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Working Paper No. 47, The Transformation of Developmental States: Patterns of Economic Development in South Korea and Taiwan

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The Transformation of Developmental States:

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Abstract: This inquiry considers similar yet contrasting patterns in the economic development of South Korea and Taiwan. Taiwan’s developmental state has tended to exhibit ‘softer’ characteristics than South Korea’s. I identify a tendency for when developmental states face crises and then transition forward to a ‘post-developmental state’. This is traced to the internal 'paradox of success' and external pressure of neoliberal globalization. Though these two countries tend to embrace and rely upon neoliberal policies for economic growth, the speed and degree of systemic change register as different. A 1997 financial crisis appears to have goaded South Korea to move quickly through a transition to a neoliberal economy, while Taiwan undertook a relatively gradual transition that offered different outcomes. In the processes of these two transitions, I cannot identify a ‘double movement’ in the Polanyian sense. Relatedly, working classes lacking in power and with uncertain targets to fight—byproducts of a developmental state—appear to dampen the spirit for effective social movements.

***Journal of Economic Literature* Classification Codes:** N15, O11, O25

Key Words: Developmental State, Post-Developmental State, South Korea, Taiwan, Double Movement

This inquiry seeks to establish that South Korea and Taiwan exhibit similar as well as distinctly contrasting approaches and patterns in economic development. The two countries share East Asian developmental states' characteristics. S.W. Yun (2002, 2) defined the developmental state paradigm as a set of theories, techniques, and arguments that relate economic performance to state-centered institutional systems. This article reviews developmental state theory and attempts to explain the economic development of Korea and Taiwan through this discussion. The review of developmental state theory can be divided into the background of the discussion, common characteristics, crisis, and the transition to the post-developmental state. Based on the understanding of the theory, this paper compares the patterns of development in Korea and Taiwan, focusing on the process of transition to a post-developmental state. Lastly, with the concept “double movement” proposed by Polanyi, this paper tries to describe the reaction of the systematic change at the time.

Part 1. The Developmental States and the Post Developmental States

In the mid-20th century, East Asian countries achieved rapid economic growth as followers in a different way from the market-oriented growth of the West. Johnson (1982, 17) first conceptualized East Asian countries' economic development academically as a developmental state. Johnson (1982) analyzed the process of extraordinary Japanese economic growth in the mid-to-late 20th century, explaining that a developmental state is a country that actively intervenes in the economy and markets for the goal of prioritizing economic growth. Subsequently, scholars suggested common characteristics of developmental states in East Asia by expanding research subjects to South Korea, Taiwan, Singapore, and Hongkong. The developmental states' elements can be summarized as follows: 1) economic development as a top-priority national policy goal 2) a country that its government actively engages in the market 3) a few competent elites exert a strong influence on policy decisions. (Johnson, 1982; Amsden 1991, 284; Evans 1998; Woo-Cummings, 1999) A scholar like Loriaux (1999, 252) grouped France in the developmental category, but this categorization proved controversial. People usually use the term “developmental state” to explain the “East Asian development model”. However, it is necessary to encourage caution in using this term because the growth path of emerging East Asian countries tends not to be uniform. S.W. Yun (2005, 136) points out that, unlike South Korea and Taiwan, Hong Kong is more likely to be considered a free-market model emphasizing market mechanisms. Singapore also adopts a growth model based on slippery capital despite strong national guidance.

Low (2004, 5) defined the developmental state as one which promotes long-term entrepreneurial perspectives among the industrial elite comprising key business groups and resists growth-compromising demands from special interest groups. In terms of the market intervention of the state, H. J. Chang (2002, 142) regards it as a universal feature of late industrialization from the entire history of capitalism, while Chu (1989, 671) insists that the active and effective state can be found in different authority structures. Woo-Cummings (1999, 71) highlighted that government's role of developmental states should be understood as a unique development model with historical specificity. He argued that the government-led development could only be possible under a specific historical situation in the 20th century that East Asian countries were facing. Specifically, the emergence and growth of developmental states in East Asia result from the international Cold War externally and the unique historical conditions of East Asian countries such as the war in the colonial period, national division internally.

Scholars recognized that the possibility of a developmental state crisis and systematic transition into a neo-liberal economic system. S. W. Yun (2020, 179) points out that the phenomenon of convergence to neoliberalism occurs to some extent in any development model. This is because the state's historically successful economic intervention could result in a paradoxical result as the economy grows. For example, Amsden (1991, 20) argues that the state's economic intervention does not necessarily guarantee development because it is likely to lead to rent-seeking activities that undermine economic efficiency. L. S. Kim (1997, 83) also indicates that the decrease in the power of government institutions in globalization can lead the developmental states to risk.

The virtuous cycle between developmental state and economic growth is by no means a constant structural characteristic. Scholars who insist on the possibility of crisis believe that the state's historically successful economic intervention could result in a paradoxical result as the economy grows. The effectiveness of the state's intervention could be exhausted over time, while the emergence of 'grave-digger', such as large enterprises strongly linked to government and strong labor unions, could limit economic development and procure new social conflicts (Evans 1989, 575; Huang 2011: 139). By doing so, the authoritarian government can generate social inefficiency such as corruption. Some scholars indicate that the decrease in the power of government institutions in globalization can lead the developmental states to risk. In sum, a developmental state could gradually decline as the institutional foundations of the developmental state, such as state autonomy and strong state-social relationship (capital-labor) are weakened d as a result of long-term economic growth and globalization. Consequently, developmental states must fully or partially accept and adopt deregulation, openness, liberalization, and privatization to strengthen international competitiveness and ensure the legitimacy of the state's intervention.

East Asian developmental states, which continued to grow rapidly until the middle of the 20th century, faced a financial crisis and transformed toward a post-developmental state. S. W. Yun (2020, 21) categorized theories regarding the characteristics of the post-developmental state into three. First, there is a theory expecting post-developmental state could transform into a regulatory state in the Western sense. Jayasuriya (2005, 382) argues that after the 1990s, the developmental states go through dissolution and extinction of developmental state nature and eventually transformed into a neoliberal regulatory state. In a regulatory state, the government plays a role in ensuring the free transaction in a market and market stability, instead of implementing strategic industrial policy and active market intervention. The second theory expects that the post-developmental state will sustain the role of the authoritarian government due to the institutional inertia and path dependence. Pirie (2018, 10) argues that government intervention and developmentalism would be continuous, while states' traditional role is weakening or declining. The fact that governments also played a crucial role in restructuring shows that the state's willingness to intervene and control the overall economy could be sustained. The third theory is about the possibility of transition to a “social corporatist developmental state”. According to Evans (1989, 574), Strategic state intervention would be valid and sustainable in the future if the embedded autonomy of the developmental state, which was previously limited to the government and the capital, expands to the people such as the working class. Weiss & Hobson (1995) also expect the transition from a 'strong government - weak civil society' to a flexible state of 'strong government - strong civil society', which leads the developmental state to achieve growth and distribution at the same time.

Part 2. Approaches and Patterns in South Korea's Development

South Korea went through a rapid transformation due to the economic crisis in 1997. There was a gradual change in the economic system in Korea has been sought since the mid-1980s. S. W. Yun (2003, 4) points out that both internal contradictions of the developmental state and external pressure have led to the transformation of the Korean economic system from the developmental state to a neoliberal economy. Firstly, South Korea went through institutional change since the late 1980s because of internal conflicts. In conjunction with the democratization movement in the 70s and 80s, South Korea abolished the Industrial Development Act allowing selective and direct support to certain industries in 1986. Also, South Korea abolished the Korean Institute of Economic Planning, a symbol of the developmental state, in 1994. S. W. Yun (2002, 18) indicates that the attempt to amend the labor law in 1996 to allow layoffs is a part of the transitions. Of course, it cannot be overlooked that various kinds of pressures, such as the Uruguay Round to liberalize and deregulate the developmental state, led to the transition of the Korean economic system.

An unprecedented financial crisis and following the IMF agreement in 1997 accelerated the decline and dissolution of the developmental state in South Korea eventually. The Kim Dae-Jung administration, which took power immediately after the crisis, implemented strong restructuring based on the IMF agreement. The IMF calls for structural adjustment programs (SAPs) in countries experiencing financial crises. Kwon & Yoo (1999, 23) summarize the basic elements of SAPs as the devaluation of the currency, reduction of state intervention in the economy, abolition of price and exchange rate control, reduction of government spending on public services, and privatization of public enterprises. Consequently, Korea has experienced radical neoliberal restructuring in a short period through a Memorandum on the Economic Program and the agreement on "Republic of Korea: IMF stand-by Arrangement (SBA), Summary of Economic Program (1997)". (Kwon & Yoo 1999, 24)

Table 1. Neoliberal Transition of South Korea

Sector	IMF Structural Adjustment Programs (Kwon & Yoo 1999, 25)	Characteristics of Korean industrialization policy (Amsden, 1991)
Financial Market	■ Prohibition of government intervention in bank management ■ Adjustment of financial soundness supervision standards to the BIS ■ Expansion of foreign stock investment limit ■ Permission for Foreign capitals to establish local banks and stock companies	■ Debt Financing by controlling interest rates ■ Protecting Domestic Industry from Foreign Direct Investment
Product Market	■ Reduction of corporate debt ratio ■ Abolition of government supports and tax incentives to rescue companies ■ Abolition of trade-related government subsidies and import approval system	■ Policy financing through subsidies, tax incentives, and low loan ratio for firms ■ Protecting domestic market through high tariff and import regulation
Labor Market	■ Enhancing labor market flexibility and strengthening the function of the employment insurance system	■ Labors' learning and innovation by long-term employment ■ The combination of low wage base and fast wage increase

Table 1 summarizes the characteristics of Korean industrial policy (Amsden, 1991), which shows the industrialization process in South Korea as a late industrialized country and the contents of restructuring conducted under IMF bailout conditions. Through this table, it will be possible to understand the direction and contents of the neoliberal systemic transition of South Korea in the late 1990s.

There is a controversy over whether this shift to a neoliberal economic policy was forced from the outside. For example, Wade and Veneroso (1998, 2) pointed out that the so-called Wall Street- US Treasury - IMF Complex requested the opening of the capital market, liberalization of finance and trade, and suspension of business in bad financial status in the first negotiations between the IMF and the Korean government in December 1997. Also, B. C. Lee (1999, 126) argued that the external pressure drove the Kim Dae-Jung administration to set the restructuring t to a laissez-faire economy, even though the regime preferred German or Japanese capitalism because of external pressure. However, J. H. Ji (2007, 21) refutes this position by pointing out that Korean government officials suggested most of the structural reform proposals included in the Korean IMF program by themselves. Also, he pointed out that the systemic transition to neo-liberalism has expanded beyond the IMF's demands even after the full repayment of the bailout funds in 2001. Furthermore, this set of radical neoliberal restructuring tended to gain political justification from the labor market reform.

L. S. Kim (1997, 48) indicates that the government has oppressed laborers for a long time to allow businesses to utilize cheap labor. Because small East Asian countries lack natural resources, cheap and skilled labor was the only resource for them. Consequently, the state tended to suppress the laborers and labor unions to secure a cheap labor force. In this context, some people consider the IMF's requests to soften the labor market and strengthen labor protection as attempts to protect the working class.

Korean transition to the neoliberal system has the following characteristics in terms of its development model. First, S.W. Yun (2020, 179) evaluates that Korea's neoliberal policies are extremely instrumental, rather than aiming for the economic operation that fully realizes the market principle. South Korea utilized neo-liberal policies as incentives for attracting foreign capital, expanding corporate investment, and promoting exports. If necessary, the Korean government implements Keynesian or developmental state policies, conflicting with neoliberalism. For example, the Korean government uses public funds for some insolvent large companies.

Part 3. Approaches and Patterns in Taiwan's Development

The characteristics of the Taiwanese developmental state are softer than that of South Korea. First, Amsden & Chu (2003, 125) indicated that the goal of the financial policies (exchange rate policy, interest rate policy, policy finance) of the

Taiwanese government were not only economic growth but also economic stability. Taiwan often implements high-interest policies to balance economic growth and economic stability, which is different from the Korean government's finical policy sacrificing economic stability through aggressive low-interest policies. (D. C. Kang, 1995) In terms of industrial policy, Taiwan also conducted various policies to support and discipline industries in a less direct way. Amsden & Chu (2003, 110) argued that the Taiwanese government focused on promoting investment and production in the private sector by creating an appropriate investment environment rather than strong intervention. In terms of the labor market, S.W. Yun (2002, 11) pointed out that the Taiwanese government put efforts to embrace the working class and labor, while they were fundamentally repressive like other developmental states. Taiwanese government tried strengthened the protection for workers through the revision of the labor law of 1984 and connect the labor market between rural and urban areas. For example, the government implemented a policy promoting urban manufacturing plants by employing farmers as part-time workers.

Taiwanese soft developmental state also has experienced a transition to the neoliberal market system gradually. Amsden & Chu (2003, 136) regarded that the Taiwanese government has pursued a transformation aimed at liberalization and globalization of the economy since the 1980s. They argued that, like South Korea, Taiwan went through a process of weakening and declining developmental state due to changes in the relationship between state-world, state-civil society, and state-capital since the 1980s. However, unlike South Korea and other East Asian countries, Taiwan did not face the financial crisis in 1997 and maintained the economic system and state's overall economic policy.

Pirie (2018) argues that the pressure to change the Taiwanese economic system significantly has been raised internally and externally since the 2000s. First, the vitality of the Taiwanese economy required changes in the economic system as the low-growth and low-investment phases continued throughout the 2000s. Hwang (2020) indicated that this stagnation is partly because of the Taiwanese economy's hollowing out problem generated by Taiwanese companies' investment in China, which accelerated after the 1990s. Furthermore, as a result of the presidential election in 2000, the long-lasting rule of the Kuomintang (KMT) Party, which was the political foundation of the developmental state in Taiwan, was replaced by the Democratic Progressive Party (DPP). Chu (2013, 662) pointed out that the new Chen Shui-bian administration was quite agitated by the neoliberal shift adopted by many East Asian countries. Furthermore, to join the WTO in 2001, the Taiwanese government also had to fulfill the conditions such as deregulation in the financial sector and the opening and liberalization of international financial capital.

However, scholars tend to assess that the Taiwanese economic system maintained the institutional continuity of the developmental state despite changes in internal and external circumstances after the 2000s. (Wang, 2012; Chu, 2014; Yun, 2009). Chu (2014, 11) pointed out that the Taiwanese developmental state system has almost maintained its former form, authority, and function despite the regime's democratization and the change in the regime. In Taiwan, economic institutions such as the Economic Construction Committee and the Industrial Bureau of the Ministry of Economy are in existence, and they are still planning and implementing economic development policies. Furthermore, Wong (2005, 186) called Taiwan economic development model an adaptive developmental state because the Taiwanese government plays a vital role in transforming traditional industries into high-tech industries. Second, Chu (2014, 10) mentions that the Taiwanese developmental state maintains strong control over the financial sector through the central bank. He points out that Taiwan's state directly owned three of the top 10 commercial banks and controlled four, and owned and controlled 43% of the total banking assets in 2008. Chu (2014, 15) also points out that the Taiwanese government tried to delay the privatization of public enterprises and the privatization of banks as much as possible.

As a result, unlike Korea and Japan, which explicitly performed neo-liberal transitions, the Taiwanese government partially introduced the neoliberal policy and welfare-state policy in a specific area while maintaining the basic nature of the developmental state. However, S. W. Yun (2020, 177) indicates that the developmental state's policy performance and economic efficiency are significantly weakening, unlike in the past. He points out that the downturn of low growth and low investments in the Taiwanese economy from the 2000s implies developmental state is no longer valid in the era of neoliberal globalization, even though the institutional inertia of the developmental state is maintained.

Part 4. Double Movement in the Process of Transformation

In *the Great Transformation* (1944), Karl Polanyi argued that the development of market societies over the past two hundred years had been shaped by a double movement. On one side is the movement of *laissez-faire,* the efforts by a variety of groups to expand the scope and influence of self-regulating markets. On the other side has been the movement of protection – the initiatives, again by a wide range of social actors, to insulate the fabric of social life from the destructive impact of market pressures. (Block 2008, 1)

There is no general theory about the role of the state in Polanyi's theory of the double movement. However, he mentioned several times that the role of the state is essential in the economic development process. Polanyi (2009, 407-410) argued that the formation of self-regulating markets, which find their equilibrium by themselves, actually required state intervention. He pointed out that the liberalist did not rule out government intervention to maintain a self-regulating market but rather actively asked and utilized it to operationalize the markets. The liberalists regularly demanded coercive action from the state to pass union-related or anti-monopoly laws.

Some scholars theorized the role of the state in the double movement. Block and Somers (1984) pay attention to the role of the state performing the double movement. Block (2004, 4) argued states could follow self-regulating markets principle and the social protection principle depending on the political and economic conditions and how social actors have perceived those specific conditions. On the other hand, Gislain (1987, 150) mentions that Polanyi's state plays a role in guaranteeing social order and social system. Similarly, Searcy (1993, 222~223) insists that the power of social protection is stronger among the double movements. These studies argue that Polanyi's state is carrying out a double movement for social protection because the power of social protection is stronger among the double movements.

In either direction, the state plays a role in the movement process. A state can realize or coordinate conflicts between ideologies and classes. Clark (2015, 7) argued that a state can coordinate individual activities through enforcing laws and commandeering resources as a sovereign political entity. In the case of developmental states, the role of the authoritarian state in the process of economic development, including double movement could be even more important. As we saw in the development process of South Korea and Taiwan, the states have been actively setting a direction among economic actors. For example, the Korean government implemented low-interest rate and low-income policies for rapid economic growth, while the Taiwanese government pursued economic stability simultaneously with economic growth.

However, there was no social movement in East Asia during the transition from a developmental state to a neo-liberal state. The reasons for this fact can also be interpreted considering the historical path of the developmental states. First, in contrast to the western cases, the working-class was too weak to lead social movements. This is because developmental states companies could hire workers at relatively low wages and workers were under the protection of the corporate welfare system, not the state. For example, S. M. Eun (2009, 12) pointed out that, in 1997, Korean workers were under a corporate welfare system, where they could live only after long-term employment in decent jobs. This can be seen as a result of Korea's state-led policies supporting low wage policy and adjusting the relative price of goods in the international market by interfering with the role of labor unions as a late-industrial country (Amsden, 1986). In a fast-growing country, the low wage policy was not a big problem. As a result of the IMF restructuring, however, Korean workers lose all of the power to counter the state or the market when fired. The situation can't be described as just such a high unemployment rate. According to a newspaper article at the time, the abandonment without various shields destroyed individuals physically and mentally and their home as a basic unit of society. The newspaper article follows describes the situation at the time.

> The financial crisis first destroyed homes. People cheated on husbands/wives secretly, abandoned old mothers, and killed fathers.... and domestic violence increased. There was prostitution by Housewives.... a housewife who sold her body to earn tutoring expenses for her child, and a young female left the house at night to pay for her baby.... Not a few children were abandoned by their parents. Parents, especially single parents, who have no living expenses, left their children in the nursery for a while, and they didn't come again. (CBS Special Coverage, 2001)

Second, it was not clear who people would protest against. In the process of transition from the developmental state to a neoliberal system, the state did not necessarily make a decision that was beneficial to the enterprise. Amsden (1984, 93-106) indicates that developmental states, as followers, adjust prices through policy financing and export subsidies to protect their domestic businesses. However, in such developmental states, the IMF took measures to establish financial supervision standards in line with BIS standards and reduce the scope of policy financing in a short period. Consequently, many companies went bankrupt. K. Kim (1998, 15) argues that it was completely unreasonable to immediately impose the BIS standard, which was gradually introduced over a long period to advanced countries due to concerns about corporate bankruptcy. As a result, austerity policies resulted in mass unemployment and large-scale corporate bankruptcy, which led to a vicious cycle leading to corporate insolvency, bankruptcy, and insolvent debt. In this situation, people consider the market as a victim suffering the same pain rather than an enemy. Furthermore, in Korea's case, the Kim Dae-Jung administration, who led the transition, gained power as a result of the democratization movement in the 1980s and early 1990s. Thus, it was also hard for citizens to make the government an enemy.

Conclusion

This inquiry has sought to establish that South Korea and Taiwan exhibit similar as well as contrasting approaches and patterns in economic development. While both countries offer examples of successful, developmental states, the characteristics exhihbited by Taiwan's developmental state's characteristics were softer than for South Korea. According to a theory of the 'developmental state', the internal 'paradox of success' taking the form as high rates of high growth in per capita output undermine the state's structural foundation, while external pressures associated with neoliberal globalization serve to generate crises. One particular crisis led the transition from a developmental state to a post-developmental state. South Korea experienced a rapid transition to a neoliberal economy, with the financial crisis taking place towards the end of the 1990s, while Taiwan experienced a relatively gradual transition to a post developmental state. Consequently, while the models found in both countries tend to converge towards neoliberal systems, the key characteristics of their developmental states differ. In other words, both nations have a strong tendency to instrumentally embrace neoliberal systems for economic growth, even though the degree of systemic change is different.

Invoking the term "great transformation, Karl Polanyi described emergence and societal transition to a market economy. Following Polanyi's lead, this inquiry has also considered the transition of the developmental state as an important 'transformation' while also seeking to bear out the societal reaction to change. This research suggests that in both South Korea and Taiwan, we cannot identify a "double movement" in the Polanyian sense taking place in the transformation from the developmental to post-developmental state. When considering South Korea, we cannot identify a significat social movement, even though the transformation changed people's lives fundamentally. We explain this tendency to the relataively powerless working classes that appears related to the use of industrial development policy. We can also identify that targets to achieved tended to remain uncertain and this is traced to the mixed relationships between agents that served to dampen the spirit for social movement. When people evaluate the transformation of the developmental state of the formal economy, it could be shown as a successful one. However, it is necessary to examine the transformation of the substantive economy—emphasized by Polanyi—by looking at the change of society through the change of the economic system.

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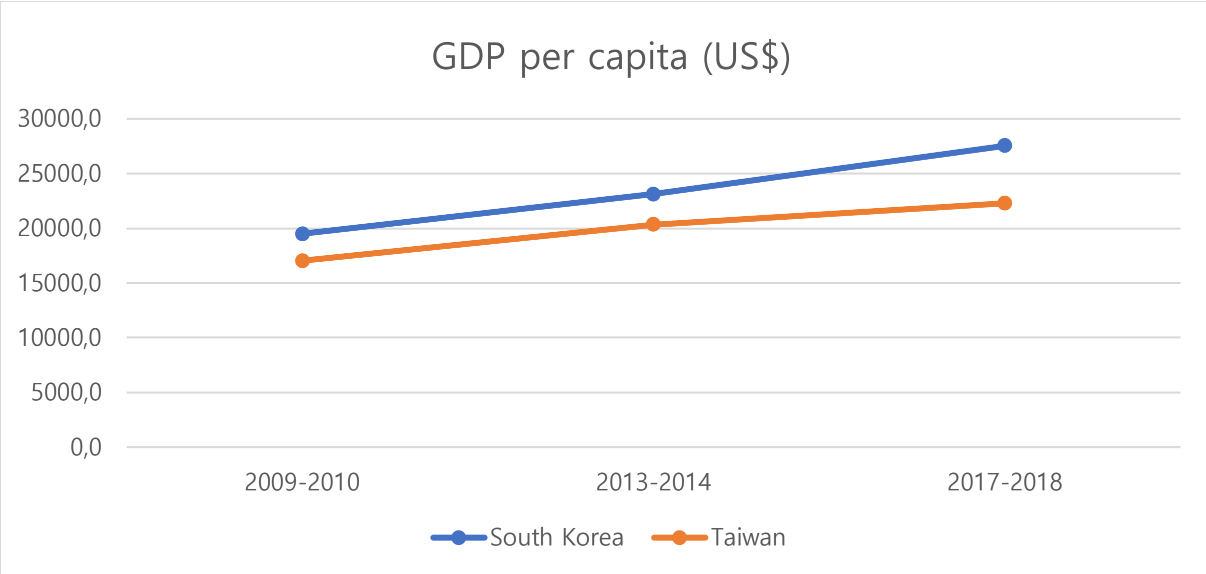
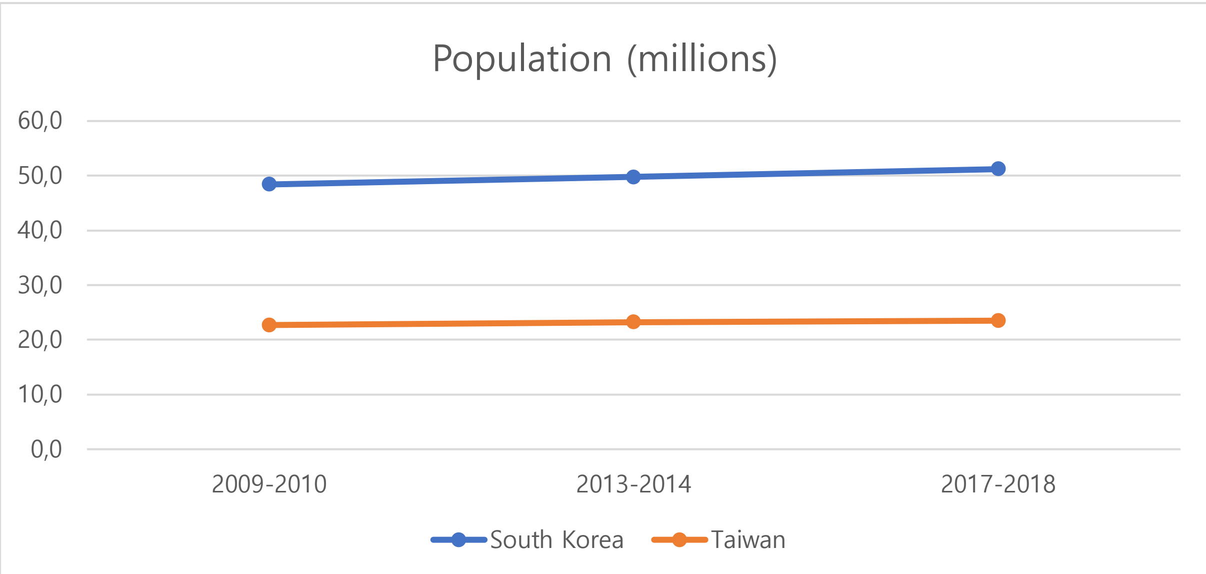
Appendix

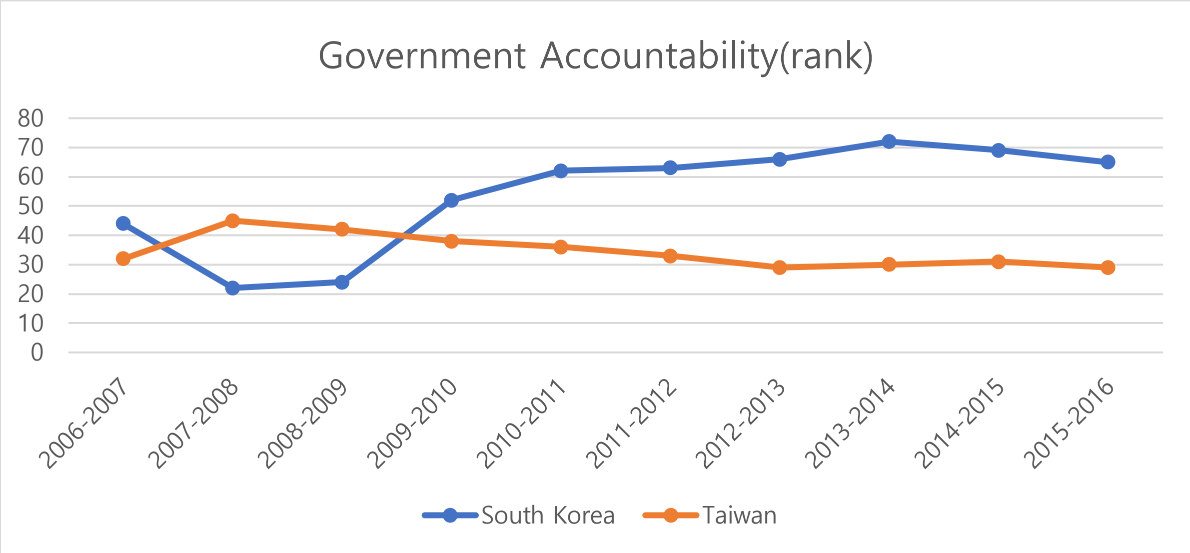
*Data Sources: The Global Competitiveness Index, World Economic Forum (2005-2019)

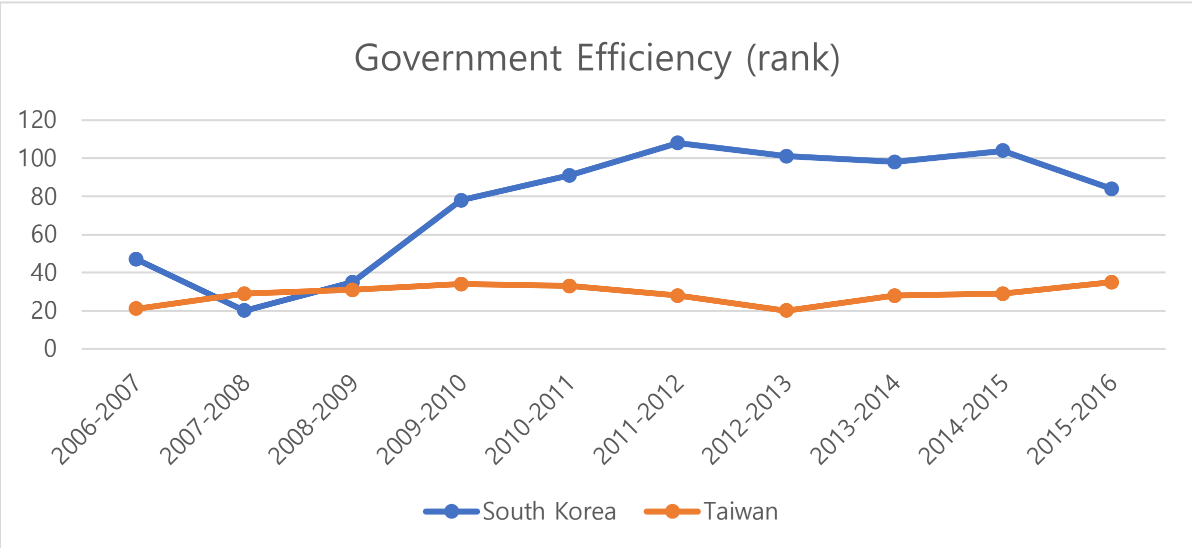
1. Economic Profile

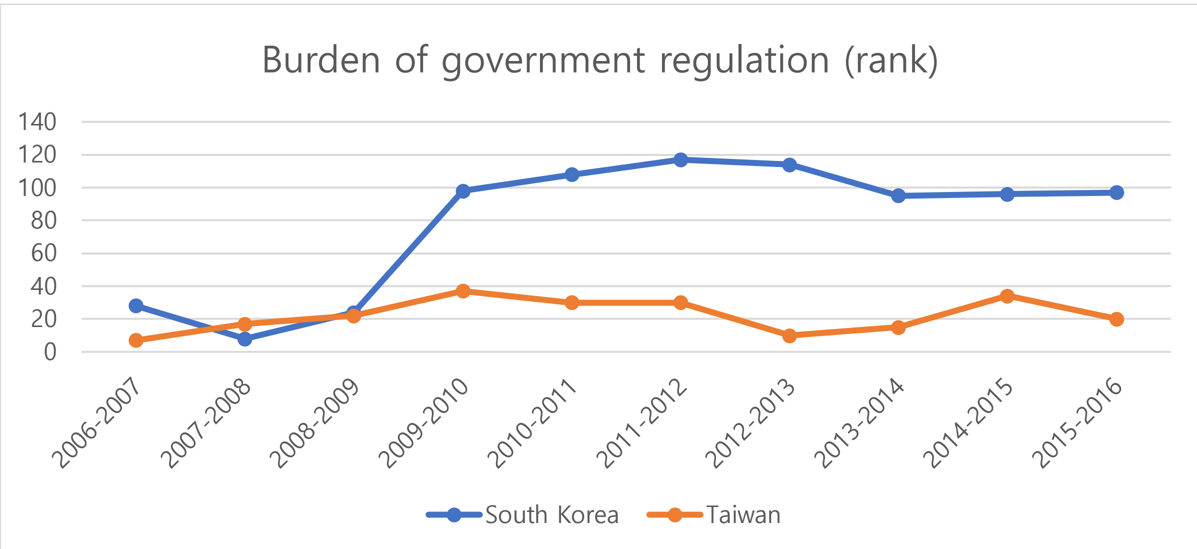




2. Government (rank, the lower rank indicates the higher value)







3. Market (rank, the lower rank indicates the higher value)