

Determinants of Growth in North and South Korea: a Comparative Approach

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Abstract

A wide range of literature that addresses the issue that democracy, as opposed to auto-cracy, suggest it stimulates economic growth in a country. Well known authors reviewed in this paper argue that as democracy consolidates and becomes more stable, and income grows more rapidly which feeds into more democratic stability. A remarkable outcomes of some East Asian countries seem to challenge the widespread hypothesis that a democratic system inevitably leads to a better economic performance for a country as in the North and South Korean case here analyzed, where a policy choices inside a political regime determine sustained growth.

Keywords: democracy, economic development, political regime.

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Resumen

Una amplia gama de la literatura académica que aborda el tema de la democracia frente a la autocracia, sugiere que la primera estimula el crecimiento económico en un país. Conocidos autores discuten acerca de la manera como la democracia se consolida en un país y se vuelve más estable. En estos casos el ingreso crece más rápidamente, y se asegura que de esta manera se preserva la estabilidad democrática. Los resultados encontrados en algunos países de Asia oriental desafían esta hipótesis generalizada, y consideran que sin un sistema democrático, como lo definimos en Occidente, es posible elevar el desempeño económico como ocurre en Corea del Norte y Corea del Sur gracias a las políticas públicas adecuadas por parte de cada gobierno.

Palabras clave: democracia, desarrollo económico, régimen político.

Introduction

Attending Paris School of International Affairs – Sciences Po Paris, we suggest in the present paper that it is frequent to find that countries with similar endowments, characteristics, geography, and culture have divergent economic outcomes. That is why numerous academics tend to find an answer in the countries' different political regimes. There is a wide range of literature that addresses the issue that democracy, as opposed to autocracy, stimulates economic growth in a country. Persson and Tabellini (2006) argue, for instance, that as democracy consolidates and becomes more stable, income grows more rapidly which feeds into more democratic stability, and yet more economic growth. However, remarkable outcomes of some East Asian countries seem to challenge the widespread hypothesis that a democratic system inevitably leads to a better economic performance for a country (e.g., South Korea during the 1960s, China since 1978).

Some authors (e.g., Besley and Kudamatsu, 2007 and Collier, 2009) argue that autocracy can actually produce better economic outcomes under certain circumstances. After the Korean War, South Korea started an astonishing process of industrialization under a series of autocratic regimes. However, North Korea, a country with an identical social configuration as for 1953, has not managed to grow under its own autocratic regimes. Why these two similar countries, randomly divided by the 38 Parallel, have had such divergent economic outcomes?

From the political point of view, on one hand, there are authors who argue there is indeed a positive correlation between democracy and economic performance. For instance, Rodrik and Wacziarg (2005, p. 55) claim that “major democratic transitions have, if anything, a positive effect on economic growth in the short run”. Similarly, Persson and Tabellini (2006, p. 3) discuss that “as democracy consolidates and becomes more stable, income grows more rapidly”. On the other hand, there are academics who argue that un-

der certain conditions, an autocratic regime can lead to economic growth. Besley and Kudamatsu (2007, p. 43) claim that “autocracies are successful if the ‘selectorate’ can remove poorly-performing leaders”. Collier (2009) makes a similar argument by suggesting that in countries with very low incomes per capita, democracy retards the reform of economic policies and governance. Moreover, he also argues that autocracies do not work well in societies where there is great ethnic diversity, but that the opposite might be the case in homogeneous societies (Collier, 2007). Finally, Duncan (2004, p. 49) develops this point further when he argues that “good economic performance can result from an autocratic system following a development strategy that exploits comparative advantage, while providing the necessary institutions for markets to operate effectively.”

This theory is a good starting point. But it can be concluded from evidence that what matters are not political regimes per se, to allow a society to develop. Acemoglu and Robinson (2012) refer to it as institutional development and Besley and Person (2010) name it state effectiveness or state capacity, which comprises extractive/fiscal capacity (infrastructure to raise taxes from broad bases) and productive/legal capacity (infrastructure to enforce contracts or protect property rights).

North Korea and South Korea have brought a unique understanding about how these factors determine economic growth and development. After the end of the Korean War, North Korea and South Korea found themselves with similar initial economic conditions. A study, published by the United States Central Intelligence Agency in 1978, estimated that North Korea’s per capita gross national product equaled South Korea’s as late as 1976 (Congress Library, 1994). However, overtime they experienced divergent economic outcomes.

Historical background

Although Koreans nowadays express hatred towards Japan, for these nationals that started colonization between 1910 and 1945, it laid however some of the key foundations for Korea’s later entrance into modern economic growth (Mason et al. 1980), which became evident only after 1960. According to Amsden (1987), the Japanese achieved overnight in 1910 what the dynastic Korean rulers had failed to do for centuries: the abolition of slavery, the codification of civil law, and the adoption of a new tax system based on payments in cash rather than in kind, among other reforms. They also created a modern infrastructure in the areas of finance, transportation, and commerce. The core of the Japanese colonization was agriculture (extractive institutions), as stated by Amsden, was both the object of Japanese aggression and the heart of the Korean economy and society. The Japanese colonial government’s objective was to raise land tax revenues. This kind of extractive institutions allowed for economic growth, although not sustainable growth, since the result was a society that was unable to support itself. Due to peasants that opposed the

landlords, and a miniscule army incapable of national defense, Korea was again fell victim of the great powers (Amsden, 1987).

The Japanese withdrew from Korea on 1945, and soon thereafter in 1950, the Korean War began, confronting two different ideologies. What distinguished North from South, or Left from Right as it is exposed by Cummings (1981) was firstly, a commitment to a thorough extirpation of Japanese influences in Korea, secondly, a commitment to mass politics and mass organization and to the social equality that this implied, and thirdly, a commitment to the reform of Korea's feudal legacy, feudalism being a code for gross inequalities in the allocation of resources, particularly land. Russia recognized these policies immediately, but the US did not recognize them, after which point an American alliance was created, which finally ended up in the Korean War and the division of the country into two ideologically separate parts.

After the Korean War, 1953, and the partition, North Korea had an authoritarian regime under Kim Il Sung. This period of authoritarianism has continued after his death in 1994 to this day. North Korea recovered from the war with foreign aid especially from China, the Soviet Union and East Germany. Frank (2008) shows that by 1954, collected donations of 23 million German marks in cash and 13 million German marks in kind were shipped to North Korea. During the 1950s, North Korea was growing three times faster than the South (Cole and Lyman, 1971). Since the mid-1950s Kim Il Sung pursued a policy called *chuch'e* (lit. self reliance) from other countries. According to Lee (2003), Kim Il Sung defined *chuch'e* as "being the master of revolution and reconstruction in one's own country". In pursuing these policies of isolation from its major supporters, he followed a policy of autarky. During this period, Kim Il Sung aimed to establish a powerful base of heavy industry with the machine building industry at its core, which would equip light industry, agriculture, transport, and all other branches of the economy (Lee, 2003).

Kim Il Sung's autarkic policies together with the inefficiencies arising from emerging bottlenecks (e.g., lack of arable land, skilled labor, energy and transportation) (Library of Congress, 2008) proved to be catastrophic for North Korea's economic growth. Even though North Korea had experienced levels of economic growth of 9.3 percent between 1954 and 1960, there was subsequently a dramatic decline of economic growth. Kim, and Lee (2007) estimated that between 1960 and 1965 North Korea's economic growth plummeted to 3.3 percent per year. North Korea's economic growth continued to decline and by 1990 the country had negative economic growth levels of negative 3.7 percent (Rhee, 1992).

South Korea initially followed a similar pattern of authoritarian rule as North Korea. The country had an extended period of authoritarianism under the rule of Park Chung Hee (1963-1979). Similar to North Korea, South Korea was also heavily dependent on foreign assistance. During the 1950s, the country was almost entirely reliant on interna-

tional aid from the U.S. for war reconstruction. According to Cole and Lyman (1971), the average annual inflow of aid from 1953 through 1958 was \$270 million excluding military assistance, which was nearly 15 percent of the average annual gross national product and over 80 percent of foreign exchange.

In contrast to North Korea, Park Chun Hee's regime was based on three pillars: a statist approach, export oriented industrialization -which was successful in pursuing a policy of export promotion on the basis of its comparative advantage due to low wages-, and control of the financial sector and the government business ties. As a result, South Korea increased growth rates dramatically. Between 1962 and 1971, the real growth rate of GNP averaged 9 percent per annum. From 1972 until 1979, growth was even higher averaging 10 percent each year (Amsden, 1989). These policies could be more easily implemented thanks to the legacy of the Japanese colonization, given that the impact of the U.S. occupation on Korean industrialization was similar to that of Japan. The difference between them was that the Japanese colonial administration had enacted a model of centralized state management, whereas the U.S. advisors preached private ownership and decentralized control (Amsden, 1987). These features encouraged investment and trade. Political leaders invested in education, achieving high rates of literacy. Companies were quick to take advantage of the relatively educated population, the policies encouraging investment and industrialization, exports, and the transfer of technology.

Despite the economic successes of the authoritarian regimes of Park Chun Hee and his successor Doohan Chun, in 1987, protests for democracy were strong enough for the Chun administration to give way to the transition to democracy based on a direct election of the president, a guarantee of human rights, guarantees of freedom of speech, local autonomy, and securing freedom of political parties (Heo, Jeon, Kim and Kim; 2008).

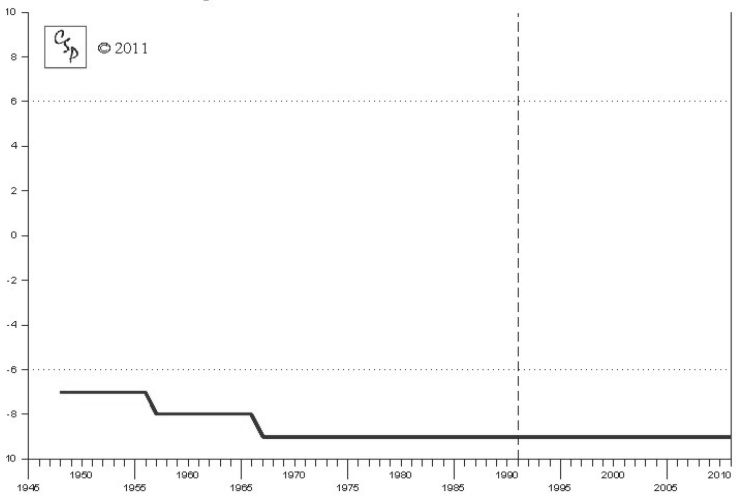
The presidential election of 1987 resulted in the victory of Tae Woo Roh. As stated by Heo et al., Roh's administration focused on human rights improvement, a better reflection of public opinion in policymaking, fair elections and freedom of speech. No major changes were pursued in economic policy. Moreover, these changes led to the legalization of union labors which increased wages and initially conducted to decreased exports and a loss of competitiveness. Nevertheless, these unions are considered a necessary counterweight to the power of chaebol -business conglomerates driving the economy since its conception in the 1960's- and to thank for gains in workers' rights and working conditions since then (Jeong, 2011).

In general, economic institutions established during the autocratic governments, fostered economic activity, productivity growth and economic prosperity, but for them to keep functioning, a change to democracy was necessary, given the pressure from workers and population in general.

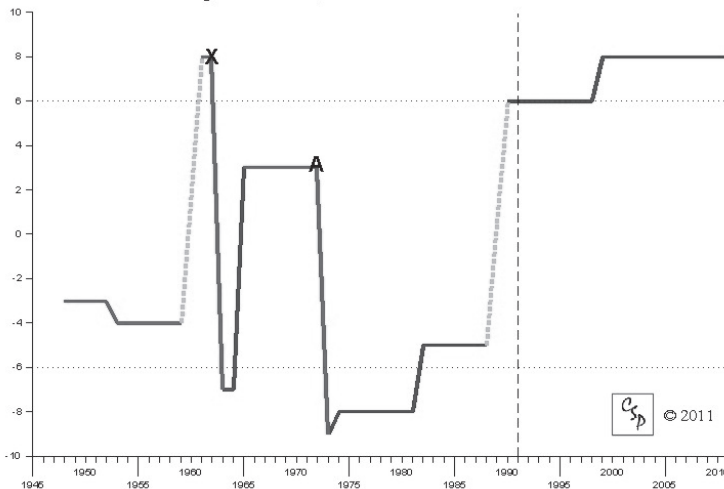
Conclusion

It is not the political system, nor the culture, nor the geography what determines the economic success of a country. Neither is the foreign aid aimed at delivering economic growth. Policy choices inside a political regime -and their appropriateness to a country's own characteristics and comparative advantage- are what determine economic success. In other words, such success relies in the policies and institutions that each regime allows to develop, and how they seize and manage the opportunities the country is presented (i.e. aid, natural resource endowment, foreign investment inflows).

Authority Trends, 1948-2010: North Korea



Authority Trends, 1948-2010: South Korea



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