New Approaches to Building Markets in Asia

Working Paper Series

Mike W Dowdle

The Delusions of Agency: How Markets Build Regulation More than the Other Way Around

WORKING PAPER No. 36

New Approaches to Building Markets in Asia is a research project run out of the Centre on Asia and Globalisation at the Lee Kuan Yew School of Public Policy, National University of Singapore.

The New Approaches to Building Markets in Asia Working Paper series presents draft papers originally delivered at each of the research project's three workshops. The series serves as an opportunity for project participants to present work in progress for the purpose of gaining feedback and refining the contributions for peer reviewed publication.

The papers have not undergone peer review. Subsequently, all of the papers should be treated as 'not for citation' unless the consent of the author is obtained. Further, the views expressed in the papers are those of the respective authors and should in no way be construed as those of the Centre on Asia and Globalisation, the Lee Kuan Yew School of Public Policy or the National University of Singapore.

For more information on New Approaches to Building Markets in Asia please visit the project's website at:

http://www.caglkyschool.com/content/new-approach-building-markets-asia

The Delusions of Agency: How Markets Build Regulation More than the Other Way Around

Michael W. Dowdle[1]

ABSTRACT: *An investigation into "new approaches to building markets in Asia" provokes a number of presumptions. "Building markets" is closely associated with the idea of "development". And "building" implies a process of human agency. This implies, consistent with much of the developmental literature, that development itself is primarily a product of human agency. A subtitular focus on "regulation" suggests that these markets are being constructed in significant part by strategic deployment of particular regulatory structures. So building markets in the context of regulation suggests that we can use particular regulatory institutions to foster development.*

This paper seeks to show that in fact, regulation does not work to build markets. Rather, its markets that shape regulation. In particular, this paper argues (1) that a particular polity's industrial-economic structures, including much of its developmental capacity, is strongly shaped and constrained by transnational, geographically factors that operate beyond the reach of strategic human agency; (2) the kinds of markets these transnational geographic factors generate significantly effects what kinds of regulatory structures can function and survive in that particular market environment; (3) that significant aspect of the building of markets, of their regulatory predicates, and even of "development" per se, therefore lie beyond the reach of human agency, particularly insofar as the lesser-developed parts of the world (what we will call "the periphery") are concerned; and (4) that particular regulatory structures that seem dysfunctional from the perspective of developed economies can actually be functional from the perspective of the special conditions of peripheral economies.

On the relationship between regulation and development

An investigation into "new approaches to building markets in Asia" provokes a number of presumptions. "Building markets" is closely associated with the idea of "development".[2] And "building" implies a process of human agency. This implies, consistent with much of the developmental literature, that development itself is primarily a product of human agency. A sub-titular focus on "regulation" suggests that these markets are being constructed in significant part by strategic deployment of

[1] Michael W. Dowdle is an Assistant Professor at the Faculty of Law, National University of Singapore.

[2] For the purposes of this paper, economic "development" refers to a process by which a local economy is able to push itself up the value chain so as to generate a standard of living, quality of life, and general social-political-economic environment and that increasingly resembles that found in the advanced industrialised countries of the North Atlantic. See, e.g., [REFERENCES MISSING]

particular regulatory structures. So building markets in the context of regulation suggests that we can use particular regulatory institutions to foster development.

Such a conclusion is endemic to the literature on economic and political development. It is a core component of the international developmental community. The World Bank, the IMF, and the mass of scholarship they commission and otherwise generate are all premised on a presumption that development is overwhelmingly a product of "getting the [regulatory] institutions right", and that getting these institutions right is itself a product of human agency. The principal focus of this literature is on identifying what these institutions are, and how they can be introduced into needy environments. Such a focus dominates political development initiatives as well, although the focus is more on institutions associated with liberal governance rather than institutions associated with neo-liberal economies.

This paper seeks to show that in fact, regulation does not work to build or "structure" markets. Rather, it is markets that shape, and in many cases even constrain, regulation. In particular, this paper argues (1) that a particular polity's industrial-economic structures, including much of its developmental capacity, is often strongly shaped, and even constrained, by transnational, geographically factors that operate beyond the reach of strategic human agency; (2) the kinds of markets these transnational geographic factors shape significantly affects what kinds of regulatory structures can function and survive in that particular market environment; and (3) that significant aspects of the building of markets, of their regulatory predicates, and even of "development" per se, actually lie beyond the reach of human agency, particularly insofar as the lesser-developed parts of the world (what we will call "the periphery") are concerned.

The paper is organised as follows: The next part of the paper, Part II, will introduce the reader to the various ways that natural and human geography affect local socio-economic conditions. These include not simply the physical geographic factors as famously explored recently by Jared Diamond, and later by Jeffrey Sachs (working with a variety of others) and which have consumed the lion's share of the development community's recent attention to geography (but which are actually of little independent relevance to this paper's particular focus), but even more significantly, paradoxically less recognised factors such as transportation costs, agglomeration effects, and cultural affinities. As we will see, these factors affect a variety of social variables, including capacity for wealth (surplus value) generation, social and economic stability, and economic autonomy.

In Part III, this paper then explores how these different socio-economic factors that economic geography imposes on peripheral social locales affects how regulation works in these locales. We will see, in particular, that it requires these locales to adopt regulatory structures that are more relational, less specialised and professionalised, more pluralist, less autonomous, and less reliant on the maintenance of a strict regulatory between public and private than those associated with more advanced industrial locales. We will then, in Part IV, use the example of "neo-patrimonialism" to show how understanding this distinctive "regulatory logic" of the periphery allows us to see how particular regulatory structures that are commonly dismissed as dysfunctional by the developmental literature can actually be affirmatively functional.

The spatial dimensions of economic ordering

In this part, we explore the transnational forces that affect domestic economic environments (markets).Our starting point is the distinctive geographical patterning of economic development, in which development centres in a small core geography and the further out one goes from this core, the less developed the economic system. This is the core-periphery gradient. We then explore what causes this gradient. These include, most prominently, transportation costs. But agglomeration effects and cultural biases also play a part. In recent times, the core-periphery gradient has been further exacerbated by the disaggregation of production. We will then conclude by examining the macro effect these factors have on peripheral economic systems. We will see in particular, that they inhibit capacity for sustainable wealth generation, they destabilise the socio-economic environment, and they inhibit capacity to support more complex forms of industrial and social structuring.

Economic geography and the core-periphery gradient

The relationship between geography and economic development has been recognised for over a century. It emerged out of studies done by a 19th century German agrarian economist named Johann Heinrich von Thünen (1783-1850). Von Thünen noticed that economic – industrial activity in Germany tended to evince a common geographical pattern. This was a bulls-eye pattern in which the centre, or core, was occupied by an urban centre, with concentric rings of different kinds of agricultural activities – which today are referred to as "Von Thünen rings" – arraying themselves around this core. Thus, immediately outside the urban core one would encounter a concentric zone dominated by dairy and perishable, high-value crop (e.g., fruit and vegetable) production. Further out, agricultural activating would come to be dominated by timber production. Further out still, one would encounter a zone dominated by grain and other lower-value, field crop production. And furthest from the city would be a concentric zone focusing on live-stock production.

Von Thünen's model was originally developed to explain patterns in local agricultural production. Some 150 years later, the seminal French economic historian Fernand Braudel found that a similar spatial patterning of economic activities could be seen operating at the transnational level. Looking primarily at the long-term economic history of Western Europe from ca. 1400-1800, he found that the economic activity of that world-region was consistently arranged in distinctive concentric zones similar to those identified by von Thünen in the context of local rural agriculture. Braudel partitioned this large-scale geography into three general "zones": "a narrow *core*, a fairly developed middle zone and a vast *periphery"* [emphasis in original][3], in which:

> The centre or core contains everything that is most advanced and diversified. The next zone possesses only some of these benefits, although it has some share in them: it is the "runner-up" zone. The huge periphery, with its scattered populations, represents on the contrary backwardness, archaism, and exploitation by others.[4]

[3] Braudel 39
[4] Braudel 39

Moreover, Braudel also showed that this particular patterning was not unique to Europe, but could also be clearly seen the Middle East, in Southeast Asia, in China and East Asia, among other places.

In the 1990s, Braudel's geographic patterning was given econometric foundation in a famous study produced by Paul Krugman and Anthony Venebles. They showed, *inter alia*, that core-periphery patterning of the kind described by von Thünen and Braudel could be wholly explained simply by the presence of transportation costs (see below). They also showed that von Thünen's agrarian model also applies to manufacturing economies.[5]

---

[5] See also Fujita, Krugman and Venables 1999.

By contrast, developmental organisations, and mainstream developmental scholars, particularly in the United States, have historically been sceptical of possible geographical influences on economic development. Within the international development communities however, the idea of geographical determinants to development had historically been peremptorily dismissed as mere recitations of then discredited dependency theory. Like the theories discussed above, dependency theory proceeds from the observation that the global economy is lumpy, with a few wealthy industrialised regions contrasted against vast regions of relatively poor countries. Dependency theory attributes this lumpiness to particular dynamics within the global financial and trade system which are said to work to surriptiously transfer wealth out of the developing world into the wealthy economies of the North. No such mechanisms were ever identified. Moreover, many associated dependency theory with a particular strategy of development called import substitution, which advises that economic development could be stimulated by having underdeveloped countries remove themselves from the international trading system, thereby severing the regressive transnational wealth transfers posited by dependency theory. In fact, import substitution did not work to promote development. Quite the opposite: import substitution was most famously associated with the developmental policies of Latin American countries during the 1960s and 1970s, and many neo-liberal economists in particular blamed it for the "lost decade" that Latin American experiences in the 1980s following the oil crisis and resulting world economic recession of the late 1970s.

The problem with this pro forma dismissal is two-fold. First, it could neither deny nor explain the fact that economic development is so starkly geographically ordered. Second, there is no inevitable relationship between the geographical-economic observations of von Thünen and Braudel, and the theoretical explication of these observations by Krugman and Venables on the one hand, and dependency theory and / or import substitution strategies on the other. In fact, the theories advanced by these scholars, which attributed geographical economic orderings to transportation costs from consumer centres, do not support a claim that transnational trade generate wealth transfers from peripheral to core economies. They do not claim that one can escape geographical influences by simply severing oneself off from the global economy. In fact, they argue just the opposite: being the product of transportation costs, the geographical ordering is inevitable.

By the late 1990s, however, theoretical support for the relationship between development and geography become impossible even for the international development community to ignore. Catalytic to this was the publication in 1997 of an international best-selling book by Jared Diamond entitled *Germs, Guns and Steel*. In contrast to the studies by von Thünen, Braudel, and Krugman and Venebles discussed above, who were interested at the relative geography of Thünen, Diamond was interested in the absolute geography that located advanced economic development primarily in temperate regions and relative underdevelopment in more tropical geographies, and which he attributed to a variety of human-evolutionary factors (such as the fact that most human food comes from temperate regions of the world). Diamond's work attracted the attention of the very influential American development economist Jeffrey Sachs, the intellectual architect of the economic restructuring strategies of Eastern Europe and the countries of the former Soviet Union. In collaboration with a number of other authors (including Diamond himself), Sachs produced numerous statistical studies showing that that "levels of per capita income, economic growth, and other economic and demographic dimensions are strongly correlated with key geographical and ecological variables, such as climate zone, disease ecology, and distance from the coast." (Sachs 2003.See also Gallup, Sachs, and Mellinger, 1998, 2000; Gallup and Sachs, 2001; Sachs and Malaney, 2002.)

Between the two, the popularity of Diamond and the prestige of Sachs made the linkage of development and geography impossible for both the international development community and the

Factors underlying the core-periphery gradient

As noted above, geographers have identified a number of factors that contribute to core-periphery ordering that continue to escape the attentions of the developmental community. These include not simply transportation costs as per von Thünen, Braudel, and Krugman and Venebles, but also physical geography (as per the more recent work of Sachs and Diamond), agglomeration effects, cultural affinities, and the dynamics of comparative vs. absolute advantage – particularly as they relate to the disaggregation of production (aka production chains). We shall examine each in turn.

1. Ecology and physical geography

Interestingly, the ecological and physical geographic variables most famously explored by Jeffrey Sachs and Jared Diamond, are actually the least relevant to this paper's own particular investigations. Inter alia, these studies find that "levels of per capita income, economic growth, and other economic and demographic dimensions are strongly correlated with key geographical and ecological variables, such as climate zone, disease ecology, and distance from the coast." (Sachs 2003. See also Gallup, Sachs, and Mellinger, 1998, 2000; Gallup and Sachs, 2001; Sachs and Malaney, 2002.) For example, Gallup, Sachs, and Mellinger (1998: 11) find:

- That tropical regions are significantly less developed than temperate regions, probably, they hypothesise, because of "higher disease burdens and limitations on agricultural productivity." This is likely due in some significant part to the fact that, as famously argued by Jared Diamond (1997), industrial and societal innovation has long been shaped primarily by needs and resources particular to temperate latitudes. (See also Diamond 2000)
- That coastal regions and regions fed by ocean-navigable waterways are significantly more developed than more fully landlocked economic regions. This is likely due to the fact that trans-regional trade is an important contributor to local economic prosperity, and location on ocean-navigable waterways facilitates such trade.

(largely American) developmental scholarship that fed that community to ignore. Through the earlier part of the 2000s, studies began to appear first refuting the Diamond-Sachs argument, and later seeking to re-locate a developmental role for institutions within that argument. And by the end of the 2000s, a truce had been declared. The developmental community now recognises the geographical implications of development, but it also claims to be able to surmount these implications, and thereby re-establish the ultimately relevant of strategically designed institutions.

Whether this has actually solved the conundrum of developmental geography insofar as its particular foci are concerned is debatable. But even more problematic, the developmental community's recognition of the diversity of geographical predicates affecting development remains highly impoverished. Developmental studies have focused their new-found geographical interests precisely on those particular geographical dynamics that seem vulnerable to strategic institutional intervention. In doing so, it continues to ignore much more profound macro-geographical forces, like transportation costs, whose effect on development are actually likely to be much more determinative – and much more resistant to institutional manipulation – than those that have heretofore been granted recognition by this community.

- That high population density contributes to economic development in coastal economies, but actually appears to inhibit economic development in landlocked economies. This may be due to the fact that the greater global economic integration of coastal economies allows greater population density to trigger particular kinds of "agglomeration effects" that lead to more favourable kinds of trade (see below), whereas the greater economic isolation of landlocked regions in coastal regions impedes the development of such trade-promoting agglomeration effects.

The relevance of these particular factors to the core-periphery patterning described above (which is found in wholly temperate regions as well as in tropical regions) would appear to be slight, however. Most of the economic consequences that Sachs et al. identify in the context of physical-geographical differences – lesser wealth, location on transportation networks that facilitate trade, population density – can also be accounted for by focusing on other variables explored below; transportation costs insofar as location in trade networks is concerned; and agglomeration effects insofar as effects of population density are concerned. This is not to deny the veracity of these ecological factors. But for the most part, they will not be necessary for the development of the particular observations presented in this article. It is included here for the sake of completeness.

2. Transportation costs

The studies by Sachs et al. discussed immediately above look at the relationship between economic performance and physical, or absolute, geography—i.e., the particular location on the Earth's globe that the economic region finds itself in. But economic performance is also significantly affected by particular factors involving "relative geography"—by how a particular economic region is situated relative to other economic regions. Perhaps the most well-studied of these factors involves transportation costs.

As noted above, it has been well shown how simple transportation costs, in and of themselves, can generate the distinctive, concentric core-peripheral geographical patterning common to regional economic ordering. The germinal demonstration of this is found in the iconic 19th century study of the economic geography of rural German written by Johann von Thünen, (1966; original, 1826), entitled *Der isolierte Staat [The isolated state]*. Thünen sought to explain why agricultural production tended to arrange itself in a particular pattern around the urban centre that constituted the principal source of market demand for that region's agricultural product.

The key to this ordering, von Thünen demonstrated, lays in the interaction between transportation costs and land prices. Urban centres will be centres of consumption. Everything else being equal, transportation costs will decrease the closer a producer of consumer goods is located to that urban centre. This means that, again everything else being equal, a producer of some particular commodity that is located closer to that centre will reap higher profits than some other producer of the same commodity who is located further away. This will increase demand for such land, which means that land prices will also be higher the closer one is to a consuming centre. And since land prices closer to the centre are higher, this will push industries that yield less revenue per acre further away from the consuming region.

It is important to note that this industrial gradient is based on revenue generation and not necessarily profit generation. It is not necessary that more interior industries generate more profit than more peripheral industries, simply that they generate more revenue so that they can pay the higher land costs. Of course, profit generation also has its effects on location. Within a particular industry, a more profitable firm will be able to locate marginally closer to the consumer centre. But this effect seems to be marginal. Even with these profit variations, von Thunen rings are invariably industry specific, meaning that at the larger scale, it is the kind of industry, much more so than the level of profit generation, that locates one within the core-periphery gradient.

The higher land costs effect other markets as well: stores have to charge more for their good to cover their higher land costs. Higher land costs and costs of living mean that more interior firms have to pay their workers more (to the extent that those workers have to live where the firm is located). This, in turn, causes more interior industries to favour smaller, more highly skilled workforces. It creates greater demand and competition for highly skilled labour, while again pushing industries that are more labour intensive and that rely on more unskilled labour farther out into the periphery.

Our cursory analysis of the economic-spatial effects of transportation-cost allows us to begin flushing out the particular features and dynamics that distinguish the core end of the core-periphery gradient from its peripheral end. The first of these is that core regions have more innate, indigenous wealth. This wealth is to a significant extent non-transferable outside the region – it exists in geographic-specific features such as property values and quality of the local labour force. But it can, of course, be transferred to other actors within the core: it can serve as a basis for wealth redistribution. So, the greater wealth of the core translates into a larger public fisc.

Core economies will be relatively more consumption and consumer oriented. Indeed, it is precisely this consumption orientation that generates the core-peripheral patterning. Peripheral economies, by contrast, will be more oriented towards production, and in particular towards production for export.

Core regions will also be characterised by an emphasis on capital intensive rather than labour intensive production. Its workforce will tend to feature a greater proportion of highly-skilled workers. Its production technologies will tend to be more technologically advanced and more complex. Innovation will thus focus on technological improvement. As we shall see below in our discussion of agglomeration effects, this environmental emphasis on more complex production technologies also results in a more diverse economy.

More peripheral regions, by contrast, will support much lower levels of public wealth. Both nominal wages and firm revenues will be lower, which means less access to the more technologically advanced products produced by the core. Hence, there will be lower standards of living and less use of more advanced production technologies. These economies will also tend to be more export oriented. For this reason, their socio-economic environments will be less autonomous and more sensitive to external factors.

3. Agglomeration effects

Somewhat related to transportation costs is the phenomenon that Michael Storper has termed “agglomeration effects”. As noted above, core economies tend to emphasise and focus on more complex forms of production. Because of this complexity, core industries tend to make use of a wider diversity of distinct but synergistic specialisations. Storper’s

famous study of the Hollywood film industry provides a good demonstration of this phenomenon. The success of that industry does not derive simply from the convenient presence of actors, directors and studios. It also depends on a plethora of ancillary synergistic niche industries specializing in things like special effects, the production of props and scenery, film editing, and sound mixing. Local educational institutions also contribute to this agglomeration by providing high-quality, specialised educational programmes in skills particular to the film industry: UCLA, for example, offers degree programs in animation, cinema and media studies, cinematography, "moving image archive studies", producing, production and directing, and screenwriting; across town, the University of Southern California also offers degree programs in animation and digital arts, interactive media, producing, writing, media arts and practice, film criticism, and 'business of entertainment'.

Obviously, there are distinct advantages to concentrating these diverse specialisations within a single locale: it allows for the development of more intimate social and professional networks linking these diverse but synergistic sources of knowledge. This in turn facilitates the development and dissemination of more innovative, more detailed, more robust, and more up-to-date local knowledge about markets, technologies, and production processes relevant to the industry. Storper refers to this particular feature of agglomeration as "untradeable interdependencies," and argues that it results in the locale enjoying an *absolute* as opposed to merely comparative advantage in the industries involved.[6] This advantage accrues not just to production, but also to innovation, thus allowing this absolute advantage to reproduce itself over time.

However, these agglomeration effects are much less likely to occur in the more peripheral economies.[7] As noted above, peripheral economies are much less able to support complex production processes. And because of their comparative emphasis on lowering labour costs, they lack incentives and wealth to develop and retain the more skilled and specialised labour force need to populate a diversity of highly specialised industries. The overall effect of all this is to impede the development of the horizontal linkages across distinct but synergistic specialisations that trigger agglomeration effects.

Agglomeration thus works to lock-in a particular core-periphery structuring by giving core regions not simply a comparative, but an absolute advantage in the more complex, high-value sectors of production in which they specialise. (Curiously, the developmental community, while recently beginning to recognise the geographical implications of agglomeration, continues to presume, without any support, that agglomeration advantages are merely comparative, not absolute.) It also accentuates core-periphery wealth and revenue differentials by allowing regional cores to extract monopoly rents from these particular industries (see also Schumpeter).

Agglomeration effects also offer a possible explanation for the curious finding of Sachs et al., discussed above, that population density correlates positively with

---

[6] Storper, Michael (1997).The Regional World, p. 5, 28.See also Gianmarco I. P. Ottaviano, Diego Puga Agglomeration in the global economy.

[7] See, e.g., José A. Borello, Hernán Morhorlang and Diego Silva Failde, "Agglomeration economies in semi-industrialised countries: Some evidence from Argentina and some general inferences about research and policy in similar countries," paper presented at the Association of American Geographers 2008 Annual Meeting (Boston: April 19, 2008), also available at http://globelics2007.sstu.ru/globelics.nsf/0/AF35A69E7BA8B2E9C32572AF0080FCBA/$File/Agglomeration%20economies%20in%20semi-industrialized%20countries-Borello-et%20al-Argentina-paper-1st%20version.doc (accessed January 31, 2009).

economic performance in core economic regions but negatively with economic performance in peripheral regions. This could be because in core regions, population density is associated with greater economic diversity of specialised skills, and thus facilitates agglomeration. In peripheral regions, by contrast, population density does not result in a corresponding diversification of specialised skills, and thus does not trigger agglomeration. In such environments, higher population works primarily to reduce nominal wages (by increasing supply of unskilled labour), rather than generating additional sources of regional wealth creation.

4. Price vs. product competition

The core-periphery gradient is further aggravated by the Ricardian dynamic of comparative advantage. The phenomenon of agglomeration gives core regions absolute advantage in markets dominated by product competition. This causes peripheral regions to focus on markets dominated by price competition. The overall effect of this symbiosis is to further cause wealth and technology and high value human resources to concentrate in core regions.

Market competition comes in two general forms: price competition, in which market success depends more-or-less exclusively on one's ability to offer particular good or services at lower prices than one's competitors; and product competition, in which market success depends to much more considerable extent on one's ability to offer goods and services of superior design and quality, somewhat independent of price considerations.

Price competition and product competition have different economic effects. One of these involves the distribution of the surplus value of the product. Surplus value is the difference between the cost of production and the value generated by use. If a widget costs two dollars to make but brings its ultimate owner three dollars in revenue, then its surplus value is one dollar. Because price competition causes a product's price to converge with its production cost, it effectively allocates surplus value to the consumer. Product competition, on the other hand, can work to allow the producer to retain the surplus value itself. This is because a product distinguished by a unique design somewhat resembles a monopoly. If people are buying the product based in significant part on its design characteristics at least somewhat irrespective of price, and there are no other competitive products with those particular design characteristics, then the producer can sell above production costs (since there is no competing product at the level of production costs). In such a case, then at least some of the surplus value is able to accrue to the producer rather than to the consumer.

Firms in peripheral economies are much more likely to engage in price competition, since their comparative advantage lies precisely in their lower production costs (lower land rents and lower cost of labour). Due to agglomeration effects and their absolute advantage in knowledge-intensive production, however, firms in core economies are more likely to engage in product competition. Note also in this regards that since the knowledge developed by such firms is often proprietary, the uniqueness in design that that knowledge produces can often persist for a significant period of time.

This asymmetry enhances the ability of core economies to generate and retain wealth vis-à-vis that of peripheral economies. Recall that peripheral economies are innately export oriented. This means that the surplus value of a not-insignificant portion of price-competitive products made in a peripheral economy actually ends up accruing to consumers in core economies. But since core economy exports to peripheral economies are more likely to be product competitive rather than price competitive (the

higher product costs innate to core economies means that price competitive products cannot compete with competing products from peripheral economies if they find themselves in the same market), core economies are able to retain the surplus value of a greater portion of their exports.

5. The disaggregation of industrial production

The core-periphery gradient is further being catalysed by the increasing disaggregation of industrial production into transnational production chains. This occurs when a firm employing a complex production process decides to concentrate its activities primarily on the core routines of that process – those routines which make use of its unique local or proprietary knowledge and special competences – while contracting out other more standardisable production needs to third-party subcontractors. Since complex production processes are a characteristic of firms in core economies, these contracting firms will tend to be located in core economies. They retain in-house control over design, marketing and perhaps assemble–knowledge intensive tasks that are most sensitive to their own proprietary knowledge and internal expertise. They will contract out more standardisable production processes to what are often referred to as "upstream" firms. Because they are more standardised, these contracted out processes will generally be less knowledge-intensive and more labour-intensive, and when that is the case, they will be contracted out to firms that enjoy a comparative advantage in labour-intensive forms of production. As we saw from our discussion above regarding the large-scale spatial effects of transportation costs, these upstream firms will therefore tend to be located in more peripheral economies, where the workforce is less trained but also less expensive.

The result is the formation of what are called production chains.[8] Production chains are disaggregated production process, in which firms in core regions that produce complex, high-value-added products, contract out particular aspects of their production process to upstream suppliers, who may in turn contract out particular aspects of their sub-processes to even more upstream suppliers, *ad infinitum*. Since downstream task will tend to be more knowledge and skill intensive; while more upstream tasks will tend to be more labour intensive, these production chains will tend to flow along core-periphery gradients, in which the more upstream components of production tend to take place in more peripheral regions.

These production chains contribute to core-periphery asymmetries in at least two ways. One is through the creation of asymmetric bargaining relationship. Another is by creating asymmetric allocations of market risk.

- *Asymmetries in bargaining power*

Production chains produce asymmetric bargaining relationship between core and peripheral firms. This occurs because supplier firms tend to be more fungible than core firms. This greater fungibility is due to the fact that peripheral firms make less use of skilled labour, and thus their productive efficiency is less likely to be founded on a set of inputs relatively unique to them. Peripheral firms also tend to be smaller and more

[8] Henry Yeung has correctly pointed out that such 'chains' are perhaps better thought of as 'networks' (see also Dickens et al., 2001).The added insight contributed by the 'network' metaphor is not particularly relevant to my analysis, however, whereas the 'chain' metaphor does help me highlight the point-to-point relationships that feature in this argument.

numerous. Because they are standardised and not particularly skill or knowledge intensive, core firms will often have many subcontractors for a particular aspect of production. On the other hand, the standardised components demanded by a core firm are likely to be in some degree unique to that firm. What this means is that it is easier for a core firm to find a replacement source of upstream supply than it is for an upstream component manufacturer to find an alternative purchaser for its component.

The clearest manifestation of this particular asymmetry is the phenomenon known as ”squeeze”, in which downstream firms can use threat of going elsewhere to pressure upstream firms to reduce operating costs and profits margins to the barest minimum, and upstream firms have no ability to resist or retaliate against such pressures. This power to squeeze is most evident when new supply costs arise that need to be allocated between the upstream and downstream firm. Such costs will tend to be allocated upstream. A good example of this can be seen in the allocation of the costs associated with compliance with new social corporate responsibility (CSR) codes of conduct. Due to consumer and political pressures, downstream brand-name companies in electronics and textiles are increasingly requiring their suppliers to demonstrate conformity with various codes of corporate conduct. Such demonstrations often involve significant monitoring and certification—a new development in the costing of production, since monitoring and compliance cost money. But despite the fact that the political and social pressure for such monitoring and compliance is being directed at downstream firms, the additional costs associated with this monitoring and compliance are to-date invariably being borne wholly by the upstream supplier firms.

Asymmetry in bargaining power is further accentuated by the fact that in industries where substitute downstream purchasers can be found for a particular upstream product, downstream industries can, and do, collude in the setting and distribution of costs much more easily than upstream suppliers. This is because these downstream industries generally consist of fewer but larger firms, and it is therefore much easier for them to organise. And to-date, most standard competition law does not forbid domestic collusion when it is directed against outside suppliers.

- *Asymmetries in market risk allocation*

Asymmetries in bargaining power result in asymmetries in the allocation of market risk. One of the principal advantages of production disaggregation lies in the fact that it allows core firms to reduce its fixed assets and associated fixed costs. Fixed assets and fixed costs impede a firm’s ability to respond to qualitative or quantitative changes in market demand. When demand slackens, fixed assets become idle, but the fixed costs associated with these assets remain the same despite reduction in revenue. If production processes involving significant fixed costs and fixed assets are contacted out, however, then the firm can simply adjust the terms of the contract, ordering more or fewer components in response to changes in market demand, for example.

In this way, production chains push the costs associated with market volatility upward into the more peripheral economies. These include not simply monetary costs (such as we saw above in the case of CSR), but social costs as well. For example, one of the ways that upstream peripheral suppliers adapt to the threat of variability of demand is by employing temporary and casual labour. When demand drops, these firms can simply lay-off or refuse to rehire workers, thus temporarily reducing their labour costs in response to loss of demand. This effectively transfers the costs associated with market volatility onto the workforce, and ultimately onto civil society.

6. Cultural geography

Core-peripheral gradients are further catalysed by the dynamics of global finance. In particular, it makes capital more expensive and more volatile. It also makes the peripheral economy as a whole more volatile. And finally, because peripheral economies are naturally much more dependent on outside sources of capital, it restricts policy autonomy in these countries.

Geography enters into global financial flows through a number of channels. These include "home bias", meaning innate investor preference for investment in local firms and project; cultural and social affinities, meaning investor preference to invest in places who share the investor's culture or whose people are included in the investor's social networks; the greater information asymmetry between core-peripheral investment as compared to core-core investment; the tendency of investors investing in more foreign and alien locales to be more skittish and more prone to herd impulses; and the simple fact that peripheral economies have less access to capital from local sources.

Because of lack of indigenous sources of wealth, peripheral economies are more dependent on international sources of investment capital. Obviously, most of that capital is going to come from core economies, where there is more indigenous wealth. In the context of today's world, a majority of the world's transnational investment capital comes from Anglo-American sources (or Anglo-American controlled sources, such as the World Bank).

Investors have long been known to evince a "home bias". Basically, all things being equal, investor will prefer investments in more local firms and projects over investments in more distant firms and projects. More globally, investors also evince a preference for investing in firms and projects whose larger economic environment resemble that in which the investor herself operates. And they show a preference for investing in firms and projects whose leading personnel circulate in the investors' social networks. These preferences are due at least in part to the fact that location, culture and social networks can be important sources of local information about the quality of the investment. Shared social networks can also be a significant source of enforcement. But there is also evidence that these preferences might also be reinforced somewhat by cultural biases—as evinced, for example, in the fact that social networks are not infrequently exclusory of people from outside the culture of that network.

Since most of the world's investment capital comes from core economic regions, this means that firms operating within these regions have significant greater access and less cost to such capital than firms operating in more peripheral regions. Core-core investment is much more likely to be more local; is much more likely to be intra-cultural; and, because of local proximity, is at least somewhat more like to be embedded within a shared social network.

Of course, core investors do invest in peripheral firms and projects that are outside their locality, outside their culture, and outside their social circles. But the preference structures detailed above mean that core-peripheral finance will evince a different kind of logic and dynamic from core-core finance. And to the extent that these preference structures are significantly fuelled by informational inefficiencies, they will be even further catalysed in the context of core-peripheral investment by the fact that peripheral regions are innately more opaque and less transparent than core regions irrespective of issues of local knowledge, shared culture or embeddedness in shared social networks. This is because the lesser wealth of peripheral economies makes it

more difficult for them to institute and maintain more advance transparency inducing regulatory technologies, since these technologies often involve more complex institutional process and greater reliance on a highly skilled workforce, both of which, as we saw above, are innately problematic for peripheral economies (we will explore this further in the next Part to this article).

A better understanding of how core-periphery finance involves a different logic than core-core finance can be gleaned by looking at the common distinction between "growth-based" (or "growth optimal") and "value-based" investment. Value-based investment looks to the economic fundamentals of the investment (such as the price to earnings ratio). Growth-based investment looks to the market momentum of the investment, i.e., the history of its selling price on the secondary market. Because of the greater information available regarding core investments, core firms and projects will enjoy an absolute advantage in attracting value-based investment. This means that core-peripheral finance will feature a significantly greater emphasis on growth-based investment.

This distinctive emphasis on growth-based investment imparts a particular character to core-peripheral finance. Growth based investment is more risky than value based investment. Since core investments are always going to be perceived as safer than peripheral investments, peripheral investments need to focus on providing higher return, hence increasing risk, but also hence making them attractive to growth-based investment strategies. But increased risk means increased volatility.

This volatility is then accentuated by a number of other factors. First, core investors are aware of the greater volatility of peripheral markets, and they are aware that they lack the local knowledge that might allow them to anticipate market shifts – both good and bad – that might affect growth. For this reason, they evince a greater tendency towards "herd behaviour" – herd behaviour is actually a kind of information pooling strategy – and this makes the rise and fall of market fluctuations more pronounced. Investors will also prefer short-term and more liquid investment to longer-term and more committed investment, so as to allow them maximum flexibility to respond quickly to changes in the market. Finally, transnational capital further accentuates economic volatility in peripheral environments by demanding that global financial transactions be denominated in American dollars, which in turn forces the peripheral borrower rather than the core lender to bear the disruptions caused by fluctuations in global currency markets (McKinnon 2000).

7. A concluding comment on state borders

Finally, we might also note that many of the geographic differentiations described above tend to be aggravated when they play across national borders, and conversely, can be mitigated when they play wholly within countries. Thus Sachs et al., for example, note in their study that landlocked economic region that are located within a similarly or conterminously landlocked country, are generally less economically developed than similarly situated regions that are located in a country that also possesses significant coastal regions as well. Crossing national borders will tend to increase transportation cost and transaction costs, which will have particular negative impact on the wealth-generating capacities of peripheral economies due to their greater reliance on price-based competition.

National borders also delineate geographies of progressive wealth redistribution. This redistribution is in part strategic, as when a central government

uses tax money that is collected predominantly from wealthy regions to fund services offered in more peripheral regions; but there is good reason to suspect that it is largely spontaneous, a product of the distinctive unifying, national-market effect of Fordist industrialisation.

But here, too, the core-periphery distinction becomes relevant, because peripheral countries are less able to capture the wealth-redistributive effects of national inclusiveness. Peripheral countries are less likely to be able to generate unified national markets: they are less industrialised (and hence less able to generate economies of scale), and a greater portion of its sectors that are industrialised will be directed to serving foreign markets rather than domestic markets. State efforts to strategically transfer wealth will be impeded by less developed and pervasive national accounting practices, a less developed banking infrastructure, and the more cash-based nature of the economy. Individual regions will thus have greater incentives to engage in economic protectionism; which the centre will have difficulty preventing due to the less effective enforcement capacity associated with the lesser state funding available to relatively wealth-poor peripheral economies.

For the present day, a classic example of this is China. China's last thirty years of economic growth have been legendary. And its overall economy has industrialised significantly. Nevertheless, China has been unable to generate or construct a unified national market or unified national economy (Bing 1995). Economic growth has overwhelmingly benefited the coastal regions, and it has fed primarily through interactions with international rather than domestic markets. China's landlocked regional economies, by contrast, may actually be less viable now (at least in term of generating employment and social welfare) than they were in 1980. Tax collection, and hence strategic redistribution, is greatly hindered by China's significantly cash-based economy, and by a lack of effective accounting practices and auditing capacities.

Effects and Consequence:

Collectively, the dynamics of economic geography explored above result the core-peripheral gradient manifesting itself along three distinct dimensions. These are (1) capacity for wealth generation; (2) trajectories of innovation and capacity to develop and maintain complex technologies and processes; and (3) capacity for stability and autonomy. We will conclude with an observation as to what this means for the possibilities of "development" in peripheral regions.

1. Wealth effects

The most obvious dimension to the core-periphery gradient is that of wealth. More core regions generate and retain wealth much more easily than the periphery. This is for a number of reasons. Recall that peripheral regions will enjoy comparative advantage vis-à-vis the core in markets dominated by price competition. Price competition benefits consumers: it pushed the price of goods down to the cost of production, and this allows the surplus value of the good – the utility value that is created over the aggregate value of the component materials when the product is assembled – to accrue to consumers. Recall also however, that peripheral economies are more export oriented – this means that the surplus value of their exported product is actually accruing to consumers in core economies. By contrast, core economies enjoy comparative advantage in markets dominated by product competition. Product competition, particularly when it occurs

under the penumbra of an intellectual property right regime, causes the surplus to accrue to the producer (in the form of monopoly "rents"). In this way, even when core products are exported, their surplus value is more likely to remain at their place of production.

Core regions also have better capacity to retain wealth in the core geography due to their innately higher labour costs and land costs. Product competition requires more highly skilled labour, and this raises the cost of that labour. The high wages that result in attracting population, which in turn raises the cost of land, and through that the cost of living. The higher value of labour and the value of land represent geographically specific repositories of wealth (land and labour cannot be removed from the locale).

Note that in noting that more core regions have comparative advantage in collecting wealth (via the capture of surplus value) and retaining wealth (via the higher value of labour and land), I am not claiming that core regions tend to generate higher rates of profit or higher returns on investment; I am not claiming that core regions tend to enjoy higher rates of GDP growth. They don't. (In fact, as we saw above, firms in core regions actually tend to provide less return on investment, which may be another factor contributing to the core's tendency to accumulate wealth vis-à-vis the periphery.) We are here talking simply about the aggregate amounts of wealth that reside in a particular geography, not about the rates of growth found in that economy.

2. Stability and autonomy[9]

The great levels of indigenous wealth enjoyed by the core have several knock-on effects. One is that it buffers the socio-economic environment against external shock. But other factors also contribute to core stability and autonomy. Capital markets are made more volatile in the periphery due to the more pronounced herd behaviour of foreign investors. And since these markets show a greater preference for high-return investment over safe investment relative to more core markets, this encourages local industry to engage in more risky economic projects (since risk correlates with return). Asymmetries in market risk allocation caused by the disaggregation of production also result in greater labour-market sensitivity to changes in international market demand, which in turn converts global market fluctuations into more dynamic domestic fluctuations in the economic vulnerability of the general population.

Relatedly, peripheral economies are less autonomous than core economies. In other words, peripheral economies are more susceptible to factors and developments that lie outside their regulatory reach. This stems from their export orientation under conditions of price competition, their greater dependence on foreign sources of capital, and the relative instability of that capital. Export orientation means that peripheral economies will be more affected by economic downturns in consuming regions.[10] This susceptibility is further catalysed by the universal practice of pricing exports in the currency of the importing core economy. Peripheral currencies tend to be much more susceptible to "attack" by outside traders. They are much more susceptible to somewhat

[9] See Alicia Mullor-Sebastian, "A New Approach to the Relationship between Export instability and Economic Development," *Economic Development and Cultural Change* (vol. 36 (1988): 217-236).

[10] The converse is not true, however. Import orientation per se does not make core region equally susceptible to economic changes in exporting peripheries. This is because the appeals of peripheral products lie in their cost, not their unique design. If economic changes disrupt a particular peripheral economy's capacity to export, core consumers can much more readily find substitute goods from other peripheral economies.

arbitrary swings in the investment mentality of foreign investors brought about by their greater skittishness and correspondingly greater tendency towards herd behaviour.

3. Capacity to develop and maintain complex technologies

Core regions have much greater capacity to develop and maintain complex technologies and production processes. This is due to their naturally more highly-skilled workforce; their ability to develop agglomeration effects; and their comparative advantage in knowledge-intensive production. Note the complex technologies refers not simply to production technologies, but to managerial technologies as well – such as monitoring and auditing routines, or the construction of a more nuanced and responsive and professionalised private regulatory system.

Note also that the periphery's limitation in this regard does not simply make it more difficult for it to develop such systems, it also makes it difficult for it to reproduce, or sustains, these complex technologies if it is able to adapt them from elsewhere. In other words, the periphery's disadvantages in this regard cannot be overcome simply by the transplantation of more complex technologies from more core regions. This is not to suggest that transplantations do not occur, or that they cannot be beneficial to the recipient locality. The geographical limitation does not apply, for example, to technologies of lesser complexity. And even for more complex technologies, a transplant can take root, but it is likely to be significantly altered in the process – simplified and adapted to the lesser wealth and lesser human capital available to peripheral regions.

4. Implications for "development"[11]

One of the more unsettling implications of the spatial geography of development is that it suggests a possibility that for much of the peripheral world, "development" as that notion is commonly conceptualised by the development community is not a realistic option. More particularly, it suggests that a locale's developmental capacity is capped by its location in its larger regional economy. Of course, it is possible for a country to underperform despite its capacity, due for example to particular policy choices (see, e.g., China ca. 1960-1980), or to global disruptions (see, e.g., the effect of Sino-Soviet-American competition on Korea and Southeast Asia during the same time period). And where this has been the case, then a strategic pursuit of development would make sense. But a quick look at the globe, and at the stability and geographic patterning of its levels of development, suggests that most countries are operating at their natural levels of development. And for them, there may actually be little prospect for further development

The developmental community has kind of recognised the strong persistence of developmental stasis, particularly in the middle-income countries of what we are calling intermediate and peripheral economic regions. But the presumption that dominates this community is one of universal development, as this persistence is attributed to what are sometimes called developmental "traps", or the presence of some "low-level" kind of developmental equilibrium that nevertheless imply a possibility of escape to higher developmental levels. But in fact, this persistent stasis could well be due to the country's

[11] "The argument made by Martin and Ottaviano (1996*a*, 1998) and Walz (1996*a*, *b*), that location and the long run rate of growth of the economy cannot be treated independently, also needs to be followed upon.", from Agglomeration in the global economy.

simply having reached its innate developmental capacity (or equilibrium) as determined by its location in cultural-economic space.

The effect of economic geography on regulatory capacity

The social-economic structuring of economic geography can shape regulatory institutions. In this sense, markets "build" regulation perhaps even more than regulation builds markets. Here, we will explore how the distinctive economic conditions of the periphery result in a distinctive regulatory logic. A "regulatory logic" refers to the evolutionary tendencies that particular kinds of environments impart to their regulatory systems. As explored in the first section, the distinctive socio-economic shape of the periphery that we examined above causes some regulatory structures that are functional in more developed, core economic environments to become dysfunctional when transplanted to the periphery, and create more pronounced incentives for other kinds of regulatory strategies that are not typically associated with more core regions. This will be followed by a demonstration of how a better appreciation for both the distinctive economic logic and distinctive regulatory logic of the periphery can provide a more robust appreciation for particular regulatory practices associated with the periphery, in this case that of neo-patrimonialism.

On the "regulatory logic" of the periphery

In this section, we will examine how the distinctive shape that geography imparts to the socio-economic structuring of the periphery can also impart a distinctive shape to its regulatory capabilities. These include an evolutionary pressure for regulatory strategies that have lower administrative costs and are less organisationally complex; an evolutionary preference for relational and networked forms of governance; less regulatory autonomy; less regulatory coherence; and a less clear delineation of the public-private divide.

1. Cost and complexity concerns

Because peripheral economies are much less capable of generating wealth, their choice of regulatory regimes are much more likely to be constrained by administrative cost concerns than those of more core economies. Comparative analyses of peripheral regulation, by contrast, rarely consider administrative costs (but see Braithwaite 2006).

Peripheral regulatory regimes will be less able to support and thus rely upon a highly professionalisation and specialisation workforce. Moreover, more complex regulatory schemes impose corresponding complexity and cost demands on the regulated sector. For example, complex auditing and reporting requirements require firms to have persons specialised in these particular requirements. Complex procedures for collecting public input require civil society organisations to have persons specialised in these procedures. As noted above, because of their innate difficulties in generating wealth, peripheral economies also have greater difficulties generating and retaining more highly trained and professional workforce. It is expensive to train such workers. And such workers are in high demand in wealthier core economies that are able to provide better wages and better standards of living. This impacts the public sector's abilities to implement more complex regulatory regimes. And it impacts the private sector's ability to comply with more complex regulatory regimes.

Some suggest that the greater costs of these more sophisticated regulatory systems will pay for themselves through the increased economic efficiency and growth (Ogus et al., cf. Rodrik et al., 2004). But for reasons explored above, such a presumption is unjustifiable (see also Glaeser et al., 2004). As we saw, peripheral capacity for economic development and growth in local wealth is likely to be constrained by critical exogenous factors that are outside a domestic system's regulatory reach – such as transportation costs and greater innate instability. Along these lines, studies by Randall Peerenboom (2004) suggest that growth-effective regulatory reforms seem to become much more difficult to implement in intermediate-peripherally developing countries such as China and India when they reach mid-range levels of economic development. Peerenboom attributes this primarily to a failure of political will, but it is difficult to see why they should fail here and not earlier in the developmental process. For regions described above, perhaps a better explanation is that middle income countries are likely to have reached the developmental limits imposed by their location in economic-geographical space. This being the case, then they would not be able to compensate for the greater cost of more complex regulation simply through a subsequent growth and development.

2. Relational governance and networked governance

Another regulatory logic characteristic of peripheral environments is a functional tendency towards more relational styles of governance. This tendency is well recognised in the literature, but it is generally regarded as dysfunctional (see, i.e., "crony capitalism"). But in fact, in peripheral economies relational governance enjoys significant advantages vis-à-vis juridified governance, in that it is particularly adapted for the greater volatility and diversity (complexity) characteristic of peripheral regulatory environments.

As we saw above, peripheral regulatory environments are likely to feature greater volatility, and therefore greater unpredictability, than regulatory environments at the core. It is well recognised that because of their focus on long-term, repeat interactions, relational bonds are much more resilient in the face of unforeseen disruptions than are arms-length relationships governed by abstracted, juridified rules. In addition, because of greater internal diversity, peripheral regulatory environments are likely to be more innately opaque and more characterised by informational asymmetries. This is due to a number of factors. One is the problem peripheral governments have developing and retaining independent specialists with local knowledge of regulated sectors and technologies. Another is the periphery's less developed civil society, which in core regulatory systems often serves as another critical source of regulatory information. Here, too, relational governance brings identifiable advantages. As evinced by the experiences of early regulators in the United States for example, relational ties with industry and other social sectors therefore can provide the peripheral regulator with valuable access to critical outside regulatory information that regulators in more wealthy core economies can afford to develop in-house.[12] (In fact, for

[12] Critics of relational government may acknowledge these functionalities, but respond by arguing that juridified regulation is still be preferred because it better promotes economic growth. But there is good reason to doubt this assertion: as described above, in peripheral regions, economic growth is likely to be constrained by a variety of transnational factors that operate independent from the reach of the domestic regulatory system.

these reasons, relational governance is actually frequently found even in advanced industrialised societies, particularly where the regulation involves new and more dynamically evolving technologies, or must oversee more opaque, more remote, and relatively localised environments.)

Closely related to the phenomenon of relational governance is what has sometimes been called "networked governance". Unfortunately, the literature on networked governance at present focuses almost exclusively on networked governance as is works in the context of the advanced industrial economies of the North Atlantic (and in particular that of the EU). Insofar as its application to more peripheral economies are concerned, it is almost non-existent (but see Bronwen Morgan 2006; Braithwaite 2006), although some scholars have recognised that networked governance may be particularly suited for developing countries (Braithwaite 2006, Drahos 2004). One exception to this would be the literature on production chains, which is a kind of networked corporate governance.

3. Effects on regulatory autonomy

The economic geography of the periphery also impedes what we might call regulatory autonomy—meaning the ability of a regulatory decision maker to insulate itself from outside influences. Regulatory autonomy has two dimensions to it: an external dimension that describes the regulator's ability to insulate itself from transnational influences; and an internal dimension, that describes the regulator's ability to insulate itself from internal factors—what is sometimes referred to as politics. Both these dimensions are implicated by economic geography.

- External autonomy

One of the most obvious regulatory effects of economic geography is that it makes domestic regulatory system in more peripheral countries much more sensitive to transnational influences. As we saw above, peripheral economies are innately more export oriented, but while producing more transnationally fungible products, they must rely more heavily on transnational sources of capital. External actors, particularly in the core countries that serve as the periphery's primary source of consumers and credit, can arbitrage this sensitivity into channels for influencing domestic regulatory systems. This is well recognised, and not generally regarded as a particularly bad thing—as least in the developmental community. Both foreign governments and international development agencies, for example, overtly use this sensitivity to impose conditionalities on loans and import agreements that are designed to force the target peripheral country to adopt regulatory practices that are thought to be more conducive to long term development. Indeed, even private transnational influence, particularly to the extent it comes from actors in core economies, is also often regarded as developmentally promotive, with the actors' interests being seen as reflective of the invisible hand of true economic rationality in peripheral environments that otherwise disregard that hand's wisdom.

- Internal autonomy (regulatory independence)

Economic geography not only affects the peripheral regulatory environment's autonomy from external influences, it also affects its autonomy vis-à-vis internal

influences. Our received understanding of the regulatory state tells us that regulators should be "independent" of their regulatory environment—i.e., that they should sit outside and above the internal dynamics – what is often termed "politics" – of the social environment they are charged with regulating. But such logic is also difficult to sustain in more peripheral economies.

Regulatory independence is actually a complex condition to put together. In the context of the United States at the end of the 19th century, it required the melding together into a coherent, technocratic epistemology of four forms of highly technocratic knowledge that had been previously developed by civil society: accounting, public economics, industrial organisation, and an explosion in statutory bases of law. It required an advanced educational and training infrastructure that would allow this new, syncretic knowledge to propagate in the public sphere. It has ultimately required a civil society that was itself sophisticated and experienced enough in these diverse forms of technocratic knowledge to be able to itself use and develop this new syncretic knowledge, and thus freeing it from capture by a particular institution's *ad verecundiam* authority.

In sum, it requires what we identified above as agglomeration effects. But as we saw, agglomeration effects tend to accrue in core regions, they are difficult to develop or maintain in more peripheral economies. Lack of public wealth limits the ability of government to attract, re-train and sustain the diversity of already highly skilled professionals which are necessary to maintain a regulatory capacity that is able to operate independent of industry assistance. As we shall see below, civil society organisations are also likely to be significantly less developed, and significantly less sophisticated in more peripheral economies.

Where they do not, it suggests that the regulatory environment will be less responsive to systemic interventions by human intentionality (since we will have a harder time predicting how the conflicting logics will play out)—and correspondingly more susceptible to what Robert Merton famously termed "the law of unintended consequences".[13]

4. Coherence

Lack of regulatory autonomy also affects the peripheral regulatory environment's capacity to generate and maintain regulatory coherence. The external and internal influences on regulatory autonomy, described above, are themselves the products of the regulatory logics of the particular regulatory environments in which their proponents operate. But where these proponents are more external to the subject regulatory environment, the regulatory logics that their influences reflect will be more often external as well, different from those operating in the domestic regulatory environment itself.

This makes peripheral regulatory environments more likely to embed multiple and inconsistent regulatory logics. To the extent these different logics tend to attach to different groups within that environment, it suggests that the regulatory environment will be less coherent, from a policy perspective, and more sociologically fragmented (see, e.g., Gillespie) than core environments – more resembling what has sometimes

[13] Robert K. Merton, "The Unanticipated Consequences of Purposive Social Action," *American Sociological Review*, Vol 1 Issue 6, Dec 1936, pp. 894–904

been termed "legal pluralism".[14] At the same time, they will be less responsive to more centralising forms of law-based, bureaucratised regulation characteristic of Weberian "rule of law".

Of course, fragmentation and unresponsiveness are well recognised features of peripheral regulatory environments. But as noted above, conventional developmental wisdom attributes these features to endogenous factors within the domestic regulatory environment itself: to a political failure to come together for the common good, in the case of regulatory fragmentation; or to a lack of "political will" in the case of unresponsiveness to developmental strategies. It suggests that these characteristic can therefore be transcended through development and application of proper political will (perhaps as itself catalysed by well-meaning external intentionalities). What our focus on regulatory logic shows is that this is not likely to be the case. The greater fragmentation, incoherence and seeming unresponsiveness of peripheral regulatory systems is the product of regulatory factors that operate far outside the reach of any domestic or transnational political will. They are a natural and innate consequence of the spontaneous orderings of transnational economic space.

5. Less delineation of the public-private divide

Modern capitalist states bifurcate their political-economic environments into distinct public and private sectors, in which the private sector is organised to promote economic growth, and the public sector is organised to promote egalitarian distribution (or redistribution) of goods and services relevant to citizenship. Because of their differing political-economic functionalities, the rules that govern the operations of these two political economies are different. Private economies are driven by principles of competition; public economies are driven by principles of equality.

Because of the different principles driving these two political economies, they can be arbitraged. One gains a competitive advantage in the private economy if one can secure goods and services non-competitively in the public economy, and then use them as inputs for competing in the private economy. Such arbitrage, however, compromises the functionality of both the public and the private economies. It compromises the functionality of the private economy, because fair and full competition – not only in the production of goods but also in the procurement of inputs – is critical to the distributional efficiency of the market. It compromises the public economy, because it diverts public resources that would otherwise provide for the needs and demands of citizenship.

For this reason, modern regulatory systems maintain a strict separation between the public and the private. They do this by having the resources that comprise the public economy be clearly identified as public, and by ensuring that resources that are have been identified as "public" only be used for public-economic purposes. The emergence of this regulatory feat is closely associated with the onset of advanced industrialisation,

[14] Legal pluralism describes a condition in which multiple autonomous legal epistemologies inhabit the same regulatory space. This pluralism may be formally articulated, as is the case with federalism. It may be organised informally, and perhaps surriptiously – as seems to be the case with competition regulation in Vietnam, for example. Because states seem to gain legitimacy from claims of internal coherence, and since peripheral states are weaker vis-à-vis more core state, peripheral legal pluralism will more often be informal rather than formal. From an outside perspective, such informal legal pluralism can be indistinguishable from local protectionism or corruption, since outsiders will lack local knowledge of the regulatory system.

and in particular with managerial capitalism. Industrialisation greatly increased the amount of wealth in society, which in turn allowed government to hire and retain the skilled auditors and accountants necessary to keep track of public resources; and managerial capitalism popularised the use of the more advanced accounting and auditing techniques that would allow them to do suit also catalysed the spread of a national credit-based economy, which made financial transactions and the movement of financial resources much easier to monitor.

Peripheral economies, on the other hand, have difficulty establishing and maintaining the public-private divide, for at least two reasons. First, designating and keeping track of public resources is a highly specialised activity. And as described above, peripheral economies have greater difficultly developing and retaining capacity for more specialised forms of regulation. In addition, one of the biggest problems in monitoring maintaining the public – private divide is that of money. Money, being highly fungible, is particularly difficult to designate and keep track of. In modern economies, the designation and tracking of public monies is greatly facilitated by the development of a credit-based economy, since the circulation of credit leaves a much more robust paper trail. Peripheral economies, by contrast, tend to be significantly more cash-based than credit-based, since credit-based economies are more technologically complex. Compared to credit, cash is more difficult to institutionally segregate, monitor, and keep track of.

The other reason peripheral economies have difficulty maintaining a strict separation between public and private economies involves converting liquid resources (i.e., resources that could be used for either public or private purposes) into more fixed resources (i.e., resources that can only be used for private purposes). As famously described by Oliver Williamson, fixed resources are more expense to retain, and are particularly less functional – and therefore are more expensive to maintain – in more dynamic economic environments. Peripheral economies, as described above, tend to be more dynamic, and at the same time lack the greater levels of wealth necessary to maintain fixed assets.

Peripheral environments are thus more inclined to support regulatory devices that intermingle public and private political-economic functions—corporatism as opposed to agencification, for example, or patronage-based (machine) governance as opposed to an administrative state.[15] We will explore this further in the next section.

Demonstration: rethinking "neopatrimonialism"

In this section, we will explore the regulatory logic of one particular regulatory practice commonly associated with the periphery, that of "neopatrimonialism." Neopatrimonialism describes a form of government that is both bureaucratised (legal-rational) and relational; and in which political elite use public resources to secure personal loyalties from clients and subordinates. It is commonly regarded as a developmental "trap" – a low-level developmental equilibrium that works to impede further progression up the developmental scale. But as examined above, the developmental capacity of peripheral environments is often limited by factors that exceed the reach of the domestic regulatory environment. And we shall see that where this is the case, neopatrimonialism can play a role in peripheral economies that is

[15] *When Federalism Works*, p. 75; see also George Washington Plunkitt. Daniel P. Moynihan, 1976.

functionally similar to the role that agencification theoretically plays in the more advance regulatory states of the North Atlantic.

As noted above, neopatrimonialism describes a form of government that is both bureaucratised (legal-rational) and relational; and in which political elites use public resources to secure personal loyalties from clients and subordinates. In this way, it parallels the particular regulatory logics of the periphery we explored above: namely, relational and network governance; a porous public-private divide; legal pluralism and regulatory incoherence (namely, the intermingling of personalism and legal-rational disciplinary forms – what is sometimes called "institutional hybridity"). The literature on neopatrimonialism also recognises that these governmental attributes are systemic phenomena, that they arise out of and are structurally embedded in the peripheral social environment. To use the vocabulary of this essay, it recognises that neopatrimonialism is a distinctive "regulatory logic" arising out of and in response to its larger regulatory environment.

1. Neopatrimonialism as developmental trap

Because of its systemic persistence, and its pronounced divergences from modern theories of the regulatory state, neopatrimonialism – at least as it is manifest in peripheral societies – is often portrayed as a "developmental trap"—a state of low-level socio-economic equilibrium that prevents lower and middle income countries from further development. This trapping effect is seen as a product of neopatrimonialism close structural affinity with corruption. Simply put, corruption involves the appropriation of public resources for private gain. The attributes associated with neopatrimonialism are all consistent with this definition. This dynamic is rather straightforward in the use of public resources to secure personal political loyalty. Similarly, the intermingling of personalism with legal-rational forms of governance corrupts the public benefits of legal rational ordering by subordinating this ordering to an alternative form of ordering that relocates political power in the private person of the patron rather than in the public institutions of modern governance.

Recognising this linkage, the arguments for the developmental trapping effect of neopatrimonialism stem directly from the standard tropes of developmental economics regarding corruption. The intermingling of the public-private divide both impedes the efficiency of the private market and prevents public resources from serving the public good. The presence of personalism adulterates the predictability that legal-rational governance would otherwise impart to the economic environment, and this impedes economic planning, innovation and expansion. The result is a relatively unpredictable and inefficient market environment preventing further growth and development and which is maintained and promoted by a weak and corrupt political economy, a political economy that is directed primarily to preserving the political power of its political-economic elite rather than to pursing regulatory and economic reforms that are necessary for further economic developments but which threaten the political power bases of this elite.

But there are a number of reasons why we might question this explanation. First, contrary to the presumptions of developmental economics, corruption does not appear to hinder economic growth. Studies have found a clear correspondence between levels of corruption and levels of economic development. But they have found no inverse correspondence between corruption and economic growth. Whatever corruption is

doing to an economic system, it does not appear to be doing what the developmental trap thesis says it is doing in the context of neopatrimonialism.

Second, while corruption is not completely persistent – it can evolve dynamically over time, its evolutions occur at the regional level not at the level of the state. In other words, the best predictor as to whether corruption levels in a particular country are evolving is whether they are evolving in its neighbouring countries. Corruption appears to be a transnational phenomenon, and this inconsistent which an explanation that attributes corruption solely to the domestic (internal) political economy of a country.

And relatedly, as we noted above, there are distinct, persistent transnational patterns to economic development as well. Again, the best predictor of economic development of a particular country or even subregion within a country is the economic development of its neighbouring countries or subregions. This strongly suggests, again, that development is shaped – or at least constrained – by transnational factors. And this is incompatible with a hypothesis that attributes developmental dynamics to a wholly domestic regulatory structure such as neopatrimonialism.

But of course, all of these observations are perfectly consistent with and supportive of our understandings of economic and regulatory geography. The transnational geographical ordering of development is consistent with our understanding that development is capped by transnational transportation costs, transnational cultural affinities with core economic regions, and transnational comparative economic advantages stemming from agglomeration effects, not by domestic political economies.

It might also be noted that the relationship between neopatrimonialism and corruption is not as simplistic and one-to-one as most if not all regulatory critiques make it out to be. Corruption is at the core of the neo-institutional critique of neopatrimonialism—and indeed, is at the core of developmental critique of peripheral (or Southern) governance in general. It is via corruption that neopatrimonialism manifests it trapping character. But in fact, nothing in our definition of neopatrimonialism leads per se to corruption. As noted above, neopatrimonialism simply describes a situation in which political patrons use public resources to secure the person-focused loyalty of political clients. In this sense, it does involve a piercing of the public-private divide. But corruption involves more than simply piercing the public-private divide; it involves a piercing that is also both (1) for private gain and (2) socially unacceptable.

These additional criteria complicate the phenomenon of corruption considerably. Take the first of the two, that the appropriation has to be for private gain. In fact, just about all professional involvement in the public economy has some element of anticipated private gain attached to it. Simply collecting a salary as a public official would technically satisfy this criterion. In addition, a public position often carries with it considerable perks, which are even more important to many than the salary per se. Indeed, in many places, many people enter the public sector because they expect it to give them an advantage later on in gaining elite positions in the private sector. Of course, not of this is considered corrupt, because of the second of these additional criteria, which says that the appropriation of the public to the private must be socially unacceptable. Most of us would not find it socially unacceptable were someone to take public service simply because it offered a better salary and better economic prospects than he or she would enjoy through employment in the private sector.

In other words, corruption is ultimately a social construct. All public service involves some degree of prospect for private gain. Indeed, without prospect of private

gain, it would be impossible to secure public servants. Indeed, it is this prospect of converting the public status and power of public office into private gain later on that allows many modern governments to secure qualified and highly trained civil servants at a discount compared with the private sector. So the question as to whether a particular appropriation is appropriate or not is simply a question of social mores. In the United States, giving money directly to the person of a congressman is corrupt, but giving it to his campaign fund is not. In both cases, the congressman derives personal benefit (cash or employment) because of the public power and prestige associated with his office. But for whatever reason, American society has chosen to perceive the former as unacceptable while regarding the latter as at least minimally tolerable.

But recognising that corruption is ultimately simply a social construct severely complicates the relationship between neopatrimonialism, corruption and development. Of course, there is undoubtedly some corruption which provides no ancillary public benefit. But given the fact that access to opportunities to use public resources to increase private benefit itself would lower the cost of public labour, we have to be very cautious in identifying such extreme forms of corruption. Systemic opportunity for corruption lessens labour costs, in that way along provides some degree of public benefit. The vast majority of corruption is going to be 'mixed' in the sense of providing some degree of both private and public gain. This means that most corruption is primarily a matter of subjective social construction.

All this this makes it highly problematic to associate such subjective corruption with some particular objective or functionalist consequent, such as an objectively inhibited development. Social evaluations of appropriateness are unlikely to reflect the actual costs (or benefits) of the behaviour in question. Moreover, social understandings of what constitutes corruption are often contested, fragmented and evolving even within a particular polity. As we noted above, the modern idea of corruption itself is closely associated with industrialisation, since it was industrialisation that made visible and stabilised social perception of a public-private divide. A given national society will consist of many subsocieties that are more or less industrialised, and in different aspects. Public-private transferences can benefit certain populations at a cost to others.

Thus, to simply note that in a particular polity political patrons divert public resources to secure personal loyalties from clients actually tells us very little about the economic implications of that diversion. It does not translate per se into a development trap. In order to show a development trap, one has to show that this transfer is in fact impeding identifiable socio-economic dynamics that would otherwise be leading to "development" even in the face of that polity's location in transnational socio-economic geography. Few, if any, investigations into or complaints about peripheral corruption come anywhere close to considering such detail.

Of course, impeding development is not the only harmful consequent associated with corruption, and by association, with neopatrimonialism. Corruption – and neopatrimonialism – is also often said to increase inequality and poverty, and lower standards of living and quality of life among the poor and even the middle class.

Corruption also threatens regime legitimacy. But even in this, its implications for neopatrimonialism are complex. Corruption threatens legitimacy by definition – corruption being defined as behaviour that is in part socially unacceptable. But this begs the question as to what causes society to interpret particular behaviours as acceptable or unacceptable. One would suspect, for example, that rapid changes in the socio-economic organisation of society would disrupt settled expectations of what constitutes acceptable behaviour, and by themselves led to a significant increase in perceptions of

corruption. In addition, the disruption of settled routines would disrupt established 'rituals of visibility' – to use Michael Power's phrase. But social-industrial transformation may also represent a social condition that neopatrimonialism is particularly well equipped to regulate, given its comparative advantages in accommodating the social flux, regulatory ambiguity and low public income levels that are likely to accompany such transformations.

A similar observation holds true for societies facing rapid integration into globalised economic and political environments. As with social industrial transformation, this integration often results in significant disruptions of settled patterns of behaviour and social expectations. It disrupts rituals of visibility. And so, it would likely result in significant increases in social perceptions of corruption – i.e., corruption. But again, at the same time, neopatrimonialism would seem to offer comparatively regulatory effectiveness in such an environment: particularly insofar as the less industrialised and less wealthy "developing" countries of the Global South are concerned.

In both these cases, corruption is not so much the product of neopatrimonialism as it is a simply a fellow traveller. And as a fellow traveller, it could often be one that actually makes the trip easier, not more difficult.

2. Neopatrimonialism as agencification

Since in this light, neopatrimonialism per se is not necessarily dysfunctional. Its relational character provides stability and flexibility in environments that are often too innately unstable to support a modern regulatory state. The intermingling of public and private reduces the costs to government of expertise. In this way, neopatrimonialism can be seen as functioning as a peripheral form of agencification—whose value to more advanced regulatory environments is said to lie precisely in its capacity to bring both flexibility and expertise to regulatory decision making.

A good example of the functional equivalence between neopaternalism and agencification is found in the story of international efforts to provide social protections to rural populations in Thailand left vulnerable to the Asian Economic Crisis of the late 1990s (see generally Pasuk and Baker 2000, p. 35-82, 97-104). Many in the international development community had attributed that crisis at least in part to a failure on the part of the affected Asian countries to adopt effective regulatory institutions. This, they argued, had allowed corruption and "cronyism" to corrode the efficiency of these countries' economies and markets. For this reason, when the Asian Development Bank (ADB) and the World Bank set up a program to assist Thailand in implementing social safety networks for persons left vulnerable by this crisis, the "Social Investment Fund" [SIF], they framed that program in rigorously regulatory terms—terms that demanded detailed, rationalised, rule-bound standards for eligibility, project structure, and fiscal monitoring. Such a regulatory framing, it was believed, was necessary to prevent the cronyism and corruption that had allegedly caused that crisis in the first place from corrupting the effectiveness of this project.

In this sense, the SIF was set up as a kind of independent agency within the Thai regulatory environment. It was governed by public international institutions that were not a part of Thailand market environment. This independence was buttressed by deployment of high levels of regulatory expertise, particularly in fiscal monitoring, but also in project development.

But it was also a failure. It was inaugurated in August of 1998. After ten months of operation, the SIF had only been able to disbursed 5% of its available capital. One month later, in July of 1999, the World Bank and ADB suspended the project. The failure of the SIF program was due to the fact that, for the most part, Thailand does not sport the modernised, industrialised form of social organisation presumed by the SIF's regulatory framework. Thailand's economy is dominated by small enterprises and agriculture, rather than large enterprises and manufacturing. Because businesses are small and relational, accounting practices are not especially developed, particularly in the rural areas where almost 70% of the population lives. Industrial labour is primarily migrant and seasonal, rather than permanent (see also Deyo 2000; Pasuk and Baker 2000, p. 82). The result is a highly fragmented, dynamic, diverse and opaque socio-economic environment. Such an environment is simply not conducive to the remote (i.e., centralised), standardised, regulatory processes that the SIF used to identify, reach and monitor appropriate targets for funding (Pasuk and Baker 2000, p. 80-1; cf. Sabel 1994, Scott 1998).

On the other hand, another international social welfare assistance program that had eschewed the classical regulatory organisation, and simply dispersed funds directly and in a pro forma manner to rural leaders, actually proved much more effective in reaching Thailand's rural populations. This was the "Miyazawa Scheme" that Japan set up in late 1998. In stark contrast to the SIF, the Miyazawa Scheme "abandoned all pretence of careful targeting [and] elaborates bureaucratic procedures," and "disbursed funds through local government bodies" (Pasuk and Baker 2000, p. 81). These local governmental bodies were chosen due to their relationship with Japanese firms doing business in the region.

And in fact, the Scheme was in fact much more effective in getting needed support to local rural populations than the SIF. Like the SIF program, the Miyazawa Scheme was given an annual budget of around 10 billion Baht. But whereas the SIF was only able to disburse some 5% of its funds in the nine months of its operation, the Miyazawa Scheme successfully disbursed almost all of its funds within the same time frame (Pasuk and Baker 2000, p. 81). Perhaps even more interesting is the fact that follow-up studies found little corruption in the administration of these programs, or in the disbursement or use of funds, particularly in rural areas (United Nations Economic and Social Commission for Asia and the Pacific 2001, p. 57-108).

In other words, instead of eschewing the neopatrimonial governance structures of rural Thailand, the Miyazawa Scheme chose to work through these structures. For this it was vigorously criticised by the World Bank and others in the developmental community. But there is good reason to suspect that it was precisely in its neopatrimonial arrangements that the relative success of the Miyazawa Scheme lay. Its reliance on private economic relationships to identify and discipline local agents allowed it to secure expertise in targeting local social-political environments that the more regulatory structures of the SIF caused it to miss. Rural environments in Thailand lack capacity to fund and maintain independent public and NGO regulatory structures. Monitoring expertise is therefore highly tied up with the private sector. Neopatrimonialism was essential for giving the Miyazawa Scheme access to this necessary expertise.

Nor is this unique to Thailand. In fact, other examples in which neopatrimonial arrangements proved effective surrogates for regulatory governance in environments that could not support such kinds of governance can be found in pre-industrial United States. The regulatory state is a product of industrialisation, and as the experience of the

SIF shows, has difficulty being effective in non-industrial environments. The onset of industrialisation in the latter part of the 19th century created a need for modern regulation, in the form of national markets and social capacities, without necessarily providing the means for achieving that regulation, in the form of higher levels of public revenue and public expertise. This resulted in what became known as The Gilded Era, an explosion in neopatrimonialist forms of governance most famously characterised by machine style governance in the context of large municipalities. Subsequent studies have found, however, that these frequently maligned structures in fact were relatively effective in delivering public goods to target populations (see also the Civil War pensions schemes). Nor were they developmental traps. Driven by the invention of new monitoring and disciplining technologies (what Alfred Chandler famously identified as ”managerial capitalism”), the United States would soon emerge as a core industrial economy, and in the process subsequently inventing the independent regulatory agency and, through that, regulatory state.

In this sense, both neopatrimonialism and the regulatory state that would succeed it were much more examples of market-built regulation rather than of regulation building or impeding markets.

Conclusion: rethinking the periphery

Recognising the different regulatory logics that may often be operating in peripheral economies gives us a new perspective of how “regulation” is likely to work in the Global South. “Law and development”, the dominant lens through which we approach such issues, presumes, in both its analyses and prescriptions, that the regulatory capacities of peripheral economies are innately unconstrained. Peripheral deviations from more the growth-maximising or justice-maximising practices of the industrialised north are simply dismissed as bad regulation. This effectively makes the perfect enemy of the good: it causes us to ”require” (be it through grant conditionality or via intellectual/moral censure) that peripheral, developing regions continually strive for an unattainable and possibly dysfunctional regulatory perfection at the price of actually attainable, ”best-second” regulatory solutions. An understanding of the distinct regulatory logics operating in the Global South not only allows us to recognise the occasionally superior functionality of such best-second solutions, it also allows us to explore what such solutions might actually entail. It allows us to begin distinguishing truly suboptimal regulation from regulation what is simply reflexive of the innately non-optimising economic capacities of the periphery.

Moreover, and more importantly, it allows “regulatory theory” to begin entering into a meaningful dialogue with the Global South: a dialogue in which the South is recognised as a distinct source of positive regulatory knowledge. We might note, along these lines, that the economic structuring’s’ characteristic of peripheral regions are not unique to the periphery. As post-Fordism proceeds to dismantle the centralising and rationalising tendencies of industrialisation, conditions of ”peripherality” – such as increasing resort to numerical flex – are increasingly appearing even within the core nations of the industrial North. Who knows? — the South might just have a thing or two to teach us about ”regulation” as well.