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IJAPS, Vol. 5, No. 1 (January 2009)

THE WITHERING STATE DEBATE: EVIDENCE FROM MALAYSIA'S AND VIETNAM'S GLOBALISING ECONOMIES

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ABSTRACTS

It has been frequently argued that under globalisation, the state's ability to make autonomous decisions declines and the state withers away as it adapts to the lowest common denominator of taxation and social services in order to attract global investment flows. This paper challenges the withering-state theory. States are not hapless victims of globalisation, but active facilitators. Through the case studies of Vietnam and Malaysia, it is demonstrated that the state makes decisions about globalisation—either to engage in it or to retreat from it—based on the state's perceived interest. Moreover, the state is perfectly capable of reversing these decisions as state interests change over time.

Keywords: globalisation, governance, race to the bottom, Malaysia, Vietnam

INTRODUCTION

Critics of globalisation have made a strong argument about the future of the state: in an era where every day billions of dollars worth of footloose capital without any national allegiance slosh around the world for the best return, the state withers away, losing its sovereignty to investors, credit rating agencies and international financiers. Corporations have all the power, and

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states—especially small and poor ones—must play by the investors' rules or see precious capital go elsewhere. A race to the bottom ensues, where taxes, regulations and social wages converge to the lowest common denominator. Only developed countries with large domestic economies can use market power to attract investors without reducing environmental regulations, labour standards, minimum wage and social charges. Smaller nations with less financial attraction for investors, such as Malaysia or Vietnam, find their ability to act in the best interest of their citizens reduced to a bare minimum.

This is a powerful claim, echoing the position of dependency theory of earlier days. Dependistas argued that engagement with the global economy holds only pain for the peripheral economies, since all power resides with global finance in the core countries. The intellectual heirs of dependency theory among globalisation critics now argue that power lies with the global elites—colluding beneficiaries of globally mobile money—while the masses are either duped into cooperation through hegemonic discourses, or forced into compliance by force. The state can no longer protect its citizens and either plays second fiddle to the captains of banking and industry, or actively participates in the exploitation of the masses.

There are undoubtedly a number of examples where the state is declining. This paper, however, taking its cues from what appear to be strong, yet successfully integrated states, challenges the withering state hypothesis. It takes a close look at two strong states that have integrated into the global economy, Malaysia and Vietnam. The cases are chosen on account of their claims of different experiences with globalisation. In Vietnam, clear majorities of both the leadership and the population at large are highly supportive of economic globalisation, that is, foreign investment and international trade integration. In Malaysia, Prime Minister Mahathir has changed his tune. Until the 1997 Asian financial crisis, he was an active globaliser, arguing that integration would bring Malaysians out of poverty and into the modern world. Since the collapse, he has emerged as one of the most vocal critics of the phenomenon of globalisation.

Both countries have, however, a clearly active state. The paper will show that in both cases, the state maintained agency throughout its engagement with the global economy. In the case of Vietnam, it has so far managed this engagement successfully. In the case of Malaysia, early success led to domestic policy mistakes and economic problems, yet the state remained in the driver's seat and in the aftermath of the crisis provided powerful evidence that where the state sees limits to global market forces in its interest, it remains free to impose them.

GLOBALISATION AND THE RACE TO THE BOTTOM

Developing countries have a high number of underemployed workers and little capital. The developed world has the capital, but faces cost structures that are unprofitable for labour-intensive manufacturing and assembly. Thus, money roams around the world in search of the best deal—low wages, weak regulatory regimes and pliant governments. With many countries in need of the money, the bargaining power rests with the capitalist, and countries either comply with the demands of investors or lose out to a competitor who will. Wages and regulation levels converge at the lowest possible denominator. This so-called convergence theory represents a structuralist view, one in which economic globalisation imposes its logic and states simply have no alternative.[1] One author sums it up when he says: "The humane and compassionate state is being phased out" (Falk 1997: 130). In this Darwinian race, the state either offers what global finance wants or bears the bitter consequences of poverty. Mittelman (2000: 5) summarizes this view well:

> [Economic globalisation] offers major benefits, including gains in productivity, technological advances, higher standards of living, more jobs, broader access to consumer products at lower cost, widespread dissemination of information and knowledge, reductions in poverty in some parts of the world, and a release from long-standing social hierarchies in many countries. Yet there is a price for integrating in this global framework and adopting its practices. Expressed or tacit acceptance of being encompassed in globalisation entails a lessening, or in some case a negating, of the quantum of political control exercised by the encompassed, especially in the least powerful and poorest zones of the global economy.

The cause for this seemingly Darwinian race is "hypercompetition" (Mittelman 2000: 4). Many scholars, activists and even political leaders, especially those critical of the phenomenon of globalisation, believe that the pressures from extremely mobile capital and the sheer size of capital flows that can be initiated by pressing a button on a computer in New York or London overwhelm the state's power to counteract theses forces. As a result, states will engage in "regulatory arbitrage," investing in or importing from the country with the lowest costs. Thus, developing countries dependent on investment and exports for hard currency are forced to align their tax

[1] This formulation borrows from the former British Prime Minister Margaret Thatcher, who referred to globalisation as TINA: "There Is No Alternative."

structure and regulations downwards to a lowest common denominator to avoid being left out (Drezner 2001: 57–8).

Mittelman, taking a Gramscian approach, asks who the hegemon[2] is in globalisation. Since no central authority can claim control over the global financial or trading system, the structure of globalisation should be non-hierarchical. If there are, however, hegemons who impose their order on the structure, as most globalisation scholars believe, then who are these champions of globalisation (Mittelman 2000: 920–21)? In the context of the 1997 Asian financial crisis, Malaysia's then-Prime Minister Mahathir Mohamad was in the forefront of criticising globalisation, accusing global financiers of willfully destroying Malaysia's economy. For him, as for many critics of globalisation, the hegemon is 'the West,' its investors and speculators, the International Monetary Fund (IMF) and the U.S. Treasury Department, even large investors who impose the rules of the game on small countries in need of capital and factories that hire the workers who want to escape the poverty of rural subsistence life (Mahathir 1999; Makaruddin 2002). The structure of globalisation, for Mahathir, is one of domination. History has come full circle, with globalisation bringing poor countries back to the era of colonialism, with the West dominating the rest, just under a different umbrella. Dominant states, in this view, remain active agents shaping the process of globalisation; only the weak ones are subjected to the convergence imposed on them by forces created by the hegemon.

But Mahathir's record on globalisation also allows for an alternative view of the state in globalisation, namely one of the state as active facilitator. In the case of Mahathir's Malaysia, globalisation allowed Malaysia to partake of the benefits of increasing wealth and new technologies. This was Mahathir's position prior to the financial crisis, when he actively pushed Malaysia—and particularly ethnic Malays—to leave the countryside and join a modern economy. To bring about these changes, Malaysia's government actively vied for foreign investment, promoted manufacturing for export and worked hard to allow its industries to climb up the value chain. Only after the 1997 crisis shook Mahathir's government did the emphasis turn toward the alleged price of this modernising policy—renewed submission to the world's dominant powers. Which Mahathir is right? The one who claims that far-away high finance can destroy an economy with sound fundamentals at the click of a button on a computer

[2] While the term hegemony generally describes a situation of dominance or superiority, Antonio Gramsci defines it as the power to dominate others while leading the oppressed to believe that their submission is in their own best interest. The oppressed thus participate in their oppression.

keyboard by withdrawing billions of dollars and sending them somewhere else across the globe where the government has consented to cutting taxes and regulations even further? Or the one who argues that states have the ability to shape globalisation to their benefit, imposing rules on the global economy and implementing capital controls, as Mahathir himself has done in 1998? While Mahathir's writings are full of contradictions and attempts at minimising the role of his government in bringing about the conditions for the 1997 economic crisis, scholars have made coherent arguments about whether globalisation rings in the end of the state.

The argument here put forth is that the state has not been changed as much as globalisation critics perceive. The state is still dominated by elite groups that shape policy in their interest. As a result, globalisation is harnessed by these elites for their benefit. To evaluate the impact of globalisation on the state, one must look at elite interest, not an abstract structure that pushes countries around like billiard balls, leaving them without agency of their own. A state's response to the demands of global finance depends on the interests of the state's elites, not an inevitable logic of the structure of globalisation. If globalisation is inevitable, it is because elites the world over share similar interests, and push in the same directions. The two examples in this paper, Malaysia and Vietnam, two developing nations that have done comparatively well under conditions of trade opening and global integration, have retained a significant degree of policy autonomy to act in the interest of the dominant elite actors. If they have accepted a reduction in their autonomy at times, it is because the elites found it in their interest to do so.

THE CONCEPT OF THE STATE

Before we can discuss the impact of globalisation on the state, we must define these amorphous concepts. Globalisation has been defined in a variety of ways, including a shrinking of the time-space continuum, and through various cultural aspects, but for the purpose of this discussion, we shall only look at its economic expressions. Globalisation in our context is synonymous with trade opening, free markets and competition for international investment flows. Both Malaysia and Vietnam have opened their domestic markets to foreign investors, have focused on export production and made concessions to foreign producers and adopted international trade and investment regimes in return. Nothing about this process challenges national sovereignty. Nothing can prevent governments from setting their own standards, rules and regulations. Even in economic

relations with investors and international markets, the domestic government remains the primary contracting party, rather than a United Nations (UN) agency, the World Bank, a transnational corporation or a non-profit organisation (Spruyt 2002: 145). This paper concerns itself with the question whether, to what degree and why the state may have lost autonomy in the domestic sphere.

Defining the state is more complicated. First, for this discussion, we do not see 'the state' as a physical entity, such as a territory within recognised boundaries, nor is it synonymous with 'the government' or 'national institutions.' These are manifestations of what we consider 'the state.' Instead, we define 'the state' as the outcome of the continuous process of capturing and recapturing the benefits of control over these manifestations by various interest groups. This is the liberal view of the state, and one that suits us well for a discussion on how the state changes under conditions of globalisation. Vietnam and Malaysia are excellent case studies because the dominant interest groups in each—the United Malays National Organisation (UMNO) in the case of Malaysia and the Communist Party in Vietnam—have been exceptionally stable over time. It is thus easier to see what impact an exogenous force like globalisation has had, than it would be in countries where domestic contestation among interest groups has been more vigorous and led to frequent realignments or constant struggle.

The state, under the above definition, acts on society by imposing norms that are beneficial to the dominant interest group or groups. These norms change in detail depending on which groups are in control, but in principle they remain fairly stable: the state lays out and enforces the rules of the game with emphasis on continuity, stability and predictability to avoid rapid social changes. To do so, the state needs to be the monopolist over the means of violence, for a system with one single entity providing enforcement is more efficient than competing enforcers (Tilly 1985). This view represents, of course, an extension of Max Weber's state as being a claimant of a monopoly over the legitimate use of violence. But, as Mygdal adds, a monopoly over the use of violence is not enough, since few states enforce their rule by violence alone. States and their citizens are in a constant, mutually transformative relationship (Mygdal 1997). The dominant elites aim at legitimacy, since enforcement though acceptance is easier than through force alone.

In this sense, states that are part of the globalising economy behave exactly like states before the liberalisation of trade flows and global investment regimes. The only difference under globalisation is how states go about obtaining their objective—maintaining their subjects' obedience

(Mygdal 1997: 223). In other words, what has changed in the global economy is the rationale for a state's legitimacy; what allows the state, the dominant groups that have captured it, to demand obedience from the rest of society? While legitimacy of rule used to be based on tradition (inheritance, divine right) and success in war (Spruyt 2002: 144) or consent of the governed (democracy), many states today tout their role in providing strong economic growth, high levels of employment and rising living standards when claiming their (continued) right to rule.[3] The Chinese concept of the *Mandate from Heaven* reflects this historical claim to legitimacy. As long as no invaders breach the defenses and no natural catastrophes befall society, the ruler retains legitimacy. But a serious reversal of fortunes would indicate that the ruler has lost the support of the heavens and revolt becomes legitimate. This is an example of state legitimacy based on successful governance in the common interest. Such a concept of legitimacy by success indeed limits the autonomy of the state. Rulers must accept the discipline of the market if their claim to continued rule depends on the economy's performance within the global market. Depending on one's views of the state, benign or predatory, such a limitation will either render politicians incapable of protecting their subjects from the vagaries of capitalism, or render them incapable of fleecing their subjects at their will. But in either view, the state is curtailed by the forces of the market (Wolf 2001: 178).

WITHER THE GLOBALIZING STATE?

Limited autonomy of states is nothing new in the neo-realist literature that has dominated international relations theory for decades. Neo-realism has traditionally assumed that states behave as "like units," acting as the international, anarchic structure requires, in order to assure their survival (Waltz 1979: 74–77). This does not necessarily mean they have no agency at all, but that they are limited in their actions by external pressures exercised on them. In spite of this stripped-down version of state agency, the global system in neo-realism remained state-centric. Reduced domestic autonomy for the state has not led to realist claims that the state withers in the international arena. Iraq, North Korea, Iran and Cuba have intentionally shut out most of the effects of globalisation, yet they remain crucial actors in international politics. Similarly, states do not lose their power of agency

[3] This is true both for democracies, where economic performance is routinely a key electoral argument, and for authoritarian regimes that argue that economic stability and progress grant the ruling elite the right to continue their domination over society for the public good.

in the global economy. Vietnam and Malaysia, the two states discussed in greater detail below, have joined globalisation, but at their own pace. Malaysia has gone a step further and actively retreated from globalisation during the Asian financial crisis as the state saw fit. The world's largest corporations continue to apply to the state for licenses.[4] Tax rates are still set by states, not lenders or investors,[5] and they differ from state to state. Fiscal policy is driven by the state, and most states regulate banks, currency markets and other crucial financial institutions, rather than abdicating them to the vagaries of the market. The sovereignty of the state thus remains intact. At question is domestic state autonomy. To what degree are states hamstrung by the forces of globalisation once they have made the choice that they want to participate in international trade and investment regimes? As already indicated, the initial choice of acceptance or refusal to be inside the structure of globalisation is undoubtedly still the state's to make, and continues to be, unless and until the international system of anarchy is undone. The issue is to what degree the decision to join the global economy, once it is made, restricts the state in its ability to shape what can be called the "terms of engagement" with globalisation (Othman & Kessler 2000: 1015).

The question, thus, is not whether the state is in retreat, but to what degree it finds itself in a straightjacket once it has taken the decision to participate in the global economy (Weiss 2005: 345–46). But why would states make choices that limit their domestic policy autonomy? Policy choices are made for rationally functional reasons, and no agents would make a decision to join the global economy just to see their fortunes wane. If states forfeit autonomy in the process, they must expect benefits that outweigh the limitations. Hence, the structure that limits state action is not mainly the international one called globalisation, but largely that of domestic institutional arrangements and competition among elite groups. The evidence for this assertion lies in the empirical observation that although there is too much commonality in state action for it to be random, there is also too much divergence to support the claim that globalisation is an outside force that overpowers the state and turns it into a mere puppet manipulated by the forces of globalisation. In short, as the cases of Malaysia and Vietnam will show, globalisation delineates limits to state behaviour for

[4] In the autumn of 2008, the Vietnamese government rejected a multi-billion dollar investment project by Korean steel maker POSCO over environmental concerns. While the government may have feared protests by people working in the region's tourism industry, it is clear that the state retained significant autonomy over the regulation of international capital.

[5] Vietnam is consistently rejecting a reduction in corporate taxes, in spite of less than subtle suggestions made by international chambers of commerce and investors.

states that chose to join it, yet significant residual agency remains within those limits. Most of all, elite interest trumps the demands of the global economy. The state's dominant elites determine whether they see it in their interest to accept the limits set by globalisation or to reject them in part or entirely. The differing institutional arrangements and incentive structures in different countries explain the differences in response to globalisation across countries and at various times.

Moreover, the evidence that proponents of the withering state theory propose is coming under increasingly critical scrutiny. Approximately 90% of Foreign Direct Investment (FDI) flows into developed countries, where labour standards, tax rates and social wages are high, not into nations converging toward the lowest common denominator (Drezner 2001: 67). Localities can still tax and regulate if they have specific advantages that are not easily moved, such as natural resources, human capital, large markets and the like. It is harder under conditions of globalisation, however, for jurisdictions to demand high taxes without providing something in return. Scandinavia shows that high taxes do not necessarily lead to mass emigration, as long as the services provided in return are excellent (Wolf 2001: 186–8). Falk's assertion (Falk 1997: 130; above) that globalisation is phasing out the Scandinavian model does not bear out.

Even within the developing world, convergence is not observable. Drezner points out that if trade opening and competition for FDI were to lead to lower labour standards, then these standards should be especially lax in Export Processing Zones (EPZs), which are specifically set up to attract foreign corporations. But he finds that wages tend to be higher in such zones, and that strong labour union activity in EPZs leads to no reduction of investment by international corporations (Drezner 2001: 68). In Vietnam, female migrants are more likely to receive health insurance from their employers than their male counterparts, because female migrant workers are most likely to work for foreign-owned companies in EPZs, which in turn are significantly more likely to provide health insurance than domestic enterprises (General Statistics Office of Vietnam 2006). Corporations do not simply take "random walks" whenever a slightly better deal opens up elsewhere. Much of European capital outflows today are portfolio investments, not shifting production facilities to places where regulations, taxes and wages are lowest (Weiss 1997: 8–10). Some states have even actively tried to push industries out to assure that they make use of cheaper labour rates elsewhere before losing international competitiveness. Japan tried to push companies to go offshore to stay cost competitive and to reduce its politically damaging trade surplus. Singapore financed industrial parks in developing countries, just to make Singaporean companies take the

plunge and go offshore. Korea and Taiwan are also helping their firms to establish overseas production facilities. The assumption that companies will always seek out the cheapest places is overly simplistic (Weiss 1997: 22–23).

Not even the presumably footloose capital sloshing around the world is observable. It has been pointed out that the level of trade and investment today is comparable to earlier periods in the late nineteenth and early twentieth century (for example Wolf 2001: 179–80). Economic integration creates pressures, but they are moderated, adjusted or heightened by domestic institutional factors. Conformity can be enhanced by globalisation, yet states still act based on domestic interest, that is, the interest of the dominant elite of the moment (Weiss 2005: 345–6). If states accept a straightjacket, it is because their elites determine that the benefits from that straightjacket exceed the costs. The following discussion of East Asia and the particular cases of Vietnam and Malaysia will support this claim, and show that as states feel that the straightjacket is becoming too costly, they are perfectly able to shed it.

A LOOK AT EAST ASIA

East Asia has a long history with state involvement in economic development, and particularly with the state's shaping of the terms of engagement with the global economy. At the beginning of the 'East Asian miracle' is what is commonly known as the developmental state. This was a strong state with a wide degree of autonomy, but also one that actively sought export markets, which implies accepting the discipline of the international economy (White & Wade 1988; Johnson 1995; Yoo 2006). The three most successful developmental states, Japan, Taiwan and South Korea, intervened not only in the allocation of resources in the domestic economy, but also forced their industries to produce for exports (World Bank 1993: 261, 358–60). By imposing the discipline of international markets on their key sectors, they prevented industries from using their growing clout for domestic political protection. The state intentionally gave up influence in return for better economic performance.

Table 1
Level of Globalisation – 2006 Ratings (Selection).

2006 rank (Selection)	Economic dimension 2006	Trade 2006	FDI 2006
1 Singapore	1	1	1
2 Switzerland	9	17	7
3 United States	58	62	36
4 Ireland	4	4	5
5 Denmark	8	20	6
6 Canada	23	30	12
7 Netherlands	21	11	52
8 Australia	18	55	3
9 Austria	15	15	18
10 Sweden ...	19	21	16
19 Malaysia …	3	2	11
29 South Korea …	32	26	41
35 Taiwan …	12	9	32
51 China …	28	27	21
53 Kenya	55	42	60
54 Colombia	51	54	33
55 Egypt	42	35	42
56 Pakistan	60	59	53
57 Turkey	47	38	47
58 Bangladesh	61	57	58
59 Venezuela	48	44	44
60 Indonesia	52	36	61
61 India	59	58	49
62 Iran	67	46	62

Source: Kearney (2006)
Notes: Numbers next to country name represent ranking among 62 states studied. Total ranking is calculated from four dimensions: economic, personal, technological and political. To evaluate convergence theory, the economic dimension is most relevant and listed here. The economic dimension is composed of the importance of trade and FDI in the overall economy.

The table lists the top and bottom ranking ten countries in terms of global integration, and adds countries of particular interest to this discussion, Malaysia, South Korea, Taiwan and China. Kearny did not rank Vietnam.

Full report: http://www.atkearney.com/shared_res/pdf/Globalisation-Index_FP_Nov-Dec-06_S.pdf

Importantly, it was the state that chose the form of the country's international economic engagement to make use of global market forces for domestic goals—both by using integration and by limiting it at certain points. In a similar way, Vietnam and Malaysia, in their own contexts, shaped the terms of engagement with the global economy. These more recent examples fall more directly into the time period that is generally considered the era of globalisation. The main difference between the export-based disciplining of the domestic economy and the recent Southeast Asian (and also Chinese) success stories lies in the latter's increased emphasis on foreign direct investment. While emphasis on exports imposes a degree of discipline on industries, export promotion does not require the same

domestic limitations on state predation as does a focus on attracting FDI. Importing goods does not require long-term trust in the performance of the exporter's economy. If a product's quality or cost changes or government regulations make dealing with exporting companies difficult, contracts can be cancelled and other suppliers found without great difficulty. Investors, by contrast, need to be reasonably certain that the business conditions in the host countries will remain conducive throughout the length of time it takes to recoup the sunken costs.[6] These business conditions include low taxes, low levels of red tape, an investor-friendly regulatory environment, and cheap and docile labour, the key ingredients of the convergence argument. But even the investment-dependent countries defy convergence theory. As Table 1 shows, the most economically open nations are not the ones with the weakest state. Singapore ranks as the most globalised nation overall. It also tops all other 61 countries in a study in terms of trade openness and FDI (Kearney 2006: 77). Yet Singapore is a strong state that intervenes in many of the areas where convergence theorists would expect a withering of the state: social policy, a safety net for the poor and regulation of the economy. The second-highest ranked Asian country is Malaysia on nineteenth place in overall globalisation level, but second in trade openness and eleventh in FDI. All the top-ranked countries other than Singapore are developed Western nations, all have strong welfare states. While some rank high on the economic dimension of globalisation, others do not. The United States (US), for example, owes its high globalisation ranking to the other dimensions, while ranking fairly low on the economic side. No connection between trade openness, impact of FDI on the overall economy and economic integration on one hand and role of the state in society on the other hand is visible. Instead, interest groups harness the forces of international trade and investment for their purpose. This was visible in the developmental state and remains so today.[7] The following two case studies underline this point.

[6] Hence the relationship between stability and cost structure. In a stable country, costs can be higher if returns are good, since the risks are low. The higher the risk of a reversal of conditions, the faster the investor wants the investment back, and the higher the risk premium.

[7] As a recent example, in the 2008 US presidential campaign, Senator John McCain emphasized the importance of free trade, while Senator Barack Obama spoke about fair trade and the possibility of reversing unpopular trade agreements. Both candidates spoke to their political base in order to gain votes. Not the global economy, but electoral considerations dominated the issue of trade.

Vietnam—Bottom-Up and Top-Down Globalisation

In January of 2007, Vietnam was admitted into the World Trade Organisation (WTO). This achievement marked the culmination of Vietnam's decade-long reversal of a previously centrally planned, autarkic economy. But unlike Eastern Europe, the economic change was not precipitated by a change in political leadership. The same single party government that dominated Vietnam in the years of protectionism and a state-led, domestic-oriented economy now commits the country to trade openness and membership in as many free trade agreements as possible. Since the economic reforms initiated in 1986, called *doi moi* (renovation), Vietnam has joined the Association of Southeast Asian Nations (ASEAN) and the ASEAN Free Trade Area, concluded a host of bilateral trade agreements, including one with the erstwhile enemy, the US, and then pushed its way into WTO with an unshakable sense of purpose.

Clearly, the communist government of Vietnam did not 'globalise' for ideological reasons. Most of the current leadership came of age during the war against capitalist imperialism. They joined the rest of the world not because they were ideologically so predisposed or because they bought into the dominant Western discourse, but because they realised that due to a groundswell of popular demand, the elite's very own success was advanced by it. While globalisation opponents argue that the hegemon of globalisation can be found in the developed world (see Mittelman & Mahathir above), in Vietnam, this hegemony is internal. The majority in the Communist Party decided on reform because it remembers the traditions of old: the state's legitimacy derives from the performance of the tasks expected from it. This *Mandate from Heaven* once implied defending the people from their external enemies and from the wrath of nature, like drought and flood. Today, the first indicator of state performance is the provision of a steady increase in material well-being, except in situations of severe crisis, such as war or cataclysmic catastrophes, when the priorities shift to survival. Singapore's Lee Kuan Yew has claimed repeatedly that democracy is not an Asian concept; instead, government is legitimised by its performance (Rohwer 1995). So the Vietnamese elites espouse the discourse of the market and provide economic growth.

Yet this is not the convergence theory that eats away at the power of the state to regulate and protect. The government has made it very clear that its *doi moi* policy is "growth with equity," not a race to the bottom. A race to the bottom would not advance the claims of the elite to the right of continued rule. The government has maintained a strong hand in the economy to assure a socially equitable distribution of the gains. The poverty

rate has indeed declined from 58% in the early 1990s to just under 20% today (Vietnam News Agency 2007). Clearly, both autarky and trade integration were decided by the state for the perceived interest of the elite groups that dominate the state. First, the Vietnamese elites decided on the centrally planned economy that failed. When they saw it in their interest to reform, they decided on the reversal of policy as well as on the course of reforms. Hence, if globalisation is inevitable, it is not because of the dominant discourse of corporations or what is generically called 'the West,' but because of the groundswell of demands from large numbers of regular people. The elites saw it in their interest to join the global economy, in order to maintain their power and to benefit economically. They could only do so by satisfying a bottom-up demand for economic improvement. A large number of Vietnam's new jobs are created in the export sector. Then-Deputy Prime Minister (and former Trade Minister) Vu Khoan recognised the importance of FDI and export processing for social stability when he wrote:

> FDI accounts for 14–15% of GDP and approximately 30% of industrial output and export volume. As a result, economic integration in general and WTO accession in particular has become an inherent demand of the Vietnamese economy (Vu Khoan 2005).

Yet where the openness leads to social problems that undercut the stated goals of the government, elites determine whether the state should step in or let the market forces run their course. An example for Vietnam's ability to control the forces of globalisation when the state sees it in its interest is in labour rights. Vietnam has a higher minimum wage rate for foreign than for domestic companies. In 2006 and 2007, an increasing number of wild-cat strikes hit industrial zones around Ho Chi Minh City. Strikes are illegal in Vietnam. The strikes hit primarily Taiwanese and South Korean firms, said to offer comparatively bad working conditions among foreign-owned factories. The government not only did not crush the strikes, but increased the minimum wage by 40%, very much to the anger of the companies involved (Economist 2006; Vietnam News Agency 2006; China Post 2007). In 2007, foreign-owned firms paid a minimum wage of about $50 a month, a rate which has increased further in 2008. Foreign investors, especially in the low-end manufacturing sectors, have already begun to complain, arguing that they had come to Vietnam because of low wages and the virtual absence of labour action. Investors were quoted in international business magazines, putting the government on warning. The Economist, for example, quoted a an official from Taiwan's representative office (the unofficial embassy) as saying that while "Chinese wages are

higher [...] the quality and efficiency are also higher." He then urged the Vietnamese government to keep Vietnam investor-friendly (Economist 2006). The government, however, remained unimpressed and implemented the wage increases. More strikes occurred when companies were slow to apply the new rates. Again, the government did not act according to the race-to-the-bottom predictions, but supported the workers over the foreign investors. Foreign investment is not seen as a good in itself, but as a means to an end—socio-economic improvement.

Vietnam reflects well what Weiss calls the dualism between the logic of capital versus the logic of voice (Weiss 2005: 347). The logic of capital assumes that capital leaves if conditions are not favourable. The logic of voice assumes that a widespread demand in society has an impact on elites and will supersede the logic of capital and impose limits on it. While the Vietnamese elites have always acted in their perceived best interest—by eschewing globalisation first, and by espousing it later—the logic of voice has played a major role in providing incentives for and limiting the possible range of policies. Their collective voice, in the end, is what allows regular people to enter into the elites' calculation of the elite self-interest.

Malaysia—State-Managed Globalisation

Malaysia's form of government is one of consociational democracy. Democracy, however, is an amorphous concept. It is not just a question whether there are regular, free elections. More to the point is the question to what degree a regime is obligated for its own survival to respond to its citizens' demands (Dahl 1971: 1–2). Democracies respond to pressures from below, for governments depend for their survival on the continuous support from the populace. Malaysia is one of the many regime types that are categorised in the 'ambiguous' or 'mixed' type. Its institutional framework is essentially democratic, with regular, free elections, a parliament and an independent judiciary. But there is a wide range of authoritarian controls that limit the possibilities of the opposition. In short, the ruling coalition is extremely unlikely to be defeated at the polls (Crouch 1996: 4–6), reducing the political voice of those outside UMNO's coalition of supporters. The consociational nature of the system adds to UMNO's strength. Elites are not limited by public opinion overall, but mostly by the win-coalition whose support UMNO needs to assure in order to maintain its dominant position within the multi-ethnic country.

Merdeka—independence in 1957—is based on a bargain in which the Malay majority of just over 50% of the population assumed political control in return for granting the Chinese minority (approximately 25%)[8] citizenship rights. As UMNO lost its two-thirds majority in 1969, unrest broke out and the government decided to calm the population by initiating the New Economic Policy (NEP). The goal of the NEP was to alter the economic conditions for the Malay majority and to bring the mostly rural Malays into the country's economic mainstream (Chin 2000: 1041–45). The affirmative action policies initiated to that end, however, created a rentier class that made fortunes through government-provided monopolies and legal preferences. These benefits turned rentiers into a Malay upper class of the well connected, known as UMNO *cronies*.

Malaysia's various responses to globalisation are closely associated with the interests of this elite group. To distribute wealth from Chinese to Malays, it was necessary to access foreign capital for Malaysia's economic modernisation. Had the available Chinese capital been mobilised, the Chinese could have maintained their dominant role even in the new Malay-led country. Thus, the Malay elites found it in their interest to open the financial markets to foreign portfolio investment (indirect investment, rather than direct investment in tangible factories). It needs to be stressed that this rapid opening of financial markets with few institutional controls was not caused by the power of the U.S. Treasury Department, the IMF or transnational corporations, but by considerations over political power within the Malay political elite.

Regardless of the reasons for the opening, this rapid and uncontrolled opening caused price bubbles and speculation together with capital misallocation (Jomo 2004: 32). The financial crisis of 1997 in Malaysia, which Prime Minister Mahathir blamed flatly on the forces of globalisation (Makaruddin 2002), is largely a consequence of this rapid and uncontrolled opening of financial markets. Where bubbles are allowed to emerge, they will eventually burst. Yet the hegemon in Malaysia's decision to join globalisation and on what terms was domestic. It was a coalition of political and economic domestic interests groups, the cronies whose fortunes were made through their collusion with the government under the NEP.

After the Asian financial crisis struck Malaysia in the summer of 1997, UMNO's grip on power depended on its ability to continue to distribute resources to its cronies in particular and the Malay ethnic group in

[8] According to the U.S. State Department's Country Profile dated September 2007. The other ethnic groups are Indigenous 11% and Indian 7%, non-citizens 6% and others 1%. http://www.state.gov/r/pa/ei/bgn/2777.htm (accessed October 3, 2007).

general. Massive capital outflows threatened this redistributive capacity of the state. In this climate, an open row broke out between Prime Minister Mahathir and Deputy Prime Minister and Finance Minister Anwar Ibrahim, his political rival within the Malay political arena. Both had supported fiscal discipline and pro-market policies in the aftermath of the crisis. But in April of 1998, Anwar challenged Mahathir's leadership in UMNO when his supporters denounced cronyism at the UMNO national assembly. On May 21, 1998, Indonesia's President Suharto was toppled after he had lost his ability to continue to provide sufficient financial gains to his win-coalition. The message was not lost on Mahathir. In July of 1998, a full year after the crisis broke out and Malaysia's economy was already recovering, he implemented an economic stimulus package, the first deviation from IMF prescriptions and also from Anwar's policies. And in September, Anwar was arrested and charged with sodomy. The very day of his arrest, Malaysia introduced capital controls, the antithesis to the preferences of the free-market. Anwar had been highly respected in financial institutions around the world for his calm and pro-market approach in the aftermath of the crisis, the counterforce to Mahathir's fiery condemnations of the West, the IMF, currency speculators and the global Jewish conspiracy. With Anwar gone, Malaysia risked a renewed outflow of international capital, due to the fears that the calming force in the government had been eliminated. Thus, the controls were designed not to counteract the financial crisis, which had largely blown over by the fall of 1998, but to avoid a second meltdown in the wake of the finance minister's arrest. The state had shown that where its interest lies in opposition to globalisation's, the state has all the autonomy it needs to act. Mahathir used the rhetoric of neo-colonialism from abroad and traitors from within to gain support for his capital controls while at the same time ridding himself of a political challenger (Chin 2000: 1054).

Domestic interests trumped the demands of the global economy. Malaysia's path through the crisis was determined, as Tourres points out, by Mahathir's personality more than anything else. He was determined to avoid relinquishing control, sovereignty and independence (Tourres 2003: 71). Hence he followed IMF advice for over a year, but without accepting IMF money, which would have been tied to binding conditionality.[9] In 1998, he learned the lessons from Indonesia, where the fall of the rupiah and the evaporating treasury reserves no longer allowed President Suharto to maintain his system of political cronyism, which led to the Indonesian

[9] Malaysia was in a position of rejecting IMF loans because its debt was largely domestic, unlike in the other crisis countries. Moreover, the influx of hard currency from natural gas and palm oil helped the government maintain liquidity.

regime's downfall. Mahathir rapidly determined that he needed to be in tight control of his economy and money, to assure that the groups crucial to his government's survival continue to see their advantage in political continuity. The hegemon, in the case of Malaysia, was in fact a very narrow interest group of the leaders of UMNO supporting Prime Minister Mahathir Mohamad.

Similarly in 2007, Malaysia failed to come to an agreement with the United States on a bilateral trade agreement, presumably because provisions in the agreement would have required open and equal bidding procedures for all government contracts, thus challenging the institutionalised preferences for Malays over other ethnic groups. Key industries in Malaysia supported the agreement, yet again, regime interests prevailed over the logic of globalisation.

THE STATE AS ACTIVE GLOBALISER

The evidence in this paper indicates that in contrast to the withering state theory, the state is an active participant in globalisation. Consistent with this view, Weiss argues that beginning with the developmental states, the state has actively assisted its industries to integrate into the global economy. The state provides incentives for investment, promotes technology alliances and encourages regional relocation of production networks. State capacity thus becomes a condition for successful internationalisation (Weiss 1997: 20–21). This is why industrialised economies attract the lion's share of FDI, in spite of their high labour costs and significant regulatory burden; this is also why the most globalised countries do not exhibit a race to the bottom, as the Kearney report (Table 1) clearly indicates.

The two case studies support this assumption. In Vietnam, the state plays a significant role in human capital creation and infrastructure provision, in support of promoting inward investment. This is often done by provincial cadres who see their own fortunes improve as international investment flows into their provinces, employs their residents, pays taxes to allow them to pay better social wages (keeping their residents willing to accept single-party rule) and ultimately allows for a limited, albeit still lucrative amount of rent seeking. In Malaysia, it was the state that, based on elite group demands, opened its financial markets to portfolio money inflows. It was also the state that reacted to the financial crisis of 1997 by first following market orthodoxy, then rejecting it for domestic power considerations. In both cases, domestic elites were the ultimate beneficiaries of pro-market as well as anti-market decisions. The state should therefore be

seen as a facilitator or perpetrator of globalisation rather than a victim (Weiss 1997: 20).

None of this means that globalisation has no limiting effect on states. Like every choice, the decision to join the global economy opens some doors, and closes others. Few small countries can gain access to the latest technologies and cheap consumer products unless they accept to participate in the global economy. Small markets do not allow for the local production of capital-intensive goods. Producing automobiles for a market of the size of Malaysia (25 million inhabitants) is not profitable, as the case of Malaysia's Proton vehicle painfully demonstrates. The attraction of globalisation lies in the access to products and financial tools that would be unavailable to an isolated, small national economy. States join in because their domestic elites see the benefits of foreign investment and export markets in pursuing their goals. At least in the East Asian context, it would appear that these benefits have trickled down to the population at large, as poverty rates have fallen and social wages increased in the successfully globalising countries in the region, from developmental states to today's export-led growth success stories. The industrialised countries have equally continued to grow their economies, in spite of domestic protests against job transfers to the developing world.

On the other hand, if globalisation is driven, as here argued, by the state's elites, it remains entirely possible that it does not benefit the regular people. A predatory state remains a possibility, but would not appear to be a consequence of globalisation, but of domestic institutional arrangements. After all, states have been predatory long before globalisation. But if we recall Wolf's assertion that under conditions of globalisation the state is either impotent to protect its citizens from the vagaries of global capitalism or is rendered too weak to fleece its own population (Wolf 2001: 178), the picture becomes more hopeful. If the state remains strong enough to maintain its autonomy, as Vietnam, Malaysia and the entire developed world demonstrate, then the problem of an inability to protect citizens is not of concern—the question turns to one of the state's willingness to use its autonomy to serve and protect its subordinate groups. At worst, the state can continue to fleece its own people, as it always could in the past. At best, it is limited in that power of predation by the demands of the global economy. As long as it is in the interest of the elites to reduce the level of their short-term predation in order to attract investors for long-term benefits, average citizens may indeed benefit from the demands of investors: that states create

rules of the game that maintain social peace and economic stability, and enforce these rules predictably.[10]

As Malaysia has shown, when the state feels it is in its interest to limit the power of the global market, it still can. Vietnam has done the same in some sectors it considers strategic and vital. Western countries engage in selective reversals of their free trade policies when it suits their elites.[11] Globalisation may be irresistible, but the forms of engagement are negotiable. States are still in the position to devise policies for framing these terms. If human priorities are asserted by societies from the outset, if they capture globalisation rather than being captured by it, there may be genuine benefits from globalisation (Othman & Kessler 2000: 1014–15). This is arguably what Vietnam did. After the catastrophic experiment with centrally planned autarky, the state set the goal of socio-economic development and then joined the global economy to achieve it.

The crucial issue is whether the state really has an interest in equitable development, and whether its subjects have enough 'voice' to push the state to engage with globalisation on terms that benefit society overall. A rent-seeking, authoritarian government could still capture globalisation in a way that is not in the interest of the majority. The proposition that the engagement with globalisation can be captured by interest groups asserts the primacy of the political over the universalising processes of globalisation. This assumption prevails in this analysis. But it must be pointed out that domestic institutions are historically determined. A key determinant for the success of the developmental state was that the state used its power not primarily to engage in predation, but to develop and grow the economy. The elites made the choice to aim for long-term power through the legitimacy that comes with improvements of living conditions for all. In other countries, elites have made a different bargain. Numerous dictators who have moved vast amounts of money to Swiss bank accounts used brute force to hold on to power as long as they could and then fled to a life in exile–and luxury. Why many Asians have made one choice and many African, Central American and Caribbean rulers the other must be the subject of another analysis. Suffice it to say that initial conditions likely have a role to play. Where a country is made up of competing and hostile groups, the state, if composed primarily of members of one group, will have few scruples to grab what it can. In homogeneous countries, the impulse to steal and run is

[10] For a discussion on how FDI limits elites' predatory powers and devolves power downwards from central to provincial elites and further from provincial elites to ordinary citizens in the case of Vietnam, see Jandl.

[11] US tariffs on steel and catfish or European limits on shoe imports are among the recent examples.

socially less acceptable, even within the elite group. Low initial income inequality may play a role as well. When the poor and the rich live next to each other, the incentive to push for redistributive policies is great. Where most are equally poor, redistribution is a less attractive option than growing the pie for all. Due to the devastating impact of World War II on elites in Japan and Korea and the communist revolution's equalizing effects on Vietnam and China, these countries had more incentive to engage in pro-growth policies than in large-scale redistribution (Easterly 2002: 265).

Malaysia's consociational system posed a different set of challenges, and clearly not all groups have benefited from the economic growth of the country equally. Redistribution has taken place under the NEP. But the initial bargain under *Merdeka*, independence, that allowed the Chinese to retain significant economic powers in return for granting the Malays political supremacy may have been crucial to keeping both parties on board on the key principles of national unity and ethnic peace. Both sides may have felt that their success depended on the respective other. Malays knew they needed a strong, even if Chinese-dominated economy to make the NEP succeed. The Chinese wanted to avoid race riots at every economic downturn and thus took the *Merdeka* bargain as an acceptable compromise. Both dominant groups were reasonably assured that what they got under *Merdeka* was the best they could hope for, and at the same time provided sufficient benefits to them to be worth the compromises. The Indian population, small in numbers and economically marginal, had no bargaining power and lost out.

The determination whether states engage in rapacious predation or pro-growth policies is made domestically, but participating in international arrangements to attract FDI has a tendency to limit the state in the area of oppression more than in the area of protection of its citizens.[12] The crucial issue is not a power shift between state and non-state actors, such as international organisations or transnational corporations, but a sort of "entwinement" (Weiss 2005: 346). In the modern era, state and corporations have grown in power. The latter look to the state to assure adequate conditions for investment. The former has retained the capacity of regulating business to match the demands of the citizenry in terms of access to jobs, consumer goods and social wages. Thus, the degree to which the state's elites are willing to offer political voice to citizens is a research question that should focus more on the domestic political realm than on the forces of globalisation.

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[12] The exception is a situation where easily monopolisable resources are the mainstay of the economy.

CONCLUSION

In this paper, we have laid out the withering state theory that informs much of the anti-globalisation argument. Globalisation critics have argued that global economic processes represent a structural constraint that small states cannot hope to escape. As a result, small states have two options: either stay outside the global economy and face the consequences of isolation—lack of economies of scale and scope and the poverty that comes with economic and technological marginalisation; or integrate into the world economy and accept its rules and limitations, but at the price of forsaking state autonomy. Doubts about this view have been voiced when empirical evidence from around the world did not conform to some of this theory's predictions.

Here, we showed that the state is not withering in two case studies of highly globalised—that is, economically integrated—states. These two cases add evidence to the arguments of those who doubt the withering state theory. But more importantly, the two cases add a theoretical angle to the debate. By bringing in assumptions why states behave the way they do, we expand the discussion from one of empirics to one of causality. So far, proponents of the withering state and convergence theories have provided us with assumptions about the phenomenon of globalisation as a structural force imposing itself on states. We remove the state from this realist framework in which all states are assumed to be forced to act in a manner predetermined by the unalterable structures of the international system and look at domestic processes, the capture and re-capture of the state by its elites. The state turns from a subject acted upon into a process, with elite groups and their utility-maximising interests as the causal factors for decisions made in contesting the position in the global economy. The two cases, Vietnam and Malaysia, have acted and reacted differently to global economic stimuli as a consequence of their different domestic arrangements. The elites, based on historical and demographic factors and resource endowment, have positioned themselves differently in their attempt to maintain power and wealth. This positioning determines the policy decisions they take during the state's engagement with the global economy.

This approach allows the observer to investigate more fundamental processes than global structures or state reactions. We can ask, what arrangements have the elites that capture the state made to assure their power? With this understanding, we can then evaluate policies in the context of elite interest. When high inflation caught up with Vietnam in early 2008, for example, it was predictable that the Vietnamese elite would try to bring inflation under control even at the expense of immediate elite interest (such as deflating real estate prices and stock market value), since

the Communist Party—Vietnam's ruling elite—has made the determination that its fortunes are inextricably linked with the ability to provide continued economic improvements for all strata of society. Withering state theory would have predicted the opposite outcome, focusing on the power of investors in FDI-dependent Vietnam. Empirical analysis of earlier data alone would have provided little, since the rapid emergence of high levels of inflation is a first in Vietnam's period of global integration. Linking what we know about global economic forces to domestic institutional arrangement provides us with a fuller picture of causal factors about decision-making under changing economic conditions.

In contrast to Vietnam, Malaysia the ruling elite is less growth and more distribution-oriented. As a consequence, it focuses on keeping crucial segments of society content rather than society on the whole. A view on global processes or analysis of existing data alone would not have yielded these insights; instead, an understanding of Malaysia's domestic processes as determinant factors for its decisions on how to engage with the global system yields richer results.

If globalisation is inevitable, it is not because of the dominant discourse of corporations or what is generically called 'the West,' but because of the groundswell of demands from large numbers of regular people. The elites saw it in their interest to join the global economy, in order to maintain their power and benefit economically. They could only do so by satisfying a bottom-up demand for economic improvement. But where elites have managed to limit what Weiss (see above) called the "logic of voice" to a smaller segment of society, reaction to crisis will be different than in a society where 'voice' is broader.

No case study can claim universal generalisability, but the insights into the examples of Vietnam and Malaysia allow us to ask better questions for more research. Both Malaysia and Vietnam are strong states and internationally well integrated economies. Further studies should look at countries with weak state capacity and countries that have remained at the margins of the global economy. The suggestion emerging from this paper is that weak states attract less FDI than stronger ones, and that less globalised states would exhibit lower social wage levels than more integrated ones. Cases could be studied in countries where due to the fractured nature of the state because of unresolved elite capture and constant infighting, state capacity is extremely low. Atzili argued that such states end up as international trouble makers, since their internal instability spills over into regional conflicts (Atzili 2007). These countries, because they never even temporarily resolve the conflict among elites for control over the state, cannot provide the conditions for international investors to take the risk and

commit resources (except in natural resource extraction, where the limited availability of the resource is a natural limitation on investors' location decisions). As a consequence, the elites continue to engage in battles over distribution rather than growing the pie. The result is a very broad pyramid of wealth distribution, with a broad base of widespread poverty and an extremely small top, with little in between. Cases include sub-Saharan Africa, where it appears that the weak states are indeed attracting very little FDI. Central and South America contain fractured states. Eastern European states such as Ukraine or Georgia fall into this category. Studying these and similar cases would provide a test for the hypothesis that trade integration does not lead to a withering state, but on the contrary, that the withering of the state (or its failure to consolidate in the first place) does not allow for successful international integration. These would be welcome tests for the central tenet of this paper, that significant state capacity is a precondition for integration and continued participation in the global economy.

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