

Northeast Asia's Future: Mobilization System Lifecycles

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Mobilization systems I

- Cope with some intense fear or overriding goal: war, recovery from war, domestic instability...
- Focus on economic growth, usually at severe cost to geopolitics, politics, social comfort
- Reach around world for best practice to overcome weaknesses of existing system
- Structure polity around strong leadership
 - With strong social support because of shared fears
 - Impose “harmony” on business-labor relations...
- Rely on political-business-(military) coalitions to dominate politics regardless of formal constitutional structure



Mobilization systems II

- Rely on banks more than capital markets, because government can control banks
- Impose wide-ranging administrative guidance on firms so government can achieve its goals
- Government underwrites survival of major banks and firms
 - In return for right to guide them
 - In order not to lose a key link in managing war or warlike efforts
- Japan copied these elements from Hitler's Germany and Stalin's Soviet Union as part of war mobilization
- South Korea, Taiwan, Singapore, Indonesia copied from Japan
- China copied from South Korea, Taiwan, Japan, Singapore



The Asian miracle: What Japan taught Asia

- **Global search for best practice**
- **Gradual economic opening**
- **Gradual marketization**
- **Ruthless implementation of whatever was necessary for economic efficiency—aluminum, textiles...**
- **Rising domestic & international competition**
- **Emphasize export efficiency rather than import replacement**
- **S Korea, Taiwan, Singapore, Malaysia, Thailand, Indonesia followed**
- **Economic success generates geopolitical influence even without great military power**



The Asian miracle restructures geopolitics

- Now any country can become powerful, prestigious and influential through rapid economic growth and downgraded priority for military
- Modern military technology renders traditional rise through conquest Pyrrhic



Japan in longer term perspective

- Japan 1955-'75 was dynamic, reformist, globalizing
- Japan 1975-present was dominated by reactionary interest groups, turning inward, rejecting globalization & competition
 - **Agriculture, banks, construction, property, retail dominate politics**
 - **Success, actually based on globalization, became ascribed to “unique Japanese cultural characteristics” (copied from Germany, USSR)**
- Japanese voted against LDP, not for DPJ
 - **DPJ is an incoherent collection of LDP reactionaries, old socialists, religious groups, and idealistic youth**
 - **Role of Ozawa showed that the old interest groups still dominate**
- DPJ government is a phase of continued decline, not revitalization



Japanese decline is quiet but risky

- Thoreau: “Most men lead lives of quiet desperation.”
 - In Japan’s case, very quiet
- Real incomes gradually shrink
- Permanent employees decline; temporary & overtime rise
- People know they won’t get full value of their pensions
- Anomie, anxiety, like a U.S. executive who fears being fired
- Political alienation; votes don’t matter; election outcomes have little effect on policy
- Quiet desire for serious leadership; vacuum awaiting charisma
- Rise of right wing under Koizumi/Abe/Aso shows dangers
 - Abe & Aso were so bad that this danger abated



Mobilization system decline

- Fear dissipates, may become hubris
- Sense of urgency ceases to bind bureaucracies, business
- Bureaucracies & business achieve a scale & coherence that provides enormous influence
- Interest groups dominate government--zoku
- Most dynamic people join business, not government
- Globalization drive dissipates; protectionism & emphasis on local culture rise
 - Japanese ascription of success to “unique cultural characteristics”



Others follow parallel pattern

- Malaysia has been suffering from mobilization system decay
- Indonesia: Suharto stayed on a decade too long, far worse outcome than Japan
- South Korea & Taiwan escaped decline, achieved competitive political & economic systems
- Singapore lasted longer, because of small size, reached decision point in 2011, now heading toward liftoff
- China is at the decision point



Does Japan need a crisis?

- Great periods of globalization, innovation and growth have followed shocks
 - Early Meiji era
 - Post-World War II recovery
- Koizumi averted a great shock
 - But saved the 1955 system, prolonged Japan's agony
- Everyone hopes Japan can revitalize without a crisis
- If not, bond market collapse will affect whole world



Mobilization systems

- **Are useful for:**
 - **Preparing for and fighting war**
 - **Recovering from war**
 - **Initiating economic development**
- **Are not useful for:**
 - **Managing a complex modern economy & polity**
- **Usually arise only in conditions of:**
 - **Great fear or stress**
 - **In societies with some minimum level of cohesion**



South Korean history

- **Syngman Rhee, 1950s, focused overwhelmingly on military**
 - **Continuation would have led to North Korea-style decline**
- **Democracy under Chang Myon, 1960-'61, was weak**
 - **Inflation, ideological division, corruption, disorder**
 - **Economically, militarily & politically inferior to North Korea**
 - **Students rioted against weakness**



South Korean mobilization system

- **Park Jung Hee, 1961-1979, introduced mobilization system**
 - **Coup, then elected, perpetuated his rule by dictatorial methods**
- **Overwhelming priority for economic development**
 - **Cut military budget**
 - **Deemphasized ideology**
 - **Tightly managed economy from Blue House**
 - **Built infrastructure**
 - **Established a dozen chaebol**
 - **Gradually marketized & liberalized the economy**
 - **Built solid government institutions**
 - **Globalized talent—think tanks**
- **Regime supported by chaebol, military, rural people, non-Christians**



South Korea's transition

➤ Political changes

- Satisfaction of basic needs surfaced other values
- Complexity: interest groups
- Crisis of 1979
- Transparency & corruption
- Crisis of 1980: democracy, Kwangju, Chun Doo Hwan

Full transition delayed until 1988 & beyond

➤ Economic changes

- Complexity
- Worker revolt
- Corruption, borrowing and the crisis of 1997

➤ Gradual transition to fully competitive economy & polity



Taiwan

- Under Chiang Kai-shek, fully committed to socialist economics & Leninist politics
 - Communist Party & Guomintang very similar
 - Guomintang captured the cities first, was defeating the Communist Party, but was crippled by the Japanese invasion
- On Taiwan, big Party enterprises dominated the economy, Taiwanese confined to 200,000 small trading firms
- Land reform, as in South Korea & China, improved income distribution & urban industry
- Gradual economic liberalization; formerly small firms became dominant
- Gradual political liberalization



South Korea & Japan 1998

- **National financial crisis—worse in Korea**
 - **Leading companies in trouble—worse in Korea**
 - **Banks illiquid—worse in South Korea**
- **Security fears over North Korea**
 - **South Korea's problem worse**
- **Imminent demographic decline**



South Korea & Japan today (I)

Korea

- Bank reforms stronger
- Economy more open
- Labor more globalized
- Society more globalized
- Women more equal
- Political leaders prioritize growth

Japan

- Bank reforms weaker
- Economy less open
- Labor less globalized
- Society less globalized
- Women less equal
- Political leaders ignore economic reform



South Korea and Japan today (II)

Korea

- **Democracy provides real choices**
- **Growth vigorous**
- **Stock market bullish**
- **Samsung, Hyundai, Korean Airlines stronger**
- **Rising international influence**

Japan

- **Key interest groups control both parties**
- **Growth negligible**
- **Stock market flat**
- **Sony, Toyota weaker, Japan Airlines bankrupt**
- **Declining international influence**



Korea's role

- **Old theory: South Korea the meat pressed into a sandwich between technologically superior Japan and faster developing China**
- **New reality: Japan increasingly the meat pressed into a sandwich between more competitive Korean firms and larger Chinese firms**
 - **Samsung-Sony**
 - **Korean Airlines-Japan Airlines-Air China**
 - **Financial markets: China is bigger, Korea more sophisticated, Japan fading**
 - **No Japanese Apple, Microsoft, Google**

China

- **Followed earlier Asian miracles, but with Chinese characteristics**
 - **Land reform**
 - **Gradual economic opening**
 - **Gradual marketization**
 - **Gradual political reform**
 - **Excellent infrastructure**
 - **Superb, flexible planning**
 - **Globalization**



Hu/Wen era: Three great achievements

- Superior management of global financial crisis
- Extraordinary development of China's interior
- Progress of extraordinarily effective public administration system

- Economic achievements were accomplished without new reforms



China's new politics I

1990s

- **Charisma**
 - **Entrepreneurial**
 - **Decisive, risk taking**
 - **Leaps: Hong Kong 1982/1997**
- **Cosmopolitan**
- **Centralizing power**
- **Government halved**
- **Political reform rapid**
- **Corruption structurally curtailed**

Today

- **Institutionalization**
 - **Administrative**
 - **Pragmatic, unemotional**
 - **Incremental compromise: HK 2010**
- **Local**
- **Interest groups, provinces**
- **Government doubled**
- **Political reform stalled**
- **Corruption structurally enhanced**



China's new economics I

1990s

- **Growth at any cost**
- **Rapid market reform**
 - **50 million lost SOE jobs**
- **Emphasis on markets**
- **Inefficient state enterprises**

Today

- **Enviro consciousness**
- **Inequality consciousness**
 - **Income; region**
- **Stalled market reform**
 - **“Harmonious society”**
- **Emphasis on SOE value**
 - **In financial crisis**
 - **In interior—Chongqing**
- **Overprofitable SOEs**



After brilliant crisis management, pre-crisis dilemmas have returned

- Exports, infrastructure no longer effective drivers of GDP
- Persistent inflation, higher than official statistics
 - Housing prices still rising; jewelry, tea, commodity bubbles
- SOEs fabulously profitable, liquid
- SMEs financially squeezed; few new firms
 - 21% bank reserve ratios squeeze out marginal customers (SMEs)
 - Negative real interest rates subsidize SOES
- Economy like a school of fish with big ones eating children
 - Big fish very happy & energetic, but at great cost to future



China at the crucial decision point

- **Business as usual scenario: Modified Japan trajectory**
 - **Economy will do better than Japan**
 - More competitive at home
 - More open abroad
 - More committed to globalization
 - **Politics will do worse**
 - Stalling at low level of income, technology, higher inequality, lower legitimacy
- **Reformist globalization: Modified Singapore trajectory**
 - **China has already avoided trap of Japanese provincialism**
 - **Singapore model limited in a very large population**
 - **Interest groups, expansion of government inhibit reform**
 - **Nonetheless, this model could carry China to global leadership**



Northeast Asian geopolitics

- Economics will continue to determine geopolitical weights
- South Korea will be the consistently dynamic, rising power
- Japan will continue to be the regional sick man
 - **Could blow up financially, could reform (probably after blowup)**
- U.S. will continue for many years to be the predominant military & technological power
 - **But not the hegemonic provider of public goods. Hence, G-0 world**
 - **U.S. military will be pushed offshore**
- China's geopolitical influence will rise even without reform (Japan 1975-89) but then stagnate or become predominant
- Russia will continue to be Canada with a lot of weapons but very little influence



Appendix



China's new politics II

1990s

2011

- **Designated succession**
 - **Secure**
- Princelings restricted
 - **Leaders admired on merit**
- Popular resentment of stress of social reform
- Leadership with military background
- Popular fear, support for rapid change
- Expanding rights & rights consciousness

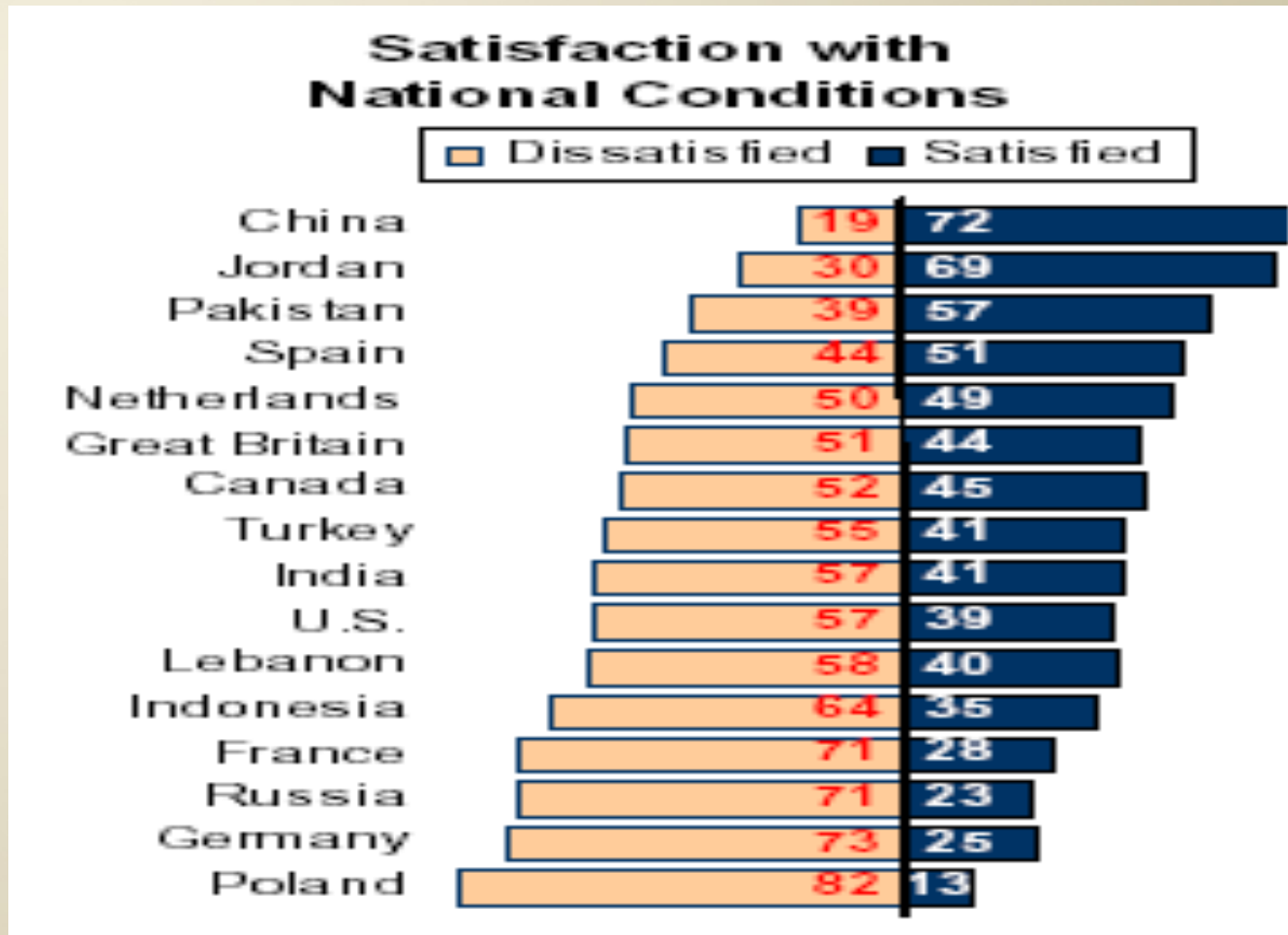
- **Succession competition**
 - **Insecure**
- Princelings ascendant
 - **Rising popular resentment**
- Popular resentment of princelings, elite arrogance
- Leadership without military background
- Popular confidence, resentment of stress
- Rising emphasis on control



Jasmine revolution? No (1)

- **Authoritarian regimes are not all alike**
 - **African tribal dictatorships, disintegrating empires, Iranian theocracy, Latin American caudillos, totalitarians**
 - **China is a mobilization system like old South Korea, old Taiwan, old Indonesia, old Japan**
- **China's government delivers the goods**
 - **Rapid growth has raised all groups' living standards at least 600%**
 - **Life expectancy has risen from 41 to 73 since 1955**
 - **Unlike India, the roads get built, the children educated**
 - **Political improvements have been gradual but far-reaching**
- **Academics, students generally see government positively**
 - **Almost unique in emerging markets**

Jasmine revolution? No (2)



➤ Source: 2005 Pew Global Attitudes Survey

Jasmine revolution? No (3)

Chinese More Satisfied With Their Country's Direction

% Satisfied

	2007	2008	2009	2010
	%	%	%	%
China	83	86	87	87
Egypt	47	40	31	28

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China's new economics II

1990s

- Weak banks
- Coast outperforming
- Labor abundant

- RMB over or fairly valued
- Incentivize FDI
 - Better than local

Today

- Strong banks
- Interior outperforming
- Labor shortage
 - Min wage to rise >13%
 - Actual rise now >20%
- RMB undervalued
- Selective about FDI
 - Squeeze technology

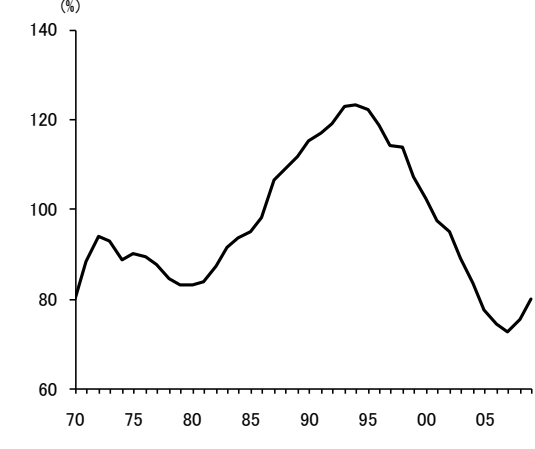
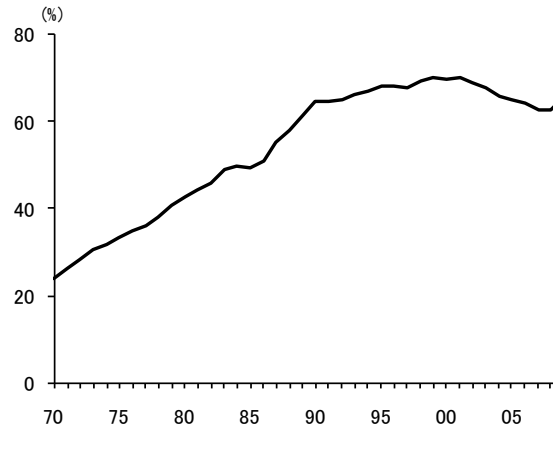
Bubble trouble? China leverage vs Japan bubble

➤ (i) Loans to nominal GDP ratio

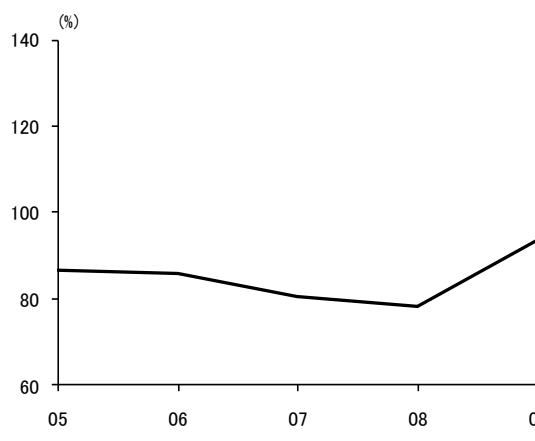
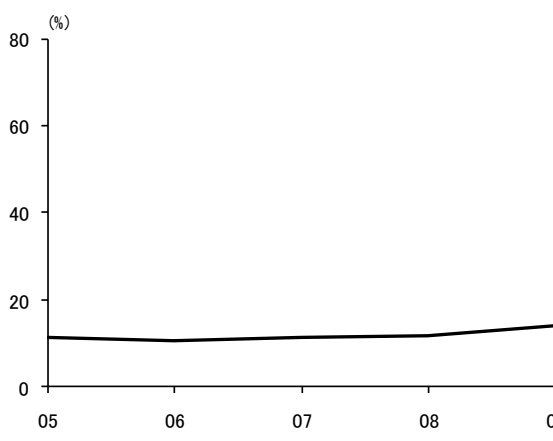
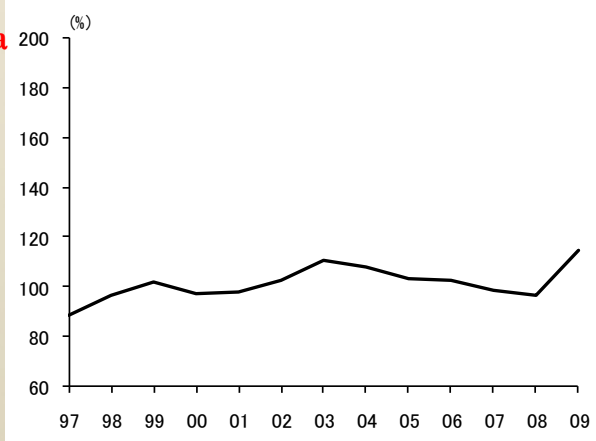
➤ (ii) Loans for households to nominal GDP ratio

➤ (iii) Loans for enterprises to nominal GDP ratio

➤ Japan



➤ China



➤ Source: CBRC, BOJ



Bubble conclusions

- China has significant financial problems
 - **property prices, inflation and emergent bank NPLs**
- Modest compared to the world's great bubble crises
- China has the tools to manage these problems and is using them proactively.
 - **Monetary squeeze will continue to affect stock market**
 - **But stock market is more attractively priced than any previous time**
- Government is exceptionally competent
- Intense political rivalries now impinge on management



China's domestic economic dilemma preceded crisis

- **A Jimmy Carter moment in early 2008**
 - High inflation, wave of bankruptcies
- **Real issue: an obsolete model**
 - Capital-intensive; declining TFP
 - State-intensive/SOE-intensive
 - Resource-intensive
 - Exploitative of labor & rural areas
- **Needed model**
 - Increasingly SME-based, private-oriented, services-intensive
 - Requires freer capital markets, tougher accounting, better deals for workers & rural people
- **Crisis is (temporarily?) driving China in the opposite direction**



Scenario I: Worst case: Japanese-style decay

- **Overconfidence leads to complacency**
- **Divisions & overconfidence stall market & political reforms**
- **Interest groups, localities, bureaucrats overwhelm national interest**
- **SOEs' dominance of funding constrains SMEs**
 - **Limits future jobs, innovation**
- **Protectionism: FDI, currency**
 - **Currency a subsidy to trialing edge industries**
- **International hubris**
- **Public opinion shifts against central leadership**
 - **Vicious circle of elitism, discontent & repression**



Worst case scenario: Japanese-style decay (2)

- Patchwork socialist solutions to:
 - Hot money
 - Bubbles, inflation
- This scenario sets in very gradually--decades
- But China is far more globalized & competitive than Japan



Scenario II: Best case: Visionary reform program: Wang Yaohui

- **Three phases of globalization**
 - **Industrial: Britain as leader**
 - **Financial: U.S. as leader**
 - **Talent: China as leader**
- **International education**
 - **University presidents 78%**
 - **Directors of key research labs: 72%**
 - **Academicians of Academy of Sciences: 81%**
 - **Returnee entrepreneurial parks: 150**
- **Vision will only work in context of vigorous political & market reform**



Scenario II: Best case: Reinvigorated reform

- **Reassertion of marketization**
- **Shift toward domestic demand (see new 5 year plan)**
 - **Higher salaries; assured pensions, medical insurance, education**
 - **Market-based currency to raise purchasing power**
 - **Market-based interest rates to raise household returns**
- **Successful funding of SMEs/exploding service sector**
 - **Market based stock listings, accounting crackdown to boost credit**
 - **Stimulate employment expansion, innovation**
- **Market treatment of SOEs**
 - **Taxation, dividend payouts, market interest rates**
 - **Bank, SOE leaderships no longer Party-appointed**



Reinvigorated reform (2)

- **Resumption of gradual political reform**
 - **Reassertion of central control vis a vis interest groups, provinces**
 - **Educated middle class demands accountability, freedom**
 - **Princelings need democratization, rule of law to defend their holdings**
 - **Elections at more levels**
 - **Improvement of human rights, legal system, information freedom**
- **Stronger international posture but moderate**
 - **Settlement of territorial waters, seabed disputes**
 - **Moderation on Taiwan, multilateralism on North Korea**



Reinvigorated reform: the crucial caveat

- **Fear-based support for highly stressful reform won't revive**



Drivers of Northeast Asia's future

- Japan has failed to make the transition from mobilization system to globalized democracy
 - Will decline until shock induces changed political structure
- South Korea has made the transition & is Asia's fastest rising star
- Taiwan made the transition but lost crucial time under Lee Teng-hui & Chen Shui-bian
 - Lost ground economically, geopolitically
 - Corruption revived after being suppressed by Chiang Ching-kuo
 - Will be pulled increasingly into China's orbit
- China is at a crucial transition
 - Man, chased by a tiger, took a nap, now has to decide how fast to run



U.S. policies

- Japan becomes very sensitive to “Japan passing”
 - **Very angry reaction against President Clinton’s visit to China**
- **Armitage Report 2000: Bipartisan call for return to Cold War relationships**
 - **U.S. should pay less attention to China**
 - **Japan should be the cornerstone of all U.S. policy in Asia**
 - **Japan should be pressured to take stronger defense role**
 - **Bush strongly implements the recommendations**

Replaces China experts with Japan experts in key policy roles



Results disappoint

- Under Bush, enormous frustration with Japan over
 - **Futenma—Pentagon disillusioned**
 - **North Korea nuclear program—State Dept disillusioned**
 - **Economic stagnation**
- Many influential analysts disturbed by:
 - **Encouragement of rewriting of history, alienation of neighbors**
 - **Seeming effort to maintain Japan's role by keeping China down**
 - e.g., emphasis on excluding China from regional security arrangements
 - **2005 “2+2 Agreement” bringing Taiwan under the alliance**
 - Fundamentally altered China's view of U.S. alliances & bases
 - **Four power naval exercises**



Key consequences

- Widespread feeling that Japan was not an effective partner
- Serious concern about the rise of the far right
 - Koizumi invited to visit Elvis Presley's memorial rather than to address the U.S. Congress
- Concern in some circles that the alliance was becoming an alliance of the right wings of the two countries rather than the peoples



China became U.S. partner on key issues

- North Korea
- War on terror
- Regional crime
- Regional drugs
- Freedom of trade
- Freedom of investment
- Above all, global financial crisis
- Solution of environment & climate change issues seemed to depend largely on whether U.S. & China could agree
- Easing of Taiwan-PRC tensions
 - **Reduction of U.S. defense budget targeted at China**



G2 concept discredited quickly (I)

- Above trends led to emergence of the (never widely accepted) G2 concept
- U.S. sense of betrayal over Copenhagen conference on climate change
- Slow Chinese acceptance of stronger sanctions on Iran
- Chinese toughening on FDI—destroyed the pro-China business lobby
- Chinese overreaction to Dalai Lama visit with Obama
- Chinese overreaction to Taiwan arms sales overshadowed cross-Straits rapprochement



G2 concept discredited quickly (II)

- Chinese error that financial crisis constituted a permanent, radical reduction of U.S. economic & power position
- Chinese failure to denounce Cheonan sinking, North Korean killing of civilians on YongPyeong
- Cyber “cool war”
- U.S. insensitivity on tires, currency when China lost 30 million jobs
- Anti-China instincts in U.S. Congress & media: Sudan, energy security
- India given a free ride on borders, nuclear, territorial waters
- Four power naval exercises
- Indian efforts to ally with Japan to dominate South China Sea



China's new geopolitics

1990s

- **Lack of confidence**
- **Low posture**
- **Weak in Taiwan Strait**
- **Rigid Taiwan policy**
- **Settle land borders**
- **More flexible on N Korea**
- **Leadership unchallenged on unity & security**
- **Imminent G-2**

Today

- **Hubris**
- **High posture; but low cost**
- **Strong in Taiwan Strait**
- **Flexible Taiwan policy**
- **Assert sea borders**
- **More rigid on N Korea**
- **Leadership vulnerable on unity & security**
- **Heightened U.S. tensions**



Reasons for new geopolitics

- Confidence from own success
- Some conviction that U.S. is in decline
 - Financial crisis
 - Hu/Obama meeting paralleled Khrushchev/Kennedy
- Rising interest group influence
 - Military, Commerce, Media
- Insufficient toughness a vulnerability in succession



Current situation

- U.S.-China relationship successful on most practical issues
- But mutual suspicion, economic stresses, security tensions are rising
- Every significant segment of U.S. opinion wants:
 - **Japanese economic success**
 - **An influential Japanese role in Asia**
 - **A strong U.S.-Japan alliance**
- Most influential Americans of both parties view Japan as largely weak and ineffectual
 - **U.S. leaders now always visit Japan before China, but the important dealings are with China**
- South Korea the new favorite ally

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