

# The Role of Economic Development Strategies in Korea

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## 1. Introduction

Korea has very remarkable achievement in both economic and political development for the past 60 years. GDP per capital has increased from 80 dollars in 1960 to 22500 in 2012 and political system changed from an autocratic state to a more democratic society. There are not many countries which showed such an impressive achievement in last century..

This paper attempts to review the past 60 years of economic history and to show the main elements to bring such an excellent performance of Korean economy. And we focus that Korea's experience can be very useful when other developing countries try to take off economic development. Especially, we try to emphasize these experiences may be useful to the Asian developing countries because still many Asian countries struggle to take off and because Korea share many cultural and historical things together.

For this purpose, we show first the past experience of Korea's economic performance. We look at the several macroeconomic performance indicators such as GDP per capita or Inflation rate. And later we examine its development strategies and evaluate them. And finally we show the meaning lesson from these performance and strategies.

It is too obvious that we cannot cover all elements to contribute to the economic and sociological achievement in this short paper. Considering that so much volume of paper and books are written for these topics, doing this job in this short paper may look ridiculous. But we think this still very useful because still there are so many economists and politicians who do not clear idea of it.

This paper has four sections as follows. The first section is an introduction and the second one shows the reason why Korea's experience is so important in formulating economic development strategies of Asian developing countries. The third section tells the several important major strategies of Korean government which contribute to the rapid economic growth of Korea. The fourth section gives some valuable lessons which developing countries in Asia may take when to initiate development planning of their countries.

## 2. Why Korea's experience is important?

### 1) One of Asian countries.

Korea's experience is very important to the Asian countries which try to take economic development in 20s and 21 century simple because Korea belongs to Asia and Korea shares lots of common things with other Asian developing countries. For example, it has a long history of Asian culture and civilization. Many Koreans go to Buddhism Temple while others show great respect to Confucius. Almost all Koreans eat rice every day by using chopsticks. It has had a very long diplomatic relationship with neighboring other Asian countries such as China or Japan for thousand years. It met for the first time the western civilization very recently like other Asian countries and it was also once colonized in 20 century. Beside these, we may count thousand things that Korea share with other Asian countries commonly. The fact that Korea shares lots of common things mean that Korea may have the same advantages or disadvantages as the other developing countries when to take any development strategies As a result, Korea's experience may give more valuable lesson to other developing countries.

### 2) Starting under very miserable conditions

When we look at the modern history of Korea, it is quite surprising to know how miserable the Korea was at the earlier stage of development. Korea met the western civilization in 16th to 17th century for the first time, but it is in 1876 when Korea officially began to open its country to foreign countries. In 1910, Korea became a colony of Japan and finally became independent in 1945 as the WWII ended.

Afterward, Korea was divided into two parts of South Korea and North Korea and had experienced three years of civil war from 1950 to 1953. These three years of civil war destroyed most of infrastructure or private capitals such as machine and buildings. Especially, Seoul and its suburban area where most developed area in Korea is located are very heavily destroyed.

After the Korea was divided into two different regimes, the industrial inequality has been very serious. Most raw materials such as iron ores or coals were located in northern area of Korea. When North Korea cut the supply of electricity in late 1940s, South Korean firms or people had a very hard time..

While Korea was very dense and has enough workers in 1950s, its quality was very poor and the number of skilled workers is very limited. Most of them living in rural area only complete the elementary school.

Even Korea does not have enough food to feed its people up until 1970s. Rapidly growing population makes it difficult for a country to provide enough rice and other basic foods. It had to depend upon the food assistance from US or other advanced countries.

In addition, Korea had never been practicing economic development plan or democratic system before.

In conclusion, we may say that at the earlier stage of development, Korea was in the very miserable condition and finally overcome it later

Table 1 Major Historical Events of Korea

1876	Kingdom of Cho sun Opened to Foreign Country, Japan
1882	First Diplomat Relationship with A Western Country, US
1910	End of Kingdom and Colonized by Japan
1945	End of WWII, Liberalized
1948	Republic of Korea born
1950	Beginning of Korean War
1953	End of Korean War
1960	Student Revolution
1961	Military Coup
1962	First 5 year Economic Development Plan Begins
1970	New Village Movement Begins
1978	Reach 1,000 Per Capita Income
1986	Current Account Surplus for the First Time
1988	Seoul Olympics
1992	First Civilian President Elected in 30 years
1994	5 year Economic Development Plan Abandoned
1995	10,000 dollar income and Join to OECD
1997	Financial Crisis occurs and IMF assistance received
2001	Pay all of standby credit of 19.5 Billion dollars to IMF
2008	20,000 dollar of Per Capita Income

### 3) Excellent performance: from low to high income country

In early 1960s, Korea was one of the poorest countries in the world. The nominal GDP per capita in 1950s and 60 was only 70 to 80 dollars and its industrial structure belongs to the stereo types of developing countries. But as seen in figure 1, per capita

income of Korea increases to USD 22,500 in 2011 and its size of GDP ranks to the 9<sup>th</sup> in the world. The inflation rate which was 10 to 20 percent in 1960s and 1970s has been stabilized to less than five percent after 1980s.

#### 4) Medium size of the land and population

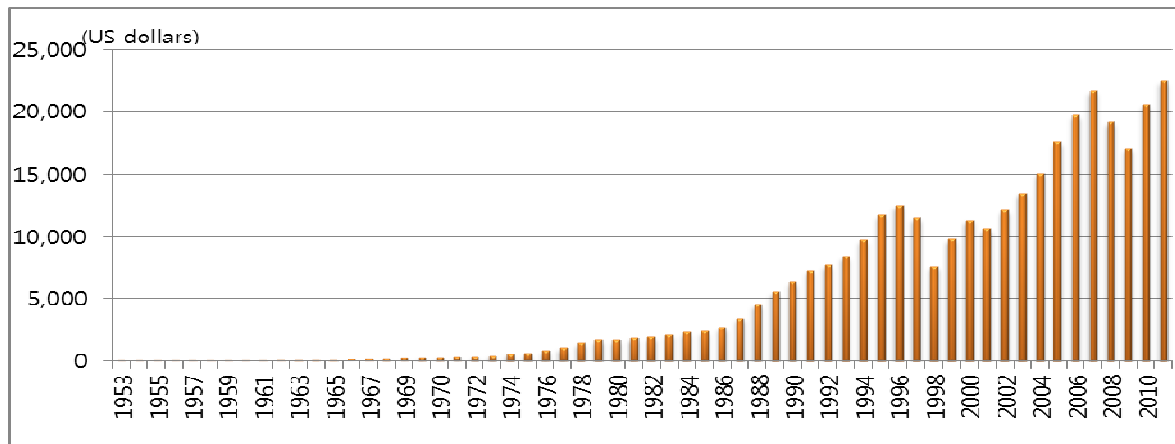
Korea has 99,000Km<sup>2</sup> of land and 49.8 millions of population in 2011. When it took off its economic development in 1960, its population was only 25 millions of population but later it has increased very rapidly. It is not a big country as China or Indonesia but not a small one as Singapore. We may say that it belongs to a group of medium sized countries like many Asian countries.

Korea had to take care of many problems related to this rapid change of population of development. For example, it has to solve the problem of urbanization or intensive dwellings for the past several 60 years. Providing proper education has been also one of the major challenges in Korea. Now most of Asian countries are having very similar problems and as a result, they may get some important lessons from what Korea had done for the past years.

#### 5) Political development

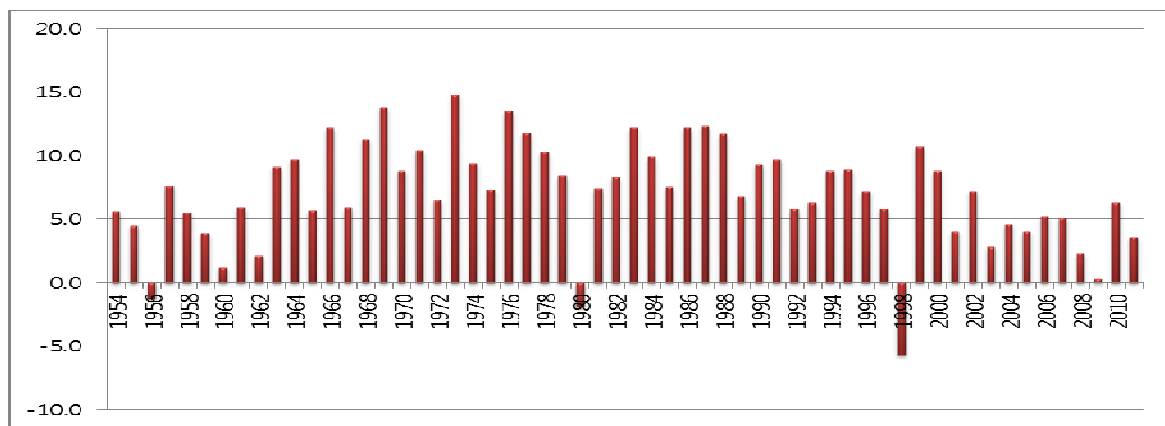
One of important characteristics of Korea's recent history is that it has achieved a political development as well as an economic development. Korea had never experienced a democracy in modern term until 20 century so that it has to spend time and resources to build its customized democratic society. While the republic was announced 1948, still dictator ruled the country until he was outcast by the student revolution in 1960. The third president who took power after the military coup of 1961 managed a less democratic regime and was finally assassinated by his own men 1979. The next two presidents from 1981 to 1992 were from military officers and finally, Korea was able to have a civilian president. Afterwards, Korea moved forward to the more democratic country.

Figure 1 GDP per Capita of Korea(1954- 2011)



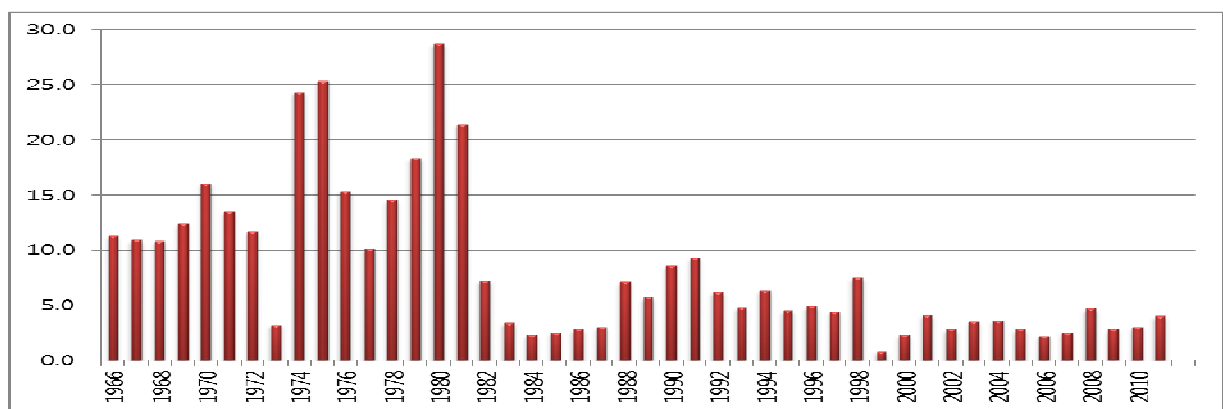
Source: Bank of Korea, ecos.bok.or.kr

Figure 2 GDP Growth Rate of Korea



Source: Bank of Korea, ecos.bok.or.kr

Figure 3 CPI Inflation



Source: Bank of Korea, ecos.bok.or.kr

### 3. Major Development Strategies of Korea

#### 1) From government initiated economy to market oriented one

At the earlier stage of development, most of development strategies were initiated by the central government. Since Korea was too less developed and market was too less organized, government had to initiate its economic development and manage it. Its economic strategy was focused on the industrial policy.

The first step of Korea's industrial policy was to select some of industries to promote. Korea did not any internationally marketable natural resource and the number of skillful worker or amount of capital were very limited in early 1960s. So it had to focus on manufacturing industry, especially labor-intensive one which required less skill and capital. At the same time, it has to build infrastructure such as power plants or high way. Afterwards, every five year, Korean government makes new five year development plan in which promotion industry are continuously reviewed and revised.

Second, it was not easy for Korean government to promote any specific industry. Korean economy has been based upon the market oriented economy so that its policy instrument should be acceptable under its system of capitalism. Most commonly used instruments are direct or indirect subsidies, tax exemption or financial supports. For example, a firms engaged in certain selected industries were eligible for a specific loan with a lower interest rate. Some firms in a special industry zone are waived for the tax for some years.

Of course, this government initiated development strategy brought some side effect as well in some fields. For example, under this system, role of financial industry is very limited because major amount of fund were allocated not by the will of financial institution but by the government policy. Or any favored few can be rich within a very short time. As the size of economy grew, the disadvantage of this system was getting bigger and bigger.

As a result, Korean government began to encourage the market principle to work and finally, it stopped making any five year development plan in 1994.

#### 2) Continuously change of industrial structure

If a firm likes to survive in the market, it must have its competitiveness over other companies. At the earlier stage of development, Korea did not have any things to sell in the oversea market. All they have was large number of unskilled workers who had less

education in the country side. So Korea had to choose some of labor intensive industries to promote. For example, textile, garment, wig or food processing were the first industry to choose.

As time went by, Korea began to accumulate the capital and technology, and then they transformed its industrial structure into more advanced one. It first focused on low-tech capital intensive industry and later does on high-tech capital intensive one. For example, assembling radio or TV is the one of the few industries which Korea was able to take in early 1970s. From 1990s. Korea mainly focuses more on technology based industry such as semi-conductor or software industry.

It was very important issue that which industry to promote at the each stage of development because each industry require different level of technology or skillfulness of workers

Table 2 Industrial Structure of Korea

Sector	1960	1970	1980	1990	2000	2005	2010
1. Agriculture	39.9	31.1	14.6	9	4.6	3.3	2.6
2. Industry	18.6	28.4	41.4	44.7	42.8	37.7	39.3
Mining	2.3	1.3	1.4	0.5	0.3	0.3	0.2
Manufacturing	12.1	19.1	29.6	28.9	31.5	28.4	30.6
Construction	3.5	6.4	8.2	13.2	8.2	9.2	6.5
Utilities	0.7	1.6	2.1	2.1	2.8	2.3	2
3. Services	41.5	40.5	44	46.3	52.6	59	58.2
Total (GDP)	100	100	100	100	100	100	100

Source: Bank of Korea, ecos.bok.or.kr

Table 3 Manufacturing Industry of Korea

	1960	1965	1970	1980	1990	2000	2005	2010
1. Food and beverages	36.5	26.1	19.6	10.8	7.4	7.4	5.3	4.1
2. Textiles and leather	25.2	28.3	28	23.3	13.5	8.3	5.1	4.2
3. Wood, paper products	9.2	10.8	8.9	4.8	5.1	4.3	3.6	3
4. Petroleum, coal and chemical prod.	9.7	13.9	14.2	19.8	14.5	15.3	17.2	15.7
5. Non-metallic mineral prod.	4.9	4.4	6.3	6.5	6.7	4.2	3.6	3.3



6. Metal products.	10.3	11.3	2.7	10.2	13.9	12.8	16.7	17.2
7. General machinery	2.7	3.9	2.9	4.4	6.7	7.9	8.3	8.9
8. Electric machinery			4.3	10.5	15.6	24.8	23.6	24.5
9. Precision instrument			0.9	1.7	1.5	1.4	1.5	1.5
10. Transport equipment			8.6	5.2	11.8	12.4	13.6	16.3
11. Other manufacturing	1.5	1.3	3.7	2.9	3.3	1.6	1.6	1.4

Source: Bank of Korea, ecos.bok.or.kr

Table 4 Labor Structure of Korea

Sector	1965	1970	1980	1990	2000	2005	2010
1. Agriculture	58.6	50.4	34	18.3	10.9	7.9	6.6
2. Industry	13.3	17.3	28.7	34.7	27.7	23.8	23.3
Mining	1	1.2	0.9	0.4	0.1	0.1	0.1
Manufacturing	9.4	13.2	21.7	26.9	20.1	18.1	16.9
Construction	2.9	2.9	6.1	7.4	7.5	7.6	6.3
3. Services	28.1	32.3	37.3	47	61.4	68.3	70.1
Total	100	100	100	100	100	100	100
Number ('000)	8,206	9,745	13,706	18,036	21,061	22,856	23,829

Source: Bank of Korea, ecos.bok.or.kr

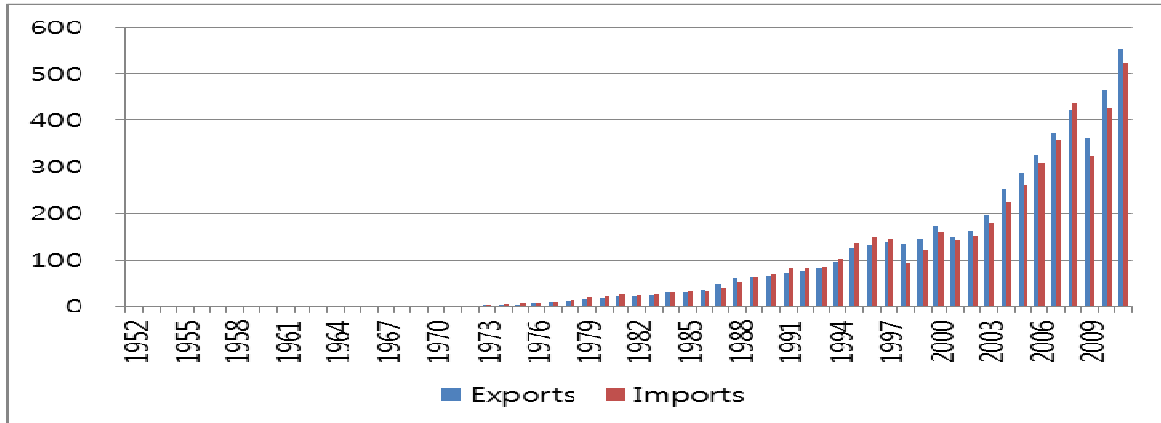
### 3) Focus on External Trade

Korea did not have enough natural resources. As a result it had to depend upon the external trade to get any basic necessities. For example, it did not have enough fuels to warm the house or building. Without selling something in overseas market, Koreans could not heat themselves during the winter time.

Export-driven policy brought lots of things to Korean economy. First, it enabled Korean firms to enjoy the economies of scale effect. Considering the size of population or land, Korean market was too small. As a result, it had to look at global market from the beginning.

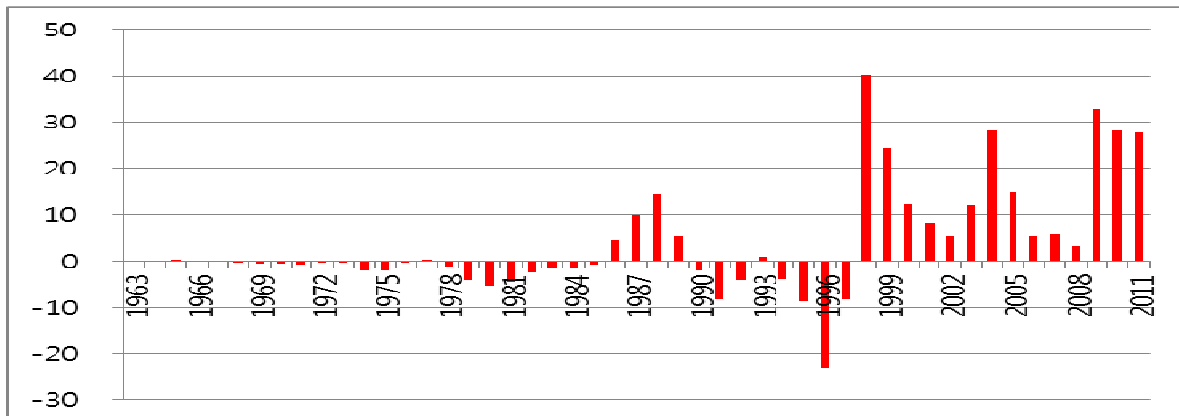
Second, Korean company had to compete in the very competitive market under this strategy. At first, it was very difficult for Korean companies to survive in the global market. Not only their production qualities were not good enough but also they were not used to the business activity of the international market. But eventually, they got used to these harsh conditions and were able to overcome it.

Figure 4 Export and Import of Korea



Source: Bank of Korea, ecos.bok.or.kr

Figure 5 Current Account of Korea (US billions dollars)



Source: Bank of Korea, ecos.bok.or.kr

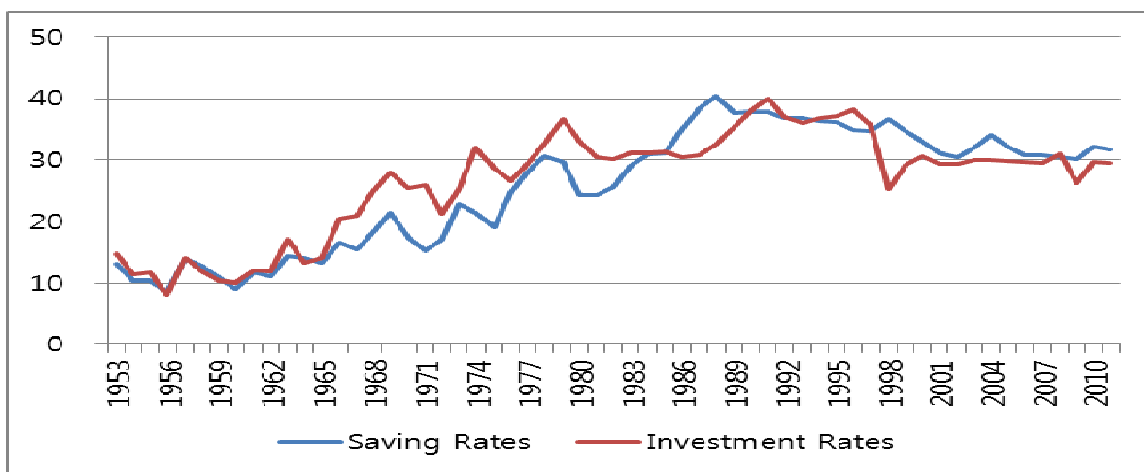
#### 4) Extensive Promotion of Domestic Saving and Investment

Like many other developing countries, the savings rate was very low and financial market was not well organized at the earlier stage of development. Korean government

took two policies at the same time. First, it promoted the domestic saving and restricted the consumption. Especially, bank loan for consumer expenditure was strictly restricted.

Second, it had to extensively utilize foreign financial resources. Interestingly, Korea tried to take a loan from foreign financial institution rather than foreign direct investment. Korea was not in the good position to take foreign direct investment in 1960s and 1970s because there were too many political and economic risks in Korea in 1960s and 1970s and Korea was relatively unknown to foreign investors, especially to western investors.

Figure 6 Savings Rates and Investment Rates (%)



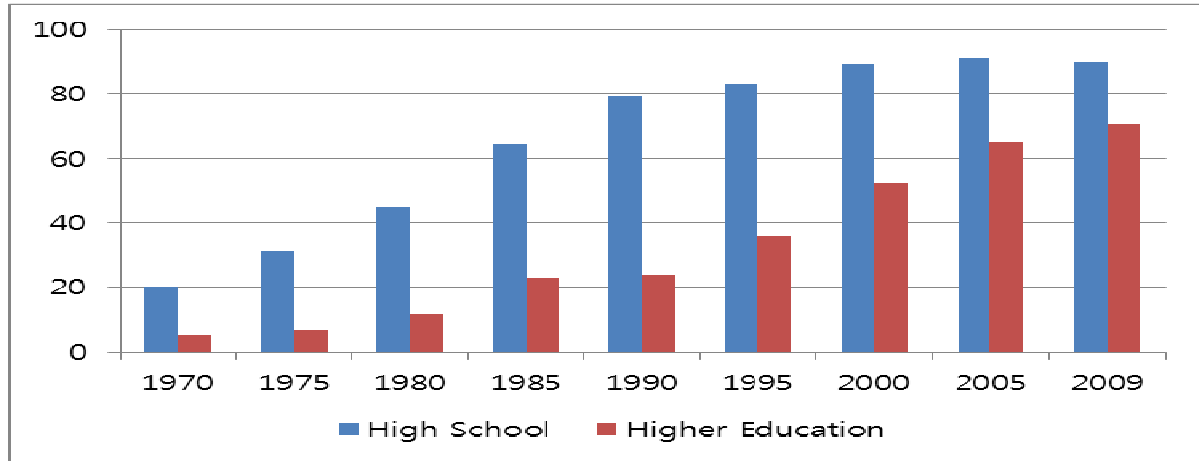
Source: Bank of Korea, [ecos.bok.or.kr](http://ecos.bok.or.kr)

## 5) Providing Proper Education

One of the major problems which Korea had in earlier stage of development is that there were only limited quantities of skilled workers. In 1970, the high school graduate rate was only 25 percent and university or college entrance rate was less than 10 percent. However as seen in Figure 7, the former increased up to 90 percent since 2000 and the latter up to 70 percent in 2010.

This rapid increase of higher education is another example of cooperation of government and private sector. First more people realized the importance of the education and they kept asking better education. At the same time, government allocated so much money on education for the past years. In addition, it allowed more school and college open in 1970s and 1980s.

Figure 7 High School and Higher Education Institution Enrollment Ratio



#### 4. Lessons from Korea's experience

##### 1) Right Policy at the Right Time

As explained in the above section, Korea has revised its development strategies continuously for the past 50 or 60 years. At the earlier stage, it promoted the labor intensive industry but later it has more focus on capital intensive one. More specifically, it has revised its industrial policy every five years. Furthermore, it succeeded in transforming it from government derived economy to a more market oriented one. Based upon it, we may claim that taking an appropriate strategy or industrial policy at the certain stage and time is very important.

##### 2) Important Role of Government.

At the earlier stage, developing countries were not equipped with basic condition for development. Some of them do not natural resources and other may lack of human resources. Market was not developed and asymmetric information problem are very serious. Most of industry may belong to non-competitive markets.

As a result, market may not provide an appropriate solution to promote an economic growth and consequently, the role of government can be very important. It has to design not only economic policy but also economic structure.

Korea's experience shows that the role of government is very important especially in the earlier stage of development. We think that the high capability of technocrat may contribute to improvement of the role of government.

### 3) Cooperation among Government and private sector

It is the private sector that is actually engaged in economic activities of production or consumption. We may say that economics policy or plan cannot be successful if private sector did not cooperate with it, no matter how good the development strategies are. For example, when Korea government declared to build steel factory in Pohang area in 1969, most foreign specialist had a very gloomy perspective on it. However, with a corporation of government and private sector, it becomes one of the most efficient steel factories in the world. Simply, steel company and its employee worked very hard despite the very harsh conditions.

We also like to emphasize entrepreneurship of Korean company owners. While some of them may have problem in managing their companies, it is true that they worked very hard and finally succeeded in increasing the size of their companies, which eventually contributed to the development of Korea.

### 4) Surviving under the Global Competitive Market

One of the important reasons why Korean firms maintained their competitiveness for a long time is that they had to play in the global market from the beginning. Since the market size of Korea was relatively small, they had to focus on the very competitive global market and they had to compete with foreign competitors. At the beginning it was very painful because they had never engaged in foreign business before and their competitiveness was very weak. Korea was located in the Far East and it did not have much relationship with other countries before. But they soon realize that once they were used to it and that they were able to overcome it, they can be very competitive in the long run. It shows that government protection should be temporary and should not last long

### 5) Importance of Human Resource

It is quite surprising how the small and resource lacking country like Korea achieved such remarkable an economic achievement during a past half century. We may say that it is because skilled workers are continuously supplied for decades. How could it possible? First, many Korean parents tries to make their children have better education and they also study very hard. Second, Korean government spend so much money to provide better education by building new high school and university. We may say that

this enable Korea to transform its industrial structure from a labor intensive industry to more sophisticate one for the past years.

#### 6) Reform of Social and Political System

Korea has succeeded in building both economically advanced country and more democratic and transparent society. Ironically, it is the military government which initiated the first economic development plan in 1962. Despite many problems of this military government such as violation or repress of human rights, we cannot deny its contribution of economic development and modernization.

However, Korea has slowly forwarded into a more democratic country for the decades. Several nationwide street protests of students and civilians happened in 1980 and 1987 and finally, the civilian candidate became a president in 1992 and a formerly prosecuted politician was able to be a president in 1997. Now we may say that Korea is one of the most civilized countries in the world. Slow but continuous steps into democracy were taken and people should be very patient.

#### 5. Concluding Remark

This paper attempts to review Korea's past development strategies and to show some meaningful lesson for other Asian developing countries. It may look ridiculous that we cover 60 years of development strategies of Korea and then give important lessons from this short paper.

However, still many policy makers and academicians do not know the general idea of Korea's development strategies as well as its possible usefulness to them. If this short paper succeeds in this job, we think it is worth of writing it.