

Evaluation of Economic Transition Outcomes of CLMV Countries in Southeast Asia and Its Implications for North Korea

: Development of New Transition Indicators and Its Application

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I. Introduction

The changes in the North Korean economy after Kim Jong-Un's inauguration in December 2011 are largely increasing in magnitude. The most notable example was seen in April 2018, when it switched its center of attention from the previous two-pronged strategy of pursuing both economic development and nuclear capabilities, to solely focusing on establishing a socialist economy. It may be safe to assume that this signals North Korea's economic transition. Of course, it appears to be regressing towards a central economy system as toughened sanctions since 2018 led the authorities in the North to stiffen the control over the economy. However, this is believed to be a temporary action due to international sanctions and COVID-19.

The most recent cases of economic transition can be found in Southeast Asia, namely Cambodia, Lao PDR, Myanmar, and Vietnam, also grouped as "CLMV" countries. Their economic transitions are proceeding gradually, encouraged to emulate the economic transition paths of China or Europe and the US and are highly export-oriented.

Thinking about which form of economic transition North Korea should choose once it fully opens its economy remains questionable. However, we believe that the closest path it would choose, considering its geographical proximity and familiarity with Chinese influence, would resemble one of the CLMV's. Therefore, the history of CLMV's economic transition would shed a light on the potential roadmap of North Korea's economic transition.

The purpose of this study is to evaluate the degree of economic transition in Southeast Asian countries so far. The economic transition indicators are designed specifically to assess the level of economic transition throughout the observed period. They serve as a yardstick of measuring how close CLMV countries are to the market economies in Europe and US or Chinese state capitalism. Then lessons for North Korea's future economic transition are drawn from the quantitative analysis of CLMV's economic transition.

II. Methodology

Transition can be classified into economic and political transitions. This study covers the former only. Economic transition can be divided into two prototypes; one is the market economy epitomized by the United States, and the other is state capitalistic transition (or East Asian transition), represented by China. Due to page constraints, we limit our scope to the market economy, which is well-represented by the Washington Consensus.

The Washington Consensus is the ideological framework of market economic transition first developed by John Williamson in the 1990s. It focuses more on the institutionalization of the market economy rather than producing outcomes from this. The International Monetary Fund (IMF) and the World Bank have suggested reformation of economies in developing nations on the basis of the Washington Consensus.

The most representative measures to evaluate the degree of economic transition are transition indicators developed by the European Bank for Reconstruction and Development (EBRD). This includes transition indicators that are tailored to evaluate the level of transition in Eastern Europe and Baltic countries.

First developed in 1997, these indicators have gone through numerous restructurings. Some of the sectors were subdivided and new sectors for evaluation added in 2010. The concept of inclusive growth was first introduced in 2013, aiming for balanced growth and providing equal opportunities for all market participants. This is represented in the components of gender equality, opportunities for the youth, and regional disparity. Six other sectors were added in 2017 to reflect the latest trend of efforts to establish a sustainable market economy.

This study proceeded in two stages of designing transition indicators suited to evaluate the degree of CLMV's economic transition. First, we rearranged all the categories and sectors between 1997 and 2010 (See Table 1). Inclusive growth and sustainable growth components are excluded as the observed period of Southeast Asia was not a time when CLMVs focus was on any of these components. The EBRD indicators in the observed period show a clear map of a transition economy whether its institutional transition to market economy is well established.

Table 1. Specific sectors used by EBRD for evaluation of transition outcomes since 2010

Category	Sector
Corporate (3)	Agribusiness, General industry, Real Estate
Energy (3)	Electric power, Natural Resource, Sustainable Energy
Infrastructure (5)	Railways, roads, urban transport, water and wastewater, telecommunications
Financial Institutions (5)	Banking, Insurance/other financial services, capital markets, private equity, MSME finance

Source: EBRD (2010), p. 5.

Table 2. Policy targets and corresponding provisions of the Washington Consensus

Policy target	Washington Consensus
I. Macroeconomic stability	<ul style="list-style-type: none"> • Fiscal discipline • Independency of central banks and inflation targeting
II. Reorientation of public expenditure and income redistribution	<ul style="list-style-type: none"> • Tax reform • Social safety nets • Poverty reduction • Reorientation of public expenditures
III. Free and competitive market economy	<ul style="list-style-type: none"> • Financial liberalization • Deregulation • Prudent capital-account opening
IV. Trade liberalization	<ul style="list-style-type: none"> • Competitive and unified exchange rate • Trade liberalization • Upholding WTO agreements
V. Raising efficiency and profitability of the enterprises	<ul style="list-style-type: none"> • Privatization • Raising efficiency and profitability of the enterprises • Anti-corruption
VI. Legal framework	<ul style="list-style-type: none"> • Secure property rights
VII. Financial codes and standards	<ul style="list-style-type: none"> • Financial regulation and standards • Non-intermediate exchange rate regimes
VIII. Raising labor productivity	<ul style="list-style-type: none"> • Labor market flexibility
IX. Stable inflow of foreign direct investment	<ul style="list-style-type: none"> • Openness to foreign direct investment

Source: Author's classification.

Next, we matched the major components of the Washington Consensus to its policy targets (Table 2). This sheds a light on what policy targets countries in transition are focusing on.

There are 84 reconstructed transition indicators out of original transitional indicators from the EBRD (1997–2010) and corresponding components of the Washington Consensus. The specifics of criteria for evaluation are not introduced here due to the limited number of pages. Please refer to Choi et al. (2020) “Evaluation of Transitional Outcomes of CLMV countries and its Implications for North Korea.”

Each and every sector of reconstructed transition indicators are given with scores that range

between 1 and 5 according to the corresponding criteria. For instance, when it comes to privatization, the value of 1 is given to a case where there are only state-owned enterprises and no institutional framework for privatization. A score of 2 is given where there is an institutional or legal framework for privatization, yet the extent of pursuing it is limited. When the private sector’s share of the total asset of a firm ranges between 25 and 50%, then 3 is given. If this share exceeds 50 but is lower than 75%, 4 is given and if it is above 75%, then a perfect score of 5 is granted. There are 84 sectors evaluated in total and we averaged the scores according to the sector. The interpretation of the average scores is presented in Table 3.

Table 3. Interpretation of overall scores from evaluation of transitional outcomes

Scores (α)	Interpretation
$a < 1$	<ul style="list-style-type: none"> There is no policy target in regards to transition in the economic sector.
$1 \leq a < 1.5$	<ul style="list-style-type: none"> There is a policy target in the economic sector and a plan is established to meet the target accordingly.
$1.5 \leq a < 2$	<ul style="list-style-type: none"> There have been attempts to transition to a market economy, yet no concrete outcomes are spotted.
$2 \leq a < 3$	<ul style="list-style-type: none"> Progress has been made in the economy and certain indicators show the economy is growing.
$3 \leq a < 3.5$	<ul style="list-style-type: none"> Significant progress has been made in the economic sector and a framework for the market economy has been established. Still in need of laying groundwork for economies of scale and sustainable economic growth
$3.5 \leq a < 4$	<ul style="list-style-type: none"> Transition in the economic sector has reached close to world average levels and a firm and stable framework has been established for the market economy. There is no substantial barrier hindering a free competitive market economy after joining WTO. (There might be some discord within the country in terms of domestic firms sustaining losses following trade liberalization.)
$4 \leq a$	<ul style="list-style-type: none"> Legal and institutional framework is well-established like those in middle-income or advanced countries.

Source: Author’s construction.

III. Results

Here follows a brief summary of how the transition took place in the respective CLMV countries, provided before interpretation of the evaluation outcomes.

Cambodia declared its transition into a market economy after ending a decade-long war with Vietnam under the Paris Peace Accords, which was signed in 1991 and came into effect in 1993 along with the first democratic election. This can be marked as the 1st stage of transition between 1989 and 1992. External relations were normalized after the United States lifted its trade embargo in 1992. This marks the end of the 1st stage and opens the 2nd stage of transition, which is between 1993 and 2003. After the proclamation to introduce a market economy, the country started restructuring state-owned enterprises, enacted the foreign investment act as part of policies to open its economy and legislated the Banking Act in the same year. When Cambodia joined the World Trade Organization (WTO) in 2004, its transition to a market economy was deemed near complete.

The Revolutionary Party declared the introduction of the New Economic Mechanism, a market-oriented policy, at the 4th Party Congress which took place in 1986. The 1st stage of transition of Lao PDR can be segmented into the time period between 1986 and 1990. The governing party legalized the market economy when it established the constitution of the nation in 1991. That marks the start of the 2nd stage of transition of Lao PDR which lasted until 1996.

As it initiated negotiations to join the WTO in 1997, the 3rd stage of transition began. The 4th and final stage of transition started in 2013 after joining the WTO as a full member.

Myanmar declared its transition to a market economy in 1988 but only began large-scale transition efforts in 2011. The 1st stage of transition in Myanmar took longer than any other CLV country, lasting until 2007. The 2nd stage of transition began in 2008, with the inauguration of a democratic administration and adoption of the Constitution of Myanmar. The 3rd stage commenced in 2011 with the forming of the first civilian government, which established a comprehensive national development plan and enacted the Special Economic Zone Law. Since 2016, the 4th and final stage of transition has been proceeding with the normalization of relations with the US.

Vietnam's transition took place in five stages. The 1st stage began in 1986, launched with the proclamation of the Doi Moi policy. The 2nd stage began in 1991 and the administration amended the nation's constitution the following year when relevant laws were renewed to ensure the establishment of a market economy. The 3rd stage commenced in 1996 when the State Securities Commission was established and transition measures were implemented in the finance sector. The 4th stage was initiated when the transition of Vietnam was accelerated in preparation of joining the WTO in 2001. The final stage can be seen as beginning in 2006 as it joined the WTO this year.

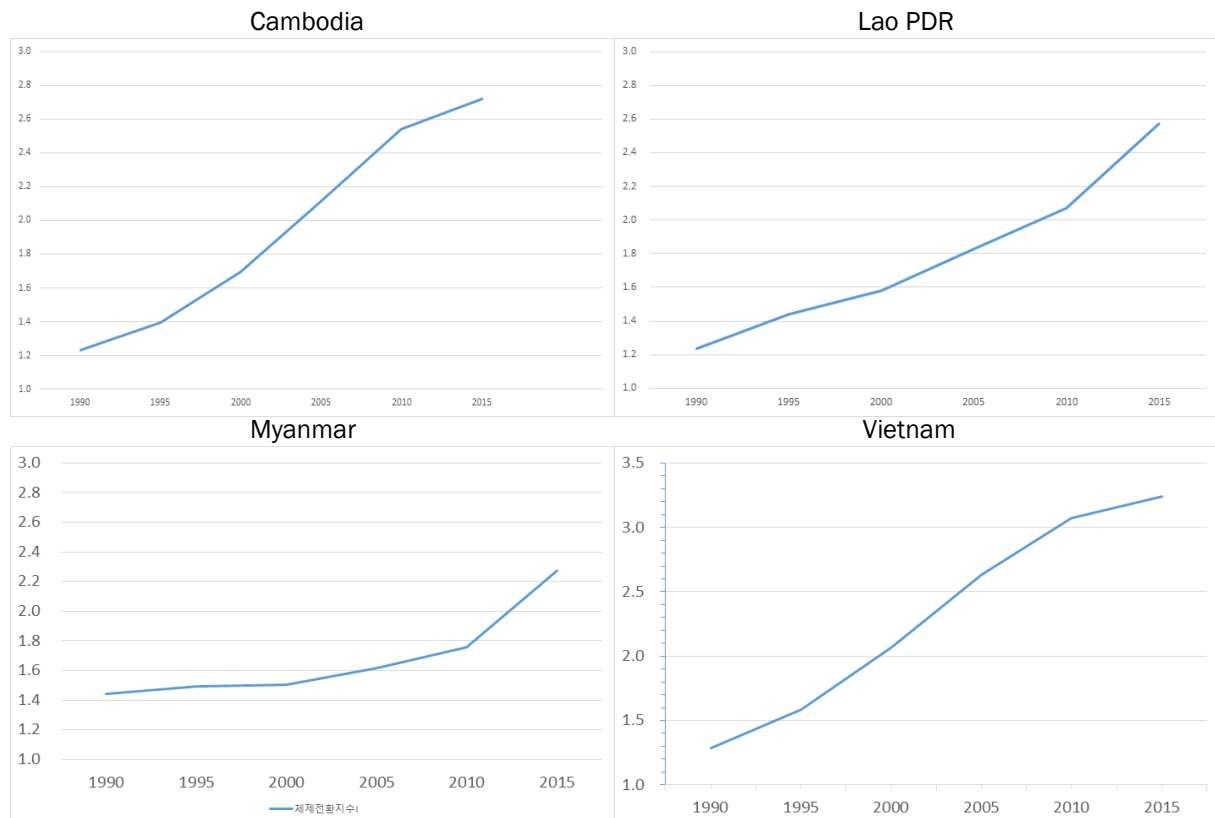
Figure 1 displays the transition rate of CLMV countries. Vietnam's transition proceeded at the most expeditious rate, followed by Cambodia, Lao PDR, and Myanmar.

Now if we break this down according to policy targets included in the Washington Consensus, the situation becomes far clearer in exploring which sector developed the most up to now. All four countries focused on trade liberalization and attracting foreign capital, establishing a free and competitive market economy and macroeconomic stability. They all marked around 4 in all four policy targets. The meaning of the score 4 is that their economies approached the

world average and a market economy system had been securely established.

Yet not all of the sectors are well developed. Legal frameworks, reorientation of public expenditures and income redistribution, raising efficiency and profitability of enterprises, raising labor productivity are policy targets where performance in these nations remains relatively poor. Most of these components were marked at around 3 or below. This can be interpreted as “some progress in transition with moderate success.” There is an observable transitional outcome in the countries, but it is difficult to say a market-economic framework has been well established.

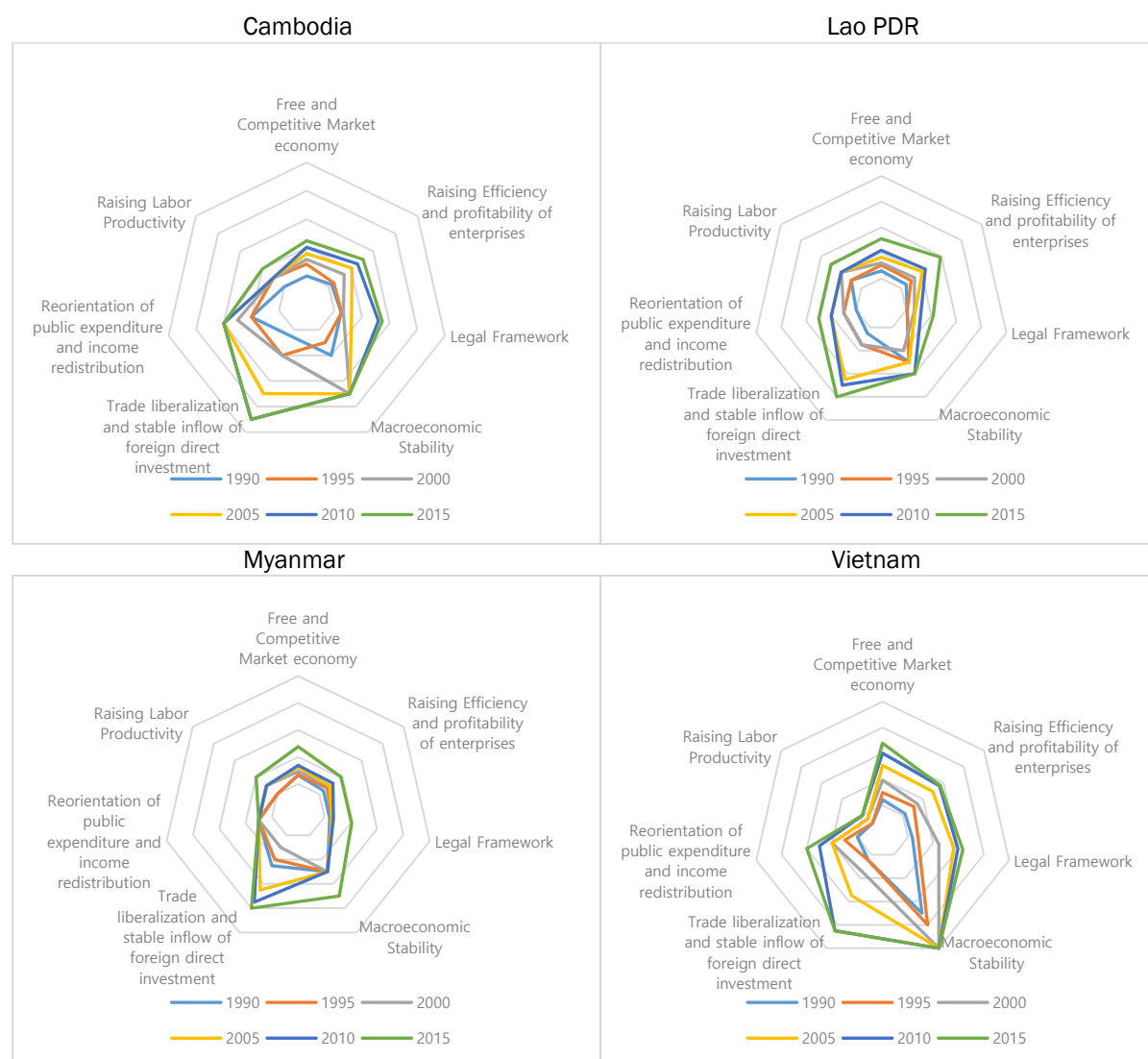
Figure 1. Transition Rates of CLMV



Source: Author's construction.

Figure 2. Transition rates according to policy targets

(Clockwise: Free and competitive market economy, Raising efficiency and profitability of enterprises, legal framework, macroeconomic stability, trade liberalization and stable inflow of foreign direct investment, reorientation of public expenditure and income redistribution, raising labor productivity)



Source: Author's construction.

IV. Conclusion

The economic transition of CLMV nations took place over the long haul and can be best described as export- and foreign direct investment-oriented. Whether this kind of transition

led to economic growth or other tangible outcomes can be identified by categorizing the CLMV countries. On one hand we have Vietnam and Lao PDR, whose economic transition did lead to economic growth, while another outcome is seen in Cambodia and Myanmar,

which did not enjoy the fruits of this transition. This is an intriguing phenomenon as all three of Cambodia, Myanmar and Lao PDR are classified as least developed countries (LDC), yet Lao PDR is the only whose transition to a market economy actually resulted in economic growth.

There are a couple of lessons to be learned from these examples of transition in CLMV countries. One is the need to target a certain area first in the process of economic transition rather than aiming for transition in every sector equally. If an administration wishes to achieve fast economic growth and development, it is best to place export- and foreign direct investment-oriented policies at the top of the list and set aside the rest of related policies for the time being.

The other is that it is crucial to maintain political stability within the nation and a stable bilateral relationship with the United States, which was not covered in detail in this study. Among the CLMV countries, Vietnam and Lao PDR were able to establish a stable bilateral relationship with the US, stabilized their internal political affairs, and achieved economic development. On the other hand, Myanmar and Cambodia suffered from civil wars and population outflow, and have not been able to realize concrete economic outcomes.

Last but not least, it is safe to assume that it would take at least 10 to 15 years for North Korea to attract foreign capital and enterprises to generate profits, considering the CLMV's transition history.

The research outcomes of this study will be the very foundation to set the direction of North Korea's transition and prioritize agendas at each stage of transition. This study differentiates itself from previous studies of transition as it evaluated Cambodia, Lao PDR, Myanmar and Vietnam to develop an analytic framework based on quantitative measures. In addition, this study made a novel attempt to investigate transition of CLMV countries in Southeast Asia from the perspective of state capitalism shaped by China. This would contribute to extending the horizon of studies of transition economies.

In a follow-up study, we would like to evaluate the degree of transition of North Korea by making use of the newly developed transition indicators from this study. A comparison of evaluation results gained from North Korea and CLMV countries would present a broad picture of where North Korea stands in terms of transition stages and offer a clue to build a roadmap of transition that would yield solid economic outcomes. **KIEP**

References

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