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## Transformation of South Korea from a Third World Agrarian economy to a Technologically Advanced First World Country

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### ABSTRACT

*History of Korea traces back as early as 2233 BC with various dynasties ruling it. It remained Independent until many centuries only to be colonized by Japan in 1910. Japanese colonization ended in 1945, which resulted in the formation of modern Korea. It was 1960 and Korean War just ended. Korea officially split into two parts North and South. South Korea had used up all its resources in war and was one of the poorest nations in Asia. There was no advanced industries and industrialization was yet to happen in South Korea. Its economy was completely agriculture based. Per capita income was just \$100 and the country was recovering from the devastating Korean War. No one would have thought that the Korea, which down and dusted after decades of war will rise up so quickly on its feet. Within a span of forty years, Korea was one of the four Asian tigers and a leading economic power. Not many nations have grown at such a rapid rate like South Korea did and it is important for scholars and academicians of today to conduct research on Korea's meteoric rise. Several types of research have been conducted on this subject before but there is always a room to add and discover something new. This is such a topic that will be researched for many more coming years and prove to be a model of growth for many under developed countries. There so many factors that can be attributed to the rapid rise of the South Korean economy but major ones should include liberal government policies, hardworking and progressive people, FDI, labor intensive exports. All the factors will be elaborated in detail later in the paper [1][10]. (Oh, 2010) (Chowdury, 2016).*

**Keyword:** Growth, Korean Model of development, Economic Power and Government Policies.

### 1. LITERATURE REVIEW

Prior studies have already made on the rapid economic growth of South Korea. Many authors have highlighted different factors which have remained instrumental in the development of the South Korean economy. They are as follows.

Firstly, most believe that the main factor behind South Korea's growth is due to the infusion of Japanese capital and support through economic partnerships and inflow of its latest technology which helped the Koreans compete in the world market<sup>[11]</sup>. (Pham, 2015) The willing foreign investments from abroad made it possible for the country to shift to an economic model of industrialization through the process of exports<sup>[11]</sup>. (Pham, 2015) The export orientation is one of the major reasons for its current level of foreign exchange and employment<sup>[14]</sup>. (Villa & Han, 1990).

Secondly, the country had access to cheap labor which was six to ten times lower than the US wage rates during its industrialization period from the 1970s to 1980s. Since the government rules restricted external intervention between a labor and the employer, the unfair advantage was taken by the industries in South Korea<sup>[14]</sup>. (Villa & Han, 1990).

Thirdly, the government played a huge role in facilitating industrialization in South Korea. The electronics sector was focused more on the government's policies in the fifth five-year plan (1982-87) which elaborated specifically on semiconductors<sup>[14]</sup>. (Villa & Han, 1990) It is no wonder that the South Korean semiconductor industry is the second largest in the world exporting to the US and the rest of the world. The effectiveness of the state was particularly due to the effective economic planning board<sup>[11]</sup>. (Pham, 2015).

Fourth, the South Korean growth is majorly interlinked with the growth of its electronics industry. At initial stages it was majorly engaged in the adaptation of foreign technology and less in technological innovation, thus focusing on marketing, competitiveness and user requirements<sup>[14]</sup>.

(Villa & Han, 1990) Only in the mid-1980s, the four major enterprises (Samsung, Hyundai, Gold Star, and Daewoo) started producing advanced microchips without foreign licenses, thus becoming self-reliant in LSI and VLSI production in component electronics<sup>[14]</sup>. (Villa & Han, 1990).

## **2. HISTORY OF SOUTH KOREAN ECONOMY**

In the 1960's, the major source of income for South Korea was through subsistence agriculture. The country had been colonized by the Japanese between the period from 1910 to 1945, which brought some degree of modernization and industrialization. The Korean war of 1950-53 had devastated the whole economy. The per capita income during the 1960's was 40% below India's and other sub-Saharan countries. Even though the economy was majorly dependent on agriculture, it is important to note that the cultivable land area was only 30% and arable land available per farm household was the least in the world. Absolute poverty was prevalent among 40% of the population<sup>[5]</sup>. (Kim K. S., 1991).

The agriculture sector contributed up to 44.6% of the GNP in 1954-56. The dependence on agriculture gradually reduced in the coming decades, as its contribution to GNP reduced to 28% in the year 1967-71, and 13.5% in the year 1982-86<sup>[9]</sup>. (Major Statistics of the Korean Economy, 1986).

The political situation in South Korea was not conducive for foreign investments and economic development during the 1945-62 period. The American military government took over the country in 1945. The Korean War of 1950, destroyed infrastructure and assets of the nation leading to the widespread disparity. The failed import substitution policy in 1950-53 under the regime of Rhee and occupancy by the military coup led to a stagnant economy. The election of Park Chung-Hee saw the country transition from the policy of import substitution to an export oriented nation. At the end of 1970's, South Korea had a lot of foreign debt due to its high growth rate and a high inflation. It was followed by the assassination of President Park, recession due to oil in 1980-81 and failure of the crop in the country which led to an unstable economy. The government had to impose stabilization program to control inflation levels and imbalances within the industry as well as between urban and rural areas. The exports and GNP of South Korea grew rapidly in the period between 1962-79. It grew 33.7% and 9.3% respectively. This was due to the various government policy measures and reforms were undertaken during the period which saw the growth of Chaebols in South Korea<sup>[6][7]</sup>. (Kuznets, 1994) (Kwan, 1991).

## **3. PRESENT STATE OF SOUTH KOREA**

South Korea is among the wealthiest countries in Asia currently. Moreover, is the part of affluent four dragons of Asia that consists of Taiwan, Singapore, Hong Kong and South Korea. It ranks 29<sup>th</sup> in terms of GDP per capita of \$35,751 according to World Bank's latest report. It joined trillion clubs of economies in 2004.

For many decades South Korea was regarded nothing more than a mini version of Japan. However, today it has an aura of its own and Korean brands, culture, music, and technology have become popular all over the world. South Korea has also become a popular tourist destination famous for its exotic nightlife, world-class cities, diverse food, and culture.

Year by year South Korea is witnessing a rise in exports and foreign direct investments. It is a fifth largest exporter in the world. With exports equivalent to 45.6% of its GDP.

According to the UNCTAD 2017 World Investment Report, approximately 10 billion USD flow in the country in terms FDI. After having to reach a record breaking in 2013 (USD 12.7 billion) and plunging down in 2015 (USD 4.1 billion, due to the withdrawal of Tesco), FDI stood at USD 10.8 billion in 2016.

South Korea's temptation in terms of foreign direct investment (FDI) is due to country's rapid economic development and the consistent improvement in new information and communication technologies. However, opaque rules and regulations is a major concern to foreign investors and is a major barrier to FDI.

South Korea has made a transition from low standards of life country to a country of high living standards with the majority of South Koreans living economically sound. South Korean consumption behavior has been increasingly mimicking the developed countries consumption patterns.

South Korea has also made tremendous progress in terms of infrastructure, transportation. It is one of the third countries in the world to have Maglev train system, and its airports are consistently ranked best in the world. Seoul is frequently named as the most technologically advanced city in the world. South Korea also leads the pack in terms of internet connectivity and speed with fastest data network in the world<sup>[2][13][4]</sup>. (Santander, 2018) (Kim H. , 2017) (Forbes, 2017).

In first 17 years of 21<sup>st</sup> century South Korean government has spent more than US\$300 billion on airports, roads, railways and other infrastructure. Additionally, it will spend US\$60 billion on the construction of more than 100 new power-generation facilities in the future.

The current state of South Korea reflects an ideal economy. And it is bound to be even better in future if South Korea is able to correct small flaws in its political and economic future. It will interesting to see if South Korea will be able to overtake Japanese economy in future as Japan's GDP growth has slowed down to 1% while South Korea's GDP is still growing at a rate of 3%<sup>[2][13][4]</sup>. (Santander, 2018) (Kim H. , 2017) (Forbes, 2017).

## **4. REASONS FOR THE MASSIVE GROWTH OF SOUTH KOREA**

### **Role of the Government**

The Government of South Korea saw industries like petrochemicals, iron and steel and oil as the basis for a developing industrial economy. The country's first steel company, Pohang Steel Mill was started in 1968, with a production capacity of one million tons a year. The increased government support for steel mills helped foster the industry as it increased the supply to cover over 90% of the domestic market demand and started exporting the surplus.

The Government shifted its focus to ship building industry as they prove to be consumers of the steel produced. It later also started producing oil tankers, steamers, and other shipping related products <sup>[5]</sup>. (Kim K. S., 1991)

Similarly, in 1969, the government focused on the domestic electronics industry in South Korea and named it as a "strategic export industry". The government established various centers like the Korea Institute of Electronics Technology, Korea Advanced Institute of Science and Technology, and the Electronics Industries Association of Korea for research and development for the development of the industry. The government provided several incentives for its strategic industries through centrally imposed constraints by several ministries. The incentives were provided only to firms that performed well. The firms which were below standards were allowed to fail by the stoppage of subsidies <sup>[3]</sup>. (Kang, 2002) The incentives include tax exemptions, loans and deductions for the import of capital goods, faster depreciation of necessary equipment, arrangements for licensing technologies, facilities and savings for the import of intermediate goods, differential pricing or directly beneficial expenditure, quantitative restrictions on imports of goods and capital, and quantitative targets for exports and overhead investments. Once strategic industries were located, the government left the task of developing it to the private sector. The role of the public sector in setting incentives was only to respond to desirable private sector requests such as subsidies, credit, and foreign exchange allocation. The trade reforms aimed to shift the economy from import substitution to export promotion. President Park personally acknowledged to business leaders that he would not consider corruption within the business as seriously as corruption in the state, thus providing full support for the growth of the private sector <sup>[3][5]</sup>. (Kang, 2002) (Kim K. S., 1991)

Government directed the growth of South Korea by means of intervention, discrimination and use of finance as a means of control. As between the period of 1970-1980, the labor costs per unit annually increased 17.5% as against 7.1% in Taiwan and 0.8% in Hong Kong. This was due to the governments wish to replace labor-intensive industries like textiles by capital intensive industries like the iron and steel <sup>[5]</sup>. (Kim K. S., 1991).

### **Availability of Cheap Labor**

The heavy growth of industries put enormous pressure on the industrial wages, but it remained constant during the early stages of industrialization from 1961-1966. And there was a sudden increase in the real wages during the period of 1967-1978 and the productivity increased faster by 50% due to government's policy reforms to change the structure in different labor markets and to meet the violent Korean labor unions demands <sup>[5]</sup>. (Kim K. S., 1991).

In the start of 1980s, an average Korean worked about 50-53 hours a week which was higher than other industrializing economies in Asia. They were underpaid as their productivity and wage rates did not match. There were no traditions of strong labor union movements in South Korea as only 20% of the industrial labors in 1986 were officially registered in labor unions <sup>[5]</sup>. (Kim K. S., 1991).

### **Chaebols in South Korea**

Chaebols or large industrial houses played a crucial role in the industrialization of South Korea. They often acted an instrument of government policies and reforms which has fostered their huge growth. The growth rate that they achieved was remarkable in the history of any enterprise as between the period of 1973-1978, they achieved an annual growth rate of 30% (10 largest Chaebols) and contributed up to 31.8% of the GDP in 1973. Since the government credit was based on past achievements, few entrepreneurs raced against each other to build an empire as several ventures could be launched at the same time. Hence there was a concentration of growth within a few large firms as against small firms at the start of industrialization. When the South Korean economy moved to advanced sectors such as electronics and automobiles, it required large capital to start the business. This led to the Chaebols dominating the industry in South Korea and also partner with foreign firms for transfer of technology <sup>[5]</sup>. (Kim K. S., 1991).

### **Japanese Investments and transfer of technology**

Investments from Japan was a prime cause in Korean industrialization as it provided the needed technology and quality to its exports. These investments came out of necessity as Japan underwent rapid growth between the periods of 1950-1960. It started with investments in textiles in South Korea due to increasing domestic labor cost and American protectionist policies towards Japan. Infusion of Japanese technology through joint ventures led to increase in the quality of Korean exports, thus helping the Korean business to enter the global market <sup>[12]</sup>. (Pham, Political Economy of East Asia, 2015).

## **5. CHALLENGES FOR SOUTH KOREAN ECONOMY**

The south Korean economy is doing well currently but there are many challenges awaiting if it has to replicate its historic growth.

- Curbing down 'chaebols' for growth and development of small businesses: Chaebol is a term used for a family run multinational conglomerates based in South Korea. Example: Samsung, Hyundai, L.G etc. These Chaebols are dominating Korean market since decades leaving a little opportunity for growth of small businesses and entrepreneurs. They also get unfair political advantage and tax benefits by developing connections with the government or sending company executives for parliamentary elections.

- The south Korean government has not done much about Chaebols that is suppressing entrepreneurship in the country. If the economy has to grow at a faster rate in future and markets have to be more competitive then government needs to set some strict rules and guidelines for chaebols and prevent the misuse of their powers.
- Resolving conflict with North Korea: South Korea and North Korea have had strained relations since many decades and even after signing a reunification agreement in 2000 their relationship has not improved. South Korea is always in a danger of getting into a full-fledged war with North Korea. Which might have an effect similar to Korean war on its economy. Even if North Korea and South Korea unite in future it will cost South Korea an estimated about of 1 trillion Dollar. Thus, North Korea has become a double-edged sword for South Korea and it is important for them to reach a concrete and peaceful solution <sup>[8]</sup>. (Lee, 2017).
- Aged population and inequality: South Korea's birth rates are declining as increasing number of youngsters are not choosing to marry and raise kids due to skyrocketing cost of living. Moreover, the income inequality in South Korea is highest among all 22 Asia Pacific countries according to an IMF report in 2016. Introducing new reforms and policies that will resolve these issues is a major challenge for the country in next 10 years <sup>[8]</sup>. (Lee, 2017).
- Combating air and nuclear pollution for sustainable development: With the rise of heavy industries and modernisation in South Korea. Air pollution and nuclear waste increased at an exponential rate. South Korea is also getting pollution from the incoming air pollutants coming from the east coast of China. South Korea is planning to build 20 coal-powered plants by 2029 that will further contribute to the increment of pollution. Another area of concern for South Korea will be lack of disposable areas for nuclear waste that might become a big problem if the country switches the majority of its electricity generation from coal to nuclear power <sup>[8]</sup>. (Lee, 2017).
- Stiff competition from China and Japan. : China is bound to overtake the U.S as the superpower of the 21<sup>st</sup> century in upcoming years and it is spending billions of dollars in the development of new and better technologies that will challenge the authority of South Korea in electronic products. In addition to it, Japan has become alert to growing power of China and hence it is developing new tech products and creating strategies to compete with China in terms of Exports. It is crucial for South Korea to match up with Both China and Japan otherwise, it will lose its position in World economy in coming years <sup>[8]</sup>. (Lee, 2017).

## 6. CONCLUSION

South Korea has achieved a huge growth in the past decades and is currently one of the leading economies in all aspects whether it is financial, military or technological advancements. The huge growth had been jumping started by then President Park Chung-Hee. The conducive government policies along with the infusion of foreign aid and technological transfers helped Korea move towards rapid industrialization. The availability of cheap labor has provided the country with an edge over others, thus proving to be an ideal destination for foreign investors. The export orientation policy and the growth of Chaebols are an integral part of South Korean growth history. The aging population and rising inequality in the country are posing as a major challenge for the South Korean economy. The high pollution levels and the growing trouble with North Korea due to its nuclear missile development program is an alarming issue for the government to look into.

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