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## THE NATIONAL STATE, MODERNIZATION AND GLOBALIZATIONS: THE CASE OF SOUTH KOREA'S TRANSFORMATION IN THE 1960S TO EARLY 1980S

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У статті автор досліджує зліт Південної Кореї (або Республіки Корея), особливу увагу приділяючи періоду 1961-1987гг., Коли відбулася трансформація Південної Кореї - від бідного, залежного від США номінального держави, розхитаного руйнівною війною 1950-1953 рр., у заможну, успішну, сучасну азіатську економіку, що швидко розвивається.

В статье автор исследует взлет Южной Кореи (или Республики Корея), особое внимание уделяя периоду 1961-1987гг., когда произошла трансформация Южной Кореи - от бедного, зависимого от США номинального государства, расшатанного разрушительной войной 1950-1953 гг., в богатую, успешную, быстро развивающуюся современную азиатскую экономику.

The paper examines the rise of South Korea (or the Republic of Korea) with a particular focus on the period of 1961 to 1987 when South Korea transformed itself from an impoverished, US aid reliant, nominal state, still reeling from the destruction of the Korean War of 1950-3, to the rich, gleaming, thrusting, Asian economic behemoth of more recent times.

**Ключові слова:** національна держава, модернізація, глобалізація, Південна Корея.

### Introduction

The paper examines the rise of South Korea (or the Republic of Korea) with a particular focus on the period of 1961 to 1987 when South Korea transformed itself from an impoverished, US aid reliant, nominal state, still reeling from the destruction of the Korean War of 1950-3, to the rich, gleaming, thrusting, Asian economic behemoth of more recent times. The story told therein is not necessarily one of an effortless passage to greatness and a highly respectable GDP per capita, there were undoubtedly challenges along the way but there is a narrative that South Korea, due in part to its successful industrial conglomerates – the *Chaebols*, both ruthlessly competitive and highly innovative, combined with solid property rights and inherent entrepreneurship, was set (destined perhaps?) to achieve this deserved status. There is some merit in the above but it was far from the whole story.

Whilst commentators, such as, for example, Evans [11], have noted the essential role of the *Chaebols* in the development of South Korea, with the State serving as a key instrument in underpinning the modernization project, this paper seeks to go beyond the surface appearance and examine other key important events and factors that also lay behind South Korea's successful transformation.

There is the key role of the South Korean army which, in addition to its military role, also constituted a source of political and economic power, particularly in the era of Chung Park Hee.

In addition, there is also the economic role of the *rapprochement* with Korea's former colonial power, Japan and South Korea's re assumption of its periphery role in Japan's economy, which had been seemingly terminated in 1945 following the latter's defeat by the newly emerging superpower, the USA. South Korea's own development would also closely parallel that of the rise of the American Empire, particularly through its substantial involvement as a key US ally in the Vietnam War – indeed a number of the *Chaebols* would rise to prominence through their business and commercial involvement in this war.

The winding down of the Vietnam War in the late 1960s and early 1970s might well have had a negative impact on Korea's modernization trajectory but for the increasing trend of the globalization of capitalism, particularly in respect of the inflows of international capital and South Korea's growing importance to Japan as an integral element of its own economic expansion.

The 1973 Oil Crisis led to an opportunity for South Korea as it became a major beneficiary of recycled petrodollars in an arrangement that closely mirrors the triangular trade of the eighteenth century by which the then emerging power, England, benefitted, as noted by Beaud, Gunder Frank, Williams and Wolf [5], [12], [36], [37].

Thus South Korea's own *primitive accumulation* of capital throughout the period was an essential ingredient in it realising its modernizing strategy, or ideology.

Finally, the paper will take a brief look at whether "inclusive institutions" were as important to South Korea's modernization as has been suggested or whether other factors were equally, if not more important, in achieving its transformation.

### **The Analytical Framework**

The Northian Framework is both explained and amply demonstrated in two of North's most recent books [26]. In particular, in the latter book, a number of case studies are examined in the light of their progression, or otherwise, from Limited Access Order to Open Access Order, by reference (supposedly) to the developments in the countries' respective Political/Economic/Violent Capacity organisations.

South Korea is of particular interest given its progression to Open Access Order status in a relatively fast timeframe of a few decades, when compared with the centuries taken by others such as England, France and the USA. There is no intention here to critically appraise the actual facts contained in the relevant chapter which, at first appearance, provide an abridged, but relatively coherent and straightforward, version of historical events of South Korea.

In terms of the Political and Economic Organisations, particularly the latter in the form of the *Chaebols*, North has sought to capture some of the salient points. But a key omission is the third organisation in the Northian Framework – the Violent Capacity organisation, in the form of the South Korean army, which launched the coup in 1961 and remained effectively in power for almost thirty years thereafter, (and a decade thereafter watching from the sidelines). The Korean Army, through President Park (1961-78) and through its creation, the Korean Central Intelligence Agency (KCIA), wielded significant power (if not control) over the Political and Economic organisations. Their influence on South Korea's development was indeed *transformative* and yet has been little addressed. A strict application of the Northian Framework should therefore comment on their involvement and this is taken up in this paper.

A key assumption of the Northian Framework could also be viewed as one of its more serious flaws: namely its reliance on the nation-state as its unit of analysis. To remedy the shortcoming of the nation-state as the sole unit of analysis, we might wish to introduce world-system analysis to supplement the Northian Framework. World-systems are defined as: "intersocietal networks in which the interactions (eg. trade, warfare, intermarriage, information) are important for the reproduction of the internal structures of the composite units and importantly affect changes that occur in these local structures" [8, 28]. As Wallerstein has highlighted: through developments in transportation, military technology and communications, and combined with both political power and military resources, global capitalism spread outwards from its "core", ie the leading societies of western Europe, across the globe. Peripheral, poor societies were coerced into the dominant world system run by the "core". Based on the definition above, at one level, there are attractions contained in adopting this form of analysis with particular emphasis on: *intersocietal networks, interactions, internal structures*. The first two provide a "bridge" to reflecting on linkages and reactions to events, while "structures", although not defined, point towards "institutions" and "organisations" in a nation-state.

However, it might be argued that world-system analysis tends to downplay internal organisations or implicitly assume they have no role in affecting the eventual outcome – that a country has no choices as there is an inevitable process of assimilation into the global capitalist economy. And yet, South Korea, as we will see, evolved from a periphery to a semi periphery to core membership, through both its choices as well as organisational design and adaptation.

In this vein, it is worth noting that Wallerstein did not address Japan or Korea in his four volume work although he has carefully described the amalgamation process into the global capitalist economy for Africa, South America and a substantial share of the Asian continent. 19th century Japan was a notable exception in driving change in its society and economy, through a combination of factors, including significant organisational design and adaptation of western institutions, including that of the VC component, to aspire to core status, as outlined by Moulder [22].

It is therefore interesting to reflect that a former officer of the wartime Japanese Army, Park Chung Hee, South Korea's leader from 1961 to 1978, was a keen admirer of the Japanese Meiji reforms and shared a similar vision for his own country's development<sup>1</sup>.

#### **Mann's 4 Sources of Social Power**

According to Mann, the four sources of power are<sup>2</sup>:

1. Ideological – derived from the human need to find ultimate meaning in life to share norms and values, and to participate in aesthetic and ritual practices. Examples are religion and secular ideologies. It may be *transcendent* – diffusing through boundaries of economic, military and political

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<sup>1</sup> Park's book *The State, Revolution & I*, akin to Lenin's own work, point to his political background. He was a member of the South Korean Workers Party – which amalgamated with its northern part to form the Korean Workers Party, the North's current ruling organ. His brother was killed for his leftist beliefs. Park was saved by his military superiors from suffering a similar fate after 1950. His military background was in intelligence. The US was as alarmed by his assuming leadership of the military coup in 1961 as the North was hopeful of reunification. He was to surprise them both in coming years.

<sup>2</sup> Mann, *The Sources of Social Power*, Volume 2, 2012 edn, p. 258-261

power organisations. It may solidify in an existing power organisation, thus developing its *immanent morale*.

2. Economic - derived from the need to extract, transform, distribute and consume resources of nature. It combines *intensive*, everyday labour cooperation with *extensive* circuits of distribution, exchange and consumption of goods – *circuits of praxis*. All complex societies have unequally distributed control over economic resources and Mann distinguishes between classes which relate to each other vertically and *segments* which relate to each other horizontally within the class they are located.

3. Military – the social organisation of physical forces. Military organisations are essentially *authoritative* and “*concentrated-coercive*”.

4. Political power – derived from the usefulness of territorial and centralised regulation. Political power means *state* power. Its organisation is twofold: Domestically, “*territorially centralised*”, and externally, involving geopolitics.

According to Mann, the struggle to control these organisations sets the stage for social development. Societies are structured primarily through the entwining of these powers. There are *linkages and interactions* between them – ideological, military and political organisations help structure economic ones and vice versa. The power sources generate *overlapping, intersecting* networks of power relations and their *interrelationships* can produce unanticipated, emergent consequences for actors.

Mann also adds Leadership as a determinant power, citing the “development of a kind of vision” by statesmen and generals, “or sensing what will work and what will improve”.

Mann’s analysis would appear, on the face of it, to combine the Northian Framework – Violent Capacity/Political/Economic organisations, with a perspective that encompasses both interactions within a stated territory between them, as well as influences and other factors falling outside the boundaries of a nation-state – geopolitics. It also contains another ingredient, namely of Leadership, which can have a marked influence on the substantive sources of social power. It therefore represents both an advance on, and enhancement of, the Northian Framework.

Furthermore, the above paper’s title explicitly borrows from Mann in its plural use since the development of South Korea was influenced by the globalization of capitalism, the globalization of the nation-state and the emergence of the first global empire, the American Empire.

#### **Primitive Accumulation**

Perelman has examined the attempts by classical political economy to downplay the role of primitive accumulation in the rise of global capitalism. Economists have demonstrated some reluctance to give the area serious examination. Keynes briefly noted his profession’s averseness to considering “the dark side” of economic history in his 1930s work [13, 150-159]. It has therefore been left to writers such as Gunder Frank and Amin to follow up on Marx’s own (incomplete) musings on the subject. Williams has looked at the links between slavery and the Industrial Revolution in England by which the former assisted in financing the latter. Beaud’s own work looks at this “triangular trade” between England, West Africa, the West Indies and North America whereby England’s manufactures (including arms) were swapped for slaves, which were then shipped to the plantations in the West Indies and North America for the production of sugar and cotton, which then were transported to England for the fast developing textile industry located in and around Manchester.

Other works of note include Wolf who, in addition to considering the fur trade and slave trade, examined the financial and trade linkages between Brazil-Portugal-England as well as England-India-China (the Opium trade).

#### **The Military as an Institution**

It is noteworthy that the Northian framework gives specific mention to three organisations: Political organisation; Economic organisation; and Violence Capacity organisation. North sets out how the organisations evolve between the stages of fragile, basic, mature Limited Access Order before meeting three “doorstep conditions” to reach the pinnacle status of Open Access Order. The underlying themes of the framework encompass the following:

- The centrality of violence.
- Centrality of organizations in structuring relationships both within and between polity, economy and the wider society.
- Rents.
- Dynamics of society – constant changes.

For this particular section, attention is focused on the VC organization and its underlying purpose of effecting coercion. Following the military coup of May 1961, the South Korean military, through Park, was to exercise considerable power (if not outright monopoly) over the politics of the country for the better part of the next three decades. It (and particularly, Park) occupied a near central role in structuring the economy and society as a whole. The military, as well as through its

guise as the Korean Central Intelligence Agency (KCIA), also became a key participant in the circulation of rents either as a direct beneficiary or as a key participant in their creation, *selection* and distribution.

The critical figure in South Korea from 1961 to 1978 was Park Chung Hee, a former officer in the Japanese Army and a general in the ROK army, who was a leader of the military coup in 1961. For two years, Park governed South Korea through the junta's Supreme Council of National Renewal and then as the country's President from 1963 onwards.

Soon after the coup, Park had arranged the arrest of over 20 leaders of the major *Chaebol* business groups on grounds of corruption [17, 273-274] and had used this to force the arrested businessmen to come to terms with the junta to secure their release in return for investing in Park's engines of economic growth. While this form of coercion was not entirely successful, it had focused business leaders' minds on the need for cooperating with the new government to secure support and funding for their future business ventures.

In addition, Park renationalized banks which had been privatized in the 1950s. The banks would serve as a key instrument for ensuring *Chaebols* invested in sectors and industries, according to Park's plans. Allocation of domestic and foreign loans, through credit rationing, at low interest rates served as a means for favoring certain firms and exporters in return for political contributions – “monopolistic clientelism,” and their monopolies were protected by restricting the entry of other firms into specific industries, thus permitting the incumbents to enjoy “monopoly rents”. Such a mechanism would only be unpicked after the 1997 Asian financial crisis.

Park had also, on consolidating power, initiated a Comprehensive 5-Year Economic development Plan which would focus South Korea on building up a Heavy and Chemical Industry (HCI) base. Interestingly, the initial chosen instrument for implementing this policy was the newly established KCIA but a series of scandals, including this agency's involvement in setting up the regime friendly political party, the Democratic Republican Party<sup>1</sup>, had led Park to switch economic policy being effected through the Economic Planning Board, which was firmly under his control. The KCIA would be tasked with ensuring Park's political allies were adequately funded through subventions from the *Chaebols*, running a covert foreign policy to seek an agreement with the former colonial power, Japan, and engaging in intelligence gathering, blackmail and coercion against the more recalcitrant elements of South Korean society, including trade unions and the political opposition<sup>2</sup>.

The first task of the new economic plan was a reorganization of the power industry but the substantial priority of Park was to establish an integrated steel mill, as part of the country's national defence and as a step towards creating an industrial capacity to counter North Korea's own military-industrial base. Park's stated policy was *pukuk kangbyong* (“rich nation, strong army”<sup>3</sup>) based on the Japanese slogan of the Meiji era reforms of *fukoku kyohei*. For Park, “Steel is national power” and it was viewed as a measure of military prowess, economic modernization and technological progress. Iron and steel in the 1960s was the country's second largest import after oil and thus a further motive of import-substitution could also be added. The *rapprochement* with Japan in 1965 (see later below) would provide the funds to proceed with this project which had hitherto been rejected by the World Bank.

The military's involvement in running the economy was deployed alongside the growing cooperation with the *chaebols* to secure particular industrial objectives. We have seen that military officers were used to reorganize the power sector and a trusted officer colleague of Park was selected to run the Pohang Iron & Steel Company (Posco). Park also sought to build up rival *chaebols* to sidestep the conservatism (and/or opposition?) to his ideas. Thus, he built up Kyongsang *chaebols* at the expense of northern ROK *chaebols*, such as Ssangyong and P'anbon which entered the “Top 10” Korean companies by 1965 whilst 4 out of the ten largest *chaebols* in 1960 had dropped out of the “Top 10” by 1965. Park was also using regional references as a further means of establishing local political support: for example, building Ulsan-Mip'o in North Kyongsang province in 1962 as a centre for HCI – Hyundai Motors was housed here by Park<sup>4</sup>.

In addition to “socializing” the risk of the foreign currency loans taken on by the *chaebols* as well as directing strategic projects to them, Park also ensured that his government served as the

<sup>1</sup> Of particular note: Park's nephew, Kim Chong-p'il was in charge of the KCIA. One of the scandals was the extraction of rents from an early car venture, Saenara, which collapsed as a result. Park would learn by this mistake when it came to, say, Posco, which was exempted from paying such rents.

<sup>2</sup> Including a Korean variant on rendition involving the kidnapping from Japan in 1973 of the opposition leader, Kim Dae-jung. He was saved from a more unpleasant fate due to the uproar which ensued from Japan and later released unharmed. He became South Korea's President between 1998-2003.

<sup>3</sup> As imitated perhaps by the later North Korean variant: to “build the DPRK into a militarily strong and economically prosperous state (Kangsong Taesuk)”?

<sup>4</sup> Kim & Vogel ed, 2011. Re Posco, p96, p324-5 & p334-344. Re *Chaebols*, p281 & p638-9. Re Hyundai, p298. The building of Posco was central to Hyundai's success with its “Pony” motor car.

guarantor of their business risks. Thus, the State became both “predatory and developmental” while the *chaebols* were both “cronies and entrepreneurs”. Park was serving as the principal regulator of the ensuing moral hazard. As the *chaebols* were central to the development plans, this might lead to actions that could lead to property rights – a key institution in the Northian diagnostic framework for Open Access Order status, being undermined. For example, South Korean companies were borrowing from banks and paying interest at 24-26%; this led to an unofficial curb market in loans to the conglomerates. When the *chaebols* encountered significant problems in their businesses in the early 1970s, the government passed the Emergency Decree on Economic Stability and Growth which unilaterally reduced the corporate borrowers’ financial burden by 2/3 on average at the expense of private lenders [17, 250-251, 282].

Thus, the key to political power in South Korea was “guns, money and regionalism”. Park was in firm control of the military, via the KCIA but also an increasing plethora of other secret agencies with overlapping functions and answerable to Park. In addition to the banks, rents were generated by high tariff rates (far higher than compared with Japan and Taiwan) and through reparations from Japan and the growing involvement of Korea in Vietnam (see later) and directed to *chaebols* for starting up new activities. For Park, “development and rent seeking were different sides of the same coin” [17, 152, 202, 230-231]. Regionalism was achieved by the targeted direction of HCI projects to favoured provinces to solidify political support. The “guns” also served to coerce any countervailing powers in society at large to remain broadly quiet in opposition. Historical circumstances involving the destruction of the *yangban* landlord class through land reform after the Korean War, which might have served as countervailing power, had removed this potential source of opposition [17, 28], [23, 299]. Park had also served to insulate the bureaucracy from politics by “purging” those unfriendly after the military coup and promotion of friendly, technocratic, often military linked, supporters to key positions as well as tight control of strategic agencies from the Blue House.

In December 1971, following a close run Presidential election, the National Assembly passed the Special Law for National Security which effectively accepted military intervention in politics as “part of everyday life”. The *Yushin* state was a garrison state in law as well as in practice.

#### **The South Korean Economic Miracle: Trick or a US “treat”**

We can examine the timeline of South Korea’s economic miracle by reference to its statistics which provide a measure of the outcome of the policies adopted<sup>1</sup>.

From 1962, when Park Chung Hee introduced his first Five Year Plan, to 1971, South Korea’s average rate of GNP increased by 10 % per annum, with a peak of 14% in 1973, just as the Oil Crisis was starting to take hold in the developed world. Per capita GNP increased between 1963 and 1973 from \$ 100 to \$395. Exports grew from \$ 32 million to \$ 3.2 billion in 1973 to \$ 5.1 billion in 1975.

Following the 1973 Oil Crisis, GNP growth slowed to 8.5% while exports growth decreased from an average of 35% per annum (1965-75) to just 6% in 1975.

The “miracle” was obtained not without considerable cost. While the export statistics were impressive – trade as a share of GNP had increased from just 2.9% in 1960 to 36.8% in 1971 and 61% in 1974 (compared with just 20% in Japan), South Korea was heavily dependent on imports in the form of US grain (to feed her citizens – self sufficiency in food production had fallen from 80% in 1969 to 65% in 1969), cotton (for her textile industry), imported ore and scrap iron (for her steel industry), imported lumber (for her sawmills), imported components (for her electronic industry) and imported oil (to run all her industries). South Korea also ran a substantial trade deficit from 1962 which amounted to around \$ 1 billion per annum between 1968 and 1973, and which rose to almost \$ 2 billion in 1974.

Indeed, in the light of its ongoing trade deficit problems, the IMF had signed a standby arrangement with ROK in 1968 which was renewed in 1969. In June 1971, the IMF would step in again with another arrangement to assist South Korea in return for conditions [17, 249, 121, 222, 231, 243].

The trade deficits were met by a number of sources: firstly the US had provided substantial aid to South Korea throughout the 1950s and early 1960s – US aid financed 90% of the ROK’s government budget as late as 1961, some of it in the form of agricultural aid and outright grants of \$ 4.5 billion. Overall, US post (Korean) war aid and economic assistance was seven times that enjoyed by North Korea<sup>2</sup>. Secondly, by recourse to foreign loans. Accordingly, cumulative foreign

<sup>1</sup> Unless otherwise stated, this is drawn from: [Gittings et al, Crisis in North Korea, 1977, p57-62 & p125-138; and Hwang, The Korean Economies: A Comparison of North and South, 1993].

<sup>2</sup> Between 1959-63, US aid totalled \$ 230 million per annum. In 1961, GNP was around \$ 1.9 billion. As far as I am aware, this aid would exclude US military’s consumption of goods and services ie 60,000+ US troops spending their wages and significant military construction contracts awarded to local firms such as Hyundai.

debt had increased from \$ 3.6 billion in 1973 (34% of GNP) to \$ 8.4 billion in 1975, and South Korea required new loans to meet repayments of existing loans.

In 1974, US banks had rejected a South Korean request for a loan of \$ 200 million but, as part of the recycling of oil monies to be effected by US banks, agreed to initiate re lending in the Spring of 1975. According to Gittings et al, by August 1975, 83.5% of foreign bank loans and credit lines to South Korean banks (\$2.3 billion) was derived from US banks.

This however also ignores *indirect* US assistance which was granted through the World Bank (WB) and the Asian Development Bank which was respectively a further \$ 1 billion in loans and credits (from the International Development Association – provider of “soft loans” by the WB) and \$101.5 million. The US government owned EXIM Bank had provided a further \$ 502 million to South Korea.

A further source of finance was derived from the Japanese. In 1965, despite significant popular opposition to doing so, and requiring army on the streets to curb significant disorder<sup>1</sup>, South Korea reached an agreement with Japan to settle a significant number of issues arising from the Japanese colonial occupation and for the Japanese to make reparations. The reparations had initially been proposed in the form of Japanese consumables but President Park had an alternative means of employing the reparations.

In the late 1960s, President Park had pursued a vision of establishing the country's own modern steel plant but had encountered significant resistance from foreign lenders, including the World Bank, in realising such an ambitious industrial project. The World Bank, in particular, had cited concerns over the risks of establishing such an industry given the smallness of the size of the domestic market and its financing. Park turned to the Japanese for a solution and had secured the almost \$ 800 million of reparations in the form of project assistance in the construction of South Korea's state owned steel company – Posco, which is now one of the world's largest steel producers.

The agreement with Japan had also led to South Korea increasing its dependence on Japan for capital loans and investment. The 1965 agreement had led to a significant upsurge in Japanese loans in the 1960s which had fuelled South Korea's development until problems arose in 1971. The Park plans for Heavy and Chemical Industry depended for their accomplishment on the “continuing Japanese desire” to relocate their industry overseas arising from high domestic costs, land costs and pollution, and thus achieve the “structural incorporation of Korean industry into Japan's reproductive capacity”<sup>2</sup>. Thus the export sector, which accounted for 70% of industry, while nominally in Korean ownership, was actually Japanese or underwritten by the US government, business and banks.

Problems in South Korean firms' propensity for borrowing had led in 1970-1 to a search for direct investment. The Park government had announced incentives, including total tax exemption and strike-free labour force, to foreign investors. The first Export Processing Zone, with free roads, water, harbours et al was established in Masan. 90% of all the investment in the EPZs was derived from Japan and Japan was the leading foreign direct investor in South Korea in 1973 and 1974.

The terms of trade with Japan were such that 40% of all South Korea's imports came from Japan between 1969-74, and such trade accounted for almost 70% of the country's trade deficit.

In both form and substance, South Korea had rejoined the world-system from which it had been liberated in 1945 by exchanging a nominal peripheral status as aid recipient for its former colonial role as an integral component of Japanese manufacturing system.

A darker, and more seamier, side of the Korean-Japanese rapprochement was felt in the increased levels of Japanese sex tourism in South Korea which is believed to generated revenues of \$ 120 million per annum in the mid 1970s.

#### **The Korean involvement in Vietnam**

Korean involvement in the Vietnam War<sup>3</sup> had initially been of a token amount but over time would amount to the second largest foreign involvement, after the US – at its peak, 50,000 troops, and by the war's conclusion would lead to 300,000 Korean troops having served in this theatre of war. Park was keen to stabilise a relationship with a critical ally which had been strained throughout the Kennedy presidency. The offer to send troops would provide evidence of the ROK as a critical and loyal ally of the US; minimise the possibility of the Johnson administration transferring US troops from the Korean peninsula which might destabilise Park's industrial agenda and political administration, as well as emboldening North Korean designs for a “military solution”; and to also secure a monetary advantage for the country.

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<sup>1</sup> Kim & Vogel ed, op cit, 2011, p172: “threw society into turmoil that could be controlled only by the military”, & p380.

<sup>2</sup> Gittings et al, op cit, 1977, p61.

<sup>3</sup> See Gittings et al, op cit, 1977, p115, p121, & p124; Kim & Vogel ed, op cit, 2011, p174, p177, p279, p405, p419-20, & p.425-6.

Under the Brown memorandum of 4 March 1966, South Korea would receive \$ 1 billion of military and economic aid between 1965-70, which accounted for around 19% of South Korea's total foreign exchange earnings. There were also US AID loans for US\$ 150 million as well as a further \$ 150 million in program loans for supporting ROK exports and development projects.

The South Korean armed forces were one of the largest participants in the Vietnam War after the US itself and by the mid 1970s almost 300,000 (out of a total of 595,000) had served in the Vietnam theatre. The South Korean armed forces were heavily subsidised by the US with the South Korean government responsible only for food and clothing.

Between 1965-70, the US provided \$927 million as financial support to South Korea. Total ROK earnings from the Vietnam War were estimated to be over \$ 1 billion between 1965-72. At the same time, ROK increased its exports to South Vietnam ten times between 1964 and 1973. The critical connection with the US had also served as a helpful backdrop to securing several billion dollars of foreign loans to fund strategic projects and alleviate the ever present foreign exchange problems.

Between 1971-6, under a military modernisation plan agreed in 1971 as part of the US drawdown in Vietnam and the drawdown of one US army division from South Korea, it was agreed that US military assistance and sales to South Korea would amount to \$ 2.1 billion, although this excluded the cost of maintaining 40,000 US troops on the Korean peninsula, with South Korea committed to spend a further \$6.5 billion. The agreement also served to finance the construction of a giant industrial complex in Ch'angwon in April 1974 for the manufacture of military weapons. This modernisation plan was revised again in 1975 with the US to invest a further \$ 2 billion by 1980.

In addition to the abovementioned arrangements, South Korea further benefited from the construction contracts granted to Korean firms, particularly Hyundai Construction<sup>1</sup> which gained contracts in both South Vietnam and Thailand, as part of the offset agreement, which led to significant numbers of Korean workers working overseas and sending back remittances. The export of labour was to constitute a major growth area of the economy. Overseas work contracts in 1975, as the Vietnam War, concluded was estimated to be worth around \$ 850 million.

Another beneficiary of the Vietnam War was Hanjin, the shipping company, airline and bus and truck transport and logistics conglomerate, which also gained considerable business contracts from the US.

#### **Korean migrant labour**

We have noted above that the South Korean construction companies were able to generate significant construction contracts in Vietnam which generated substantial foreign exchange earnings. In addition, as of September 1975, South Korea had 40,000 seamen (principally working on Japanese vessels), 11,000 nurses and 7,000 miners working overseas sending back remittances<sup>2</sup>. However, at this time, South Korea would enjoy a further positive economic shock which would greatly assist it overcome mounting problems in its foreign exchange reserves and ongoing trade deficits, as well as funding the Chaebol's development plans.

It has been noted that the Vietnam War was concluded in 1975 although the US (and effectively South Korean) involvement had been sharply reduced in the early 1970s. In October 1973, the Arab countries had announced an oil embargo against the US, European and other developed countries in the light of the Yom Kippur War. Oil prices had sharply increased in the aftermath and South Korea had experienced a significant slowdown in both GNP and export growth, as well as increased trade deficit from adversely affected oil imports.

The increased oil prices had led to windfall gains for the OPEC states and, in particular, the regimes of the Middle East. The US, through its then Secretary of State, Henry Kissinger, had negotiated to ensure that the petrodollars earned by a number of the states, ie Saudi Arabia, would be "recycled" back into the global financial system by US banks. The petrodollars would also feed into increased purchases of industrial and manufacturing facilities by the Arab states as they sought to establish an indigenous industrial base to diversify away from reliance on oil production. Western (and principally US) defence companies would also benefit from significantly increased arms sales. To give one example: the then Shah of Iran invested \$ 8 billion in the modernisation of the Iranian armed forces after 1973.

With petrodollars, the Middle Eastern states would also be able to finance a considerable amount of infrastructure projects and construction, including of highways, in their relevant countries and would look to South Korean construction companies (who had enjoyed a high reputation for their work in Vietnam) to meet their requirements. The Economic Planning Board co ordinated

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<sup>1</sup> See A van Agtmael, *The Emerging Markets Century*, 2007, p145]; Hyundai was founded just after WWII and grew rich through the Korean war and after, through US military contracts. In the 1960s, servicing construction contracts with US military accounted for 70% of profits and 25% of revenues.

<sup>2</sup> Gittings et al, op cit, 1977, p67, note 18.

South Korea's response to this opportunity through its Commission on Enhanced Cooperation with Middle Eastern Economies regarding construction projects [17, 277].

Between 1975 and 1985, 1.1 million Koreans would work in the Middle East on such projects on behalf of over twenty South Korean companies, including Hyundai Construction. Indeed, Hyundai Construction's first project in the Middle East was in Iran building a shipyard for the Iranian navy near Bandar – e Abbas. Average wages paid to South Korean workers were around twice that in South Korea and migrants remitted home around 80% of the total.

Other facts and statistics reveal the magnitude of the importance of this business opportunity:

- Hyundai Construction successfully bid for the Jubail Industrial harbour in Saudi Arabia – a contract worth \$ 931 million, which was approximately half of the ROK's annual national budget.
- By 1985, South Korean construction companies had earned \$ 80 billion – a significant share of which was transferred to the *chaebols*' manufacturing affiliates to finance development projects such as the auto sector.
- Such earnings significantly contributed to the ROK's GNP growth from the late 1970s to the early 1980s and were a substantial generator of foreign exchange for a country that was prone to recurring financial crises through its indebtedness and significant trade deficits<sup>1</sup>.

#### **South Korea's "Triangular trade"**

Taking the above into account and now looking at the facts established in respect of the 1960s and 1970s, we can observe that GNP (or GNI) in South Korea was already influenced by the aid that it was already receiving from the US from the 1950s and early 1960s (before it was to be "tapered off") and the indirect benefits of the US forces stationed in the peninsula awarding construction contracts to local firms or even spending by GIs serving in the country. The surge in GNP arose from the South Korean involvement in Vietnam in the mid 1960s as the US provided direct aid in return for military assistance, and major South Korean firms, such as Hyundai Construction and Hanjin, generated substantial profits that were remitted back to South Korea. As noted, between 1965-72, South Korea earned over \$ 1 billion from its involvement<sup>2</sup>.

A further windfall materialised in the mid to late 1960s with the conclusion of the reparations agreement with Japan for which South Korea derived \$ 800 million. The encouragement of Japanese MNCs to relocate to South Korea also provided benefits: the South Korean government financed the construction of necessary infrastructure (further adding to GDP and GNP) and Japanese firms, while paying wages and salaries, and generating profits (both contributing to GDP and GNP). Given the Japanese propensity to invest profits in newly established operations, it is unlikely that there were substantial profits remitted back to Japan to impact GNP, until much later in the life cycle of the Japanese owned South Korean subsidiaries.

At the same time, due to its Vietnam War involvement, South Korea also received significant loan packages from US banks as well as further aid and assistance from various institutions such as the IMF, World Bank, US AID, EXIM Bank and ADB, which may have also served to "cushion" GNP as well as staving off foreign exchange crises and fund the various strategic HCI projects of Park and the *Chaebols*.

The twin effects of the Vietnam War and the *rapprochement* with Japan would also set the stage for South Korea to bring together (or intermediate between) Japanese MNC investment with a benign US market to become a major exporter. Thus, the USA accounted for 40% of its exports while Japan accounted for 40% of total imports, and South Korea was dependent on foreign loans to finance 25% of its imports.

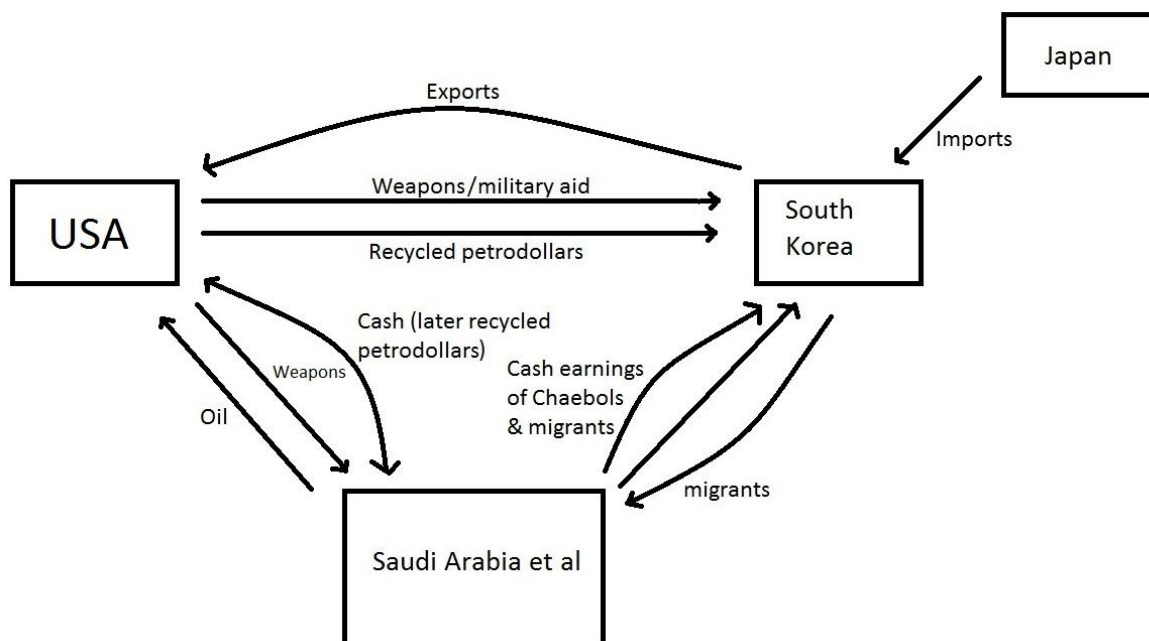
The 1973 Oil Crisis became a further opportunity for the South Korean economy to flourish in terms of GNP. While the US, in the light of its drawdown in Vietnam and to allay security fears of its South Korean ally, still provided significant aid assistance during the 1970s (thereby positively impacting South Korean GNP), South Korea also benefited from the construction boom from which over one million South Korean workers remitted 80% of their average wages (twice the South Korean national average) and firms remitted substantial amounts of profits – both positively impacting South Korean GNP.

At the same time, South Korea enjoyed substantial loans from US and other western banks to continue its development strategy – the level of lending as well as South Korea's strategic importance to the US made it a candidate even then for "Too Big to Fail" in the event of concerns over its economy. The overall movement of people, goods and financial flows for the mid 70s to mid 80s can be summarised as follows:

<sup>1</sup> Re Hyundai and forex earner, see [Kim & Vogel ed, op cit, 2011, p292; ME earnings, ditto, p. 228.

<sup>2</sup> Interestingly, Gittings et al, op cit, 1977, cite a source stating that, in fact, South Korea generated, in total, \$10 billion for new military equipment, assistance to South Korean businessmen and employment of South Korean civilian workers in South Vietnam, including payments to Korean troops in the Vietnam theatre of \$ 1.7 billion. See p144, note 6.





The scale of the transformation in South Korea can be viewed by reference to the following table showing the sectoral contributions (in %) to total GDP at the onset and conclusion of the Park era:

	Agriculture	Industry	Services	Total
1960	38.0	20.5	41.5	100
1980	14.9	31.0	54.1	100

The increases in both GNP and GNP per capita for the period can be demonstrated as follows:

Year	GNP (US\$ millions)	GNP per capita (US\$)
1960	1,948	79
1965	3,006	105
1970	8,105	252
1975	20,795	590
1980	60,327	1,589
1985	89,695	2,195

#### Further Considerations

After the death of Park in 1978, the KCIA and other security agencies were to still serve as major tools of coercion up to 1987 when South Korea achieved its democratic breakthrough. The military was to be involved in the violent repression of the Kwangju Uprising in 1979. Notwithstanding, the rise of the Army Security Command taking over the KCIA and various reorganisations, that led to its present form, the National Intelligence Service, the agency is still believed to be involved in wiretapping of politicians and has occasionally surfaced in other high profile cases of a national security character, including the arrest of a South Korean politician over allegations of connections with North Korea.

Given South Korea's progress has been heavily influenced by external factors, in addition to the multifaceted relationships with US and Japan, it is also worth bearing in mind, the following developments in the world economic order [17, 20]:

- Tariff barriers in the developed world were lowered in the 1960s through the Kennedy Round of GATT (General Agreement on Trade and Tariffs, now supplanted by the World Trade Organisation).
- Nontariff trade barriers, including financial subsidies (of considerable importance in the context of the government's assistance to the *Chaebols*) were left until the Tokyo and Uruguay rounds, thus providing South Korea with a two-decades long advantage.
- Expansion of international commercial lending throughout the 1960s and given an additional boost in the light of the recycling of petrodollars post 1973.
- Multinationals relocating declining business via technology licensing and direct investment, as exemplified by the concept of "flying geese".

Furthermore, while Evans view of corporate coherence and embeddedness<sup>1</sup> are key to the “developmental state” and are therefore relevant in the context of South Korea, its most critical component was the “visible hand” of Park whose vision was to achieve a “second Japan” and to this effect, wielded the full array of tools from coercion to intra elite coalition building to realise that dream. While the “developmental state” was intentionally bound to society, its embeddedness was more “asymmetric and political” with Park negotiating deals with the *Chaebols* in the Blue House.

#### **South Korea versus North Korea: Do Institutions matter?**

Partway through North’s chapter on South Korea, the author poses the question: “Does the Korean case suggest that economic growth comes first and transition to Open Access Order comes later?” Park himself stated: “Democracy blossoms only on the fertile soil of economic development” [17, 388]. The question and statement raise important questions for the role of institutions in a country’s development.

I would suggest that the author has reached a conundrum in part due to weaknesses in carrying out a historical institutional analysis as well as encountering the limits of the Northian Framework. The Northian framework is constrained by its focus on the nation-state at the expense of wider considerations. Given the South Korean economy was reliant, inter alia, on aid, windfall gains and exports, it was always likely to be a challenge to adequately link economic development with these determinants when the measure is GDP, rather than GNP, and one is analysing domestic affairs without recourse to external dynamics. I would also proffer the view that the Mann model, which adopts a more holistic approach, with its ability to reflect on geopolitical and leadership sources of power, is a far more appropriate model to apply. Indeed, a further drawback is also the *failure* to correctly apply the Northian Framework by considering the VC organisation in greater depth. The VC organisation in South Korea suffused and permeated the other organisations, both Political and Economic, and this might have served as a “lever” to extract the relevant facts.

In their book [1, 70-73], Acemoglu and Robinson, compare South and North Korea. In their analysis (as with North), there is no mention of significant US aid or the windfalls gained from the diplomatic rapprochement with Japan or the Korean benefitting from the Vietnam War and the Middle Eastern construction boom. South Korea’s status is all due to “inclusive economic institutions and secure property rights”.

Even North does not go this far. On the contrary, the author notes the clear breach of property rights in the bank renationalisations as well as the Emergency Decree of 1972 to avoid the *Chaebols*’ financial collapse through overborrowing. The author also notes [27, 318]: “The rule of law was weak even for elites”. Park’s approach to such matters was pragmatic, to say the least, and all matters of the law were of secondary importance to retaining power and pursuing the “second Japan” project. Martial law was employed at will and from late 1971, military rule was enshrined in both law and practice.

Both North and Acemoglu, particularly in the light of “inclusive institutions” (as opposed to “extractive”) might also take note of the following observations by Kim et al [17, 202]: “development and rent seeking were different sides of the same coin”. Also “the market was viewed as an instrument of his political goals, a device of the dirigiste state to speed up modernisation through telescoping the stages of economic development”. On the contrary, rent extraction served to “grease the wheels” of both politics and business in the country – for example, in 1969 of the \$800 million government loans granted, \$ 160 million was returned as political funds, - and operated within certain Park made constraints. Markets were a “means” rather than an “end”.

Indeed, a strict comparison between South and North Korea might not support Acemoglu and Robinson’s premise since upto around 1970-5, North Korea’s economy was viewed as being the better performer of the two<sup>2</sup>. South Korea’s per capita GNP only started to exceed North Korea’s at about this time. Given both countries were effectively run by Military powers, which directed Economic power, albeit North Korea’s possessed a stronger Ideological power than South Korea, one is left to examine the following salient differences: 1. South Korea’s trade as a % of GNP amounted to around 60-70% while the North’s was around 7%. South Korea traded externally with both the US and Japan, while the North had opted to avoid Comecon membership and concentrate on meeting its own domestic needs. The North was (and still is) subject to a US trade embargo.

<sup>1</sup> Evans, *Embedded Autonomy: States & Industrial Transformation*, 1995; and Kim & Vogel ed, op cit, 2011, p200-1. On p10-13, there is a significant discussion on why Evans is not wholly relevant in the case of Park’s South Korea.

<sup>2</sup> See Armstrong, *Tyranny of the Weak, North Korea and the World 1950-1992*, 2013, p58-9: “By the early 1960s, according to American officials, South Korea appeared to be a ‘black hole’ for aid assistance, while the North had impressively industrialized”. See also Bibliography re Brun & Hersh, 1976 & Breidenstein & Rosenberg, 1975; also Choi, *A Study on the Structure of Industry in North Korea*, 2006.

2. Both had incurred significant foreign indebtedness and trade deficits in the late 1960s/early 70s. South Korea enjoyed a significant influx of initially loans, and the direct investment, and when it encountered serious financial difficulties, its economy was backstopped by both the US and the IMF. North Korea defaulted on its foreign borrowings in the mid 70s, it was (and still is) barred from the global capital markets.

3. South Korea signed a treaty with Japan in 1965 and received \$ 800 million. To date, North Korea has never received reparations from Japan for the colonial era. While North Korea's ideological power contains a strong anti Japanese component, even in the South the agreement was viewed as widely unpopular and provoked considerable unrest.

4. While the North received aid from the USSR, Eastern bloc and China, the amounts were a fraction (around one-seventh) of that obtained by South Korea from the USA upto 1975. North Korea enjoyed no windfalls comparable to that enjoyed by the South for its participation in the Vietnam War.

Therefore, rather than institutions, other factors, primarily of a geopolitical nature, served to accentuate the growing disparity between the two's relative economic performance, which would widen even further after the Middle East construction boom from 1975-85.

### **Conclusion**

The use of Mann's analytical approach provides some a richer texture than applying the Northian Framework. We noted that "Ideology" is present in the form of Park transforming "economic development [into] the ideology of the day". We might also add that "Leadership", a Mann concept derived from Weberian roots, in the form of President Park is a central figure in the development of South Korea.

It is however the "Political Power" which has been most elaborative in that this has overcome the Northian Framework constraint of the "nation-state" and its domestic focus. Mann's inclusion of "geopolitics" and his use of "globalizations" have enriched our understanding of South Korea's economic development by drawing attention to the diplomatic agreement with Japan (pursued by the KCIA and popular discontent subdued by the Military through martial law) as well as the involvement in Vietnam which generated a substantial uplift in both direct and indirect financial assistance, ranging from US direct aid to US bank loans, as well as a ready market for exports<sup>1</sup>. The former can be viewed as South Korea's reattachment to the globalization of capitalism and the latter to the development of the US as the first global empire. The winding down of the Vietnam War was eased by the opportunities arising from the mid 1970s in the Middle East as well as the recycling of petrodollars, facilitated by, inter alia, US financial institutions and US backed international financial institutions, in terms of loans to South Korea. These circumstances would lead to South Korea's accumulation of capital - its primitive accumulation, which served as a major contributory factor to enable it to achieve its growth trajectory. The *Chaebols*, a source of Economic Power, were enriched by both the Vietnam War and Japanese inward investment, as well as by the Middle Eastern construction contracts post 1975, as well as benefitting from Park's ideological vision to create a "second Japan" – the globalization of the nation-state. Indeed, the share of GDP produced by the Chaebols rose from 21.8% of GDP in 1973 to 33.2% in 1978.

The Military Power suffused Political and Economic Powers in terms of the military dictatorship employing the KCIA to coerce parts of society and to retain labour competitiveness and the use of the KCIA to obtain rents and use to solidify political support as well as assist in pursuing economic objectives. During the Park era, 42.4% of all cabinet-level ministers had backgrounds in the military – this fell to just under 25% by 1981-87 [18, 180]. The Military transformed society and directed its personnel to run important sectors of the economy. The Military also was a lead actor in the development of an indigenous steel sector, - a source of military and technological advantage.

Indeed, it might be argued that the only substantive institution that operated throughout the takeoff was the Military itself. As has been demonstrated, the Military power suffused all other sources of social power. The Military exercised both domestic political power and geopolitics, through the KCIA's secret diplomacy with Japan. The Military waged war in Vietnam and ensured domestic tranquillity. It also exercised significant Economic power through arranging the windfall revenues from both Japan and its Vietnam war involvement; it provided its personnel to run new ventures; it developed the indigenous HCl industry with military applications; it trained, organised and inculcated its male population; it facilitated the growth of the Chaebols. It enthused society with the "soldiers spirit".

It was the key source of social power and innovation in South Korea, and was instrumental to the country's primitive accumulation that significantly contributed to its economic success. Without it and Park, its present status would have been unlikely.

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<sup>1</sup> Kim & Vogel ed, op cit, 2011, p211]: "Park was able to secure foreign capital only when he brought politics into a foreigner's...calculation of costs and benefits".

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