

State and Industrial Transformation in East Asia: A Case Study of South Korea

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Abstract

The role of state is integral to proper functioning of the market. A state, with its prescribed set of rules and an organization is much needed for the economy to function in a proper way. From the poorest to the most advanced welfare economies of the world today recognize the pervasive influence of the state as an institution and as a social actor. One of the interventionist arenas of state intervention has been industrialization. A primary concern for all the states has been that of promoting industrial growth and build up assets that would strengthen the national economy. But the role of state in the process of industrial transformation needs to be understood under the broader rubric of its relation and bargaining with the private entrepreneurs who are equally important players in the economy.

INTRODUCTION

The role of state is integral to proper functioning of the market. A state, with its prescribed set of rules and an organization is much needed for the economy to function in a proper way. From the poorest to the most advanced welfare economies of the world today recognize the pervasive influence of the state as an institution and as a social actor. One of the interventionist arenas of state intervention has been industrialization. A primary concern for all the states has been that of promoting industrial growth and build up assets that would strengthen the national economy. But the role of state in the process of industrial transformation needs to be understood under the broader rubric of its relation and bargaining with the private entrepreneurs who are equally important players in the economy.

In classical liberal theory, the role of state has remained confined to making war and enforcing order, safeguarding private property and providing certain basic infrastructural facilities that are beyond the capacity of the market. In modern times, a third role has increasingly stolen the limelight i.e. industrial development. As Peter Evans points out that, in modern time's political survival and internal peace are more defined in economic terms and therefore states have become responsible for industrial transformation¹ National power is not merely understood in terms of possession of military power but is evaluated primarily by the country's level of industrialization. The legitimacy of the state is largely based upon its economic role and its potential to adjust with the changing international conditions. In order for the state to cope with the changing international environment, it becomes an imperative for the state to the most suitable industrial strategy. This further implies, shifting away from the traditional roles and strategy and bring about large scale economic transformation.

Elaborating on the nature of state intervention in promoting industrialization, Evans has categorized state as 'predatory' and 'developmental'. Predatory states lack the ability to prevent individual incumbents from pursuing their particularistic goals. There exists a nexus between the state and the patrimonial elements of the society. The primary objective is the enhancement of individual maximization of profits and personal gains. The idea of collective good is negated. On the other hand, a developmental state is one in which a nation of general welfare of the society exists and the task of promoting general welfare is taken up by the state. Thus, the state gets directly involved in building a strong national economy along with the societal actors. A developmental state is characterized by a coherent internal organization that closely approximates to Weberian bureaucracy. There are no personal ties involved in the bargaining process and a sense of corporate coherence exists. The government enjoys a good deal of autonomy from the private entrepreneurs in decision-making. But this is not to say that the state stands insulated from the societal ties. Evans says that, "the state is embedded in a concrete set of societal ties that binds the state and society, and provides institutionalized channels for continued negotiation and renegotiation of goals and policies."² The state does not get captured by any of the societal groups but creates an autonomous space for itself in framing policies. This kind of state-capital nexus has been termed as 'Embedded Autonomy'. The discussion on state-society relations has been further elaborated by Theda Skocpol in her book 'Bringing the State Back In'. She has defined state autonomy in terms of three analytical categories which are as follows:

- Linkages of states into transnational structures which gives certain amount of discursive space to the state officials to follow certain strategies without any resistance from the societal actors.

- The task of establishing order and fulfillment of the basic needs of the people enhances the state autonomy.
- There is a formation of collectivities of state officials who draw new strategies especially in times of crisis without any kind of interference from the societal forces.³

The next section reviews the theoretical explanations on state and industrial transformation.

SECTION-I

A Critical Analysis of theories explaining Industrial Success of East Asia

There has been a deluge of literature to interpret East Asian economic success. But they have been broadly classified into following theories:

- Free Trade Theory
- Simulated Market Theory
- Governed Market Theory

Although, these theories differ in their view regarding state intervention in promoting industrial transformation, they endorse the fact that export-led growth strategy was a key to success in East Asia. Now let us take an overview of what each theory has to say about East Asian industrial growth.

I begin my discussion with the free market model. An abundant literature attributes the industrial success of the five newly industrializing nations – Japan, South Korea, Hong Kong, Taiwan and Singapore to their reliance on free market. They interpret the remarkable economic performance as due primarily to the actions of private individuals and enterprises responding to the opportunities in a free market scenario. The scholars espousing the free market model believe that an autonomous space was created for the private entrepreneurs to flourish. The government's task was confined to creating a suitable environment for the entrepreneurs to perform their functions freely. The involvement of state in resource allocation into proper channels is found to be absent in East Asia. The scholars also deny the existence of centralized planning and decision-making in these nations. They tend to suggest that the East Asian tigers emulated the American conception of free enterprise under which state intervention in market is negligible. In their view, the state politicians and the bureaucrats lacked the entrepreneurial capacity and thus, they were compelled to rely heavily on the private entrepreneurs for industrial development.

Scholars like Milton and Rose Friedman attempting to make a comparative study of industrial policy making in East Asian and Latin American countries arrive at a conclusion that Malaysia, Singapore, South Korea, Taiwan, Hong Kong and Japan which relied completely on private markets, without state controls, are thriving. In contrast, India, Indonesia and Communist China following centralized planning and protectionism experienced high levels of economic stagnation. To put it in simpler words, the free market theorists believe that East Asia does better than the rest because the East Asian states do not intervene in the market. The business groups were left free to pursue their goals and markets were allowed to function freely. The role of the state was restricted to providing public goods and build up infrastructure.

The free trade theorists commit the mistake of equating minimal interference of the state with market opening. But these are two different phenomena and cannot always be placed on the same; at least it does not hold true for East Asia. This shortcoming would be elaborated further when I discuss the Governed market theory.

The core assumption of the Governed Market theory is that the governments of East Asia have played a more positive role in industrial transformation by giving moderate incentives to the private firms for export-promotion. These incentives were very close to the relative prices of products that prevail in a situation of free trade. It is a unique kind of set up where the government seems to be simulating the market. The main proponent of the theory is Jagdish Bhagwati. He accredits the superlative economic performance in these countries to the adoption of liberal trade policy by the government of these countries. Bhagwati cites the cases of India and South Korea to justify the superiority of liberal trade regimes and the danger of protectionist policies. Figures indicating growth rate of the two countries have been compared by him. The graph shows an upward trend for South Korea since 1960s when it made a shift towards export-led growth strategy. Indian Economy that was much ahead of South Korea in the 1950s and 1960s remained stagnant due to its protectionist policies. For instance, South Korean manufactured products, negligible in 1962, amounted by 1980 to nearly four times those of India. Similarly, South Korea's manufacturing sectors was less than 25% as large as India's in 1970; by 1980 it was already upto 60%. In Bhagwati's view, the contrasts in success with industrialization not just economic growth in general, have been so enormous between the trade liberalizing and the protectionist countries that the old fashioned view that protection favours manufacturing in developing countries has lost its appeal.⁴

As observed, both the theories endorse the view that trade liberalization has been the key to success in East Asia. What is the basic difference between them? The glaring contrast in the two approaches lies in their view regarding state intervention. The Simulated market theory pointing towards an active role played by the government in export promotion refute the claims made by the free trade proponents that minimal government intervention in the market is responsible for the success. Bhagwati points out that, "for those who seek in the experience of these economies and endorsement of free trade in the context of passive government, these facts present obvious difficulties."⁵ It implies that the government has a more positive role to play, much more than laying conditions for the market to function freely. The government along with private entrepreneurs initiated export promotion in East Asia. The first step was to formulate policies that would facilitate the process.⁶ This was followed by giving moderate financial incentives to offset the residual bias against exports by making the average incentive for export exceed the average incentive to import. However, the incentives were allotted selectively i.e. provided to only those specific industrial sectors that showed some amount of export potential. A free trade regime would not have permitted such selectivity. It is also important to note that the states were not completely averse to protection, as the free trade theorist interpreted. As Robert Wade points out that, a major difference between free market and simulated market theory is in terms of the distinction between free trade and neutral trade regime. The former is one with no or few impediments to import; the later is one where any incentive for the domestic producers to sell on the domestic market than export because of protection is offset by subsidies.⁷ Therefore it can be said that a neutral trade regime may go with some amount of governmental intervention, including protection of the domestic market. But, the incentive effect of such protection in biasing sales towards domestic market if offset by export promotion measures. Export promotion in East Asia has been geared by governmental incentives in the form of subsidies and credits. Government's credibility lies in its commitment to

maintain a policy framework that enhances the export promotion strategy. The government is most likely to lose its legitimacy if it drifts away from this strategy. According to Bhagwati, the Far East governments issued prescription to private entrepreneurs rather than proscriptions where as countries such as India did just the opposite.⁸ He further goes on to say that the government of *dos* generally produces economic performance superior to that produced by government of *don't*.⁹ Even if we take it for granted that the prescriptive government may prescribe as badly as the proscriptive government, the latter will have no scope for initiatives, while the former would still keep open areas where initiative can be taken. So, even if the government distorts allocation of the existing resources, the prescriptive government would keep areas open for technical change and entrepreneurial activity, while the proscriptive government will stifle all such initiatives which will result in stagnation of the economy. Prescriptive governments in East Asian countries have worked symbiotically with the private entrepreneurs. There are two major advantages flowing out of this collaboration which are as follows:

- When engaged in planning for a particular industry the government can make use of the industrial experience that the bureaucrats and the politicians lack.
- The symbiosis can reinforce the credibility of the government's commitment to an economic strategy as outward orientation.

The Simulated Market interpretation of East Asian success shows little interest in analyzing the nature of governmental intervention in East Asia, though they recognize its existence. Even if the theory accredits the success of East Asia to prescriptive role of the state, it still holds a minimalist notion of state autonomy.

Having elaborated a great deal on the Simulated Market theory, I now switch over to the most comprehensive interpretation of the East Asian success. This is offered by the theorists most of whom belong to the Neostatist paradigm and the theory is called as 'Governed Market Theory' by Robert Wades. Scholars like Peter Evans, Robert Wades and Alice Amsden are the major proponents of this theory. The core assumption of the theory is that the role of government in East Asia has been more direct than merely setting broad rules of the game and in influencing the economy indirectly through the market forces. The state plays the role of a guardian in East Asia which means that it nurtures the industrial firms. It would be worthwhile to study the interpretations from each scholar's point of view.

Peter Evans advances the conception of 'Embedded Autonomy'. It rests on the assumption that the East Asian states have been developmental in nature which comes very close or nearly approximates Weberian bureaucracy where a coherent internal organization exists. The existence of highly centralized decision-making machinery in East Asia disciplined the capital and labor. The state played the role of a mentor in directing the energies of the private entrepreneurs into productive investments. Peter Evans says that, "corporate coherence gives the state apparatus a certain kind of autonomy."¹⁰ But this does not lead to isolation of the policy makers from the societal ties. The state structures are embedded in a coherent set of social ties that binds the state to the society and provides institutionalized channels continued negotiations and renegotiations of goals and policies. Evans makes a comparative study of state's role in promoting certain industrial sectors in India, Brazil and South Korea. Through his empirical analysis he comes to the following conclusion. The Korean state according to Evans fits well

within the 'Embedded Autonomy' framework, while countries like Brazil and India are considered as the intermediate cases, exhibiting partial or imperfect approximation of embedded autonomy. The argument put forward by Evans approximates closely to Atul Kohli's understanding of state-directed development. Kohli also tries to give an explanation of 'what kind' rather than 'how much' intervention by the state in the market, by evaluating the capacities of the governments in India, Brazil and Nigeria. In Kohli's view there is a range of variation in the state capacities to pursue economic transformation, from fairly effective, growth promoting state in South Korea to a rather ineffective and corrupt state in Nigeria, with Brazil and India providing mixed cases.¹¹ Kohli delves into the patterns of state authority, including how the politics of the state are organized and how state power is used. According to him, the pattern of politics, bureaucratic organization has a decisive influence on the economic context within which private decisions are made.¹² In each of the cases he makes a historical analysis of colonial experiences and its impact on the state formation and state-society relations in the post-colonial period. The conclusion that he arrives at is that, different kinds of state structures create different capacities for action. Structures define the role that the state is capable of playing. Outcomes depend on how well the roles fit in the context and how well they are executed.

Robert Wade, who is the introducer of governed market theory, emphasizes the developmental virtues of a 'soft authoritarian' state in East Asia which has a corporatist relationship with the private sector. The centralized bureaucracy is said to have had sufficient power to influence the allocation of resources in line with long term interests of the national economy. The general interest of the society as a whole has been given primacy over the narrow particularistic interests of the business groups. As Wade points out that, the state's steering of resource allocation is the economic counterpart to its political restrictions on 'free trade' in interest groups.¹³ The presence of a centralized state interacting with the private sector from a position of preeminence so as to secure the developmental objectives has been called the 'developmental state theory of East Asian industrial success. This is just in contrast with the free market and the simulated market thesis where efficient allocation of resources in East Asia has been accredited to the presence of freely functioning markets. The Governed Market theory considers capital accumulation as the generator for growth, and interprets superior East Asian performance as a result of a level of composition of investment different from what free market or simulated market would have produced. The state has played the role of a midwife in accelerating capital accumulation, by giving export incentives to private entrepreneurs and ensuring that productive investments were made. According to Wade, the superiority of the East Asian economic performance is due in large measure to a combination of the following factors:

- very high levels of productive investments; transfer of new technology into production
- More investment in certain key industries than would have occurred in the absence of governmental intervention.
- Exposure of many industries to international competition in the foreign market.¹⁴

The comparative advantage of certain products drove the state to launch such industrial sectors in the international market. By using incentives, controls and mechanisms the government in East Asia governed market processes of resource allocation so as to produce different production and investment outcomes. Robert Wade looks into the factors that enabled the state to

discipline the capital and labor. This was achieved by corporatist and authoritarian political arrangement of East Asian countries. The coherent internal organization of the state provided the basis for market guidance. The state took a number of measures to ensure that the discipline was maintained.¹⁵

In a nutshell it can be said that, the Governed Market theory gives primacy to the state with regard to its role in industrial transformation. Without the proper guidance provided by the state, the East Asian countries would have had the same fate as others, like Nigeria or even intermediary cases like India and Brazil. The policy framework adopted by the states in East Asia enabled the economy to grow so rapidly that by mid 80s these countries surpassed others who were much ahead of them in the early 60s.

Baldev Raj Nayar advances a different kind of interpretation of the East Asian success. He suggests that it was the impact of the ever increasing influence of economic globalization i.e a tendency of the market towards relentless expansion to bring the entire globe under its reign that the countries of East Asia had to rethink their industrial strategy. The movement in the path of globalization involved reduction in transaction costs, or large increment in benefits from international economic transactions. The benefits flowing from globalization propelled the states of East Asia to integrate their economy with the international market.

The fourth quarter of the twentieth century has been described as the phase of intensive globalization, which has been characterized by dramatic changes in technology, transportation and communications. The East Asian nations began harnessing such benefits as early as mid 1960s by following an outward oriented strategy. Intensive globalization has given a unique dynamism to the world economy. This assumption has been well supported by the economic boom of the East Asian nations. Nayar points out that, what stands in respect of these economies is their greater integration into the world economy through their high participation in the international trade as a consequence of having purposely chosen outward-oriented growth strategies.¹⁶

The nature of globalization has also been described as 'truncated', given the concentration of more or less economic interactions within the triad of the United States, Japan and the European Union. The benefits of globalization have largely flowed to the developed countries lodged in the triad. The countries of the triad have determined the pace of globalization. They employ a variety of mechanisms to shape globalization in the service of their interests and pass on the costs of adjustments to the less developed countries.

There is a contradiction in between these two understandings of globalization developed by Nayar. The transaction benefits of globalization facilitated the opening up of economy by the newly industrializing nations. Harnessing the opportunities provided by integration, the East Asian nations have been uplifted from periphery to semi periphery, and now moving towards the core. However, the other side of the argument that looks at the impact of geopolitics on globalization, and that leads to what Nayar calls truncated globalization, seems to inhibit integration into the global market. Nayar fails to look at the crucial role played by the state in the entire process. He ignores the discipline that the state imposes on capital and labor and the guidance it provides by supporting selective industries through financial incentives. Globalization is not the sole driving force behind global integration. Had this been the case, the goal of building up a national economy would have been shattered by the interests of a few profit maximizing private entrepreneurs.

Moreover, the dominance of the sophisticated manufactured products of the western firms would have jeopardized the fate of these companies in the international market. The selective promotion of certain industries has averted the danger of leading the economy in the hands of a few Hobbesian individuals.

After having browsed through the theoretical interpretations of East Asian miracle, it is worthwhile to analyze or rather test their validity in the South Korean case. The second section of the paper draws a historical sketch of the South Korean political economy. It begins with the analysis of colonial period since a lot of experiences of this time help us understand state formation in the post colonial period. The second phase begins with the establishment of the independent Republic of South Korea. This period has been characterized by high levels of corrupt practices involved in the state-capital alliance. At this stage South Korea opts for Import Substitution model. But whether the strategy so adopted was an authentic one or not, needs to be explained. The third phase is characterized as the period of South Korean miracle when the country witnessed rapid industrial growth. It is during this period that an authoritarian state is established and a transition from import substitution to export-led growth takes place.

SECTION-II

The History of the Role of State in Industrial Transformation in South Korea

As the record of the developing countries goes, South Korea is one of the greatest economic success stories of the twentieth century. The growth rates of the country sky shorted within a very short period. Other countries of the developing world that were much ahead of Korea in terms of economic development were all super headed by it by the late-1970s and early-1980s. The enormous achievement of South Korea raised the intellectual curiosity of many economists, political scientists and policy makers. It would be an endless narrative to delineate the success of South Korea. Therefore, rather than intruding too much into the grand narrative, it would be worthwhile to analyze the secret behind the grand success.

The story begins from the colonial period.

Phase I: The Colonial Period

South Korea's economic dynamism begins from the colonial period, which is the second half of the 20th century. Atul Kohli argues that, "the Japanese colonial influence on Korea, from 1905 to 1945, was important in shaping a modern political economy that later evolved into high growth path to development".¹⁷ The colonial masters transformed Korea in a relatively short period. Kohli has advanced three influences of Japan on the political and economic transformation of South Korea. These are as follows:

- From a relatively corrupt and ineffective agrarian bureaucracy into a highly authoritarian, penetrating organization capable of transforming Korean society.
- The emergence of the new state's production oriented alliances with the dominant classes.
- The structural changes in the economy, opting for an export oriented growth study.

The Japanese imperialists transformed the corrupt, inefficient and powerless Yi state into a well organized, cohesive and growth promoting state. The impact of the Japanese colonial power was decisive in altering both the nature of the Korean state and its relation with various social classes. The patrimonial elements of the monarchical state was completely destroyed and replaced by a highly centralized cabinet-style government run

by Japanese bureaucrats. The presence of Korean bureaucrats, well trained and employed by the Japanese was sizeable. The new bureaucracy enabled the state to undertake many economic activities that contributed to economic growth; and the repressive measures adopted led to the establishment of order, letting the state elite focus on developmental matters.

Now let us take a close look at the activities of the government in the economic front. Following the First World War, the profits of the Japanese companies sky shorted. Japan sought opportunities for export of capital and thus relaxed restrictions against production of manufactured goods in Korea. By the 1930s nationalist pressures for co-opting Korean businessmen made the colonial state involve a few of them in manufacturing. Along with Japanese investors, enterprising Korean businessmen who generally had their roots in landed property were allowed to enter medium to large scale manufacturing. They were supported by financial incentives such as credits, bank loans, subsidies and other public supports.¹⁸ As scholars like Carter Eckert say that, "Korean capitalism came to enjoy its first flowering under Japanese rule and with official Japanese blessing." Therefore it can be said that the major business conglomerates of today's South Korea actually got their start up during the colonial period. The existence of business-government cooperation can be traced back to the early 1930s. The mutuality provided a platform for establishing a strong industrial base in South Korea.

In a nutshell, the contribution of the colonial masters in the economic success of South Korea can be located on following grounds:

- Establishment of a highly cohesive and disciplined bureaucratic structure.
- Co-opting the Korean entrepreneurs in the task of industrial development, so that by the end of colonial period we already have an industrial class well equipped with the production and marketing techniques.
- Building up a strong infrastructure as compared to other colonized nations and establishing a highly educated and disciplined labor force.

Phase II: Rhee Regime

This phase came to be characterized as one that witnessed the highest political and economic turmoil in the history of South Korea. With the retreat of Japanese, the country got divided into communist North and American-controlled South. Syngman Rhee dominated South Korean politics during this period, especially after the ghastly north and south war. Two major developments that took place during this period were as follows:

- The role of American capital in overcoming the destruction of the economy caused by north-south war.
- Adoption of Import Substitution Industrialization.

After the departure of the Japanese, an interim Korean People's Republic was formed that comprised elements having populist, anti-imperialist and left leanings. The KPR was soon removed as they proved to be contrary to the wishes of the Americans, and the power was transferred to Rhee. The Americans supported the establishment of a rightist autocratic state and maintaining cohesion that Korea had inherited from Japan. But, the power of Rhee was constrained to a large extent by the American military presence. The task of promoting industrialization and economic growth was relegated to the background and garnering political support by repressing any potential threat became a prior concern. Rhee took no interest in promoting technology or facilitating

investment. Few socialist programmes were undertaken like, pursuing land reforms and establishing state owned enterprises, but such policies were conceived mainly as actions in defence or in support of capitalism and not as interventions at humanizing the harshness of markets. So, utmost effort was made to maintain the Japanese-style capitalism.

The major impediment that the policy makers were confronted with was how to overcome the economic misery caused by the war. Kohli mentions two important factors that led to quick economic recovery after the war. These are as follows:

- Financial aid from the United States.
- The presence of a strong Korean entrepreneurial class that had gained sufficient industrial experience during the colonial period. Secondly, one notices that the transfer of Japanese owned mines, plantations and other kinds of property to the Korean entrepreneurs brought additional tools in their hands to apply their innovative skills and industrial knowledge.
- The presence of a well trained, educated and skilled labor force.

Due to these two factors, a modest growth rate could be maintained between 1953 and 1960.

Turning onto the Import Substitution model adopted by Rhee, one needs to ask the question as to whether the strategy so adopted was genuine one or not. Kohli refuses to accept the genuineness of the strategy and advances a number of reasons for the same. The US occupation force introduced import quotas and tariffs in South Korea, aimed at minimizing imports. With an overvalued exchange rate, Rhee subsequently increased the tariffs which averaged about 40%. Now this figure is just in contrast with the tariff figures of India and Brazil that amounted to 100%. This obviously gives a distortionary picture of the ISI model in South Korea. Secondly, a variety of subsidies were provided to the exporters that overshadowed the effect of the overvalued exchange rates on the exports. Thirdly, having privatized most of the Japanese owned mines and factories, the establishment of a public sector enterprise was done away with. This was precisely due to the reason that both Rhee and Americans viewed state ownership of property with suspicion.¹⁹ Therefore, one can state that the developmental strategy fell short of a full blown import substitution model. The exporters weren't sidetracked, as would have been the case if a rigid ISI model was followed. The state support that the private firms received during the colonial period was continued by Rhee and further strengthened by Park later.

A certain kind of nexus between state and capital is observed during this period. The purpose of cooperation was not based on any long term objective of building a potent national economy, but to fulfill the vested interests of the parties involved in transaction. Control and allocation of scarce foreign exchange, credits etc to a handful of businessmen was simply a method used to channel quick money for the Liberal party of Rhee. As a result, we find that there were no productive investments and the state-capital alliance was based on corruption. As Evans points out that, Rhee's dependence on private donations to finance his political dominance made him dependent on clientelistic ties with individual businessmen. Thus, Rhee's regime was more predatory than developmental.²⁰ Nevertheless, the benefits of Rhee's policies that had a strong bearing on the miracle of 1960s cannot be neglected. Some of the positive traits of the political economy during this period are as follows:

- A cohesive, centralized colonial state maintained under American tutelage.

- Presence of a well trained entrepreneurial class that had its origin in the colonial period grew stronger and now came on its own.
- Presence of a skilled and educated labor force.
- American aid for educational and infrastructural development.
- Incentives to the exporters continued to some extent.

Phase III: Park Chung Hee's Regime

It is this period in the South Korean history that witnesses tremendous economic success, so much so that it has been characterized as the period of South Korean miracle. It drew the attention of scholars and policy makers throughout the world towards the exceptionality of the strategy adopted by the South Korean government for industrialization.

In 1961, a military coup was staged and the Rhee regime was overthrown. A new government under the leadership of Park Chung Hee was formed. Since then the political economy of South Korea underwent radical changes. The junior officers involved in the coup had reformist convictions. The goals and objectives of the new developmental state went beyond the narrow, particularistic interests of the private entrepreneurs. The first step taken in the direction of industrial transformation was establishing state's stranglehold over private capital. The new government abandoned the import substitution model and opted for export-led growth. There was a tremendous rise of exports during this period. Growth rate of exports increased from 1.3% in the decade 1950-60 to 310.8% in 1960-70.

Park did harness private entrepreneurship and managerial expertise in order to pursue his economic policies. Through allocation of capital, the state promoted some of the leading companies such as Daewoo, Samsung and Kia in the international market. The allocation of finances through credits, loans and subsidies was strictly based on performance of the industries on the export front. One of the first things that was done by Park was to nationalize the banks in order to centralize the financial control. Now the question that arises is that, how did the government control the credit market? As said before, the government owned major commercial and specialized banks. The government employed tight control on interest rates and directed credit loans to support specific sectors and industries allocating more than half of bank credits in directing programmes. Bank ownership implied that the government could also dictate the objectives of the banks directly. Since, bank managers were appointed by the government; their incentives were determined by a hierarchy. Performance evaluation was based on confirmation to policy guidelines framed by the government. Managers carefully executed government decisions and prudently avoided visible failures such as large loan defaults. They were pressed to monitor their loans closely, held directly responsible for the failure of any discretionary lending and were encouraged to make the directed loans profitable. These checks by the government disciplined the firms involved in the transaction business. The government, being the creditor could not only cut off official credit but also impose punitive measures against the borrowers in case of dissatisfaction with their performance. But the government also played the role of a guardian to the business groups, by securing continued credit support to the firms and bailing out firms in situations of financial distress. The chaebols strongly depended on bank loans and the government for the expansion of their business.²¹

The government did not insulate itself from the societal ties. It did co-opt the representatives of various groups in

the developmental process by asking for constant input and suggestions from them, from time to time. Nevertheless, the final decisions were taken by the government, and it was a prerogative of the government to accept or reject such recommendations. The industrial associations in South Korea facilitated the consultation of policy decisions and implementation, channeled market information to the government and assisted in the effective transmission of policy goals to industrial activities. There were also monthly briefings on economic trends and monthly export promotion meetings, chaired by the president and attended by senior government officials, bankers, business representatives and labor union leaders. By attending such meetings, all the participants shared a common understanding of current economic conditions and issues. In the monthly export promotion meetings, the Ministry of Trade and Industry would make reports not only on achieving annual export targets, but also the problems and difficulties faced by the industrial firms in meeting their export goals. The performance of exports was reviewed item by item, and country by country in the meeting. After the discussions and deliberation about the bottlenecks for exports of specific projects at these meetings, the president gave instructions as to how the problem should be resolved; and asked the government officials, bankers and representatives from private sector for their suggestions and inputs. In this way the government, the financial sector and the industrial firms shared a common responsibility in achieving prescribed goals. This triad has been termed as 'government-led internal organization' by Thomas Hellmann and Yoon Je Choo.²²

Now let us test the validity of interpretations advanced by the governed market theorists. Peter Evans visualizes the presence of a developmental state at work during this period. This is in view of the fact that a symbiotic relation existed between the state and chaebol. While, the state could maintain its autonomy by extending domination over country's finances and disciplining the market through its credit controls, it did delegate some amount of economic power to the chaebols without whose cooperation it was nearly impossible to lay a strong industrial base of the country. Thus, we find that embeddedness in market had to go along with state autonomy. However, it had to be ensured that embeddedness concentrated in a few ties should not degenerate into particularistic predation. This kind of cooperative association between state and chaebols is just in contrast with the corrupt nexus that existed between state and a few businessmen during Rhee's regime. While in the former case, cooperation was based on a broader goal of building a strong national economy, the latter case involved a bargaining where vested interests of each party could be fulfilled.

Robert Wade accredits the economic success of South Korea to the crucial role played by the state in governing the market. The strict control over the credit market; disciplining the allocation of finance; giving incentives to selective industries for export promotion; adherence to the policy guidelines set by the government; disciplining the labor force to check any kind of upsurge on that front; clearly indicate the extent of penetration of state in the market. According to Wades, the state played the role of a guardian in South Korea that resulted in productive investments. The existence of corporatist regime checked competition amongst profit maximizing businessmen and prevented the market to go out of hand. The companies that showed greater capacities in building up economic assets of the countries were the recipients of the financial incentives. Some of the promising businessmen were also given representation in the government-led internal organization, but they were all subordinated to the government.

It is also important to note that a number of public sector enterprises flowered during 60s. Public sector, during Park's regime constituted a leading sector of the economy. The establishment of public enterprises helped in overcoming the imperfections of the private market. The number of public enterprises increased from 59 in 1965 to 119 in 1969. The value addition of public sector grew from 90.6 billion won in 1964 to 271.7 billion won in 1972. By 1972, Korea's leading public sector enterprises, both central government and para-statal, had 2 lakh employees and an output of 870 billion won. This undoubtedly indicates the stranglehold of government over the economy. Another major implement of governing the market was the public ownership of the banking system. It was through a well regulated banking system that the government could reshape the investment structure.

There is none other than Alice Amsden who has made a methodical analysis of South Korean industrial success. Falling within the governed market paradigm, she takes a radical stand asserting that state played the role of a guardian in South Korea by disciplining the capital and labor. In her view, Korean state acted as an entrepreneur, banker and shaper of the industrial structure. The state disciplined the use of subsidies and other supports, rewarding those who used the subsidies well. This phenomenon has been termed as 'qualitative subsidization' and is considered to be the driving force behind triumphant industrialization. Amsden believes that in some ways, the late industrializing nations had an advantage over the early industrializing nations. This is in view of the fact that there was no need to take extra efforts in developing technology as the early industrializing nations had to do. Easy access to technology could be achieved by harnessing technology from the west. The state took the following initiatives in the direction of industrial transformation:

- Make firms internationally competitive by directing their energies into productive investments.
- Establish a highly advanced, technically sound industrial structure.
- Made the labor force skilled and efficient.

The first objective was achieved by selecting a few competent chaebols and giving them financial incentives such as subsidies, loans and credits. For accomplishment of the second objective, transfer of technology was required from the advanced nations. This was made possible by creating a suitable environment for the foreign corporations to invest in the country. A number of incentives were advanced to these firms, one of which was creation of export free zones for them. Most of the corporations were of Japanese origin and concentrated in manufacturing, especially in chemicals, electronics and textiles. A skilled labor force could be established by engaging managers and business groups in the process and advancing pro-active policies.

Amsden believes that late industrialization was based on learning and borrowing. Learning meant borrowing, adapting and improving upon foreign designs. Amsden calls the South Korean state as an entrepreneurial state because it took the initiative of promoting competent firms in the international market. In her view, South Korea witnessed rapid industrialization mainly due to two reasons:

- By preventing the market to function freely.
- Subsidization process was made qualitatively superior.

Stephan Haggard delves more into the policy framework adopted by the state. According to him, what accounted for divergence in policies was mainly due to the interplay of four factors which are as follows:

- International
- Domestic coalition
- Political institutions
- Ideas

Haggard focuses on the economic, legal and institutional reforms advanced by the state to accomplish industrial transformation. According to him, a shift in the strategy from ISI to Export-led growth was not simply a result of economic liberalization. In this regard, he raises a question that, "if export led growth was a superior strategy then why has policy reform elsewhere proved so infrequent and hesitant?"²³ Most of the neo-classical theories tend to discount, how domestic forces constrained economic policies and shaped state's responses to the external environment. Haggard refutes the ideas of dependency and neo-classical theories on the ground that they focused entirely on economic and functional theories of politics and ignored the role of institutions and processes.

SECTION-III

Critical analysis and conclusion

In most of the South Korea's industrial development it is largely taken for granted that the authoritarian state from the 1960s to the end of Park era not only dominated Korean society, but could literally govern by decree. Therefore, most of the scholars falling within the neo-statist paradigm tend to divert their entire concentration on the role of state. Consequently, the authoritarian nature of the state becomes the only causal variable to explain the industrial success of South Korea. But, by taking such a one-sided view, one tends to deviate from the analysis of the capacities and power of the business conglomerates, without whose collaboration a proper application of the policies and strategies would not have been possible. Timothy Lim recognizes that power is subject to structural limitations and therefore, all enduring power relations involve some element of reciprocity and open-endedness. It implies that, all social agents have certain powers i.e. dispositional capacities that they possess by virtue of their place in the social relation. Power is dynamic in nature. It is not simply a static social distribution.²⁴ In South Korea, state power has been complimentary to the structural powers of the chaebols in accordance with latter's purpose to invest; to look for and act upon new opportunities; to meet its production deadlines etc. The state's legitimacy was entirely based on its commitment to export-promotion strategy. Secondly, the basis of power of chaebols was their entrepreneurial capacities and management skills that they inherited from their colonial masters. The chaebols had garnered sufficient industrial experience in the colonial period that became a source of their power in the post-colonial period. Above all, the transfer of colonial property like factories, plantations etc had made them well equipped. It was an imperative for the state to co-opt them in the developmental process and grant them sufficient amount of economic power. The eminent position held by some of the prominent businessmen in the government-led internal organization is a clear indication of this. The importance of state lies in checking free competition and creating an incentive environment for few chaebols. Adopting a policy based on free market economy or even simulated market economy would have left the economy entirely in the hands of a few profit-maximizing entrepreneurs, who anyways lacked the capacity of competing in the international market. Therefore, it can be stated that the joint collaboration between a developmental, centralized and cohesive state and few skilled, committed and innovative chaebols led to the establishment of a solid industrial structure in South Korea. The argument closely

approximates to the embedded autonomy thesis. It implies that the state had carved out an autonomous space for itself but was also embedded in the market. The state was not at all insulated from the societal ties. Therefore, overemphasis on the autonomy and capacity of the state tends to neglect the other side of the story that involves the role of prominent businessmen in the industrial process. One needs to focus on the state-capital alliance in Korea to understand its economic success carefully.

The second crucial variable explaining industrial success of South Korea is the appropriate strategy adopted in the context of a highly competitive international market. The adoption of export-led growth strategy is one of the most important factors for achieving the prescribed goals. The figures clearly indicate that the countries following protectionist policies were entrapped in high levels of stagnation, while export-promoting countries developed rapidly. The export led growth strategy adopted by the government was based on comparative advantage of the firm in the international market. Companies like Samsung, Daewoo and Kia that demonstrated their versatility across the globe were the recipients of governmental incentives.

Thirdly, it is important to note that the developments in the colonial and the first decade of the post colonial period did contribute to the industrial development during 60s in South Korea. There are basically two views in this regard. The first one espouses the continuity thesis which says that the unique capacity of the state to enforce compliance was legacy of the past. The discontinuity thesis endorses the view that there has been a complete break from the past in Park's regime. The government formed under the leadership of Park revamped the entire economic system and eliminated all kinds of corrupt practices embedded in the political system. Once the dominance of state got secured, its developmental ambitions were realized by the adoption of export-led growth strategy. Thus what came into existence was a new born "Korean exceptionalism".²⁵ Although the discontinuity thesis holds some amount of validity in the South Korean case, it is difficult to claim that the new state made a complete break from the past. After all, an experienced entrepreneurial class and an adroit labor force was a gift of the legacy. Secondly, one cannot ignore the importance of American investment in infrastructural development and education during the Rhee regime, and the American financial support in overcoming the economic crisis of mid-1950s. Had there been no American aid, the crisis would have definitely sustained for a longer period. Therefore, it would be a fallacy to advocate a strict incommensurability between the two periods of South Korean history to understand industrial transformation.

In conclusion it can be said that, in a scenario of a highly competitive international economy, protectionism and inward looking industrial strategies have lost their validity. The only alternative left before the less developed nations is to open up their economy and integrate with the international market. Lessons can be taken from South Korea in this regard. Most importantly, the success of East Asia in general and South Korea in particular, is accredited to the guardian role played by the state in bringing about changes in the economy. The state's ability to discipline capital and labor and check free competition led to the establishment of a potent industrial structure. It is also important to recognize the presence of a skilled entrepreneurial class, which was equally responsible in carrying out the developmental tasks most prudently and successfully. It was an imperative for the state to co-opt them and seek their suggestion in framing industrial policies from time to time. The eminent positions held by the business groups in the government-led internal organization are a clear indication of this fact. Therefore,

in understanding the South Korean miracle, one needs to avoid the overemphasis on power, autonomy and capacity of the state, and understand state autonomy within the broader framework of state-capital alliance.

ENDNOTES

- 1 Peter Evans, *Embedded Autonomy: State and Industrial Transformation*, (New Jersey: Princeton University Press, 1995) p.5.
- 2 Evans, *Embedded Autonomy*, p. 12.
- 3 Peter Evans, Dietrich Rueschemeyer and Theda Skocpol, *Bringing the State Back In*, (Cambridge: Cambridge University Press, 2002)
- 4 Jagdish Bhagwati, *Protectionism*, (Cambridge: MIT Press, 1988) p. 93.
- 5 Bhagwati, *Protectionism*, p. 94.
- 6 One of such policies was substantial reduction of the overvaluation of currency rates which was deemed to be one of the main hindrances to free trade.
- 7 Robert Wade, *Governing the Market: Economic Theory and the Role of Government in East Asian Industrialization*, (New Jersey: Princeton University Press, 1990) p. 24.
- 8 Bhagwati, *Protectionism*, p. 98.
- 9 Here the government of 'dos' refer to liberal trade regimes and the government of 'don't' refer to regimes following protectionist policies.
- 10 Evans, *Embedded Autonomy*, p. 12.
- 11 Kohli, *State Directed Development: Political Power and Industrialization in Global Periphery*, p. 2.
- 12 Kohli, *State Directed Development: Political Power and Industrialization in Global Periphery*, p. 2.
- 13 Wade, *Governing the Market: Economic Theory and the Role of Government in East Asian Industrialization*, p. 29.
- 14 Wade, *Governing the Market: Economic Theory and the Role of Government in East Asian Industrialization*, p. 26.
- 15 in page 27 Robert Wades mentions the following initiatives taken by the state in prompting industrialization:
 - a. Controlling finance capital and making private financial capital subordinate to industrial capital.
 - b. Maintaining stability of the economic parameters like exchange rate, interest rate and price level.
 - c. Modulating the impact of foreign competition in the domestic economy and prioritizing the use of foreign exchange.
 - d. Promoting exports.
 - e. Technology acquisition from the MNCs and building a national technology system.
 - f. Assisting particular industries.
- 16 Baldev Raj Nayar, *Geopolitics of Globalization*, (New Delhi: Oxford University Press, 2005) p. 262.
- 17 Kohli, *State- Directed Development: Political Power and Industrialization in the Global periphery*, p. 27.
- 18 see page 54, Atul Kohli says that apart from these financial incentives they enjoyed preferred interest rates on credits, lower charges on electricity and indirect subsidies. The budding Korean entrepreneurs financed their investments by governmental subsidies and bank loans from government controlled Choson Industrial Bank.
- 19 Kohli, *State- Directed Development: Political Power and Industrialization in the Global periphery*, p. 80.
- 20 Evans, *Embedded Autonomy*, p. 52.
- 21 In South Korea the industrial sector could be broadly divided into 35 to 50 chaebols who had firms producing goods and services in almost all sectors.
- 22 Hellmann, Thomas and Yon Je Choo, "The Government Role's in Japanese and Korean Credit Markets: A New Institutional

- Perspective", *Seoul Journal of Economics*, 1994
- 23 Stephan Haggard, *Pathways from the Periphery: The Politics of Growth in the newly Industrializing Nations*, (New York: Cornell University Press, 1990) p. 15.
- 24 Lim, Timothy, "Power, Capitalism and Authoritarian State in South Korea", *Journal of Contemporary Asia*, 1998, p. 465.
- 25 Chibber, Vivek, *Locked in Place: State-Building and Late Industrialization in India*, (New Jersey: Princeton University Press, 2003) p. 57.