Political Regimes, Financial Market Institutions, and Stability in Asia

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How much does the type of government in a country affect the shape of its stock market? Are non-democratic regimes more likely to produce unstable financial markets?

To begin answering these questions, Mary Cooper plans to compare the stock markets of China, India and Taiwan. China and India not only have experienced dramatically booming stock markets in recent years, but also are among the world's fastest-growing economies and are both of great strategic importance to the United States. Taiwan is smaller, but its complicated history and ongoing tensions with China make it significant.

Most research on financial markets falls into two camps: analyzing the causes of economic liberalization and covering its consequences. Few studies take regime type into account, and those that do use quantitative methods almost exclusively.

Cooper's research goes beyond previous studies in several ways. First, she has a more complete concept of financial markets that looks not only at the extent of economic liberalization, but at other variables such as:

- types of companies on the stock exchange
- types of investors
- mechanisms for openness to foreign capital
- the state's role as regulator and/or participant
- the political foundation for creation and operation

Second, Cooper's use of case studies allows a more detailed understanding to emerge. Combining quantitative data from stock markets and regulatory agencies with qualitative analysis that incorporates sources such as government officials, financial market participants, the media, think tanks and local universities, her research will help clarify the political decisions that determine how and when a market is opened to foreign capital.

The project builds on Cooper's previous research in which she found that China's authoritarian political system had significant effects on the design of its stock market. Established in n1990, the Chinese stock exchange was designed not to promote a market economy but to strengthen the central government's ability to allocate capital.

Market rules instituted a strict separation between different categories of investors including state, domestic corporate, domestic individual, and foreign shareholders. This arrangement has not only limited privatization, but also prevented foreign investors or domestic shareholders from gaining economic power independent of the state.

A grant from the Mershon Center has enabled Cooper to do research in Beijing at the China Securities Regulatory Commission and other agencies. She will also conduct interviews in Taiwan and India.

Cooper plans to publish two articles. In the first, comparing China and Taiwan, Cooper finds that party and state play quite different roles in the financial markets. While in Taiwan the role of the Kuomintang Party eclipsed the role of the state, in China the state (rather than the Communist Party) is a key participant in stock markets. This trend has been reinforced since Taiwan began democratizing in the late 1980s.

Cooper's second article will compare China and India, countries with a similar level of economic development but different political systems. She hopes to find out whether a democratic vs. authoritarian government produces different types of financial liberalization, and whether one financial system is more vulnerable to instability.

Eventually Cooper plans to produce a book that expands her analysis of financial markets in Asia to include several additional cases.

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