

The Role of the State in Economic Development: Japan, South Korea, and Taiwan

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Postwar economic growth and social progress in Japan, South Korea, and Taiwan have been attributed to various factors. Geopolitically, they were considered the main battlefields against the communist movement. In order that they effectively resist the communist threat through economic success and social prosperity, core capitalist countries provided them with substantial aid and development opportunities in the world system. These included: (1) controllable foreign capital; (2) US military aid; (3) state dominance in the Triple Alliance; (4) a docile labor force; (5) emphasis on public education; (6) Confucianism, conscientious leadership, respect for authority, collectivism, industriousness, and frugality; (7) economic strategies of high investment ratios, small public sectors, export orientation, and labor-market competition; and (8) shrewd and smart statesmen and technocrats (Deyo 1987; Berger and Hsiao 1988; Perkins 1994).

On the role of the state, there are two schools of thought. The bureaucratic regulation thesis regards the state as a dominant force in incorporating various resources into a positive thrust for economic development (Johnson 1982). The market regulation thesis, on the other hand, emphasizes the quick response to market changes and the adept grasp of trade and production opportunities from Asian industrialists (Samuels 1987). Both, however, agree that the state plays an important role in the East Asian miracle.

This paper provides a comprehensive analysis of the role of the state in economic development in Japan, South Korea, and Taiwan. Through such an analysis we hope to gain a thorough understanding of why and how an essentially undemocratic government pushes private initiatives for economic growth and social progress.

The Role of the State: Reasons

Why does the state have a role to play in East Asia's economic development? What underlying force or environmental factor prompts the state to enter the economic sphere?

There are both historical and geopolitical reasons. First, traditional Asian societies were built around a feudal hierarchy of power. Civil society was weak and subordinate to ruling elites. There was no developed merchant class, much less any industrial corporation. Japan, in the mid-19th century, lacked every single condition for the development of a market economy. 'Foundations for a new era of expansion seemed, at any rate to casual observers, to be ill prepared' (Allen 1981: 167). Change had to be imposed from above. There was a phenomenal lack of initiatives from below.

Second, Western advance put the Emperor and power elites to shame. While Qing Royal Court in China and Tokugawa Shogunate in Japan endeavored to resist Western influence, civil society seized a chance to grow with its newly-acquired scientific knowledge and bourgeois commercialism. But the old regime remained an obstacle to the development of a Western-style merchant class and industrial system. A new power center was needed to lead the nation in the pursuit of a new discourse.

Third, in Japan, the House of Tokugawa was overthrown in 1868. The succeeding Restoration Government 'judged that the rapid adoption of Western methods in war and industry could alone enable her to retain her independence and ultimately to secure the abrogation of the unequal treaties' (Allen 1981: 32). Social restrictions were removed. Freedom of movement, communication, enterprise, cropping, and acquiring properties were introduced. Realizing that *laissez-faire* was not suitable for its backward economy and that few entrepreneurs were able to build up Western-style industrial and commercial enterprises, the Japanese state assumed an active role in the founding of new industries. Manufacture, munitions, and foreign trade were created and expanded with direct state involvement. State sponsorship continued throughout the early and middle Meiji period and remained strong during Japanese ascendance to a regional and international power.

Fourth, with newly-acquired energy from development, Japan soon assumed the role of imperialist expansion in Asia, in a sense on behalf of Western powers. In Taiwan as early as 1895, in Korea since 1910, Japan started an exploitative industrialization under its colonialist rule. Although factories were built, infrastructure was constructed, and external trade established with Japan, indigenous nationals were not given any real opportunities to learn and accumulate knowledge and experience for their own economic prosperity. There were neither sizable locally-owned industries nor a nationally-situated business class. When the Japanese surrendered, Taiwan and Korea were left more with national shame than industrial expertise. The newly-installed state took over shattered colonial assets

and, in fact, had to start industrialization from scratch (Fei, Ranis, and Kuo 1979; Oh 1994). As late industrializers, Taiwan and Korea faced the double challenge of overcoming internal backwardness and finding a niche in the already exhaustively explored world economic system.

Fifth, the weak and the strong were leveled up to some degree by World War II. Japan, like Taiwan and Korea, faced the same problem of reconstruction, vitalizing the war-crushed economy, and pursuing modernization. In Korea and Taiwan, due to the lack of domestic industries and capitalists, the state became a key player in economic development. In Japan, in spite of existing industrial facilities and a fully-fledged business class, the state was still the only agent capable of pulling the country out of the war shadow and pursuing a new course toward prosperity and dignity.

Sixth, late industrialization, weak civil society, and lack of an influential bourgeois class determined how Western forerunners interacted with East Asian states. Instead of supporting a particular social class, the United States counted on the nation state to achieve its geopolitical goals in East Asia. Large amounts of military aid, access to the US market, and the multiple opportunities of the Korean and Vietnam Wars all helped the East Asian states reinforce their leverage upon domestic groups and rivalries (Allen 1981; Bunge 1981; Gold 1986). In terms of timing and extensiveness the geopolitical force stimulated the East Asian states to become initiators or sponsors on the economic front.

Also of relevance is the fact that Japan, South Korea, and Taiwan are all resource-impoverished and population-pressured. Only through rational state planning and coordination of economic activities have they rapidly found a niche in the world economic system and achieved balanced economic growth and social development at home.

The Role of the State: Conditions

If historical and geopolitical forces have made East Asian states initiators and sponsors of development, it is Oriental culture and Western capitalism that enable them to play their role properly.

According to the Confucian hypothesis, a diligent work ethic, emphasis on education, respect for order and harmony, and group orientation are the core Oriental values behind the rise of Asian industrialized economies (Sonoda 1991). As far as the state is concerned, respect for order and harmony explains why statesmen are conscious of their responsibility and people are cooperative in the pursuit of an overall social well-being. Con-

fucian order is a hierarchy in which the Emperor gives order, courtiers handle state affairs, and people live a peaceful life following the Emperor and his courtiers. Harmony stems from a reciprocal relationship in which the ruler is concerned with the people and the ruled conscientiously serve their country. In other words, if the government is committed to economic progress, people should all contribute their energy and wisdom for a full collective support (Tai 1989).

Attachment to Western capitalism is a consciously pursued, geopolitically-secured policy for East Asian states. When Japan decided to pursue modernization, she was already aware of the necessity to learn from the West and determined to model herself on Western industrial institutions. After World War II, Japan, South Korea, and Taiwan all realized that they could only rebuild their respective territories with Western aid and sponsorship. Attachment to the West provided East Asian states with a direction, model, and goal to move forward, the direction being modernization via industrialization; the model being individual development, private right to own property, and free trade, market, and enterprise; and the goal being individual affluence, social prosperity, and national strength. In the 20th century, many newly-independent countries in the world had the same, even stronger determination than Japan, South Korea, and Taiwan to pursue modernization. However, since they followed Soviet or Chinese socialism, they finally fell into economic inefficiency, technological scarcity, political corruption, and social stagnation.

Second, advanced Western countries provided a chance of learning technological know-how and an inspiration to cultivate the capacity of innovation. In close alliance with the West, Japan, South Korea, and Taiwan sent their students, workers, and professionals to the West for career education, work-related training, and other learning opportunities. At the same time, Western engineers, experts, and advisers were invited to the three countries to help solve practical problems, direct production projects, and conduct training programs. As a result, industrial technologies are not only kept updated but are enabled to become innovative.

Third, attachment to the West ensures that economic missions are not jeopardized by political vicissitudes and changing strategies. In early years, through civil and military advisers as well as cash and program aid, the United States actually commanded Japanese decision-making and implementation processes, and wielded veto power over the economic lifeline of Taiwan. In Taiwan, American advisers, through consultations with Kuomintang (KMT) bureaucrats, were able to diffuse KMT's obsession to restore Mainland China and keep it on the economic development track. When export-oriented strategy was stretched beyond capacity and

the economy fell victim to its past success, it was American advice that directed it towards new development in petrochemicals, electrical equipment, advanced electronics, precision machine tools, and computer terminals and peripherals (Gold 1986).

Fourth, Western sponsors have made cash aid, investment, and markets available to the three countries. Taiwan and South Korea have been dependent upon their alliance with the West to launch into the Western consumer market and explore other markets in pursuit of their characteristic export-oriented development. Japan took advantage of Western demands for raw silk to pay for industrial and military equipments in its early pursuit of modernization. The lavishly given American aid was the key to its recovery after World War II. 'Special procurement' for the Korean War came in when 'aid' was drying up. In the middle 1950s, Japan was able to overcome its difficulties in the balance of payments and maintain its economic growth, largely due to the great expansion of the American market and world investment (Allen 1981). Even in the 1960s, an economically-stabilized Japan continued to benefit from its partnership with the United States through the Vietnam War.

It ought to be pointed out that American aid not only saved these countries from military expenditure but also helped them maintain autonomy from domestic forces such as landlords and comprador bourgeoisie. The three national states, in general, 'encountered no effective class opposition' in their pursuit of outward-looking industrialization (Koo 1987: 171).

The Role of the State: Processes

Modernization through capitalism and attachment to the West determine that East Asian states intervene in the economy in accordance with market forces. This distinguishes them from feudal and socialist regimes that either show no interest in economic affairs or grasp all economic power to the extreme of market stagnation.

Despite some scholars' assertions that Japan and its colonies operated a controlled economy until the US pressured post-war liberalization (Johnson 1982), 'Japan could at no time be considered to possess a planned economy in the modern sense' (Allen 1981: 171). Freedom of movement, enterprise, trade, communication, property acquisition, and entry into professions was declared as early as 1869 when the Meiji government was determined to seek Western-style prosperity. Afterwards, although economic growth had been associated with the expansionist policy, it was

propelled mainly by 'the newly-found freedom in the country's economic life', more specifically, by 'many alert individuals eager to seize opportunities' (Allen 1981: 170).

US-pressured liberalization in the 1950s and 60s brought about significant changes in the three Asian economies. Various nonmarket instruments were lifted. In South Korea, the currency was devalued in 1964 for a near-equilibrium exchange rate. Tariff-free imports were instituted for all export productions. Trade policies became, therefore, more market-oriented. In 1958 Taiwan began to liberalize imports for both export production and domestic use until import controls were dramatically relaxed in 1972. Japan came up with a master plan for trade liberalization in 1960. It set out to liberalize 80% of trade in three years and make foreign investment and technology imports market-oriented. Economic liberalization improves access to the capitalist world market and therefore made the three states more capable of influencing the economy in the strong current of international competition.

Unlike in socialist countries where the state monopolizes trade and production, the three East Asian governments are not greatly involved in direct business ownership or operation, even less so than some Western countries like France and Britain. In Taiwan, although the KMT regime was in charge of more than 40% of industrial output during the early 1950s, public enterprises declined to 20% of industrial value-added products after 1964 (Gold 1986). In South Korea, public enterprises comprised only 6.98% of gross domestic products in 1960. Despite subsequent increase of public investment in chemicals and heavy industry, public enterprises accounted for only 9.07% of GDP in 1972 (Amsden 1989). Limited public enterprise prevents the state from monopolizing production, setting prices, controlling the market, suppressing private initiatives, and making the economy suffer from dysfunction, corruption, and inefficiency.

Finally, an economy-wide measure of incentive rates shows that East Asian states act upon market forces. Despite strong protection applied to infant industries and high subsidies granted to major sectors, the incentive regime, measured by both effective protection rates (EPRs) and effective subsidy rates (ESRs), remains neutral or near-neutral in the three economies. No systematic bias is found against the market mechanism in state promotion of export and import-substitution among private sectors (Alam 1989).

It is obvious that the three states intervene in economic development with standard macroeconomic instruments. Market-compatible intervention can be observed in the following spheres.

Foreign Trade: The state policy to control imports, promote exports or import substitution, and keep the balance of payments is implemented through import licenses, export quotas, tax credits, and preferential loans. In South Korea, an import roster of prohibited items and items subject to automatic or prior approval is compiled. Imports are made conditional to exports through a minimum export performance standard. Export destinations, firms, industries, and products are officially designated and protected. Most saliently, the President presides over Monthly Export Promotion Meetings with trade and industry representatives. An Export Day is nationally celebrated for outstanding exporters and export achievements (Amsden 1989). Similarly, the Japanese Ministry of International Trade and Industry (MITI) maintained a foreign exchange budget to control imports until 1964. A special Export Conference was headed by the Prime Minister from 1954 to 1969 to set export targets, make export promotion policies, and award tax credits to outstanding exporters (Alam 1989).

Financial Markets: Interest rates, credit allocations, and loan supplies are handled differently in the three economies. Taiwan has adopted a policy of incentive rates since 1950. It curbed inflation and increased deposits. In banking, long-term loans were so restricted that the maturity of loans from commercial banks was limited to less than one year. In South Korea, credit allocation and foreign-loan guarantees are used to influence the economic behavior of large firms that, unlike the postwar Japanese conglomerates, have no financial affiliates abroad. The influence was particularly apparent during the country's expansion in heavy and chemical industries and the recent switch to 'skill-intensive' manufacturing. In Japan, the financial system is so organized that the government can monitor and modify investment and lending activities. The Ministry of Finance controls the Bank of Japan. The latter lends money and applies 'window guidance' to city banks that supply industrial finance to corporations. Moreover, MITI and the Ministry of Finance propose the annual Fiscal Investment and Loan Plan to allocate postal savings, postal life insurance, pension accounts, bond and loan receipts, and other funds to policy-implementation organizations such as the Japan Development Bank (JDB) and Export-Import Bank. Since JDB's participation in loan syndicates for high-risk projects represents an official guarantee against loss, its lending policies are habitually taken by city banks as a base to determine their lending priorities (Johnson 1982; Alam 1989).

Direct Foreign Investment (DFI): Compared to Latin America, foreign capital has played a less important role in East Asia. There used to be a debate on how East Asian states were able to control foreign capital, minimize extractive investment and thus avoid debts and dependency.

However, in their strategic transformation from import substitution to export orientation, Taiwan and South Korea both took important steps to lure foreign investors and achieve rapid growth by participating in world trade. In Taiwan, foreign capital, especially from overseas Chinese, played an important role in its Import Substitution Industrialization in the 1950s. Taiwan built the first East Asian Export Processing Zone (EPZ) in 1965. Foreign firms are provided not only with land, utilities, transport facilities, and buildings at subsidized rates, but also with duty-free entry of goods for re-export, control of union organizations, and other incentives. Another two EPZs went into operation in 1970 (Gold 1986). In the same year, South Korea opened its first EPZ in Masan. Another followed as did various sector-specific Export Industrial Estates. EPZs reflect the state's intention to utilize foreign investment to fuel development and explore the world market. South Korea had a gross external debt of \$43.1 billion in 1984, 53.16% of its GNP. Foreign-invested firms shared 31.4% of its total exports in 1974 and 18.3% in 1978 (Amsden 1989). In Taiwan, the share was 30% in 1975 (Deyo 1987).

While they attract foreign investment, the three states also take actions to maintain their decision-making autonomy and protect domestic markets. Despite periodic debt services, South Korea maintains its export growth in order to ward off massive rescheduling and structural adjustments as in many Latin American countries. The Korean government employs delicate tactics to screen DFI entries and regulate DFI operational contracts in the interests of domestic firms. For example, it compiles industries for DFI entry and requires foreign capital to fit its allocative priorities. Specifically, it controls the share of wholly-owned foreign subsidiaries, reviews joint venture contracts, defers DFI firms from competition with domestic enterprises, and keeps foreign banks out of local currency deposits, export financing, and real-estate ownership.

In Japan, entry of DFI was screened case by case before liberalization in the 1960s. Admissions to GATT, IMF, and OECD led to automatic approval of DFI to most industries in 1968. But the government still maintains control over technological contracts, it designates screening-needed industries, and applies MITI guidelines. There has never been a scaled inflow of foreign capitals. Even today, Japan is still accused by the West of its deep-rooted intractable trade protectionism.

Public Enterprises (PE): Public enterprises signal official priorities, transmit bureaucratic policies, and spearhead new or high-risk industries beyond the competence of the private sector. In Taiwan, the KMT government initiated ten major development projects in 1974 and another twelve in 1979. They not only fueled economic expansion in the 1970s but

also laid a firm foundation for continuous growth in the 1980-90s (Gold 1986). In South Korea, public investment averaged 30% between 1962 and 1973, making PEs a leading sector in the country's miraculous economic development (Amsden 1989).

In Japan, government participation in industrial activities is not limited to the involvement of public enterprises in strategic sectors such as electricity, shipbuilding, aircraft, and exports. Quasi-PEs or the so-called national policy companies also can help the government to support high-risk enterprises of official priority. Moreover, retired officials can serve on the board of directors in private enterprises and business owners or managers can sit in government commissions, thus providing 'consciousness of kinship' and 'administrative guidance' (Johnson 1982).

Price Controls: Late industrialization can easily push both the domestic market and foreign trade into disequilibrium. At home, a handful of early entrants may assume monopoly and oligopoly roles due to the weakness of consumers and producers. In the capitalist world system, late entry poses a challenge to national enterprises that are weak, inexperienced, and lacking in competence. As a result, the government has to get relative prices 'wrong' to cure market failures, protect infant industries, stimulate exports, and maintain equilibrium. In South Korea and Taiwan, price controls were initially used as an anti-inflation device. Afterwards, they were employed mainly to deal with excess profits in disequilibrium situations like monopolistic and oligopolistic markets (Jones and Sakong 1983; Alam 1989).

Price control has its own drawbacks. For instance, distortions of relative prices entrench some interest groups. Devaluations hurt import-dependent firms. Upward adjustment of interest rates discourages investment. It takes a strong state to maintain an overall healthy growth in the national economy.

The three states intervene in economic development through an array of fiscal and commercial instruments that are not only characteristic of a market economy but also rooted in the political, economic, and cultural soil of East Asian societies.

The Role of the State: Results

Given the role of the state in economic development, what credit does it merit?

Economic Growth: Economic growth in the three societies has been high compared to other societies at a similar level of development. Taiwan

scored an average GNP growth rate of 10.8% from 1963 to 1972 and still had a growth rate of 6.1% in 1992 (Lai and Chih 1994). South Korea still has high growth even today, having had an average GDP growth rate of 8.1% from 1989 to 1993 (Oh 1994). In Japan, the per capita GNP growth rate averaged 4.8% from 1965 to 1983, more than two points higher than the average of 2.5% for industrial market economies in the same period (Kuznets 1988).

Included in this rapid growth is the increase of export and manufacturing industries. The three economies have all experienced transformations from labor-intensive to capital- and knowledge-intensive, and consolidated their trading markets in the capitalist world system. In South Korea, the export growth rate averaged more than 30% during 1960-70s and remained as high as 8.8% from 1990 to 1993. Manufactured exports totaled only 39 million US dollars in 1963 but climbed to 77,908 million in 1993 (Oh 1994). In Taiwan, exports grew from less than 40,000 in 1986 to 81,470 million US dollars in 1992 (Lai and Chih 1994).

The continuous economic growth in the three societies owes to the state: (1) appropriate national planning and strategies adopted during economic transformation; (2) suitable incentives applied to protect infant industries, promote exports, and correct market distortions; (3) low labor costs maintained in the labor-intensive period in order to gain competitiveness in the world market; (4) low-profile labor movements; and (5) proper interest rates applied to accumulate development capital.

Social Stability: The three societies have remained stable during economic development. In Japan, the Liberal Democratic Party has been in power even since the Occupation Authority. Its conservative policies provide a political guarantee for continuing economic progress. In Taiwan, the KMT regime controlled the island completely. Local elites were liquidated earlier through the '2-28' Incident. The landed class was weakened later by land reform. In the 1950-60s no effective opposition existed to KMT's pursuit of economic development and political restoration of Mainland China. In the 1970s, KMT experienced its first change in political leadership. The second, which even led to democratic reform (Gold 1986), was successfully achieved in the 1980s.

South Korea is relatively volatile. The Park regime came into power by a coup and was terminated by an assassination. Then followed Chun, a General. After Chun came Roh who was also from the military. Only in 1993 did the Republic of Korea see its first civilian President, Kim. Before Kim, the political landscape was marked by frequent police confrontations with student protests and dissident movements. However, the three military regimes were all devoted to economic development and pursued a

consistent growth policy throughout the 1960s, 70s, and 80s. The economy, therefore, served as a common ground to unify people, channel private initiatives, and legitimize political actions.

What accounts for social stability in the three economies? Economic growth is obviously a factor. It is true that Japan's loss of a war, South Korea's competition with North Korea, and KMT's determination in Taiwan to restore Mainland China, motivate the respective state to build solidarities with the people. But if the economy did not grow and people lived in poverty, solidarity built upon political objectives would soon erode and civil disobedience eventually ensue. Economic growth brings confidence and material well-being to people and reinforces their solidarity with the state in the national commitment to economic development.

Also important is that the three states are conscientious about income distribution and social equality. Late development and rapid growth usually cause uneven sacrifice among different regions and groups. Since the state follows the Confucian notion of the mandates of Heaven for people's welfare, economic growth in the three societies seems translated into universal affluence. Land reform removed a traditional barrier for the rural poor. Dissolution of *Zaibatsu* in Japan and confiscation of property after the military coup in South Korea paved the way for lower-middle entrepreneurs. In Taiwan, it is national policy that all groups benefit from development. Taiwan saw a decrease of Gini coefficients from 0.558 in 1953 to 0.303 in 1980 (Kuznets 1988). Japan had a Gini value of 0.335 for 1967-72, lower than the 0.366 average of OECD countries in the same period. In 1980, the lowest quintile in Japan shared 8.7% of total household income, higher than the 6.3% average for all industrial countries (Kuznets 1988). South Korea experienced an increase of Gini from 0.332 in 1970 to 0.389 in 1980. By international standards, however, it is still a low-inequality country (Kuznets 1988).

Democratic Reform: The impact of economic development in Japan, South Korea, and Taiwan is remarkable. At the global level, Japan has become the second strongest economy in the world. Economic triumph has compensated for political retreat. Taiwan is known for its huge foreign reserves. South Korea has a large number of industrial giants. They both maintain considerable trading space in the world market. More importantly, economic strength gives both Taiwan and South Korea political advantages over their respective communist rivals.

Within their borders, economic growth has led to higher living standards, lower infant mortality, and higher life expectancy. More saliently, public education has improved. People are becoming aware of their individual rights. Interest-groups are developing. The middle-class is evolving.

Civil society is beginning to shake up the social-political power balance. The state and its authoritarian rule now face growing questions and resistance. In other words, the state has created a challenge to itself through economic development.

How does the state face this challenge? In Japan, the national political system has remained democratic since the Occupation Authority imposed a constitution to put sovereignty in the hands of the people. While LDP's continual control provides an uninterrupted pursuit of private economy, opposition also persists in developing different interests and checking the execution of national power. In the Diet, opposition parties are active in criticizing LDP policies and proposing alternatives. In 1993, a coalition government was first formed with a non-LDP Prime Minister. Trade unions, consumer groups, intellectuals, and mass media also play a significant role in curbing the unbridled exercise of political power, improving bureaucrats' decision-making styles, and promoting democratic practices in government and business.

In South Korea, despite political vicissitudes under Park, Chun, and Roh, democracy is taking root gradually as the economy develops. The democratic form of rule and basic human rights were early written in the Constitution. Opposition parties are represented in the National Assembly. Moreover, economic prosperity raises the general educational level and broadens opportunities for individual development. People are becoming concerned with national unity and democratic reform. They complain, demonstrate, and thereby contribute to the development of political tolerance and democratic institutions. In 1992, Koreans elected their first civilian President. Power was smoothly transferred from the military to the civilian administration in 1993. South Korea is now proud of being a successful example of economic development and democratic reform for other developing nations (Oh 1994).

In Taiwan, the KMT regime has been in power since it landed on the island. KMT was originally a Leninist party in favor of complete control over society. However, as the economy grew, with social stability provided by the tight control, Taiwanese civil society became gradually empowered. In the 70s, political messages from intellectuals, businessmen, and social activists began to be distributed among workers, peasants, and the petite bourgeoisie. The Chung-Li Incident occurred in 1977. Nonparty activities ensued rapidly, resulting in the formation of *Tangwai*. Using a network of liaison stations, *Tangwai* received about 25% of votes in local elections by the early 1980s (Gold 1986).

With *Tangwai* as its political base, the Democratic Progressive Party (DPP) was formed in 1986. It soon joined the power apparatus, turning the

authoritarian state into a multi-party system. In 1992, DPP won 32% of the seats in the Legislative Yuan. There are also DPP mayors and magistrates. In 1994, DPP even took over the most powerful mayorship of Taipei. Public election of the President was conducted smoothly in 1996. Democracy is beginning to take root in Taiwan.

In general, economic development brings about free trade, exposure to Western democracies, increased living standards, improved communication, awakened intellectuals, mature middle-class entrepreneurs, and better educated bureaucrats. It is these changes that drive political reform toward democracy.

The Role of the State: Prospects

The maturity of entrepreneurs raises the question of state intervention in economic activities. Given that Japan is a developed economy and South Korea and Taiwan are continuing their development drive, what can be expected of the state in relation to the economy?

At issue is the interaction between liberalization and intervention. Given the close relationship between the state and business and the Oriental culture of official supervision and merchant management, intervention will continue, but in new forms. First, the state needs to pull out of particular sectors and focus on the overall economic system. Compiling plans, providing information, predicting trends, making rules, and enforcing laws will become the main control measures in place of loan guarantee, credit allocation, risk-sharing, and procedural supervision. Preventing monopoly in enterprise systems, promoting fairness in market transactions, safeguarding consumer interests, protecting the environment, and running social welfare will become the main control activities instead of rearing industries, building production complexes, distributing resources, and achieving economies of scale.

In order to effectively manage the economic system, the state needs to take charge of a supporting network including infrastructure, scientific research, technological development, employment training, and the information system. Infrastructure has been periodically expanded by private-sector growth. This demonstrates that the state has to create a physical environment to accommodate private achievements and sustain economic development. Moreover, as small and medium-sized enterprises are preoccupied with routine operations and few corporate giants are willing to support a professional staff for long-term projects, the state also needs to maintain a 'soft' infrastructure of scientific research and market study for

the continual invention of new products, competitive in terms of high efficiency, low energy consumption, and high consumer satisfaction.

The state must also make tough decisions regarding the phasing-out of 'sun-setting' sectors and the phasing-in of new industries. The phasing-in of new industrial products under developed conditions differs from the introduction of basic industries in poor economies. There are experienced entrepreneurs to count on and sufficient funds to move forward. However, resettling employees and equipment from old sectors, exploring new markets, and training staff for new products can be risky, controversial, and difficult. The state cannot just let market forces lead the uncompetitive to bankruptcy. Nor can it simply dump money to make high-tech or highly-competitive productions come into being. Instead it has to remain behind the scenes and apply incentives skillfully.

This new style of intervention implies liberalization. In fact, liberalization becomes inevitable with development. Japan is the world's second largest economy. Membership in world economic organizations obliges it to observe capitalist rules and ethics in a range of games. Protectionist policy is criticized. Pressure from Western partners is building up. Japan needs to open its domestic market and balance its external policies with internal measures. South Korea and Taiwan are squeezing late into the world system, but they see the need to tear down man-made barriers to market rationality.

Human resources are changing as the three economies develop. Individuals are becoming independent. Entrepreneurs, with access to various market situations and information services, know where to explore, what to choose, and how to accomplish it. Bureaucrats with liberal education prefer policy consultations and software services to teaching entrepreneurs what and how to do with their businesses. The new relationships between government officials and business communities will also result in institutional changes.

Development is bringing about business saturation in all sectors in the three economies. In view of the numerous private businesses, the state simply cannot favor any particular sector. Also, a considerable number of corporate giants have expanded their businesses in the global market. This is a strong argument in favor of self-decision and -management. The state obviously needs to be restrained and intervenes only with general measures.

If integration into the world system, changes in human resources, and the growing power of businesses pressure the state to liberalize, what can be expected of the liberalization process? Will the state and its relationship with the business community change from 'plan rationality', 'organization-

oriented systems', and 'purpose-governed state' to 'market rationality', 'market-oriented system,' and 'rule-governed state' (Samuels 1987)?

Economically, man-made distortions will be replaced with market forces. As early as 1982, South Korean President Chun called for 'institutional reforms to strengthen the functioning of the market mechanism' (Kuznets 1988: 34). This reflects state recognition that economic rationality and efficiency are stimulated by market forces. It is a belief shared by both bureaucrats and business communities that a market-oriented system, a rule-governed state, and the rationality of the market are the ways and means toward economic well-being and national strength.

As far as market rationality is concerned, a rule-governed state is expected to concern itself more with the form than the substance of the economy. Economic planning and industrial policy will continue to provide general guidelines for economic activities. However, they will no longer be implemented with government inputs. Competition, fair treatment of businesses, protection of consumer interests, and equitable distribution of social wealth will be pursued only through widely-applicable policies and laws. From being initiator, participant, or backstage manipulator, the state will become a simple regulatory authority.

Switch from plan-rationality to market-rationality in the economic sphere may spark off political change. The developmental state used to monopolize political power, suppress dissidence, and wield a strong hand in civil affairs. Since it was devoted to economic growth, it was characterized as a 'soft' authoritarian regime. Now, with a population that is conscious of individual rights and a middle class that presses for political participation, 'soft' authoritarianism has to give way to 'hard' democracy in which different interests are free to develop, vie for power, and check each other. Although a democratic form of government is evolving in the three societies, feudal ideas, patriarchal rules, and discrimination against women and newcomers are still part of the culture and collective conscience. Here, Japan is well ahead. South Korea and Taiwan are still experiencing the pangs of their endeavors towards a more democratic way of life and government. However, 'hard' democracy will eventually take root in all three societies.

Given the long solidarity between business and the state, liberalization obviously cannot replace intervention altogether, but can only change the way it acts upon the economy. Even with a liberalized state, it is still hard to predict that Japan, South Korea, and Taiwan will not put aside market rationality in order to seize vital opportunities or fight tough challenges in the world market.

Conclusion

While it plays the role of sponsor, the state itself is not a base, condition, or reason for economic development in the three societies. It is geopolitical dynamics, the global trading environment, individual initiatives, conscientious leadership, cultural heritage, social responsibility, and national solidarity that combine to make the East Asian economic miracle. The role of the state is to seize chances, coordinate different forces, and translate them into a common good of economic prosperity.

What can be learned from Japan, South Korea and Taiwan as regards the role of the state in economic development? As far as the three economies themselves are concerned, while state sponsorship of the economy is a valuable tradition to cherish, they need to explore new forms of government intervention in economic affairs that do not interfere with market forces and create business dependency. To developed Western economies based upon market rationality, participation of East Asian states in economic activities is a reminder that the state ought to be concerned with the economy, its operation and well-being. It is not advisable for the state to remain aloof and be involved as a salvation army only when the entire economy falls into dysfunction, crisis, or depression.

To all developing countries that are often plagued with poverty and lack of resources and opportunities, the successful experience of the three Asian economies serves as a warning that in the initial period of development, there should exist a strong state authority that is able to unify different interests, motivate people, and concentrate limited resources in times of economic crisis. A weak state, even in a democratic form, could lead an economically undeveloped country to a disarray of contradicting interests, perpetual squabbling, and anomie, thereby preventing the country from concentrating its energy towards overcoming economic underdevelopment.

A distinction must be made between socialist and capitalist countries with regard to state sponsorship of the economy in the initial stages of development. In developing capitalist countries, the disunity and ineptitude of a weak state are often to blame for economic failure. The state should therefore be strengthened. In developing socialist countries, however, an ideologically-misguided state takes command of the economy and is primarily responsible for economic corruption, inefficiency, and stagnation. The experience of Japan, South Korea, and Taiwan obviously does not suggest that the planned economy of socialist states be continued. But it serves as a measure of how much state control over and participation in economic activities may be retained, when a socialist economy is trans-

formed into a market economy. In other words, economic reform in socialist countries should not be radicalized as a total dismantling of the command system, a thorough privatization of public business, and a complete retreat of the state from the economic sphere. Instead, it should be conducted in a phased way that avoids drastic impacts on economic operations.

To sum up, economic success and all the agents for that success in Japan, South Korea, and Taiwan occur in a historically specific context. The East Asian experiences may help other countries and the three economies themselves cope with their respective challenges now and in the future. But they are by no means a panacea applicable in every situation.

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