

# South Korea – “The Miracle of Han River”

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## 1. Introduction

South Korea, a name so intimate with the worldwide manufacturing industry of the 21st century has come a long way, bewildering the economists of the world through its spectacular growth in the last five decades. Surprisingly, this journey of South Korea from the rags to riches took not more than one generation. This rapid journey from a developing country to a developed country is popularly known as the “*Miracle of Han river*”.

The objective of the paper is to shed light through various angles on the factors responsible for this miracle. In the following section, we will contrast the Third World Korea of 1960s with the First World Korea of the 21<sup>st</sup> century. In the later sections, we will explain the major growth factors - the Korean society and culture followed by a section on the leadership and government in South Korea which created a propitious climate for rapid economy growth. We will briefly analyze the neutral and non-neutral economic policies of the Korean government leading to this unimaginable transformation. In the penultimate section, we will have a look at the Korean economy through the macroeconomic principles of the Solow and Romer Growth model.

## 2. A contrast between South Korea of 1950s and today's

Its GDP which was just US\$2.7 billion in 1962 took a leap and attained a high value of US\$230 billion in 1989 at a whopping growth rate of over 8 percent per year and the story continued leading it to cross the trillion dollar mark in 2006. The exponential growth can be gauged from the fact that its GDP per capita which was a meagre \$103.88 in 1962 reached an unimaginable value of \$20,000 in 2006. Even the ratio of domestic savings to GNP rose from 3.3 percent in 1962 to 35.8 percent in 1989 which actually suggests the immense wealth among the commons.

According to Larry Westphal, the manufactured products constitute over 90 percent of total GNP (in 1990) from a meagre 3 percent in 1960s. A country which was plagued with low savings rate to various other economic shortcomings such as a tiny domestic market and an unskilled labor went on to adopt an outward-looking strategy in 1960s and began its economic growth through labor-intensive manufactured exports. The fruits of this impressive economic growth were reaped by the people and could be verified from the fact that the urban population grew from 14.5% to 65.4% within a period ranging from 1945 to 1985. Even Seoul went on to become the largest urban settlement beating the likes of some of the cities in US and other European economies. There were very evident improvements in the living standards throughout this period. More and more planned urban settlements started coming up, improvements in the medical facilities which in fact increased the health and life span of its citizens, government took up various measures to uplift the education which could potentially accrue in the form of skilled labor.

Beginning its journey from being an economic wasteland to becoming the world's 11<sup>th</sup> largest economy, it put up before the world an exemplary story of nation-building. During the last five decades, its incredible growth has culminated into its being one of the most high-tech industrialized economies of the world. Though there were some major economic jolts such as the Asian Financial Crisis and the recession of 2008, the brief periods of its economic slump are well masked by the stupendous show of its economic growth during the past five decades. Thus, there is definitely a huge contrast in the economic conditions of this country in the last five decades but what has remained intact is the country's perseverance to sustain and even augment further its figures.

## 3. The Confucius Connection – the Korean Culture

Hofstede et. al. define culture as “collective programming of mind that distinguishes the members of one category of people from those of another”. Cultural ideas inherited by South Korean people have played an important role in the establishment of successful business activities which have helped the nation to outperform others in terms of economic growth and development. Futurologist Herman Kahn has labelled the culture of East Asian countries like South Korea as “Neo-Confucian”- that is based on the teachings of Confucius. In Korea, Confucianism has a strong influence on family relationships, political attitudes, problem solving approaches and many other aspects of life. Confucianism emphasizes on various aspects like persistence, ordering relationships by status, the quality of utilizing of one's resources with in a rational

manner and having a sense of shame for wrong doings. The studies and experiments done by various organizations like IBM and Chinese Value Survey clearly indicate that the countries which score high on Confucian ideas are strongly associated with high economic growth. The boom in their economy can also be related to their belief in traditions, reciprocation of greeting, favors and gifts. South Korean economy developed on the path of assimilation of capitalism. Correspondingly, Confucianism can undoubtedly be considered a favorable factor giving an impetus to the establishment of concord conditions which result in a community-oriented society which further adds to the input factors for the growth of the country. As per the Confucian culture, the practice of the Korean firms being operated by kin of the owner's family is quite common and much prevalent in Korea. Korean firms also indulge in exchanging of money within a family. This clan-culture helps to evolve unity and reduces losses due to conflicts. South Korean society has always been a proponent of fostering harmonious interpersonal relationships. Some other qualities such as cooperation and social solidarity among the members of an organization have played a vital role in development of Korean economy. It is quite clear from the understanding of Korean culture that Confucianism is one of the major reasons responsible for the boom in South Korean economy.

#### 4. The South Korean Society

With the onset of the economic developments in South Korea, a middle class society (bourgeoisie) prevailed the social landscape. Though the *yangban* aristocracy had an upper hand in the ownership of land, educational system and the civil service examinations, the emerging middle class played a crucial role in the economy and demanded attention in the economic and political landscape. The present capitalism in South Korea was actually incorporated by its colonial masters (Japan) which eventually provided access to a market of sufficient size and dynamism and resulted in a chain of prolonged capital accumulation. Surprisingly, it was this Korean bourgeoisie that accepted this capitalism so easily and co-existed comfortably with the authoritarian governments. From these commoners emerged the entrepreneurs who skillfully took advantage of every major economic opportunity. For instance, South Korea's participation in the Vietnam War also gave a number of entrepreneurs, especially in the transport and construction industries, a substantial boost in the late 1960s. Some positives such as the elevation of the status of women in society and the decline of extended-family system in turn boosted the factors of growth since these led to an increase in the labor force as well as the consumption.

Over time big business groups have developed in South Korea called *chaebol*, which dominate the South Korean economy, and currently Samsung and Hyundai, are among the fifty largest industrial firms in the world. Though there has been an egalitarian system in South Korea, the absence of a social revolution in South Korea, moreover, has prevented the influx of liberal, or even radical, ideas into the country, it is the state that has always structured and controlled the educational and legal systems. People do enjoy the fundamental rights but the bourgeoisie press is still censored by the state. The elite of the society have shown their support for authoritarian politics since they are the majority stakeholders in the conglomerates. Undoubtedly Korea's capitalist elite have succeeded in exhibiting intelligence in developing their companies, but we can't neglect the fact that they have historically been the recipients of a series of special privileges and favors from the state. It can be claimed unanimously that all sections of the society are not on equal footing at least in economic status.

The recent times have showed us there is a definite shrinkage in the number of households being identified as being middle class which must be taken as a positive effect of the proliferation of ideals of other civilizations in the society. Although, Bourgeois political power in South Korea is clearly growing, it is still trivial in both scope and impact from what has traditionally been wielded by the *yangban*.

#### 5. Korean leaders and government and its Miraculous Economic Policies

The government has always played a crucial role in giving an impetus to the economy. Be it supporting the entrepreneurs in the 1960s to the providing of financial stages, government has played an inevitable role in the establishment and sustenance of multinational companies like Samsung, LG, Hyundai and Daewoo, although financial dependence on the state has been a reflection of the scarcity of available private domestic capital, especially after the Korean War. Also it's because of the desire on the part of the country's various regimes, including the colonial Government-General, to maintain control over the allocation and flow of capital and credit for both economic and political reasons. Later also in post-colonial period through their ownership or supervision of all of the country's banks, government had the prerogative to decide the interest rates, and control the approval and guarantee of all commercial loans and investments from foreign countries, and thus was able to direct capital toward targeted industries.

In the 1960s, the state adopted an outward-oriented development strategy based on the inducement of foreign capital and technology and the promotion of exports. In the 1960s, the dominating economic activity in the Korean economy was primary sector comprising of agriculture and mining. During the course of rapid growth, the Korean economy has evolved with its increasing reliance on the manufacturing sector. The Korean government has practiced selective state intervention virtually free-trade to evolve a unique development strategy – ‘export led industrialization’. The rapid and equitable transformation can be ascribed to a great extent to the economic policies of Korean government explained as follows:

- *Stimulating exports industries using neutral policies*  
The industrial policies provided stimulus to exports business by inducing an environment of virtual free trade and thus making it easy to procure capital and intermediate inputs relaxing the quotas and tariffs. Also, unitary exchange rate was introduced and managed in place of multiple exchange rate to equate the world and domestic prices. The Korean government also provided the exporters with easy finance options in proportion to their export activity. The government decided the export targets for all commodity segments on quarterly basis and the Korean ministers kept a close vigil to identify any potential shortfall in the exports. The highest exporting businesses were awarded while those resorting to indolence were deterred.
- *Encouraging infant industries using non-neutral policies*  
The Korean economy policy has promoted, protected and sometimes involved in the creation of infant industries dealing in cement, fertilizers, steel, petrochemicals, etc. These ventures were provided with both long and short term credits and impunity against direct and indirect taxes. Several import controls were instituted to provide “absolute” protection to these infant industries. The government has been successful in creating market agents such as Samsung, Chaebol, Daewoo and Hyundai to foster infant industries in South Korea.

It was a landmark decision to open the South Korean economy to the larger capitalist world and thus it has been instrumental in developing the knowledge and experience of the private sector to a point where it is now as or more capable of making sound economic decisions than the state, especially in the context of the growing complexity of both the South Korean and the world economies.

## 7. Solow and Romer Growth Model

Solow long run economic growth model developed by Robert Solow provides an explanation to long run economic growth of any nation by considering factors such as capital accumulation, labor or population growth and change in productivity. This model appears to explain growth of South Korean economy in a way conforming to the numerical observations of growth. The intervention of military rule in 1961 in the nation brought a change in the exchange rate system, led to devaluation of currency, raised the real interest rate and brought in effect a number of wide-ranging reforms. These reforms were in accordance with Solow’s model. Domestic savings and investment by people saw a surge. Rapid technological upgrades and a stunning transformation in the composition of output took place due to accumulation of capital contributed primarily by domestic saving. The nation experienced a rapid shift in labor and population growth due to government policies which led to rapid industrialization. This shift was accompanied with a rise in female labor force participation. All these factors are in perfect agreement with the Solow model.

Romer model emphasizes the importance of human capital investment, innovation, R&D and knowledge in the economic growth of a nation. South Koreans owe their economic development to high level of investment in education and human capital. According to the policy makers of South Korea, high labor productivity is essentially a product of human capital investment. Besides this human capital is indispensable for a continued growth through innovation and moreover is equally necessary for the assimilation of ideas and techniques globally. The heart of South Korean economy transformation lies in development and innovation investment. Innovation in technology, research and development are the major pillars that have supported South Korean export competitiveness and fuelled the country's remarkable economic rise over the past decades. The Organization for Economic Co-operation and Development (OECD) released a survey data showing that R&D constitutes 4.29% of the GDP of South Korea. For the South Korean companies, innovation and R&D activities are essential to face the cutting-edge competition in the era of globalization. Large multinational organizations like Samsung, LG also have invested heavily in research, development and innovation. These multinationals

have gained major share of the electronics market around the world and their world-class products are a result of the sincere efforts put in research and development.

## 8. Conclusion

The growth in the last 50 years has been quite robust to the impediments coming in the way of development and has led to South Korea becoming one of the wealthiest countries in the world. The Korean government's economic policies have become an exemplary role model for many third world countries in the world. The x-factor for the consistent growth is its macroeconomic stability – Asian Financial Markets Crisis which plagued the various economies of the world in 1990s had a severe effect on the economy and hence the country embarked on a path of economic reforms with the aim of making the country's growth model more robust to economic shocks. The economy was only one of the few nations that shielded itself against the recession in 2009. Government has also succeeded in keeping the consumer price inflation and unemployment levels low. With a national debt less than 40% of GDP the country has definitely outperformed various economies of the world. Further the country is still doing well and is destined to excel even more if it continues to tread the similar path with a concoction of non-linear and resilient thinking, adaptability and constant innovation. Hence these enviable stats conform to the exceedingly well implemented schemes and the stupendous economic growth. Truly the stunning growth of South Korea can be branded no less than as the

“MIRACLE OF HAN RIVER” !!!!

## 9. References

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