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Is Economic Progress Compatible with Democracy?

I. Introduction

The Korean economy has succeeded in making great transition from a poor agrarian nation to an industrial modern nation. For almost ten years after the end of the Second World War, Korean people were still living in misery compared with other less-developed nations such as Taiwan, Singapore and Hong Kong, which are the newly industrializing countries of East Asia.

In 1950, the outbreak of the Korean War totally demolished the social and industrial infrastructure of Korea. For example, the Korean War destroyed as much as 45% of all industrial establishments.¹⁾ And, in the Seoul area, the ratio of destruction of industrial complexes and public utilities was above 80% while that of office building and housing was almost 75% and 50%, respectively.

Since the end of the Korean war(1950-53), the Korean people were still shackled by political instability. The First Republic regime of President Syungman Rhee became brazenly autocratic until it was overthrown in April 1960 by a massive "Student Uprising."²⁾ Though the Second Republic Premier Myon Chang tried to run his regime along the lines of a western style democracy complete with institutionalized corruption reform programs, it was almost impossible to sustain such a government due to the avalanche of accumulated problems.

The history of rapid development in Korea began with the military coup d'état executed by General Chung Hee Park. The military junta under Park which led the Third through the Fifth Republic for 26 years from 1961 to 1987, was unequivocally authoritarian. Nevertheless, Korea succeeded in making tremendous economic achievements under President Park's rule.

In 1953, the per capita GNP was only about \$ 67.³⁾ By 1995, the per capita GNP

1. Byeong-Ho Gong, *The Power Shift of Korean Economy*(in Korean), Chang-Hae Publishing Co., 1995, p.23.

2. John Kie-Chiang Oh, *Korea's Democracy on Trail*, Cornell University Press, 1968, p.51-71.

3. The Bureau of Statistics, *The Review of the Korean Economy in terms of Statistics*(in Korean), 1995, p.315.

was \$10,076, and South Korea's GNP was the 11th largest in the world.⁴⁾⁵⁾ The performance resulted in Korea being dubbed the 'Han-River Miracle'.⁶⁾

For anyone interested in economic development, the experience of the Korean economy is a very interesting and useful example. Specifically, many scholars, economists, and politicians in developing countries usually have an important question : How did Korea achieve its rapid growth over the last 30 years?

In describing the economic development of Korea, the stereotypical hypothesis is that Korea is an example of 'authoritarianism-capitalism nexus'.⁷⁾ In his examination of the success story of East-Asian nations, Chalmers Johnson emphasizes two types of authoritarian governments-one being 'a soft authoritarian' government such as Japan, the other being a 'hard state' such as Korea and Taiwan.⁸⁾

In both types of governments, authoritarianism has played a key role in developing the economy. Generally speaking, Japan is a successful case of economic development by governmental industrial policy. Government intervention to achieve its national goals is regarded as 'plan rationality', which is contrasted with 'market rationality'.⁹⁾ In Japan, the market is not replaced by the state. However, the market mechanism is heavily constrained and led by the industrial policy, which is designed by the bureaucratic elite.

As for Korea, in the name of political stability for the sake of economic growth, the authoritarian government suppressed human rights and the labor movements, meaning that fewer civil liberties could be enjoyed by the Korean people. On the other, however, they succeeded in escaping serious poverty and in bringing material prosperity to the nation.

Additionally, many scholars have argued that the role of bureaucrats and politicians

4. Korea Development Institute, *The Report on the Korean Economy in the 21st Century*, 1996.

5. Around 1950, the per capita GNP is as follows: Japan 163\$(1951), Thailand 102\$(1950), Burma 35\$(1951) and so forth. Sung-Je Go, *The Theory of Korean Economy*(In Korean), Iljokwak, 1952, p.338.

6. Even though the Korean economy has recorded a rapid growth rate in the last 30 years, the quality of life in the Korea lags behind the advanced nations such as the eight member nations of the OECD. One study, which was done by the Seoul National University, indicates that in the comparison with the advanced nations, the level of Korea is around 50% with respect to objective and subjective material index and subjective non-material index such as human rights, leisure and so forth.

7. Chalmers Johnson, "Political Institutions and Economic Performance: The Government-Business Relationship in Japan, South Korea and Taiwan." In Frederic C. Deyo, ed., *The Political Economy of the New Asian Industrialism*. Cornell University Press, 1987, p.136.

8. Chalmers Johnson(1987), p.137.

9. Chalmers Johnson, *MITI and the Japanese Miracles*, University of California Press, 1984, p.18-26.

has been important in economic development.¹⁰⁾ They argue that the division of labor between the government and business sectors has facilitated the accomplishment of goals.

According to this theory, government is the driver and business is the engine in a car. The relationship between government and business is not parallel but hierarchical in character. Therefore, Korea's economic development is basically the result of authoritarian state leadership or, at most, a 'synergy between government and business. In describing this phenomenon, the scholar Alice Amsden invented the terminology 'Incorporated, as in Japan Inc. or Korea Inc.'¹¹⁾

Recently, a few scholars have been putting forward quite a different view.¹²⁾ They maintain that the role of the authoritarian government has been too heavily justified without enough concrete evidence. A current research paper sheds a different light on the hidden issue of Korea's success story and then warns about the misconceptions surrounding the idea of a wise and benevolent authoritarian government. The paper says, I quote :

"First, the argument that Korean economic development results from the guidance of an authoritarian government and its industrial planning is misleading. The authoritarian Chung Hee Park's administration implanted this statement into the popular consciousness of Korea, and used it both for overcoming its lack of legitimacy generated by the social and economic contradictions and for getting popular support. The role of the Korean state in economic growth has been exaggerated by some state theorists as well as in academic circles around the government. Overall, the business sector, who should have received most of credit for economic growth, has been considered as a dependent variable.

A careful examination of the success of the electronics and automobiles industries

10. Alice H. Amsden, *Asia's Next Giant: South Korea and Late Industrialization*, Oxford University Press, 1989, Leroy Jones and IL Sakong, *Government, Business, and Entrepreneurship in Economic Development: The Korean Case*, Harvard University Press, 1980, World Bank, *The East Asian Miracle: Economic Growth and Public Policy*, Oxford University Press, 1993, Robert Wade, "East Asia's Economic Success: Conflicting Perspectives, Partial Insights, Shaky Evidence." *World Politics* 44(2), 1992, p.270-320.

11. Amsden(1989).

12. Young-Yong Kim and Young-Duk Jeon, *Institutional Change and Economic Progress in Korea*(In Korean), The KERI Center for Free Enterprise, forthcoming in January, 1997, In-Young Kim, *The Political Economy of A Chaebol's Capital Accumulation in South Korea: The Case of Samsung, 1938-1987*, Ph.D. dissertation of The University of Hawai'i at Monoa, 1996, and Byeong-Ho Gong(1995).

in Korea disproves the claim that economic success can be attributed to the bureaucrats' shrewd investment guidance promotion of key industries. The claim simply misses the point that the Korean bureaucrats often failed to perceive the technological complexity of the automobile and semiconductor manufacturing sectors"¹³⁾

Most people still subscribe to the popular myth that an authoritarian government is necessary at the early stage of development. Arising from this, people also tend to draw the mistaken conclusion that the government should take the initiative in accelerating economic development and that by doing so it can maximize the effect of industrial policy. Despite these fallacious interpretations, research into the opposite point of view is still at early stage.

In this paper, I would like to explore the relationship between economic progress and democracy. In particular, I would like to examine the question : Is economic progress compatible with democracy? In this regard, I believe the experience of Korea shows us a general pattern between economic progress between democracy.

Additionally, I also would like to evaluate the role of government in economic development. In particular, I would like to examine the assumptions that the active role of government is justified in the early stages of economic development. Also, based on Korea's example, I would like to look at the assertion that the adoption of goal-oriented economic development plans by such governments are unconditionally positive and that as a result it is reasonable to assume that other developing countries should follow this model.

This paper consists of the following : Chapter II gives a general perspective of the relationship between economic progress and democracy and also discusses the effectiveness of active government intervention. Chapter III investigates two kinds of hypothesis using the experience of Korea. Finally, the last chapter summarizes the results and thus derives some lessons.

13. In-Young Kim(1996), p.218.

II. General Perspective : Economic Progress and Democracy

(1) Is Economic Progress Compatible with Democracy?

Let me start this chapter by defining 'democracy'. As you know, there are so many types of democracy such as liberal democracy, people's democracy, social democracy and so on. To remember the true meaning of democracy, it is necessary to trace the evolution of democracy since its origins in Athens, Greece.

The democracy of Athens, around the fifth century B.C., is considered as a classic model of democracy. Having remained dormant for centuries, democracy slowly evolved in England and France and reemerged in America with the birth of the new nation. Through its long history, democracy has evolved into several variations on the original theme, such as social democracy and people's democracy.

In this paper, I would like to use the term 'democracy' in the sense of liberal democracy, which is characterized by the existence of electoral competition among politicians and parties for governmental powers and also principles like the rule of law and the separation of politics and the marketplace.

At an early stage of economic development, people are so preoccupied with obtaining the basic necessities that they have little time for thinking about political-economic systems. In addition to that, the system of democracy and the free market economy is a sort of public good and thus people don't have any incentive to correct the weak points of the system and to invest enough time and energy to participate in the reform movement of the system.

If people succeed in overcoming their miserable circumstances, they need to have more political and economic freedom. In the transition period between being a poor nation and a wealthy nation, conflict between the government and the people is inevitable. However, eventually, such conflict results in the government conceding power to the people. As people become wealthier, a free market economy becomes virtually prerequisite for a stable democracy. This process whereby, it is argued, prosperity stimulates democracy, is called the Lipset hypothesis.¹⁴⁾

Recently, some scholars have furnished enough evidence to support the above-mentioned argument. According to Robert Barro, improvements in living

14. Seymour Martin Lipset, "Some Social Requisites of Democracy: Economic Development and Political Legitimacy", *American Political Science Review*, 1959, 53, p.69-105.

standards promote democracy.¹⁵⁾ Barro talks about the relationship between democracy and economic progress at the early stage of development as follows.

“A panel study of 100 countries from 1960 to 1994 strongly supports the idea that improvements in a country’s standard of living predict increases in democracy (as measured by a subjective indicator of political freedom). Democratic tendency rises with real per capita GNP, life expectancy, and a smaller gap between male and female primary schooling.”¹⁶⁾

However, the Lipset hypothesis is not effective all the time. As people get wealthy, they develop an attachment to the ideology of majority rule, which is the key concept in democracy. As the result, majority rule filters into all aspects of life, both political and economic. Thus, the free market economy is slowly replaced by the political process, which is justified by the majority. The needs of the majority give rise to new legislation and changes in the current law.

Democracies with unlimited or nearly unlimited jurisdiction for simple majorities of the population or representative parliaments tend to erode the basic principle of the free market economy, such as safeguarding property rights and reinforcing the rule of law, and increase government activity. This, in turn, diminishes efficiency, savings, productive investment and innovation in the market and leads to situations perceived as crises by the population.

Peter Bernholz in the Mont Pelerin Society explains that the development of unlimited democracy eventually erodes the foundations of free market economy. Even though the below-mentioned citation is a little long, it is worthy of quotation.

“Democracy is no precondition for a capitalist market economy, as can be seen from the example of Hong Kong, Chile under Pinochet and South Korea under Park. Moreover, democracy may even endanger a free market economy in the long run. . . . This usually occurs in unlimited or scarcely limited total democracies. By a total democracy I understand a democratic regime which is not restricted in its jurisdiction by constitutional or other safeguards. Thus shifting majorities in parliament, i.e., small minorities of the population only inadequately controlled by

15. Robert J. Barro, “Determinants of Democracy”, a discussion paper in the Mont Pelerin Society, General Meeting, September 8-13, 1996.

16. Robert J. Barro(1996), p.1

rationally uniformed voters, can enforce their goals on the rest of the population. Since several parties compete for voters and need financial support to cover the expenses for their organizations and for election campaigns, one has to expect in time an ever increasing sphere of government activities. Thus growing public expenditures, more and more regulations by government, tax loopholes and subsidies to special minority interests and pressure groups, flow from the incessant activity of legislative bodies. This is true for issues in which decisions impinge only marginally on the situation of consumers or taxpayers, since they then have little reason to incur the costs of informing themselves, given the negligible effect of individual votes on election outcomes.”¹⁷⁾

If I investigate several advanced countries like America, Japan, England, Germany, France and so forth, I have a confidence that there exists a stereotypical road from poor nation to unlimited democracy. As far as I know, it is not easy for any country to deviate from the pre-ordained path toward unlimited democracy. For example, in carefully examining the political process in England after the end of the Second World War, one must conclude that following such a path is almost inevitable.

This may be partially attributed to the growth of interest groups under the structure of current democracy.¹⁸⁾ The suggestion that the increasing effect of interest groups on democracy by the economist Mancur Olson, is very powerful in explaining the common problems most nations will face in the process of economic development. He suggests a hypothesis that economic stagnation can be traced to the growing proliferation of interest groups that occurs in stable democratic societies.

In the absence of external shocks such as war and revolutions, a society's organizational ability tends to go increasingly into the creation of new distributional cartels that accelerates the rigidities of economy. He says, “countries that have had democratic freedom of organization without upheaval or invasion, will suffer the most from growth-repressing organizations and combinations.”¹⁹⁾ Olson also insists

17. Peter Bernholz, “Necessary and Sufficient Conditions for a Viable Democracy”, a discussion paper in the Mont Pelerin Society, General Meeting, September 8-13, 1996. 3.

18. Mancur L. Olson, *The Rise and Decline of Nations*, Yale University Press, 1982, Francis Fukuyama, *Trust*, Free Press, 1995.

19. Mancur Olson(1982), p.77.

that one of the main reasons for the British economic decline over the past centuries is the fact that the British experienced a steady increase of efficiency-destroying groups.

At the early stage of economic development, most nations have only a few interest groups and the power of the interest group is not enough to influence the direction of economic policy. In time, it is natural for a society to experience the creation of many interest groups, because of the increase of economic activities and distributional income.

Moreover, the accumulation of wealth enhances the possibility that the government has a strong impact on the distribution of income through various types of subsidies. Because the current democracy has not any break system to reject the systematic and consistent requests of the interest groups, it is clear that interest groups generate an unstoppable momentum of their own, leading to the ongoing creation of new kinds of legislation. Thus, if we maintain the current structure of democracy, it is inevitable that we will become subject to the influence of interest groups. It is this influence which erodes the foundations of the free market economy such as private property rights and small government. I would like to label this kind of phenomenon as the tragedy of unlimited democracy.

Many interest groups maximize the use of political slogans on the basis of 'social justice' and 'distributional justice' and thus the majority of people tend to support the needs of interest groups. Therefore, the popularity of unlimited democracy eventually leads to high tax rates, subsidies and discriminative legislation. People do not work hard and they want to enjoy a free-ride. Slogans like 'Less Work and More Welfare' give a distorted incentive structure for the ordinary people.

Unlimited democracy replaces free market and private property with more government interventions in the form of regulations and planning. This development, however, leads in time to decreasing efficiency and freedom and reduces productive investment and innovative activity. Resources are misallocated and growth rates fall.

As a consequence, after some time the political-economic system moves into a crisis engendering widespread voter dissatisfaction. And this, in turn, brings calls for reforms. At this time, the characteristic of the reform will decide the future of the nation. Nowadays many people are paying attention to the success of New Zealand's economic reform. After a long period of socialization in the market economy, New

Zealand entered an economic crisis, with low growth rates, a high unemployment rate, and high inflation rates. However, not every nation that hits on economic crisis has a chance to find the right way out. In a crisis situation, there are always severe conflicts about the direction of economic reform. Peter Bernholz emphasizes the influences of ideologies on economic reform during crises as follows :

“Taken generally, different theories and ideologies compete during crises with their often widely diverging proposals for problem solutions. Here, by an ideology, let us understand a worldview, a *Weltanschauung*, which tries to interpret major aspects of the world and their interrelationships. Many such ideologies contain supreme values which have to be pursued to solve the problems of individuals and/or society. Ideologies thus respond to widespread human demands for spiritual goods, for the implied *Weltanschauung* offers safety and provides meaning in an otherwise incomprehensible world. As far as it is shared with others, it offers feelings of warmth and belonging, of safety in the womb of collectivity. Major religions, but also Communism and National-Socialism are examples of such ideologies.”

Summing up the relationship between economic progress and democracy, at the early stage of economic development, economic growth enhances the democracy. However, at the second stage, in which people accumulate wealth, democracy deteriorates into unlimited democracy, which violates market principles like property rights, work incentives and so forth. At the third stage, people enter an economic crisis and thus strongly feel the need for reform. However, it is not easy to choose the right direction of reform because of the conflicts between diverse ideologies.

(2) Does the Active Role of Government Accelerate Economic Development?

People make money by adding knowledge and information to natural resources. Therefore, the essential economic problem facing each nation is how to fully utilize the knowledge and information of the people in the nation. The importance of knowledge as a sort of “brain power” has been almost forgotten. However, Friedrich A Hayek, one of the great scholars of the 20th century, has once again helped us to recognize the true value of knowledge in the real world. He defines knowledge as

follows :

“Price expectations and even the knowledge of current prices are only a very small section of the problem of knowledge as I see it. The wider aspect of the problem of knowledge with which I am concerned is the knowledge of the basic fact of how the different commodities can be obtained and used, (footnote : Knowledge in this sense is more than what is usually described as skill, and the division of knowledge of which we here speak more than is meant by the division of labor. To put it shortly, “skill” refers only to the knowledge of which a person makes use in his trade, while the further knowledge about which we must know something in order to be able to say anything about the processes in society is the knowledge of alternative possibilities of action of which he makes no direct use. It may be added that knowledge, in the sense in which the term is here used, is identical with foresight only in the sense in which all knowledge is capacity to predict.), and under what conditions they are actually obtained and used, that is, the general question of why the subjective data to the different persons correspond to the objective facts.”²⁰⁾

Most economists do not consider economic problems as the problems of knowledge. In this perspective, Hayek makes an invaluable contribution to our understanding of the economic world. Basically, Hayek thinks that knowledge consists of two types. The first one is scientific knowledge, which can be easily communicated through writing or speech. In school, we are educated in scientific knowledge such as mathematics and the sciences. Regardless of a specific place and time, scientific knowledge can be applied everywhere.

However, we should pay attention to another kind of knowledge, which is known as tacit knowledge.²¹⁾ Tacit knowledge has not general, but time and place-specific characteristics. In the market economy, most people are more expert in their jobs than in other economies. Generally speaking, scientific knowledge depends on the duration of education periods. However, tacit knowledge is knowledge which is not

20. Friedrich A. Hayek, “Economics and Knowledge”, *Individualism and Economic Order*, The University of Chicago Press, 1980, p.51-52. Hayek mostly discusses knowledge in the the papers and book, such as “Economics and Knowledge”, “The Use of Knowledge in Society”, “The Pretence of Knowledge”, and *The Fatal Conceit*. Friedrich A. Hayek, *The Fatal Conceit-The Errors of Socialism*, The University of Chicago Press, 1988, p.85-88.

21. The terminology of tacit knowledge originally comes from Michael Polany, *The Tacit Dimension*, Doubleday & Company, INC, 1969..

necessarily dependent on educational background.

For example, most successful businessmen have a sort of know-how, which is called entrepreneurship. Mises emphasizes the role of entrepreneurship as follows. "In any real and living economy, every actor is always an entrepreneur."²²) By this he means that most people have a specific knowledge like tacit knowledge.

Usually, when we talk about the wise role of government, we mean that bureaucrats and politicians use fine-tuning in planning the direction of the economy. A good plan is possible, if the planner has enough knowledge and information about the real world. If we look back on the history of the 20th century, we find that there was very ambitious planning involved in reconstructing the ideal society advocated by socialists and government interventionists.

Most socialists and government interventionists emphasize economic planning as a way to attain national goals, goals which have been very well designed by a few bureaucrats. Their basic idea is based on the strong assumption about types of knowledge. They think that the human is only capable of scientific knowledge and thus can collect all knowledge and manage to increase the efficiency of resources allocation in a society. The socialist idea is a fatal conceit, which makes people bear the burden of costs resulting in its own ultimate collapse.

The knowledge which makes the real world function is tacit knowledge. It is very hard for a few clever planners to derive tacit knowledge from each person, because tacit knowledge is personally embedded into the brain of each human being. In addition to that, tacit knowledge is fragmented and dispersed throughout the members of a society and thus it cannot be collected and managed by an entity such as government. Therefore, every individual, in their own particular environment, is better equipped to make judgements about the task in-hand than any statesman or lawmaker.

Bureaucrats in government are experts in the field of reporting or briefing. However, they are not experts in all kinds of work in the real world. Even though bureaucrats may not have any specific knowledge in the economic field, it is true that they do have general knowledge for economic development. When it is well used, such general knowledge can lay the foundations for entrepreneurship by ensuring political stability, prohibiting the activities of interest groups, and building a

22. Ludwig von Mises, *Human Action*, 1st ed. Yale University Press, 1949, p.253.

sound social infrastructure.

The basic preparation for economic development is attributed to scientific knowledge. It is important for bureaucrats and politicians to accept that they do not have tacit knowledge in economic development. The role of government must not surpass the limits of scientific knowledge. If bureaucrats and politicians have ambitions to use fine-tuning policies based only on scientific knowledge, sound economic development is not possible. Furthermore policies based on scientific knowledge alone can distort the allocation of resources and result in the decline of economic progress.

Summing up the relationship between economic development and the role of government, I suggest that governments should accept the limitations of their tacit knowledge in the real world. That is, if government is involved in fine-tuning (industrial) policies using scientific knowledge, the gap between the real world and theory can have a negative impact on economic development.

III. A Case Study : An Experience from Korea

(1) A Brief History of Korea

As a background for discussion on economic development and democracy, a brief overview of Korea will be useful. Throughout much of its long history, Korea remained secluded from the outside world, especially the western nations. Therefore, the country was often referred to as the Hermit Kingdom or the Orient's Land of the Morning Calm. In the latter part of the 19th century, however, Korea was forced to open its door to Japan and the western powers.

For almost five thousand years, Korea was governed through a sort of traditional 'oriental despotism', like most oriental nations.²³⁾ Under that system, the king would have absolute authority and there was no separation or sharing of power, as seen in the west. Before the Japanese colonization of 1910, the Korean people had no experience of democratic government. Therefore, the most prominent characteristic of

23. K.A. Wittfogel, *Oriental Despotism: A Comparative Study of Total Power*, Yale University Press, 1959.

the modern political heritage in Korea may be summarized as authoritarianism.

During the colonial era of 1910 to 1945, the administration of the colonial regime in many ways resembled an authoritarian government, with Korea being exploited as a source of food supplies to the Japanese until the 1930s. However, as time went by, the policy of the Japanese toward Korea became more oriented to industrialization, reflecting Japan's imperialistic ambitions. During this time, the share of manufacturing in net commodity-product grew from less than 4 percent to over 20 percent.²⁴⁾

However, with the Japanese failure in the Second World War, Korea won independence. For the first time in its history, Korea turned to a democratic system of government, resulting in the foundation of the Republic of Korea in 1948. But the Republic of Korea only consisted of people in the southern part of the Korea peninsula, while the people in the northern part established the communist based People's Democratic Republic of Korea (commonly known as North Korea).

Economically, the distribution of industrial establishments was quite unfair between South Korea and North Korea at the time of independence. That was because the Japanese paid more attention to the development of the northern part. For example, North Korea produced 90 percent of the nation's electricity and accounted for almost 80 percent of mining output. Between 80 and 90 percent of chemicals and metal products were produced in the North.

After the division of the Korea peninsula, the Korean War (1950-53) broke out. This war destroyed almost two-thirds of the nation's production capacity, and almost 1 million civilians were killed. Total industrial production in 1953 was estimated to be not much more than one-third of the production level of 1940.²⁵⁾

The President of the First Republic, Syungman Rhee was elected in the first general election in 1948 at the age of 73. And the Rhee administration became a crisis government during the period of national emergency occasioned by the Korean War. Faced with the huge task of reconstructing a war-torn nation, the government became strongly autocratic until it was overthrown in April 1960 by a massive "Student Uprising".

24. Il Sakong, *Korea in the World Economy*, Institute for International Economics, 1993, p.1.

25. Frank, Charlse R., Kwang S.Kim, and Larry E.Westphal, *Foreign Trade Regimes & Economic Development: South Korea*, Vol. 7, National Bureau of Economic Research, Columbia University Press, 1975, p.9.

During the regime of President Rhee, the average growth rate was almost 5 percent with this relatively strong economic growth was partially made possible by massive American economic assistance. President Rhee devoted his leadership energy primarily to solidifying the new nation and rehabilitating the Korean economy. During the First Republic, Korea laid a foundation for successful outward-oriented economic growth by investing in education, introducing land reform, and completing the first stage of import substitution.

However, no cohesive economic development program was initiated during the Rhee period. Rhee's determined role in holding the infant republic together during the darkest days of the Korean War should not be underestimated. However, there were many problems. In particular, the aging and increasingly bad-tempered autocrat is sometimes accused of not doing enough to push forward with economic development.

After the 'Student Uprising', the so-called democratic Second Republic was established in 1960. The Council for Economic Development of the Second Republic announced an ambitious economic planning in December 1960, which was a draft five-year plan for economic development. The draft was followed by additional details announced by the Council in February in 1961.²⁶⁾ The plan, which emphasized land development, reforestation, road and dam construction was to be implemented from 1961. However, its implementation was thwarted by a military coup.

The military coup d'etat of General Park opened a new way for political and economical development in Korea in that it transformed the government from a quasi-democratic one into an authoritarian one. Despite the authoritarian government, Korea witnessed the emergence of a political leadership committed to economic development. This commitment was realized in the form of economic actions and policies such as the adoption of an outward-looking development strategy, active inducement of foreign capital, and various institutional reforms. During the 1961-79 period, President Park executed the Five-Year Economic Development Plans and succeed in making rapid economic progress.

If we look at the ideas of President Park, we can get a clear picture of the

26. Won-Chul Oh, *The Korean-Style Economic Development*(in Korean), Kia Economic Institute Korea Economic, 1996, p.?

characteristics of the Third Republic. In a strikingly revealing statement, Park declared that most Asian countries, including Korea,

“have to resort to undemocratic and extraordinary measures in order to improve the living conditions of the masses. . . . One cannot deny that people are more frightened of poverty and hunger than totalitarianism. . . .”²⁷⁾

“Park summed up his political-economic goals : The purpose of this revolution is to reconstruct the nation and establish a self-sustaining economy, and its essential purpose is to restore to all the people the political and economic systems that had become the possession of a few privileged classes.”²⁸⁾

After the assassination of President Park in 1979, General Du Hwan Chun came to power using a sort of coup’etat, and became the President using an indirect election. The regime of President Chun was still authoritarian and also used the same economic strategy of outward-oriented development. In managing the economy, the new government had to shift gears toward private initiatives and away from government intervention while reforming the nations’s economic structural abnormalities. Stabilization and liberalization programs were implemented simultaneously with strong leadership initiatives. Generally speaking, the performance of the economy under President Chun was fairly good.

In 1988, the Sixth Republic was inaugurated under the leadership of President Tae Woo Rho, who came from a military background and was a close friend of President Chun. Unlike the Chun government, the Sixth Republic was close to a democratic one. During the Sixth Republic, the demands of labor unions drove up wages excessively. As the result, Korea began to seriously worry about losing its competitive edge in many industrial sectors.

In 1992, the Korean government was peacefully replaced by a popular civilian President, Young Sam Kim. The economic performance has not been quite as good as the past, with various interest groups eargely vying against each other. Now Korean people face an entirely new set of challenges.

27. John Kie-Chinag Oh(1990), p.28.

28. Chung Hee Park, *The Country, the Revolution and I*(in Korean), Hyanmunsa, 1963, p.105.

(2) Economic Progress and Democracy

Whenever we evaluate economic development in Korea, we can ask one important question : Is it necessary for a nation to have an authoritarian government in order to achieve rapid economic development? After all, some people argue, the authoritarian government cannot endure for long and is therefore just a temporary tool to get the nation on target for economic development for a certain period.

If we confine the relationship between economic development and democracy to the experience of Korea, it is reasonable to speculate that under the First and the Second Republics(1948-60), it was almost impossible to achieve rapid economic progress. The reason is that countries cannot have economic progress without political stability.

However, political stability does mean that we should shy away from democracy and opt for strong leadership at any cost. The experience of Korea at the early stage of development does not indicate that it is necessary to accept or tolerate authoritarian rule as a pre-condition of economic development.²⁹⁾ Rather, it strongly suggests that the pre-condition of economic progress is a strong leadership that properly understands economic problems and has the capability to persuade people to accept institutional reforms for development, and then to consistently seek the right solutions. Especially, in Korea, politics and economics certainly have been closely interwoven, since the President has enjoyed relatively strong power in the separation of powers among the three branches of government.

In the First Republic, the President did not pay attention to the economy. He was a politically-oriented person who knew and cared little about the Korean economy. The first consideration by Rhee in appointing cabinet members was their personal relationship or loyalty to him, with scant attention paid to their expertise or experience. As a result, his cabinet members did not have any incentive to focus attention on economic problems.

John Kie-Chiang Oh talks about the choices of President Rhee as follows :

“Rhee appointed and abruptly dismissed cabinet ministers largely to strengthen his political control. To economy-related ministers, namely, Finance and Agriculture, he

29. Duck-Woo Nam, “Korea’s Economic Takeoff in Retrospect”, In Sung Weung Kwack, ed., *The Korean Economy at a Crossroad*, Praeger, 1994, p.6.

appointed a total of 23 ministers from 1948 to 1953. Of the eight Finance Ministers, only two could list their immediate previous occupation as economy-related. These two were bankers. Of the 15 Ministers of Agriculture, only two were from farming backgrounds.³⁰⁾

There exist two conflicting views about the economic situation in the First Republic. One is to emphasize the misery, as we can see from this example :

“Korea under Rhee was an almost totally nonfunctional society economically. Toward the end of Rhee’s regime in 1959, Korea’s per capita income was estimated at about \$81. Inflation also spiraled during the period. Between 1945 and 1957, whole sale prices increased 1,840 times, and retail prices 1,890 times. The ordinary Korean people barely subsisted, while the President was preoccupied with politics. . . .”³¹⁾

The emphasis on misery helped to put President Park’s regime into a better light. This argument is in line with the popular view that President Park saved Korea from poverty and raised the economic status of Korea in the world and eventually provided the ground for today’s political freedom. Moreover, some people argue that the authoritarian rule of Park Chung Hee was inevitable in the initial period of economic development.³²⁾

Recently, the opposite view has been relatively gaining ground. The main point of those who put forward this argument is that the achievement of President Park is emphasized rather than that of President Rhee. Ho-Chul Sohn argues that the economic growth rate was not outstanding, but it was respectable.³³⁾ (See Table 1) Sohn also insists that we pay attention to the the rapid growth of import-substitution industries, even under the bad conditions such as social turmoil after the collapse of

30. Sung-Jo Han, “The Power Elite in Korean Politics(in Korean)”, in Wung-Tae Kim ed., *Treaties on Korean Politics*, 2nd ed. Pakyongsa, 1989, p.405-407.

31. John Kie-Chiang Oh(1990), p.19

32. Cho Kap-Je, “Reconciliation between Park Chung Hee and Kim Young Sam”, *Monthly Chosun*, November 1993, Kim Chong-Su, “Leadership with Vision Save the Poor Country”, *Monthly Chungyang*, November 1994.

33. In-Young Kim(1996), p.20, Ho-Chul Sohn, “State and ‘Civil Society’ in Korea:A Reappraisal.” Presented at Georgetown Conference on Korea II “The Korean State and the Rise of Civil Society,” Georgetown University, May 1995, p.5-8.

Japanese rule, and the destruction caused by the Korean war.(See Table 2)

In addition, In-Young Kim claims that GNP for Korea between 1954 to 1963 steadily increased(Table 1) and that many of the contrasts in the achievements of the Rhee and Park periods(Table 2) are exaggerated for political purposes. Thus, Kim praises the economic performance of the Park administration and justifies his authoritarian rule.³⁴⁾

〈Table 1〉 Comparative Growth Performance of Korea, 1950-87

(average annual growth rates, percent)

| | 1950-64 | 1964-73 | 1973-9 | 1979-87 |
|-----------|---------|---------|--------|---------|
| Korea | 6.1 | 9.6 | 9.0 | 7.0 |
| Taiwan | 8.3 | 11.0 | 8.4 | 7.4 |
| India | 4.3 | 2.7 | 3.4 | 4.6 |
| Argentina | 3.0 | 4.9 | 2.3 | -0.4 |
| Italy | 5.7 | 5.1 | 2.6 | 2.2 |
| Japan | 9.5 | 8.9 | 3.6 | 3.8 |

Source : In-Young Kim(1996), p.49.

〈Table 2〉 Economic Performances of the First and Third Republics

(annual real growth rate of manufacturing, percent)

| | The First Republic (1950-60) | The Third Republic (1961-80) |
|-------------------------|---------------------------------|---------------------------------|
| Developing Countries(a) | 5.0 | 6.6 |
| Korea(b) | 16.8 | 20.3 |
| (b)/(a) | 3.36 | 3.07 |

Source : Source : In-Young Kim(1996), p.49.

However, when we consider the economic performances of the First and the Second Republics, we cannot disregard the contribution of American aid. For instance, economic assistance by the US during 1953-61 accounted for 7-12% of GNP and financed 60-80% of imports.³⁵⁾

34. In-Young Kim(1996), p.21.

35. Ima Adelman, "Review of Korea's Social Development", *The Korean Economy 1945-95: Performance Vision*

I do not wholly agree with the first view about the role of President Park and sceptical about the view that it may have been possible for the Korean economy to perform well without the intervention of President Park. What I do believe, however, is that President Park's achievement was to bring political stability to ordinary people. When I review the political turmoil of the First and the Second Republics, it is difficult to imagine that the Second Republic regaining political stability and providing the momentum for economic development. Even though the bureaucrats in the Second Republic Five-Year Plans, I doubt if the execution of such plans could be feasible under the weak Second Republic Government.

The character of the Third Republic was totally different from the First and the Second ones. Basically, President Park established an authoritarian government and then transformed it into a dictatorship in the last part of the 1970s by changing the election system and the power structure. Economic development since the early 1960s has been based on a series of Five-Year Economic Development Plans. In addition to these, there have been other blueprints for the nation's development, including the annual Overall Resources Budget, drafted by the Economic Planning Board to coordinate the mobilization and use of resources to the Plan' target. There has also been Long-Term Economic and Social Development Program, 1977-91, prepared by the Korea Development Institute to give long range perspective to the five year plans by analyzing problems and policy options for the 1980s.

In analysing Korea's economic development, there is a strong tendency to attribute its success to the economic development plans. However, it should be remembered that plans are only meaningful in terms of their declaration of intent. In the next discussion, we may partially understand why the plans themselves were not really effective, since there are several other elements at work in contributing to the growth rate of the Korea economy.

In any case, the authoritarian government did succeed in rapid economic growth. During the 1962-1979, the annual average growth rate was almost 9.3%. This reflects the fact that President Park needed rapid economic growth to maintain this authoritarian dictatorship, while he needed an authoritarian regime to keep the rapid growth rate.

〈Table 3〉 The Economic Performance of President Park

| | Economic Growth Rate(%) | Export (Million Dollar) ¹⁾ | GNP per Capita (Dollar) | Population (Thousand Persons) | Agricultural Portion of Industrial Structure ³⁾ (%) |
|------|-------------------------|---------------------------------------|-------------------------|-------------------------------|--|
| 1961 | 5.6 | 40.7 | 82 | 25,766 | 38.7 |
| 1962 | annual average 9.3 | 54.8 | 87 | 26,513 | 39.8 |
| 1972 | | 1,624.1 | 318 | 33,505 | 28.7 |
| 1979 | | 15,055.5 | 1,640 | 37,534 | 22.9 |
| 1980 | -3.7 | 17,504.9 | 1,592 | 38,124 | 17.8 ²⁾ |

Source : Bank of Korea, Yearbook of Economic Statistics,

As the price of economic development, the political freedom of Korean people was deferred. However, it is not possible for people to postpone political freedom indefinitely. Thus, at the end of the 1970s, the anti-government movement began to grow, centered around labor unions, Protestant, and Catholics. In 1978 and 1979, the political situation got worse because of the strong crackdown on anti-government activities. As a result, the anti-government movement for democracy led to the assassination of President Park. Summing up the Third Republic, we may say that the Korean people obtained economic success. However, the price they paid was the postponement of political freedom.

General Chun came to power in 1980 using a crackdown against anti-government activities. His regime was somewhat better than that of President Park in terms of political freedom. However, the degree of political freedom in Korea was far from the original concept of democracy. There was strict control of the press and people were very cautious about criticising the government. Even though the degree of political freedom was far from democracy, the economic performance of the Fifth Republic was relatively good.

The year 1988 was a significant milestone for Korea. The Korean government was peacefully replaced by the popularly elected new government, the first time political power was transferred in this way in modern Korean history. But it should not be assumed that democracy was bestowed on the people by the government. Though the

Korean people may tolerate a considerable degree of governmental actions, there appear to be limits beyond which people's tolerance and acquiescence will not stretch. It was only the massive people's struggle for democratization in the spring and summer of 1987 that forced the powerful Chun regime to accept direct elections and other sweeping democratic reforms. Therefore, democracy is not given to people, but achieved by the people.

For the first time in many years, however, the political leadership's commitment to economic growth and development was substantially weakened. As an obvious result, insatiable political demands overpowered economic logic that was politically rather unpopular. The most pressing problems arose in the economic sectors, particularly in the form of bitter and frequent labor disputes and strikes.

For example, the number of unionized workers had swollen from 948,000 in 1980, the first year of the Fifth Republic, to 1,267,000 in 1987, its last year. Strikes occurred with an increasing frequency, often resulting in sharp wage hikes. Real wage increases started to outstrip productivity gains. Korea began to lose its competitive edge in many industrial sectors. For the Sixth Republic, the Korean people enjoyed political freedom, although political instability, frequent labor strikes, and high wage increases eroded the foundation of the economy.

In 1993, the Seventh Republic was started under President Young Sam Kim. The frequency of strikes has rapidly diminished, but wages continue to climb. Compared with the Sixth Republic, in the Seventh Republic, the power of interest groups has been increasing and their activities have been intensifying. Sometimes, economic and social policy are determined by interest groups, which fully utilize their right to mass demonstration.

Right now, the main item on Korea's reform agenda is the labor-related law. The conflicts between employers and employees are so severe that government can not find any good way to change the rigidity of the labor market. From the employer's perspective, the labor law does not comply with international standards, and it is not easy to do business in Korea.

At this moment, I would like to refer to the second stage of economic development mentioned in Chapter II in which it is shown that unlimited democracy may have an adverse effect on economic progress. From the Sixth Republic to the Seventh Republic, the degree of unlimited democracy has been increasing slowly. In

order to overcome current difficulties, some politicians and scholars strongly press for reform. However, most politicians worry about losing voters still do not agree. On this respect a believe Korea is at a critically important crossroads. Appropriate policy responses to current challenges will be necessary if Korea is to be successful in making the leap from developing to developed nation status.

(3) Success of Economic Development

Most people think that the active intervention of government in the economy is the most important element in the success of Korea. Still, there are many politicians, bureaucrats and scholars, as well as ordinary people, who have a very similar ideas. As a result, there is sometimes an assumption that the role of the Korean government in economic development is a very good model for other developing countries.

Is this popular argument right? Moreover, is there any reasonable evidence to support it? If not, why is this kind of argument so popular? Regardless of the country or time, planning always has a wide gap between reality and theory and thus planners cannot hope to have good evidence. From this perspective, Korea is not a special case.

The success story of industrial policies, which is based on a sequence of Five-Year Plans, is partly exaggerated for political reasons. In order to justify an authoritarian developmental dictatorship, the President needs strong support for the active role of government and economic performance. And it is reasonable to assume that government-funded think tanks such as the Korea Development Institute, were mobilized for this purpose.³⁶⁾

At the early stage of economic development in Korea, there were no think-tanks which criticized and monitored economic policies by government. Under the authoritarian dictatorship and repressive political system, it was very difficult and dangerous to criticize the government's economic policy. Critics were considered as a challenge to the regime's authority. Moreover, traditionally, Koreans have been reluctant to tolerate different ideas and views because they have not any historical

36. As examples of KDI activities which justify the active role of government in economic development, In-Young Kim cites eight volumes published by the Council on East Asian Studies, Harvard University, under the series title, *Studies in the Modernization of The Republic of Korea, 1945-1975*.

experience in liberalism and they lean toward collectivism rather than individualism.

During the economic development period, the most powerful think-tank was KDI and it had a very important role in the planning and justification of industrial policy. Some key scholars of KDI entered high positions in the government. Most papers in English about economic development of Korea were supplied by KDI and they justified the active government's policies.³⁷⁾ The other important reason that there does not exist enough criticism, was due to economic research funding, most of which came from government.

Park's success story was continuously advertised by the media and education. During the school year, Koreans were not informed about the failures of the regime's industrial policies. Because of the media and education, most people including scholars, were won over by the traditional idea that government intervention in the Korean economy was beneficial for all of society and whenever problems occurred with the economy, the mass media demanded more 'government intervention'.

Most social scientists are very interested in visible elements, which are possible to measure. Compared with the natural sciences, the social sciences deal with such a complex world that most social scientists, including economists, tend to overlook the unquantifiable factors. Sometimes, this is even intentional. In particular, economists have an inclination to seek for the relationship between measurable elements and thus they do not accept any unmeasurable elements in their research.

Whenever we review the industrial policy in Korea, we may find that there are many cases of government failures. The success of strategic industries in Korea was not the intervention of government but the entrepreneurship of business sectors. Moreover, the deep involvement of government incurred huge costs on the private sector. At the same time, it is very hard to cite the successful cases of government intervention.

During 1973-79, the government planned very ambitious industrial policies for the so-called Heavy and Chemical Industrialization(HCI).³⁸⁾ The World Bank's evaluation

37. Ki-Hwan Kim and Danny Leipziger, *Korea: A Case of Government-Led Development*, World Bank, 1993, Edward S. Manson, Man Je Kim, et. al. *The Economic and Social Modernization of the Republic of Korea, 1945-1975*, Council on East Asian Studies, Harvard University, 1980.

38. For the government failure in the the HCI, see Jong-Chang Rhee, *The State and Industry in South Korea: The Limits of the Authoritarian State*, Routledge, 1994.

of this drive was summed up in the following sentence :

“The costs of the HCI drive are still not fully known,
but they were high.”³⁹⁾

The failed implementation of the state's heavy and chemical investment resulted in over-investment. Subsequently, in 1981 the government again intervened in the so-called Reorganization of the Heavy and Chemical Industries.

During the HCI, the Park regime actively promoted construction of large shipyards without considering Korean companies' technical abilities, their fragile debt-ridden financial structure, and their heavy dependency on overseas demand. Unlike the government predictions, in the mid-1980s the Korean shipbuilding industry, dependent on overseas demand for 70 to 90 percent of its orders, experienced a serious decline in new orders due to a shipping slump. Shipbuilders faced a financial and unemployment crises. If private companies were allowed to control their own production capacities, they could have been prepared to cope with this downturn.

The automobile and electronics industries are the most important industries in Korea. In these sectors, the government was strongly involved in resources allocation, with bureaucrats deciding that Korea should have one or two companies because of the scarcity of resources. In the automobile industry, they forced companies to specialize in either trucks or automobiles, despite the strong resistance of the business community. Right now, the success of Hyundai, Daewoo, and Kia Motor companies comes from their resistance to the government's active role. If the government succeeded in enforcing its plan, it would not have been possible for Korea to have several competitive motor companies.

The electronics industry is worse than the the automobile industry. Bureaucrats insisted that the monopoly system was important to keep competitive edge. Their basic idea was to invest huge amounts of money in one company with the hope of building one giant company. In the 1960s, GoldStar, which is a subsidiary of the LG group, almost monopolized the electronics industry. The Samsung group had a very

39. World Bank, *The East Asian Miracle : Economic Growth and Public Policy*, Oxford University Press, 1993, p.308.

hard time to persuade bureaucrats and she got direct permission from President Park. If the bureaucrats had persisted with their ideas, Samsung Electronic Companies could not have become such a renowned company in the global semiconductor or electronics industry.

Therefore, I am sceptical about the popular view that the success of Korea's economy is attributed to the active role of government, including the industrial policies and the direction of elite bureaucrats. Rather, I want to suggest the main reasons for Korea's success as follows :

Firstly, during the First Republic, the foundation of capitalism was well established by the constitution and its related economic policies. Without that foundation, it would not have been possible for the Korean people to achieve rapid economic growth.⁴⁰⁾

The adoption of a constitutional parliament in 1948, paved the way for socialism, which contains the concepts of nationalization and profit-sharing with workers. However, in the sale of Japanese property, politicians in the First Republic minimized the scope of nationalization. And that means that most of the companies were distributed among the private sectors. Additionally, the labor unions strongly requested labor participation and the profit-sharing system. And even though the constitution declared the right to profit-sharing, the related laws do not give rights to laborers. That means that the cornerstone of the Korean economy is the right to private property ownership.

Like the distribution of companies, the Land Distribution Act demolished the land class and established the right to own property. Korea's land distribution system is highly regarded compared with other developing countries.

Secondly, President Park provided favorable conditions for economic development, such as political stability. Usually, in the First and Second Republics, businessman could not anticipate the future, because of political instability accompanied by high inflation, massive demonstrations and corruption. Political stability, to some degree, may be possible for an authoritarian regime rather than a democratic regime. But strong leadership in a democratic government may lay the foundation for political stability. Regardless of the pattern of government, leadership is a precondition for political stability.

40. Young-Yong Kim and Young-Duk Jeon(1997).

Thirdly, President Park led people out of poverty and gave them a vision for the future. Throughout their long history, Korean people had become well adjusted to poverty. Thus President Park's development drive had a positive impact on the people.

Fourthly, in making economic policy, President Park, who was known for his willingness to learn, accepted the ideas of businessmen. Whenever he met businessmen, he carefully listened what they said and then wrote down key factors. If he liked the ideas, he directly ordered their implementation and then monitored the process. In the early period of President Park, the ideas for economic development were supplied by businessmen, including most large scale projects like Wul-san industrial complex. Especially, the members of the Federation of Korean Industries played a key role in supplying good ideas.

Additionally, President Park tried to separate politics and economic policies, based on the principle that economic policy should promote economic development and national safety.⁴¹⁾ Also, the Korean War totally destroyed the basis of interest groups, therefore reducing their influence on the establishment and on economic policy-making.

Moreover, at the early stage of economic development, world economic circumstances were favorable for the Korean economy, with cheap oil prices and easy accessibility to advanced markets. Additionally, the Vietnam War and the Middle-East construction boom added momentum to economic progress.

Importantly, Korea had diligent and ambitious entrepreneurs. Through the severe competition, some of them succeeded in the establishing Big Business Groups, known as Chaebol. Additionally, Korean culture always emphasized education and thus a well-educated labor force was a very important element in enhancing economic progress.

41. Jeong Chung-Gil, *The Leadership of Presidents*(in Korean), The Korean Economic Daily Newspaper Co., 1994, p.35.

IV. Conclusions

The success of the Korean economy was achieved under an authoritarian regime. Therefore, many people think that it is not easy to lay the foundations for economic development under a democratic government. Thus, it is argued that the developing countries which are pursuing rapid economic development must inevitably turn to an authoritarian government.

In this paper, I examine the relationship between economic progress and democracy using Korea's experiences. Political stability is one of the most important elements in economic development. However, the First and Second Republics in Korea were actually quite turbulent. Under the First and Second Republics(1948-60), good economic progress was not possible. During the Second Republic, the Five-Year Economic Plan system was already established, but it could not be implemented by government.

Even though the regime of President Park(1961-79) was authoritarian, it contributed to political stability and economic progress. But that does not mean that an authoritarian regime guarantees economic progress. Political stability largely depends on leadership, regardless of the patterns of the political system.

As people become richer, economic progress helps to consolidate the foundation of democracy. But democracy eventually erodes the foundation of the free market such as the safety of property. During the Sixth and Seventh Republics(1988-), the Korean people enjoyed more political freedom than in previous Republics. However, they confronted the excessive demands of interest groups such as labor unions. Interest groups already have a strong influence on economic policy. Like the western advanced nations, Korea is transforming from a democratic nation to an unlimited democratic nation as living standards improve. I call this kind of phenomena 'the tragedy of unlimited democracy', which is a traditional example of a welfare state.

Additionally, in Korea, we should be careful in explaining the active role of government in economic progress. The wise and benevolent role of Korea's government is intentionally exaggerated in order to justify the authoritarian government of President Park. In strategic business areas like shipbuilding, automobiles, electronics and so forth, the intervention of government resulted in the

misallocation of resources at a huge cost to the people. The main reasons for the success of the Korean economy are as follows : the adoption of a constitutional parliament, land distribution, political stability, the depolitisization of economic policy, the dissolution of interest groups due to the Korean War, ambitious entrepreneurs, and diligent workers.

Above all, economic progress and democracy at the early stage of require political stability. In a weak democracy, we cannot expect economic progress. We also cannot have economic progress in an unlimited democracy, because of the influence of interest groups. In time, we also should worry about unlimited democracy and seek for the ways to maintain both leadership and the rule of law.

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