

Chapter 9

Does Institutional Diversity Affect Firms' Innovative Activities in Asian Economies? An Institutional Approach to Innovation

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ABSTRACT

This chapter looks to contribute to the recent literature on institutional comparative analyses of Asian economies; it makes three distinct contributions. First, we investigate the institutional diversity of Asian economies by using multivariate methods, and show five different groups within Asian economies that can be distinguished from advanced economies. Second, based on firm-level data, we determine whether institutional environments have a favorable effect on the innovation activities of firms; concurrently, we discuss whether or not joining a global supply chain induces firms to engage in innovation activities. Our analytical results show that institutional characteristics have a positive effect on firms' decisions to engage in those activities, and that institutional configurations provide the foundation for a global supply chain built in East Asian economies. Third, we emphasize that the current institutional diversity can persist, given the positive interaction between the institutional diversity of Asian economies and the innovation activities of Asian firms.

1. INTRODUCTION

The past few decades have seen an increasing amount of debate concerning economic integration within East Asia¹, with the backdrop of rapidly growing economies in Asia². The economic integration in Asia has, it seems, progressed in terms of the evolution of the international division of labor amongst such countries as China, Japan, South Korea, and other ASEAN countries, along with increases in foreign

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direct investment (FDI) and international production networks among these countries and with other Asian economies. This *de facto* integration has been led by massive and rapid capital inflows from transnational corporations (TNCs).

However, Asian economies have not institutionalized regional integration; they have quite different historical and development paths on one hand, and on the other, the countries in this region have competed actively with each other to gain competitive advantages.

In discussing the relevance and feasibility of economic integration, we need to understand the differences among these economies and their interdependence or complementarity with each other. Hence, we must clarify the institutional diversity of Asian economies and investigate how that diversity has evolved and will continue to evolve.

The past two decades have seen an increasing number of comparative institutional studies of advanced capitalism. For example, studies taking the *Régulation* or Varieties of Capitalism approaches (Amable, 2003; Boyer, 2004; Hall & Soskice, 2001) argued that an economic system is not entirely characterized by a particular institutional domain; rather, it comprises a bundle of different institutions. These studies also indicated that, under certain conditions, institutions can be complementary (Aoki, 2001; Hall & Soskice, 2001). Simultaneously, empirical analyses have documented a wide diversity of capitalism by using statistical methods and quantitative data (Amable, 2003; Hall & Gingerich, 2004; Hall & Soskice, 2001; Pryor, 2005).

Despite these studies' significant contributions to the diversity of capitalist theory, they have several limitations when applied to Asian economies. First, most assume that Asian economies are homogeneous. Amable (2003) analyzed 21 OECD countries, including Japan and South Korea. His analysis argued that the classification of capitalism could not always be binary, as earlier suggested by Hall and Soskice (2001), but is better expanded to five types. Japan and South Korea are categorized into a group described as representing "Asian capitalism" in comparison to advanced forms of capitalism³. Although it is possible to understand a specific "Asian capitalism" different from Western forms of capitalism, we find it problematic to restrict the breadth of Asian economies to be represented by these two countries.

As the center of the global economy has begun to shift from Western to Asian economies, Asian capitalism has come under the global spotlight (cf. Storz, Amable, Casper & Lechevalier, 2013), and some researchers have begun to grapple with Asian economies within the literature on the institutional diversity of economies (Harada & Tohyama, 2012; Tohyama & Harada, 2013; Walter & Zhang, 2012; Witt & Redding, 2013; Zhang & Whitley, 2013). These studies have demonstrated that Asian capitalism can be institutionally distinguished from that of advanced economies but that there is also institutional diversity within Asian capitalism.

For example, Harada and Tohyama (2012), using a methodology based on Amable (2003), identified five types of Asian capitalism by applying multivariate analysis methods, including multiple factor analysis (MFA) and cluster analysis, to institutional datasets covering five different domains. Though analyzing a different dataset, Witt and Redding (2013) also found five types of Asian economies based on five institutional domains. Unlike Harada and Tohyama (2012), they argue that (post-) socialist economies such as India and China should be classified into a specific cluster. The existence of this type arises from the adoption of the "role of the state" as an institutional domain. Although we recognize the importance of Witt and Redding's argument in that they have incorporated an institutional domain, the state, that was missing in Hall and Soskice (2001) and Amable (2003), we find it problematic that rapidly growing China and India are categorized in the same group as Vietnam and Laos. Theoretically speaking, such a classification would encounter serious problems in explaining why the two more populous countries

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