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W.G. Huff , Dewit & Oughton

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Discussion

Building the Developmental State: Achieving Economic Growth Through Co-operative Solutions: A Comment on *Bringing Politics Back In*

W.G. HUFF, G. DEWIT and C. OUGHTON

Drawing on the insights of game theory and East Asian experience, this short note argues the importance of co-operative solutions in achieving economic development. To realise these, even genuine developmental states must convince a sceptical private sector of their commitment to economic development. Because of this, credibility should be added to the mix of ingredients necessary for a successful developmental state.

The developmental state, able to promote economic development as in Singapore, South Korea, Taiwan and Japan, has generally been seen largely or even wholly as a matter of political acumen and a competent bureaucracy. While our comment on a recent article in this Journal [*Leftwich, 1995*] does not dispute the importance of these fundamentally political attributes, its purpose is to draw attention to a hitherto little considered requirement in the creation of a developmental state.¹ We use the insights of game theory to emphasise the necessity for economic complementarity between state and private sector (together, civil society) and in this the prime importance of credibility and reputation building, if even the most politically astute developmental state is to succeed. In the absence of a command economy or dominating degree of state capitalism, economic policies sufficiently credible to elicit private sector investment should be added to the components identified as important to the developmental state: an autonomous, technically competent developmental elite and non-challenging, or even subordinate, civil society.

W.G. Huff, University of Glasgow; G. Dewit, National University of Ireland, Maynooth; C. Oughton, University of London. Address for correspondence: W.G. Huff, Department of Economics, University of Glasgow G12 8RT, UK; e-mail: w.g.huff@socsci.gla.ac.uk

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The need to achieve economic credibility is essential for a state wishing politically to become developmental so long as the private sector, after sizing up state economic policies, has the freedom to decide whether to invest or not. For example, Campos and Root [1996: 2] describe how in South Korea and Taiwan 'the business community was courted to build a dynamic industrial base'. In essence, the would-be developmental state's problem can be illustrated with a simple prisoner's dilemma.

Few states come to power without espousing the goal of economic development. Yet most in fact have other priorities. In developing countries states usually turn out to be 'soft' in Myrdal's [1981] sense of corruptly serving narrow group interests, or worse, become kleptocratic states like Mobutu's Zaire. Let us assume, however, a state meets the criteria of 'good' politics: the state is 'hard' in the sense of not merely talking the words of economic development but also having a genuine political commitment to it and demonstrating this with productive investment. Nevertheless, the state has no certainty of realising its developmental goal since the attainment of this objective depends on whether it can convince the private sector to invest too. In the pay-off matrix of Figure 1, the government and private sector each have two possible economic strategies, to co-operate in investment or to defect.

While the government may be committed to a policy of investment co-operation, that is to say it is developmental, unless the private sector can clearly perceive state economic policies as developmental, its best strategy is defection, which implies not investing. If so, the developmental state becomes unachievable; the state's best strategy would similarly be defection. Accordingly, the game's unique or Nash equilibrium is low investment and low development (1, 1) – a no-growth deadlock. Investment by the private sector does not materialise unless it judges the state's economic programme to be credible. Only when this happens can the civil society co-operate. Modelling such co-operation would imply a multi-stage game in which the civil society moved in a co-ordinated way, thus remaining for a sustained period of time at a superior, high growth, high

FIGURE 1
INVESTMENT COOPERATION OR DEFECTION – A PRISONER'S DILEMMA

		Private Sector	
		Co-operate	Defect
State	Co-operate	5,5	0,7
	Defect	7,0	1,1

investment equilibrium, illustrated by the outcome of (5, 5) in the pay-off matrix of Figure 1. A (5, 5) outcome was achieved in East Asia. En route to it, economic growth, widely shared among the population, legitimised the state and this 'reinforced the credibility of the regime, further stimulating investment and economic expansion' [*Campos and Root, 1996: 2*].

Most evidence indicates that a private sector investing its own money formulates an independent judgement of whether economically, not just politically, the state is developmental or not and so whether to support it and invest in productive enterprise. Acting in its own, not national, interests a private sector which does not regard the state as economically credible withholds co-operation in the form of investment. Even regimes politically determined to pursue investment can founder on this rock of economic credibility and reputation: 'economic bureaucracies must generate sufficient confidence in the minds of the always sceptical audience of private entrepreneurs so that they are willing to bet their capital in ways that will make expected policy outcomes a reality' [*Evans, 1998: 68*].

Because the private sector has no way of knowing for certain whether the state's economic strategy is to be believed, typically the intending developmental state must put in place some independent, external check on its credibility. We argue that because an economic policy shift towards export orientation can be seen objectively to succeed (or not), this affords an independent check on economic competitiveness and so the credibility of the state and its developmental rhetoric. Bruton [*1998: 921*] notes of Taiwan in the 1950s and South Korea in the 1960s that just such a policy shift to export orientation 'convinced many observers that the two countries were reducing distortions, moving toward getting prices right, and – most evident of all – were exporting'. The demonstrated credibility of economic success in world markets would help to explain why so many of the states cited as developmental have also been economically export-oriented. A balanced growth model featuring an enhancement of agricultural development and so the size of the domestic market has also been suggested as conferring the necessary government economic credibility to elicit private sector investment [*Grabowski, 1997*].

International and domestic economic policies are not, of course, mutually exclusive: they can reinforce one another, as the experience of successful developmental states shows, in building an ongoing relationship with the private sector. From a policy viewpoint Singapore was unusual in that the private sector with which the government established credibility and reputation consisted overwhelmingly of foreign multinationals. By the 1990s they accounted for three-quarters of manufactured output and over four-fifths of Singapore's direct (that is, made in Singapore) manufactured exports [*Huff, 1995, 1999*]. But the importance of credibility was identical.

Multinationals knew that they 'could trust Singapore because other MNCs always said that Singapore lived up to its commitments'. According to the chairman of DuPont, 'In other countries things would constantly come unglued, whereas in Singapore, once they said something, they stuck to it' [Schein, 1996: 125]. Sound economic policies, an ability to implement them and the 'government's role in winning credibility' have been judged the three 'crucial and general lessons' of Singapore's development experience [Soon and Tan, 1997: 265].

Once the state has successfully achieved its developmental objective and the economy enters into a new phase of development, it can comfortably assume the role of a leader [Rodrik, 1992]. Then, the private sector becomes the follower, merely reacting to the policies of the state. Under these circumstances, the state can limit its intervention to 'directive' policies only (for example, subsidy programmes), rather than investing itself.

One can imagine how credibility of state economic policies with accompanying reputation may be gained over successive stages and, as suggested above, modeled as a game with multiple moves played between the duopoly of state and private sector [Dixit, 1996; Huff, Dewit and Oughton, 2001]. The larger point, however, is, given both the state's political and economic credibility, the possibility of the superior, high-level growth equilibrium. In contrast to a view of the economic development process which sees growth being achieved through the competitive struggle, this note stresses that study of the developmental state suggests co-operation as the superior alternative. A state's mere claims to be developmental or even its genuine aspirations in this direction are not sufficient. Co-operation necessary to achieve the developmental state must grow out of an ability to convince the private sector of the government's commitment as well as its power to implement developmental economic policies.

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NOTE

1. Leftwich [1995, 1998] offers especially clear and useful statements of the political attributes of the developmental state. For other literature on the developmental state see Amsden [1989], Evans [1995], Johnson [1999] and Wade [1990].

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