# East Asian ‘miracle’ economies I

- The Original Five: Japan and the Four first-tier NICs (Newly-Industrialising Countries)
  - South Korea, Taiwan, Singapore, and Hong Kong
- The Second-tier NICs: Malaysia, Indonesia, and Thailand
- China

- Moreover, differences between the Original Five
- Hong Kong needs to be distinguished from the others
  - It has largely pursued a free-market, free-trade policy, although all the land is publicly owned and there is a substantial public housing programme.
  - It is not a country, like the others, but has always functioned as a city in a bigger entity – first of the UK and then of China.

# East Asian 'miracle' economies II

- Among the other four, Singapore is also quite different.
  - It has practised free trade and relied heavily on TNCs.
  - However, it is not a case of laissez-faire like Hong Kong, because TNCs were attracted through very targeted industrial policy, providing not just tax advantages but also custom-designed infrastructure and skills.
  - At 22% of GDP, Singapore has one of the biggest SOE sectors in the world
  - Almost all the land (87%) is publicly owned – the interesting point to note is that, going against worldwide trends towards privatisation in the last few decades, it has actually extended public ownership of land from 49% at the separation from Malaysia (1965) to 87% at present.

# East Asian ‘miracle’ economies III

- The other three – Japan, Korea, and Taiwan – are rather similar to each other.
- They all practised strong infant industry protection and very targeted industrial policy, while not relying on TNCs very much.

- However, there were also some differences between the three.
  - Taiwan had one of the largest SOE sectors in the world.
  - It is 16% of GDP today, but in the early days of its existence, SOEs were absolutely dominant in the industrial sector, as the Nationalist Party that ruled the country for the first half a century, believed in national ownership of key industries.

# East Asian 'miracle' economies IV

- However, there were also some differences between the three. **(continued)**
  - Japan had very few SOEs in the industrial sector after the Second World War (although it used them actively in the early days of its industrialisation in the late 19th century), while Korea took a middle road, using SOEs when it was deemed useful.
  - Japan and Korea were dominated by privately-owned conglomerates, while Taiwan's private sector had few large firms and were dominated by SMEs, with strong supports from the government in R&D.
  - SMEs were also strongly promoted in Japan, both by the government and by the large firms, which actively helped their suppliers upgrade their technologies.
  - In contrast, SMEs in Korea remain weak.

# Economic ‘miracle’ I

- Per capita incomes in East Asia grew at about 5-6% per annum during the ‘miracle’ years (roughly 1950-90, although the exact period differs across countries).
  - During the Industrial Revolution, today’s rich countries grew at between 1% and 1.4% per year in per capita terms.
  - During the ‘Golden Age of capitalism’ (roughly 1950-1973), their per capita income grew at around 3% per year.
- These rates of growth, if sustained over a long period of time, they can produce most remarkable results.
  - If you are growing at 6% for, say, 40 years, it means that your income will grow by something like 9 times.
  - If you are growing at around 2%, your income will barely double during the 40 year period.

**Table 1. GDP per capita Growth for Selected Countries**
(Annual Average Compound Growth Rates)

| | 1900-1950 | 1950-1987 | 1980-1990 | 1990-2000 | 2000-2010 |
|---|---|---|---|---|---|
| **"OECD"** | | | | | |
| Australia | 0.8 | 2.1 | 2.2 | 2.9 | 1.8 |
| Austria | 0.5 | 3.9 | 1.9 | 1.5 | 1.4 |
| Belgium | 0.8 | 2.8 | 1.9 | 1.7 | 1.0 |
| Canada | 2.0 | 2.0 | 2.1 | 1.9 | 1.0 |
| Denmark | 1.6 | 2.6 | 1.8 | 2.0 | 0.5 |
| Finland | 1.9 | 3.6 | 2.9 | 2.4 | 1.8 |
| France | 1.2 | 3.2 | 2.0 | 1.3 | 0.6 |
| Germany | 1.0[1] | 3.8[1] | 2.3 | 1.2 | 1.1 |
| Italy | 1.1 | 3.7 | 2.4 | 1.3 | -0.3 |
| Japan | 1.0 | 6.0 | 3.7 | 1.0 | 0.9 |
| Netherlands | 1.0 | 2.5 | 1.8 | 2.3 | 1.2 |
| Norway | 2.1 | 3.4 | 2.3 | 3.0 | 1.0 |
| Sweden | 2.0 | 2.7 | 2.2 | 1.4 | 1.6 |
| Switzerland | 1.9 | 2.2 | 1.4 | 0.0 | 1.1 |
| United Kingdom | 0.8 | 2.2 | 3.0 | 2.1 | 1.0 |
| United States of America | 1.7 | 1.9 | 2.4 | 2.2 | 1.0 |
| "OECD" Average | 1.3 | 3.0 | n.a. | n.a. | n.a. |
| **USSR** | 2.1 | 2.6 | n.a. | -4.6[2] | 5.7[2] |
| **Asia** | | | | | |
| Bangladesh | -0.1 | 0.3 | 2.2 | 3.2 | 4.3 |
| China | -0.3 | 4.5 | 9.1 | 9.2 | 10.2 |
| India | -0.1 | 1.7 | 3.7 | 4.2 | 6.6 |
| Indonesia | -0.1 | 2.5 | 4.5 | 2.5 | 4.1 |
| Pakistan | -0.1 | 2.2 | 3.7 | 1.2 | 2.8 |
| Philippines | 0.4 | 1.4 | -1.3 | 1.0 | 3.0 |
| South Korea | 0.1 | 5.5 | 7.9 | 4.7 | 3.7 |
| Taiwan | 0.4 | 6.1 | n.a. | n.a. | n.a. |
| Thailand | 0.1 | 3.5 | 6.3 | 3.3 | 3.6 |
| "Asia" Average | 0.0 | 3.1 | n.a. | n.a. | n.a. |
| **Latin America** | | | | | |
| Argentina | 1.2 | 1.0 | -2.1 | 3.0 | 4.6 |
| Brazil | 1.8 | 3.2 | 1.0 | 1.5 | 2.6 |
| Chile | 1.8 | 1.0 | 2.7 | 5.3 | 2.9 |
| Colombia | 1.7 | 2.1 | 1.6 | 1.1 | 3.0 |
| Mexico | 1.2 | 2.3 | -0.9 | 1.5 | 1.2 |
| Peru | 1.5 | 1.5 | -2.1 | 3.0 | 4.7 |
| "Latin America" Average | 1.5 | 1.9 | n.a. | n.a. | n.a. |

# Economic ‘miracle’ II

- in 1961, after a decade of ‘miracle’ growth, Japan’s per capita income ($402) was at the same level as that of Chile ($377), Argentina ($378), and South Africa ($396).
- In 2012, Japan’s per capita income ($47,870) is 6.3 times that of South Africa ($7,610), 5.7 times that of Argentina ($8,450 in 2010 – 2012 data not available), and 3.4 times that of Chile ($14,280).

- In 1961, Korea’s per capita income ($82) was similar to that of Kenya ($72) and 46% that of Ghana ($179), 41% that of the Philippines ($200), and 29% that of Mexico ($279).
- In 2012, Korea’s per capita income ($22,670) was 27 times that of Kenya ($840), 14.6 times that of Ghana ($1,550), 9.2 times that of the Philippines ($2,470), and 2.3 times that of Mexico ($9,740).

**Table 2. "Initial Conditions": Human Capital and Manufacturing Base**

| | 1961 per capita income (current $) | 1961 per capita MVA (1958 $) | Literacy Ratio circa 1960 | 1938 per capita MVA (1958 $) | Literacy Ratio circa 1945 |
|---|---|---|---|---|---|
| Indonesia | 49 | 3 (1958) | 47% | 4 | n.a. |
| Tanzania | 50 | 4 (1958) | 17% | n.a. | n.a. |
| Pakistan | 54 | 9 | 16% | n.a. | 18% (1951) |
| Zaire | 67 | 11 | 31% | n.a. | n.a. |
| India | 69 | 11 | 24% | 6 | 19% (1951) |
| Kenya | 72 | 12 (1958) | 20% | n.a. | n.a. |
| Korea | 82 | 22 | 71% | 9 | 22% (1945) |
| Thailand | 88 | 9 | 68% | 6 | 53% (1947) |
| Sri Lanka | 122 | 18 | 61% | 16 | n.a. |
| Taiwan | 122 | 23 | 54% | 12 | 50% (1950) |
| Brazil | 129 | 50 | 61% | 16 | 43% (1940) |
| Ecuador | 143 | 26 | 67% | 19 | n.a. |
| Ghana | 179 | 8 (1958) | 27% | n.a. | n.a. |
| Philippines | 200 | 16 | 72% | 13 | 52% (1948) |
| Malaysia* | 215 | 27 | 23% | n.a. | 38% (1947) |
| Mexico | 279 | 83 | 62% | 45 | 57% (1950) |
| Chile | 377 | 82 | 84% | 72 | 77% (1940) |
| Argentina | 378 | 114 | 91% | 98 | 86% (1947) |
| South Africa | 396 | 138 | 57% | 62 | n.a. |
| Singapore | n.a. | n.a. | n.a. | n.a. | 46% (1947) |
| Japan | 402 | 227 | 98% | 75 | n.a. |
| USA | 2308 | 926 | 98% | 375 | n.a. |

Notes: *Malaya

# The free market view

- "The East Asian economies succeeded through a free-trade, free-market system."
  - They 'got the prices right' – by keeping inflation low, liberalising international trade, welcoming foreign investment, liberalising domestic finance, keeping exchange rates at the right level.
  - The dominant view between the mid-1970 and the late 1980s
- These days, very few people believe this story in its pure form, but it is important to know this view, because more recent mainstream explanations are basically attempts to save the policy conclusions of the free market view, while recognising the existence of state intervention in East Asia.

# The free market view – evidence I

- Not supported by empirical evidence.

- **The extent of trade liberalisation has been highly exaggerated.**
- Average industrial tariffs were still 30-40% in the 1970s and 20-30% in the 1980s.
- There were many non-tariff trade barriers, such as quotas and domestic taxes that discouraged imports of luxury goods.
  – For instance, in Korea, up until the late 1980s, the domestic price of imported scotch whisky, whose tariff was only 100%, was over nine times that of c.i.f. price after various inland taxes, e.g., liquor tax, luxury consumption tax, and value added tax.

# The free market view – evidence II

- **The extent of trade liberalisation has been highly exaggerated (continued).**
- Strict foreign exchange rationing by the government, meant that often importing a certain item was impossible not because of high tariffs or quantitative restrictions, but because it was impossible to get the foreign exchange to pay for it (priority: capital goods – intermediate inputs – basic consumer goods – luxury consumer goods).
  - This makes the calculation of 'openness' based on tariff and tariff-equivalent of QRs meaningless.
- There were huge export subsidies, which are as distorting as protective tariffs, from the point of view of 'getting the prices right'.

# The free market view – evidence III

- **Financial markets were heavily regulated.**
- Domestic financial markets were highly regulated and the government directed where credits go (‘directed credits’.
  - The government owned all the banks in Korea until the mid-1980s while state-owned banks dominated in Taiwan until the late 1990s.
- Interest rates were artificially suppressed in order to encourage investment, but savings kept rising.
  - For example, in Korea, savings rate rose from less than 5% of GDP in the early 60s to around 25% of GDP in the late 1970s, despite the fact that real interest rates were negative during the whole period, except between 1965 and 1969, when Korea tinkered briefly with liberalised finance with disastrous consequences.

# The free market view – evidence IV

- **Financial markets were heavily regulated (continued).**
- Foreign capital flows were heavily regulated.
  - Short-term financial investments were prohibited until the 1970s and very heavily regulated until the early 1990s.
  - Key industries were closed off to foreign direct investments, majority foreign ownership of enterprises was banned in most industries (100% foreign ownership was allowed only in Export Processing Zones).
  - There were conditionalities related to export, technology transfer, and worker training.

# The free market view – evidence V

- The mainstream story that low inflation was behind the East Asian miracle is not supported by evidence either, at least in Korea.
  - Average inflation rates in Korea were 17.4% in the 60s and 19.8% in the 70s.
  - In the 60s, the average annual inflation rates were 1.3% in Venezuela, 3.5% in Bolivia, 3.6% in Mexico, 10.4% in Peru, and 11.9% in Colombia and 21.7% in Argentina.
  - The average inflation rates in the 1970s were 12.1% in Venezuela, 14.4% in Ecuador, and 19.3% in Mexico, 22% in Colombia, and 22.3% in Bolivia.

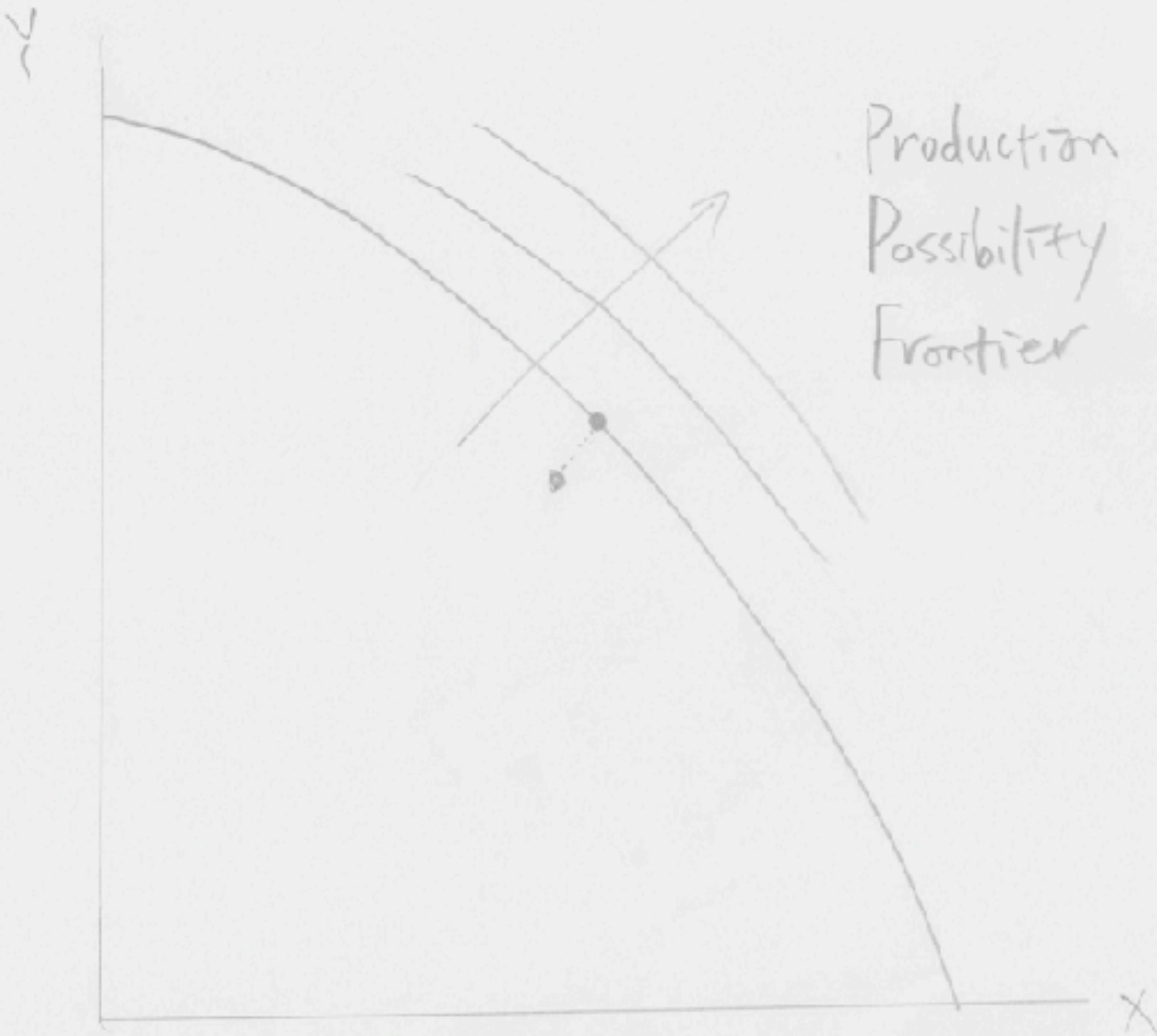
# The free market view – theories I

- Even if "liberalisation" in East Asia was as comprehensive as the proponents of free market story insist, it is not necessarily true that a "more market oriented economy" is more efficient, even in purely Neoclassical terms.

- As the theory of the Second Best tells us, removal of market distortions in some, but not all, markets does not guarantee that the economy achieves higher allocative efficiency.

# The free market view – theories II

- More importantly, the mere existence of “distortions” does not tell us anything about the dynamic performance of the economy.
- All that Neoclassical theory tells you is that an economy without price distortions will use its existing resources in the most efficient way.
- However, being “efficient” in the Neoclassical sense does not say anything on the changes in your resource availability, that is, growth, over time


Y
Production
Possibility
Frontier
X

# The modified views – Virtual free trade I

- This was first proposed by Little and Lal and subsequently adopted by the World Bank in its 1987 World Development Report.

- This theory argues that, in the East Asian countries there existed widespread price distortions due to one set of state interventions (e.g., import protection), but they were cancelled out by another set of interventions (e.g., export subsidies), thus resulting in a neutral incentive structure between production for export and production for the domestic market, which is expected under free trade.

# The modified views – Virtual free trade II

- The problem is that there is no reason why the structure of relative prices under this régime should be the same as the one under genuine free trade.

- What matters in determining the relative attractiveness between export and production for the domestic market is the *relative* price structure, and not the “average” incentives.

- Anyway, this theory in the end relies on the static notion of comparative advantage, and therefore has little to say on long-term, dynamic performance.

# The modified views – The EAM I

- In the *East Asian Miracle* report, the World Bank admitted that there are justifications for many "unorthodox" policies which it had denounced but had been widely practiced in East Asia (such as selective industrial policy and directed credit programme).
- However, despite such revisions, the *EAM* claims that, in the end, the Bank's free-market, free-trade policy package still remains the best of all developmental strategies.
  - Most of the non-orthodox policies used in East Asia – or what it calls Northeast Asia (the original five) are failures when you really get to know them more closely (e.g., industrial policy).

# The modified views – The EAM II

- However, despite such revisions, the *EAM* claims that, in the end, the Bank's free-market, free-trade policy package still remains the best of all developmental strategies. **(continued)**
  - And in those few instances where non-orthodox policies worked (e.g., directed credit programmes), they are too risky for other countries to try, because they demand a lot of institutional capacities (especially a competent bureaucracy
  - For this reason, the Southeast Asian economies, which used much fewer 'selective' interventions, are recommended as better examples for other developing countries.
  - The Report argues that developing countries should focus on getting what it calls the 'fundamentals' – like macroeconomic stabilisation, human capital investments and agriculture – right.

# The modified views – The EAM III

- Criticism I: The so-called fundamentals are too vaguely defined to be of practical use.
  - For example, what is meant by a "stable" macro-economy? – 0% inflation, less than 10% inflation, less than 40% inflation, or non-accelerating inflation whatever the level is?
  - Moreover, should macroeconomic stability measured simply by inflation rate – how about stability of output, employment, etc.?

- Criticism II: The fact that a country does not have the institutional capacity to implement a particular policy now does not mean that it should never try such policy
  - Indeed, the East Asian examples themselves show that institutional capacity itself can be changed through conscious policy actions.

# The productivity growth debate I

- Prompted by Paul Krugman’s 1994 *Foreign Affairs* article.
  - Growths in the East Asian economies can be mostly explained by increased inputs of capital and labour (or what he calls “perspiration”), rather than total factor productivity (TFP) growth, that is, growth in output that cannot be explained by growth in inputs of capital and labour (or “inspiration”).
  - Therefore, the East Asian economies would not be able to sustain their growth in the future, as diminishing returns sets in.
  - As only individualistic, free-market economies can generate enough innovation to sustain productivity growth, growth in the “collectivist” economies of East Asia will grind to a halt, as it did in the Soviet economies, which also had a period of rapid growth based on factor accumulation in the 1950s and the 1960s

# The productivity growth debate II

- TFP growth is not the same as technological progress or, even less what Krugman calls “inspiration”.
- It is a residual term in growth accounting, which even include measurement errors, and it is not obvious how we should interpret the TFP figures.

- If TFP truly measured an economy’s level of ‘inspiration’, how do we explain that, in Young’s study (on which Krugman heavily relies), countries like Bangladesh, Egypt, and Congo have higher TFP growth rates than all the East Asian countries?

# The productivity growth debate III

- TFP estimates for the East Asian countries vary widely, and it is not clear which of these are the "correct" estimates (Young and Kim & Lau that Krugman relies on are actually "outliers").

- Some recent studies (e.g., Collins & Bosworth) also suggest that over time TFP growths have accelerated at least in some East Asian countries (Korea and Singapore), so Krugman's assertion that these economies are inherently incapable of generating productivity growth becomes even more problematic.

# Interpreting the East Asian ‘miracle’ I

- The East Asian countries did just about everything ‘wrong’ according to mainstream, neoclassical economic theory, and all the attempts to reconcile the East Asian experience with neoclassical economics have failed.

- The obvious conclusion to draw, but a conclusion that most mainstream economists hate to draw, then, is that neoclassical theory is unable to explain economic development – an observation strengthened by historical evidence from other rich countries.

# Interpreting the East Asian ‘miracle’ II

- The East Asian development experience shows that economic development cannot be achieved by ‘getting the prices right’ in the neoclassical sense.

- It shows that, in order to develop their economies, developing countries need to defy the market signals and ‘get the prices wrong’, as Alice Amsden provocatively put it in her book on Korea, Asia’s Next Giant.

- “Defying the market” may sound radical, but it is something that is done by business managers all the time

# Interpreting the East Asian ‘miracle’ III

- Why did similar trade and industrial policies work so well in East Asia and not in other countries?

- **<u>1. Policy Differences</u>**
- The policies were similar, but not the same.
- The East Asian countries did certain things that others didn’t
  - emphasis on exporting, which enabled the producers to attain scale economy and get exposure to global quality standards
  - emphasis on R&D and training, which facilitated technology absorption and innovation
  - better regulation of FDI that maximised technology transfer and spill-overs.

# Interpreting the East Asian ‘miracle’ IV

- **2. Policy Realism**
- Although the final goals were often ambitious, the choice of strategic sectors were made only after careful considerations had been given to things like world market conditions and the development of local technological capabilities.

- **3. Policy Flexibility**
- Like any other businessman trying to move into new sectors, East Asian policy makers often made mistakes.
- However, they were quite willing to acknowledge mistakes and re-direct their policies if they did not work.

# Interpreting the East Asian ‘miracle’ V

- **<u>State Autonomy</u>**
- The East Asian states were willing and able to withdraw protection and other supports from industries whenever necessary (e.g., when the performance is lagging too much or when the industry has outgrown its need for protection), because they were highly autonomous, not beholden to private sector interests.
  - In this sense, a country whose state is not interested in productivity growth or not able to discipline the private sector may be better off not using East Asian style industrial policy, as the *East Asian Miracle* report argued.
  - However, it is possible to reform the state and increase its policy implementation capability over time, as indeed it happened in the East Asian countries themselves.

# Asian financial crisis (1997-8) I

- **Did the ‘East Asian model’ cause the crisis?**
- “The model provided explicit and implicit government supports to unviable industrial firms and banks that lend to them, eventually causing the crisis.”

- However, the crisis countries are actually not the countries that were usually associated with the East Asian model, except for Korea.
- Even in the case of Korea, we cannot say that its ‘traditional’ economic model caused the crisis, because it had abandoned that model by the early 1990s, by radically liberalising the financial sector and largely abandoning selective industrial policy.

# Asian financial crisis (1997-8) II

- **How about the underlying institutional structure?**

- **<u>1. Lack of transparency</u>**
- "Foreigners lent too much money to the Asian countries because there was a lack of transparency, which made it difficult for them to properly assess the risk."
- However, at least at the macro level, all the basic information that was needed to know was available (the BIS, George Soros).
- More importantly, it was already well-known that there was a lack of transparency at the corporate level in these countries, so the wise thing would have been not to lend to them.

# Asian financial crisis (1997-8) III

- **<u>2. The moral hazard argument</u>**
- “Foreign lenders lent too much because they thought that the Asian governments would bail out the troubled firms and banks, if things went wrong.”
- However, no evidence that there existed any exceptional government guarantee in these countries.
- Against this, some people counter that the Asian government bailed out a lot of banks and firms after the outbreak of crisis, which proves the existence of such guarantees.

# Asian financial crisis (1997-8) IV

- **<u>2. The moral hazard argument</u>**
- However, no evidence that there existed any exceptional government guarantee in these countries **(cont’d)**.
  - Such bail-outs were necessary in order to avoid a total collapse of the economic system, as we have witnessed in the rich countries after the 2008 crisis.
  - Actually the Asian countries closed a lot more banks and other financial institutions compared to what the rich countries have done since the 2008 financial crisis.
  - In the recent crisis, no bank in Britain was allowed to go bankrupt and only one major bank – Lehman Brothers – was allowed to go bankrupt in the US.

# Asian financial crisis (1997-8) V

- **2. The moral hazard argument**
- However, no evidence that there existed any exceptional government guarantee in these countries **(cont'd)**.
  - In contrast, following their crises, Indonesia had to close down 16 major banks overnight and Korea closed over 1/4 of financial institutions and nationalised many of them, thus wiping out the wealth of existing shareholders.
  - Unlike in the rich countries in the current crisis, many managers were severely punished in those countries – especially in Korea, many top managers of the failed banks ended up in prison for dereliction of duty.

# Asian financial crisis (1997-8) VI

- **3. Crony capitalism**
- "Some firms and banks were run by cronies of government leaders, making people think that they have no downside risk."

- However, this story is not very convincing.
- First of all, cronyism and corruption have been there all the time in the crisis-stricken countries, so it is difficult to explain why these things suddenly created the crises.
- Second, countries like Korea and Malaysia were perceived as being relatively uncorrupt by developing country standard.

# Asian financial crisis (1997-8) VII

- **<u>3. Crony capitalism</u>**
- However, this story is not very convincing. **(continued)**

- Third, if anything, corruption was perceived to be diminishing in all the crisis-stricken countries throughout the 1990s.
- Fourth, by definition, cronyism has to be restricted in scope – in order to be meaningful, cronyism has to be selective, so it can at best explain only part of the problem (e.g., all the 3,000-plus manufacturing firms that borrowed from overseas in Indonesia couldn’t have been cronies of Suharto).

# Asian financial crisis (1997-8) VIII

- Unregulated financial markets have a natural tendency to generate temporarily self-fulfilling expectations which are not sustainable in the longer run and do not need corruption or moral hazard created by government guarantees in order to generate crises.
  - The fact that the Scandinavian countries, probably the most transparent and clean countries in the world, had almost equally bad financial crisis in the late 80s and the early 90s proves this point.
- The post-crisis events also questions the orthodoxy.
  - In particular, Korea, which has adopted a neo-liberal model with a vengeance, has seen its growth rate falling (from 6-7% to 2-3% per year in per capita terms) and a significant rise in poverty and inequality.

# Drawing lessons from East Asia I

- “Whatever the merits of policies used in East Asia may be, they are of little relevance to other countries, as these countries are ‘special cases’.

- **<u>1. Size</u>**
- “Tiny countries, so easy to govern.”
  - In terms of population, Korea is the 12th biggest developing country, and Taiwan is about median size.

# Drawing lessons from East Asia II

- **<u>2. Ethnic Homogeneity</u>**
- "Ethnic homogeneity promotes social peace."
  - Hong Kong, Singapore: multi-ethnic
  - Japan: many minority groups (although small in numbers)
  - Taiwan: at least two groups (Mainlanders vs. Taiwanese)
  - Korea: regional rivalry

- **<u>3. Colonial Legacy</u>**
- "Japan's 'Developmentalist colonialism' gave good human capital stock and industrial bases to Korea and Taiwan.
  - True, but the extent was actually very minor (see table 2).

**Table 2. "Initial Conditions": Human Capital and Manufacturing Base**

| | 1961 per capita income (current $) | 1961 per capita MVA (1958 $) | Literacy Ratio circa 1960 | 1938 per capita MVA (1958 $) | Literacy Ratio circa 1945 |
|---|---|---|---|---|---|
| Indonesia | 49 | 3 (1958) | 47% | 4 | n.a. |
| Tanzania | 50 | 4 (1958) | 17% | n.a. | n.a. |
| Pakistan | 54 | 9 | 16% | n.a. | 18% (1951) |
| Zaire | 67 | 11 | 31% | n.a. | n.a. |
| India | 69 | 11 | 24% | 6 | 19% (1951) |
| Kenya | 72 | 12 (1958) | 20% | n.a. | n.a. |
| Korea | 82 | 22 | 71% | 9 | 22% (1945) |
| Thailand | 88 | 9 | 68% | 6 | 53% (1947) |
| Sri Lanka | 122 | 18 | 61% | 16 | n.a. |
| Taiwan | 122 | 23 | 54% | 12 | 50% (1950) |
| Brazil | 129 | 50 | 61% | 16 | 43% (1940) |
| Ecuador | 143 | 26 | 67% | 19 | n.a. |
| Ghana | 179 | 8 (1958) | 27% | n.a. | n.a. |
| Philippines | 200 | 16 | 72% | 13 | 52% (1948) |
| Malaysia* | 215 | 27 | 23% | n.a. | 38% (1947) |
| Mexico | 279 | 83 | 62% | 45 | 57% (1950) |
| Chile | 377 | 82 | 84% | 72 | 77% (1940) |
| Argentina | 378 | 114 | 91% | 98 | 86% (1947) |
| South Africa | 396 | 138 | 57% | 62 | n.a. |
| Singapore | n.a. | n.a. | n.a. | n.a. | 46% (1947) |
| Japan | 402 | 227 | 98% | 75 | n.a. |
| USA | 2308 | 926 | 98% | 375 | n.a. |

Notes: *Malaya

# Drawing lessons from East Asia II

- **4. Geopolitics**
- "Aid and 'special market access' given by the US to Korea and Taiwan, as 'garrison states' in the Cold War."
  - Exceptional levels of US aid in the 1950s, but not afterwards
  - Other countries with a lot of US aid made a mess of things (Philippines)
  - 'Special market access' is an urban legend.
  - Most importantly, being a client state of the US in the Cold War has had its costs
    - 6% GDP on defence (as opposed to 2-3% world average)
    - Young workers locked up in compulsory military service (2-3 years)
    - In the Korean case, destruction from the Korean War (1950-53) in the case of Korea – 50% of manufacturing facilities and 75% of railways destroyed

# Drawing lessons from East Asia III

- **<u>5. Culture</u>**
- "Confucian culture has made people work hard, save a lot, invest in education, and put up with authoritarian rule, thus promoting economic development."

- However, problems
- 1. Arguments invoking Confucianism are trying to explain a new phenomenon (economic development) with something that has been around for the last thousand years (Confucianism). (compare with Max Weber's 'Protestantism and the rise of capitalism' thesis, which is at least trying to explain one new thing – capitalism – with another new thing – Protestantism).

# Drawing lessons from East Asia IV

- **<u>5. Culture</u>**
- 2. Confucianism has many elements which are harmful for economic development.
  - The Confucian contempt for commercial and industrial activities was often blamed for the relatively poor East Asian economic performance in the 1950s.
  - Its emphasis on social hierarchy is routinely criticised for creating a conformist attitude, which discourages entrepreneurship (a basis of Krugman's thesis).

# Drawing lessons from East Asia V

- **<u>5. Culture</u>**
- 3. A lot of what you think are ‘cultural’ traits are recent creations.
- We all think that Japan has peaceful industrial relations because of its culture of harmony and cooperation, but this is only a relatively recent phenomenon (see the labour dispute figures in table 3).
  - The Japanese workers became peaceful only because the Japanese capitalists made a lot of concessions in terms of lifetime employment and company welfare schemes.

**Table 3. Number of Working Days Lost in Industrial Disputes, 1955-80**
(per 1,000 employees)

| | 1955-59 | 1960-64 | 1965-69 | 1970-74 | 1975-80 |
|---|---|---|---|---|---|
| Japan | 254 | 177 | 107 | 151 | 69 |
| USA | 615 | 301 | 513 | 539 | 389 |
| UK | 220 | 146 | 175 | 624 | 521 |
| France | 180 | 197 | 163 | 201 | 195 |
| Italy | 433 | 932 | 1,204 | 1,404 | 1,434 |
| West Germany | 47 | 23 | 7 | 55 | 41 |
| Sweden | 19 | 6 | 38 | 69 | 222 |

# Drawing lessons from East Asia VI

- **<u>5. Culture</u>**
- 3. A lot of what you think are 'cultural' traits are recent creations. **(continued)**
- In the early 1990s, Korea used to have literally the highest household savings ratio as a proportion of GDP (over 20%), making a lot of people claim that this was a manifestation of Confucian cultural trait of frugality.
  – Today, it has one of the lowest such rate (at 2-3%) in the world (Brazil 7-8%) – all thanks to financial liberalisation that made mortgage loans and consumer loans (credit cards, payday loans) freely available in the context of increasing job insecurity and a weak welfare state.

# Drawing lessons from East Asia VII

- **<u>6. Reverse Resource Curse</u>**
- "The East Asian countries had to develop their economies because they had 'reverse resource curse' of not being able to rely on natural resources."

- However, the 'resource curse' thesis itself is dubious.
- Many rich countries are resource rich (USA, Canada, Australia, New Zealand, Scandinavia), while some resource-rich developing countries have done well (Botswana, Malaysia)
- In the early 20$^{th}$ century, resource-poor Asia was shrinking while 'resource rich' Latin America and Africa were doing much better.

**Table 4. Historical Rates of Economic Growth by Major Regions during and after the Age of Imperialism (1820-1950)**
(annual per capita GDP growth rate, %)

| Regions | 1820-70 | 1870-1913 | 1913-50 | 1950-73 |
|---|---|---|---|---|
| Western Europe | 0.95 | 1.32 | 0.76 | 4.08 |
| Western Offshoots* | 1.42 | 1.81 | 1.55 | 2.44 |
| Japan | 0.19 | 1.48 | 0.89 | 8.05 |
| Asia excluding Japan | -0.11 | 0.38 | -0.02 | 2.92 |
| Latin America | 0.10 | 1.81 | 1.42 | 2.52 |
| Eastern Europe and former USSR | 0.64 | 1.15 | 1.50 | 3.49 |
| Africa | 0.12 | 0.64 | 1.02 | 2.07 |
| World | 0.53 | 1.30 | 0.91 | 2.93 |

*Australia, Canada, New Zealand, and the USA.

# Drawing lessons from East Asia VIII

- **<u>7. State Capabilities</u>**
- "Countries without high state capabilities should not use 'difficult' policies used by the East Asian countries" ("Don't try this at home.")
- However, Korea and Taiwan are actually excellent examples of how state reform can turn around even the most hopeless cases.

- The Kuomintang regime, which later engineered an economic 'miracle' in Taiwan, managed to lose mainland China despite massive Western support, because their ministers and generals were so corrupt and incompetent.

# Drawing lessons from East Asia VIII

- **7. State Capabilities**
- Korea in the 1950s was receiving a massive amount of US aid but produced pathetic results, prompting one American aid official to call the country a “bottomless pit”.
- Korea was sending its bureaucrats to Pakistan and the Philippines for extra training until the late 60s.

- The best way to cope with limited state capabilities in the long run is to increase them through state reform, not to try only ‘easy’ policies.

# Drawing lessons from East Asia IX

- **<u>Conclusions</u>**
- The East Asian economic success was not mainly due to some ‘special conditions’ that other countries cannot replicate.

- The East Asian countries succeeded because they followed the ‘wrong’ policies (that is, from the mainstream point of view) and put in place measures that are intended to enhance national productive capabilities – such as infant industry protection, control over short-term financial flows, regulations of FDI, and investments in R&D and training.

# Drawing lessons from East Asia X

- **Conclusions**
- This is not to say that structural conditions did not matter.

- But these countries could overcome many of those conditions exactly because they re-shaped their states and established the sense of national project through political measures, including repression, ideological exhortation, and restraints on the behaviours of the ruling elite.