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THE Southeast Asian ECONOMIC MIRACLE

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Preface

That the countries comprising the Association of Southeast Asian Nations (ASEAN) and some of their neighbors recorded dramatic increases in key economic, social, and development indicators in the 1980s and early 1990s—the "economic miracle" in the region that is so extensively written about in scholarly and popular media—is of little debate amongst academics, government officials, economists, political scientists, geographers, and others who study the area. There is less agreement, however, about the sources of this growth, and whether the improvements in income, industrial and agricultural production, health, nutrition, and other quality of life measurements are a permanent or transitory feature of the Southeast Asian landscape.

The American Council on Asian and Pacific Affairs (ACAPA) and the Institute of World Economy of Seoul National University convened a conference in November 1993 in Washington, DC, to address these and other questions about the Southeast Asian economic miracle and this book is the product of those discussions. The co-sponsors are grateful to the Jinro Cultural Foundation for generously providing support for this project.

I also would like to acknowledge the valuable contribution made by experts in the field who contributed significantly to the success of the conference as guest speakers, moderators, and discussants. They included, in the order of their appearance, Gaston J. Sigur, ACAPA and The George Washington University; Ezra Vogel, Harvard University; Daniel Lev, University of Washington; John Merrill, Department of State; John Bennet and Alisdair Bowie, both of The George Washington University; Hakchung Choo, Center for Economic Education, Korea Development Institute; Robert Muscat, Institute for Policy Reform; David Steinberg, Georgetown University; Evelyn Colbert, SAIS, Johns Hopkins University; Catherin Dalpino, Department of State; Elaine Grigsby, AID, Department of State; Paul Cleveland, Department of State; Tae Yong Hahm, Korea Long-Term Credit Bank; H. Leedom Lefferts, Jr., Drew University; Danny Leipziger, The World Bank; Robert Sutter, Congressional Research Service; Vance Hyndman, CAPA, The Asia Foundation; and Harry Harding, Brookings Institution.

Young C. Kim

1 THE TRANSITION IN THE POLITICAL ECONOMY OF SOUTH KOREAN DEVELOPMENT: ISSUES AND PERSPECTIVES

Hak K. Pyo

Since after Lipset[1] advanced the proposition that democracy is a product of economic development, there have been voluminous theoretical and empirical studies investigating its validity. The critics of democracy argue that dictatorships can insulate the state from particularistic pressures and, therefore, are better at mobilizing savings. On the other hand, the defenders of democracies argue that only democratic institutions can constrain the state to act in general interest and that dictatorships of any stripe are a source of inefficiency; democracies are better at allocating investment.

After reviewing 18 empirical studies, Przeworski and Limongi[2] conclude that the statistical evidence on the Lipset proposition is inconclusive. Among the 21 findings generated by those studies, eight found that authoritarian regimes grew faster, eight found in favor of democracy, and five discovered no difference.

On the other hand, Lipset's proposition has been examined by a number of comparative historical studies. Moore,[3] for example, has come to skeptical conclusions about the chances of democracy as capitalist economic development spread around the globe. More recently, Huber, Rueschemeyer, and Stephens[4] have examined democratic transition and breakdown in Europe, South and Central America, and the West Indies. They have concluded that the level of economic development is causally related to the development of political democracy. They argue that the underlying reason for the connection is that capitalist development transforms the class structure, enlarging the working and middle classes and facilitating their self-organization, thus making it more difficult for elites to exclude them politically.

The purpose of this chapter is to examine the current democratic transition in South Korea both in an empirical and historical context. The success story of South Korea in development provides us with two edges of the connection between economic development and political regime. On the one hand, as cited by Sah[5] and Bardhan,[6] its development under President Park and President Chun provides a case in favor of an authoritarian regime that fosters economic growth by insulating development-minded decision makers from short-term rent-seeking and distributive politics. On the other hand, it also provides a case for the Lipset proposition in the sense that its economic development invited democratic transition under President Roh and the current President Kim. In this regard, a careful examination of the South Korean case is fully warranted. In my view, South Korea is a perfect example of supporting the view of comparative historical research, advanced by Huber, Rueschemeyer, and Stephens[7] and endorsed by Bardhan,[8] that the level of economic development is causally related to the development of political democracy. In the present chapter, I examine how capitalist development in South Korea has transformed the class structure and the nature of economic dependency.

In the next section, the capitalist development in South Korea under two consecutive authoritarian regimes is analyzed and its dependent nature and limitations are examined. This is followed by a discussion of the transformation of the class structure and the changes in economic dependency that ultimately have brought about a Lipset phenomenon. The final sections discuss the ongoing democratic transition and the conditions for the survival of democracy and reach a contentious conclusion.

ECONOMIC DEVELOPMENT UNDER AUTHORITARIAN REGIMES AND ITS LIMITATIONS

After the independence from Japanese colonial rule, the division of the Korean peninsula, and the subsequent Korean War, South Korea remained a poor underdeveloped country. The Rhee government relied heavily on U.S. military and economic aid. During the period of 1954–1961, the average growth rate of real GNP was about 4.0 percent with an average annual inflation rate of 22.1 percent, as shown in table 1. The balance of payments could be maintained at equilibrium only with U.S. aid.

In a recent article, which refers to South Korean development as an economic miracle, Lucas[9] has compared the country's economic situation in 1960 with the Philippines. Both countries had about the same standard of living with per capita GDP of about 640 U.S. dollars in 1975 prices. The college enrollment rates in South Korea and the Philippines were 5 percent and 13 percent respectively. Only 20 percent of South Korean GDP was generated in industry while the comparable number in the Philippines was 28 percent. Primary commodities made up 86 percent of Korean merchandise exports and 96 percent of Philippine merchandise exports. However, from 1960 to 1988, GDP per capita in the Philippines grew at about 1.8 percent per year, while in Korea it grew at 6.2 percent per year.

President Rhee followed a typical course of development dictatorship, oppressing the opposition party and bribing voters to hold the majority in the assembly. He also alienated himself not only from the public but also from the ruling class. Ultimately, the nationwide voting scandal in the 1960 general election invoked strong opposition by the opposition party and student activists.

The Rhee government was toppled by a student uprising in April 1960 and a cabinet system was formed under the new constitution. Even though the Second Republic under Prime Minister Chang was a seemingly democratic regime, it was too weak to consolidate power and secure both political and economic stability. It could not handle effectively the rampant demands by student activists and the newly formed opposition party.

It was setting up a classic situation for military intervention. While division among elite groups—with no individual group powerful enough to hijack the state by itself—may somewhat enhance the chance of democracy, it should nevertheless be pointed out that in some countries intra-elite conflicts may get out of hand (inviting extra-constitutional interventions, perhaps from the military).[10]

The political instability has provided the military both opportunity and legitimacy to intervene. Following a coup in May 1961, President Park consolidated military power and formed a new government. At the beginning of his rule, he rode on the popular sentiment of suppressing capitalist groups established under the Rhee government. Several well-known businessmen were put into jail and had to surrender their assets to the public. But soon Park realized that he needed their help to restore economic stability and, therefore, released most of them but requested that they come up with development project proposals. He started using the stick and carrot to control the business circle.

President Park was desperate to build the legitimacy of his government against the hesitant U.S. recognition and the vigorous opposition activities. He tried to establish it by making the public concentrate on two issues: national security from the North Korean threat and economic growth to avoid the vicious circle of poverty. The phaseout of U.S. economic aid increased public awareness of economic hardship and, therefore, the slogan for mobilizing national resources for the economic take-off was effectively penetrated into the public's mind.

Throughout the period of Park's presidency (1961–1979), South Korea managed to pass the take-off stage and to achieve a remarkable industrialization. The government drafted successive five-year economic development plans beginning in 1962. However, there was tight security control and political suppression. The political opposition to Park's regime was at its peak in October 1972. After being reelected with a narrow margin against Dae-Jung Kim, President Park declared what is called the "Restoration System" and made himself an almost permanent president by changing presidential election law from direct vote to indirect vote.

However, at the same time, he was able to insulate the development-minded bureaucrats from particularistic pressures and the marauding lobbies of distributive politics.[11] The South Korean economy managed to overcome the first oil crisis in 1974 and to pass the Lewisian turning point in 1975, ending the period of unlimited labor supply. During the 1960s, in order to fill the gap between domestic savings and investment demand, South Korea relied on foreign capital. Foreign capital inflow was made mostly in the form of borrowings from international lending institutions such as the World Bank and bank syndicate loans. The role of foreign direct investment was relatively low. The combination of capital and abundant but well-educated labor made it possible to achieve successful export-led growth.

After 1975, President Park pushed for a second stage of industrialization, focusing on heavy and chemical industries as strategic industries. He became more confident about the country's industrialization after successfully overcoming the first oil crisis. But, pressure from the Carter administration on the human rights issue and the pullout plan of the U.S. forces in South Korea made him obsessed with the goal of self-defense. At the same time, domestic opposition was getting more organized and, consequently, he put more people in jail as the political situation worsened. In addition, a worldwide recession and the second oil crisis was about to come.

As Przeworski and Limongi pointed out,[12] regimes do differ in their probabilities of surviving various economic conditions: authoritarian regimes are less likely than democracies to survive when they perform badly. In 1979, the South Korean economy was heading downward due to sluggish export demand, rampant inflation, and violent labor disputes. The Park regime did not survive: President Park was assassinated on October 26, 1979, by the chief of the Korean Central Intelligence Agency. The downfall of an almost absolute power created a huge vacuum in both political and economic life in Korea. In the following year, the Korean economy recorded a negative growth rate of real GNP (-3.7 percent) and the division of the main opposition party created another classical set-up for military intervention.

In retrospect, no one can deny that President Park became a developmentalist leader[13] and achieved his goal of industrializing the South Korean economy. As summarized in table 1, the economy grew at an average rate of 9.2 percent with inflation averaging 18.5 percent. The economy followed a route of high-pressured extensive export-led growth. Even though the Park government was closely connected with large enterprises and business groups, it promoted competition among them by allocating bank loans through government-controlled banks.

However, the insulation of the development-minded policy elite from politics is only a necessary condition of a developmental state, not a sufficient condition. As Bardhan[14] noted properly, large-scale technocratic development projects directed from above by an insulated modernizing elite were far removed from domestic realities and quickly became white elephants. The downfall of the Park regime was accelerated by inefficient resource allocation. It is evidence for the view that while an authoritarian regime can foster growth, it creates its own limitation. Only democratic institutions can work in the interest of the general public. It is for this reason that we do not observe any single industrial nation with a dictatorship.

In the aftermath of President Park's sudden death, a military group consolidated power and its leader, Mr. Doo-Hwan Chun, became president by another indirect vote after suppressing violent demonstrations in Seoul and Kwangju against the military intervention.

When President Chun began his presidency in 1981, he had to face the same situation President Park had faced two decades ago. The economy was in deep recession with hyperinflation and his regime had to establish political legitimacy. He relied heavily on experienced bureaucrats and supported them in their efforts to carry out a package of stabilization policies. The inflation rate came down and the economy was put back on a sustained growth path. Again the authoritarian regime managed to insulate bureaucrats successfully from politics.

During the Chun regime, the Korean economy went through a significant structural change. A revitalization plan for heavy industries was carried out, streamlining some of the inefficient enterprises. At the same time, major conglomerates started investing in more technology-intensive industries such as semiconductors and automobiles. A series of import liberalization plans were initiated and the industrial policy changed from a direct industry-specific support system to an indirect functional support system (for example, providing tax incentives for investments in energy-saving equipment). In other words, the Korean economy was changing from an extensive growth mode to an intensive growth mode. The latter mode puts more emphasis on productivity growth and quality upgrading of products while the former mode basically depends on the quantitative expansion and accumulation of factors.

Even though President Chun was not popular at all, he must be credited for not exercising further military intervention near the end of his presidency and for ending his single term as he had promised. Somehow he paved the way for the subsequent democratic transition.

President Roh was elected in 1987 by popular vote, taking advantage of divided opposition parties. During his presidency, he was also far from being a popular president but initiated a series of democratic transitions. His military background clouded his image of being a president elected by popular vote. However, his presidency can be viewed as a bridge between the authoritarian regimes of Park and Chun and the current civilian president, Kim. In this regard, economic development and the democratic transition in South Korea during the last three decades seems to have been causally related as Huber, Rueschemeyer, and Stephens[15] argued in the context of endogeneity of democracy.

The macroeconomic performance during the early years of the Roh presidency was quite satisfactory even though it was mainly helped by low oil

TABLE 1
Major Economic Indicators during Authoritarian Regimes: South Korea (1954–1992)

President Period	Rhee 1954–61	Park 1962–79	Chun 1981–87	Roh 1988–92
(1) Growth Rate in Real GNP	4.0 (2.7)	9.2 (3.3)	9.7 (2.9)	8.3 (2.6)
(2) Growth Rate of GNP Deflator	22.1 (19.3)	18.5 (6.2)	6.2 (4.6)	7.9 (2.5)
(3) Balance of Payments: Average Current Account Balance in millions of U.S. dollars	–2.0	–309	473	741

Note: 1) The figures in parenthesis are standard errors of the growth rates.
Source: The Bank of Korea, National Income Account (1988) and National Accounts (1990) (1992).

prices, low international interest rates, and the depreciation of the dollar against the yen. As shown in table 1, the average annual growth rate of real GNP was 8.3 percent with an average inflation rate of 7.9 percent. The current account surplus reached 14.2 billion dollars in 1988 and 5.1 billion dollars in 1989. However, it turned into a deficit from 1990 due to macroeconomic mismanagement.[16]

The significance of the Roh regime in the causal development between economic growth and democracy lies in the fact that economic growth can be sustained under a weaker authoritarian regime or in a period of democratic transition. It survived in the most violent period of wage inflation[17] and labor disputes.

THE LIPSET PHENOMENON IN SOUTH KOREA

The remarkable economic growth in South Korea under the authoritarian regimes brought about a Lipset phenomenon. As a result of late but rapid industrialization, there emerged a balance of class power between the capitalist group and the working and the middle classes that is the core of democratic transition.

The major indicators of structural change between 1965 and 1991 are summarized in table 2. The share of Machinery and Transport Equipment in total merchandise exports increased from 3 percent to 38 percent, which is a clear indication of manufacturing-based export-oriented growth. The secondary school enrollment rate increased from 35 percent to 87 percent, signaling the emergence of the power of the working class and the middle class through dissemination of information and knowledge. As a consequence, the wage differential, measured by the ratio of administrative manager wages and production worker wages, declined from 3.59 in 1971 to 2.58 in 1989.

The emergence of the working class is evident by looking at both urbanization and unionization rates as summarized in table 2. The share of compensation of employees in national income at factor cost increased from 30.1 percent in 1965 to 60.5 percent in 1991, which is further evidence of the emerging working class. The trend in income distribution is mixed. It improved according to data from the urban workers' household income and savings market survey but deteriorated according to data from urban family expenditure. The discrepancy might have been due to the usual omission of capital gains and property income in the family income survey. An improved income distribution indicates the emergence of the middle class. At the same time, a deteriorated distribution of family expenditure also indicates the emergence of the middle class, particularly self-employed professionals and proprietors who tend to report taxable income less than actual income.

Another requisite of democratic transition is the changing nature of economic and geopolitical dependence. Huber, Rueschemeyer, and Stephens[18] regard the transnational structure of power as a relevant element for the chances of democracy. They have argued that the international economy and system of states shape the balance of class power and the balance of power between state and civil society and constrain political decision making. They also have argued that dependency can have long-term effects on the structures of class and that war and geopolitical factors can strengthen the role of the security forces. They expected dependency to be an important factor but one without a clear-cut, unequivocal effect.

The changing nature of dependency in South Korea has been examined by the author.[19] Its economic dependence was examined in the context of trade, technology import, and investment. South Korea has pursued export-led growth by depending on Japan and the United States as both major trading partners and technology suppliers. In particular, it depended on the United States as the largest export market and on Japan as the largest import source of goods and technology. However, the degree of economic dependence has declined significantly over time. As shown in table 3, the share of the U.S. market in total exports has declined from 47.3 percent in 1970 to 23.2 percent in 1991. Over the same period, the share of imports from Japan declined form 41.0 percent to 25.9 percent. The share of the United States and Japan in total technology imports declined from 87.5 percent during the period of 1962–1976 to 75.8 percent during the period of 1977–1991 in terms of number of contracts. The same share in total amount of technology import contracts declined from 82.2 percent to 78.9 percent between 1962 and 1976. It is also noted that the share of U.S. technology in both number and amount has increased while that of Japanese technology has declined between 1977 and

TABLE 2
Major Indicators of Structural Change: South Korea

	1965	1991
1. Industrialization		
Share of Manufacturing in GDP (%)	18	28
Share of Merchandise Exports (%)		
Machinery and Transport Equipment	3	38
Other Manufactures	56	55
2. Education: Enrollment Rate (%)		
Secondary	35	87
Tertiary	6	39
3. Urbanization		
Share of Urban Population (%)	32	73
4. Share of Compensation of Employees to National Income at Factor Cost	30.1	60.5
5. Income Distribution: Gini Coefficient		
Urban Workers' Household Income	0.341[1)]	0.304[2)]
Savings Market Survey	0.444[3)]	0.297[2)]
Urban Family Expenditure	0.290[4)]	0.333[2)]
6. Wage Differential by Occupation		
Administrative Manager Wages/ Production Worker Wages	3.59[5)]	2.58[6)]
7. Unionization		
Union Members (1,000 persons)	302	1,803
Total Number of Employees	2,609	11,287
Unionization Rate (%)	11.6	16.0

Notes: 1) For 1963; 2) For 1990; 3) For 1967; 4) For 1966; 5) For 1971; 6) For 1989.
Sources: The World Bank, *World Development Report* (1990), (1993); Economic Planning Board, *Urban Family Expenditure Yearbook* (each year); The Bank of Korea, *Savings Market Survey* (each year); The Bank of Korea, National Accounts (1990), (1991); The Ministry of Labor, *Occupational Wage Survey* (each year).

1991. In general, we can argue that South Korea's trade dependence has declined significantly but its technology dependence continues to exist.

On the investment dependence, we may refer to Tharakan[20] who estimated the share of multinational companies' export in total manufacture exports of newly industrializing economies. The share in South Korea (27.8 percent) was lower than Singapore (90 percent), Mexico (45 percent), and Brazil (43 percent). Since the authoritarian regimes allocated credit via state-controlled banks as an important means of controlling the business sector, they preferred syndicated bank loans to foreign direct investment and multinational enterprises. Therefore, the investment dependence has not been of significant concern in South Korea.

While economic dependency has been reduced to a significant extent as a result of export-led growth, geopolitical dependency seems to remain as it did

TABLE 3
Trade and Technology Dependence: South Korea (1971–1991)
%

	Trade				Technology Import			
	Export Share		Import Share		Share in Number of Contracts		Share in Amount of Contracts	
	1970	1991	1970	1991	1962–76	1977–91	1962–76	1977–91
U.S.	47.3	25.8	29.5	23.2	21.8	26.9	26.1	48.1
Japan	28.3	17.2	41.0	25.9	65.7	48.9	56.1	30.8
Others	24.4	57.0	29.5	50.9	12.5	24.2	17.8	21.1
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Sources: The Bank of Korea, *Economic Statistics Yearbook* (selected years); Korea Industrial Technology Association, *Technology Import Report* (1992).

in the past. It has been the main aspect of dependency that has affected and constrained the political decision making of the past authoritarian regimes. Even with the end of the cold war, geopolitical dependency in South Korea did not change significantly and the nuclear issue with North Korea has constrained domestic policies. While there is increasing demand for welfare and social overhead capital, the defense and security budget has not been reduced. The tension with North Korea and the uncertain prospect for unification will continue to influence the future course of South Korea's democratic transition.

DEMOCRATIC TRANSITION AND SOCIOPOLITICAL REFORM

Even though former President Roh was elected by direct popular vote under a new constitution, his military background and the fact that President Chun hand-picked him as his successor obscured the legitimacy of his government. However, the current President Kim had won last year's presidential election against two prominent candidates, Dae Jung Kim, long-time opposition party leader, and Joo Young Chung, the owner of Hyundai business group who had no military background. Therefore, the current government is called the first civilian government since the Rhee government three decades ago.

In fact, the restored legitimacy seems to have provided President Kim with confidence in carrying out a series of sociopolitical and economic reform since his inauguration in February 1993. He introduced the asset registration system of public officials, including ranking officials in the administration, judicial system, and the assemblymen. A series of investigations led by the Justice Department resulted in the purge of several prominent assemblymen, bureaucrats, and generals who are believed to be beneficiaries of the previous authoritarian regimes.

Even though President Kim's campaign for sociopolitical reform has been quite popular among the public with an approval rating well over 70 percent, he has been confronted by explicit or at time implicit resistance by built-in political interest groups. Even within the ruling party, genuine supporters of his reform campaign belong to a minority group because the majority of assemblymen in the party were hand-picked before, either by President Chun or President Roh. Most ranking bureaucrats and military officers were those who were favored and raised under three decades of authoritarian regimes. Since President Kim had won a power struggle against the majority of Roh followers, his personal popularity does not seem to be well backed up by organized political forces.

Some have argued that his campaign for reform aimed against his political adversaries. Others have argued that his reform is doomed to fail because it is basically a negative campaign, not a positive one. In other words, they have claimed that the new government aims at disabling interest groups with veto powers from doing what they should not but does not enable them to do what they should. However, it must be pointed out that the interests of favored groups under authoritarian regimes of three decades have been rooted so deeply that it seems extremely difficult to pursue both democratic transition and sociopolitical reform simultaneously.

President Kim declared that he would not accept any political contributions from business and that he would pursue revisions of the political funds act and the political party act. In August 1993, he introduced a real-name system in all financial transactions by an emergency presidential order. In the past, anyone could hold an account at banks under a fictitious or borrowed name if he or she wanted to withhold sources of income and maintain confidentiality. Since a combined income tax system has not been introduced yet, interest income has been taxed separately. Even though such a system was not a transparent one, it has helped in channeling funds in the unorganized curb market into savings in financial institutions. The reform of the apparently non-transparent system into a "real-name system" was conceived in the early 1980s during the Chun administration but actual implementation has been delayed due to politicians' and business interest groups' lobbies against it. The Roh administration had once planned to implement it but gave up due both to intensive lobbies and the uncertainty about its effects on the economy.

At the initial stage, there was much concern about the potential impacts of the real-name system on the economy, which had been already in recession. Quarterly real GNP growth rates during the first two quarters of 1993 (3.4 percent and 4.2 percent) were much lower than those during the corresponding periods of 1992 (7.4 percent and 5.9 percent). Some speculated that there would be a financial crisis in October because medium- and small-scale industries and retail proprietors who relied on the private loan (curb) market would not be able to finance their businesses.

In fact, South Korea is the first developing country that introduced such a system. Knowing that even Japan has not introduced a full real-name financial system yet, such worries could not be ignored. However, as it turned out, there was no financial crisis and, instead, the stock price index has jumped from 650 to 800 since the system was put into effect.

The real-name financial system may not solve all the problems but may facilitate further reform and help democratic transition. The alliance between political power groups and big business has become more difficult to operate and the contribution of political funds will have to be more transparent than before.

The sociopolitical reform initiated by the president has gained overwhelming popularity with the public who have been discontent with the abuse of power and wealth accumulated and exercised by a few beneficiaries of past authoritarian regimes. However, public support will continue if and only if their economic well-being improves. As Bardhan[21] writes, if the rate of economic development in a democracy is too slow to meet the ever-widening circle of democratic awareness and raised aspirations among the people, the resulting demand overload may endanger the survival of democracy. In addition, the organized apparatus of the state is not necessarily for drastic reforms. Therefore, unless there emerge organized political groups and bureaucrats who can actively support the president's campaign, the prospect for the success of reform programs is quite uncertain.

Barro[22] could find in the entire world only three countries, Chile, South Korea, and Singapore, where dictatorships were not hostile to private property. Indeed, the past authoritarian regimes in South Korea have protected capitalist property from private encroachments by organized workers and landless peasants. There was an implicit alliance between the military and the capitalists through the authoritarian regime that somehow promoted economic growth. Now that a democratic transition is settling in, insecure capitalists are hesitant in making investment decisions. The task ahead is to combine capitalism with democracy and safeguard property rights while promoting development against increasing demands for equal distribution and social welfare.

Harberger[23] estimated private after-tax rates of return on capital in selected countries and called South Korea (15.2 percent) an "outlier" in comparison with other countries: the United States (7.6 percent), West Germany (5.6 percent), the U.K. (4.4 percent), and Canada (6.4 percent). However, according to my recent estimate,[24] South Korea is no longer an "outlier." Its private after-tax rate of return had declined from 15 percent in 1971 to 6.3 percent in 1991: a convergence toward the level of industrial nations. Therefore, with rising wages and falling rates of return on capital, South Korea must face slower growth but increasing social demands.

SUMMARY AND PROSPECTS

In the present chapter, I have reviewed economic development in South Korea under authoritarian regimes. The insulation of the development-minded decision makers by the authoritarian regime from the ravages of distributive politics and the inevitable lobbies of group predation has been one of the most important factors for the success of economic development. The protection of property rights by the regime was another contributing factor for sustained private investment. In addition, more egalitarian initial wealth distribution[25] and more mobility of social status by means of education have also provided the state with a conducive environment for rapid development.

However, such authoritarian development lacked autonomy and participation of the people. When things go wrong, authoritarian regimes are less likely than democracies to survive, as noted by Przeworski and Limongi.[26] The downfall of the Park regime occurred not by accident but by the limitations of authoritarian development.

As a result of authoritarian economic development, there appeared a Lipset phenomenon in South Korea. We have examined the phenomenon in the context of the emergence of the working and the middle class and the changing structure of dependency. The democratic transition had been far from smooth, costing the state violent demonstrations and labor disputes. In a genuine sense, the democratic transition has just begun with President Kim who had been a prominent opposition party leader but was elected by last year's popular vote.

Lastly, we have also reviewed President Kim's campaign for sociopolitical reforms and the difficulties with such reform programs. To make these reform programs a success, the current regime needs to provide leadership in resolving collective action problems. Bardhan points out "this leadership has two aspects: formulating cohesive developmental goals in line with a nation's collective aspirations and, more importantly, avoiding prisoners' dilemma-type deadlocks that can occur in the pursuit of even commonly agreed upon goals."[27]

The success of the current democratic transition will depend on two aspects of sociopolitical change. The first is how to reorganize political groups and bureaucrats who have been proponents of democracy and supporters of the sociopolitical reform programs and mobilize them in implementing collective action programs. The second is how to transform the cause of political pluralism and the raised expectations of the working and the middle classes into an engine for renewed growth. In this regard, we are back to a classic proposition of whether democracy fosters or hinders economic growth. If Korean society can endure a slow and at times exasperating process of democracy and constrain itself to act in the general interest, it will succeed in completing the combination of capitalism and democracy. However, it it fails to do so, we will have further evidence to the claim that capitalist democracy was a part of history that may not be repeated.

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11. Ibid., p. 46.
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13. Ibid., p. 65.
14. Bardhan, p. 47.
15. Huber, et al., op. cit.
16. See H. K. Pyo, "Combined Terms-of-Trade Shocks and Structural Adjustments in a Rent-Seeking Economy: Korea, 1985–1989," in Academic Studies Series, *Joint Korea-U.S. Academic Symposium on Impact of Recent Economic Developments of U.S.-Korean Relations and the Pacific Basin,* (Washington, DC: Korea Economic Institute of America, 1991).
17. The average growth rate of monthly earnings in all industries during the period of 1987–1991 was 16.6 percent while that of value-added labor productivity was 10.4 percent.
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2 MALAYSIA: THE ANXIETIES OF SUCCESS

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AN ECONOMY AS PERSPECTIVE

The concept of economics is a prism imposed on the Malay world by the West, an attempt to displace the spectacles of religion and ancient culture that gave breadth and depth to life in those fifteenth century islands. Some in that world shed spectacles for prism, some did not, many kept both. But since some views of the world were changed, all were changed. Westerners—the British in Malaya—reshaped all human relationships in this context. Where the Malay did not fit the Western economic mold, the British simply placed the Chinese or the Indian. For 200 years the British perspective shaped economic policy and structure in Malaya. At the end of the era the Malayan economy was an appendage of the British economy, an outgrowth of the land rather than its people, and ill-prepared for the even newer dreamscape presented by the internal post-Western challenge of Marxism-Leninism. In the years of turmoil after World War II, Malaya remained a soil-based economic entity where prosperity remained directly tied to what Mother Nature had provided.

Emerging from colonial domination as an economic novice along with most of the developing world, Malaya (Malaysia after 1963) made its initial attempts at industrialization only in the late 1950s, after independence in 1957 and following a 1955 World Bank report, which had recommended import substitution as the appropriate tack under mild protection, backed by investment incentives. Heavily reliant on exports of tin, rubber, and other primary commodities, Malaysian GNP growth was 4.8 per annum in the 1960s.

Recognizing early the dependence on primary products, the Pioneer Industries Ordinance of 1958 offered specific incentives to stimulate investments in manufacturing in Malaya. The focus in this initial stage was primarily on the production of consumer goods. A radical shift from an inward-looking defensive industrialization strategy of import substitution to an outward-looking aggressive strategy of export promotion took place after 1968 and the Investment Incentives Act of that year. Export allowances and acceleration of depreciation were a part of the process introduced.

But the muddy economic roads traveled in the heady first decade of independence left what would become a bloody residue of imbalance in wealth and health in Malaysia. While the Chinese population had prospered in the laissez-faire atmosphere of the 1960s, Malays had not. When Chinese political gains in the 1969 West Malaysia election threatened to give Malaysian Chinese dominance in both business and politics, economic frustration was translated into street fighting and then military suppression. Government intervention in halting ethnic conflict was followed by equivalent intervention in social and economic policy.

The establishment of free trade zones beginning in 1971 reflected the onset of the New Economic Policy (NEP), a 20-year plan designed to redistribute equity from primarily foreign hands into *bumiputera* (indigenous peoples, primarily Malays[1]) hands. Under the NEP and in the effort to bring Malays more fully into the mainstream of the economy, manufacturing became the leading sector, growing at an average rate of 12.5 percent a year and commanding 20.5 percent of GDP in 1980.

The generation of employment in manufacturing was impressive, expanding 7.6 percent a year to reach 15.8 percent of all employment by 1988. Employment of Malays in non-agricultural sectors expanded. By 1980 Malay unemployment dropped from 8.1 to 5.1 percent of the Malay workforce. By 1980 the share of agriculture, forestry, and fishery decreased from 30.8 to 22.2 percent of GDP, while the services sector expanded, especially government services. GNP growth averaged 7.8 percent a year in the decade. Its stimulus was public expenditure, investment, and exports (commodities and oil).

In the same period, fixed public investment rose from 6 to 11 percent of GNP; public consumption increased from 16 to 18 percent of GNP; overall government expenditures, including those from public corporations, accounted for nearly one-third of GNP growth. Private investment rose from 13 to 19 percent of GNP. Exports expanded from 45 to 62 percent of GNP, as crude oil, copper, palm oil, and manufactures led this expansion. Manufactures were increasingly important in the last year of the decade. Most importantly, the incidence of poverty fell from 49 to 29 percent of all households. This was a major achievement.

The second oil shock of 1979 and the world recession of 1980–1982 hit Malaysia hard, particularly in exports of commodities. The value of exports dropped below that of imports in 1981. The combined current account deficits for 1981 and 1982 averaged almost 12 percent of GNP. Government budget deficits in 1981 and 1982 were enormous. Austere budgets were imposed in 1982, 1983, and 1984. Per capita real private consumption fell by 9 percent in 1980–1982. Living standards fell but were lower in rural areas because of depressed agricultural prices. The state of the global economy was about to undermine the progress already made for *bumiputera* and negate the impact of the NEP on social reform.

This was the atmosphere in which the Heavy Industrialization Scheme was launched, based on import substitution to develop industries utilizing Malaysian energy and raw material resources. The 1981–1983 period also saw the launching of the "Look East" policy based on selective emulation of the Korean and Japanese models for commercial management and organizational behavior. The target of the policy was the Malays, with a government hope and intention that some of the sense of order and drive found in those models could be imparted to a new Malay entrepreneurial class.

In pursuit of a corrective strategy, Malaysia resorted to fiscal conservatism beginning in 1984. Negative growth occurred in 1985 but GNP growth resumed in 1986, reaching 5.4 percent in 1987, 8.9 percent in 1988, 8.8 percent in 1989, and 10 percent in 1990. Inflation in the second half of the 1980s was also low, ranging from 0.4 to 2.8 percent in 1989. By 1990, real GNP had increased seven-fold since 1960. Ninety-six percent of all children were completing at least six years of schooling. By 1991, agriculture's share of GDP had declined to 20.4 percent (from 30.8 percent in 1970). Manufacturing rose to 25.1 of GDP (from 13.4 percent in 1970). Per capita GDP income was $2,000 in 1990 (from $500 in 1970). Nevertheless, the real mean income of Chinese in 1989 was 65 percent higher than that for Malays.

The economy has been very open and subject to international economic fluctuations. There are structural problems; the base of the economy still is concentrated in a handful of commodities, which exert a powerful influence on it. While the manufacturing sector has grown well it also is focused on only a few products (electronics and textiles). Much manufacturing is in the hands of multinationals, some of which have little local involvement. There is a growing labor shortage. Macroeconomic management is generally sound but there are weaknesses that stem from political interference (such as in protected heavy industry). Budget deficits have been large by Asian standards. External debt is relatively heavy by NIE standards. Ethnic rivalries still color virtually every aspect of national life. But the NEP survived and so did the image of Dr. Mahathir's guiding hand. *Bumiputera* made measurable and visible economic gains.

Communal leaders have behaved in a reasonably pragmatic and responsible fashion to avoid disturbing racial harmony and political stability during this period. Chinese and Malays are determined to avoid race riots such as occurred in 1969. Important structural changes are underway with both the manufacturing and primary sectors being upgraded through R&D efforts. Malaysian palm oil was the savior of the economy in the 1980–1982 recession and it holds a virtually unassailable comparative advantage in upstream production, refining, and downstream manufacture of high-value products. Downstream value-added is the focus of great R&D effort in Malaysia today.

Significant industrial restructuring is taking place in the manufacturing sector. There has been a shift from labor-intensive to capital-intensive industry, both in technology and human capital. Mohamed Ariff, in his book, *The Malaysian Economy: Pacific Connections,* makes some of these same observations and suggests that "(i)n the long run, the Malaysian manufacturing sector may entrench itself in resource-intensive industries which also happen to be capital-intensive, technology-intensive, and skill-intensive as well" (chemicals, tire manufacture, food-processing, and wood-based industries).

Malaysia is likely to join Korea, Taiwan, Hong Kong, and Singapore as an NIE before the year 2000. This does not thrill many Malaysians who fear this may mean the loss of GSP and other trading advantages Malaysia now enjoys. Malaysia is well-placed in the Pacific economy to enjoy the advantages of Pacific Rim growth, while retaining its economic and commercial ties with the West and continuing its ventures in South-South cooperation, particularly in Southern Africa. Most importantly, Malaysia is in a position to divide a growing economic pie among its competing ethnic groups. Political will and political capability, not economic resources, are the issue in determining equity.

INTO THE GLOBAL ECONOMIC COMPLEX

Malaysia has become an example in the political theory literature of the context within which a consociational democracy can serve to stabilize an otherwise conflictual political system that is afflicted by fundamental ethnic differences, which in turn might be exacerbated in a simple majority-rule system.[2] Malaysia's ethnic/economic circumstances are unique and the solutions that have been employed to bring the society through the traumatic years of the 1980s and 1990s, as successful as they have been, probably will not serve as an example to other national social systems. In the face of ready contributions of criticism and complaint, the Malaysian government has adopted an offensive strategy as the best approach to a good defense.

Malaysia has unabashedly taken the lead in what the *Far Eastern Economic Review* has called a "new East-West confrontation"[3] over differing Asian and Western approaches to human rights. Washington and the West have been accused of trying to impose alien values derived from "post-Renaissance liberal western traditions." Prime Minister Mahathir Mohamad has accused the West of seeking to use human rights policy to create dependency, "This is what the West wants—not democracy, not freedom, not human rights," the prime minister said in a recent speech.[4]

Prime Minister Mahathir pointedly did not attend the November 1993 Asia Pacific Economic Cooperation (APEC) Ministerial meeting in Seattle because the United States had previously opposed his concept of a subregional East Asian Economic Caucus. Mahathir and Malaysia were portrayed in the Western press as out of step. Meanwhile, the Kuala Lumpur Stock Exchange continued to soar and Malaysia will apparently register 8 percent or so economic growth again this year. The Malaysian economic example was cited by the Chilean finance minister in a November 24, 1993, *Washington Post* ar-