Paemika Khongthon
ID: 6204640616

The effect of the development of past industrial policy on the economy in comparison between Thailand and South Korea during 1961-1979

In the big picture, Professor Akira Suehiro presented the idea that for society will be able to develop and drive technology growth at a fast pace, it must have the social capability to absorb modern technology, which consists of a strong public sector, talented and proficient firm, and high skilled labor. The states with all three components are called “developmental states”. This is because these components act as the main player in terms of driving effective industrial policy and economic growth. The developmental state was mostly found in East Asia Countries like Japan and South Korea. Moreover, Alexander Gerschenkron, an economic historian of Harvard University assumed about how the economic system in many developing countries miraculously being able to keep up with developed countries. In this case, Gerschenkron assumed on the factor these economic systems have in common, which is the formulation of economic structures in favor of the big and well-known businesses or the vested interest group in leading and fostering economic growth. Hence, raises an interesting question regarding the impact of the economic structures and the application of the past industrial policies on the economy in the past and how it is nowadays.

To be more specific, I would like to compare and elaborate precisely on the state of development between Thailand and South Korea. This is because a developing country like Thailand exists a Thai Sakdina autocracy (feudal system), which became the primary failure in terms of the country’s industrial policy. While South Korea, which is a developed country has a system called “Chaebol”, which refers to large family businesses, such as Hyundai and Samsung. The similarity between the two systems is how the structure of the economic institutions was formulated to support and favored the big firms in order for them to drive economic growth and embraces sustainability in driving the growth of the country. While the difference between the Thai Sakdina autocracy (feudal system) and Chaebol is how the two countries have different rules for governing.

In the case of Thailand, the economic outcome of Thailand reflects a narrow coalitional structure over the past four decades, which further turned into a big failure for the country. Moreover, the Thai state was unable to implement any effective coherent policy, as well as promote a long-term entrepreneurial perspective among the vested interest group. In addition, inequality was also one of the biggest mistakes made by the Thai state and was commonly found in various sectors, such as a drastic growth in the metropolitan area and the inequality in income distribution, which can be perfectly seen in comparison to the East Asian NIEs.

In the middle of the 1970s, the Thai state experienced drop-in labor productivity and total factor productivity due to a lack of skilled labor, a decrease in the rate of secondary enrollment, a shortage of infrastructure, as well as a low level of productivity in the agricultural sector. These factors altogether perfectly portray a rising in poverty rate, hence, driving sustained economic growth became the main challenge for the Thai state during the middle of the 1970s. The Thai state is now in the first stage of market reform, in which the state needs to focus on aggregate growth by attracting foreign demand and/or FDI inflows into the state in order to continually push the growth of the economy instead of focus on the vested interest group. The changes in policy reform, which were mostly favorable to the vested interest group can be seen in the period of the Sarit government during 1957-1963. For example, the role of the Thai state was to focus on providing a stable investment environment for the private sector and was believed to be a humanitarian dictator. Moreover, only selected import-substituting industries were given investment incentives. Overall, the Sarit-Thanom-Prapath regime comprises unfair competition, rent seeking, and corruption, which further drive down the economic growth and implement an effective policy and market reform as a whole. Unfortunately, the state was rarely found to have social and economic bases for democratic development.

The Thai industry consists of big firms and small firms. Specifically, the widely known big firms in Thailand include CP, Chang, Singha, and the Chirathivat Family. In addition, these big firms refer to as the "vested interest group" due to the fact that these firms have a big influence on the economy, which implies the wealthiness and how they can easily control the market. According to the research, Thailand is considered to be a country with a very high rate of inequality, while the economic outcomes of the country turned out to experience a significant improvement. In my opinion, the reason for the high rate of inequality in Thailand is that Thailand has a narrow(governing) coalition, which greatly reflects the Thai Sakdina autocracy (feudal system). For example, the government may implement the policy in favor of the vested interest group, such as tax policy, which positively affects the big firms, while the small firms, such as SMEs may not benefit from the newly implemented tax policy. However, as a result of the Thai Sakdina autocracy (feudal system), the economy of Thailand experienced drastic growth in 1980. Until 1997, the economy of Thailand experienced a significant drop in its growth rate due to the Asian Financial Crisis.

Overall, the effect of past industrial policy on the Thai economy mostly turned out to be negative in the long run. The negative result came from many factors, including the Thai Sakidina (feudal) autocracy, failed to maximize benefit from FDI by supporting technological transfer from foreign firms, delivering the value creation and knowledge to domestic sectors, ineffective policy implementation, and a significant increase in the poverty rate and inequality, especially an inequality in income distribution.

Let's look at the case of South Korea and the system of Chaebol. During 1960-1980, which was the period of Park Chung-Hee, who was the former president of South Korea by carried out Coup d'etat in 1961. South Korea began to design an industrial policy to promote economic growth, which was to stimulate technology growth. Hence, it can be seen that the industrial policies were structured to support large family businesses or Chaebol, thus, the economy of South Korea was mainly driven by Chaebol. Therefore, Chaebol became the leading player in terms of fostering economic development. Moreover, the evolution of Chaebol did speed up the economic development of the country even faster. As a result, South Korea successfully managed the transition from an upper middle-income to a high-income economy in 1995. However, due to the Asian Financial Crisis in 1997, the economy of South Korea experienced one of the most significant negative impacts on its economy.

Chaebol became the key engine that powered the economy of South Korea from the 1960s to the first half of the 1990s. In addition, during the 1960s-1970s, the South Korean government implemented policies to stimulate economic growth and deliberately centered on Chaebol, which mainly focused on industrial and export sectors. For example, the South Korean government announced a 5-year economic development plan, which provides tax incentives and benefits, along with low interest on loans with the purpose to stimulate the growth of Chaebol in heavy industry and chemical industry, as well as providing financial assistance to Chaebol to be able to cope with the oil crisis in 1973.

The Chaebol-based growth model may be an attractive choice for developing countries to successfully chase developed countries. However, the growth is not going to be sustained. As Chaebol has economic powers to prevent small and medium size businesses from entering the market. Moreover, financial institutions and policymakers greatly support Chaebol financially and provide other business-related benefits. In addition, the Chaebol-based growth model possessed a negative impact on the domestic economy. Since Chaebol businesses failed to deliver value creation and technological transfer to local businesses and labor, the unemployment rates the along with poverty rate experienced rapid growth. Hence, domestic demand decreased and the wage gap between small and medium size businesses and Chaebol businesses became wider as the economy of South Korea was concentrated on a small portion of big Chaebol businesses. Furthermore, policymakers were disagreed open to the foreign investment inflows by limiting foreign shareholding to only 26% of the capital. Therefore, there was not much competition going on in the economy of South Korea during 1960s-the 1970s. Unfortunately, with insufficient competition, small and medium size businesses cannot participate on a level playing field, which contributed to a further decrease in wages with an increase in the price of goods and services.

The example of the Thai Sakdina autocracy (feudal system) and Chaebol greatly reflects how the coalitional breadth and participation shape the linkages among economic actors in society. Even though, Thailand and South Korea applied a similar conceptual framework. Surprisingly, the economy of South Korea was able to recover in a short period of time and finally step up to the fast-growing economy until today, which mainly resulted from the financial support from the IMF under the condition of economic reform in terms of promoting competition in the market. The market reform consists of more entry and a higher rate of collaboration from the small firms. Hence, the reform consists of the reformulation of the Antitrust Laws, including the corporate governance of Chaebol and policy implementation to promote competition as a whole. As a result, a higher number of small firms and non-Chaebol businesses were able to enter the market. Moreover, the economic or market decentralization allows these businesses to be able to involve in the innovation creation and the growth of the economy as a whole. Since South Korea was able to reform the economy by applying the broad coalitional structure, then it is foreseeably for the country to escape the middle-income trap and experience sustained economic growth.

In addition, according to Accemoglu et al. (2006), a higher rate of FDI is one of the greatest ways to bring in innovation and technology growth. Hence, at the starting point of the economic reform, big firms and multinational firms should be in charge of importing innovation into the country until the point where the economy is no longer growing, which implies that the country no longer has the engine of growth. At this point, the country will need to innovate and stimulate growth itself by promoting competition. The interesting point is that South Korea became successful in promoting competition and its market reform, while Thailand failed to apply a broader coalitional structure and apply new policy formation for the market reform.

In conclusion, the economy of Thailand and South Korea have shown an improvement from time to time. However, the economy of South Korea reached marvelous success with a significant drop in poverty and unemployment rate. While Thailand failed to escape the middle-income trap, with wage gap continues to widen. This is because the Chaebol-based growth model is not going to benefit the economy in the long run as swiftness in policies is needed. Without any changes, the industrialization and modernization of Thailand have developed at a slow pace and failed to step itself up to become a high-income economy.

<u>Timeline</u>

Former President of South Korea

- Park Chung-hee (1961-1979)

Former Prime Minister of Thailand

- Sarit Thanarat (1957-1963)
- Thanom Kittikachorn (1963-1973)
- Sanya Dharmasakti (1973-1975)
- Mom Rajawongse Kukrit Pramoj (1975-1976)

- Thanin Kraivichien (1976-1977)
- Kriangsak Chamanan (1977-1980)

References

EE363 lecture notes

Eleanor Albert. (2018, May 4). South Korea's Chaebol Challenge. www.cfr.org. Retrieved July 1, 2022. From https://www.cfr.org/backgrounder/south-koreas-chaebol-challenge

Carlos Tejada. (2017, February 2017). Money, Power, Family: Inside South Korea's Chaebol. www.nytimes.com. Retrieved July 2, 2022. From https://www.nytimes.com/2017/02/17/business/south-korea-chaebol-samsung.html

Daron Acemoglu, Philippe Aghion, Fabrizio Zilibotti. (2002, July). Distance to Frontier, Selection, and Economic Growth. www.nber.org. Retrieved July 2, 2022. From https://www.nber.org/papers/w9066

Akira Suehiro. (2014). Responses to the Middle-Income Trap in China, Malaysia, and Thailand. www.link.springer.com. Retrieved July 3, 2022. From https://link.springer.com/chapter/10.1007/978-981-13-2859-6_2