, and the election of Barack Obama for President is an American response to this criticism.

But on the other hand, all states are at times also developmental (Beeson 2003). How strong should a country succumb to *gaiatsu*? In the 1990s, some authors (e.g. Nakatani 1998) were calling for a "third industrial revolution" (or the information revolution) in Japan. They argued that so long as Japan fails to make a rapid shift from the economic system of the catch-up model to a system that is open to the world, its prospects would not be bright. On the other hand, Katzenstein (2003) demonstrated that external pressure in Japan emanated largely from Washington. In the interest of gaining better access to Japanese markets, US actors tend to pressure directly the Japanese bureaucracy and its ancillary political and social interests.

Japan, however, also showed its other brighter side, as it has been extensively elaborated in chapter 4. It was and remains to certain extent an entrepreneurial state. It has pursued, to the extent possible, a policy of independence in the economic arena. Although it is severely hit by the current crisis, it still does not have as many debt problems as other countries. Its main problem are so many neo-liberal reforms undertaken throughout the 1990s, both at the labour market and in the field of industrial policies. Yet I am sure its developmental creativity will show itself again in its full glitter, because it

definitely has the potential. Japan has not constrained itself through regional integration. Moreover, it has nurtured a set of asymmetrical relations with the smaller states of East and Southeast Asia who have depended heavily on Japan for capital and technology but not for markets (Gould and Krasner 2003).

On the other hand, small and transition countries such as Croatia are certainly reactive states. However, the extent of their entrepreneurship (in the sense of developmentalism) also varies, and is certainly in correlation with their economic development. Hopefully this will also become an issue of a future academic research. Thus, as Yamamura (2003) claims that for Japan, the possible *modus vivendi* can be achieved when decisions to alter policies and practices are made by critically assessing how the long-term strengths of cooperation-based capitalism can be best preserved. This means that decisions must be made unaffected by the Anglo-Saxon capitalism promising perpetual prosperity. Obviously, this is valid for any developing country, and especially for the post-socialist states.

Moreover, as Hook and Harukiyo (2001) note, the next important task for Japanese democracy is to establish a triangular relationship among democracy, globalism and localism at the local level in order to discover an alternative, democratic globalization in place of the present neo-liberal and uncontrolled globalization. Here again, this is a rather general, but still valid statement for many post-socialist countries.

Nevertheless, it has to be restated that every country needs its own implementation. In asking himself whether Japan is the model of the past, Waldenberger (1998) investigates the application of the Japanese production system, such as a model job rotation, work groups and decentralization, in the German car industry in the 1990s. He emphasizes that, although the Japanese model could be implemented to a certain extent, it was not meant to be a universal and global model. Rather, it is up to the creativity of different countries to develop models that suit them best.

In order to maintain healthy state-business relations, institutions are necessary. Japan, as an 'old' developmental state, has been working on its institution restructuring. Aoki (1998: 549) suggests that the bureaucracy alone cannot ever be an autonomous force of institutional change. Even if it designs a blueprint for institutional building, the long-term outcome of its implementation may be different from the one it initially intended. In order for that legal and organizational framework provided by the government to have an impact on institutional building and economic development, complementary change in the private sectors needs to take place. Hence the development of civil society and institutional reform remains a great challenge for the old, but also some potential, developmental states. And this precisely renders them more not merely states, but broader developmental societies.

6.2.2 THE STATE AND SOCIETY

By the same token, Sorensen (2006) rightly observes different changes in statehood. No one can dispute those changes. The real confusion emerges, however, if one, similarly to the inveterate globalists, claims that changes in statehood automatically imply the death of statehood. As this thesis has attempted to show, both theoretically and on the concrete level from two different perspectives, roles of the state changes, but its basis remains. Both industrialized and transition states, however, as we have seen in Japan-Croatia comparison in chapter 5, there has been a clear emergence of diverse groups, associations and movements: briefly, of civil society.

Civil society today is mobile and transnational, since it is concerned with global issues such as development, environment, gender, human rights, security, democracy, ethnic and religious identity, sexual liberation and the rights of indigenous peoples. As Sorensen (2006: 219) notes, though the state may exert a controlling, even coercive influence over civil society, it cannot obliterate it. Also, civil society is sustained by the interaction of associations or communities that vary greatly in form, size and membership.

With changing roles of the state and civil society, theories and their authors also adapt. Pierson (1996) notes that Marxists afford some explanatory autonomy to the state, while pluralists begin to acknowledge that the state may exercise certain powers over society. In the similar vein, many Marxists come to recognize that social forces other than class influence the state conduct, while neo-pluralists concede that business has a privileged position in its access to the state.

Marsh and Stoker (1995) show that states are not a place or structure or agency, but a complex mixture of all three. In what they call a structured privilege, they argue that certain groups enjoy privileged access to the state because of their structural position. Accordingly, states are the sites of intentional and strategic action by various groups of social agents. There is a limited number of bases of structured inequality and privilege, not constituting exclusively in economic and property resources, but also in gender, political resources, and knowledge.

There is a growing recognition that the state has to be taken seriously as an independent source of social power, but this does not put into question the issue of contingency of its policies. In other words, the outcomes over the state and society are in part contingent and open-ended. Not all outcomes are possible, but no outcome can be said to be pre-given, because history, as we have seen in our case studies, plays a determinant role. Finally, it is recognized now that state and societal structures are not given by some underlying characteristic of society, but are forged through political struggles, within and between the state and society.

Pierson (1996: 92) therefore concludes that there are two trends in the recent state theory. Firstly, much greater emphasis upon the uniqueness and contingency of particular state-society formations is placed. Secondly, a self-conscious blurring of the lines that divide the state from the society takes place, and the awareness of their complex interaction is raised. In Pierson's opinion to which I completely adhere, proper object of our critical attention should not be

either the state nor society, but rather the ways in which their shifting division is defined.

Put differently, Japan did not industrialize without a particular historic motivation; its developmental state was also successful and afterwards criticized, again with strong historic motivation; its civil society emerged with a clear historic motivation. Opposed to that, Flath (2005: 37-39) tries to apply the theory of Alexander Gerschenkron to the case of Japanese industrialization. The principal thesis: "The more delayed the industrial development of a country, the more explosive was the great spurt of its industrialization, if and when it came," seems to fit perfectly in the case of Japan, the country which surprised everyone growing out of isolation and poverty. Although Flath finds the thesis very compelling and applicable to Japan, one cannot help but observe how superficial it really is.

Was therefore the developmental state Japan's choice? Its further implementation - definitely, but how about its emergence? As Johnson (1982: 306 ff.) showed, the high-growth system, like the basic priorities of the state, was not so much a matter of choice for Japan as of necessity. He points out that this system grew out of a series of economic crises that assailed the nation throughout the Showa era, such as financial panic of 1927, the oil shock, the invasion of Manchuria in 1931, the fascist attacks on capitalism during the 1930s, the war with China from 1937 to 1941, the Pacific War, the collapse of the economy in 1946, the Dodge Line of 1949, the post-Korean War recession of 1954, the trade liberalization of the early 60s, the recession of 1965, the capital liberalization of 1967-76, and the health and safety crises of the early 1970s. Moreover, as Gao (1997: 224) observes, the famous rejection of the profit principle had originated in 1931-45 to ensure the national mobilization for war. It was therefore more historically than ideologically conditioned, or more than simply following a certain economic theory.

Now the reader might wonder the contradiction: but how can a post-socialist state ever become developmental and creative, if everything is just

determined by history? How can this thesis claim that Croatia has a choice, if the history had already made that choice for it? My answer is simple: the emergence of the developmental state was indeed a historically determined necessity. But, the fact that so many countries, such as notably the Latin American countries, have also tried to recognize that necessity but failed, leaves us with the question: why could it work in Japan?

Because it firstly recognized the necessity, and secondly it was capable enough to implement the right policies to answer this necessity. What I am arguing is that the historic determination is already there: Croatia is standing at the crossroads between the past and the present, but it can choose, and not merely be chosen. Without that conviction, I would have never written this thesis in the first place. Croatia has to choose the model now, and everyone out of the plenitude of social actors should be invited to participate in this decision. The state itself should not and cannot be ripped off its role, because it has been conferred the confidence of the rest of society.

When iron triangles on the one hand, and *gaiatsu* on the other became too much of a pressure, the Japanese realized it was time for them to engage more actively in their country's policy. As already mentioned, they started forming the NHAs (neighbourhood associations) as early as 1960s. However, a need for civil society exploded with catastrophes such as the large-scale earthquake in Kobe (1995) with approximately 5500 victims, and the gas poisoning in the Tokyo-subway in the same year, which motivated solidarity and showed how civil society, if well-associated, can act more swiftly than the state.

On the other hand, the state itself reformed, which was not only a consequence of the Asian crisis, but also of different politicians (notably Prime Minister Koizumi) who, irrelevant if one supports their decisions or not, plucked up the courage to lance new programmes. Under the pressure of society itself, the state could neither vanish, nor be transformed into an Anglo-Saxon variant of a capitalist machine.

Similarly, as discussed earlier, Yugoslavia almost turned into a Soviet-type communism. Why it did not do that, was not due to a super-intelligent leadership able to foresee the consequences of the Soviet communism. As the failed First Five-Year Plan (1947) shows, everything was set and ready to introduce the Soviet etatism in Yugoslavia. However, a political misunderstanding and dispute of Tito and Stalin in 1948 brought about Tito's famous "No" to the latter. Hence, it would be misleading to conclude that Tito and the Communist Party were absolutely clear-sighted and that they rationally chose an alternative economic system. Rather, they simply changed their strategy, as a consequence of a new world order in which Yugoslavia was backed by the United States, France and Great Britain, because the Partisans had fought on the right side.

Moreover, social ownership and self-management were socialist constructs which had another intention behind just ensuring economic welfare: they were the glue of Yugoslavia and the notion of Yugoslavhood. The Croats had no choice but to accept it, due to their miserable four years of the state sponsored by Nazi Germany. But actually, can any pure economic or political theory ever explain this? Did Croatia, a country that followed European industrialization as long as its history allowed it to do so, deliberately choose socialism? Was it 'the state's choice'? Obviously, it is very naive to argue that.

Likewise, was the Croatian independence and also the Croatian choice of capitalism, on the other hand, an entirely Croatian decision? In 1990, the Berlin Wall collapsed and this implied the end of communism. All over Europe, new states emerged, and with them new waves of economic privatization and liberalization, being a wrong, extremist answer to previous wrong and extreme policies. Claude Lévy-Strauss was right: as history teaches us, it is always 'either-or'.

Therefore, with all the necessary respect for the ability of the state to undertake radical changes, it is never alone. Society, somehow in the backstage, but undoubtedly present and led by history, always assists the state.

Going to Vukovar, a hero-city as it is called in Croatia, reminds one of those who initiated the process of what books and theories professionally call independence. Thousands of innocent people died there, maybe not informed of economic or state theories, or of political decision-making, but simply wishing a change.

In Hiroshima, on the other hand, one is profoundly stirred when standing before a little burned tricycle of a boy whose body was blown into bits after the atomic bomb explosion on 8 August 1945. Without any pathos: no changes would have occurred, neither in Japan nor in Croatia, if it had not been for hundreds of thousands of Hiroshima and Vukovar victims. In the similar vein, the First World War had preceded the birth of the first, and Jasenovac and Bleiburg victims had anticipated the creation of the second Yugoslavia. Similarly, Nankin victims marked the culmination of the Japanese imperialism. Thus society, often in the most brutal way, assists the radical changes in political and economic systems.

But today, everything is different, the reader will say. There are less wars and slaughters. However, today, in the shape of organized civil society, society is as active, since it discusses on the global level different government proposals and initiates revisions of planned and already implemented state policies. Hence, talking of a societless state implies a discourse as ahistoric as talking about a stateless society.

6.3 SUMMARY

In this chapter, I have introduced the distinction between the notions of state authority, state power and state capacities. In my view, it is extremely important to be aware that state authority, seen as an ideal concept of societal confidence, is omnipresent. Rather, what society contests is the notion state power, or perhaps better its representatives, the executive and the bureaucracy. Moreover, the state has different capacities, which it can or does not have to

use. If it does, it forms different policies, which are either initiated direct through the pressure of different social groups, or it is rather reverse, that is, society responds to the state policies and calls for their revision.

I believe that starting with such a distinction enables us to understand better the state as a not entirely predatory or vicious instrument of somebody or something. Moreover, I hold that the power does not originate exclusively from monetary resources, and that historic relations of different social groups determine to a certain extent their future relations. In this way, confining ourselves to a state-economy analysis, as it was done in the traditional developmental state analysis, is rather misleading. Societal groups all play a crucial role in any state, and in particular in transitional, post-socialist states. They restrict bureaucracies and governments on the one hand, and the business on the other, traditionally seen as the most powerful and best-organized social groups.

Moreover, I referred to both the state and its environment as heterogeneous, consisting of different groups sometimes overlapping in tasks and definitely crossing the state borders. This facilitates the foreign pressure on the state, and makes it to a certain extent reactive. If it is not well-organized inside, its reactive nature will prevail. However, if it is developmental, or entrepreneurial, it will shape such policies which will be beneficial for its citizens and broad society in general.

Clearly, the state cannot form such policies without the feedback from these same citizens. In this context, I supported the theory of social capital, often criticized as ambiguous. It is indeed ambiguous if we base the entirety of our state-society research only upon the theory of social capital (as the World Bank did, in one of its periods). Yet, as I tried to point out, every theory can teach us something new, but none of them is entirely right. If we simply accept that social relations and therefore social capital are variable, but however can be accepted as a starting point for analyzing state-society relations, then the suggestion of Halpern (2005) to recognize *different types of social relations*

among *different and not homogeneous actors* is indeed helpful for further analysis.

I did not enter into a perpetual capitalism-democracy debate, but I have to emphasize that a Japanese-type capitalism, which arguably contained many elements of socialism, was not shaped by ideologies. In that sense, if we restrict ourselves to debating whether capitalism is really compatible with democracy, we will actually overlook the fact that there is not only one universal type of both capitalism and democracy. The Japanese type of capitalism and of democracy does not necessarily have to correspond to that in Croatia, but *this equally does not imply that the Croatian version of capitalism and democracy has to be identical to that of the Anglo-Saxon world*. I do not contest universal human rights, but I simply think that understanding today under capitalism only capitalism of the United States, whereas there was and is Japan, and understanding socialism only as a Soviet-type communism, whereas there was Yugoslavia, is at least erroneous. Nevertheless, many easily fall into the trap of remaining extremely theoretical and superficial, rather than trying to understand profoundly different social contexts.

CONCLUSION

Alfred Marshall once claimed that all the bad economic policies usually have a two-word, rather catchy name that eventually becomes a cliché (think of *moral hazard*, *crawling pegs*, *crony capitalism*, or the most recent, *subprime mortgage*). I do not believe in such clichés, and hopefully my thesis emphasized that as much as I wanted to. I argued that no theory is universal, and that my developmental state theory revision could be applicable to Croatia and other post-socialist states, but I do not deny the diversity of ‘post-socialisms’. Other countries require other studies. They all certainly have much in common, and they might be thinking about state-society relations in the similar way. Nevertheless, my analysis primarily focused on Croatia and its Yugoslav past.

I also do not believe in extreme ‘-isms’ of any kind. In order to combat them, I argued, society and the state need each other. All ‘-isms’ normally start with a rather moderate proposition, which is then, in line with Straussian binary opposition, brought to an absurd. Thorsen and Lie (2007) argue, for instance, that neo-liberalism and liberalism have little in common, because the first is only one and the extreme version of the latter. On the other hand, Marxists remain very powerful critics of modern statehood, and their analysis is very valuable. However, in many post-socialist states they are rather negatively associated with the past, and therefore rather discredited. Therefore, this discussion precisely leads us back to the question from the introduction, asked by the citizens of these countries: “Should we have chosen something else instead?”

The aim of this thesis was to argue that the citizens of post-socialist countries are not some narrow-minded shoppers in a department store who should buy everything one offers to them. Why should they *choose* a system? Should they rather not *construct* a system which does not deny the benefits of both systems they have had up to now? One should always keep in mind the Japanese case. The Japanese built on their own strengths: their bureaucracy, their

homogenous society and the markets available to them, as Johnson (1982) was the first to show. It is less relevant in this final conclusion *what* they built (this thesis elaborated this earlier), but rather the fact that they did not simply and passively choose.

Even after the Asian crisis, many of them repeated: “We must (...) reexamine our system and our laws in the light of the new global environment in which they must function, and based on this Japanese core, construct a distinctly Japanese form of capitalism. The last thing we need is to alter our ‘consciousness, values and worldview’ only to replace them with the Anglo-Saxon model of capitalism” (Sakakibara 1998: 87ff). To generalize this, I would say that the last thing *any country* needs is to alter its consciousness, values and worldview only to replace them with *any economic model* which is currently ‘trendy’ – whatever this model promises.

“Do not rush like geese into fog”, said Stjepan Radić to the Croats before his assassination. This was mentioned in chapter 4, in a slightly different context, but it can certainly be re-employed here. In this line, I will finish my reflection with a personal anecdote that in my opinion fits very well here. In summer 2008, while doing research for this thesis as a scholar of the Japan Foundation in Osaka, I also had to follow an intensive Japanese-language course. Its final objective was to speak and write relatively fluently about one’s doctoral dissertation topic. After my relatively lengthy presentation, it was time for questions from the audience. One of my teachers, a young Japanese male, stood up and asked in Japanese: “Can you reveal us, what do you think is a single and the most important element that Croatia should borrow from Japan?”

The question seemed very easy, but it was in fact incredibly hard due to its brutal preciseness. To single out one element among many is definitely a challenge. I started answering by recalling similarities and differences between Japan and Croatia, their histories and economies, but I still did not seem to answer his concrete question. One single element... Powerful industry? Social wealth? Social equality? Labour productivity? Incredible patience and endurance?

Diligence to start from zero which eventually enabled Japan to surpass all its competitors? I was fighting with Japanese sentence patterns, grammar, my thoughts, and the question, for approximately ten minutes. And then, it occurred to me.

“The most important lesson that Croatia can learn from Japan”, I said, “is to follow Japan’s readiness and ability to construct its own model. Therefore, a single element to be borrowed is certainly this brilliant mind set which was aware that the economic development should be achieved by constructing, and not by merely selecting. After the war and destruction, isolation and poverty, Japan was tempted to choose between the capitalism, which was to a certain extent imposed to it, and, on the other hand, socialism, as it was the case of many countries that had disputed capitalism. But, Japan chose its own model. It built up its own economic, political and social structure, taking into consideration its own society, and not the world trends. Despite its sudden opening, the American presence and the proximity to Russia and China, Japan did not choose any of the systems its neighbours offered to it. Certainly, historic circumstances also played a role, but it is primarily the Japanese society which should take the credit.”

Suddenly, I realized how stunned the Japanese people in the room were by my answer, as if they had for the very first time realized their own uniqueness. Hopefully, my thesis elaborated much more in detail the bravery of the Japanese approach, than this rather concise answer given on a hot and humid August day in Kansai.

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