Intellectual and institutional convergence in East Asia: the voluntary euthanasia of the Asian model?

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Paper presented to the 2003 International Studies Association Annual Convention, Portland, Oregon, 26 February – 31 March 2003.

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Abstract

How did East Asia, generally viewed in the mid-1990s as an economic miracle, become seen only a few years later as the bastion of failed 'crony capitalism'? I argue that the Asian crisis of 1997-8 is insufficient to explain this reversal of opinion, as is the dominance of the US in the IMF and other key international forums. Rather, the de-legitimation of the 'Asian model' was due to a combination of the crisis with the contemporary ascendance of a set of broader, conventional economic ideas about optimal economic governance. Moreover, this shift in thinking was replicated within many of the East Asian countries themselves. The crisis empowered those who were able to use these ideas to push for convergence upon western governance models (particularly Anglo-Saxon ones), both within East Asia and without. Nevertheless, ideas alone have not so far been sufficient to achieve full convergence, creating a large gap between the new rhetoric of governance in Asia and regulatory and private sector practice.

Intellectual and institutional convergence in post-crisis Asia-Pacific: the voluntary euthanasia of the Asian model?

1. INTRODUCTION

Up until the very eve of the crisis of the Thai baht in mid-1997, the developing countries of East and South-East Asia were commonly lauded as exemplars of successful economic development. Successful forays into consumer electronics and other technology-intensive sectors and the growing importance of the region as a source of manufacturing exports and as a destination for foreign direct investment seemed to underline their ruthless efficiency. The 'East Asian model' had become commonplace in economic and political science literature and, it seemed, provided a viable alternative to neoliberal development models (Amsden 1989; Berger and Hsaio 1987; Haggard 1990; Wade 1990; World Bank 1993).[1]

In a matter of months, however, as the financial crisis spread from Thailand to Indonesia to Korea and elsewhere, this conventional wisdom was completely reversed. Now, the East Asian countries were being damned for a 'crony capitalism' that created moral hazard, inefficient investment and deep financial vulnerabilities (Corsetti et al. 1998; Haggard 2000; Krugman 1998). Given this diagnosis, the remedy was for greater transparency and, above all, deep institutional reform that is directed towards a complete change in the nature of economic governance in the developing East Asian economies. The template of reforms all aimed at promoting one thing: moving East Asian countries away from a 'cronyist-relational' model of economic governance towards an arms-length,

[1] I am not arguing that a single Asian model did exist, but as we will see, the official critique that dominated the subsequent debate about what happened to Asia tended to assume one did.

market-based ‘best practice’ model of economic governance. The IMF packages in Thailand, Indonesia and Korea all focused heavily on such structural reforms (Goldstein 2001; Kapur 2001).

There is a puzzle as to why the conventional wisdom of the 1990s concerning the so-called East Asian model was so dramatically reversed. The financial crisis of 1997-8 is insufficient to explain this reversal, since cronyism and moral hazard had long been attributes of extraordinarily successful economies in the region. Furthermore, many countries have recently suffered financial crises, including the US in the 1980s (the Savings and Loans debacle), the UK in 1992 (the inglorious exit from the European Exchange Rate Mechanism) and Mexico in 1994-5, but these did not always lead to such dramatic reversals of conventional wisdom. Certainly, the Asian crisis was much deeper and more sustained than those in most of the developed world in recent years, but it was far from clear that this meant that their whole structure of economic governance needed to be entirely rebuilt. Nor, I will argue, is the reversal explained away by argument that the US, through its dominance of the IMF, effectively enforced this ‘western’ interpretation on unwilling governments in East Asia (Wade and Veneroso 1998; Soederberg 2003).

This paper makes two main arguments. First, it is only possible to explain the reversal of conventional wisdom in the East Asian case by reference to a broader global context that provided fertile intellectual ground for a fundamental shift in conventional thinking about optimal economic governance. Second, this shift in thinking was replicated within many of the East Asian countries themselves, both before and after the crisis. What the crisis did was to empower those who were arguing for convergence upon western governance models (particularly Anglo-Saxon ones), both within East Asia and without.

The paper is structured as follows. The next section discusses the ideas (or intellectual fads) that help us to understand the shift in conventional thinking about East Asia that occurred in the late 1990s. Section 3 then shows how various East Asian governments themselves accepted the nature of the critique and the proposed reforms. In this section, I discuss official East Asian attitudes towards the IMF packages and East Asian participation in international 'standard-setting'. Due to space constraints, this paper does not consider the subsequent fate of the reforms, that is, the extent to which they have been implemented in various East Asian countries. However, I discuss in a conclusion how the victory of a particular set of ideas may not (yet) have resulted in dramatic system transformation in East Asia.

2. FROM ASIAN MIRACLE TO CRONY CAPITALISM

Up until the crisis, the East Asian developmental 'model' was seen as an extremely successful alternative to the Washington Consensus. Authors typically praised the region's 'strong governments' for pursuing policies that avoided the trap of pandering to vested interests (Haggard 1990; World Bank 1993). Within a few months of the crisis, however, East Asian governments were seen as 'captured' by an alliance of domestic bankers and large corporate conglomerates, often family owned. Cronyism, corruption and nepotism (or 'KKN', to use the Indonesian acronym) became the diagnosis in key policy circles. Now, it seemed, cronyism needed to be rooted out of these economies through deep institutional reforms. The following section argues that the rapidity and extent of this reversal in attitudes towards East Asian developing countries cannot be explained by the crisis alone, which was diagnosed differently by various experts and academics. The reversal needs to be understood in a broader context of two conventional wisdoms that had emerged by the late 1990s, concerning 'agency independence' and the superiority of the US economic model.

The East Asian crisis and its interpretation, 1997-9

The East Asian crisis was undoubtedly important in undermining previous arguments about the superiority of the so-called Asian model.[2] However, the crisis by itself could not do this, since there were competing, plausible explanations of the crisis that did not place blame upon Asian cronyism or domestic policy failures. There were two notable contributions that placed the blame upon global capital markets. The first was from Steven Radelet and Jeffrey Sachs (1998) of Harvard, who argued that imperfections in capital markets leading to a financial panic were the primary cause of the crisis. Although weaknesses were evident in the Asian economies, these were insufficient in their view to explain the extent of the panic (see also Wade and Veneroso 1998). The second was from Joseph Stiglitz, then chief economist at the World Bank, who argued publicly against the IMF's diagnosis and policy solutions (see Stiglitz 2002).

Others placed the blame for the crisis squarely upon domestic political structures and policy failures. Paul Krugman's analysis of January 1998 put the basic argument clearly. 'Severe moral hazard problems' were created by 'implicit government guarantees' to politically connected banks and firms in East Asian governments, leading

[2] I do not wish to imply that there was only one Asian model, or that its nature was not contested (see Foot and Walter 1999). However, for the purposes of describing the post-crisis debate this assumption is reasonable.

to over-leverage, excessive concentration and financial vulnerability (Krugman 1998).[3] Another influential article, entitled 'Paper Tigers? A Model of the Asian Crisis' (Corsetti et al. 1998), similarly argued that moral hazard combined with financial opening facilitated over-investment and excessive external (and often short-term) borrowing in Asia. This analysis, however, also accepted that financial liberalization was premature and may have combined with capital market imperfections to produce high levels of financial fragility in the region.

The evidence thus provided potential support to both the capital markets imperfection explanation and the domestic policy failure explanation. Indeed, Sachs and Radelet, in a later article (1999), acknowledged the importance of both factors. Meanwhile, Krugman (1999) had gravitated towards the capital markets imperfection argument. Although there is no space here to recount this debate, it is sufficient to note that initially, prominent economists differed fundamentally on both the diagnosis and the implied policy solution.

In the major international policy circles, there was also some conflict over the diagnosis of the crisis. The US and UK governments were ill-disposed to the Radelet-Sachs interpretation, as were international banks and the IMF, which notably shared the KKN diagnosis (see Lane et al. 1999). However, there were other G-7 voices, notably the Japanese and Germany's Finance Minister, Oskar Lafontaine, who were more disposed to blame the international banks. One of the reasons that this view was not pushed vigorously within the G-7 was because of problems at home in Japan and Germany. As argued below, the Japanese were too politically weakened by their own ongoing crisis to

[3] Krugman went on to say that this account was an over-simplification, but it nevertheless appealed to and captured the attention of many critics of the East Asian model.

defend Asian practices vigorously. In the case of Germany, there were more conservative voices within the Bundesbank and Finance Ministry who were much more willing than their finance minister to blame crony capitalism and to advocate domestic reform and greater transparency. These conservative German voices were especially concerned to prevent further international ‘bailouts’ of what they saw as corrupt governments. For example, in its annual report of 1997, the German Bundesbank offered the Krugman (1998)/Corsetti et al. crony capitalism-moral hazard diagnosis of the crisis and concluded the need for domestic regulatory reform in Asia:

> [T]he answer to the crises in eastern Asia cannot be a return to a system of regulated capital movements; nor would that be possible, indeed, in an era of global capital markets. Instead, what is needed in the individual countries is a strengthening of the financial and supervisory systems, calculable underlying macroeconomic conditions, a stability-oriented economic policy and a more transparent economic situation, to enable market players to take rational decisions based on comprehensive data. (Deutsche Bundesbank 1998: 9).

The Bundesbank’s views proved to be influential. A key step in the official entrenchment of this particular diagnosis and policy solution was the decision by the October 1998 by the G-7 countries to commission Hans Tietmeyer, the recently retired President of the German Bundesbank, to recommend various reforms to promote international financial stability. The Tietmeyer report of February 1999 unsurprisingly advocated little in the way of reform to the existing international architecture, other than more coordination amongst the key international and national authorities involved in financial sector stability. The main emphasis was upon formulating and disseminating a set of international ‘best practice’ standards and codes for financial sector governance. The Financial Stability Forum, established in April 1999 by the G-7 in response to the Tietmeyer report, was placed in charge of this task. Its various working groups, which have included developing country representatives, including a number from East Asian countries, in turn placed emphasis not upon the regulation of international financial flows, but upon reforms to domestic regulatory governance.[4]

Consistent with this approach, the G-7 Finance Ministers, reporting to the heads of government meeting in Cologne in July 1999, strongly prioritized the importance of domestic institutional reform in emerging market countries (G-7 Finance Ministers 1999). The new emphasis on domestic financial governance reform did not entail the rejection of the Washington Consensus; rather, it supplemented it. Financial liberalization continued to be promoted as welfare enhancing, with the additional proviso that an effective prudential regulatory framework is in place. Larry Summers' well-known airline metaphor captures the dominant view nicely, which is that financial liberalization is worth having despite the risks, and that the solution is to build a (domestic) regulatory infrastructure that can support it.[5]

Agency independence in economic governance

The emergent policy orthodoxy outlined above was not simply a product of the brute political power of conservative, pro-market voices within the G-7. Its appeal was also in part due to another existing economic orthodoxy, that on agency independence in economic regulation. This argument was made most prominently in the literature on monetary policy and credibility. Delegation of monetary policy to a conservative central banker with assured political independence could be an optimal societal solution to the

[4] For example, the emphasis of the report of the working group on capital flows is upon on the costs imposed by 'distortions that may arise from national policy measures or international regulations that biasing capital flows towards forms that can generate greater volatility or risk.' The group included representatives from Malaysia, Japan, Brazil, Chile, and South Africa (Financial Stability Forum 2000c).

[5] A related line of argument is that financial openness combined with trade closure renders economies especially vulnerable to financial crisis (such combinations are most marked in Latin America). Again, the recommended solution is greater trade openness rather than financial closure (IMF 2002: 108).

‘time-inconsistency’ problem (see Rogoff 1985). Again, although this view did not go uncontested in the economics literature,[6] it was highly influential in Europe (as embodied in the Maastricht treaty) and in the international financial institutions since the 1980s (see McNamara 1998).

The focus of the economic literature on central bank independence (CBI) was entirely upon CBI as a solution to the problem of monetary policy credibility. However, one tradition of economic literature had long warned of the possibility that regulators in general could be captured by interest groups and of the need to insulate such agencies from political influence.[7] Furthermore, it was easy and some might say logical to extend the CBI model to argue that not only should central bankers be independent of governments, but financial regulators (who are frequently central banks) should be as well. If politicians can easily manipulate monetary policy for short run electoral gain, so too they have private or electoral incentives to intervene in financial regulation or in competition policy in ways that are inconsistent with general social welfare.

The US FDIC Improvement Act of 1991 was a key public policy development in this respect, since it explicitly reduced the scope for regulatory discretion in dealing with the problems of weakened financial institutions. Regulatory forbearance, or the deliberate failure to apply regulations generally or in specific cases, was deemed to be endemic in the Savings and Loan sector in the 1980s. Regulatory discretion regarding all insured depository institutions was to be minimized by a new framework of ‘Prompt Corrective Action’ (PCA), which would entail specific regulatory actions automatically triggered

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[6] See, for example, the various articles in *Oxford Economic Papers*, Volume 50(3), July 1998.
[7] This included American economists such as James Buchanan and George Stigler as well as the German ‘Ordoliberals’ such as Walter Eucken and Wilhelm Röpke.

when these institutions fall below designated safety and performance thresholds. This regulatory elaboration on the old 'rules vs. discretion' debate in the monetary policy literature essentially shifted the emphasis towards fixed rule regulatory regimes. Although this constrained financial regulators more than in the past, it was also intended to empower them to resist pressures for forbearance from political or business quarters. Prompt corrective action, along with 'forward-looking criteria' for loan quality evaluation, have since become ubiquitous in financial regulation worldwide. Notably, the model of the independent but rule-constrained regulator was adopted by the UK in 1997 and by the Basle Committee on Banking Supervision when it was negotiating the Basle Core Principles for Banking Supervision over 1996-7 (see below). In both cases, the model was accepted before and independently of the Asian crisis.

Shifting economic fortunes: the US, Japan and Europe

The dominance of American and British voices on financial regulation within the G-7 over 1997-9 also owed something to another conventional wisdom well-established by this time, that of the superiority of the US or Anglo-Saxon economic model. It is also evident that this conventional wisdom, as with that on the causes of the East Asian crisis, went beyond mere empirical 'fact' in its sources of support.

From the early 1990s, market capitalism appeared to be launching the US economy towards a new productivity miracle. US productivity growth appeared to be on a marked upward trend, and by the late 1990s, Alan Greenspan among others argued that a permanent rise in productivity growth due to the information technology revolution had raised the sustainable level of economic growth in the US and, perhaps, asset prices as well.[8] As one of Greenspan's fellow-Federal Reserve Governors, Edward Gramlich, remarked in early 2001:

> Using the internationally comparable OECD data to compare rates of productivity change across countries, we see that in the 1981-95 period the United States had the lowest rate of overall productivity change of all thirteen countries [of 1.2%]…But in the post-1995 period, the U.S. sleeping giant awakened. In this recent period, the U.S. overall rate of labor productivity rose to third among the countries, behind only Ireland and Australia…In several countries--France, Italy, Japan, the United Kingdom, the Netherlands, and Spain--overall labor productivity growth slowed quite sharply.[9]

That the US economy would be outperforming its erstwhile competitors, Japan and Germany, in growth potential by the end of the century would have surprised most 1980s commentators. Along among the major economies, the US now appeared uniquely poised to dominate the IT revolution and to restore its dominance across whole swathes of manufacturing industry as well as services. One indication of the wide perception of this new US dominance can be found in the annual Financial Times-PricewaterhouseCoopers survey of chief executives of the world's most respected companies. The 2000 survey ranked 15 American firms in the top 20 and 8 in the top 10. Sony and Toyota, both Japanese, were the only non-American firms to make the top 10. General Electric and Microsoft consistently dominated the top two spots in the late 1990s, symbolizing America's newfound pre-eminence in manufacturing and services.[10]

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[8] Alan Greenspan, 'Information, productivity and capital investment,' remarks before The Business Council, Boca Raton, Florida, 28 October 1999, available at: http://www.federalreserve.gov/BOARDDOCS/SPEECHES/1999/199910282.htm, accessed 1 February 2003.

[9] Remarks by Governor Edward L. Gramlich before the International Bond Congress, London, U.K., 20 February 2001, available at http://www.federalreserve.gov/BOARDDOCS/SPEECHES/2001/20010220/default.htm, accessed 1 February 2003.

[10] 'World's Most Respected Companies – Overview', *FT.Com,* December 13, 2000, available at: http://specials.ft.com/wmr2000/FT3GX6PUNGC.html, accessed February 5, 2002.

Meanwhile, economic performance in Germany and especially Japan remained consistently unimpressive throughout the 1990s.

Credit was also given to America's efficient capital markets. An American invention, venture capitalism, was accorded particular importance in financing the development of the booming information technology industry. The efficiency of US risk capital markets in general became the envy of the world, in the process reversing the views of only a few years earlier that the US financial system promoted 'short-termism' on the part of managers of non-financial firms (see Porter 1992).

The contrast between the general perceptions of the US and its main 1980s challenger, Japan, could not have been starker. As the long crisis of the Japanese financial system and economy in general wore on in the 1990s, the Japanese challenge faded away entirely in public and political perception. In fact, as Japanese economic growth consistently struggled to remain positive, Japanese weakness became seen as an economic and political threat to US interests in the Asian region. As Japan's financial sector problems deepened, so too the weight that Japan carried by the late 1990s within the G-7 and G-10 on governance issues eroded.[11] Simply, Japan increasingly lacked credibility on some of the key issues being addressed in the various international forums in the late 1990s, notably issues relating to effective bank regulation, supervision, risk management and financial disclosure. One of the most poignant examples was the demise

[11] Confidential interview, senior Bank of Japan official, Tokyo, 18 June 2002.

and ultimate failure of Long Term Credit Bank, formerly one of the largest banks in the world, whose chief executive had authored texts on risk management.[12]

Specifically, Japan's chronic financial sector problems in the 1990s reduced its influence in the G-7 debate over what happened to East Asia. The weak prudential regulation aspect of the 'Asian model', which was difficult to deny, became even more difficult to defend after the Asian crisis broke, since it seemed to many of Japan's G-7, G-10 and OECD colleagues to fit a general pattern prefigured in Japan itself. As Mr Sakakibara, one of Japan's key negotiators on international financial issues through the 1990s, remarked: "who could disagree with the need to implement 'best practice' regulation?"[13] In the rest of Asia, there is a general recognition of Japan's diminished credibility on these issues.[14]

By contrast, the US system of financial regulation, led by the Federal Reserve and the Securities and Exchange Commission (SEC), achieved almost a cult status by the late 1990s.[15] The comparative contrast between the US and Japan in the 1990s suggested that with effective domestic regulation, financial liberalization could be made to work for the general good, since it would minimize moral hazard and promote financial stability and efficiency. The lesson for East Asia and other countries was clear: *financial liberalization*

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[12] For a general and readable account of Japan's problems, see Kerr 2001. In private international organizations that exercised some influence over official deliberations in these areas, such as the Group of Thirty and Institute of International Finance, Japanese banks have also had little influence (Kentaro Tamura, LSE PhD thesis, 2003).

[13] Interview, Mr Eisuke Sakakibara, ex-Vice Minister of Finance for International Affairs, Tokyo, 18 June 2002.

[14] Based on confidential interviews with officials and other commentators in the East Asian region, 2002.

[15] Although the US accounting and auditing scandals of 2001-2 have certainly taken the shine off the US model since then, this has only strengthened the view that agency independence and best practice rules are core requirements of good governance. The US regulatory response, for example, has been to legislate for greater auditor and corporate board independence, increased SEC financial resources and powers, and new accounting standards. In much of East Asia, governments have responded similarly to 'Enronitis'.

was dangerous in the context of KKN and endemic moral hazard, but beneficial with good domestic economic governance (cf. Corsetti et al. 1998). This conventional wisdom was applied universally to developed and developing countries alike (as in the Bundesbank quotation in 2.1). The policy conclusion was therefore not for Asian governments simply to retreat into 'financial repression', but to pursue *continued financial opening and deep regulatory reform.*

3. EAST ASIA: *MEA CULPA*

The previous section argued that the official KKN interpretation of the Asian crisis was facilitated not only by the 'facts on the ground' in Asia, which had various interpretations, but also by particular conventional wisdoms that favoured the approach and diagnosis adopted by the US and UK governments and the German financial establishment. I argue in this section that this was also true in Asia itself, where various groups shared both the official western diagnosis of the crisis and the recommended policy solution. I provide evidence for this in two areas of policy: in attitudes towards the region's IMF programmes of 1997-8 and in East Asian participation in specific international standard-setting processes.

East Asian technocrats and the IMF packages

It is often argued that this shift on the part of East Asian developing countries was coerced rather than voluntarily adopted. Sachs for example argued that the IMF (and behind it, the US Treasury) was attempting to 'make the world safe for … short-term money managers'.[16] The institutional reform agenda of the IMF, adopted from the time of the first Thai programme of August 1997, was running considerably ahead of the G-7's ruminations on domestic governance reform. All the IMF-led financial assistance to

[16] Jeffrey Sachs, in *The Economist,* 12 September 1998, p.24. See also Feldstein 1998 and Rodrik 1999:6.

Thailand, Indonesia and Korea required structural reforms to bank supervision, corporate governance, insolvency regimes, accounting standards and other areas of governance. Over 60% of these conditionalities were related to the financial sector (Goldstein 2001). There is also evidence that the US government used its position within the IMF to achieve structural reform and economic governance changes in the crisis-hit countries.[17] In addition, the crisis-hit countries in Asia also had to be concerned about restoring their reputation vis-à-vis international investors, who may have shared the US official view.

The argument that the reform programme was externally imposed rather than voluntarily accepted is perhaps most persuasive in the case of Indonesia until May 1998, when President Suharto left office. There was opposition to the IMF programmes in all of the three crisis-hit countries, but only in the case of Indonesia did this opposition extend to the heart of the government. There is little doubt that this opposition was due to the direct threat reform represented to the entrenched economic privileges of the Suharto family and friends, rather than a high-minded attachment to an 'Asian' economic model. However, even here, most of the objections were to specific provisions of the programme (such as ending various monopolies that had been granted to Suharto family members and cronies, or closing connected banks), not to the broad economic governance reforms agreed to in the IMF packages (Blustein 2001: 207-34).

Nevertheless, that powerful western governments and private sector interests shared the IMF critique of the Asian model should not obscure the fact that economic reformers and rising politicians in Asian countries, including in Indonesia, also shared it.

[17] The US Treasury (2000: 1), in an annual report to Congress, argued that many of these conditionalities were 'supported by the vigorous use of the voice and vote of the USED [US Executive Director] at the IMF.'

Within most countries in the region, technocrats and liberal reformers saw this pressure for convergence upon a broadly Anglo-Saxon model of economic governance as an opportunity to push for reforms (such as central bank and regulatory agency independence) they had long sought. For many reformers, IMF intervention was often a blessing in disguise.[18] This is not to say that these governance reforms were *widely* supported in the East Asian countries, though many civil society activists in the various countries did.

Korea is perhaps the starkest case of a reformist government using the crisis to effect fundamental political and economic change. President Kim Dae-Jung, elected in November 1997 in the midst of the crisis, was determined to use the crisis to reduce the political and economic power of the large chaebols (family-controlled industrial groups) in the Korean economy. A number of economic reformers joined the new administration and filled key positions in the government and bureaucracy, notably the new independent financial regulators, the Financial Supervisory Commission and Financial Supervisory Service.

Before the crisis, moves were afoot to reduce the power of the Ministry of Finance and the Economy (MOFE), which had pursued economic development at the expense of prudential regulation and which had hitherto prevented Korean banks (or firms) from failing. Pressure for reform grew to the point where a Presidential Commission on Financial Reform was established with a mandate to review and recommend reforms to the financial regulatory and supervisory structure in Korea. MOFE was explicitly excluded from committee membership because of its well-known

[18] On the Thai case, see Siamwalla 1998: 11.

opposition to reforming financial regulation. Some members privately referred to it as the 'death to the banks committee,' reflecting their view that chronic regulatory forbearance, aided and abetted by MOFE, had created weak banks and endemic moral hazard in the financial and corporate sectors.[19] The committee made a series of recommendations, including that the various separate regulatory agencies be merged into a single unified and independent financial regulator. It also argued for the adoption of PCA and other forms of regulatory 'best practice.'

Draft legislation was submitted to the National Assembly on 23August 1997, months before the Korean crisis, but opposition from major chaebols, the Bank of Korea and MOFE ensured that it stalled. Only once the crisis broke did political support for this reform programme increase. Opponents of enhanced prudential supervision now found it difficult to oppose reform. In the midst of the crisis, on 29 December 1997, the reforms were passed by parliament. Korean-authored reforms, not an IMF blueprint, therefore formed the basis of Korea's post-crisis reform programme in financial sector governance. The IMF essentially rubber-stamped this Korean plan.[20] Domestic technocratic reformers were now in a position to drive the reform process. They explicitly replaced Korea's previous Japanese governance benchmark in financial sector governance with a US-UK benchmark. The new Kim Dae-Jung government, with its own anti-chaebol political objectives, allowed them to pursue these goals. Reformers now in positions of importance were as frank as any IMF staffer on the failings of the old model. For example, Il-Sup

[19] Author interview, Dr Buhm-soo Choi, Advisor to the Director, Financial Supervisory Commission, Seoul, Korea, 20 September 2000.
[20] Confidential author interviews, Seoul, Korea, September 2002.

Kim, the new chairman of the Korea Accounting Standards Board, argued in October 2000 that:

> More fundamental causes of the recent crisis that hit Korea can be found in the structural problems embedded in various sectors of the economy. The government-led high-growth strategy over the last three decades brought about some serious adverse side effects. Korea's corporate management and financial systems lacked transparency; moral hazard was endemic, and overall the economy was suffering from the absence of market discipline as a result of the collusive relationship that had built up between the business community and political circles (Kim 2000).

Similar political changes were already underway in Thailand not long after the outbreak of the Baht crisis in July 1997. The new Democratic Party government under Prime Minister Chuan was also committed to economic reform of a kind that was very compatible with the emergent international economic governance standards. As in the Korean case, the IMF was happy with the new government's proposal for making the Bank of Thailand and the Securities and Exchange Commission (SEC) independent.[21] Certainly, the political mandate for reform in 1997-8 was less strong than in Korea, as evidenced by the resistance of some members of the governing coalition and the legislative gridlock that has resulted in Thailand. However, at least at the beginning of the post-crisis period, prominent reformist technocrats succeeded in utilizing the IMF programme to achieve reforms they had long sought.

Although in Indonesia there was no rapid change of government that could launch the country towards domestic-led reform, technocrats found their power somewhat restored even under the last months of the Suharto regime.[22] Indeed, economic liberalism

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[21] Author interview, Dr Pisit Leeahtam, Professor of Finance, ex-deputy finance minister, Chulalongkorn University, 6 March 2002.
[22] Blustein 2001: 101; author interview, Dr Soedradjad Djiwandono, (ex-Governor, Bank Indonesia), Singapore, May 14 2002.

has a long history in Indonesia, notably during the early Suharto years in the 1960s and 1970s in which technocrats from the 'Berkeley mafia' dominated economic policymaking. The Indonesian elite is also notably more westernized than, say, those in Japan or Korea. As elsewhere, the technocrats' hope was that the crisis, by weakening powerful corporate groups and cronies, could be used to achieve a greater degree of implementation than had been achieved in the past.[23] Indeed, when the IMF mission went to Jakarta in September 1997 to negotiate the programme, several senior economic policymakers confided to IMF staff that they wanted the Fund to impose various reforms they had long favoured. Mar'ie Muhammad, the Finance Minister, claimed he wanted a frontal attack upon the many monopolies and subsidies that had flourished under the cronyistic Suharto regime (Blustein 2001: 101).

The basic problem technocrats had with the Suharto regime was the pressure for regulatory forbearance.[24] Although the Indonesian negotiators tended to support the various reform demands being made by the IMF team and US representatives, their need to obtain Suharto's agreement to bank closures and other reforms put them in a difficult position (Blustein 2001: 101-2). After the Habibie government replaced Suharto in May 1998, outwardly resisting the internal and external political pressure for reform became untenable. In November 1998, Bank Indonesia undertook to completely revise its regulatory structure and practices, using the Basle Core Principles as the benchmark.[25]

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[23] Author interview, Dr Tubagus Feridhanusetyawan, Senior Economist, Centre for Strategic and International Studies (CSIS), Jakarta, 27 May 2002.

[24] Author interviews, Binhadi, Chairman, Bank Mandiri, and ex-Governor, Bank Indonesia, Jakarta, 29 May 2002; Dr Soedradjad Djiwandono, (ex-Governor, Bank Indonesia), Singapore, May 14 2002.

[25] Author interviews, Mrs Siti Ch.Fadjrijah, Director, Bank Supervision, Bank Indonesia, Jakarta, 27 May 2002; Mr I Gde Made Sadgana, Mr Imansya, Mr Agus Edy Siregar, Directorate of Banking Research and Regulation, Bank Indonesia, Jakarta, 30 May 2002.

Similar commitments were made regarding corporate governance and accounting standards.

Thus, although the crisis increased the leverage of the IMF and US in Asia, more importantly at the domestic level it empowered economic technocrats and reformists and the ideas they shared with the critics of the Asian model. Generally, technocrats wished to reverse the priorities of developmentalism (and also corruption), which in their eyes had socialized risk, created endemic moral hazard, and rendered prudential regulation ineffective. It had also encouraged weak monitoring of sprawling corporate groups by banks, with the result that dominant families managed corporations at the expense of minority shareholders, and had a strong preference for debt over equity (Capulong et al. 2000; Claessens et al. 1999a).

That this domestic political shift was not simply due to IMF leverage is also demonstrated by similar reforms in other Asian countries that were less affected by the crisis. Singapore and Hong Kong in particular, home to two of the region's most important financial centres, moved quickly to converge upon best practice norms in economic governance generally and especially in financial regulation. In Singapore, the crisis prompted a policy struggle over the financial sector reform process, leading to the resignation of a Deputy Monetary Authority (MAS) governor and the appointment of Deputy Prime Minister Lee Hsien Loong, one of Lee Kwan Yew's sons, as MAS Chairman. Since November 2001 he has combined this job with the Finance Minister portfolio, among other duties.[26] This centralization of power facilitated an acceleration of the reform process in Singapore. Both countries have also strengthened their corporate

[26] Estandards Forum, *Weekly Report*, vol. II, no. 35, April 29-May 3, 2002: 7.

governance codes in recent years and months, both have explicitly adopted the Basle Core Principles as a supervisory framework, and both have converged upon International Accounting Standards to reduce compliance costs for international firms.

Perhaps more surprisingly but tellingly, Malaysia, having explicitly and vocally criticized the IMF programmes as a threat to the Asian model in 1998, has also been quietly converging towards the western model itself. Until mid-2001 and the exit of Daim Zainuddin, the former finance minister, this was certainly true more in theory than in practice. Nevertheless, concerns about corruption eventually forced Dr Mahathir, the prime minister, to push out Mr Daim and to pledge an acceleration of the pace of financial reform. Even before this, Bank Negara, Malaysia's central bank, claimed that by mid-2000, it was in compliance with 23 of 25 Basle Core Principles, and would be in full compliance with all by the end of 2000, once market risk was included in its capital adequacy framework.[27] In terms of corporate governance principles and accounting standards, Malaysia has also committed itself towards convergence.[28] Furthermore, Malaysia is said to have been very supportive of financial sector reform in the APEC Finance Ministers' meetings since the crisis.[29]

East Asia and international financial standards

Although the G-7 has largely controlled the agenda of the reform debate, 'systemically important' emerging market countries have been invited to participate in various reform negotiations to promote the legitimacy of the standard-setting process. The US Treasury unilaterally convened the G-22 grouping in April 1998, with strong

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[27] Remarks by Mr Awang Adek Hussin, Assistant Governor, Bank Negara, in ADBI 2000: 4.

[28] For Malaysia's very Anglo-Saxon style corporate governance code, see http://www.combinet.net/governance/finalver/malaysia.htm, accessed 21 January 2003.

[29] Confidential interviews, foreign embassy representatives in Asia, May 2002.

representation of those developing countries Washington deemed as systemically important.[30] The G-22 created three working groups, bringing together representatives from 25 countries, including many in East Asia, to discuss different aspects of international financial reform.[31] Notably, the reports were highly critical of the standards of private and public sector governance in the Asian countries in the run-up to the crisis.[32]

Similar criticism was heard and accepted by the APEC Finance Ministers meeting only a few months later at Kananaskis in Canada. The Asian Policy Forum, a network comprising of academics and various regional institutions with expertise in financial regulation based in Tokyo, sought an independent voice but has in practice largely endorsed the regulatory reform agenda pushed in Basle and Washington (Asian Policy Forum 2001; Shirai 2001a). The Asian Development Bank, in which Japan and the US have equal financial weight (unlike the IMF and World Bank), also conducted a study of Asian corporate governance that reached conclusions consistent with the KKN diagnosis (Capulong et al. 2000).

In September 1999, the G-7 Finance Ministers, meeting in Washington D.C., agreed to establish the G-20 grouping to consider ongoing proposals for international financial reform. This largely followed the G-22 model, though it also included representatives from the major EU institutions and the IMF and World Bank (see table 3). The G-20 had less East Asian representation than the G-22, but still included Japan,

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[30] These countries were: Argentina, Australia, Brazil, Canada, China, France, Germany, Hong Kong SAR, India, Indonesia, Italy, Japan, Korea, Malaysia, Mexico, Poland, Russia, Singapore, South Africa, Thailand, United Kingdom and the United States. See 'Rubin Statement at Opening of G-22 Meeting', *USIS Washington File,* April 17, 1998, available at: http://www.usis-australia.gov/hyper/WF980417/epf502.htm (accessed January 22, 2002).

[31] The reports are available at: http://www.imf.org/external/np/g22/ (accessed January 22, 2002).

[32] See especially G-22 1998b: 7-9,13,16.

China, Korea and Indonesia.[33] So far, the G-20 has played no clear role in standard-setting or in implementation and its role seems primarily to be one of consultation and consensus-building, supportive of the work of FSF and other relevant international organizations.

[33] The Malaysian government was apparently upset to be excluded from the G-20 (*Euromoney*, 26 September, 1999).

Table 3: Overlapping memberships in key international organizations

Country	**G-7**	**G-10**	**FSF**	**G-22**	**G-20**	**OECD**
Argentina			Yes	Yes	Yes	No
Australia				Yes	Yes	Yes
Brazil				Yes	Yes	No
Canada	Yes	Yes	Yes	Yes	Yes	Yes
China				Yes	Yes	No
France	Yes	Yes	Yes	Yes	Yes	Yes
Germany	Yes	Yes	Yes	Yes	Yes	Yes
Hong Kong			Yes	Yes	No	No
India				Yes	Yes	No
Indonesia				Yes	Yes	No
Italy	Yes	Yes	Yes	Yes	Yes	Yes
Japan	Yes	Yes	Yes	Yes	Yes	Yes
Malaysia				Yes	No	No
Mexico				Yes	Yes	Yes
Netherlands		Yes	Yes			Yes
Poland				Yes	No	Yes
Russia				Yes	Yes	No
Saudi Arabia				Yes	Yes	No
Singapore			Yes	Yes	No	No
South Africa				Yes	Yes	No
South Korea				Yes	Yes	Yes
Thailand				Yes	No	No
Turkey				Yes	Yes	Yes
UK	Yes	Yes	Yes	Yes	Yes	Yes
US	Yes	Yes	Yes	Yes	Yes	Yes

Sources: G-20, G-22 and OECD websites, accessed January 29, 2002.

Notes: The membership of the G-20 comprises the finance ministers and central bank governors of the G-7, 12 other key countries, and the European Union Presidency (if not a G-7 member), the European Central Bank; the Managing Director of the IMF; the Chairman of the IMFC, the President of the World Bank, and the Chairman of the Development Committee. Various committees of the BIS, and the heads of IOSCO, the IMF, the World Bank, OECD, and IAIS are also represented at the FSF.

Because of the limited roles of groups like the G-20 in international standard-setting, we need to look in more detail at East Asian participation in standard-setting in two areas identified as crucial in the conventional diagnosis of the Asian crisis: bank supervision and corporate governance. The former mostly pre-dated the Asian crisis, while the latter occurred afterwards.

Basle Core Principles for Banking Supervision

Since its establishment by the G-10 countries in 1974, the Basle Committee on Banking Supervision (BCBS) has quietly become pre-eminent as the forum for international bank regulatory cooperation and standard setting. Although based at the Bank for International Settlements (BIS) in Basle, Switzerland, both regulators and central bankers are represented on the committee when these differ in a particular country. Like the BIS, it is dominated in membership terms by European countries; Japan is the only Asian member.[34].

The Core Principles for Banking Supervision, published in September 1997, are less well known than the capital adequacy accord and the concordat on supervisory responsibilities for international banks. However, the Core Principles now encompass both of these previous agreements (see table 2).[35] Their negotiation began after the G-7 countries called for action in this area at the Lyon summit in June 1996. A consultative document was issued in April 1997 and the final version in September 1997, in the midst of the Asian crisis. Although most of the negotiations were therefore conducted before the crisis, many of the Core Principles raised issues thought to be central to the Asian crisis then engulfing Thailand. The BCBS also made it clear that 'The Principles are

[34] There are currently 13 country members: Belgium, Canada, France, Germany, Italy, Japan, Luxembourg, the Netherlands, Spain, Sweden, Switzerland, United Kingdom and United States. Spain's recent accession to membership of the Committee was seen in Asia-Pacific as reflecting the continuing European/North Atlantic bias of the institution (author interviews, East Asian regulators, 2002).
[35] The Basle capital accord is currently undergoing another controversial revision.

minimum requirements…intended to serve as a basic reference for supervisory authorities in all countries and internationally.' (BCBS 1997: 2).

Table 2: BCBS Core Principles for Effective Banking Supervision (September 1997)

1. **Supervisory framework**
2. **Permissible activities of banks**
3. **Bank licensing criteria**
4. **Ownership review powers**
5. **Investment review powers**
6. **Minimum capital requirements for banks**
7. **Bank credit policies**
8. **Loan evaluation, provisions**
9. **Large exposure rules**
10. **Connected lending rules**
11. **Country risk rules**
12. **Market risk rules**
13. **Other material risk rules**
14. **Internal control systems**
15. **Preventing fraud**
16. **Onsite/offsite supervision**
17. **Contact with management**
18. **Offsite supervision rules**
19. **Mechanisms for independent validation of information**
20. **Consolidated supervision**
21. **Accounting / disclosure**
22. **Remedial measures / exit**
23. **Global consolidation**
24. **Host country supervision**
25. **Supervising foreign banks**

Source: BCBS, available at www.bis.org.

The BCBS has issued many additional related standards and interpretations of the above standards since the late 1990s. Neither these nor the Core Principles have legally binding status; the Committee works by consensus and on the basis of voluntary compliance. However, levels of compliance with BCBS agreements and standards are generally high for member countries. This is due to the perceived technical expertise of the Committee and its various working groups, and also because of the strong norm of mutual reciprocity between members of the club. In addition, the potential market costs of non-compliance for countries and their banks are substantial.

In the case of the Core Principles, the BCBS moved to involve regulators from non-member countries in its deliberations. East Asian countries have been courted actively and involved through the Core Principles Liaison Group (CPLG) and the EMEAP forum (Executive Meeting of East Asia-Pacific Central Banks). The CPLG's goal was to promote ownership and the broad legitimacy of the Core Principles in the major emerging market countries, whose adherence to the principles was thought crucial. This was meant to involve not merely consultation, but to enable such countries to provide input into the negotiation process itself. The CPLG included representatives from Argentina, Brazil, Hungary, India, Indonesia, Korea, Malaysia, Poland, and Singapore. Thus, in principle at least, there was substantial input from and consultation with the major Asian regulators. Furthermore, although the G-10 regulators dominated the Core Principles negotiation, the drafting committee also included representatives from Chile, China, Czech Republic, Hong Kong, Mexico, Russia and Thailand.

The Asian regulators also met on a regional basis since 1991 within EMEAP, the Basle Committee's regional dialogue partner in East Asia-Pacific, and through EMEAP's Working Group on Basle Standards. EMEAP consists of central bankers and regulators from Australia, China, Hong Kong, Indonesia, Japan, Malaysia, New Zealand, the Philippines, Singapore, South Korea and Thailand. In the EMEAP group, Hong Kong and Australia are said to be among the most vocal and active members, though Japanese representatives have also been prominent from time to time.

On the Core Principles, Asian central banks and regulators (often the same thing) were largely supportive of the broad principles elaborated by the more dominant members of the BCBS. Nor was there much disagreement within the G-10 grouping itself.[36] For most Asian central bankers on the CPLG and EMEAP groups, none of whom were yet legally independent of their governments, the Core Principles were mostly seen as best practice.[37] Interviews with East Asian central bankers and regulators did not uncover much ill-will towards the Core Principles, perhaps because they were sufficiently general as to be politically unthreatening.

This is somewhat surprising, since the Core Principles were in many respects clearly at odds with regulatory practice in a number of the East Asian countries consulted in the negotiation process. The recommendation in principle 1 that bank regulators be ‘operationally independent’ of government and political influence, for example, is especially prominent. The BCBS argues that with respect to principles 2 and 3, ‘clear and objective criteria… reduce the potential for political interference in the licensing approach.’ (BCBS 1997: 15-16). Apparently, this was pushed most strongly by the delegates from independent central banks at Basle, but was not strongly opposed by East Asian representatives.[38] Indeed, by 1999, Japan itself had both an independent central bank and a new, (theoretically) independent Financial Services Agency. Even before the Asian crisis had struck, it was difficult for countries openly to argue that a lax system of

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[36] Author interviews, Bank of Thailand, Bangkok, 8 and 12 March, 2002; Hong Kong Monetary Authority, 8 April 2002; Mr Eisuke Sakakibara, ex-Vice Minister of Finance for International Affairs, Tokyo, 18 June 2002.

[37] Dissatisfaction with the Basle process has increased significantly in Asia more recently over the negotiations on the reform of the capital adequacy framework (confidential author interviews with Asian bank regulators in 2002).

[38] Interview, senior official, Financial Services Agency, Tokyo, 20 June 2002.

prudential regulation in which enforcement was essentially discretionary was optimal from a regulatory perspective.[39]

Other aspects of the Core Principles were of some concern for East Asian negotiators. This was especially true of Principles 8-10, which include loan classification and provisioning standards, large exposure rules and connected lending rules. These related directly to areas of weakness in a number of East Asian countries that were exposed in the crisis, including connected lending, poor loan evaluation and provisioning standards and lax rules and implementation relating to large single and group exposures. Korea's Office of Banking Supervision[40] objected to some of these. Korean officials were concerned about the rule limiting large exposures to 25% of bank capital (CP No.9), since its sudden introduction could constitute a major shock to the Korean economy. The Koreans argue that they were able to prevent a clear statement of the 25% limit in the final version of the Core Principles, so as to obtain time to implement it.[41] A similar request was made concerning loan provisioning (CP No.8) and the enforcement of market risk and consolidated supervision requirements. These were clearly areas in which Korea lagged most of the G-10 countries. Additional concerns expressed by the Koreans at Basle were over the supervision of market risk and consolidated supervision.

Nevertheless, Korean arguments were largely framed in terms of implementation problems and requests for delay, rather than objections of principle.[42] This was also

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[39] Author interview, Mr Eisuke Sakakibara, ex-Vice Minister of Finance for International Affairs, Tokyo, Japan, 19 June 2002.

[40] OBS was formally located in the Bank of Korea, but in practice dominated by the Ministry of Finance and the Economy (MOFE).

[41] Written comments provided to author, FSS, Seoul, Korea, 20 September 2000.

[42] Author interview, Dr Buhm-soo Choi, Advisor to the Director, Financial Supervisory Commission, Seoul, Korea, 20 September 2000.

largely true of other Asian countries' contributions. The fact that the BCBS focused on the elaboration of broad best practice principles rather than attempting detailed harmonization of country practices goes some way to explain this. However, as argued above, it was also indicative of the extent to which economic regulators and central bankers from Asian countries did not object to the overall Basle Committee agenda.

OECD Principles of Corporate Governance

In April 1998, the OECD governments decided to develop, in conjunction with other relevant international organizations and the private sector, a set of corporate governance standards and guidelines. They did so in response to a report by an advisory group of business experts, chaired by the New York lawyer and corporate governance guru, Ira Millstein.[43] This group had been established by the OECD in 1996, well before the Asian crisis.

It was clear from the beginning that there was much less consensus amongst the major countries in this area than on bank regulation. The US supported the view, outlined in a series of American reports on the subject in the 1990s, that corporate governance was essentially about ensuring corporations were responsible to shareholders, with an independent board of directors as the key mechanism. The European and Japanese, in contrast, counted shareholders as only one set of important 'stakeholders', with other stakeholders including employees, customers, suppliers, creditors, debtors and the community in general. Monitoring of corporations by stakeholders, particularly by creditor banks, were seen as important for good corporate governance.

[43] Other members were Michel Albert (France), Robert Denham (US), Dieter Feddersen (Germany) and Nobuo Tateisi (Japan).

These differences were reflected in the composition of the advisory group, which unsurprisingly recommended that the OECD refrain from attempting to formulate and adopt a one-size-fits-all corporate governance code.[44] Even so, there was an Anglo-Saxon bias in the group's specific recommendations. To the extent that the alternative stakeholder version of corporate governance was accepted as valid, it was characterized as merely consistent with a long run attention to maximizing shareholder value. As Millstein remarked when launching the advisory group report in April 1998, the report stood on two legs: 'having a board which is capable of being independent of management, plus a recognition that the pole star is the shareholder.'[45] In his letter to the OECD secretary general introducing the group's report, the focus on shareholder value was even clearer, despite the qualification that there is no one-size-fits-all model. The advisory group, he said, had agreed that the 'fundamental parameters' of corporate governance were:

> [1] Increasingly, it is accepted that the corporate objective is maximising shareholder value, which not only requires superior competitive performance but also generally requires responsiveness to the demands and expectations of other stakeholders. [2] Increased transparency and independent oversight of management by boards of directors are the central elements of improved corporate governance. [3] Board practice should be subject to voluntary adaptation and evolution, in an environment of globally understood minimum standards. [4] There are certain areas in which the adoption of universal rules is preferable (such as in accounting).[46]

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[44] Adam Bryant, 'A Plan for Foreign [sic!] Corporate Accountability', *New York Times*, April 2, 1998, D4.

[45] Jane Martinson and William Lewis, 'OECD Urged to Draw Up Governance Guidelines', *Financial Times*, London edition, April 2, 1998, section I, 32.

[46] Letter from the Chairman of the Business Sector Advisory Group on Corporate Governance to the Secretary-General of the OECD, April 2, 1998.

It was not immediately obvious that this was compatible with the Japanese and Korean[47] positions, or with those of the continental European countries. Furthermore, these 'stakeholder' countries were in a potential majority within the OECD. Ministers from most countries found little difficulty in accepting the principles of 'fairness, transparency, accountability, and responsibility' emphasized in the report. Despite the potential difficulties, the OECD ministers agreed to establish the Ad Hoc Task Force on Corporate Governance, with the task of developing a set of non-binding principles that embodied the views of OECD members on this issue. It was to be chaired by the American deputy secretary-general of the OECD, Joanna Shelton, and included representatives from various other bodies, including the business and trade union advisory committees at the OECD, the BIS, the World Bank, the European Corporate Governance Network, the ICGN, the International Federation of Stock Exchanges, the World Federation of Investors, the Institute of Internal Auditors of Thailand, and the European Commission.

The difficulty of the task ahead was reflected in the inability of the International Corporate Governance Network (ICGN), a private organization working in the same area, to overcome competing views of appropriate corporate governance principles in July 1998.[48] Some ICGN delegates attacked the proposed statement of principles for being

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[47] Korea acceded to the OECD in 1996.

[48] ICGN was established in 1995 by a number of pension funds from various countries, though CalPERS, the Californian public employees' pension fund and a prominent corporate governance activist, played a key role in its establishment.

overly influenced by US thinking, though this approach to corporate governance did eventually triumph within ICGN (see below).[49]

During the OECD discussions in November 1998, the Federation of Korean Industries (FKI), which represents the chaebols, argued against an Anglo-Saxon approach. In addition to arguing that the task force should not assume there was a single good corporate governance model, the FDI argued that the OECD should not adopt rules that would entail a ban on holding companies.[50] In addition, the FKI argued against the adoption of specific rules relating to the composition of corporate boards (hitherto, boards of Korean companies have essentially been rubber stamps for controlling shareholders and managers). Similar concerns were expressed in Japan.[51] Finally, the FKI strongly opposed the OECD creating any binding rules in this area. The Asian corporate sector, like the European, has long been concerned that creating strong corporate fiduciary responsibilities to shareholders could foster 'frivolous' lawsuits.

The draft of the OECD code was posted on the OECD website on December 17, 1998 and invited comments from interested parties (OECD 1998). As compared with this draft, there is a little more on the primacy of shareholder rights and on the need to protect the environment, and a little less on the importance of an independent board audit committee, in the final document. Overall, however, very few differences exist between

[49] Roger Taylor, 'Conference Fails to Agree Global Code for Business Standards', *Financial Times*, London edition, section I, 4.
[50] Yoo Cheong-mo, 'FKI Concerned Over OECD Corporate Governance Rule', *The Korea Herald*, November 17, 1998.
[51] In Japan, LDP preferences for the reform of corporate governance focused on strengthening monitoring by auditors rather than strengthening the independence of boards. See 'OECD Panel Seeks Stepped-Up Corporate Governance,' *Jiji Press Ticker Service*, February 12, 1998.

the draft code and the final version, suggesting that the consultation process changed little.

When the final version of the OECD code was published in April 1999, Joanna Shelton, the American chair of the taskforce, denied the principles reflected an Anglo-Saxon bias.[52] Intra-OECD differences meant that the agreed code contained only broad principles rather than detailed requirements in five key areas: shareholder rights, the equitable treatment of shareholders, the role of stakeholders, disclosure and transparency, and responsibilities of the board (OECD 1999). Like the earlier Millstein report, it also stressed that a one-size-fits-all model did not exist and that individual countries should adapt these principles to specific local circumstances. Finally, as with most OECD agreements, the code is non-binding on country members.

The corporate governance principles are also reflective of alternative views of corporate governance. The third key principle of the code recognizes 'the rights of stakeholders as established by law and encourage active co-operation between corporations and stakeholders in creating wealth, jobs, and the sustainability of financially sound enterprises.' (OECD 1999: III). The preamble also accepts the fact that corporate governance is embedded in a broader political and legal institutional setting and cannot be understood in isolation. It also stops short of explicitly discouraging such practices as pyramid ownership structures, cross-shareholdings and of advocating the one share, one vote principle then promoted by activist groups such as the ICGN. Instead, it simply advocates transparency in relation to such practices (OECD 1999: Annotations, I.D). All of these concessions to established practice in many countries outside of the

[52] Jane Martinson, 'OECD Code to Safeguard Shareholders', *Financial Times*, London edition, section 2, 5.

Anglo-Saxon countries reflected the influence of the continental European countries and Japan and Korea in the drafting process.

Despite this ambiguity in the different OECD principles, the emphasis is nevertheless on the classical problems arising from the separation of ownership and control in Anglo-Saxon countries and the consequent potential for exploitation of minority shareholders. As the preamble states, ‘ good corporate governance should provide proper incentives for the board and management to pursue objectives that are in the interests of the company and shareholders and should facilitate effective monitoring, thereby encouraging firms to use resources more efficiently…[T]he Principles focus on governance problems that result from the separation of ownership and control’ (OECD 1999, Preamble). That the protection of shareholder rights is the first principle of the code can also be seen as reflecting an Anglo-Saxon bias.

The code also, perhaps surprisingly given the opposition to shareholder-driven litigation in a number of countries, notes that ‘the confidence of minority shareholders is enhanced when the legal system provides mechanisms for minority shareholders to bring lawsuits when they have reasonable grounds to believe that their rights have been violated.’ (OECD 1999: Annotations, II). The annotations to the code clearly associate effective board independence with the presence of independent non-executive directors on the board and its key committees, including those for auditing, nomination and remuneration (*ibid.*,V.E). Finally, although the tone of article III on the role of stakeholders is tolerant of national differences, it certainly does not advocate their inclusion in mechanisms of corporate governance. In this way, the code is consistent with the Anglo-Saxon view that the interests of stakeholders are best protected through contractual and regulatory mechanisms rather than through direct representation (Hansmann and Kraakman 2000).

Groups such as the ICGN were quick to emphasize these elements of the code. ICGN argued that it 'reflects perspectives promoted by ICGN representatives serving on the OECD's Ad Hoc Task Force on Corporate Governance, relying on the draft principles under discussion at the ICGN.'[53] However, ICGN lamented the generality of the OECD code and provided its own 'working kit statement' interpretation. The first sentence of this interpretation states that 'the overriding objective of the corporation should be to optimize over time the returns to its shareholders.' In addition, 'to be effective, corporate governance practices should focus board attention on optimizing over time the returns to shareholders with a view to excel in comparison with the company's equity sector peer group.'[54] The ICGN's own preamble omits any reference to the standard OECD qualification that there is no one-size-fits-all model. Given the interpretation of the code offered by such groups, the 'Anglo-Saxon' view of corporate governance was arguably in the ascendancy.

As noted above, notable failures of corporate governance in East Asia and the apparent success of the US model contributed to this emerging ascendancy. This was not only true abroad, but also in countries like Korea and Japan themselves. The clear failures of corporate governance before and after the crisis in countries like Korea had shifted public opinion there substantially against the old system, which had strengthened family owner-managers of chaebols at the expense not only of shareholders but of other

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[53] ICGN, 'Statement on the OECD Principles', available at: http://www.icgn.org/documents/globalcorpgov.htm, accessed 21 January 2002.
[54] *Ibid*.

stakeholders as well.[55] In addition to committing itself to corporate governance reform at the beginning of the crisis, Korea obtained a World Bank loan in 1999 to fund a foreign consultancy report on reforming the country's corporate governance framework. The report, written by the US corporate governance expert Stanley Black, argued strongly for a shift towards a US-style system of corporate governance in Korea. By then, reformers within the bureaucracy and the ruling party saw corporate governance reform as a means of reducing the excessive power of family-run chaebols.[56]

Even in Japan, opinion was shifting. The Japan Corporate Governance Forum (JCGF) was established in 1994 in the aftermath of a series of corporate failures. It was predominantly made up of major company chairmen and some academics. An interim report on corporate governance principles was published in 1997, and a final report in May 1998 (JCGF 1998). This appeared just after CalPERS published (in April 1998) its own Principles of Corporate Governance for Japan, which recommended that JCGF's Interim Report should be adopted as a benchmark for Japanese corporations. The JCGF report strongly favoured the shareholder sovereignty approach, underlining the self-critical tone of the reform debate under way in Japan. The first principle (1A) stated that the 'board of directors should require that the top management of the company be fully accountable to shareholders as well as the board of directors through provision of accurate, substantive, practical and reliable information.' (JCGF 1998). Other standard Anglo-Saxon style recommendations followed. Indeed, there is less in the JCGF principles regarding stakeholder rights than in the OECD principles.

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[55] On Korean corporate governance failures, see Capulong et al. 2000, Claessens et al. 1999a and 1999b, Department of Foreign Affairs and Trade (Australia) 2002, Jang 2001.
[56] Author interview, senior Ministry of Finance and the Economy official, Seoul, Korea, 20 September 2000.

For the two main Asian countries in the OECD, reformers were accepting the need for a basic reorientation of corporate governance practices in their domestic economies. Thus, they were less willing to agree with both the continental European and domestic Korean and Japanese opponents of the shareholder sovereignty approach.

4. CONCLUSION: IDEAS AND INTERESTS

I have argued that the earlier conventional wisdom on the East Asian model was reversed not simply by the crisis, but by a combination of crisis with a broader set of conventional wisdoms in the late 1990s. The view that regulatory agencies should be politically independent and ensure the application of strict rules was ascendant before the crisis struck, as was the apparent triumph of the American model of capitalism. While both of these were also reinforced by the crisis, they were not produced by it. Most importantly, they helped to facilitate the political triumph of a particular diagnosis of the origins of the Asian crisis that might not otherwise have won the day. The US experience of the late 1980s and its remedy (the 1991 FDIC Act) in particular helped to shape the official diagnosis and solution to Asia's problems.

The KKN diagnosis won the day not only in Washington, London and Frankfurt, but also in key circles in Bangkok, Seoul, Singapore and, eventually, Jakarta too. Even if the diagnosis was not fully accepted by the Mahathir government in Kuala Lumpur, there was a surprising degree of support for the associated policy solution there as well. It is simply wrong to suppose that the US and the IMF imposed both the diagnosis and the policy solution on the Asian countries via the stick of policy conditionality. In fact, as we have seen, the IMF found itself working with East Asian technocrats who already had their own, similar, views about appropriate institutional reform.

Nor have the reforming Asian governments adopted the trappings of western-style institutional reform simply because they felt compelled to do so by international capital markets. The sources of the policy shift that occurred go much deeper than this: the crisis was an opportunity for technocrats and their political allies to achieve fundamental political and economic change in their countries. In both Korea and Indonesia in the year before the crisis, there were attempts to encourage governments to close chronically weak banks. Only after the crisis, however, did the political ground shift in favour of those forces arguing for western-style regulatory reform. Nor does all this work necessarily in the interests of global capital (Soederberg 2003); democracy activists in many Asian countries have, for example, shared much of the pro-transparency, independent agency and rule-enhancement agenda.[57] The institutional reform programme was in this sense made more in Seoul and Bangkok than in Washington D.C. and New York.

The argument suggests that conventional ideas mattered in the interpretation of the Asian crisis because they helped to define the nature of the crisis and to map out its remedies. As Mark Blyth (2002) has argued, ideas can in this respect be powerful weapons in the policy debate that follows economic crises. Furthermore, although these ideas suited some powerful material interests (such as the US government and financial sector), they certainly did not suit powerful material interests in Asia itself (notably the often heavily indebted family firms that dominate most of the region's political economies). The KKN diagnosis and the governance reform solution forced these *status quo* interests onto the defensive: after all, what was once portrayed as an efficient 'iron

[57] For various reformist essays on cronyism, corruption and weak prudential supervision in Indonesia, see Holloway 2002.

triangle' between government, business and banks could easily (and often justly) be recast as corrupt and inefficient.

Of course, this does not ensure victory for reform, since opposing interests may regroup and block reform at the stage of implementation, even if they find it difficult to oppose the broad critique. This is especially true in Thailand and Indonesia, where implementation has been very limited.[58] Even in Korea, where the government has dropped its previous adherence to the Japanese line on many aspects of regulation to become a cheerleader for Anglo-Saxon style regulatory governance, public and private sector behaviour remains very different to that, say, in the US. This in turn suggests that even when a particular set of policy ideas become entrenched at the very top of countries' political systems and when an array of international institutions and market actors support their application, powerful domestic interests may still be able to conduct rearguard actions that substantially reduce their practical importance.[59] 'Ownership' of reforms, today the standard mantra of the IFIs, may only be skin-deep. Over time, the domestic political struggle between reformers and *status quo* interests will be decisive. For the moment, ideas have helped to undermine the legitimacy of the old 'Asian model' but the patient still shows signs of life.

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[58] See Walter (forthcoming).
[59] This may cast doubt upon the general applicability of the periodization model offered by Blyth (see 2002: 35) concerning the way in which dominant ideas subsequently promote the emergence of a new behavioural equilibrium.

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