2014 KIEP Visiting Fellows Program

Edited by JEONG Hyung-Gon

Korea Institute for International Economic Policy

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The KIEP Visiting Fellows Program is published with the aim of promoting discussions among researchers, and to remember the outstanding achievements by the visiting fellows who came to KIEP.

KOREA INSTITUTE FOR
INTERNATIONAL ECONOMIC POLICY (KIEP)
370 Sicheong-daero, Sejong-Si 339-705, Korea
Tel: (8244) 414-1042 Fax: (8244) 414-1043
URL: http://www.kiep.go.kr

LEE Il Houng, *President*

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In 2009, Korea Institute for International Economic Policy (KIEP) launched "Visiting Fellows Program (VFP)" with the view of advancing cross-border exchanges of knowledge, information, insights and expertise.

Since its inception, the VFP has demonstrated that sharing thoughts and ideas through face-to-face contacts and dialogue works as a catalyst for enhancing mutual understanding among scholars and professionals with diverse background.

By successfully implementing the VFP for the past 7 years, KIEP has been motivated to assume the role as a hub for international economic research in the region. As a host of the program, KIEP has many mandates. One of those tasks is to let more people know what has been accomplished through the program and how valuable it is.

In an effort to do so, KIEP has published series of research every year. This volume, the 6th of its series, contains seven research papers contributed by 2014 Visiting Fellows.

Publication owes many debts. Here I acknowledge just a few of them. First of all, I must express my deepest gratitude to the 2014 visiting fellows for their outstanding performances. My special thanks also goes to Ms. Juneyoung Choi, Ms. Mi Jung Woo and Ms. Jeewoon Rim from the Outreach Team who worked very hard for the publication of this volume.

JEONG Hyung-Gon
Senior Research Fellow
Korea Institute for International Economic Policy

Notes on the Contributors

Dr. Ibrohim Umarov is a senior researcher at the Institute of Forecasting and Macroeconomic Research in Uzebekistan. He received M.A. at Tashkent State Institute of Oriental Studies. He was a visiting fellow at KIEP in March, 2014.

Dr. Khalid Ahmed is an assistant professor at the Sukkur Institute of Business Administration in Pakistan. He received Ph.D. at Johns Hopkins University, USA. He was a visiting fellow at KIEP in April, 2014.

Dr. Sudhakar Yedla is a professor of Environmental Policy at the Indira Gandhi Institute of Development Research (IGIDR), Mumbai, India. He received Ph.D. in Civil and Environmental Engineering at the Indian Institute of Technology (IIT), Kharagpur, India, and was a Post Doc at Asian Institute of Technology (AIT), Thailand and got diploma in International Enviornmental Law from the United Nations Institute for Training and Research (UNITAR), Switzerland. He participated in the KIEP Visiting Fellows Program from May 9th to June 7th in 2014.

Dr. Mozafari Mohammad Hassan is a senior researcher at the Islamic Culture and Relations Organization. He received Ph.D. in Law from JMI, the Central University in Delhi, India. He participated in the KIEP Visiting Fellows Program from May 19th to June 17th in 2014.

Dr. Ni Jinli is an associate researcher at the Jilin Province of Academy of Social Sciences. She has a Masters degree in Rural Technical and Vocational Education from Jilin Agricultural University. She was a visiting fellow at KIEP from May 20th to June 18th in 2014.

Dr. Murat Ali Yulek is a professor at the Istanbul Ticaret University. He has Ph.D. in Economics from Bilkent University and Masters of Business Administration from Yale University. He visited KIEP from August 25th to September 5th in 2014.

Dr. Moaness Tahoun is a First Secretary at the Egyptian Commercial Service in Cairo, Egypt. He has a Masters of Economics from the College of Europe in Bruges, Belgium. He was a visiting fellow at KIEP in September, 2014.

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Diversification of Bilateral Foreign Economic Relations between Uzbekistan and Korea

Ibrohim Umarov[1)]

I. Introduction

Results of development around the world in the late twentieth and early twenty-first century show that despite the considerable efforts of the international community, the economic gap between the advanced and developing countries of the world is not decreasing, but actually continues to increase. One of the few exceptions to this global economic trend is the Republic of Korea. Over the past half-century, Korea went from an underdeveloped, poor agricultural country to a modern industrialized country, and now rivals the most economically advanced countries of the world in many areas. Korea's per capita GDP in 1960 was 5.4% of U.S. GDP, but this ratio had changed dramatically by 2012, with the figure reaching 44% .[2)]

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1) Senior Economist, Institute of forecasting and macroeconomic research, Cabinet of Ministers of the Republic of Uzbekistan.

2) World Bank development indicators.

It is important to note that these and other impressive achievements were secured amidst complex internal and external conditions of development. Korea did not have any significant reserves of minerals. In addition, the division of the Korean Peninsula after the liberation of Korea (1945) into northern and southern parts caused political instability. The incredibly destructive Korean War (1950-53) resulted in a South Korea that was trapped in poverty, hyperinflation and chronically high unemployment. That is why; the experience of the Korean economy in the modern era is the undoubtedly an important point of reference for all developing countries.

Korea's experience is also important for Uzbekistan, due to the fact that many structural and qualitative indicators of the Korean economy 20-30 years ago bears a close resemblance to the Uzbek economy. As in modern Uzbekistan, in Korea, the state played an important role in defining development priorities, allocation of resources, and provided direct support to individual economic sectors. Subsequently, the role of the state and the extent of its direct intervention in the economy began to decline, and the role of market mechanisms increased.

Measures to reform and modernize the economy played a significant role in this, as well as flexible and effective strategy for development. As a result, in the last three decades, Korea managed to achieve significant progress in improving the efficiency of production, the development of high-tech and knowledge-intensive sectors of the economy, and increasing its competitiveness. In modern conditions, these factors are becoming the keys to success in economic development. In this regard, the experience of the creation of a modern Korean economy and its relationship to the development of the national economy of Uzbekistan is valuable for accelerating the economic development of our country, especially in the difficult conditions of globalization of the world economy.

Among the countries with which Uzbekistan is actively developing mutually beneficial partnership, the Republic of Korea occupies a special place. The Republic of Korea is one of the first countries to establish diplomatic relations with Uzbekistan, on 29 January 1992. In April 1994, the Korean embassy was opened in the Uzbek capital of Tashkent, and work on the Uzbek diplomatic mission in Seoul began in December 1995.

Despite the enormous geographical distance between them, both countries have strong incentives to cooperate with each other on a wide range of issues. Despite the fact that there are many areas that remain untapped in the dynamics and structure of the Uzbek-Korean economic cooperation, it is far outstripped by the volume and diversity of opportunities the relationship presents for the national economies of both countries.

Since the second half of the 1990s, South Korea has assumed a leading position among foreign investors and partners of Uzbekistan. As the President of Uzbekistan Islam Karimov noted, “The Republic of Korea is one of the most important trade and economic partners of Uzbekistan. This is something we believe to be very important and we express our willingness to deepen our mutually beneficial relationship”.[3] The Republic of Korea sees in Uzbekistan as an “indicator” state in Central Asia, that largely determines the future of the entire region. Through Uzbekistan, the Republic of Korea aims to make further advances into the market not only in the Central Asia region but also the CIS in general.

II. Analysis of Economic Development of Uzbekistan

Despite the anti-crisis program and the measures taken to counter the aftereffects of global financial and economic crisis and its impact in many countries of the world the situation is, unfortunately, not improving, and is actually deteriorating in some cases. The problems of public debt and deficits of national budgets remain is most leading countries of the world, along with stagnation of production in the real economy, the continuing decline in global demand and persistently high

3) The Korea Post// 2003 y, #3, See the page 67.

unemployment that lead to deepening social tensions.

During such difficult and unpleasant processes as noted by our President Islam Karimov–"central place in our program for 2013 and the near-term should make it a priority to accelerate and increase the scale of modernization in general; the technical and technological modernization of the economy and its leading industries; and diversification of production".[4)]

Many countries at the initial stage of its development and market reforms combined the export oriented and import-substitution strategies of industrialization. Uzbekistan did the same. To implement this strategy, the state widely utilized such levers of macroeconomic regulation as the overvaluation of the national currency, subsidies to industries, the licensing of export and import operations, the establishment of sufficiently high import duties and other measures to prioritize protection of domestic producers

Import substitution of manufactured goods is one of the ways to achieve economic independence for the young state. The need for such a strategy was dictated by the lack of development of manufacturing (from the standpoint of competitiveness on the world market), as well as the specific geographical situation of the country. Uzbekistan is one of the two countries of the world, for which access to the sea passes through at least two states, which gives rise to significant transport costs, especially when transporting products of extractive industries and products with a low degree of processing.

In general, the strategy thus chosen by Uzbekistan is justified. In analyzing the dynamics of Uzbekistan's foreign trade (see Figure 1) it should be noted that the growth of foreign trade of Uzbekistan took place (especially prior to 1995) against the background of general decline in production and domestic demand. This was largely due to the reorientation of domestic consumption toward external products, a natural condition when a commodity is predominant in exports.

4) Islam Karimov, "Our main goal is resolutely to pursue the path of large-scale reforms and modernization of the country." //-T.: Uzbekistan, 2013 y.

Thus, according to the international classification and assessment of the UNCTAD international trade center,[5] commodities accounted for 78% of total exports in 1996, while the figures were 7% for processed raw materials and only 1% for labor-intensive products, respectively, despite the considerable labor surplus in the national economy.

In the years that immediately followed independence, there were great changes in the structure and geographical direction of Uzbekistan's foreign trade. For the period 1994-1996, the share of exports (from 67.6 to 22.9%) and imports (from 53.3 to 32.1%) dropped significantly in trade with the CIS countries, and exports fell in terms of absolute value, trade with the rest of the world increased significantly, both in absolute terms and in business terms-from 38.8 to 72.4%. Export value growth of Uzbekistan in 1993-1995 was based mainly on favorable growth trends in world prices, for example, of such products including cotton, gold, base metals.

In spite of this, new export items actually appeared such as automobiles and electronics. It should be noted that such commodity groups as food, instruments and apparatus, machinery and mechanical appliances and parts, electrical machinery and equipment, energy continue to be exported to the CIS countries.[6]

Later, with the deepening of processes of economic liberalization; with improvements in its structure, market development and related infrastructure; the role of foreign trade and its efficiency improved significantly.

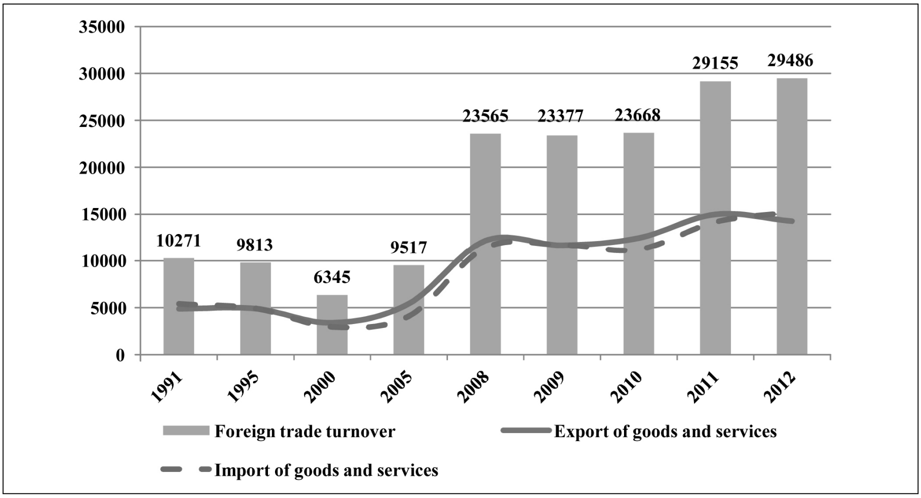
In general, exports increased during this period by nearly threefold (see Figure 1). Such growth was possible not only because of favorable world prices for major export products of Uzbekistan, but was also due to increases in the share of finished products in the composition of export. More than 80% of exports are currently accounted for by industry, with about 11% by export of services.

5) National trade performance and international demand in the Central Asian Republics prepared by the Research and Analyst Unit, International Trade Center UNCTAD/WTO//4th SPF-Issyk-Kul International Forum: “Central Asian: Economics Development in the Era of Globalization”/ Tashkent, 1-2 October 1998, page 16.

6) Uzbekistan: ten years on ways to reform the market economy. The Institute of Economics under Academy of science. Tashkent, “Uzbekistan”, 2001.

Figure 1. Dynamics of Foreign Trade Turnover of the Republic of Uzbekistan

(Million US Dollars)



Source: World Bank.

The Republic of Uzbekistan trades with more than 170 countries. The country's trade expanded to countries that are not included in the CIS. The main trade partners of Uzbekistan now include Russia, China, Kazakhstan, Republic of Korea, Turkey, Ukraine, Germany, France, etc.

Uzbek exports increased significantly in 2012 by 11.6 percent, with concomitant improvements in structure and quality of the exported products. As a result, non-primary finished goods comprised more than 70 percent of exports. The positive balance of foreign trade turnover exceeded 1.12 billion US dollars.[7]

In 2013, the gross domestic product of Uzbekistan grew by 8 percent, the volume of industrial production increased by 8.8 percent, agriculture by 6.8, the volume of retail trade by 14.8 percent. Inflation rate was lower than predicted, and was 6.8 percent.

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7) Islam Karimov, “Our main goal is resolutely to pursue the path of large-scale reforms and modernization of the country.” //-T.: Uzbekistan, 2013 y.

Within twenty years, the GDP of the Republic by purchasing power parity increased by 3.4 times-from 27.1 to 92.3 billion U.S. dollars, and the volume of industrial production tripled.

During this period, the GDP share of the industry increased from 17 percent to 24 percent, the share of services went from 34 to 49 percent. This led to creation of new industries-automotive, petrochemical, pharmaceutical, modern food and textile industry. Along with this, implementation of profound change in the structure of agricultural production, the introduction of market relations based on the rental form of land use, created a modern infrastructure for agricultural production that contributed to grain self-sufficiency and an increase in total agricultural production by 1.8 times. As a result, over the period of independence, while ensuring sustainable production of cotton in the structure of agricultural production, the share of cotton actually declined from 47.7 to 11.1 percent, while the volume of grain production increased by 3.7 times and meat by 1.9 times.

After independence, the country's foreign trade would increase by 27.1 times, including export, which increased by 29.5 times and the ratio of foreign trade to GDP increased from 6 to 56.1 percent. Uzbekistan went from a country which mostly exported raw materials and imported finished products, has turned into an exporter of finished products with high added value, mainly taking place through import of high-tech equipment for technical and technological modernization.

The results thus achieved in the development of export potential allow expansion of methods for market regulation of foreign economic activity. In accordance with the priorities of economic development, Uzbekistan is expected to continue along the path toward reducing the proportion of export share which is regulated by the state, improving the system of foreign trade by taking into account regional integration processes, improving insurance and protection against risks of export-import operations, and further development of transport corridors. New directions in integration of the national economy into the global market will facilitate the efforts of the state by national corporations through arrangements with transnational corporations.

In addition, the President issued a decree on the “Priorities of development of industry in Uzbekistan in 2011-2015” in 2010, in order to enable stable, dynamic and balanced development of the republic's industry, deepening of structural reforms aimed at diversifying Uzbekistan's major industries, the growth of export potential and further improvement of the efficiency and competitiveness of industries, complexes and industrial enterprises. This would all take place with modernization, technical and technological renovation of production, underpinning the entire process.

A key role in ensuring the country's economic development was assumed by a comprehensive plan for implementation in 2011-2015, which adopted as its main tenets development of four interrelated strategic industries-development, infrastructure, transport communications and construction, and reforms in the financial and banking system with a total investment of US$77.4 billion, all expected to produce an increase in the GDP by 1.5 times.

As a result of consistent implementation of the program adopted for priority development of the industry in 2011-2015 and sectoral programs on modernization, the manufacturing sector has come to occupy an increasingly prominent place in the industrial structure technical and technological renewal of production, leading to production of competitive products with high added value. Today, these industries generate more than 78 percent of industrial production of the country.

Active implementation of structural reforms in the economy will continue to increase, with the share of industry in GDP increasing from 24 to 28 percent, primarily due to the development of priority sectors such as energy, Petrochemicals, chemical, textile and light industry, nonferrous metallurgy, machinery and automotive, pharmaceuticals, modern construction and finishing materials. In addition, further development of the social sphere and the service sector, infrastructure projects and commissioning of housing, including in rural areas is expected in the coming years.

Strategic priorities in the modern development of Uzbekistan include ensuring a dynamic and balanced development, continuation of profound structural changes, diversification and modernization of the leading sectors of the economy, the formation of more favorable investment climate and environment for doing business, the development of high-tech competitive products with high added value primarily for development of export-oriented enterprises on the basis of deep processing of raw materials available and finally, utilization of other competitive advantages of our economy.

2.1. Reasons for Uzbekistan's Interest in Economic Development Experience of Korea

Korea is one of the most prominent representatives of a small group of countries that have most fully and successfully implemented the model of catch-up development, progressing quickly from the category of least developed countries into one of the leading newly industrialized countries (NIC) of the world. Over the past half-century, South Korea has evolved from an underdeveloped, poor agricultural country into a modern country, nearly on par with economically advanced countries of the world in many areas. In 1996, Korea joined the OECD and thus became a prime example of how a country can dramatically reduce the time necessary for industrial transformation, a process that took most existing developed countries over a century.

This paper analyzes volumes, structure and other parameters of the current state of economic cooperation between Uzbekistan and the Republic of Korea and on that basis, provides systematic advice that revitalization and improvement of performance necessitates the evaluation of production, foreign trade and investment potential of the largest number of countries from far abroad business partner of Uzbekistan.

In a relatively short period of time from 1992 to 2012, the volume of trade between Uzbekistan and Korea has increased more than 540 times from 3.7 million to nearly 2 billion US dollars.[8)]

8) UNCTAD.

From the perspective of the Republic of Uzbekistan, economic cooperation with South Korea is in its interest by virtue of the following factors and conditions:

- The desire to find a large and reliable partner in the field of international relations. Large-scale, close economic cooperation between Uzbekistan and South Korea does not overly involve risks and challenges, as the Republic of possesses a significant, even by world standards, economic potential and financial resources;
- The desire to have access to large investments, which facilitates progress in several social and economic issues-from the technical upgrading of existing industries (cotton, silk industry) to creation of new industries (automotive, issue equipment) intended to be new engines for the entire industry of Uzbekistan.

The Republic of Korea, for its part, is interested in economic cooperation with Uzbekistan, primarily because Uzbekistan possesses the largest potential in terms of population and economic capacity among countries of the Central Asia:

- Uzbekistan represents a potentially large market for large and diversified industries in South Korea, mainly manufacturing and technical. This takes into account the fact that Uzbekistan is much more active than other CIS countries in undertaking structural reform of the economy, re-equipment of the domestic industry, transport and communications, increasing output of both import-substituting and export-oriented production. This leads to growing demand for advanced technology, machinery, equipment, components, spare parts, technical equipment, industrial semi-finished products, and as a result, abundant production and exports to various regions of the world;
- There is also political stability in Uzbekistan, which is the main condition for economic cooperation, and minimizes the risks for businesses, investors and entrepreneurs of South Korea, looking to engage in bilateral or planning

efforts to establish business contacts.

- The presence of the largest in the CIS and the fourth largest (after China. Japan and the U.S.) Korean diaspora, numbering, according to published statistics, that about 240 thousand people;[9)]
- A key transit location of Uzbekistan on the revived Silk Road. Forthcoming connection of the main rail and road Railways of China and neighboring countries in Central Asia in the next few years new routes will significantly reduce the time and costs of transportation between the Far East and the Mediterranean. Obviously, not only will this allow South Korea to benefit from activities of neighbors in the region-China and Japan, but benefit itself.

For all the importance of the above factors, the fundamental prerequisite to stimulating mutual interest of Uzbekistan and the Republic of Korea for economic cooperation is a high degree of complementarity of their national economies.

Comparison of sectoral patterns of production and foreign trade of both countries show significant differences between them. Indeed, in terms of production of cotton, made of yarn and a fabric, non-ferrous metals and semi-finished products from nonferrous metals, Uzbekistan produces in excess of the Korean economy's needs. And vice versa–Uzbekistan's developing economy needs modern technology and various other products investment destination.

The Republic of Korea is well known in the international market as a supplier, to significant global parties, of diverse technological equipment, vehicles, and many other consumer goods and forms of investment; at the same time, South Korea is a major buyer of fuel, raw materials, semi-finished products. Uzbekistan on the contrary, is an importer of engineering products, including those of their species, which the Republic of Korea produces and exports abroad.

9) The Korean Post, 2003, #16, See the page 51.

2.2. Comparative Analysis of Main Macroeconomic Trends of Korea and Uzbekistan.

Some lessons for Uzbekistan can be extracted from the results of a comparative analysis of key macroeconomic trends of Korea and Uzbekistan in recent years. Many of them are characterized by similarities between Korea and Uzbekistan with respect to macroeconomic dynamics, especially in the last 3-4 years.

The main differences lie in the sources and factors of economic growth. This applies primarily to potential investment resources. So the value of gross investment in fixed capital (% of GDP, see the Figures from 2 to 5) in Korea in recent years has been 1.5 times higher than in Uzbekistan.

In accordance with the opinion of Hongik University Professor Won Am Park, effective interaction of savings, investment and growth are the key to achieving high rates of economic development.[10] Consequently, Korea's experience demonstrates the need for the creation, in Uzbekistan, all required conditions and prerequisites for expediting the transformation of savings into investment and growth in investment activity, primarily in the private sector. This conclusion is supported by data on foreign direct investment, where Uzbekistan (2.5-6 dollars per capita) is inferior to the Korean economy (50 to $ 300 in 2000-2005) in terms of volume

This largely depends on the quality of public institutions, including the strengthening of guarantees of private property rights, contract discipline, investors' rights, compliance with the conditions of fair competition, and facilitation of the business environment.

At present the Republic Korea is a leader among trade partners of Uzbekistan. In 2012 the volume of trade amounted to more than 2 billion U.S. dollars. Currently in Uzbekistan, there are 138 joint ventures with Korean businessmen, and 45 Korean companies have opened offices.[11]

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10) Industrial development policies and promoting export of Uzbekistan. Knowledge sharing project. Ministry of Finance and Economy, of Korea, December 2005.

11) According to news agencies of Uzbekistan.

Key Macroeconomic Trends between Uzbekistan and Korea in 2000-2012

Figure 2. GDP Growth (Annual %)

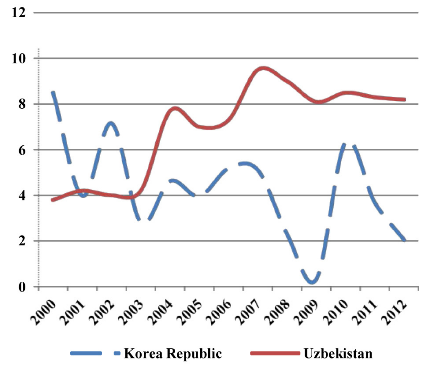


Figure 3. Export Growth (Annual %)

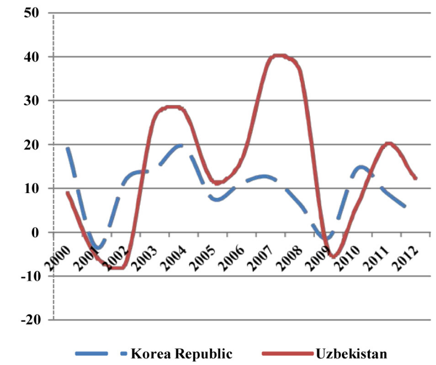


Figure 4. Export Diversification Index

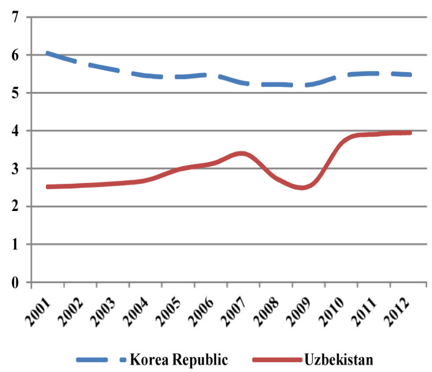
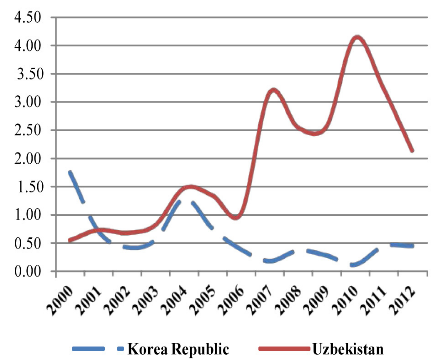


Figure 5. Foreign Direct Investment, Net Inflows (% of GDP)



Source: World Bank development indicators.

Since 2003, the growth rate of exports began to increase steadily. In the growth of export potential paled a significant role playing not only regarding the external environment, but also improved the structure of exports. More than 80% of exports is currently accounted for by industry and about 11% by exports of services.

The special significance of Korea as a trading partner of Uzbekistan due to the fact that Uzbekistan receives primarily high-tech products from there. Thus, the conditions are ripe for accelerating the process of modernization of the Uzbek national economy, and developing new competitive products.

The core of Korean exports to Uzbekistan consist of manufacturing products, including capital goods, components for the automotive industry, consumer electronics, telecommunications equipment, and sewing products. Analysis of the dynamics of commodity structure of Korean exports to Uzbekistan indicates that for the last 8 years products and equipments for the engineering were predominant, whose share in total Korean exports to Uzbekistan increased from about 60% in 2000 to 90% in years 2010-2012.

The structure of Uzbek exports to Korea (Korean imports from Uzbekistan) is similar to the structural model of exports of developing countries to developed countries. It is based on agricultural products (cotton, from 45 to 50%), imports of services (transport, communications, tourism-from 25 to 30%), and food products. In recent years the structure has been shifting towards import of certain chemical industries, as well as raw materials for pharmaceutical products.

The fact that the Republic of Korea is one of the major economic partners of Uzbekistan, has repeatedly led to bilateral and multilateral meetings of the heads of government delegations and our countries. After independence, there have been a large number of trade agreements concerning cooperation in areas such as finance, trade and investment, industry, oil and gas, energy.

In order to regularly discuss current issues related to trade and economic ties, bilateral Uzbek-Korean committees on economic cooperation and trade should be established.

It should be noted that during the state visit of the head of Uzbekistan to South Korea in March 2006, Presidents Islam Karimov and Roh Moo-hyun signed a Joint Declaration on Strategic Partnership between the Republic of Uzbekistan and the Republic of Korea. The Uzbek-Korean relationship up until the present stage has been developed on the basis of this document.

2.3. Role of Korean Capital in Development of New Economic Sectors in Uzbekistan

The most important factor in the economic development and growth of competitiveness of the Uzbek economy is to create conditions that would stimulate investment activity and inflows of foreign direct investment. Uzbekistan, as a capital-importing country, is following the path of continuous improvement of the investment climate in order to secure a number of distinct advantages. A notable feature of foreign capital is that, it not only complements the missing financial resources, but also introduces new technologies, equipment, know-how, improves the quality of products and the workforce, by attracting foreign specialists.

Enterprises in sector with participation of foreign capital represent some of the most rapidly growing sectors of the national economy. Analysis of the statistics on the sectors with joint ventures show that in recent years has become a proven tendency of expanding its scope, both in the number of existing joint venture, and in terms of its economic activity.

In the period from 2000 to 2007, their number (operating companies) increased from 525 units. up to 3579 units. or 6.8 times. The share of these sectors in the volume of joint ventures of total exports increased from 13.8 to 31.1%, and in the volume of imports-from 25.8 to 45.2%. The weight of this sector in the economy has increased from around 3% of GDP in 2001 to nearly 9% in 2007.

A characteristic feature of the sector is the fact that the growth of its foreign trade and exports in recent years has exceeded the corresponding figures for the country as a whole, which is reflected in the above statistics.

One of the leading foreign partners of Uzbekistan in creating this new, modern sector of the economy is Korea. The share of the Uzbek-Korean industries accounted for over 35% of production and services, which is higher than any other foreign trade partner of Uzbekistan. Most intense influx of Korean investments in Uzbekistan's economy was marked in the mid to late 90s.

By 2000, the total amount of Korean investment exceeded 1.1 billion U.S.

dollars.[12] In terms of The geographical structure of Korean investment in the CIS, Uzbekistan held the leading position in this period, and its share in volume of foreign direct investment of Korea to the CIS countries reached 80%.

It was during the period such major joint productions as UzDaewoo Auto, UzDaewoo Electronics and other joint ventures in the fields of automotive, telecommunications, electronics, textiles, as well as in the banking sector were created.

The production generated during this period laid the foundation for new industries in Uzbekistan-automotive, and also enabled Uzbekistan to carry out a deep modernization of telecommunication networks, saturate the consumer market with modern products and to create a large number of new jobs.

According to Korean businessmen, motivations for choosing Uzbekistan to host Korean investment include favorable legal and regulatory framework for investors, provided by state guarantees on the contracts and the availability of cheap and skilled personnel.

Despite some problems existing in trade and economic relations between the two countries, future prospects for development are evaluated by most experts as positive. Experience of creating joint ventures accumulated after independence allows us to maintain an optimistic view of the future. The main emphasis of new and recent joint projects are on the development of rich energy and natural resources, which Uzbekistan has plenty of.

During the visit in Seoul (February 2008), President of Uzbekistan Islam Karimov signed documents regarding a number of new Uzbek-Korean enterprises specializing in processing of mineral and petroleum resources, as well as finished products.

February 25, 2008 a consortium of Korean companies led by KOGAS and "Uzbekneftegaz" signed the documents to establish a joint venture for the construction UzKorGasChemical chemical complex at Surgil Field in the Ustyurt region near

12) A. Muhsinov. Economic cooperation between the states of Central Asia and the Republic of Korea. Tashkent 2002, pp. 34-58.

the Aral Sea, worth 1.84 billion U.S. dollars. The authorized capital of the joint venture, established on a parity basis, amounted to $ 600 million. The consortium of Korean companies, in addition to KOGAS (17.5%), included Lotte Daesan Petrochemical Corp (17.5%), LG International, SK Gaz and STX Energy-5%.

Field development and construction of Ustyurt Gas Chemical Complex at its base in Surgil will be the largest South Korea project in Central Asia. UzKorGasChemical will create field infrastructure, including the installation of natural gas treatment facilities and construction of gas-chemical complex with a capacity for processing 4 billion cubic meters of natural gas; producing 362 thousand tons of polyethylene, 83 thousand tons of polypropylene and 3.7 billion cubic meters of marketable natural gas. Project financing is planned to be borne by the Uzbek side, investment consortium of Korean companies as well as through foreign loans. The Korean side expressed its readiness to attract to their reserves of Fund for Economic Development and Cooperation of the Republic of Korea.

South Korea is heavily dependent on imports of raw materials, and has recently begun to develop resources abroad on the basis of various complex transactions. According to local analysts, products of UzKorGasChemical, will obviously be exported to Europe. Product gas will be exported via the pipeline SATs. The partners intend to sell gas chemical products to a wide range of countries. Agreement on a joint venture suggests that Uzbekneftegaz and the South Korean consortium will share the produced goods in equal proportions and dispose of them as each side see fit.

Uzbek government issued license to the Uzbek-Korean joint venture for production, processing and sale of gas and condensates in Surgil Field. For the joint venture, KorGasChemical was given permission for the design, construction and operation of the pipeline from the field to connect the main pipeline SATs. Experts from South Korea emphasized the need for preferential tax treatment, which was provided to the JV UzKorGasChemical by the Government of Uzbekistan.

According to a special resolution, the joint venture is exempt from payment of customs duties during the period of construction, preparation and development of imported equipment and materials; from VAT on work performed by foreign companies and services, from tax on income and property. Tax exemptions were granted for a period of 10 years from the start of production at the Ustyurt Gas Chemical Complex

Similar projects are being developed in telecommunications, manufacturing with modern textile products, medicines and other sectors of the national economy.

The rapid growth of the national economy of Uzbekistan is doubtless the objective prerequisites for expansion of Uzbek-Korean economic relations, a fact amply demonstrated in recent years. Analysis of the results in 2013 showed that the last several years, Uzbekistan reached a highest rate of economic growth since independence. Gross domestic product grew by an average of 8%, which is considerably higher than the rate of economic development in most of the CIS countries, among them Russia, Ukraine, Belarus and Kazakhstan. Fundamentally is the fact that economic growth is primarily due to the consistent implementation of a comprehensive system of sound policies and market reforms to attract foreign investment, initiate deep structural changes in the economy, modernize and renovate production processes and the create new export-oriented industries and businesses, accelerate development of business and entrepreneurship, and create prerequisites for transition to innovative economic development. Further development of cooperation between our countries have will consolidate the results achieved, which would strengthen the position of Uzbekistan in the global market.

III. Perspectives of Further Development of Uzbek-Korean Economic Relations

Although Korea is a successful example, no country can achieve rapid growth by mechanically copying the experience of Korea. This is due primarily to the fact that economic, social and political environment of each country may differ from the one in which Korea began its development. Secondly, some of the strategies and decisions previously taken by Korea, would no longer be applicable. Moreover, some of the strategies that served as important growth factors actually became causes of a number of problems later. Therefore, caution and prudence is called for when using Korea's development model for other countries.

Taking this into account, we will try to outline some of suggestions and recommendations for Uzbekistan, based on a critical observation of Korea's experience with emphasis on the sources of growth and economic policies.

First, the system of state incentives at the initial stages of industrialization should be oriented to the external market and closely linked to quantifiable, transparent and performance-based criteria. Obtaining export orders in the competitive international market means that firms have been tested for effectiveness at the international level.

Even though policies were in place to promote private business, the government did provide a system of incentives, punishing poorly performing chaebols while rewarding effective businesses by issuing new licenses in more profitable areas. As a result, these incentives contributed to improving distribution.

With respect to Uzbekistan, there is the need to establish new industrial corporations in the non-primary sectors (financial and industrial groups) of industry, initially export-oriented, with emphasis on clear and transparent criteria of efficiency, under government support.

Second, the experience of the ineffectiveness of Korea politics, in which the development of the financial sector pales into insignificance due to priority on maintenance of the real sector. In recent years, the financial sector has become a top priority in Korea. Progress achieved to date include interest rate liberalization and opening up access to the capital market. In the future, the evaluation functions and credit-risk control of firms should be transferred from the State to financial institutions.

In Uzbekistan, this would mean further liberalization of the banking sector, the growth of capitalization of the banking system, limiting government interference in decisions of commercial banks to grant loans to the real sector, increasing the number of private banks, and increasing competition in the banking sector.

Third, entrepreneurship is essential for the implementation of public policies at all stages of industrialization. Hence, it is important to educate entrepreneurs who can take a leading role in business.

For Uzbekistan, where small and private businesses represents only 12-14% of firms in industry, the priority should be on activation of private capital in industrial production. An important benchmark is provided here by the positive experience of Korea in the use of measures and mechanisms to reduce transaction costs and administrative barriers to small and private businesses.

Fourth, a disciplined workforce is essential to promoting the development of mechanical engineering, with an emphasis on foreign markets. Consequently, the training of modern engineering and management personnel, especially for industries of Uzbekistan which specializes in complex, urgent tasks and involving Korea in the decision, can be significantly extended.

Fifth, it is important that competition develops a regulatory framework to ensure fair rules of the game, with equal opportunities for all market participants. Political leadership should be able to create a national consensus for achieving such development goals. In this regard, measures for creating joint consulting and administrative councils (government-to-business public), used in Korea, could be an effective tool for increasing the effectiveness of antimonopoly policy in Uzbekistan and economic development programs in general.

Essential contribution to modern Korean economy was made by flexible economic policy and the use of indicative planning. Challenges of globalization, rapidly changing geopolitical environment, the worsening environmental problems-all these factors dramatically increases the importance of adequate and flexible economic policy in Uzbekistan. Development of methods and principles related to this policy based on Korea's experience can become the subject of a detailed investigation.

Some lessons for Uzbekistan can be extracted from the results of the comparative analysis of major macroeconomic trends of Korea and Uzbekistan for the period 2000-2013. More often than not, Uzbekistan is characterized by similar macroeconomic dynamics as for Korea.

The main differences lie in the sources and factors of economic growth. This applies primarily to potential investment resources. Thus, the value of gross fixed capital investment in recent years in Korea has been 1.5 times higher than in Uzbekistan.

In accordance with the opinion of Hongik University Professor Won Am Park,[13] effective interaction of savings, investment and growth are the key to achieving high rates of economic growth. Consequently, Korea's experience demonstrates the need for the creation of all necessary conditions and prerequisites for expediting the transformation of savings into investment and growth in investment activity, primarily in the private sector in Uzbekistan. This conclusion is confirmed in connection with attraction of foreign investment, the magnitude of which Uzbekistan is greatly inferior to the Korean economy.

It depends greatly on the quality of public institutions, including the strengthening of guarantees of private property rights, contract disciplines, investors' rights, compliance with the conditions of fair competition, and a favorable business environment.

Significant potential of growth of the Uzbek economy lay with more efficient use of resources, or to be specific, energy resources. In terms of GDP energy intensity, Uzbek economy is four times larger than Korea, which significantly limits the ability of Uzbekistan to expand export capacity, making its economy more vulnerable to unfavorable world market conditions, especially for oil and other energy products.

The main conclusion arising from the analysis of the history of the Korean economy is that all the country's achievements have been made possible thanks to the joint efforts of government, business and the public; aimed at the development

13) Industrial development policies and promotion of exports of Uzbekistan. Knowledge sharing project. Ministry of Finance and Economy, Republic of Korea, December 2005.

of modern manufacturing industries, with focus on foreign markets, i.e. creation of modern competitive industries. Depth analysis of the stages, methods and mechanisms for increasing the competitiveness of the Korean economy at the macro level (economic policy) and the sectoral (sector, chaebols, small and medium enterprises) level, is of exceptional value for the further development of Uzbekistan's economy. Furthermore, it could become the subject of continuing research in Korea's economic development experience.

IV. Conclusion

In this article, an analysis of trade and economic relations between Uzbekistan and Korea in recent years was performed and the results obtained provide every reason to justify the statement that South Korea has played and will play a crucial role in the formation of the new economy of Uzbekistan. This is due primarily to the fact that unlike other countries, such as Russia, which has a larger amount on foreign trade turnover with Uzbekistan than Korea, Korean investments made the greatest contribution to the development of new high-tech industries in Uzbekistan and sectors such are automotive, electronics telecommunications, textile industry and the banking sector. The development of trade relationships between our two countries satisfied the consumer market with modern products, created a large number of new jobs in industry, commerce and the service sector, and products were imported and produced by Korean production license.

Amidst cooperation between our countries, a mechanism has to be worked out for its further development. In order to regularly discuss current issues related to trade and economic relations, the Uzbek-Korean and Korean-Uzbek committees on economic cooperation and trade must be developed and successfully operated.

The great potential of increasing the effectiveness of economic reforms in

Uzbekistan, must be accompanied by measures and recommendations derived from a critical analysis of experience in creating modern Korean economy. The key issues here are the principles for a flexible strategy of macroeconomic regulation, demonstrated by the Korean government in the second half of the twentieth century, approaches to the role of government at various stages of industrialization and the formation of export potential, and measures and mechanisms for promoting the development of the modern small business.

With respect to findings for Uzbekistan, the results of the study of the Korean experience we obtained highlights the need for strengthening the stated incentives for export-oriented producers based on predetermined quantitative criteria for their effective functioning. In structural and organizational terms, this means creating new industrial corporations of (financial and industrial groups) non-primary sector of industry, initially export-oriented in Uzbekistan.

Experience of Korea speaks about the ineffectiveness of economic policy, in which the development of the financial sector pales into insignificance when the question of the maintenance of the real sector. In reference to Uzbekistan, this means further liberalization of the banking sector, the growth of capitalization of the banking system, limiting government interference in decisions of commercial banks to grant loans to the real sector, increasing the number of private banks, increasing competition in the banking sector.

The achievements of modern Korean economy owe much to the government's efforts to create a modern sector driven by small and private entrepreneurs. For Uzbekistan, where small and private businesses in the industry is only 12-14%, the priority is the activation of private capital in industrial production. An important role is played here by the positive experience of Korea in the use of measures and mechanisms to reduce transaction costs and administrative barriers to small and private business

Korea's experience has shown the importance that competition develops regulatory frameworks to ensure fair rules of the game and equal opportunities for all market participants, and political leadership must strive to create a national consensus to achieve development goals. In this regard, the methods of creating joint consulting and administrative councils (government-business-public) that were utilized in Korea could be an effective tool for increasing the effectiveness of antimonopoly policy in Uzbekistan and economic development programs in general.

The crucial contribution in the creation of a modern Korean economy was made by flexible economic policy and clear direction. As for Uzbekistan, challenges of globalization, rapidly changing geopolitical environment, the worsening environmental problems dramatically increases the importance of adequate and flexible economic policy in Uzbekistan. Development of methods and principles with respect to policy on the basis of Korea's experience should become a subject of a detailed investigation.

In conclusion, it should be noted that not all joint projects initiated by the two countries in the early and mid- 90s were successful. For several reasons, some of the Uzbek-Korean companies created during this period were subsequently restructured, and some of them stopped their operations altogether. But these companies have made a positive contribution to the development of the national economy, increasing the number of professionals and managers, utilizing modern technology and expertise to promote Uzbek goods and services in world markets.

Changes of the world situation and other challenges of globalization would often play a not-too-insignificant role. In fact, these conditions significantly increased the role of new high-tech sectors, enabling the Uzbek economy to withstand these challenges.

In this regard, one of the potential directions in deepening and detailing the results obtained in this project should be to study the Korean model for integration of national economies into the global economic system and training on the basis of its sound recommendations for enhancing the innovative growth factors specific to a transition economy such as Uzbekistan.

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Political Economy of SAARC and Regional Trade Integration: The Recent Ontogeny and Future Prospects

Khalid Ahmed[1)]

I. Abstract

Trade integration in the political economy of South Asia has been faced with consecutive ups and downs owing to bilateral disputes between Pakistan and India, maintaining long sensitive lists, double taxation, and countries' preference to unilateral trade liberalization. Notwithstanding an excellent trade potential, South Asian nations have yet to accomplish discernible organizational goals through SAARC. The obvious cause of such deterioration is more political and less technical in nature. Similarly, the utmost goal of trade integration within the SAARC membership has also fluctuated with the ebb and flow of political tension among SAARC members. However, the recent developments towards regional economic integration and cooperation

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1) Assistant Professor, Sukkur Institute of Business Administration (IBA-Sukkur).

have again shown positive signs. In contrast to previous developments, the current progress seems more realistic and lasting as the region is faced with increases in common problems (i.e. terrorism, environment and poverty). More precisely, it can be assumed that the increasing threat of poverty, terrorism and natural disasters (because of climate change and environmental degradation) has compelled member states to negotiate and sign specific agreements to collectively face and cope with these challenges. Therefore, in order analyze and bring forth latest updates of regional trade integration in the political economy of SAARC, this paper evaluates the regional economic cooperation and trade integration in the light of recent developments, their overall policy implications on the region and to what extend they help member states resolve their existing bilateral conflicts.

II. Introduction and Background

The increasing demand for regional blocs in the economic world today also convinced South Asian nations towards the formation of the South Asian Association of Regional Cooperation (SAARC).[2] It is considered as the foundation to trade integration in South Asia. Though the regional integration of European Nations2 and Southeast Asian nations[3] in the 1950's and 1960's respectively, established ample ground in term of both theoretical and empirical framework, South Asia remained indifferent towards regionalization until the 1980's. Undoubtedly, South Asia has undergone tumultuous political, geographical and economic transformations in the past. This region has been attractive to both traders and invaders due to its productive terrains, attractive trade and cultural strengths. So, whether they be Arab traders in the early 8th century or Central Asian invaders from 12th to 18th

2) India, Pakistan, Bangladesh, Srilanka, Nepal, Bhutan, Maldives and Afghanistan.
3) Association of Southeast Asian Nations (ASEAN).

century or the British East India company, they all came for the sake of trade and established their caliphates, monarchy and colonies, respectively. Thence, why the South-Asian Nations, amongst which trade proliferated in the 1940's turned trade restrictive in later decades is a topic of great importance in the regional political economy. However, the formal dialogues regarding economic integration in South Asia started in 1991, which subsequently resulted in the South Asian Preferential Trade Agreement (SAPTA).

Nonetheless, the free trade agreement in South Asia began with an even more conservative approach than anticipated (Weerakoon and Theenakoon, 2006). Since they very beginning, the process of overall regional integration in South Asia was faced with ups and downs. The South Asian economies rather adopted unilateral trade policy reforms in order to integrate themselves into the world economy (Taneja, 2001). In the political economy of South Asia, the security concerns among states, especially Pakistan and India,[4] has become a major hurdle (Dubey, 2007). There is ample literature available discussing the role of India towards the success of SAFTA but regrettably it has remained ambiguous till date (Taneja, 2001; Dubey,2007; Amita, 2007; Ershad and Dayal, 2009; Weerakoon, 2010; Rajendra, 2011; Fahmida and Mazbahul, 2013). The regional economic integration perseveres as member states of regional bloc give preferential trade incentives while maintaining the barriers toward the rest of the world (Hanif, 2012). Unfortunately, in case of SAARC, that notion is inconsistent with the inter-regional trade volume that is still far higher than intra-regional trade. Moreover, the serious flaws in agreement, long sensitive list of each country, the long time taken to liberalize tariffs line and per-due political interests have been keeping free trade agreements fragile in South Asia.

Nevertheless, there have been various recent developments towards the settlement of issues which represents a positive sign towards the growth of regional and economic cooperation in South Asia. It mainly includes; first, the growing bilateral relations

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4) India and Pakistan are the two largest economies of SAARC and maintain deep geographical and political disputes since their independence from British Colonial rule in 1947.

between India and Pakistan since early 2011. Second, in the joint statement of the 17th SAARC head of States' summit directed the ministerial council on SAFTA to shorten the sensitive list and enact appropriate reductions in non-tariff barriers. Third, soon after the summit, Pakistan granted the MFN (Most Favored Nation) status to India. Fourth, all member states unanimously declared to collectively fight environmental degradation, terrorism, and poverty in the region. The long-standing purpose of SAARC was to expand opportunities to exploit economic and social gains within and outside the region. More specifically, there is no doubt that South Asia has been a strong economic and cultural hub throughout its history. But why this region failed to gain momentum with the passage of time and could not catch up with the global trend of regional economic cooperation or why it took a long time even when this process was started. These are the potential problems which have been discussed before but this study evaluated the recent positive developments carried out towards trade integration of South Asia along with the bird's eye view of previous issues. Now, it can be assumed that South Asian economies have realized the importance of regional trade blocs for ensuring economic well-being, which would also help to resolve its long lasting political and geographical disputes.

This paper is a theoretical analysis of the SAARC organization, its progress towards regional trade integration and its prospects in terms of regional economic prosperity, conflict resolution and global implications. This article is divided into five parts; Part II provides detailed historical background of regional economic cooperation; Part III re-evaluates the political nature of South Asian Economy and its impacts on the process of trade integration; Part IV provide some statistics and empirical view of regional and intra-regional trade in South Asia, Part V enumerates the collective challenges that region faces and how the SAARC platform can resolve such conflicts and Part VI, has some concluding remarks and future perspective on South Asia's regional economic and trade integration.

III. Regional Cooperation to Free Trade Agreement

Historically, the South Asian region has been the hub of cultural, social and economic enterprise. The region has maintained its links to the world, and was possessed of vibrant socio-economic potential that distinguished it in all aspects, considered prerequisites for any modern and civilized society. Regrettably, its openness and attraction to the outside world brought frequent and invasive foreign intervention, thus hindering the region's ability to fully exploit its potential. Bose and Jalal (1998) provides vital referencer in detail and sophisticated insights into the social, political and economic spectrum of South Asia during the last three centuries and how the region remained fragile during Mughal empire, through the British raj, post-colonial and modern times. Technically, there is strong justification for integration of the South Asia region, in light of political and economic theories that are usually considered as the prerequisite for any successful regional integration such as Telo (2013).[5] But the legacy of British imperialism and its impacts on state formation has created an almost permanent set of negative relations that pre-empt regional economic cooperation (Reed, 1997). South Asian region possesses abundance of natural resources, huge labor and consumer market resource, as it possesses one fifth of the world's population[6] and direct access to energy rich gulf and central Asian states through sea and ground. These features undoubtedly reveal the regional economic potential of SAARC nations. In nineteenth and until the mid of twentieth century, South Asia has been a trading destination for countries in Europe, the Persian Gulf and Southeast Asia. The economies of South Asian nations which were highly open to trade at the time of their establishment in early 1940's turned protectionist by early 70s in terms of both tariff and non-tariff barriers (Weerakoon, 2010). In fact, the process of regional cooperation in the South Asia region started slightly

5) for detailed understanding of Regionalism as new paradigm shift and its impacts on global governance, see Telo (2013).
6) The total population of SAARC member states is 1.6 billion (WDI. World Bank, 2009).

late as compared to European Union (EU) and Association of South-East Asian Nations (ASEAN) which were established in 1952 (Treaty of Paris) and 1967 (Bangkok Declaration), respectively. Why these economies chose to emphasize unilateral trade liberalization with rest of the world rather than initiating regional cooperation is discussed with details in Section III.

Nonetheless, efforts for regional cooperation began soon after the partition of the Indian subcontinent during the 1947 Asian relations conference in New Delhi, and remained under discussion in following conferences i.e. in Baguio-Philippines (1950), and Colombo-Srilanka (1954). Subsequently, growing bilateral tensions between Pakistan and India over the Kashmir issue and political instability in the region led to long delays in talks. After a long pause in progress of regional cooperation and end of the cold war era, South Asian Association of Regional Cooperation (SAARC) was formally established in 1985 with seven[7)] member countries excluding Afghanistan who joined later in 2007. The core purpose of the association was set to boost social, cultural and economic cooperation[8)] between the member states and other developing countries. The regional trade liberalization was introduced into the agenda in the early 1990's. After a series of dialogues, the South Asian Preferential Trade Agreement (SAPTA) was signed and became operational beginning in December 1995. Basically, SAPTA was envisaged as a primary step to instituting the South Asian Free Trade Agreement (SAFTA). Consequently, it was decided to discourse SAFTA by year 2000 or at least before 2005.

In 1998, the growing bilateral tension between two largest member countries, India and Pakistan, resulted in the postponement of the annual head of states' summit up to three years. This setback resulted in a delay that lasted until the restoration of talks in 2002. The framework of treaty on SAFTA was adopted on January 6, 2004 at the 12th SAARC summit held in Islamabad and went into force

7) India, Pakistan, Bangladesh, Sri Lanka, Nepal, Bhutan, and Maldives.
8) Refer SAARC charter: http://saarc-sec.org/SAARC-Charter/5.

Table 1. SAARC FreeTrade Agreement: Progress and Current Status

		Major Outcome	FTA	Tariffs						Customs Duty			NTB's	MFN
Place	Date			Goods			Services			Goods				Treatment
				Full	Partial	Slight	Full	Partial	Slight	Full	Partial	Slight		
Dhaka	7-8 Dec. 1985	SAARC Charter	0	0	0	0	0	0	0	0	0	0	0	0
Banglore	16-17 Nov. 1986	SAARC Secretriat	0	0	0	0	0	0	0	0	0	0	0	0
Kathmandu	2-4 Nov. 1987	Poverty Alleviation	0	0	0	0	0	0	0	0	0	0	0	0
Islamabad	29-31 Dec. 1988	Drugs Eradication	0	0	0	0	0	0	0	0	0	0	0	0
Male	21-23 Nov.1990	Environmental Protection	0	0	0	0	0	0	0	0	0	0	0	0
Colombo	21 Dec. 1991	Est. of Com. on EC	0	0	0	0	0	0	0	0	0	0	0	0
Dhaka	10-11 Apr. 1993	SAPTA Framework	0	0	0	0	0	0	0	0	0	0	0	0
New Delhi	2-4 May. 1995	Trade Concessions	0	0	0	0	0	0	0	0	0	0	0	0
Male	12-14 May. 1997	SAPTA in Force Dec. 1995	0	0	0	0	0	0	0	0	0	0	0	√*
Colombo	29-31 Jul. 1998	↓ Tariff, Non-tariff Barriers	0	0	0	0	0	0	0	0	0	0	0	0
Kathmandu	4-6 Jan. 2002	Progress to SAFTA	0	0	0	0	0	0	0	0	0	0	0	0
Islamabad	4-6 Jan. 2004	↓ in Sensitive List (SL)	0	0	0	0	0	0	0	0	0	0	0	0
Dhaka	12-13 Nov. 2005	SAFTA in Force by 2006	√	0	0	√	0	0	0	0	0	0	0	0
New Delhi	3-4 Apr. 2007	SAFTA Effectiveness	√	0	0	√	0	0	0	0	0	√	0	0
Colombo	2-3 Aug. 2008	↓ in NTB's and SL	√	0	0	√	0	0	0	0	0	√	0	0
Thimphu	28-29 Apr. 2010	↓ in NTB's and SL	√	0	0	√	0	0	√	0	0	√	0	0
Addu	10-11 Nov. 2011	↓ in NTB's, SL and Customs	√	0	√	√	0	0	√	0	0	√	√	0
Kathmandu	Nov. 2014					To be held								

Source: SAARC, WTO and SAARC Countries, *1996, India granted MFN status to Pakistan.

in January 1, 2006. It was decided in subsequent foreign ministerial meeting[9] to reduce the tariffs to zero level up to 2016 with exception of five least developed countries[10] of the region which are granted three additional years.

The negotiations towards regional cooperation between South Asian nations have remained tumultuous over past two decades. Unfortunately, frequent deadlocks were spurred by the same factors that were supposed to have been solved at the initial level. Still, every SAARC head of states summit ended with commitment to objectives enshrined in the SAARC charter. The realization of member states are reflected in success in recent dialogues. The region has signed several agreements[11] during the 15th, 16th and 17th SAARC summits after extensive discussions of core regional issues in previous rounds. Considering the importance of environment, energy needs, and terrestrial linkage in regional integration, the feasibility of proposed projects has been sought and reviewed twice. This serious attitude has been maintained, and for the first time in history, SAARC represented the whole region with single unanimous policy and agreement authority in recent United Nations' conference on environment. However, there are many issues expected to come up as South Asian region is still striving with the basic challenges e.g. poverty, environment, energy shortage, governance, corruption, and terrorism.

IV. Trade Integration in View of Political Economy

In the political economy of South Asia, countries' individual political interests have been the major cause of indifference towards trade integration. Besides, non-tariff barriers, which are considered a key issue, has been deliberately ignored in negotiations.

9) The treaty was ratified by Pakistan and India in 2009 and by Afghanistan in 2011.
10) Bangladesh, Nepal, Afghanistan, Bhutan, and Maldives.
11) Refer this link to see list of agreements and their details: http://saarc-sec.org/Agreements/69.

The quantitative and qualitative research conducted earlier are also quite pessimistic in their viewpoint, including research since the beginning and even prior to formation of SAARC in 1985. Jayaraman (1978) and Rahman *et al.* (1981) examined and concluded that a South Asian custom union would not be significant for the small countries like Nepal and Sri Lanka. Later studies by Govindan (1994) and Bandara *et al*. (2003) brought forward inter-regional and unilateral trade liberalization as alternate policy options. The SAPTA seemed to be more susceptible when it came to the discussion of successful RTA's. However, Viner (1950) argued that the welfare effect of RTA depends upon the size of trade creation and trade diversion. Following this study, Bhagwati and Panagariya (1996) also argued that the preferential trade within RTA's diminishes the welfare in member states. In a nutshell, economic theory states that the balance between trade creation and trade diversion determines the overall welfare effect of PTA. Subsequently, when various empirical studies are conducted using a gravity model to test the trade diversion and trade creation effect of SAPTA, the results in particular were contradictory i.e. Matyas (1997/98) using augmented gravity model suggested that panel data evaluate the results better than the cross-section approach. Egger (2000) argued that the cross-sectional data approach helps to capture the business cycle, while evaluation by Rahman (2003) showed mixed results using panel data technique in order to asses trade potential of Bangladesh. Hirantha (2003) assessed diversion effect of SAPTA but could not reach a conclusion, and Cheng and Wall (2004) used country pairs to avoid heterogeneity in the gravity model, while Tumbarello (2006) tested both cross-sectional and panel technique but did not use a country pair specific fixed effect.

Notwithstanding the shortcomings and severe literary criticism, SAPTA has survived and even made progress. In spite of frequent political tension between some member states, the key politicians of the region hold an optimistic view regarding regional trade integration. Several empirical studies also backed this view (Matyas, 1997; Rahman, 2003; Weerakoon, 2010). In addition to regional trade integration, one of the primary objectives behind the free trade agreement was to accomplish the non-economic goals of SAARC. The mutual economic interest could help member states to resolve multidimensional issues like tension between India and Pakistan which are the two major economies in the region. The recurring disputes between these two countries are considered a major obstacle to the effective regional cooperation. However, recent developments indicate immense progress in overall regional cooperation, especially in terms of trade integration. The last decade from 2002 to 2012 has been the highlight of SAARC negotiations. As in the beginning, during the 12th and 13th SAARC summit, key issues were addressed and discussed, which as a consequence succeeded in bringing about major breakthroughs. It includes strong determination to fight terrorism, removal of double taxation, joint statement at COP, establishment of regional centers and the most importantly, Pakistan agreed to grant MFN status to India in February, 2014. It was the first bold decision in the history of two neighboring hostile nations towards trade liberalization. It will bolster regional trade ties and will help to resolve political issues between two nations.

4.1. Two Player Game

Pakistan and India are the two largest economies of the region accounting 94% of the GDP of the SAARC, 85 % of the population and 80% of the land area. However, the trade between the two countries accounts for just 20% of region's total trade. The potential trade calculated using the gravity model is 20 times bigger than existing trade volume (Khan, 2011). Trade integration in SAARC is highly dependent on the bilateral trade integration of Pakistan and India (Taneja *et al.*, 2014), meaning the bilateral relations of both countries also have very sever implications on SAARC. Whether it is regional cooperation or trade integration, the pleasant relations always reflect positive signs while tension between both the countries have negative impacts. In short, SAARC is basically a two player game, involving Pakistan and India.

The recent improvement in Indo-Pak relations has also brought confidence in the SAARC region. The SAARC Chamber of Commerce and Industry (SAARC CCI) of India and Pakistan chapter has urged Pakistan to announce MFN status for India. It is believed that this step would bring higher level of confidence between the two countries and its businesses as well. Now is the time for Pakistan to reciprocate India's granting of MFN status to Pakistan in 1996. There are some empirical studies which determines the impact of MFN treatment in SAARC. For example, the study of Raihan (2013) calibrated the MFN scenario using data of SAARC countries using CGE modeling. The study suggests that Pakistan's grant of MFN status to India and reduction in sensitive list of India in return will enhance the trade momentum in the SAARC region. However, the results also conclude that Pakistan should enact more measures to reduce custom clearance issues and duties, and India must fulfill its responsibility being the largest economy of region by reducing duties on Pakistani imports and making it easier to invest in India.

The prolonged dispute between both countries is now beginning to subside, and the people and the governments of both the countries agreed to strengthen bilateral relations especially in terms of economics and trade. The strong economic relations would help to peacefully resolve the major issues that existed between the two countries since their inception. Trade simply represents icebreaking, while the most noble ‘move’ would be to create harmonious political and social environment that would produce more welfare in the region.

4.2. Role of India

Throughout the history of SAARC, the role of India towards regional cooperation has been questionable. Though there is no objection regarding the importance of the role of India in region but the smaller states have deemed India's role to be hegemonic rather than one of leadership (Rao 1988; Dash 1996; Jetly 2003; Taneja and Sawhney 2007; Weerakon 2010; Gupta 2013). All these studies have also emphasized that the India must change its attitude towards the regional integration rather than just focusing on other regions. India's overall reputation in the region is nothing more than that of a feudal lord and its tenants. As a result the weary smaller states are more accommodating of economic and political influence from other states i.e. China. The increasing economic and political influence of China in the South Asian region is an open sign of security concerns among smaller countries vis-a-vis India. In early, 2010 Nepal proposed to convert China's observer status in SAARC to full membership, which was vetoed by India. However, the membership is supported by all countries except Bhutan. India is involved in border disputes with almost all of its neighboring states, aside from the fact that her immigration rules, custom duties and trade restrictions are stricter for South Asian economies than other regions. The combination of the factors has kept SAARC away from exploiting its fullest potential. It is collectively believed that SAARC may not become a successful regional cooperation association unless India redefines its role.

The current globalization and regionalization both have matured to an institutional level. The South Asian nations, no matter how much open themselves to rest of the world, the current global and regional dynamics strongly urge SAARC nations to transform themselves into a vibrant regional cooperation association in order to face the challenges and opportunities together, aside from simply being good neighbors. In SAARC, India has to take the leadership role, being the largest economy, and cultural and social center of South Asia. India has to play a greater part, so that the smaller countries will follow suit, to become an example of highly effective cooperation for the world. But, it is only possible when India recognizes and respect the sovereignty of smaller states.

Recently, many of the politicians and the scholars in India have emphasized that India must review its role in South Asia before the other powers in the region (Singh, 2011; Dingli, 2011; Chakrabarti, 2012; Scott, 2013; Kumar and Hussain, 2014). In terms of trade liberalization with South Asia, for eastern nations, India is the only transit path connecting them to Nepal, Bangladesh and Bhutan with Pakistan and Afghanistan. The change in the geo-political situation in South Asia began after Pakistan's nuclear test on May 1998. The Indo-Pak relations was given added momentum in 2002, Sri Lanka successfully ended the 20 years long violent ethnic conflict between the Tamils and the Sinhalese, and SAARC summits achieved the most rapid progress in its history and reached many of its set targets. Though SAARC yet to accomplish much thereafter, but progress during the last decade has been very spectacular. India role has been a bit more positive but India need to be much more earnest and it is believed that India will display a more mature attitude towards the SAARC common economic goals in the upcoming 18th SAARC summit to be held in Kathmandu, Nepal.

V. Regional and Intra-Regional Trade in South Asia

Although the process of regional cooperation and trade integration in SAARC nations has moved at a snail's pace, yet it represents the largest regional treaty in term of population (approx:1.6 billion inhabitants as of 2009). As shown in Table 2. SAARC is fourth place after three giant regional economies of EU, NAFTA and ASEAN. However, the direction of trade integration in most of the South Asian economies has been outward oriented. As shown in Table 3, the bilateral

Table 2. Comparison of The Largest Four Regions: The EU, NAFTA, EAST ASIA and SAARC (2012)

	Population (Millions)	As % of World Population	GDP (Billion US $)	As % of World GDP	Merchandise Exports (Billion US $)	As % of World Exports	Merchandise Imports (Billion US $)	As % of World Imports
EU (27)	505	7.1	16670	22.9	5804.6	31.4	5842.4	31.5
NAFTA	457	6.5	18661	25.7	2371.0	12.9	3191.0	17.2
ASEAN	616	8.7	2311	3.2	1254.5	6.8	1221.8	6.6
SAARC	1649	23.4	2303*	3.2	354.6	1.9	602.0	3.2
WORLD	7044	100	72490	100	18447.5	100	18559.1	100

Source: World Bank (WDI), IMF (WEO) & (DOTS), GDP is in Current US$.

Table 3. Intra-Regional Trade Share among SAARC Nations (2010) (Unit in %)

	India	Pakistan	Bangladesh	Sri Lanka	Nepal	Maldives	Afghanistan	Bhutan
India	-	0.5	0.1	0.7	0.4	0.1	0.1	0.1
Pakistan	4.3	-	0.7	0.5	0.1	0.1	2.9	0.0*
Bangladesh	10.0	1.2	-	0.1	0.2	0.0*	0.0*	0.0*
Sri Lanka	17.4	1.5	0.1	-	0.0*	0.4	0.0*	0.0*
Nepal	57.6	0.1	1.3	0.1	-	0.0*	0.0*	0.1
Maldives	10.2	0.4	0.1	6.5	0.0*	-	0.0*	0.0*
Afghanistan	6.4	23.3	0.1	0.0*	0.0*	0.0*	-	0.0*
Bhutan	77.0	0.0*	1.0	0.0*	1.9	0.0*	0.0*	-

Note: * Value less than 0.1% referred as 0.0%.
Source: SAARC, IMF (WEO) & (DOTS), Department of Trade, Government of Bhutan http://www.trade.gov.bt.

trade share between most of the SAARC economies is less than 2%, excluding India which has 11% (on average) combined with the three major economies (Pakistan, Sri Lanka and Bangladesh) of the region. Moreover, India, Pakistan, Bangladesh, and Sri Lanka liberalized trade ties unilaterally with the other three regions but have relatively meager focus on intraregional ties. The comparative advantage in same products, political instability, and bilateral confrontation between economies[12] betray the disinterest of parties. As shown in Table 4, the Intra-regional Trade Share (ITS)[13] of SAARC nations is noticeably higher with EU (27), NAFTA, and ASEAN. This reflects the fact that the India-ASEAN Free Trade Agreement (FTA) is already in effect, the efforts of Pakistan to be the dialogue member of ASEAN are making progress, and Sri Lanka has signed the second[14] B2B memorandum of understanding (MoU) with Malaysia. It enumerates the following;

12) The long lasting dispute over Kashmir between Pakistan and India.
13) Intra-regional Trade Share (ITS) is an integration indicator and referred to as a share of total trade volume of one economy holds with other member economy.
14) The first Business to Business (B2B) memorandum of understanding (MoU) was signed between Sri Lanka and Singapore in May 2011.

Table 4. SAARC Nations Trade Share with Major Regions of World (2010) (Unit in %)

	SAARC	EU (27)	ASEAN	NAFTA
India	2.2	14.4	9.1	7.7
Pakistan	8.2	13.2	11.8	18.4
Bangladesh	11.6	22.5	11.8	11.7
Sri Lanka	19.6	20.1	12.4	10.4
Bhutan	80	0	0	0
Nepal	58.1	4.8	5.3	2.5
Maldives	17.3	9.7	38.3	2.8
Afghanistan	29.9	12.2	3.3	29.1

Source: SAARC, IMF (WEO) & (DOTS), World Bank (WDI).

the trade potential SAARC economies possess and traces of economic and non-economic barriers towards exuberant trade liberalization of the region.

Although India has been facing questions because of its restrictive past yet it is commonly believed that the role of India in the process of South Asian trade integration is crucial. Nevertheless, the recent developments in term of tariff reduction as shown in Table 5, Implementation of Regional Standards (IRS), and physical connectivity among countries through roads and railway lines and rapid disaster management response system represent ice breaking steps facilitating the strategy of India in this regard. It is desired that by 2016 South Asia will be a completely free trade zone. How long and how far would the present cooperation will prevail? It is all depends on the leadership of India. The political economy of trade integration in South Asia will always be unpredictable as in past. It is observed that non-economic factors have always been dominating.

Apart from economic factors, there is a series of empirical research which analyzed Regional Trade Agreements (RTAs) and found several non-economic factors which also enhanced the effectiveness of preferential trade blocks recently. Works such as Vicard (2011) corroborated that similarities in language, culture, and maintenance of common borders and common colonial history enhanced the gains

Table 5. Reduction in Sensitive Lists (SL) under SAFTA

Country	SL before January 2012		SL from January 2012	
	LDC's	NLDC's	LDC's	NLDC's
Afghanistan	1072	868	850	695
Bangladesh	1233	-	987	-
Bhutan	150	-	150	-
India	480	868	25	695
Maldives	681	-	152	-
Nepal	1257	1295	998	1036
Pakistan	1169	-	936	-
Sri Lanka	1042	-	845	906

Note: (-) represents country's same tariff lines for both LDC's and NLDC's.
Source: SAARC.

of trade. Fortunately, South Asian economies are not only homogeneous in nature but also possess nearly all necessary potential which are considered as prerequisites for a successful regional economy. However, these economies are more inclined to deliberately sign independent RTAs out of the region even after knowing that it would cost other partners. Such a trend may constitute noncompliance with respect to the WTO article XXIV regarding RTAs.

Considering its importance, here is small annotation to test the trade dependence of SAARC nations within region and with the rest of the world.

Following is the equation;

$$TDI = \frac{T}{GDP} \qquad (1)$$

Where; T represents trade value that economy (1) maintains with other economies, and GDP stands for current GDP of economy (1), larger ratio denotes larger trade dependence.

Figure 1. Trade Dependence Index (TDI) of SAARC Members (2010)

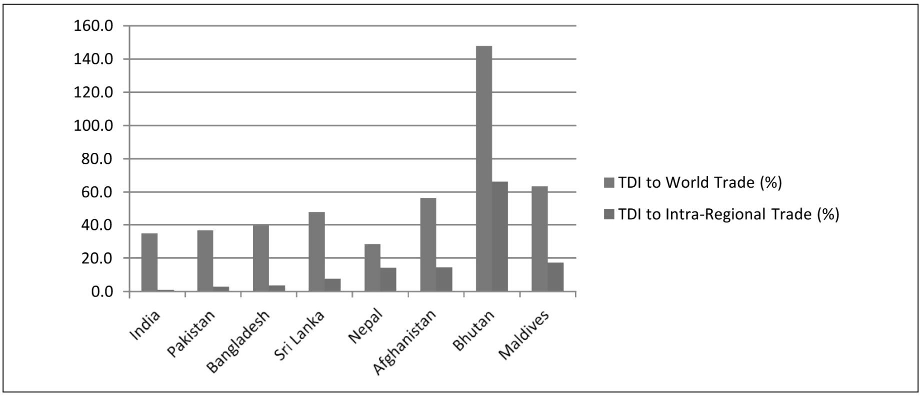

Figure 1 demonstrates the trade dependent index (TDI) of each SAARC nation to World trade and Intra-regional trade. Unfortunately, the ratio of trade dependence to intra-regional trade is very low between SAARC nations. The notion is, bigger the economy smaller the TDI ratio. India is the economic giant of the region but holds only 0.8% of TDI. Likewise, Pakistan, Bangladesh, Sri Lanka, Nepal, Afghanistan, Maldives and Bhutan has 2.8%, 3.6%, 7.7%, 14.2%, 14.3%, 17.3, and 66.2% respectively. On the other hand, the trade dependence of SAARC nations on the rest of the world is higher. Bhutan has the largest ratio of TDI around 147.8% to world trade.

VI. Collective Challenges and Conflict Resolution

Since, the Nobel Peace Prize was awarded to European Union in 2012 for maintaining peace and reconciliation among its member states and beyond, the role of regional organizations in keeping peace and conflict resolution seems significant. ASEAN[15] has generally been hailed as one of the most successful experiments in regional cooperation in the developing world, particularly in its ability to manage conflicts and maintain peace and security in Southeast Asia (Rajshree, 2003). Similarly, there are a number of studies that evaluate the role of regional blocs in conflict management as well as promotion of democracy, human rights, and poverty alleviation.

Alagappa (1995) analyzed the framework for regionalism and conflict management and emphasized that the salience of global-level security dynamic and regional dynamic should be addressed in their own terms. Vincent (2012) empirically examined how trade integration and regionalization help preserve the peace. Benjamin (2013) studied the effect of international trade on interstate conflict in the Asia-Pacific and concluded that increased trade interdependence is accompanied by reduced chances of militarized conflicts. Another study by Hegre *et al*. (2010) examined the endogeneity of trade towards the relationship between economic interdependence and the promotion of peace, and the results state that if the leaders behave rationally, the effect of trade is positive with respect to conflict management. The socioeconomic impacts of regionalism are endogenous and as a result, provide rapid solutions.

6.1. Terrorism

In recent years SAARC region has been beset by security concerns. The biggest non-economic challenge faced by region is terrorism. In the post-Cold War era, or more precisely, after the end of Afghan-Russian war, the Afghanistan that remained lost its attraction for western powers. Consequently, the country which remained 30 years in war had almost lost its physical and political infrastructure. Country descended into civil war amongst various jihadi groups and state entered a new era of violence and destruction. The repercussions of Afghan instability spread all over the SAARC region through Pakistan. Among the SAARC states, Pakistan

15) Association of South-East Asian Nations (ASEAN).

has suffered the largest economic loss due to the post-Cold War conflicts in the region.

There are also problems such as religious and ethnic extremism, drugs, and illegal weapons originating from Afghanistan spreading to the rest of the SAARC region. It is now impossible for a single country to cope this challenge individually. It needs collective response from all over the region.

6.2. Poverty

In 2008 World Bank reported that 36% of population in South Asia is living below poverty line. In 2013, SAARC reported the regional poverty profile and emphasized that 32% of the region's population lives on less than $1.25 per person a day. While World Bank stated its millennium goal to end poverty by 2030, it can never be accomplished if South Asia does not given proper attention. Poverty is one of those challenges in South Asia that has been highlighted at global and regional forums. For SAARC countries, poverty represents a big challenge which cannot be achieved without mutual support. Although SAARC dedicated year 1995 to poverty eradication, due to a combination of impractical efforts and lack of continued cooperation, poverty remains a bigger challenge even after 19 years. Ending poverty in the region, naturally, also requires a joint effort. The ASEAN model is highly effective to eradicate poverty from the SAARC region. Joint efforts at policy formulation and joint implementation constitute the easiest and shortest way for regional economies in eradicating the evil of poverty. During recent talks at the SAARC summit, poverty has been under discussion during almost all levels of talks. There were positive signs, as SAARC experienced a decade of decreasing poverty from 2006-2015. There is no doubt that regional economies are quite serious about addressing the issue of poverty because compared to the rest of Asia, South Asia still possesses the highest poverty ratio. While many developing economies were nurtured through globalization and trade liberalization, in case of the South

Asia region, the economies are still moving slowly in terms of poverty reduction.

Now, there is an urgent need to acknowledge poverty reduction as a collective goal and a strategy must be developed at a regional level; this is the only way to free SAARC region from poverty.

6.3. Environment and Disaster Management

Climate change has emerged as one of the biggest challenges of this century and its negative impacts on the planet are very alarming (Ahmed and Long, 2013a and 2014). Unfortunately, the developing countries are the most susceptible to such impacts and those impacts are already being observed in the shape of environmental degradation due to extreme weather conditions, floods, hurricanes and earthquakes (Ahmed and Long, 2013a,b). Similarly, during the last few years, many South Asian countries have been facing environmental issues stemming from changing climates in the region. Such cases include the tsunami in Sri Lanka and monsoon flood in Mumbai in 2005; and earthquakes in Kashmir in 2008, 2010 and 2011. Likewise, Pakistan experienced the worst two consecutive floods in its history, with consequent decline in agricultural output; and severe cold and warm weather affected both biodiversity and human health. The impacts of these climatic and environmental changes were felt to a greater degree due to lack of disaster management and weather forecasting system in the developing countries. As a result, in 2006 SAARC established the disaster management center in New Delhi. The climate change and its impacts are already being observed in various parts of the region, however an effective response thorough effective disaster management and forecasting system and strategically viable adaptation and mitigation techniques could minimize the impacts of these disasters on the SAARC region. This is also one of many challenges SAARC countries are facing collectively.

One of the key purposes connected to the establishment of SAARC was to achieve collective goals in a peaceful and harmonious environment. The increased trading and other socio-economic interdependence of SAARC member states lead us to anticipate active, positive results. As it can clearly be observed that increasing common physical and socio-economic challenges have brought South Asian regional economies back on track for negotiations, and the recent developments in this regard provide strong evidence. However, in SAARC, the role of India cannot be understated. It is essential to restore confidence with respect to the relationship between India and other smaller states towards the successful regional cooperation in all fields (Hanif, 2012). The normalization of Indo-Pak relations has again provides us with an opportune moment for expanding regional economic commitments in terms of trade, as well as those toward regional security, poverty alleviation, environmental challenges, water disputes and conflict management. The immediate attention, on the other hand, is required towards energy shortage in some of the SAARC economies. The long term projects to import energy through Central-Asian and the Persian Gulf region would help to eliminate overall energy shortage and to meet future requirements as well.

However, within the SAARC organization, the role of smaller countries i.e. Bangladesh and Sri Lanka cannot be ignored, as these countries are persistent in reminding everyone of the SAARC mission, in the face of constant Indo-Pak disputes. This is a positive sign that shows the serious inclination of smaller countries towards regional integration.

VII. Future Perspective: Some Concluding Remarks

The view toward regional cooperation in South Asia has always been more pessimistic due its much politicized nature. However, the South Asia region has a strong cultural and economic foundation and has been an attractive trade and business destination for many states throughout history. Today, this trade potential has increased over time but was not recognized by SAARC. For example, in terms of trade statistics, South Asian economies still show outward trade diversion. Most of their trade partners are in Europe, North America and East Asia. This trend has undergone slight change yet there are still various technical and nontechnical barriers that must be removed in order to liberalize intra-regional trade.

The trade integration in South Asia has suffered various setbacks due to non-economic barriers, which potentially point to major and inherent discrepancies within the SAARC charter. However, the members choosing economic cooperation as the primary step towards effective regional cooperation during recent rounds does represent forward progress. Optimists view this situation as increasing economic interests through trade integration amongst member states producing mutual stakes in the region and these increasing stakes would further convince members to resolve all extant issues through dialogues. This will not only speed up the regionalization process, but also help to create vibrant and prosperous regional association.

The increasing threat of terrorism, environmental change, natural calamities, improper water management, and poverty ratio has provided additional impetus to compel the members to combat these common problems collectively. The substantial reduction in list of goods and improved bilateral relations between Pakistan and India will positively influence the process as a whole. This may also attract the neighboring economies and build confidence in the region. In the light of recent development, it is highly desirable to connect this SAARC regional bloc with East Asian nations. SAARC may follow the other regional organizations i.e. EU and ASEAN in resolving their longstanding political and geographical conflicts. Such a step would help to create a harmonious environment between member states and will further spread the beneficial effects, both economic and social, throughout the region.

Last few years have been some of the most active in the history South Asian economic cooperation. The enthusiasm of member states has strengthened both economic and political ties within region which was initially desired at the time of foundation of SAARC. Undoubtedly, it is just beginning, but if this process continues with the same momentum, it will definitely lead to positive outcomes for whole South Asian region.

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3

India-Korea CEPA: Analysis of Industrial Competitiveness and Environmental Implications

Sudhakar Yedla[1)]

I. Introduction

The Indian economy, which remained inward looking and resorted to import substituting economic policies in the past, has opened doors to international markets during a decade long economic reforms that took place in the 1990's. Since then, the outlook for India in international trade has changed and has come a long way, with current exports and imports at 330 billion USD and 480 billion USD, respectively. However, India's share of international trade is abysmal and need to be augmented further and deeper if the Indian dreams of becoming a developed nation were to come true. While the West has traditionally been a strong trade partner, Indian government is now looking towards East Asia for improved trade prospects. The Comprehensive Economic Partnership Agreement (CEPA) between India and Korea and also between India and Japan are a few such steps towards increased trade

1) Professor, Indira Gandhi Institute of Development Research (IGIDR).

with East Asian countries.

The work presented in this paper analyses the positive impact of the India-Korea CEPA on trade flow between these two countries, effect on the competitiveness of firms both in India and Korea by employing Revealed Comparative Advantage (RCA) and Relative Trade Advantage (RTA) methods. It explores related issues further, including negative effects of the India-Korea CEPA on the environment and natural resources, and develops a framework of impact assessment for a future and comprehensive study on environmental impacts of CEPA. The paper explains, in qualitative terms, such possible negative impacts of India-Korea CEPA, and argues that such externalities from bilateral trade need to be internalized in order to have the benefits of improved trade trickle down to the lower strata of the society on equitable terms.

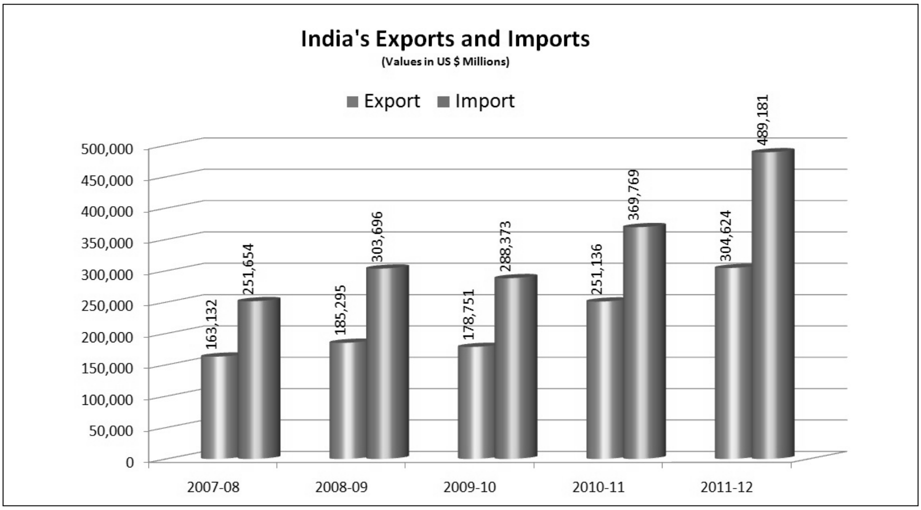
II. Pattern of Trade between India and the Republic of Korea

2.1. Export and Import Pattern for India and Korea during 2009-2013

Economic prosperity of a country depends a lot on its international trade strategies. India during its pre-economic reform period suffered from import substitution policies and not taking advantage of post-war trading opportunities in the world. The set of economic reforms that took place in India during 90's and increased globalization has resulted in an improved investment relationship between India and Korea.

To this effect India has been part of various multi-lateral trade organizations such as World Trade Organization (WTO), International Monitory Fund (IMF), and the Doha round in WTO. Further, there are various regional initiatives among ASEAN, SAARC and bilateral cooperation with China, Korea and Japan. With these trade agreements, Indian exports and imports have increased significantly in the last two decades. The present pattern of Indian exports and imports are

Figure 1. Total Indian Exports and Imports during 2007-2012



Source: Extracted from Economic Survey 2013-14, Government of India.

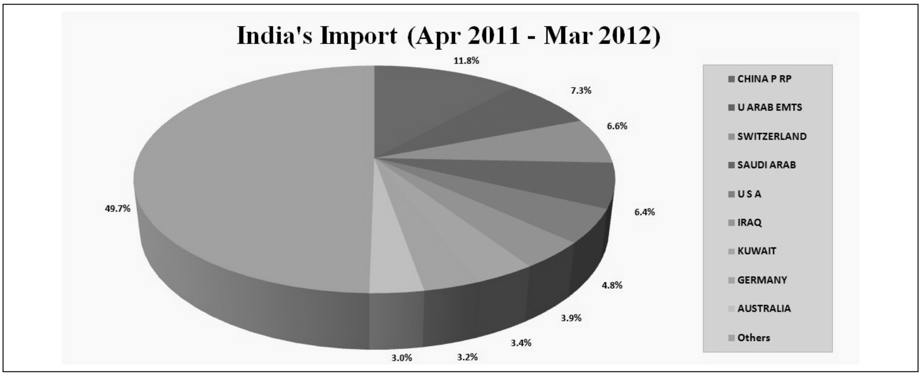
presented in Figures 1 to 5, extracted from the Recent Economic Survey of India.

The United Arab Emirates, USA and Singapore lead the list of Exports with a major share accounted for by these countries. The bulk of India's imports come

Figure 2. Details of Indian Exports to Different Countries

Source: Extracted from Economic Survey 2013-14, Government of India.

Figure 3. Details of Indian Imports from Different Countries

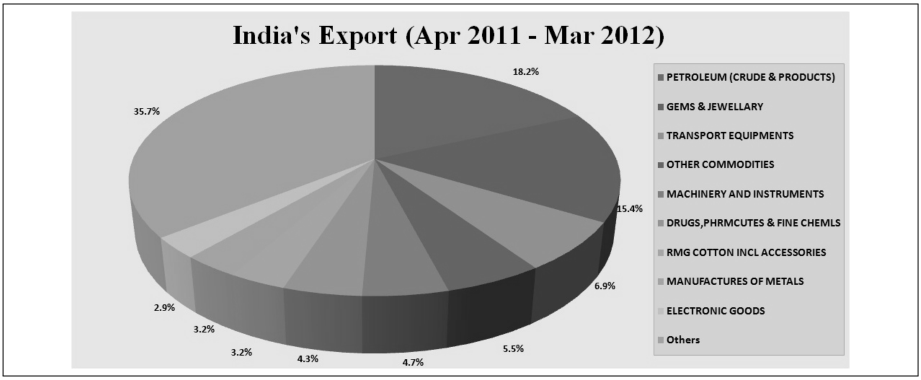


Source: Extracted from Economic Survey 2013-14, Government of India.

from China, UAE, Switzerland, Saudi Arabia and USA. These patterns are shown in Figure 2 and 3.

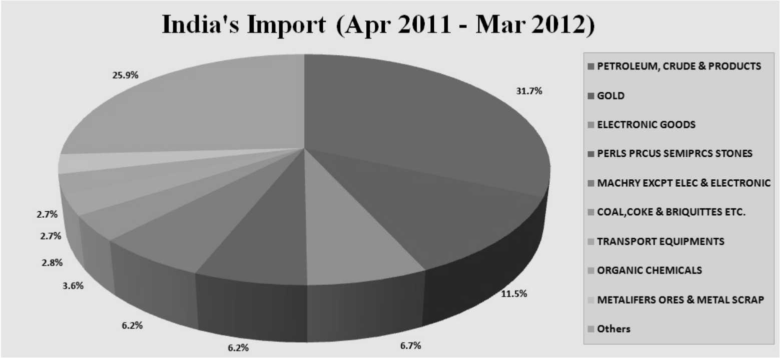
Petroleum, Gems & Jewellery, transport equipment led Indian exports to countries as listed above. Indian imports are dominated by petroleum, gold, pearls, machinery and transport equipment. These trends and patterns are presented in Figure 4 and 5.

Figure 4. Details of Indian Exports of Different Products



Source: Extracted from Economic Survey 2013-14, Government of India.

Figure 5. Details of Indian Imports of Different Products



Source: Extracted from Economic Survey 2013-14, Government of India.

Grouping of Export and Import Product

HS Group	Classification (HS 2007 Code)	Product Description
I	1~10	Agriculture and Fisheries Products
II	11~24	Food Products and Beverages
III	25~28	Mining
IV	29~40	Chemical
V	41~43	Rubber
VI	44~49	Timber and Paper
VII	50~67	Textile
VIII	68~71	Non-ferrous Metal
IX	72~83	Basic Metal Products
X	84	General Machinery & Equipment
XI	85	Electronic Equipment and Components
XIII	87	Automobiles
XII	86,88~89	Other Transport Equipment
XIV	90~91	Precision Machinery Products
XV	92~97	Other Industrial Products
XVI	98~99	Others

The India-Korea bilateral trade has taken a boost with both countries signing the Comprehensive Economic Partnership Agreement (CEPA), which allows for reducing non-tariff barriers, liberalizing trade in the services sector, enhancing cooperation in investment, and economic cooperation. Tables 1 and 2 present the pattern of exports and imports between India and Korea during the period 2009-2013. The products traded are clustered into sixteen groups based on the HS code (2007). The following table presents such clustering which is used for further analysis in this study.

Korean share of global exports has increased from 3.49 to 5.40, which indicate the growth of Korean economy in international trade. The share of Korea in global imports has remained constant except a steep increase in the year 2013. Korean exports to India have almost doubled during the last 6 years which indicates an increasing bilateral trade activity between these important countries in the region. Korea's imports from India have seen a 50% rise during the same period. Though the share of Korean exports to India to its overall exports has increased during the analysis period, it is still stands at a mere 2.03%. Imports from India are even more meagre, with only 1.2% of Korean imports coming from India. This presents a great potential for trade between these two nations.

Indian exports in general have doubled during the analysis period with its share in global export rising from 1.59 to 3.25%, a hundred percent increase. Indian imports have seen an increase from 2.43% to almost 4% as a share of global imports. Indian exports to Korea and imports from Korea have increased during the analysis period but the percentage share in overall exports and imports has declined, which indicated that the even more active international trade with other partner countries. Share of Indian exports to Korea has been lower than the imports from Korea.

Indian exports to Korea are traditionally dominated by groups such as Mining, Chemicals, Textiles, non-ferrous metal, basic metal products, food & beverage and general equipment & machinery. Over the period of analysis the agriculture and fisheries products have grown by over 10 times, becoming one of the dominant

Table 1. Pattern of Korean Exports and Imports from India during 2007-2013

Korean Exports and Imports from India

Year	World Total Exports (1000 USD)	Total Korean Exports (1000 USD)	Share in the Global Exports (%)	Exports to India	Ratio	Total World Imports (1000 USD)	Total Korean Imports (1000 USD)	Share in the Global Imports (%)	Imports from India	Ratio
2007	10639608799	371477104	3.49	6600039	1.78	11202055457	356,541,365	3.18	4,624,421	1.30
2008	13588239677	422003479	3.11	8977063	2.13	14608035389	435,309,586	2.98	6,581,241	1.51
2009	11080294474	363531064	3.28	8013290	2.20	11722874822	323,143,782	2.76	4,141,622	1.28
2010	13566467034	466591351	3.44	11434596	2.45	14409044427	425,649,574	2.95	5,674,456	1.33
2011	16476684255	555666036	3.37	12654078	2.28	17330468017	524,894,383	3.03	7,893,573	1.50
2012	16198369763	547770061	3.38	11922037	2.18	17223594505	519,510,795	3.02	6,920,826	1.33
2013	10349268517	559121437	5.40	11375792	2.03	11675138718	515,720,226	4.42	6,180,152	1.20

Source: Calculated by the author using data from World Integrated Trade Solutions (WITS) of the World Bank.

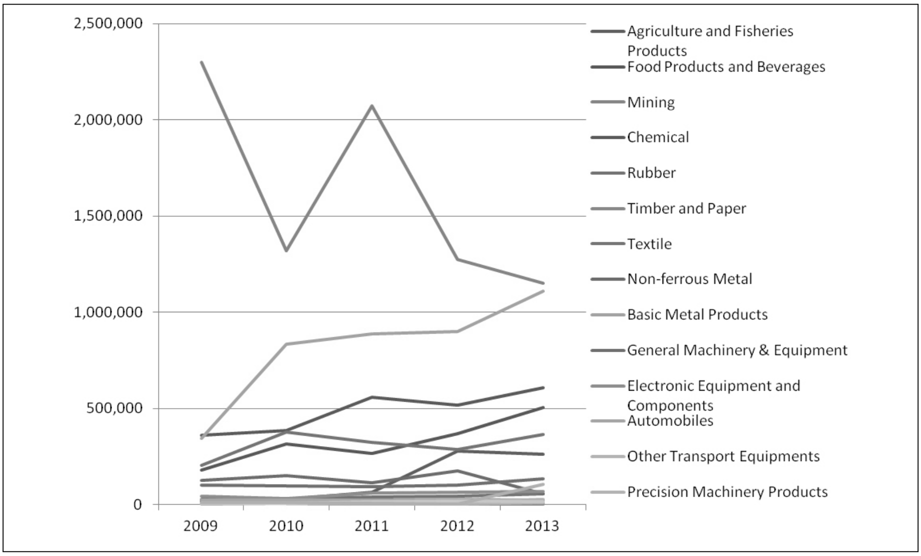
Table 2. Pattern of Indian Exports and Imports from Korea during 2009-2013

Indian Exports and Imports from Korea

Year	World Total Exports (1000 USD)	Total Indian Exports (1000 USD)	Share in the Global Exports (%)	Exports to Korea	Ratio	Total World Imports (1000 USD)	Total Imports	Share in the Global Imports (%)	Imports from Korea	Ratio
2009	11080294474	176,722,587	1.59	3,772,265	2.13	11722874822	266,401,554	2.27	8,229,752	3.09
2010	13566467034	220,408,496	1.62	3,634,463	1.65	14409044427	350,173,258	2.43	9,922,318	2.83
2011	16476684255	301,483,251	1.83	4,549,869	1.51	17330468017	462,397,821	2.67	12,362,469	2.67
2012	16198369763	289,434,140	1.79	4,076,363	1.41	17223594505	488,645,826	2.84	13,675,088	2.80
2013	10349268517	336,611,389	3.25	4,495,540	1.34	11675138718	465,887,034	3.99	12,426,660	2.67

Source: Calculated by the author using data from World Integrated Trade Solutions (WITS) of the World Bank.

Figure 6. Trends of Indian Exports Groups to Korea during 2009-2013



Source: Calculated by the author using data from World Integrated Trade Solutions (WITS) of the World Bank.

export commodities along with the traditionally dominant groups. Non-ferrous metal and mining groups, on the other hand, have shown a declining trend. Trends are shown in Table 3 and Figure 6.

Traditionally Korean exports to India are dominated by manufacturing products such as electronics, mechanical and transport equipment, steel and chemicals and these products represent a large share in Korea's exports to India. In the year 2009 Korean exports to India were dominated by groups including chemicals, basic metal products, general machinery & equipment, electronic equipment and components and automobiles. Korean exports to India have seen a high growth during 2009-13 in rubber products, non-ferrous metals and chemicals while trends remained unchanged for other traditionally dominant groups. Though continuing its dominance in exports, automobiles group has shown a negative trend in exports to India. Table 4 and Figure 7 present these trends reflected in Korean exports to India.

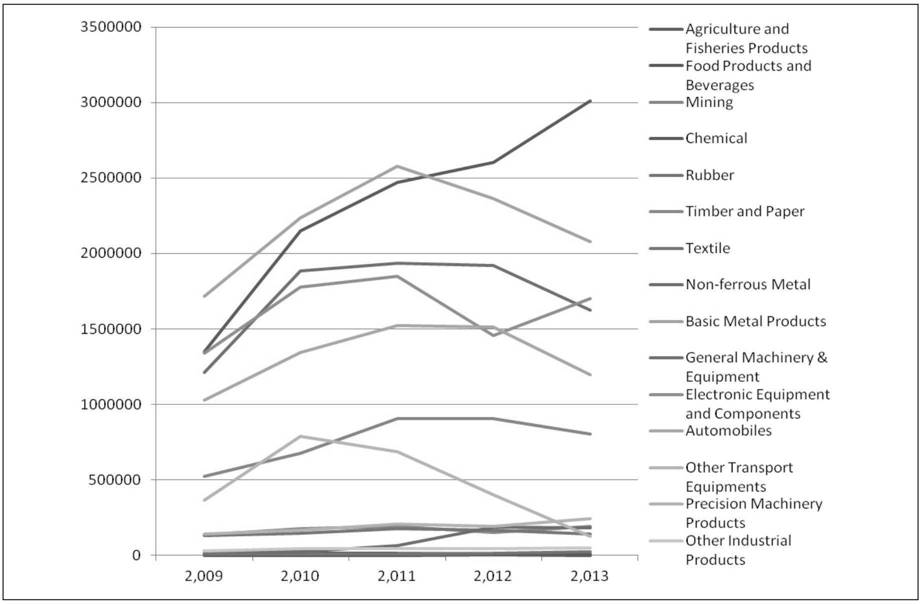
Table 3. Pattern of Growth in Indian Exports to Korea at a Product Grouping Level during 2009-2013

Indian Export (1000 USD) to Korea with Details at a Level of Grouping of Products

Group	Product Category	Year					Percentage Change between 2009-2013
		2009	2010	2011	2012	2013	
I	Agriculture and Fisheries Products	20,501	26,477	66,075	279,033	262,635	1181.11
II	Food Products and Beverages	181,178	315,586	267,069	367,734	504,392	178.40
III	Mining	2,299,985	1,321,420	2,073,534	1,275,568	1,151,188	-49.95
IV	Chemical	361,709	384,660	559,788	516,676	608,226	68.15
V	Rubber	28,095	30,520	39,585	44,774	57,588	104.98
VI	Timber and Paper	8,110	7,390	4,064	2,831	2,580	-68.19
VII	Textile	206,141	378,131	325,034	286,845	366,278	77.68
VIII	Non-ferrous Metal	126,360	149,128	113,157	175,355	55,310	-56.23
IX	Basic Metal Products	344,113	833,170	885,381	901,410	1,108,875	222.24
X	General Machinery & Equipment	102,891	96,528	93,472	100,239	133,806	30.05
XI	Electronic Equipment and Components	42,437	30,899	60,779	62,235	70,394	65.88
XIII	Automobiles	23,588	22,341	23,072	27,030	22,414	-4.98
XII	Other Transport Equipments	4,179	7,304	1,127	733	8,784	110.20
XIV	Precision Machinery Products	8,494	11,844	16,832	13,485	26,439	211.27
XV	Other Industrial Products	5,331	6,819	13,621	21,072	12,906	142.08
XVI	Others	9,153	12,245	7,280	1,344	103,725	1033.30
Total		**3,772,265**	**3,634,463**	**4,549,869**	**4,076,363**	**4,495,540**	**19.17**

Source: Calculated by the author using data from World Integrated Trade Solutions (WITS) of the World Bank.

Figure 7. Trends of Korean Exports Groups to India during 2009-2013



Source: Calculated by the author using data from World Integrated Trade Solutions (WITS) of the World Bank.

India imports huge amount of mining products, chemicals, basic metal products, general machinery & equipment, electronic equipment & components, automobiles and other transport equipment. While the same level of imports continued for the listed groups in 2013, chemicals products have registered a rapid growth. Non-ferrous metal products are also gaining momentum. These trends are presented in Table 5 and Figure 8 (1000 USD on Y axis).

Korean imports from India are strongly dominated by mining group followed by chemicals, textile, non-ferrous metals and basic metal products. Basic metal products and rubber have shown significant increase while non-ferrous metals declined by 76 percent. Mining group has shown a sharp rise in imports but fell back to its original level by 2013. Trends of Korean imports from India are presented in Table 6 and Figure 9 (1000 USD on Y axis).

Table 4. Pattern of Growth in Korean Exports to India at a Product Grouping Level during 2009-2013

Korean Export (1000 USD) to India with Details at a Level of Grouping of Products							
Group	Product Category	Year					
		2009	2010	2011	2012	2013	Percentage Change between 2009-2013
I	Agriculture and Fisheries Products	296	174	215	823	247	-16.47
II	Food Products and Beverages	10,904	11,998	13,131	8,786	9,398	-13.82
III	Mining	524,462	675,213	907,338	903,358	802,884	53.09
IV	Chemical	1,351,328	2,147,981	2,469,318	2,600,881	3,011,267	122.84
V	Rubber	7,022	7,850	8,673	15,254	21,268	202.89
VI	Timber and Paper	138,236	176,579	190,107	152,413	191,469	38.51
VII	Textile	129,153	147,371	175,188	165,375	142,872	10.62
VIII	Non-ferrous Metal	26,539	22,778	62,161	186,473	180,693	580.86
IX	Basic Metal Products	1,716,935	2,237,315	2,575,660	2,362,491	2,077,177	20.98
X	General Machinery & Equipment	1,211,243	1,885,408	1,937,731	1,920,521	1,624,387	34.11
XI	Electronic Equipment and Components	1,337,172	1,775,912	1,850,858	1,457,996	1,699,099	27.07
XIII	Automobiles	1,028,093	1,343,626	1,524,346	1,511,836	1,194,114	16.15
XII	Other Transport Equipments	364,008	790,350	686,275	399,949	127,313	-65.02
XIV	Precision Machinery Products	138,721	167,148	207,048	189,672	240,290	73.22
XV	Other Industrial Products	29,178	44,893	46,029	44,548	51,508	76.53
Total		**8,013,290**	**11,434,596**	**12,654,078**	**11,922,037**	**11,375,792**	**41.96**

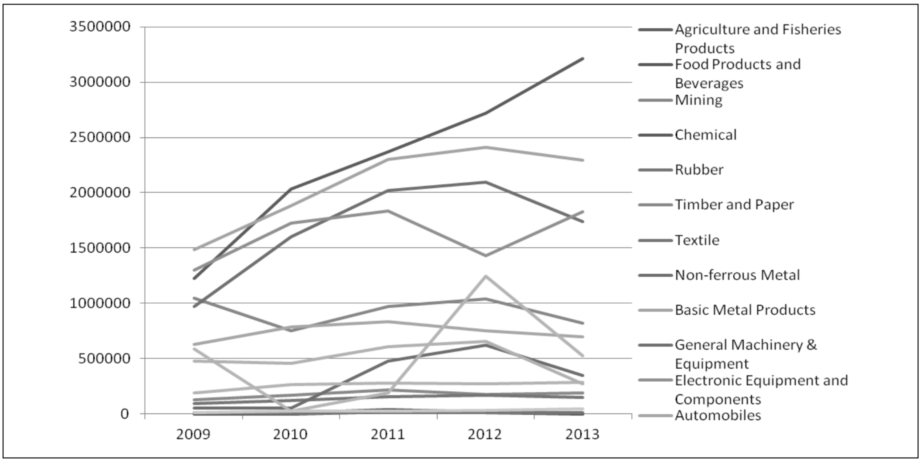
Source: Calculated by the author using data from World Integrated Trade Solutions (WITS) of the World Bank.

Table 5. Pattern of Growth in Indian Imports from Korea at Product Grouping Level during 2009-2013

Indian Imports (1000 USD) from Korea with Details at Level of Grouping of Products							
Group	Product Category	Year					Percentage Change between 2009-2013
		2009	2010	2011	2012	2013	
I	Agriculture and Fisheries Products	440	770	16,330	9,030	32	-92.72
II	Food Products and Beverages	7,076	10,008	41,388	17,191	8,094	14.38
III	Mining	1,049,113	755,564	973,748	1,041,789	822,072	-21.64
IV	Chemical	1,228,130	2,035,775	2,372,436	2,722,800	3,213,554	161.66
V	Rubber	8,568	7,721	15,644	14,622	9,856	15.04
VI	Timber and Paper	126,395	169,359	214,856	179,372	191,614	51.60
VII	Textile	96,451	121,297	158,436	169,872	147,907	53.35
VIII	Non-ferrous Metal	56,438	56,101	475,308	624,029	347,297	515.36
IX	Basic Metal Products	1,483,693	1,881,424	2,300,629	2,408,835	2,293,079	54.55
X	General Machinery & Equipment	972,576	1,600,493	2,022,543	2,094,664	1,737,217	78.62
XI	Electronic Equipment and Components	1,299,533	1,722,587	1,837,495	1,433,422	1,827,801	40.65
XIII	Automobiles	630,620	784,427	831,562	753,245	697,776	10.65
XII	Other Transport Equipments	588,858	28,551	187,811	1,246,052	527,610	-10.40
XIV	Precision Machinery Products	191,533	264,711	277,713	274,715	288,437	50.59
XV	Other Industrial Products	13,334	28,178	25,947	31,034	45,129	238.45
XVI	Others	476,994	455,352	610,625	654,415	269,186	-43.57
Total		**8,229,752**	**9,922,318**	**12,362,469**	**13,675,088**	**12,426,660**	**51.00**

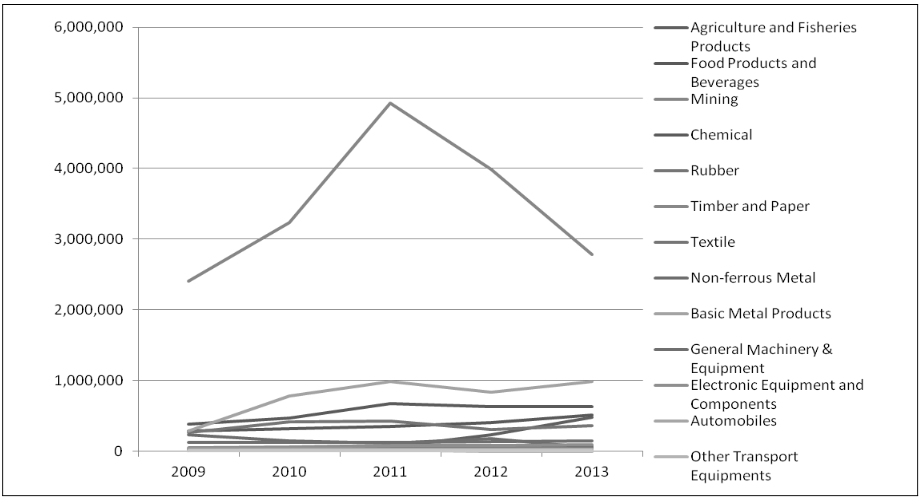
Source: Calculated by the author using data from World Integrated Trade Solutions (WITS) of the World Bank.

Figure 8. Trends of Indian Imports Groups from Korea during 2009-2013



Source: Calculated by the author using data from World Integrated Trade Solutions (WITS) of the World Bank.

Figure 9. Trends of Korean Imports Groups from India during 2009-2013



Source: Calculated by the author using data from World Integrated Trade Solutions (WITS) of the World Bank.

Table 6. Pattern of Growth in Korean Imports from India at Product Grouping Level during 2009-2013

Korean Imports (1000 USD) from India with Details at a Level of Grouping of Products

Group	Product Category	Year					Percentage Change between 2009-2013
		2009	2010	2011	2012	2013	
I	Agriculture and Fisheries Products	28,257	32,453	62,109	237,722	477,756	1590.78
II	Food Products and Beverages	289,275	313,721	355,161	403,041	513,374	77.47
III	Mining	2,406,049	3,236,722	4,926,513	3,984,579	2,783,502	15.69
IV	Chemical	381,785	468,501	671,997	628,981	634,756	66.26
V	Rubber	32,775	40,432	57,648	61,981	69,436	111.85
VI	Timber and Paper	8,681	11,482	9,857	5,692	2,906	-66.52
VII	Textile	265,232	411,617	426,869	312,794	365,193	37.69
VIII	Non-ferrous Metal	232,521	144,861	116,862	175,784	53,675	-76.92
IX	Basic Metal Products	281,778	776,670	982,813	834,713	981,713	248.40
X	General Machinery & Equipment	122,211	124,720	124,538	138,056	149,384	22.23
XI	Electronic Equipment and Components	53,434	59,028	78,496	84,120	89,785	68.03
XIII	Automobiles	24,094	25,983	29,340	26,971	24,066	-0.11
XII	Other Transport Equipments	10,959	2,215	21,768	1,264	741	-93.24
XIV	Precision Machinery Products	4,568	17,934	19,997	16,686	24,066	426.85
XV	Other Industrial Products	8119	8,118	9,602	8,338	9,798	20.68
Total		**4,149,740**	**5,674,456**	**7,893,573**	**6,920,826**	**6,180,152**	**48.93**

Source: Calculated by the author using data from World Integrated Trade Solutions (WITS) of the World Bank.

III. Comprehensive Economic Partnership Agreement (CEPA) –Basic Constructs and Key Features

India and Korea share a long term friendship, social commonalities and trade relationship. Though the quantum of trade between these two Asian countries is small, consistent growth has been observed over the years. Realizing these facts and the promise that these growing countries hold for each other, potential advantages of a comprehensive economic partnership agreement (CEPA) were pointed out by a joint study group in 2005 and led to the final approval of the India-Korea CEPA. The Cabinet approved the signing of a Comprehensive Economic Partnership Agreement (CEPA) with South Korea.

India-Korea CEPA comprises of six Agreements such as Agreement on Trade in goods; Rules of Origin and Origin Procedures; Trade Facilitation and Customs Cooperation; Trade in Services including Specific Commitments; Investment and Dispute Settlement. The CEPA was finally signed in 2009 and came into effect in 2010 with the objectives as presented in Box 1. It has provisions for substantial cuts in both tariff and non-tariff barriers and this would have to be implemented in phases. Tariffs would be reduced or eliminated on 93 percent of Korea's tariff lines and 85 percent of India's tariff lines. Details of the percentage tariff reduction schedule both for India's tariff lines and Korean tariff lines are given in Box 2. Box 1 is reproduced from CEPA (2009) and MPRA (2010).

Apart from trade in goods, CEPA opens up a whole range of services for India. Limitations have been removed in Architectural, financial and audio-visual services. Korea also offered commitments under Mode 4 regarding independent professionals, which it has not offered in any other bilateral agreement or at the WTO.

Box 1. Objectives of Comprehensive Economic Partnership Agreement (CEPA)

Chapter One
General Provisions and Definitions

Article 1.1: Objectives

The objectives of this Agreement, as elaborated more specifically through its principles and rules are to:

(a) Liberalize and facilitate in goods and services and expand investment between the Parties;

(b) Establish a cooperative framework for strengthening and enhancing the economic relations between Parties;

(c) Establish a framework conductive for a more favourable environment for their business and promote conditions of fair competition in the free trade area;

(d) Establish a framework of transparent rules to govern trade and investment between the Parties;

(e) Create effective procedures for the implementation and application of this Agreement;

(f) Explore new areas of economic cooperation and develop appropriate measures for closer economic partnership between the Parties;

(g) Improve the efficiency and competitiveness of their manufacturing and services sectors and expand trade and investment between the Parties; and

(h) Establish a framework for further regional and multilateral cooperation to expand and enhance the benefits of this Agreement throughout Asia, and thereby, to encourage the economic integration of Asian economies.

Box 2. Details of Tariff Reduction Schemes for India and Korean Tariff Lines

Percentages of Annual Tariff Reduction for Korea

Category	Entry into Force	Jan 1 Year 1	Jan 1 Year 2	Jan 1 Year 3	Jan 1 Year 4	Jan 1 Year 5	Jan 1 Year 6	Jan 1 Year 7
E-0	100%							
E-5	20%	40%	60%	80%	100%			
E-8	12.5%	25%	37.5%	50%	62.5%	75%	87.5%	100%
RED	12.5% of [Base Rate (in %s) minus 1~5%]	25% of [Base Rate (in %s) minus 1~5%]	37.5% of [Base Rate (in %s) minus 1~5%]	50% of [Base Rate (in %s) minus 1~5%]	62.5% of [Base Rate (in %s) minus 1~5%]	75% of [Base Rate (in %s) minus 1~5%]	87.5% of [Base Rate (in %s) minus 1~5%]	100% of [Base Rate (in %s) minus 1~5%]
SEN	6.3%	12.5%	18.8%	25%	31.3%	37.5%	43.8%	50%

Percentages of Annual Tariff Reduction for India

Category	Entry into Force	Jan 1 Year 1	Jan 1 Year 2	Jan 1 Year 3	Jan 1 Year 4	Jan 1 Year 5	Jan 1 Year 6	Jan 1 Year 7	Jan 1 Year 8	Jan 1 Year 9
E-0	100%									
E-5	20%	40%	60%	80%	100%					
E-8	12.5%	25%	37.5%	50%	62.5%	75%	87.5%	100%		
RED	12.5% of [Base Rate (in %s) minus 1~5%]	25% of [Base Rate (in %s) minus 1~5%]	37.5% of [Base Rate (in %s) minus 1~5%]	50% of [Base Rate (in %s) minus 1~5%]	62.5% of [Base Rate (in %s) minus 1~5%]	75% of [Base Rate (in %s) minus 1~5%]	87.5% of [Base Rate (in %s) minus 1~5%]	100% of [Base Rate (in %s) minus 1~5%]		
SEN	5%	10%	15%	20%	25%	30%	35%	40%	45%	50%

IV. Impacts of CEPA on Trade between India and Korea

4.1. Effect on Industrial Competitiveness in India and Korea by Revealed Comparative Advantage (RCA) Method of Analysis

4.1.1 Industrial Competitiveness by Revealed Comparative Advantage (RCA)

In the present days' globalized world and international trade, it is important for the countries to be competitive in order to maintain a healthy level of exports. This is particularly so for a fast growing economy like India.

The comparative advantage in trade is traditionally addressed by Ricardian theory and the Heckscher-Ohlin (H-O) theory. While the earlier theory is based on “comparative advantage” arising out of technological difference across countries, the later is based on cost differences resulting from difference in factor process across countries. Complication of applying these classical techniques is the need for the pre-trade relative process data across countries. Given the difficulties in applying these “absolute” measures to find the comparative advantages, Balassa (1965) has proposed a method where comparative advantages are revealed in the trade patterns. Refereeing comparative advantage from observed trade data is termed as "Revealed Comparative advantage (RCA). Popularly used to analyse trade data, Balassa method derives an index that measures the comparative advantage for any country. Balassa index explains whether a country has any revealed comparative advantage by observing the trade patterns. Following is the expression developed by Balassa for RCA:

$$RCA = \left({}^{X_{ji}}/_{X_{ti}} \right) \Big/ \left({}^{X_{jn}}/_{X_{tn}} \right)$$

$$RCA = \left({}^{X_{ji}}/_{X_{jn}} \right) \Big/ \left({}^{X_{ti}}/_{X_{tn}} \right)$$

Where	X	exports
	i	country
	j	commodity
	t	set of commodities
	n	set of countries

RCA effectively measures a country's export of a commodity relative to its total exports and to the corresponding exports of a set of countries such as EU, Asia, ASEAN, global etc. The same can be applied to bilateral conditions as well. RCA values greater than unity (RCA > 1) reveal a comparative advantage in the commodity/industry ‘j’ for the country ‘i’ and values less than one (RCA < 1) reveals a comparative disadvantage.

The above equation was used to calculate the relative comparative advantage of India and Korea for various trade commodities against world exports and imports. Table 7 and 8 and Figure 10 and 11 present the trends of RCA values both for Korea and India. Indian firms have shown relative advantage over the world by means of high RCA values for agriculture & fisheries, mining, rubber, textiles, non-ferrous metal. Non-ferrous metal group has been showing tremendous advantage on global scale. The comparative advantage of agriculture and fisheries, and mining has improved by 2013. Though it has remained competitive, the comparative advantage of Rubber dipped during 2010-11 and then improved subsequently. Textiles have gained more relative advantage towards 2013. Non-ferrous metals, though maintaining a high level of advantage, its intensity has declined drastically. Basic metal industries, which was at a relative disadvantage in 2009 has become a group with relative advantage group in 2013. Other automobile equipment group is slowly moving towards being relatively advantageous. Other than basic metal industries, no other group in India has transformed from a disadvantage to advantage on relative terms.

Korean firms showed comparative advantage in basic metal products, general machinery & equipment, electronic equipment & components, automobiles, other transport equipment, and precision machinery with electrical equipment group and

Table 7. Revealed Comparative Advantage of Indian Firms to the World

Group	Year									
	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
I	2.04	1.93	1.71	1.84	1.63	1.27	1.34	1.47	1.82	1.75
II	1.02	0.85	1.06	1.16	1.19	0.67	0.83	0.96	1.30	0.80
III	1.21	1.26	1.33	1.82	1.47	1.28	1.43	1.16	1.19	1.51
IV	0.99	0.99	1.05	0.93	1.02	0.80	0.84	0.86	0.99	0.85
V	2.99	2.61	2.48	2.4	2.4	2.09	1.75	1.74	1.77	2.57
VI	0.2	0.22	0.21	0.2	0.21	0.19	0.20	0.20	0.23	0.21
VII	3.3	3.21	3.18	3.13	2.83	2.59	2.64	2.43	2.51	3.69
VIII	5.65	5.68	4.58	4.66	3.65	5.56	4.26	4.21	3.81	3.08
IX	1.35	1.33	1.38	1.22	1.24	0.96	1.29	0.90	1.03	1.02
X	0.27	0.29	0.3	0.29	0.34	0.32	0.30	0.30	0.33	0.35
XI	0.19	0.19	0.23	0.24	0.32	0.44	0.32	0.35	0.33	0.38
XIII	0.3	0.34	0.34	0.3	0.4	0.43	0.54	0.45	0.54	0.40
XII	0.23	0.21	0.21	0.19	0.2	0.83	0.86	1.12	0.93	0.91
XIV	0.22	0.31	0.3	0.43	0.91	0.21	0.20	0.19	0.21	0.20
XV	0.49	0.45	0.44	0.18	0.12	0.28	0.30	0.30	0.33	0.44
XVI						1.94	0.93	2.60	0.28	0.40

Note: RCA values for 2004-08 are collected from the literature and RCA values from 2009 to 2013 are calculated by the author using data from World Integrated Trade Solutions (WITS) of the World Bank.

other automobile machinery group dominating the list. Relative comparative advantage of basic metal products, general machinery, electronic equipment and other transport has shown growing trends between 2009 and 2013, and automobile group and precision equipment groups have registered a declining trend though remaining relatively competitive. General machinery and chemical product groups are relatively disadvantaged but are moving closer toward relative advantage.

Figure 10. Patterns of Revealed Comparative Advantage of Indian Firms to the World

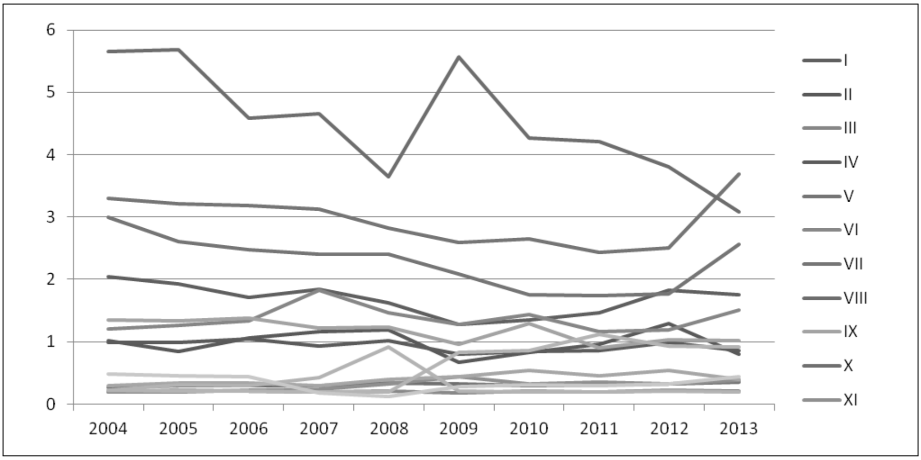


Figure 11. Patterns of Revealed Comparative Advantage of Korean Firms to the World

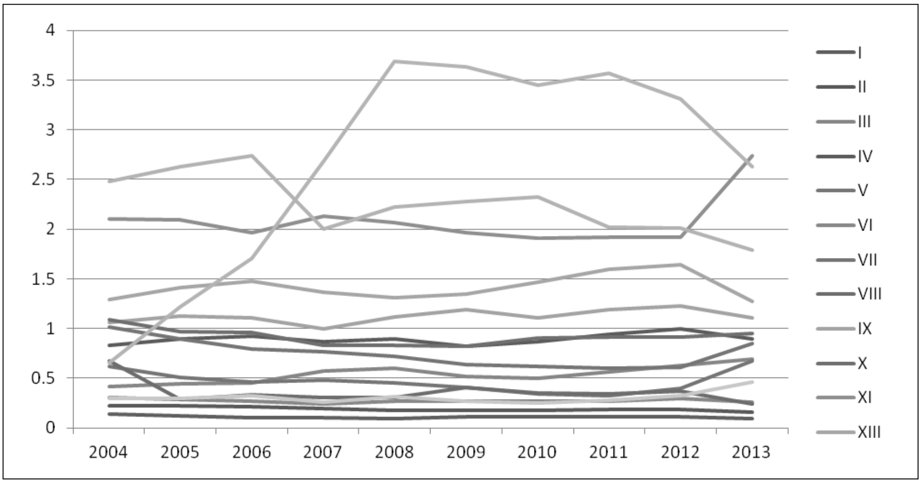


Table 8. Revealed Comparative Advantage of Korean Firms to the World

HS Unit Based Category										
	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
I	0.14	0.12	0.1	0.10	0.10	0.11	0.11	0.11	0.11	0.09
II	0.22	0.22	0.21	0.19	0.17	0.17	0.18	0.19	0.19	0.16
III	0.42	0.44	0.45	0.58	0.60	0.51	0.50	0.56	0.63	0.70
IV	0.83	0.9	0.92	0.87	0.90	0.82	0.86	0.94	0.99	0.89
V	0.62	0.51	0.46	0.48	0.46	0.41	0.34	0.32	0.40	0.67
VI	0.31	0.29	0.27	0.24	0.27	0.27	0.27	0.27	0.29	0.26
VII	1.02	0.9	0.79	0.76	0.72	0.64	0.62	0.60	0.61	0.85
VIII	0.67	0.29	0.33	0.31	0.31	0.41	0.35	0.35	0.37	0.24
IX	1.06	1.13	1.11	1.00	1.11	1.19	1.11	1.19	1.23	1.11
X	1.09	0.97	0.96	0.83	0.83	0.83	0.90	0.92	0.92	0.95
XI	2.1	2.09	1.96	2.13	2.07	1.96	1.91	1.92	1.92	2.74
XIII	1.29	1.41	1.48	1.37	1.31	1.35	1.47	1.59	1.64	1.27
XII	0.66	1.22	1.71	2.69	3.69	3.63	3.45	3.57	3.31	2.63
XIV	2.48	2.63	2.74	2.01	2.22	2.27	2.32	2.02	2.01	1.79
XV	0.3	0.3	0.32	0.26	0.31	0.27	0.25	0.28	0.33	0.47
XVI				0.00	0.00	0.00	0.00	0.00	0.00	0.00

Note: RCA values for 2004-06 are collected from the literature and RCA values from 2007-13 are calculated by the author using data from World Integrated Trade Solutions (WITS) of the World Bank.

Relative comparative advantage for various commodities is compared between India and Korea for the year 2009. This comparison discussed above is presented in Figure 12. The industries that are at a comparative advantage and their respective level of exports both from India and Korea are presented below:

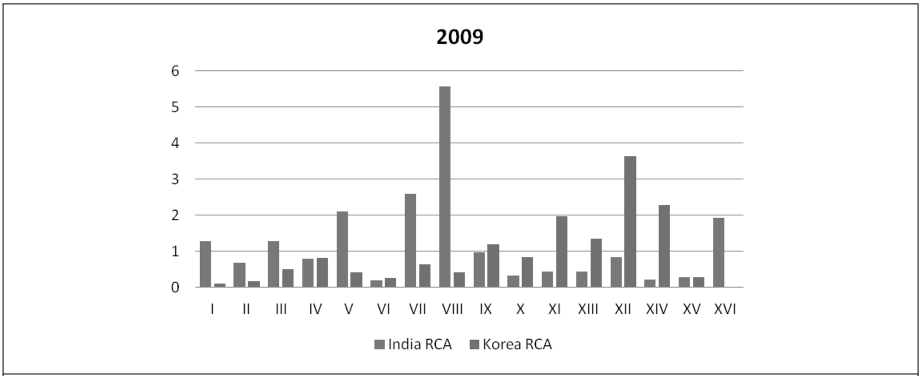
India:

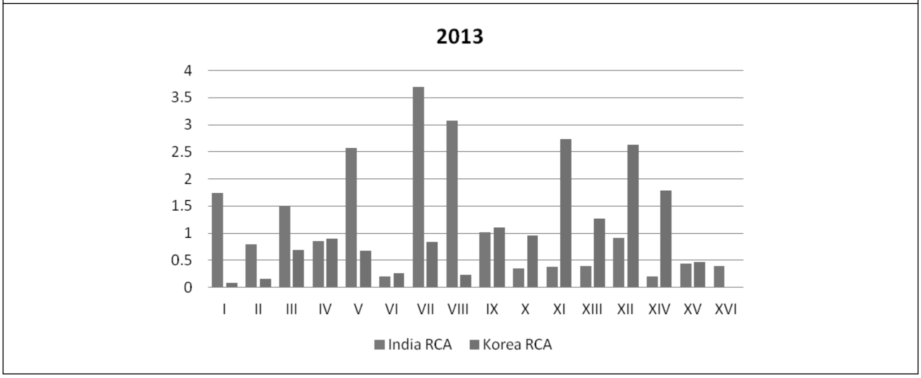
Industry Group	Intensity of Export
I	Low
III	Very High
V	Very Low
VII	Low
VIII	Very Low
IX	Very High

Korea:

Industry Group	Intensity of Export
IX	Very High
X	High
XI	Very High
XII	Very Low
XIII	High
XIV	Very Low

Figure 12. Comparison of RCA of Various Products for India and Korea against the World





4.2. Effect on Industrial Competitiveness in India and Korea by Relative Trade Advantage (RTA) Method of Analysis

Balassa's index considers exports only whereas the actual trade performance needs to include imports as well. Accordingly Vollrath (1991) has proposed an alternative way of measurement for a country's Revealed Comparative Advantage. It included Relative Trade Advantage (RTA); the logarithm of the Relative Export Advantage (lnRXA); and the Revealed Competitiveness (RC) (it is important to note that Balassa and Vollrath indices are not comparable as they are based on different concepts). The terms are expressed in the following equations:

$$RXA_{ji} = \left({}^{X_{ji}}\!/_{X_{jn}} \right) \Big/ \left({}^{X_{ti}}\!/_{X_{tn}} \right)$$

$$RMA_{ji} = \left({}^{M_{ji}}\!/_{M_{jn}} \right) \Big/ \left({}^{M_{ti}}\!/_{M_{tn}} \right)$$

$$RTA_{ji} = RXA_{j} - RMA_{ji}$$

Where	RTA_{ji}	Relative trade advantage in commodity ‘j’ for country ‘i’
	RXA_{ji}	Relative export advantage in commodity ‘j’ for country ‘i’
	RMA_{ji}	Relative import advantage in commodity ‘j’ for country ‘i’
	M	Imports
	X	Exports

Positive values of the three indices indicate a comparative advantage and the negative values can be attributed to comparative disadvantage. An important feature of these indices, unlike that of the Balassa index, is that they allow one to distinguish between a specific commodity/country and the rest of the commodities/countries.

This can potentially eliminate country and commodity double counting in world trade.

Relative and Import Advantage (RMA) and Relative Export Advantage (RCA) are calculated using the above formula both for India and Korea and the same formula is used to further calculate Relative Trade Advantage (RTA) of these countries over the world. Tables 9 and 10, and Figures 13 and 14, present the trend of RTA for various products considered for trade.

Indian firms from groups such as agriculture & fisheries, food products & beverages, chemicals, rubber, textiles, basic metal products, automobiles, and other industrial products are in a position of relative trade advantage over the world. Out of these groups, agriculture, rubber and textiles show very strong advantage. Food products & beverages, and automobiles, which were at a disadvantage during the early 2000s, have turned out to be at an advantage by 2013. Other transport equipment group which had an advantage till 2008 had lost it ever since. The

Figure 13. Patterns of Relative Trade Advantage of Indian Firms to the World

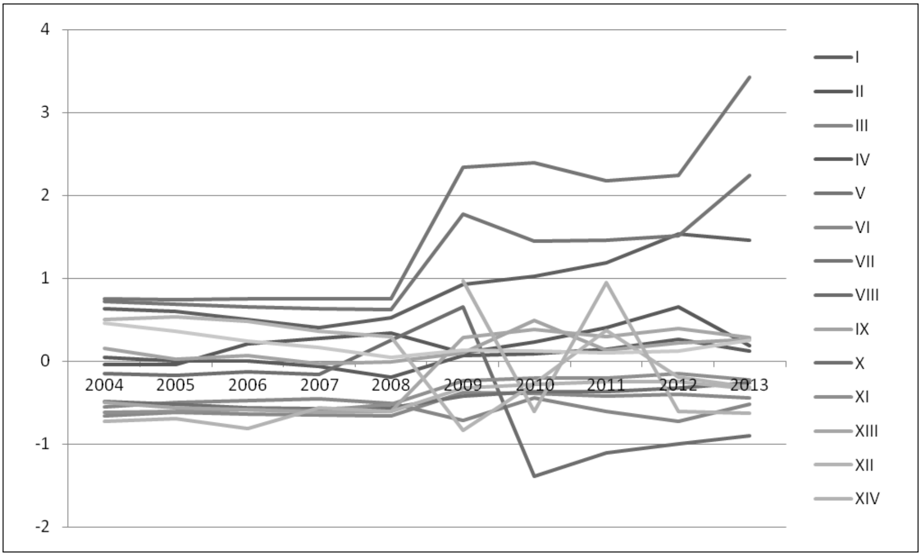


Table 9. Relative Trade Advantage of Indian Firms to the World

HS Unit Based Category										
	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
I	0.63	0.6	0.5	0.4	0.52	0.92	1.03	1.19	1.54	1.46
II	-0.04	-0.04	0.21	0.27	0.34	0.10	0.23	0.41	0.66	0.19
III	-0.55	-0.5	-0.48	-0.45	-0.51	-0.71	-0.45	-0.61	-0.73	-0.52
IV	0.05	0	0	-0.06	-0.19	0.06	0.09	0.15	0.26	0.12
V	0.72	0.69	0.66	0.63	0.62	1.78	1.45	1.46	1.51	2.24
VI	-0.66	-0.62	-0.64	-0.65	-0.66	-0.37	-0.39	-0.42	-0.40	-0.45
VII	0.75	0.74	0.75	0.75	0.75	2.34	2.39	2.18	2.24	3.43
VIII	-0.15	-0.17	-0.13	-0.16	0.25	0.66	-1.39	-1.11	-0.99	-0.90
IX	0.15	0.02	0.07	-0.03	-0.01	0.10	0.50	0.14	0.22	0.26
X	-0.49	-0.52	-0.56	-0.57	-0.56	-0.42	-0.37	-0.36	-0.32	-0.25
XI	-0.62	-0.61	-0.58	-0.59	-0.52	-0.24	-0.21	-0.20	-0.15	-0.22
XIII	-0.5	-0.56	-0.58	-0.62	-0.61	0.28	0.38	0.29	0.40	0.28
XII	0.5	0.53	0.48	0.36	0.3	-0.84	-0.27	0.37	-0.20	-0.31
XIV	-0.73	-0.69	-0.81	-0.56	-0.61	-0.32	-0.28	-0.25	-0.24	-0.33
XV	0.46	0.36	0.24	0.17	0.05	0.13	0.12	0.10	0.13	0.25
XVI						0.96	-0.60	0.95	-0.60	-0.63

Note: RTA values for 2004-08 are collected from the literature and RCA values from 2009-13 are calculated by the author using data from World Integrated Trade Solutions (WITS) of the World Bank.

same pattern is explained in Table 9 and Figure 13.

Traditional dominance of Korean firms in high end technology products is once again portrayed by the Relative Trade Advantage index. Industrial groups in Korea viz. chemicals, general machinery & equipment, electronic equipment & components, automobiles, other transport equipment, precision machinery and other industrial products showed Relative Trade Advantage. While chemical firms enjoy a marginal advantage, electronic equipment, automobiles and other transport equipment enjoys very strong trade advantage. General machinery group has evolved

Table 10. Relative Trade Advantage of Korea Firms to the World

HS Unit Based Category										
	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
I	-0.68	-0.71	-0.76	-0.70	-0.64	-0.58	-0.60	-0.68	-0.66	-0.67
II	-0.41	-0.41	-0.43	-0.38	-0.37	-0.37	-0.35	-0.32	-0.35	-0.38
III	-0.66	-0.64	-0.63	-1.29	-1.25	-1.39	-1.31	-1.27	-1.27	-1.17
IV	0.11	0.12	0.12	0.12	0.21	0.10	0.13	0.22	0.27	0.20
V	-0.12	-0.21	-0.29	-0.35	-0.31	-0.49	-0.63	-0.70	-0.64	-0.52
VI	-0.29	-0.31	-0.36	-0.38	-0.33	-0.32	-0.34	-0.28	-0.27	-0.32
VII	0.36	0.3	0.21	0.21	0.22	0.13	0.06	0.00	-0.01	0.22
VIII	-0.15	-0.35	-0.34	-0.53	-0.33	-0.25	-0.27	-0.19	-0.19	-0.26
IX	-0.13	-0.11	-0.09	-0.46	-0.52	-0.41	-0.40	-0.21	-0.11	-0.19
X	0.23	0.16	0.13	-0.04	0.04	-0.06	-0.04	0.10	0.13	0.14
XI	0.23	0.25	0.24	0.90	0.88	0.74	0.84	0.86	0.90	1.41
XIII	-0.3	-0.04	0.13	1.15	1.10	1.10	1.20	1.34	1.39	1.02
XII	0.8	0.8	0.78	1.88	2.95	2.92	2.63	2.76	2.60	2.08
XIV	0.77	0.74	0.71	0.92	1.23	1.28	1.21	0.95	0.86	0.59
XV	-0.12	-0.15	-0.2	-0.25	-0.15	-0.14	-0.19	-0.14	-0.09	0.09
XVI				0.00	0.00	0.00	0.00	0.00	0.00	0.00

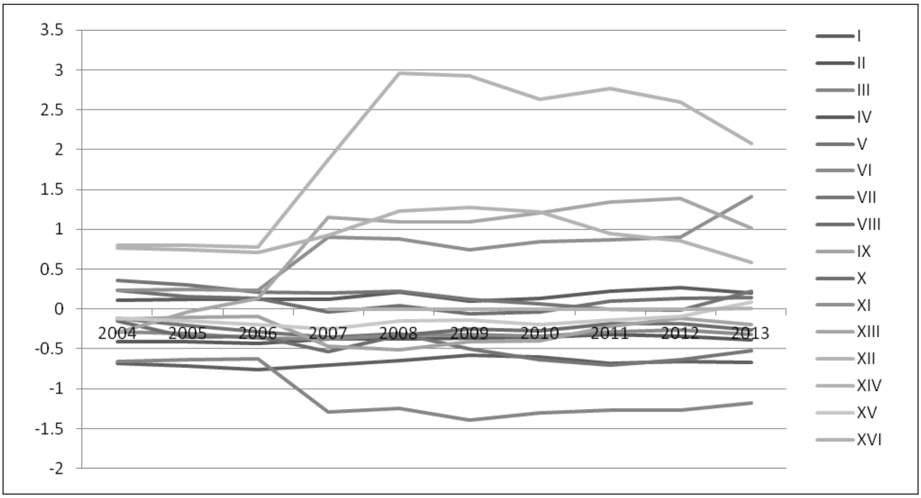
Note: RTA values for 2004-06 are collected from the literature and RCA values from 2007-13 are calculated by the author using data from World Integrated Trade Solutions (WITS) of the World Bank.

from disadvantage to advantage. The degree of advantage for precision industry is on decline post 2009. These patterns and trends of relative trade advantage for Korean firms are presented in Table 10 and Figure 14.

Relative Import Advantage (RMA) and Relative Trade Advantage (RTA) for various commodities is compared between India and Korea for the year 2009 and 2013. This comparison discussed above is presented in Figure 15 and Figure 16.

The industries that are at a comparative advantage and their respective level of exports and import (trade advantage) both from India and Korea are presented

Figure 14. Patterns of Relative Trade Advantage of Indian Firms to the World

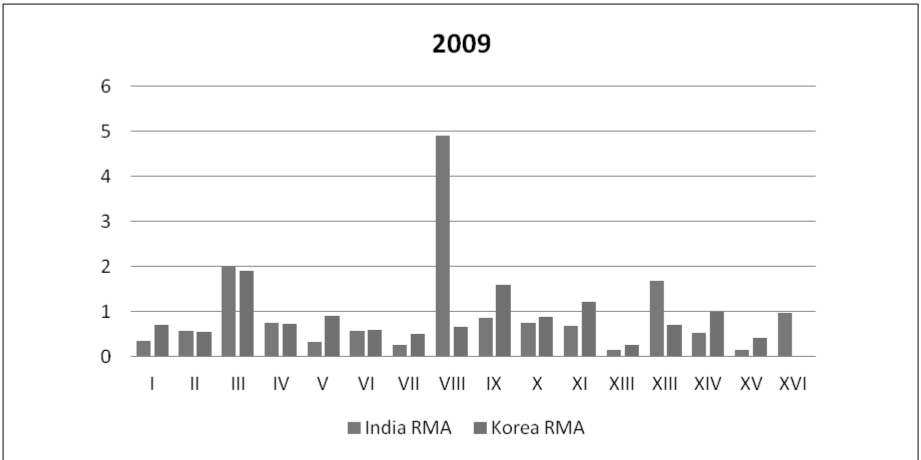


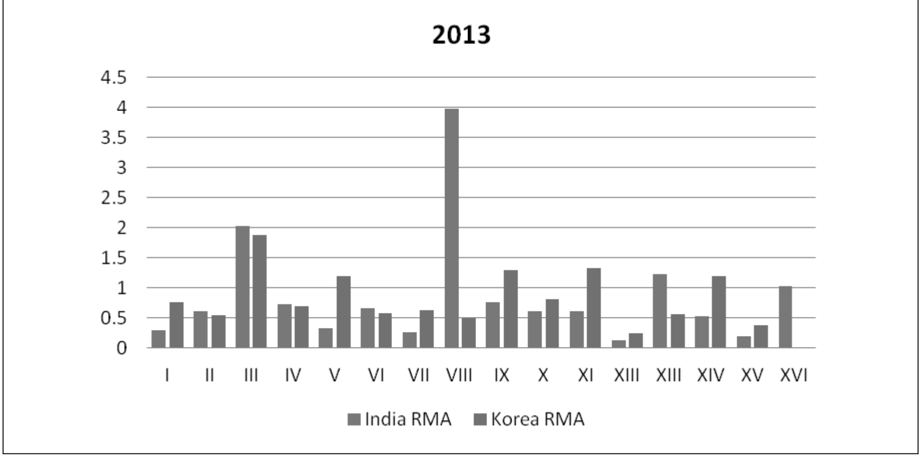
below:

India:		Korea	
Industry Group	Intensity of Export	Industry Group	Intensity of Export
I	Very Low	IV	Very High
II	Low	VII	Very Low
IV	Low	X	Very High
V	Low	XI	Very High
VII	Very Low	XII	Very Low
IX	Very High	XIII	Very High
XIII	Very Low	XIV	Low

Trade patterns between India and Korea post CEPA did not show tremendous change other than increase in trade per se. However, there are certain minor changes in the patterns which could just be the beginning of major changes that may happen

Figure 15. Comparison of Relative Import Advantage (RMA) of Various Products for India and Korea against the World

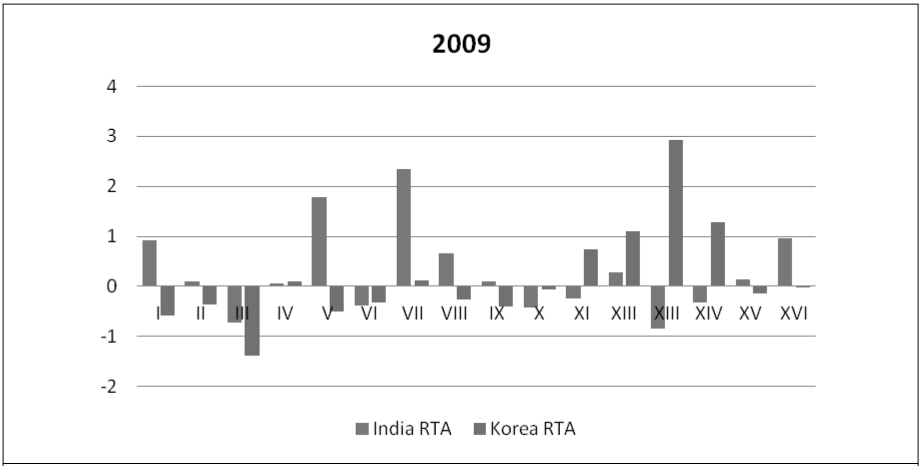


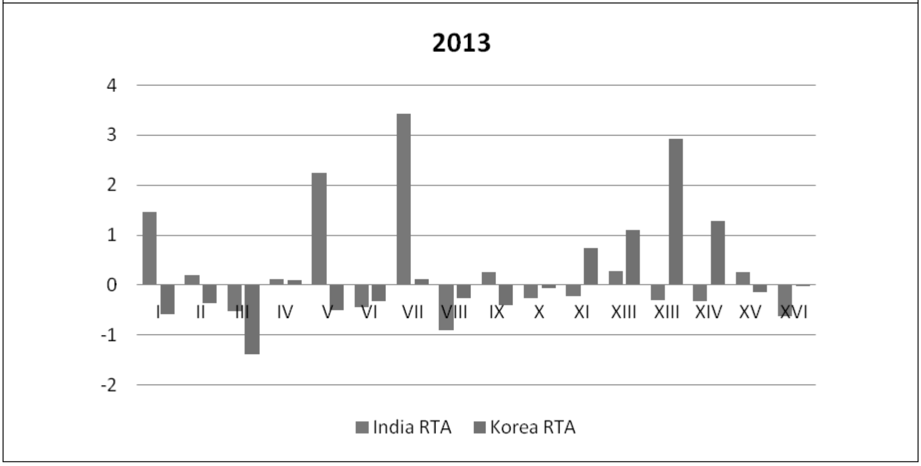


in future years.

Based on RCA, India's basic metal products group has become an advantaged group post CEPA. Other than that, textiles and rubber groups showed improvements in their competitiveness and non-ferrous metal group has shown a decline in their competitiveness. For Korea, the group of general machinery has become an advantage

Figure 16. Comparison of RTA of Various Products for India and Korea against the World





group post-CEPA. Relative advantage of electronic equipment has increased.

While high RTA values for groups with high volumes of trade promises a large quantum of trade to occur in the near future, high Relative Trade Advantage for certain groups with low trade volume at present also shows a tremendous potential for future prosperity in bilateral trade between India and Korea. CEPA did have a positive effect on the respective strengths of industrial units of both India and Korea.

V. Qualitative Analysis of CEPA's Impact on the Environment and Natural Resources Base in India and Korea

There are two sides to impacts of trade, for any country. While increased exports can end up using the natural resources in excess, jeopardizing the domestic needs of the resource in the long run (non-substitution clause), import of goods with a high footprint at the end of life can increase the overall environmental load on the country. Both would have serious consequences on reserves of natural resources and the environmental quality of the reporting country. The following table (Table 11) presents the potential implications, commodity wise, of trade on environmental and natural resources domain.

CEPA with its potential to enhance the trade of commodities such as automobiles and machinery from Korea would have implications for environment and natural resources in Korea as well as India. Similarly, enhanced trade of the commodities from groups such as agriculture & fisheries, food and beverages, textiles and mining products from India would have implications for environment and natural resources in India as well as Korea. Such potential implications qualitatively resulting from group of industries having relative trade advantages are presented in the following table (Table 12).

Indian exports focus mostly on non-technology based commodities from such groups as agriculture, food and beverages and mining which are in principle more damaging to the environment and more resource-consuming. CEPA's apparent potential for improved relative comparative advantage for Indian firms can enhance Indian exports which can lead to significant environmental and natural resources

Table 11. Environmental Implications Listed from Group of Products Considered in Bilateral Trade between India and Korea

HS Group	Classification (HS 2007 Code)	Product Description	Impact on Local Environment		Impact on Global Environment		Impact on Natural Resources	
			On Host Country	On Trade Partner	On Host Country	On Trade Partner	On Host Country	On Trade Partner
I	1~10	Agriculture and Fisheries Products	L	L	H	Nil	H	Nil
II	11~24	Food Products and Beverages	H	L	L	Nil	H	Nil
III	25~28	Mining	H	M	H	M	H	Nil
IV	29~40	Chemical	H	M	L	L	L	Nil
V	41~43	Rubber	M	M	L	Nil	M	Nil
VI	44~49	Timber and Paper	M	M	L	Nil	L	Nil
VII	50~67	Textile	H	Nil	L	Nil	L	Nil
VIII	68~71	Non-ferrous Metal	H	H	M	M	M	Nil
IX	72~83	Basic Metal Products	H	H	M	M	M	Nil
X	84	General Machinery & Equipment	M	L	L	Nil	Nil	Nil
XI	85	Electronic Equipment and Components	L	M	L	L	Nil	Nil
XIII	87	Automobiles	L	H	L	H	M	Nil
XII	86,88~89	Other Transport Equipment	L	M	L	L	L	Nil
XIV	90~91	Precision Machinery Products	L	L	L	Nil	Nil	Nil
XV	92~97	Other Industrial Products	M	L	L	Nil	L	Nil
XVI	98~99	Others						

H-High; M-Medium; L-Low

Table 12. Aggregate Environmental Load on to Each Country Based on Both Exports and sImports: and Internal and Externally Exerted

Product that have enhanced trade possibility under CEPA	Intensity of Trade Flow	Impact due to CEPA on Local Environment		Impact due to CEPA on Global Environment		Impact due to CEPA on Natural Resources	
		On Host Country	On Trade Partner	On Host Country	On Trade Partner	On Host Country	On Trade Partner
Indian Industries with High RTA and Volume of Trade							
I. Agriculture and Fisheries Products	Low	Very Significant	Nil	Very Significant	Nil	Very Significant	Nil
II. Food Products and Beverages	Medium	Very Significant	Nil	Not so Significant	Nil	Not so Significant	Nil
III. Mining	Very High	Very Significant	Low	Very Significant	Significant	Very Significant	Nil
IV. Chemical	Medium	Very Significant	Significant	Not so Significant	Low	Not so Significant	Nil
V. Rubber	Very Low	Not so Significant	V. Low	Not so Significant	Low	Not so Significant	Nil
VII. Textile	Low	Not so Significant	V. Low	Not so Significant	Low	Not so Significant	Nil
IX. Basic Metal Products	Very High	Very Significant	High	Significant	High	Very Significant	Nil
XIII. Automobiles	Very Low	Very Significant	High	Not so Significant	High	Significant	Nil

Remarks: Most of the trade, as it is natural resource-intensive and involves pollution causing activities at the production end, an increase in exports due to CEPA would result in VERY SIGNIFICANT Environmental and Natural Resources problems to India and VERY INSIGNIFICANT impacts on the Korean Environment.

Product that have enhanced trade possibility under CEPA	Intensity of Trade Flow	Impact due to CEPA on Local Environment		Impact due to CEPA on Global Environment		Impact due to CEPA on Natural Resources	
		On Host Country	On Trade Partner	On Host Country	On Trade Partner	On Host Country	On Trade Partner
Korean Industries with High RTA and Volume of Trade							
IV. Chemical	Very High	Very Significant	Significant	Not so Significant	Low	Not so Significant	Nil
VII. Textile	Very Low	Not so Significant	V. Low	Not so Significant	Low	Not so Significant	Nil
X. General machinery & Equipment	Very High	Very Significant	Low	Not so Significant	Low	Not so Significant	Nil
XI. Electronic Equipment and Components	Very High	Significant	Significant	Not so Significant	Low	Not so Significant	Nil
XIII. Automobiles	High	Very Significant	V High	Not so Significant	V High	Not so significant	High
XII. Other Transport Equipment	Low	Not so Significant	Not so Significant	Not so Significant	Low	Not so significant	High
XIV. Precision Machinery Products	Low	Not so Significant	Not so Significant	Not so Significant	Low	Not so Significant	Low

Remarks: Most of the traded entities by Korea such as automobiles and electronic equipment involve more of environmental natural resources issues at the consumption end. Hence, the increase in exports from Korea due to CEPA would result in VERY SIGNIFICANT Environmental problems to India compared to the host country.

implications domestically. Though trade can result in wealth creation, according to the principles of Non-substitution argument, it is not sustainable to have such natural resources depletion as a compromise for economic prosperity. Therefore it is very essential to study in detail the possible implication of international trade on environment and natural resources in India.

In contrast, technology oriented Korean exports have more damaging effects on end of chain i.e., in the trade partner country. Evaluation of such impacts is also essential to have a gauge on real gains of trade in general and CEPA in particular. As it appears from the qualitative presentation of possible impacts, both exports and imports seems to be pose greater threat in terms of the environment and overexploitation of natural resources to the economically poorer country (India in the present case) compared to its trade partner (Korea in the present case) leading to the issues of inequity in distribution.

As we enter the fourth year of CEPA, this may be the correct time to carry out such a comprehensive study aimed at evaluation of environmental impacts which could be worked towards strategies to internalize such externalities. In order for the benefits of India-Korea bilateral trade for the next twenty years to trickle down to the lower strata of the society on equitable terms and play a role in bringing change in the social fabric, it is important to internalize such externalities and correct the growth curve for sustainability.

VI. Concluding Remarks

Imports and Exports between India and Korea have seen a significant rise in the last 8 years. Indian exports continue to be dominated by mining, textiles and chemicals while Korean exports are largely in automobiles, precision equipment, electronic equipment and other automobile equipment. Korean imports from India are largely from mining and basic metals which complement their exports in automobiles. Other transport equipment export is in decline and India export in the same category is on rise. This could indicate a complementarity in the bilateral trade between these two important trade partners in Asia.

Relative Comparative Advantage for Indian firms continues to lie with non-machinery entities. RCA and RTA revealed a similar phenomenon of Indian and Korean firms holding a comparative advantage against the backdrop of their global trading patterns. Meanwhile, a few groups moved from being less competitive to more competitive, and others have shown significant change in trading volumes. Though not completely attributable to CEPA, the trade volumes have increased post 2009 along with the competitiveness of various clusters.

CEPA shows promise in augmenting the trading patterns with India, which continues to export basic metal and mining products and Korea in turn continues its promising exports of finished products. CEPA with its potential trade augmentation would have a significant impact on environmental and natural resources based in India. It is observed that given the nature of exported and imported goods and products India would be more susceptible to environmental impacts both from exports and imports compared to Korea.

In order to have a complete assessment of the gains of CEPA, it is essential to have a comprehensive valuation of environmental impacts along with the losses due to tariff cuts vis-à-vis gains due to increased trade between the two countries.

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Iranian Economic Policy after the Election (2013)

M. H. Mozafari[1)]

I. Introduction

Iran has a mixed economic system in which both the government and private sector are active; though the government owns a sizable portion of the economy. Furthermore, as the government is the policy and decision-maker, it has significant power, both legally and actually, to direct or adjust the economic system; and the events that transpired during the two terms of the last president constitutes the best evidence for this claim. Having the highest oil revenues in the history of Iran and the highest-recorded budget in the modern history of Iran, Ahmadinejad's programs, policies and decisions created an environment that the country has never hitherto grappled, with huge problems. These problems include mismanagement, passive foreign policy, dispute between the government and parliament and the other branches, the issue of nuclear technology and sanctions, bad implementation of the subsidies plan, stagflation, unemployment, the devaluation of the Iranian currency, negative growth, government debts and financial obligations, problems

1) Researcher, Centre for Scientific and Academic Cooperation (ICRO).

of domestic production, reduction in oil export, internal and external political divisions and disputes; all of which constitute a complex of issues inherited by President Rouhani.

Addressing these problems, the government has a new economic and political policy. The new Iranian government is trying to mobilize its supporters in the parliament and reduce the tensions at the national and international level. Dr. Rouhani's victory in the presidential election had a positive impact and some of these problems are being solved or gradually reduced. For instance, the dispute between the government and parliament and the Judiciary has been solved. Internal and external political divisions and disputes have been mollified to a certain extent. The value of Iranian currency has increased (almost 25 percent) and the tensions surrounding the nuclear issue and the sanctions have decreased in relative terms. Apart from Iranian willingness, the international community is also showing its readiness toward changes and all are attempting to cooperate.

However, though the challenges are still many, Iran holds much potential. Should Iran effectively and correctly utilize these potentials, the new government can effect change in the current situation. In this regard the president outlined some of these ‘potentials’ to the assembly: the existing capital and infrastructures, favourable conditions of transit, high capability of engineering contractors; a varied climate and wide range of land types; rich mineral resources, large reserves of oil and gas, young and educated workforce; the potential for scientific research and advanced technology, unique tourist attractions and rich cultural heritage, massive infrastructure and industrial investments. All of these could be considered important potential factors for overcoming the current situation (Rouhani, 2014).

No doubt that all over the world, there is much diversity in terms of political and ideological motives of governments seeking to address these problems and the Iranian government is not an exception. After the 1979 Islamic Revolution, Iran has experienced a whole range of political events including the revolution, the eight-year war, post-war reconstruction, along with various political and economic sanctions. What matters is that under the current situation and the existing laws and regulations, the new government should actively suggest its plans and programs.

This article attempts to provide a true picture of the status of the economy in the constitution, in addition to the general policies and the legal/economic mechanisms of decision-making, and also explain the policies of the new government. Accordingly, in the first part of the article the economic aspects of the rules and regulations and their functions are discussed, and the second part discusses the budget and monetary policies of the new government and how they would address the country's main problems, namely inflation, recession, and unemployment.

However, within the framework of research facilities and the time limit, this article studies the recent developments in the Iranian economy and based on those results, and offers some suggestions. Given that the government's current economic policies have yet to be fully implemented, there is naturally no existing literature on the topic and this paper is fully dependent on Internet sources; nevertheless, the materials are reliable because all have been obtained from official sources.

II. Various Aspects of Iranian Economic Policies

‘The Various Aspects of Iranian Economic Policies’ provides the general outline of the economic system of Iran in upstream documents like the constitution, the general economic policies including the Five Year Plans and also government decisions on budget, employment and monetary policy. This section is divided into two parts: ‘the Law and Statutory Policies’ outlines the Iranian economic system in the long term; and ‘the Fiscal and Macroeconomic Policies’ which could possibly change according to prevailing circumstances or political and economic trends of the political parties and groups who come to power.

2.1. The Upstream and Primary Documents on Iranian Economic Policies

The most important upstream and primary documents encompassing every economic, social and political issue in I.R. Iran are: the Constitution and the ratifications of the Expediency Council approved and declared by the Leader, such as 'the Vision of the I.R. of Iran (2005-2025)'. The general characteristics of the economic system of I.R. Iran are reflected in Chapter Four of its Constitution. Therefore every official strategy, plans and government decision should be in harmony with these documents. Here, this paper briefly reviews some of the most important Articles of the Constitution and the General Principles on the Iranian economic system.

2.1.1. The Economic Chapter of the I.R. of Iran Constitution

Demanding "rule of law", the Constitutional Revolution of the Iranian people in 1906 forced king to sign the first Iranian Constitution, which remained valid until the Islamic Revolution. The Constitution of the Islamic Republic of Iran that was adopted following the revolution (1979) and amended in 1989, is the second Constitution of the country. According to Article 44 of the Constitution the economy of the Islamic Republic of Iran should consist of three sectors:

- **The State Sector,** that include all large-scale industries, mother industries, foreign trade, major minerals, banking, insurance, power generation, dams and large-scale irrigation networks, radio and television, post, telegraph and telephone services, aviation, shipping, roads, railroads and the like; all of which will be publicly owned and administered by the State. Furthermore, Article 45 also states that uncultivated or abandoned land, mineral resources, seas, lakes, rivers and other public waterways, mountains, valleys, forests, marshlands, natural forests, unenclosed pastureland, legacies without heirs, and property of undetermined ownership are Public wealth and property; in addition, public property recovered from usurpers, shall be at the disposal of the Islamic government to utilize them in accordance with the public interest.

- **The Cooperative Sector,** means the Urban and Rural Cooperative Companies and Enterprises active in production and distribution;
- **The Private Sector**; or entities active in the field of agriculture, animal husbandry, industry, trade, and services. Based on Articles 46 and 47, private ownership is legitimate and respected; everyone is the owner of the fruits of his legitimate business and labour.

The most important objectives of the economic system of the Islamic Republic of Iran are: the economic independence of the society, prevention of foreign economic domination over the country's economy; emphasis on increasing agricultural, livestock, and industrial production; uprooting poverty and deprivation; and fulfilling human needs amidst the process of development while preserving human liberty; provision of basic necessities for all citizens: housing, food, clothing, hygiene, medical treatment, education, and the necessary facilities for the establishment of families; ensuring conditions and opportunities of employment for everyone and ensuring that economic policies neither results in the concentration or circulation of wealth in the hands of a few individuals or groups, without turning the government into a major/absolute employer (Article 43).

However, Article 44 of the constitution is the main reason for the increase in volume and share of government ownership and economic activities. For more than two decades since the adoption of the constitution, Article 44 has been interpreted in favor of the government sector. The Guardian Council's interpretation made domestic and foreign investors regard the Iranian economic system as a state economy with potentially high risk for investors. This was considered a serious obstacle for investment and development of the country.

The problems of inefficiency of the public sector, the relatively small private sector, potential for corruption and the tendency toward privatization, have also led to more research in this regard. The responsibility for overseeing the study was in the hands of the Expediency Council. In 1997, the Expediency Council identified that there were many problems in running the country. After hundreds of meetings attended by many experts from various legislative and executive organizations, there was finally a change in the prevailing view and interpretations of Article 44 favorable to privatization.

Thereafter, economic growth, equal opportunities, better distribution of income, and improvement of per capital income were the subjects that were given emphasis with respect to various economic activities. It was decided that the financial activities of the government sector should be transferred to other sectors and the government in no way should have any new economic activity outside of Article 44 limitations. It was recommended that in all the transfer cases, the government sovereignty should not be violated. At the same time, the Expediency Council is also responsible for supervising the implementation of the general policies of Article 44 of the constitution and the transfer process. Also as a supplement to the privatization measures, it was provided that a new study on the "justice plan" should begin.

After the Islamic revolution and especially during the 1980s, despite the tendencies of religious leaders including Imam Khomeini, most influential officials in the government were relatively socialistic in their interpretation of the article 44 of the Constitution. They were in favour of planned, state-centred economy and did not pay sufficient attention to the private sector. But when the limitations of a planned/government economy gradually became clear, with socialist economies becoming isolated and the privatization becoming a popular trend all over the world, the supporters of the state economy in Iran relented and changed their opinion (Khamenehei, 2010). However, under the title of the 'General Policies of Article 44 of the constitution', experts and members of the Expediency Council provided a wider interpretation of the Article, and the Leader communicated these policies to the government (Nezam, 2005).

Only after this was it emphasized that the government should reduce its direct activities in the economic affairs and transfer some of them to the private and cooperative sectors, and declared that foreign investors also are welcomed in Iranian economy. It is suggested that instead of expanding economic activities and increasing the size and the capacity of the public sector, the government should support and supervise all economic activities.

However, based on the General Principles, a legislative act was passed by the parliament and accordingly, 'the Supreme Council for the Implementation of General Policies of Article 44" was established. The council includes: President or First Vice President and Minister of the Economic and Financial Affairs (the Secretary of the Council), Minister for Cooperatives, the relevant Minister or Ministers, the Minister of Justice, Minister for Information, Chairman of the Management and Planning Organization, Head of the Central Bank, the secretary of the Expediency Council, the Attorney General, the chief of the General Inspector, Head of Supreme Audit Court, three MPs elected by parliament, Head of the Islamic Republic of Iran Broadcasting (IRIB), the Head of Iran's Chamber of Commerce and Industry, Chairman of the Central Chamber of Islamic Cooperatives, three economic experts along with experts from the private and cooperative sectors recommended by the Minister of Economic Affairs and appointed by the President, the Head of the privatization agency and Head of the Stock Exchange. The Secretariat of this Council is in the Ministry of Economy, and the Council also has a specialized commission. According to the abovementioned Act, the ministry shall provide regular reports on the implementation of 'the General Policies of Article 44 of the Constitution and Article 88 of the Act' to the Parliament and the Expediency Council and the Economic actors. Based on this law, more than dozen reports have been published up to this point. The base price, amount of shares of public companies and whether they should be offered, in the stock exchange or in auctions, will be decided by the Board of Transaction. For greater convenience a Provincial Headquarters of the council was established in various provinces.

As noted, the government does not have a role in the adoption, amendment and interpretations of the Constitution. But the new interpretation of Article 44 and the relevant law and regulations gave extensive powers to the government regarding the transfer of state enterprises and activities to the private sector. Therefore the new government policy of transferring state enterprises and activities can reduce the money supply, can obtain new financial source and can instead invest this revenues in new fields and try to assuage the impact of the recession and unemployment. According President Rouhani in the area of privatization and the implementation of the general policies of Article 44 of the constitution, the previous government granted only a small part of the government shares to the real private sector and most of the shares have been granted to the Social Security Organization (Sazmane Tamine Ijtemai) or The State Pension Fund (Sandouqe Bazneshastegi) or the quasi-Governmental organizations; because the government was in debt to them. Declaring his policy in this regard, the president stated: "The government primarily will encourage the Gov. Funds, Companies and Firms to offer their shares in the stock market and in this way, these institutions can begin engaging in stock management; meanwhile the major companies will remain in the government sector because they will require fundamental reform. So only after the reform, will the government follow through with the privatization process in these companies (Rouhani, 2014).

2.1.2. The General Policies on the Economy

The General Policies on the current Iranian economic system is another set of upstream and long term documents. The General Policies comprise of a set of documents on all political, social, and cultural issues. These policies, however, may change depending on changing circumstances. Policies such as ‘the General Policy on the Resistive Economy’ basically have been approved in accordance with current necessities. Based on Article 110 of the Constitution, after consulting the Expediency Council, it is a duty of the leadership to declare the general policies of the Islamic Republic of Iran. The council is a consultative arm of the leader on very important issues and currently has more than 40 members, all of whom are appointed by the leader. From Nov. 1993 to Feb. 2014, a total of 46 General Policy that passed through the Expediency Council and presented to the leader, 35 was approved and declared (Principles, 2014).

Based on Article 112 of the Constitution of the I.R. of Iran, the Council shall meet to discuss any issue forwarded to it by the Leader. Furthermore, in case of disagreement between the Parliament and the Guardian Council, if it is found that an enactment/legislation of the Parliament is in conflict with the Constitution or Islamic teachings, then upon the order of the Leader, the Expediency Council shall meet to discuss the issue (The Constitution of IR. of Iran, 1980). There are several general principles on economy as follows;

- The General Policies on Economic Security
- The General Policies on several 'Five year Development Plans'
- The General Policies on Water Resources
- The General Policies on Natural Resources
- The General Policies on Transportation, Housing, Urbanization, Investment and many other Social, Cultural and political topics.

The 20 Year Vision Plan of the Islamic Republic of Iran (2005-2025) is one of the most important texts and also considered one of the main upstream documents. Another document recently declared in response to the American and European sanctions against Iran is called the 'General Policy on the Resistive Economy' (Majame Tashkhise, 2014). Among all the General Policies, this study discusses two important documents as follows:

• The 20 Year Vision Plan of the Islamic Republic of Iran (2005-2025)

The 20 Year Cultural, Scientific, Economic, Political and Social Vision Plan was prepared by the government; and later modified and ratified by the Expediency Council and then approved and declared by the Supreme Leader. This brief document tries to outline a general and ideal image of Iran among the countries in West Asia (including Central Asia and the Middle East) in the long term prospective. Based on this document 'I.R. of Iran in 2025 is a developed country; a leading power in the region in the field of economy, science and technology that identifies itself as a revolutionary Islamic system inspiring the world of Islam, while engaging in constructive and effective interaction in international relationships'. In another part, the document added: the Iranian society will have achieved 'advanced levels in science and thus attain the capacity for producing much-needed knowledge and technology, ultimately increasing human resources and social asset for national production becoming an economic, scientific and technological leader in Southwest Asia (including Mid-Asia, the Middle East, and the neighbouring countries) with emphasis on software development and scientific production, rapid economic progress, and promoting comparative increase in income level per capita and achieving the full employment.

This brief text containing several articles is one of the upstream documents based on which other medium-term plans and annual budgets should be developed and their quantitative macro-indexes, such as the investment rate, per capita income, gross national product, employment and inflation rate, reduction of the income gap between the upper and the lower classes of the society, development of culture, education and research, and defence and security capabilities, should be adapted and clarified in accordance with the development policies and the objectives and necessities of the Vision; its policies and aims should be completely observed and followed (The Vision Plan of IR of Iran, 2005).

The Iranian Vision Plan was prepared benchmarking the experiences of other countries like Japan, the United States, some of the European and Southeast Asian countries that have their own Vision Plans; in addition to giving consideration to experiences of Iran. Having different opinions regarding the nature and scope of the Vision Plan is quiet normal. Same discussions were carried out by the Expediency Council and paralleled discussions also in the Fourth Economic Development Plan. However, all of the members agreed that the Vision's goals and objectives are achievable. It was accepted by both major political and academic elite of the Iranian society; and became a general framework for the Fourth Economic Development Plan. Fortunately, the economic section of the Vision has the measurements and assessment indexes such as increasing investment rate, per capital income, gross domestic product, and employment rate; reducing the gap between high and low classes; as well as promoting culture, education, and identifying the country's capabilities.

However, there are some experts who criticized this document on the grounds that it is not feasible, lacking evaluation mechanisms and a monitoring system. Though the four “five-year development plans” attempted to provide figures and facts to reduce these concerns but the said programs in the four plans were also unable to come up with detailed reports of performance, with no mention of how to achieve goals related to the Vision, contained no comparisons of current and earlier situations in various aspects nor predictions of the challenges facing the region. Most of all, they failed to establish a logical, specific and clear connections with the upstream documents. The present Minister of Petroleum criticized the Ahmadinejad government for nonconformity of ongoing trends in the country with the 20-Year Vision. Annual measurements were taken, and a major point of the Vision Plan is to maintain a rapid economic growth rate; if the rate slows down, it shows that we are not complying with the plan. “If we are to be the most powerful country in the region in economic terms, we must first achieve an economic growth rate of 8 percent for the entire 20-year period.” Currently, all OPEC members enjoy an average growth rate of 4.5-5 percent.

The minister also emphasized the need for economic security, which is important for achieving the goals of the 20-year Vision Plan. Furthermore, in order to succeed, the country needs to ensure a political and social atmosphere conducive to such success. Iran must go through a “period of détente and embark on establishing friendly relations with neighbouring countries, since a country that intends to achieve rapid progress will need capital and foreign resources as well as foreign technology.” Therefore, to secure sufficient foreign financing and capital as well as foreign technology and access to foreign markets to sell our products, Iran must also engage in friendly interaction. The former Petroleum Minister also discussed the importance of oil as a factor behind the plan. “No economic or political discussion in Iran could be complete without due attention to crude oil resources,” he mentioned. Given the centrality of this natural resource to the country's economy, there is a need to reshape our approach to oil and to consider it as a non-renewable resource for the subsequent generations. He warned that “if we do not correct the presently erroneous approach, we would neither establish a competitive economy, nor promote the private sector. Everything will become limited to oil and its subsequent economic rent." He highlighted the Oil Stabilization Fund as a positive step but believed that it has been "treated as a bank account (by the previous government)." Yet, in order to achieve the goals of the Vision, the government needs to decrease its reliance on oil by 10 percent every year and oil revenue must be used as a catalyst for rapid economic growth and investment (Zanganeh Namdar, 2007).

However, the eight-year program of the previous government not only did not help in achieving the Vision's goals; but in many areas like reliance on oil, economic growth, income level per capita and employment, it actually set the Vision back. Explaining the current situation, Dr. Rouhani stated that stagflation and unemployment currently are the most significant economic issues facing the country. According to him, the most important factors leading to the recession are: excessive weakness of the budget allocated to provision of public services, especially in the investment area, together with the intervention of the Central Bank to compensate for the budget deficit by issuing more notes, turning the budget into one of the decisive factors contributing to the deep recession and high inflation. The unjust sanctions imposed on the country have also led to economic recession in several ways:

Firstly, uncertainty and impossibility in forecasting the future led entrepreneurs to invest for short term profits into such things as foreign currency, gold coins and real estate, keeping them away from the manufacturing sector.

Secondly, business limitations and increase in transaction charges led to expansion of the underground economy.

Thirdly, intensive financial sanctions imposed on the Iranian banks limited their international banking activities, adversely affecting companies and finally, limitations on oil exports reduced the government's foreign exchange earnings. However, the following factors were also factors in intensifying the recession:

- A highly import-oriented economy on top of internal inflation and increasing vulnerability of production.

- Unfavorable business environment due to constant intervention of government in the economy and unpredictability of its behavior has led to a weak private sector.
- Significant increase in manufacturing costs, especially due to sudden leaps in foreign exchange and energy costs.
- Numerous problems created in the banking sector due to policies adopted and imposed by the government, leading to huge bad debts, and creating strong limitations in financing for the enterprises as a result.
- Serious irregularities created in the proprietorship status of enterprises due to inappropriate implementation of the general policies of Article 44 of the Constitution concerning privatization of state-owned enterprises.
- Unstable macroeconomic environment due to runaway inflation and high fluctuations in the foreign exchange parity rate.

These conditions led to more than a 6 % decrease in the GDP, putting additional pressure on the lower income population. A reduction in investment by more than 21% last year (2013-14) was one of the major factors in the carry-over of the recession from 2012 to 2013 (Rouhani H., 2013), as well as high inflation (40%) and economic recession (an economic growth rate of minus 5.8% and an unemployment rate that stands at 12.6%), a condition dubbed by economists as stagflation. To compare these figures with the situation when previous government came to power, it represents a rollback; at least in terms of these indicators.

• The General Policies of the Resistive Economy

Iran has been subject to increasing American and European sanctions due to its disputed nuclear program. On the other hand, Iran has repeatedly stated that its peaceful nuclear program is within the framework of the IAEA regulations. Therefore, from the international law point of view, the American and European sanctions are illegal with respect to human rights, as they represent oppressive attempts against the Iranian nation. Excluding Iran or any other nation from having a peaceful nuclear program when there exist many nations who actually have nuclear weapons constitute severe discrimination. This is why Iranian officials insist on their rights in their international negotiations regarding the so-called 5+1 format and emphasize ‘the Resistive Economic Policies’ at the national level. Recently, there were new developments in this regard. On February 2013 after consultations with the Expediency Council and holding necessary discussions, Ayatollah Khamenei the Supreme Leader of the Islamic Revolution issued an important document on the Iranian economy called: ‘the General Policies of the Resistive Economy’ (Khamenehei Seyed Ali, 2013).

Other than several paragraphs at the beginning and at the end of the document that emphasize certain issues like increasing the level of participation in economic activities, enhancing the income of low- and middle-class people, strengthening the competitiveness of the economy, creating competition between regions and provinces, improving the indicators of social justice and certain paragraphs on cultural aspects which are nationally-oriented; here I would like to mention the most important provisions of this document, which may help Iran attract trading partners as well as foreign investors:

Paragraph 6 of this document states 'increasing the domestic production and commodity (especially imported items) and giving priority to strategic products and services, diversifying the supply sources, and reducing the dependence on specific and limited number of countries.

Paragraph 7. Ensuring the Food and Health Security, and maintaining strategic reserves, with emphasis on increasing the quality and quantity of production (raw materials and goods).

Paragraph 10. Targeted support of exports of goods and services by:

- Simplifying regulations and expanding incentives;
- Expanding foreign services and necessary transportation and infrastructure;
- Encouraging foreign direct investment for exports;
- Adjusting national production according to export demands; creating new markets; diversification of economic ties with other countries, in particular

with regional countries;

- Utilization of barter trade systems to simplify exchanges in line with demands;
- Creating stability in the processing and regulation of exports, with the intention of expanding Iran's share in target markets.

Paragraph 11. Expanding free-trade zones and the country's unique economic activities with the intention of acquiring advanced technologies, simplifying and expanding production, exporting goods and services, securing export demand and financial resources from abroad.

Paragraph 12. Increasing the power of resistance and decreasing the country's vulnerability by:

- Expanding strategic links, cooperation and consultation with regional and international countries, with focus on neighbouring countries.
- Utilization of diplomacy to safeguard economic interests and objectives.
- Utilizing the capabilities of international and regional structures and organizations.

Paragraph 13. Addressing income vulnerabilities resulting from exporting oil and gas by:

- Choosing strategic customers;
- Diversifying methods of sale;
- Partnering with the private sector for sales
- Increasing gas exports;
- Increasing electricity exports;
- Increasing petrochemical exports;
- Increasing exports of petroleum products.

Paragraph 14. Increasing the country's strategic oil and gas reserves with the intention of impacting international oil and gas markets; to emphasize safeguarding and expansion of oil and gas production capabilities, particularly in shared fields.

Paragraph 15. Increasing the added value by completing the value chain in the oil and gas industries; expanding the production of goods that yield optimal returns (according to the energy intensity index); increasing the export of electricity, petrochemical, and petroleum products, with focus on conserving resources.

Paragraph 16. To economize social expenditures with focus on fundamental development of its foundations; rationalizing the size of government, and disbanding duplicate or unnecessary agencies and departments.

Paragraph 17. Reforming the government's system of income, and increasing tax revenues.

Paragraph 18. Increasing annual contributions to the National Development Fund from oil and gas exports until it is no longer reliant on the oil budget.

Paragraph 19. Encouraging a transparent and healthy economy; eliminate an environment that allows for corruption in monetary, commercial, and currency matters.

Paragraph 21. Explaining the dimensions of a resistance economy and shaping its discussion, particularly in academia and the media; and transforming this into an inclusive and popular national discussion (Scott Lucas, 2014).

The General Policies of the Resistive Economy, as well as the statements and remarks of senior officials, indicate that the policy of the new government is to resist and demand their rights. In announcing the above document, the Supreme Leadership wrote: "Having abundant spiritual and material resources, a rich and diverse set of talents, a widespread infrastructure, and most importantly, a committed and proficient manpower that has the determination to move forward; if the Islamic Republic of Iran follows the indigenous and scientific economic model derived from its Islamic and revolutionary culture, also known as a resistance economy, then not only we will overcome all economic problems and defeat the enemy, who has imposed a full-scale economic warfare against this great nation; but also enable us to, in a world where risks arising from uncontrollable developments such as economic, financial, and political crisis; safeguard our achievements, continue our progress, fulfil the goals and principles of the constitution and our 20-year vision plan (Khamenei, 2014).

In an interview with the media, the Iranian president told to the reporters that “the resistance economy determines the direction of Iran's economy in the coming years,” “We should initiate a new movement and effort within the framework of the general policies of the resistance economy because the resistance economy strengthens the basis of the country's economy to the extent that it can continue its path under different conditions" (Rouhani H., 2014).

Concerning the new economic policy, the Secretary of the Expediency Council, also said, to overcome the current situation, Iran should implement its foreign policy only with awareness of its economy. If Iran had reduced the economy's dependence on oil during thirty years following the revolution, the sanctions would not have this much impact on our economy. We have to turn the crisis of economic sanctions into an opportunity. This is one of the goals of the Resistive Economy. For example, couldn't the country use an eight-year war to develop its military power and defence? Yes. From the military point of view, we were able to become a formidable military power after 30 years. With many drones, radar and other equipment in its arsenal, Iran is in very good position militarily. This shows that we have been able to use war as a great opportunity (Rezaei, 2014).

However, there is some debate going on regarding the nature of these general policies. For instance: are they different nature in legal terms? Do these policies, such as the constitution, have higher status than ordinary law? Do they require some type of interpretation of the constitution? Basically, up to what extent and in what areas do we need these policies? Is it a must for the Parliament to observe them in its legislation, in the context of overall policy for legislation? These questions have perplexed the Expediency Council regarding the issue. Based on research on this issue, sometimes the ordinary rules of interpretation are not efficient due to fundamental change of circumstances. There were even instances when the results contradicted the objectives of legislators. However, the Constitution is a set of guidelines for the administration of a country. These guidelines basically are very general and ambiguous by nature and are not always clear. Therefore, they may be interpreted differently with different perspectives. For example, Article 44 of the constitution of the Islamic Republic of Iran is very general, that it can be interpreted as socialist, or as a traditional Islamic interpretation on ownership, capital and labor. Therefore, general policies in fact, are not a kind of "interpretation of the constitution" but in terms of circumstances, they are merely outward manifestations of its content!

However, this research has acknowledged that, the definition of the General Policies is not easily done; so by giving certain characteristics it tried to reduce some of the ambiguity of the issue. The research believes that The General Policies should:

- have the option of "Choosing a trend or a school of thought" among two or more trends; for example, to choose the Market and private Economy or the planned Government Economy.
- must be coherent and create a system that connect each part to the whole system.
- should be general and have greater focus on "strategic issues.
- should not be "temporary; so that they can utilize the constitution and make it more sustainable (Dawlat Raftar, 2010).

2.2. The Five-Year Plans on Economic, Social and Cultural Development

Based on the legal procedures in preparing the five-year, medium-term plans the government should observe the upstream documentations (the constitution, the General Principles and the Vision Plan in particular) as the framework and then send them to the Parliament for ratification. During eight years of the Iran-Iraq War, the main objective of the Iranian government was to prosecute the War and to meet minimum requirements for public life. But in the post war period, the medium-term plan was initiated and moved forward as follows: the First Development Plan from 1989 to 1993; the Second Development Plan from 1995 to 1999; Third Dev. Plan from 2000 to 2004; fourth Dev. Plan 2005 to 2009 and the Fifth Dev. Plan 2011 to 2015. The First and Second programs are referred to as the Reconstruction Period; the time of the third program is called the Reform period (president Khatami's term); fourth and fifth are called principalist or Ahmadinejad's term).

The most important goals of these programs are: greater quantitative and qualitative improvement of education, culture, science and technology; economic growth, employment, reduction of economic dependence, self-sufficiency in strategic agricultural products, controlling the inflation, improving social justice; providing the minimum and basic needs of all people, and modernization of production capacities. Other additional goals include strengthening public participation and monitoring the performances, reducing the economic dependence on oil revenues and developing exports, strengthening the country's defence and balancing the economic sectors (cooperative, public and private). Among the abovementioned development plans, the priority of the First and Second plans was to reconstruct the infrastructure damaged during war time. The Fifth Development Plan was valid until the end of 2015. Since the term of every government is four years, plans and programs of previous governments should have carried out. However, every government could also seek to modify and introduce reform in above-mentioned plans. For instance, Dr. Rouhani's government proposed several modifications to the 5th five-year plan of Dr. Ahmadinejad's government.

2.3. The Economic Problems, Government Policies and Upstream Documents

The main objectives of macroeconomic policies (in general) and monetary policies, in particular, are: price stability, economic growth and a favourable level of employment. Since it is difficult for policy makers to achieve the ultimate goal directly; therefore, determining intermediate objectives and introducing appropriate instruments are deemed necessary (Iran, 2014). In the following part the article explains the most significant economic problems of the country; as well as relevant policies and their compatibility with upstream documentation in brief.

2.3.1. The Economic Problems and Government Policies

When president Rouhani presented the national budget bill in 2014-2015 to the parliament, he emphasized that recession, inflation, unemployment and the sanctions were the major economic issues facing the country. Level of both inflation and recession in past two years were incredible. As it is common everywhere, government wished to influence the economic activities and to overcome the problems through fiscal policy, spending in various fields and sectors, and taxation. According to Article 52 of the Constitution, the annual budget of the country will be drawn up by the government and submitted to the Islamic Consultative Assembly for discussion and approval. The budget bill is an important document concerning the macro-economy, because it shows the initial signs related to the macroeconomic situation of the country for a given period, and contains useful information on government policies on the allocation of resources in public services and infrastructures. So the entrepreneurs will be able to predict the economic outcome. The budget conveys the official stance of the government policies on the economy in general to the parliament; consequently, due to credibility of the government, is considered the source of decision-making by entrepreneurs and people alike.

2.3.1.1. The Inflation

The inflation not only had unfavourable effects on the activity of enterprises but also affected the lives and livelihoods of the families. When the new government was inaugurated, inflation reached nearly 44 percent. The mass of money printed by the central bank was a major factor in the increased liquidity and inflation. In recent years, the dominant role of the banking system in financing ‘the Mehr Housing Plan’ increased their debts to the central bank and as a result the monetary base rose sharply. On the other hand, the improper implementation of ‘the Targeted Subsidies Law’ increased the stagflation in the country. Lack of attention to the fact that both lower and higher income families were receiving subsidies of approximately 1.7 times more than the amount received from the sale of energy, lack of attention to the economic enterprises even after a sharp rise in their costs, ignoring the macroeconomic effects, the energy price shock and its adverse effects on the money and exchange market were the most important obstacles with respect to the design and implementation of the plan.

Thus reducing the rate of inflation through various programs became a declared government policy. Dr. Rouhani stated: the existing capitals and infrastructures, favourable transportation/logistical conditions, high capability of engineering contractors, climate variability and wide range of land types, rich mineral resources, large reserves of oil and gas, young and educated workforce meant Iran had good potential for scientific research and advanced technology, along with unique tourist attractions and rich cultural heritage; which would make possible massive infrastructures and industrial investments that are considered to be the most important in overcoming the current situation (Rouhani, 2014).

According to the finance ministry, the Iranian government is serious about stability in the foreign exchange market. In fact, part of the government's achievements in controlling the inflation is due to the relative success in fixing the exchange rate (Tayyebnia, 2014). Within the first 100 days of the government, there was a 13 percent reduction in inflation. The monthly inflation rate that was 3.4 percent in June of 2013 dropped to one percent in November. The monthly inflation rate in food items in November compared to previous month dropped to zero, which was a considerable achievement. The statistics show that up to early June 2014 and before increasing the energy prices, the government has been quite successful. The Central Bank of Iran has announced that the inflation rate for the 12-month period that ended in the second Iranian calendar month of Ordibehesht (May 21) hit 30.3 percent.

Meanwhile, the point-to-point inflation rate hit 16.6 percent. On May 28, Iranian government spokesman Mohammad-Baqer Nobakht stated that the policy of curbing the inflation rate is being pursued. The inflation rate for the abovementioned period had hit 28.4 percent, a 2 percent decline compared to the previous month. He stated that the government has no plans to increase prices of consumer goods.

Group	Percent Change Compared to Previous Month	Percentage Change Compared to Same Month Previous Year
Index	1.2	16.6
The Main Groups		
Food and Beverage	3.4	6.7
Tobacco	0.9	4.9
Clothing and Footwear	2.2	24.1
Housing, Water, Electricity, Gas and Other Fuels	1.4	19.5
Furnishings, Supplies and Services used at Home	1.8	15.5
Health	1.3	31.7
Transport	13.3	29.9
Communications	12.9	10.7
Recreation and Cultural Affairs	0.3	16.2
Academic	0.1	13.6
Restaurants and Hotels	1.7	20.3
Miscellaneous Goods and Services	2.5	19.1
Specific Groups		
Commodity	0.5	13.7
Service	2.3	21

In March, Iranian Finance and Economic Affairs Minister Ali Tayyebnia said the country's inflation would fall below 15 percent in Iranian calendar year 1393 (March 2014, March 2015). After the rise in energy prices, the government announced that there will be a “moderate increase” in the prices. During the said period, fuel prices increased somewhere between 50 and 70 percent; the price of gas for household consumption increased by 25% and gasoline by 34%. The price of subsidized gasoline increased from 400 to 700 Touman and non-subsidized gasoline from 700 to 1000 Touman (Central Bank of I.R. Iran, 2014). According to the latest information, one dollar is equal to 3,200 Touman.

2.3.1.2. The Recession

According to experts, causes of stagflation include a whole series of economic, political, social factors like fiscal and monetary policies, the structure of the budget (means the size of the investment and consumption of the government), unsustainable law and regulations, and wrong decisions that confuse investors; prolonged projects, and increased costs of the production. On the other hand, monetary and fiscal policy such as controlling the liquidity, raising interest rates, tax hikes, and controlling government spending and presenting a budget without deficit are some of the remedies for the inflation. In the same vein, in explaining some of the causes of the country's economic recession, Dr. Rouhani stated that most significant factors that led to the recession are: weakness of the budget allocated to provision of public services especially in investment, along with the intervention of the Central Bank to compensate for the budget deficit by issuing more notes; all of which turned the budget into one of the decisive factors of the deep recession along with high inflation and unjust sanctions imposed on the country (Rouhani, 2014). But based on the abovementioned points, some of the representatives and experts have criticized Dr. Rouhani's budget that it is shrinking, while others have described it as an expansionary budget. There are experts who also believe that some of the revenues of the budget, especially the taxes, are unrealistic. However, since this article is a descriptive paper, here I directly quote a part of the official policies of the new government to overcome the recession. Explaining his government policy to the assembly the president said:

'In the area of fiscal policy, this is the first attempt to redirect the funds from the deepening recession, to stimulate growth. By increasing the oil and tax revenues, we have tried to increase the budget. Overall, as a result of the increase in oil and tax revenues and other sources, the size of the state budget in 2014 reached over 195 thousand billion Touman. It means that compared to the government budget in 2013, it represents an increase of about 50 percent. But in terms of the Capital Acquisition Plan, compared to the programs which were carried out by the previous government in 2013, the budget had increased 3-fold. Based on these policies, government spending would increase economic activity in the following year.

However in the limited time, the government managed to prioritize a series of unfinished projects with respect to their importance and time needed for completion, to reduce the period of exploitation. Therefore, instead of distributing the limited resources to several projects it became possible to concentrate on a few unfinished priority projects only.

Also the possibility of transfer to the cooperative and private sectors and public-private partnership projects were considered for ‘the Capital Acquisition Plan’. On the other hand, due to financial limitations in the supply of public funds, the use of foreign finance (finance foreign exchange) is a priority. Providing advance payments of shares in Riyal for ‘the Capital Acquisition Plan’ the necessary steps were taken. In this regard, the bank is ready to allocate almost $16 billion and activities are underway for reallocation of another amount $6 billion.

In addition, in phase 4 of ‘the Southern Pars’ the efforts had already begun, with expectations that by early 2015 another around 100 million cubic meters of gas per day will be added in the country's gas production. As a result, consumption of liquid fuel in the power plants could be reduced, which provides additional savings in foreign exchange.

The ICT field is another priority of the government for next year. The government intends to develop programs for this sector. Fortunately, it happens to be a self-financing sector. The private sector and especially the young college graduates have major advantages in this field, which would likely increase employment opportunities and benefit the younger generation.

Effective protection for science-based companies is another important priority of the program in year 2014. In this context, government will increase by 20 times the resources allocated to “the innovation and development fund” so that young educated people will be equipped to develop their talents and abilities. The fund currently has a balance of 25 billion Touman. Regarding government companies, their reliance on public funds have been reduced, and companies' commitment to fiscal discipline is being emphasized, to reduce their debts to the banking system, and implement Article 32 of the budget and Article 62 of the Public Audit Act (Rouhani, 2014).

In addition to areas that are directly related to the budget, it is also necessary to delineate a few other important issues. Changing the current situation requires a comprehensive view, in order to develop all facets of the economy. Aside from efforts for boosting investment, we believe the development of the manufacturing activities of the private sector and increasing exports should be included in the government agenda for next year. To achieve this goal, it is necessary to transform the government into a facilitator and productive organization. The government should reduce the administrative barriers for entrepreneurs and improve the business environment. Fortunately, the election created a good public atmosphere and the first phase of the nuclear negotiations was concluded. As a result, speculative activity in housing, currency and coins markets has re-infused dynamism into the capital market. In the coming months, the government is expected to increase the stock supply. Secondly, we introduced certain changes to provide resources for big companies in the capital market. If we succeed, then we can reduce the pressure of large firms on the banking system in order to enable banks to freely support the small and medium enterprises.

Another problem is the recession in the housing sector. The housing sector, while meeting the most basic needs of families, especially young families, is also the driving force for most industrial and service activities. Unfortunately, the Mehr housing project was implemented incorrectly and its inflationary effects due to the complete reliance on the central bank's resources, forced the new government to invest a considerable part of its energy and management resources to remedy the fallouts from the Mehr Housing Plan. The new government is committed to the obligations of the previous government. But after solving the financing problem in the Mehr Housing Plan, the government plans to implement its alternative housing program which can revitalize the housing sector (Rouhani, 2014).

2.3.1.3. The Sanctions

The unjust sanctions on Iran led to economic recession in several aspects: First, uncertainty and impossibility of forecasting the future led entrepreneurs to invest in the short term profits into commodities like foreign currency, gold coins and housing; keeping them away from manufacturing sectors. Second, business limitations and increase in transaction charges led to expansion of the underground economy. Third, intensive financial sanctions imposed on Iranian banks limited their international banking activities, adversely affecting companies and finally limitations on oil exports reduced the government's foreign currency income. Meanwhile six other significant factors also intensified the recession:

A highly import-oriented economy aside from internal inflation and increasing vulnerability of production;

Unfavourable business environment due to constant intervention of government in the economy and unpredictability of its behaviour, leading to a weak private sector;

Intensive increase in the manufacturing costs, especially due to sudden leaps in foreign exchange and energy costs;

Numerous problems created in the banking sector due to policies adopted and imposed by the government, having led to huge bad debts, consequently created strong limitations in financing for the enterprises;

Serious irregularities created in the proprietorship status of the economic enterprises due to unsuitable execution of general policies of the article 44 of the Constitution regarding privatization of state-owned enterprises;

Unstable macroeconomic environment due to skyrocketing inflation and high fluctuations in the foreign exchange rate.

In the realm of foreign policy, the I.R. Iran has chosen dialogue, understanding and confidence building as strategies. If the negotiating parties make use of this opportunity to develop mutual understanding and to reduce tensions, then there could be hope that obtaining a comprehensive solution within internationally recognized rules and conventions is achievable. The new government believes that American and European sanctions against Iran have caused many problems. The new government started negotiations with the superpowers to reduce and remove these sanctions. Meanwhile, Iran insists on its right to retain its peaceful nuclear technology program. No doubt that the atmosphere of the negotiations on the nuclear issue is much more positive than the previous government. The parties to the dispute have had many meetings until now and as a result have signed a document and achieved relatively satisfactory cooperation.

Economic sanctions are undesirable for both sides. Any action that creates problems, both psychological and environmental, in the international economy, will disrupt the free flow of goods and capital. Experience has shown that using the sanction as a limiting instrument for political interests will damage businesses and the interest of the people all over the world (Tayyebnia, Ali, Rokoud Tavaromi, Aftab News,-31/2 1393/ 2014).

2.3.1.4. The Targeted Subsidies Plan

Based on 'the Targeted Subsidies Plan Law (January 5, 2010)' the government, within a five- year period, should remove all the subsidies for several commodities like: petrol, diesel, gas, oil, electricity, water, wheat flour, sugar, rice, cooking oil and milk; which will be offered at prices comparable to the rest of the Persian Gulf region. From that time until today, all citizens will directly receive 45500 Toumans monthly; but according to the law, the government should pay the subsidies only to those who need them. This plan aims to reduce overconsumption, to develop the economy and increase productivity/efficiency; to end the smuggling of subsidized goods abroad, to reduce car traffic and air pollution in the large cities and also to increase social justice. However, the subsidies saved should be distributed as follows: 50% for lower income people, 30% to improve efficiency in various fields, with 20% to be left for the government's disposal.

'The IMF Consultation Mission Team' also prepared a statement on this issue and stated: the design of Iran's subsidy reform has been exemplary and reform remains a priority. The implementation of the first phase has faced significant and varied difficulties and there is a need to make the lessons known to the public. The planned increase in domestic energy prices being forwarded by the authorities is welcome, although the proposed distribution of resources among households and specific sectors presents a departure from the original design; such a departure risks undermining the strong support that was achieved during the first phase. Some measures would be needed to address such risk. First, the contemplated gradual adjustments in domestic prices need to be supported by an automatic adjustment mechanism that is underpinned by strong political support to ensure its full implementation. Second, the process for identifying and excluding less vulnerable groups requires criteria that are simple, transparent, and considered fair. In addition, the distribution of resources for supporting energy-intensive sectors needs to ensure a framework that fosters the adoption of new technologies and tighter budget constraints. In subsequent stages of the reform, transfers were made more conditional on social goals and directed toward private savings for the broader population (IMF, 2014).

However, the Targeted Subsidies Plan was not successful because of improper implementation, the devaluation of the Rial and because the price of subsidized goods remained unchanged. The new government did not include it in the budget and Dr. Rouhani stated: as long as the government does not have an alternative plan for current practices in the subsidies program, these practices will continue. The government is preparing a new plan for the subsidies, for the coming year, which should be approved by the House (Rouhani, 2014).

2.3.1.5. Monetary Policy

As stated in the Monetary and Banking Act of Iran, the Central Bank of Iran is responsible for the design and implementation of monetary and credit policies with due regard to the general economic policy of the country. Four major objectives of the Central Bank as stated in the Monetary and Banking Act are: maintaining the value of the national currency, maintaining the equilibrium in the balance of payments, facilitating trade-related transactions, and improving the growth potential of the country. To achieve the objectives, the Central Bank was given the responsibility of fulfilling the following functions: issuance of notes and coins, supervision of banks and credit institutions, formulation and regulation of foreign exchange policies and transactions, regulation of gold transactions, formulation and regulation of transactions and inflow/outflow of domestic currency (Central Bank of IR. Iran, 2014).

However, the monetary policy in Iran has not been successful in controlling the inflation and achieving the monetary targets set in the Iranian Five-Year Development Plans. Criticizing the performance of the previous government on maintaining the value of the national currency, Dr. Rouhani told to the parliament: ‘the currency rate has not only impacted the budget but it is also an important economic issue for economic actors and the people alike.’ The new government at the first stage faced two major problems in this regard, namely: ‘currency market volatility’ and a ‘multi-tiered system’. As a result of large fluctuations in exchange rates in the economic system, the country unfortunately became increasingly distanced from its internal capacities and dependent on imports. Therefore, to solve this problem “market stability” has become the government's priority. Controlling the liquidity growth facets, especially through tight restrictions on the growth of the monetary base which ensured currency exchange turnover coming from exports in the economic cycle, and recent developments in foreign policy, has helped the foreign exchange market unlike the past two years and the market reverted to relative stability. Currently, the government is busy; planning for the standardization of exchange rates in 2014.

The government will follow the gradual and deliberate path and will not act hastily (Rouhani H, Boudjeh, 2013). Anyhow, according to the Head of the Central Bank, though the increase in foreign exchange earnings had increased the interventional power of the central bank in the foreign exchange market; the reduction of the currency supply, rumours, global and regional crises such as the Ukraine conflict, the atmosphere of talks between Iran and Group 5+1 on the nuclear issue has had an impact on the fluctuations of gold prices in the global market and currency prices (Saif, 2014).

Regarding the independence of the Central Bank, some believe that the government intervention in monetary policy and banking during the previous term was the main reason behind the inflation and irregularities in the banking system. As the Vice President of strategic planning stated, the disruption that occurred in the currency market in the previous years was due to government intervention, meaning that the central bank should be independent in formulating and implementing monetary policy and foreign exchange (Nowbakht, 2014).

2.3.2. Adherence to Upstream Documents

Every government that ever gained power claim that they have followed the upstream documents faithfully. Justifying their plans and programs, they usually focus on their achievements; meanwhile they attribute their faults or failure to domestic opponents and foreign enemies. For example, Ahmadinejad emphasized that the sanctions and foreign plots were the main obstacles in achieving the goals set by the upstream documents.

In recent developments related to declaration of the resistive economic policy, Ayatollah Khamenei asked the authorities to implement these policies and to prepare the necessary rules, regulations and the road map in different fields to provide better opportunities for the economic actors. Accordingly, all the ministries have drawn up detailed plans and programs. Although the details of these programs are not yet widely available; some ministries such as the Ministry of Economy and the Oil Ministry have revealed the more important parts of their programs. For instance, according to Dr. Tayyebnia, Minister of the Economy, the new government wants to reduce the dependence of the budget on oil revenue and intends to deposit 31 percent of oil revenues to the National Development Found annually; so within 4 years, 100% of oil revenues will be directly deposited into the Fund. According to the Minister, to implement the resistive policy, his government did not withdraw even one dollar from the National Development Found last year. On the other hand 'the comprehensive tax plan' will increase the share of tax revenues. In addition, to increase exports, the Finance Ministry has a plan to reduce the time needed for customs procedures by 50 percent just within one year. In addition, the government is preparing a program to cut the subsidies of the higher classes and pay subsidies only to the lower class (Tayyebnia 1393).

In implementing 'the resistive economic policies' the Minister of Oil said in an open session of parliament (18 June 2014), in accordance with Article 14 of the resistive economic policies, his Ministry plans to increase the production capacity for crude oil and natural gas in the shared fields, and the export of gas. Related measures such as increases in the production and exports, enhancing the value added through completion of the oil and gas industry chain, and boosting petrochemical products exports correspond to paragraphs 10, 13 and 15 of the Resistive Economic Policies. Immunization of demand and the markets of crude oil and petroleum products represent another program aimed at fulfilling the policy objective of choosing the strategic customers as well as diversifying the sales of the programs.

The oil minister stated that Iran is planning to increase the production of natural gas up to 1,000 million cubic meters per day and to allot 6 billion cubic meters of gas to produce 5,000 megawatts of electricity. Other programs of the oil ministry include marketing, support for the midstream products, use of new technologies and increasing natural gas exports from $25 billion to $80 billion.

The Oil Ministry Plans to increase the production capacity of crude oil to 2 million barrels and condensation capacity to one million barrel per day; in this regard, by increasing the refineries in the Southern Pars, the capacity of refinery will reach to 3 million barrels. The Minister of Oil stated that Iran should be able to secure many customers and will not have to rely on a limited number of specific customers. It is also necessary to participate and to invest in overseas projects including refineries. As for investments, assuming the sanctions will continue, he stated that the increased stock would be of great help. To develop the petrochemical industries and to increase the number of refineries in the country, every sector should participate in the investments. This way, everyone will benefit and the benefits will not be limited to specific groups (Zangeneh 1393). However, during its one year in power, the government has steadfastly tried to observe the upstream documents, implement the laws and regulations, and as a result, confidence returned to the economy and the market has returned to relative calm.

III. Conclusion

This paper explains the theory, ideals and practical aspects of the economic system of the Islamic Republic of Iran. It tried to consult official and reliable sources and the latest government reports, documents and central bank policies available on the internet. Part of the paper is about the upstream documents such as the Constitution of the IR of Iran and the General Economic Policies, which shows the philosophical and legal aspects of Iranian Economy and its Vision, delineating the ideals and the current problems and policies; and identifying the gap between theory and practice. The paper further seeks to introduce the economic mechanisms, and explain the role of government in the process of codification, adoption of economic policy, and implementation.

However, Iran was confronted with formidable circumstances such as the revolution, the 8 year war and subject to severe sanctions from the United States and Europe, any of which could have brought the country to ruin. Iran stands independent and in some areas like health, education, technology and science have made great achievements. As explained in the last part, in terms of natural and human resources, Iran is a rich country. Therefore, identifying its strengths, weaknesses, opportunities and risks provides grounds for cooperation; meanwhile integrating the information with Iran's economic systems and diversifying market in goods, services and investment will lead to a better and sustainable economy for both sides (Korea and Iran).

This paper aimed to provide an overview on the Iranian economy and could not sufficiently address the details, so based on the general economic policies and the resistive economic policies and short-term plans, it is recommended that a broader master plan be prepared for more accurate and more detailed research on the Iranian economy. Through such an effort, fields for sustained economic cooperation between Korea and Iran can be specified.

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5

Research on Counties' Economic Development of Jilin Province

Ni Jinli[1)]

I. Introduction

With the rapid development of the Chinese economy, some problems that were hidden came gradually to the fore, such as the gap between rural counties and urban centers. So in 2006, Document No. 1 of the Central Government proposed a development of economies of rural counties. Subsequently, many provinces including Jilin Province formulated special policies to accelerate the economic development in rural regions. For Jilin Province, economic development in the counties will not only promote the coordinated development of urban and rural areas, but also determine the scale and level of economic development of Jilin province. This paper summarized the achievements of economic development in county regions of Jilin Province, carried out research on problems that arose during the process of economic development of rural counties, analyzed the reasons that cause the problems, and lastly, forwarded countermeasures and suggestions.

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1) Associate Research Fellow Rural Development Institute, Social Science Academy of Jilin Province.

II. Body

2.1. The Concepts of County, County Region, County Economy (Economy in County Region), and Basic Features of a County Economy

2.1.1. County

County represents one level of local administrative system in China. It is the most basic administrative division for organization and management of local economic and social development. And its power organs are relatively complete.

2.1.2. County Region

County region is a type of administrative regional division. It is a relatively independent social and economic unit. A county region includes many small towns the villages that form a network aside from the county seat.

2.1.3. County Economy (or Economy in County Region)

County economy is a type of regional economy with district characteristics and functions. It make the scope of administrative division as geographical space, political power on county level as the main regulation body and market as guidance.

2.1.4. Basic Features of a County Economy

One feature of the county economy that stands out is synthesis. It means that the county economy is a comprehensive economic system. In general, economic activities in county region involve not only encompasses production, circulation, consumption and distribution; but also includes all three levels of industry: primary, secondary and tertiary. To a degree, it is a microcosm of the national economy. In addition, it has departments for managing both the economy and society.

The other is its inherently rural nature. It means that the vast majority of land and population belong to rural areas. Currently, the county economy of Jilin province still essentially belongs to a rural economy where agriculture is the main industry. In essence, the shift from village to city and from agriculture to a comprehensive industrial system forms the core of economic development in county regions.

2.2. The Achievements of County Economic Development in Jilin Province

The ‘county regions’ in Jilin province are made up of 20 counties, 20 cities on county-level and 2 municipal districts with county functions (Shuangyang District in Changchun city, and Jiang Yuan in Baishan city). The population of county regions is 19.2 million, accounting for 70.4% of the total population of Jilin Province. The total area of county regions is 180,000 square kilometers, accounting for about 96% of the total area of Jilin province(Please refer to Appendix 1).

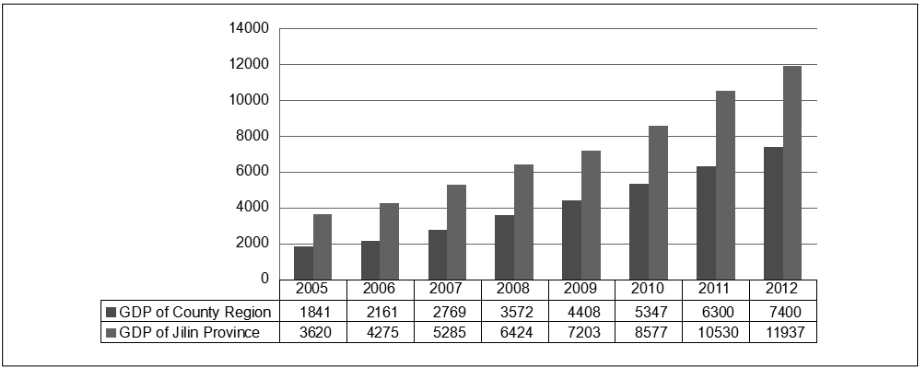
From 2005[2] to 2012, the proportion of counties economy within the provincial economy has increased. Their role in facilitating and contributing to provincial economic development became stronger.

2.2.1. Increase in the Total Amount of Economy

In 2012, GDP of county regions reached 740 billion yuan, or 100 billion yuan higher than 2011, and 4 times that of 2005. The GDP of county regions as a proportion of provincial GDP reached 62%, an increase of 11 percentage points compared to 2005. In 2012, there are 13 counties with GDPs over 20 billion Yuan, and 32 counties with GDPs is over 10 billion Yuan, or 24 counties more than that of 2005. Qianguo County topped the list with 47.63 billion Yuan, followed by Gongzhuling City and Dehui City where GDP reached 34.44 billion Yuan and

2) In 2006, Document No. 1 of Central Government proposed development of county economies. 2005 was chosen as the point of comparison with 2012.

Figure 1. County Region GDP Compared With Total Province GDP



Source: Statistics Yearbook of Jilin 2006-2013.

34.34 Billion Yuan Respectively (See Figure 1)

Economic strength, in per capita, of county regions also increased rapidly. In 2005, per capita GDP of county regions reached 9880 Yuan, accounting for 74% of provincial per capita GDP. In 2012, per capita GDP of county regions reached 39001 Yuan, or 89.8% of provincial per capita GDP, an increase of 15.8 percentage point compared with 2005 (See Table 1).

Local fiscal revenue of county regions also increased significantly. In 2012, local fiscal revenue of county regions reached 32.4 billion Yuan, 5.9 times that of 2005. It accounted for 31.1% of provincial fiscal revenue, which increased by 4.7 percentage points compared with 2005. There were 14 counties with local fiscal revenue greater than 1 billion Yuan. Yanji City topped the list with 2 billion Yuan, followed by Meihekou City and Jiutai City, which had 1.6 billion and 1.5

Table 1. Changes in Counties' Per Capita GDP

	Per Capita GDP (Yuan)	Accounting for Provincial Per Capita GDP (Yuan)
2005	9880	74.0
2012	39001	89.8

Source: Statistics Yearbook of Jilin 2006 and 2013.

Table 2. Changes in Counties's Local Fiscal Revenue

	Counties' Local Fiscal Revenue (Billion Yuan)	Provincial Fiscal Revenue (Billion Yuan)	% of Provincial Fiscal Revenue
2005	5.5	20.7	26.4
2012	32.4	104.1	31.1

Source: Statistics Yearbook of Jilin 2006 and 2013.

billion Yuan respectively. In 2005, only Yanji City's local fiscal revenue was more than 500 million Yuan. The increase in financial power not only demonstrated the effectiveness of counties' economic development in recent years, but also further strengthened the capacities of counties for self-development (See Table 2).

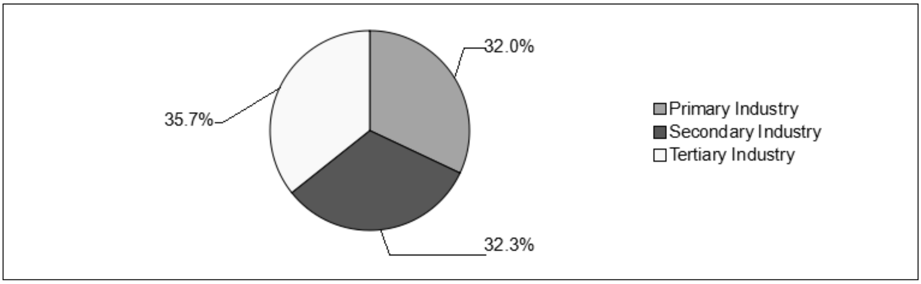
2.2.2. Optimization of Industrial Structure/ Acceleration of Industrialization Process

In the process of counties' economic development, each county implemented strategies for industry strengthening, expansion of industries, promotion of openness and changes, and make industrial economy a priority in their push forward. So the economic structure in county regions has undergone significant changes. The proportion of primary industry continuously declined, and the proportion of secondary and tertiary industries increased year by year. The proportion of three industries was changed from 32.0:32.3:35.7 in 2005 to 18.9:44.2:36.9 in 2012. The proportion of primary industry had dropped by 13.1 percentage points. Secondary and tertiary industries increased by 11.9 and 1.2 percentage points. The industrial structure of counties economy was further optimized and upgraded (See Figure 2 and 3).

Industries in county regions grew steadily and took shape as a result of such development. A large number of mainstay industries with strong development potential and good market prospects were formed and laid a solid foundation for enlarging and strengthening county economies. In 2012, there are 3176 industrial enterprises above the designated size[3)] in county regions, or double that of 2005. They collectively generated an industrial output value of 727 billion Yuan, accounting for 36.4%

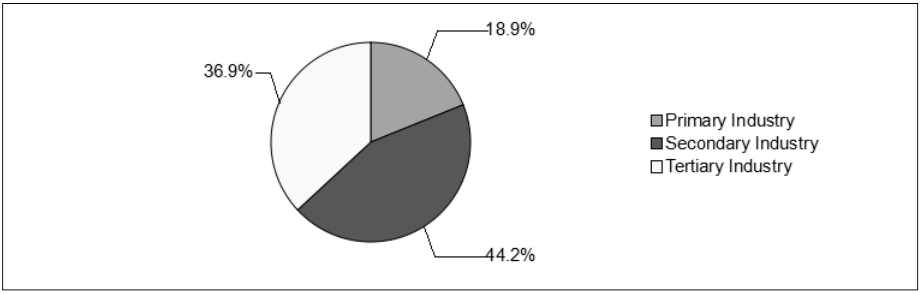
of output value of industrial enterprises of the provinces (above designated size), which increased by 16.2 percentage points compared to 2005 (See Table 3).

Figure 2. Proportion of Three Industries in 2005



Source: Statistics Yearbook of Jilin 2006-2013.

Figure 3. Proportion of Three Industries in 2012



Source: Statistics Yearbook of Jilin 2006-2013.

Table 3. Output Value of Industrial Enterprises above Designated Size

	Amount (In County Regions)	County Regions (Billion Yuan)	Province (Billion Yuan)	County Regions' / % of Province
2005	1561	78.1	379.2	20.2
2012	3176	727	1997.2	36.4

Source: Statistics Yearbook of Jilin 2006 and 2013.

3) Main business income is over 20 million Yuan.

2.2.3. Resident Incomes Increasing, Process of 'Well-off' Accelerating

The implementation of preferential agricultural policies allowed achievements of reform and openness to benefit the masses greatly. Case in point, county residents' income increased continuously. In 2005, per capita net income of farmers was 3264 Yuan, while it was 8598 Yuan in 2012, which was 2.6 times that of 2005. In 2012, per capita net income of farmers in Yanji City was more than 10,000 Yuan. There are 10 counties with per capita income of more than 9000 Yuan, 15 counties which were more than 8000 Yuan. In 2005, only Yanji City had more than 4000 Yuan.

As a result, more household appliances found their way into the homes of ordinary people. In recent years, with the rapid development of county economies, the living standards of urban and rural residents continued to improve, along with the quality of life in general. Refrigerators, washing machines, air conditioners, microwave ovens, digital cameras, cars, computers and other large durable consumer goods have also gotten into the homes of ordinary people. In 2012, the number of civilian vehicles in county regions reached 687,000; or 3.1 times that of 2005. Out of this figure, private vehicles have reached 321,000 accounting for 46.8% of civilian vehicles.

Welfare projects were implemented and major strides were made in the social security system. The social security coverage was gradually expanded. In 2012, the number of persons participating in the basic pension insurance reached 1.7 million, an increase of 30.3% compared with 2005. The number of persons participating in the basic medical insurance reached 4.1 million, an increase of 3.2 times relative to 2005. The number of persons participating in unemployment insurance reached 977,000; an increase of 15.4 % compared with 2005. The number of rural residents enjoying the minimum living guarantee reached 757,000; an increase of 64.5 % compared to 2005.

2.2.4. Increasing Potential for Economic Development

From 2005 to 2012, the macro-economy of Jilin macroeconomic continued to improve. With the rapid growth of incomes of urban and rural residents, consumer demands and markets remained continuously active. In 2012, total retail sales of consumer goods in the county regions were 215.8 billion Yuan, or 3.5 times that of 2005. The proportion counties' consumption in the province rose from 41.9% in 2005 to 45.2% in 2012, increasing by 3.3 percentage points. Total retail sales of consumer goods in Yanji City and Meihekou City reached 17.2 and 10.5 billion Yuan respectively; in 2005, only Yanji City recorded sales of over 4 billion Yuan (See Table 4). In 2012, total investment in fixed assets in county regions completed 487.6 billion Yuan, to be 9 times that of 2005. The investment in counties as a proportion of investment in the provinces rose from 33.1% in 2005 to 52.6% in 2012, an increase of 19.5 percentage points (See Table 5). Active consumer markets and increased investment in fixed assets year by year increased the potentialities of economic development.

Table 4. Total Retail Sales of Consumer Goods in County Regions

	County Regions (Billion Yuan)	Province (Billion Yuan)	County Regions /Province %
2005	61.3	146.3	41.9
2012	215.8	477.3	45.2

Source: Statistics Yearbook of Jilin 2006 and 2013.

Table 5. Total Investment in Fixed Assets in County Regions

	County Regions (Billion Yuan)	Province (Billion Yuan)	County Regions /Province %
2005	54.4	164.3	33.1
2012	487.6	926.2	52.6

Source: Statistics Yearbook of Jilin 2006 and 2013.

2.3. Problems

There were significant changes in economic development of counties in Jilin province year by year through longitudinal comparison. County economies of Jilin Province had entered a period of rapid development. However, compared with the county economies of top hundred counties or developed areas, there is still a large gap and there are many problems to be resolved.

2.3.1. Low Level of Economic Development

There exists a big gap between county regions of Jilin province and top hundred counties regarding not only the total amount of the economy, but also per capita GDP and fiscal revenue. With respect to the total size of county economies, the average value of top hundred counties was 57.8 billion Yuan in 2012, while it was just 17.6 billion Yuan in Jilin Province, or less than 1/3 of top 100 hundred counties. Regarding Per capita GDP, county regions of Jilin Province had an average per capita GDP of 38.9 thousand Yuan, or only 56.1% of average of top hundred counties. As for the distribution of top hundred counties, 25 counties were in Jiangsu Province, 24 in Shandong Province, and Zhejiang province had 20 counties. While in Jilin, only Yanji City of Jilin province was one of top hundred counties recently. Regarding fiscal revenue, local fiscal revenue in county regions of Jilin province accounted for 31% of total provincial fiscal revenue in 2012, while in Shandong and Jiangsu Province, the local fiscal revenue in county regions had already surpassed

Table 6. County Regions in Jilin Province Compared with Top 100 Counties (2012)

	Average GDP (Billion Yuan)	Per Capita GDP (Yuan)	Average Fiscal Revenue (Million Yuan)
County Regions in Jilin Province	17.6	38938	769
Top 100 Counties	57.8	69408	3939

Source: Statistics Yearbook of Jilin 2013 and Statistics Yearbook of China 2013.

70% of total provincial fiscal revenue. The average local fiscal revenue in county regions of Jilin province was 769 million Yuan, while the average fiscal revenue of top hundred counties was 3.9 billion Yuan, which is more five times that of Jilin Province (See Table 6).

2.3.2. Uneven Development of County Economies

Currently, there is no equality in terms of development of county economies. First of all, relatively developed counties are mainly concentrated in central region of Jilin Province. And economic development in counties of eastern and western areas of Jilin Province is relatively weak. There are 14 counties in the central region whose total GDP was 356.9 billion Yuan or 48.2% of the GDP of all counties in Jilin in 2012. Secondly, the county with the largest GDP was Qianguo County with 47.6 billion Yuan, and the smallest one being Changbai County with only 3.4 billion Yuan–a difference of more than forty billion Yuan difference. The county with the largest per capita GDP was Qianguo County, with 79,000 Yuan; the smallest one was Longjing County where the per capital GDP was only 20,000 Yuan. This represents a difference of nearly 60,000 Yuan between the richest and poorest two counties. Thirdly, the county with highest per capita net income of farmers was Yanji City with a figure of 10,040 Yuan; the country with the lowest per capital GDP was Daan City, with 4780 Yuan (See Table 7).

Table 7. Strong County Compared with Weak County (2012)

	GDP (Billion Yuan)	Per Capita GDP (Yuan)	Per Capita Net Income of Farmers (Yuan)
Largest County	47.6 Qianguo County	79909 Qianguo County	10040 Yanjj City
Smallest County	3.4 Changbai County	20041 Longjing County	4780 Daan City

Source: Statistics Yearbook of Jilin 2013 and Statistics Yearbook of China 2013.

2.3.3. Irrational Industrial Structure

The proportion of primary industry in county regions has been higher, and the predominance of typical agricultural economy is obvious. Secondary industries, on the other hand, are not prominent. The industries in county regions have made great progress in recent years, but they are still in the initial stage of nurturing enterprises. The traditional and small enterprises are the majority. In 2012, industrialization rate in county regions was 39.5%. County economies are still in the early stage of industrialization, and the task of completing the industrialization process is a very arduous one. The proportion of tertiary industry is relatively higher, but it is not strong enough to support the economic development on its own because of its late start, small scale and weak foundations. The industrial structure which has been formed for many years simply cannot be changed overnight, although the much readjustment of industrial structure in counties economies has taken place in recent years The proportion of three industries changed from 32:32.3:35.7 in 2005 to 18.99: 44.15:36.86 in 2012. The proportion of primary industry declines, and proportion of secondary industry rise year by year. But changes in the data can only reflect on the quantitative changes. The industrial structure has still not been well optimized, and industrial structure has yet to change qualitatively.

2.3.4. Low Level of Urbanization

Urbanization of county regions of Jilin province proceeded slowly, and not very good in qualitative terms. The urbanization rate in county regions was only 37.3% in 2012. Regarding the scale of urbanization, in 2012, average population of 42 county seats (or county-level cities) was 137 thousand. Only 8 county seats had a population of more than 200,000; 20 county seats had a population of less than 100,000; and 5 county seats had a population less than 50,000. There were even 18 county seats that experienced negative population growth.

2.3.5. Serious Shortage of Financial Resources and Talent Pool

The dearth of financial resources has remained an obstacle that plagued local economic development. Regarding fiscal revenue, local fiscal revenue of county regions only accounted for 4.4% of GDP in 2012. From 2005 to 2012, local fiscal revenue of county regions increased by an average of about 3.8 billion Yuan a year. Regarding fiscal expenditure, the local fiscal expenditure of county regions was 21.8 billion Yuan and 97.9 billion Yuan in 2005 and 2012 respectively, an increase of an average of 10.9 billion Yuan a year; meaning that increased fiscal revenue lags far behind increased fiscal expenditure. As a result, financial resources of county regions dwindled further and became more insufficient. The fiscal revenue in county regions can barely meet normal expenses and does not leave much for local construction.

Due to environmental differences, inaccessibility and low treatment, the factors that would attract and gather talented persons are few and far between. Not only do fewer college graduates return to their hometowns, but what talent that exists in local counties continues to leave. Thus economic and social development in county regions lack sufficient local talent to move forward.

2.3.6. Industrial Structure Similar, Distinctive Economy not Prominent

Regarding the internal structure of industries in county regions, the proportion of agriculture, forestry, animal husbandry and fishery are similar for most counties, with agriculture comprising the main part. In 2012 output value of agriculture, forestry, animal husbandry and fishery in county regions was 232.5 billion Yuan. Among them, agriculture output value accounted for 124.2 billion Yuan, or 53.4% of all primary industry production. The structure of planting industry is similar in many countries with corn and rice being the main crops. Regarding secondary industry, small and preliminary processing of agricultural products was the most prominent form of secondary industry in each county. Regarding tertiary industry, traditional service industries are the majority such as commerce, catering, transport and postal services. There are emerging yet underdeveloped industries such as finance and insurance, information consultation, comprehensive technical services etc. The key factor of economic development in counties lies in the formation of distinctive industries in some degree. Currently, most counties do not take advantage of their own geographic location and natural resources. Therefore, they lack competitive industries, and a number of well-known companies and brands around the country are unable to find a breakthrough point with respect to economic development. Industrial advantages are not obvious.

2.3.7. Private Economy Weak: Lack of Motivation for Economic Development

The private economy is easily the most active part and has most potent growth factor in a market economy. While state-owned enterprises of Jilin province have represented a large proportion of the national economy, in 2002, the proportion of state-owned enterprises still account for 82% of enterprises above the designated size in Jilin Province. At present, the proportion of state-owned economy has dropped to slightly below 50%, which is still more than 10 percentage points higher than the national average of 35%. Compared with the state-owned economy, the quantity and scale of private economy is small. In 2012, there were 145,000 private enterprises in Jilin province, accounting for only 1.2% of private enterprises in China. There are only 42 private enterprises for every ten thousand people in Jilin Province, while in Jiangsu and Zhejiang Province, every ten thousand people have 118 and 96 private enterprises respectively. So the difference in total amount is very obvious.

Meanwhile, there are only 3,051 private enterprises whose business income is more than 100 million Yuan. Only Dacheng(Corn deep processing), Xiuzheng (Pharmaceuticals) and Haoyue (Beef processing) were included in the list top 500 Chinese private enterprises. In terms of scale, the proportion of small/micro private enterprises reaches 97.9%.

Regarding private economic development, every county is placing greater emphasis on the introduction of external capital, especially for big projects with over 100 million Yuan, and do not devote sufficient attention to development of local small/micro private enterprises development. So, private enterprises are small scale and make little profits due to lack of capital, technology and human resources. Its role in promoting the local economy is very limited.

2.4. Causes Analysis

2.4.1. Loss of Opportunities for Earlier Development

At the earlier stage of reform and opening up in 1980s, the township and village enterprises grew and developed rapidly around the country, especially in the southeastern coastal areas because of era of shortage economy. Jilin province is in the northeast, and represents China's old industrial base. The proportion of state-owned enterprises has been large. State-owned enterprises towered over other businesses, under which township enterprises of Jilin province were not able to start up early, develop quickly, or form industrial groups of township enterprises to provide the necessary foundation for industrialization in county regions. However, in the 1990s, private economy started to develop rapidly around the country. This corresponds to the time that Jilin province mainly focused on the reform of state-owned enterprises. Thus the private economy did not get the opportunity to develop. Industrial foundation in many county regions remained weak due to lack of technology and talent. For the county economies of Jilin Province, it represented a lost chance for capital primitive accumulation at the era of shortage economy. In 2000, the GDP of county regions in Jilin Province was barely 105.5 billion Yuan, the average GDP of each county at a paltry 2.5 billion Yuan. While in Zhejiang Province, the average GDP of each county is 6.9 billion Yuan or 2.8 times that of Jilin Province. So compared with more developed areas, county economies of Jilin Province were already lagging behind.

2.4.2. The Shackles of Administrative Management System

Regarding the administrative management system, China has a system where county governments are administrated by the city government (on prefecture-level), and city governments are administrated by the provincial government. The result of having such a system is that the power of higher authorities is strengthened continuously. The powers and financial resources rise to a higher level and all kinds of production factors go toward large cities, enterprises and projects continuously; economic management power of county governments become very limited. County governments lack functions and means that would make them more efficient. In terms of policy and funding approval, county governments encounter many difficulties such as many intermediate links, low management efficiency and high management costs etc. Their capacity to contribute to local economic development were weakened. County governments thus are unable to take on the heavy responsibility to drive development of county regions.

2.4.3. Government Functions not in Place

Government functions show clear signs of “dislocation” and “absence”. First of all, the “dislocation” of government function means that government is directly involved in economic activities. The government undertakes the whole management and operation of enterprises, rather than providing support and assistance for economic development. Secondly, the “absence” of government function refers to a phenomenon where it do not provide public services it should have. Merely supplying public products and serving society are not sufficient. In some regions, bureaucracy and selfish departmentalism is rife, combined with poor ‘sense’ for providing service. The approval procedures are complicated and many items are charged. Excessive management and insufficient services thus restrict economic development in county regions.

2.4.4. Location Conditions

Although Jilin Province border on Russia and North Korea, its geographic conditions are not favorable. Compared with the developed coastal and eastern provinces, Jilin Province is a typical inland province with long winters. This greatly inhibits its transport, tourism, natural resources exploitation and industrial expansion. In remote inland areas of the province, the transportation network has not yet even formed, most nearby railways are of ordinary types; and high-speed railway is deficient. Also, the highway network between cities has not formed in the province. This makes it very difficult to attract capital, talented workforce and big enterprises. Unfavorable location conditions are not only factors hindering economic development of counties, but factors that impact future development negatively.

2.4.5. Undeveloped Market Economy

Because Jilin Province is in the process of institutional transformation and industrialization, the development level of the market economy is not very high. There are factors hampering the formation and development of a unified regional market such as industrial monopolies, regional blockade, urban-rural split, Logistics and information network platform not supporting etc.

Marketization process of Jilin province lagged behind developed provinces, and market constraints have become the main problem of affecting economic development in county regions.

2.4.6. Traditional Ideals Becoming Impediments

There is much negative impact resulting from traditional ideal in Jilin Province, which points to deep and lingering influence of a planned economy and peasant mentality,[4] in addition to weak sense of innovation. As a province where the

4) Due to making production in a small piece of land to meet their own requires for long time, no constraints, coordinations and exchanges, farmers gradually form the ideas and habits which show as conservativeness.

proportion of agriculture is still large, peasant mentality resulting from traditional agricultural production are deeply ingrained in people's thinking. The relatively abundance of resources has the led to attitudes of contentment with the current situation. The long years under a planned economy led to attitudes of dependency among the people as well as a tendency to adhere to rules or orders.

2.5. Countermeasures

County economies will take on greater meaning, and become more diversified and profound in the future. On the one hand, it will be charged with the important task as the main staging areas of Chinese manufacturing transition. On the other hand, most county regions will preserve their rural character and ensure food and ecological security for the foreseeable future.

2.5.1. Carry out Administrative Management System Reform of Counties Directly Administered by Provincial Governments

Effective management system represents an important impetus with much impact on regional economic development. It involves the critical issue of how to make the counties economy release greater vigor by administrative reform in county regions. After 2005, the provincial government began to delegate power to county governments. There were 343 authorities were delegated and 144 authorities were trusted to county governments. Some key governmental powers were delegated to county government such as the approval for construction land and projects etc. That provided breathing room for economic development of counties. Currently, in addition to furthering expanding the power of county governments to stimulate economic vitality in county regions, such as ensuring sufficient rights over economic resources configuration and economic benefit distribution, Jilin Province need to accelerate the pace of reforms related to counties directly administered by the province, and completely eliminate restrictions and inefficiencies caused by management system were prefecture-level cities manage counties. The experiences of provinces which carried out management system of direct provincial administration of counties show that this kind of management system will greatly improve operational efficiency of economic development, and produced visible impact on economic development. The scale of administrative division of county regions in Jilin Province is small. There are only 42 counties where direct provincial administration need to be carried out, bringing it well within the range of feasibility.

2.5.2. Change from Government-led to Market-decision

Currently, county governments are the key to economic development, and county economies clearly show that governments are leading the way in economic development in Jilin Province. County governments have great power on the direction and process of economic development. They perform much of the work on investment, industrial parks establishment and urban construction. But this means that from the perspective of the market economy, the market does not play a decisive role. So government powers should be limited and the role of government should be circumscribed within reasonable limits. County governments should not be involved in economic activities, and should not attempt direct administrative intervention in the operating activities of enterprises. The government-led economy should be changed into a government-service economy. County governments should only concern itself with ensuring normal and healthy operation of the market. As defenders of the market economy, governments should instead display greater resolve toward problems of “market failures”, and make efforts to create a favorable market environment for fair competition of enterprises through better market supervision, public services, social management and environmental protection etc.

2.5.3. Give Full Play to Comparative Advantages-Develop a Distinctive Economy

Regarding industrial structure of county economies, we should neither emphasize on “small and complete”, nor simply pursue equal proportion of three industries, but emphasize differences in characteristics and competitiveness. This is because that the scale of county economies is relatively small, and they cannot expand in all directions. Counties only can give full play to its advantages, and follow their own directions for distinctive development. In Kunshan City of Jiangsu Province, there are no advantages for tea growing. But the annual sales income of “Uni-President Green Tea” reached 600 million Yuan. It is also not the main production areas of wheat, but the annual sales income of “Uni-President Instant Noodles,” reached more than 800 million Yuan. To a certain extent, creation of a distinctive economy depends on sales and can only develop amidst market competition. Economic development of counties should take place in the light of local conditions in Jilin Province. If agriculture is suitable for the local economy, agriculture should be developed. It is the same with industries, commerce and tourism are the same. During the process of exploring resources, counties should recognize not only their natural conditions, but also the human factors; not only the immediate reality, but also the potentiality; not only the tangible, but also the invisible. Counties should make a breakthrough according to actual situation, in areas which caters to their personality and competitiveness. Through scientific argumentation and timely development, counties should develop the related industries and increase comparative advantages. Find a method of development which is suitable for its own features.

2.5.4. Develop Private Economy

It is an indisputable fact that private economy of Jilin Province is lagging behind.

In terms of the development trend of county economies, private economy has the prominent features of clear ownership, property right and flexible mechanism. It shows greater vitality and tends gradually to become major part of county economies. Wenzhou City of Zhejiang Province has neither location advantages, nor advantage in terms of natural resources. Its rapid development, however, benefitted from development of private economies. Thousands of families have come to operate factories, and millions of people broke into the market. Jilin Province must now move in a direction of developing the private economy to speed up the economic development of counties by utilizing people's wisdom, attracting private capital, and relying on collective strength of the masses. First, the provincial government should foster the spirit of entrepreneurship, involving creation of appropriate platforms and a good atmosphere for entrepreneurship. Second, the provincial government should carry out systematic engineering and construction work to attract, support, stabilize and strengthen merchants. It must engage in efforts to attract some of the ‘top 500 enterprises’ and central government enterprises to settle in county regions. Third, government should encourage large-scale enterprises to establish a modern enterprise system, expand production scale, and promote development of other private enterprises. Fourth, the provincial government should create a favorable and relaxed environment for development of small and micro enterprises, and enhance their development through policy support, tax relief, etc.

2.5.5. Undertake Industrial Transfer Based on Regional Integration.

With the gradual increase in land prices and labor costs in regional center cities, some industries will inevitably be transferred to county regions. On the one hand, counties can strengthen industrial support and expand the overall size of the economy through the introduction of a number of significant projects with potential to drive the economy forward. On the other hand, foreign industries can promote development of local enterprises, foster and strengthen market players by building industrial value-chains and improve supporting industries. During the process of regional integration, Jilin Province should seize this opportunity to undertake industrial transfer. First, counties should formulate systematic industrial plans, further refining the industrial division of labor, and enhance specialized production capacities of related industries in county regions. Second, counties should abandon selfish motives, break the boundaries of administrative divisions, and willingly serve regional center cities in a supporting role. However, counties should be bold in seeking out their respective positions on the downstream of industrial value-chains, and promote their own comparative industrial advantages. Third, due to restrictions in funding, technology and talent, it is not possible to build too many factories in county regions. So counties should start from production of spare parts, and then gradually move up to production of specialized, completed products.

2.5.6. Expedite Opening of County Economies

County economies must become more market-oriented in accordance with conditions of the market economy. They must seek to move beyond the boundaries of county regions to develop the economy, control resources within a larger area, and establish competitive advantages. Counties should further enhance the opening trend; and insist on implementation of trailblazing strategies regarding opening of their economies. By taking advantage of the unique geographical conditions of Jilin Province, counties should be able strengthen international cooperation in this region of Northeast Asia, and promote development and opening up of the area around the Tumen River. With Hunchun International Demonstration Zone as the window; the cities of Yanji, Longjing, and Tumen can become frontiers of this opening process; and with major cities like Changchun and Jilin acting as main bases of support; joint developments and opening up of borders and hinterland can be carried out. Counties should promote multifaceted cooperation and exchanges with Russia, Japan, South Korea, North Korea and other neighboring countries in trade, resources, science and technology. Counties should speed up construction of port facilities, and develop border and intercity trade, along with entrepot trade to promote local economic development.

2.5.7. Complete Plans for Economic and Social Development of County Regions as a Whole

After many years of development, the economies of countries in Jilin Province have accomplished much. But compared to economic growth, social development in county regions is seriously lagging behind. Therefore, economic development in counties should be coordinated with politics, culture, education, medical care, environment, and public services etc.

III. Conclusion

Through the indicators of economic development of counties in 2012 compared with that of 2005, we find that much has been achieved regarding economic development in counties of Jilin Province. But a comparison with the top hundred counties and developed provinces elsewhere in China, it is easy to discover that there is still a significant gap that must be bridged.

Currently, economic development in Jilin's counties is confronted with many difficulties and constraints, such as dislocation and absence of government functions, unfavorable geographical conditions, underdeveloped market economy etc. These difficulties are an indication that it will take time for countries of Jilin reach the level of top hundred counties of China. Industrialization, urbanization and agricultural modernization in county counties, needless to say, involve a long, drawn-out process.

Yet there are also visible changes in environment for economic development of counties that are taking place. With the rapid progress of regional economic integration and urbanization, the formation of "economic circles" and "economic zones" with major cities as the core developed rapidly and displayed economic vitality. In the course of this development, the rise of county economies as the basic regional economic unit confronts with significant opportunities for development. Giving full play to comparative advantages, speeding up collaboration with the core cities and other economies are the key points in county economies adapting to regional economic integration and accelerating ongoing development.

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Appendix.

Economic Development in County Regions of Jilin Province (2012) (100 Million Yuan)

	GDP	Fiscal Revenue	Investment in Fixed Assets	Total Retail Sales of Consumer Goods	Per Capital Net Income of Farmers (Yuan)
Nongan County	316.9	12.4	165.7	92.8	8694
Yushu City	340.5	10.0	198.2	93.7	9260
Jiutai City	331.9	15.1	187.5	90.0	8885
Dehui City	343.4	11.8	195.1	94.7	9465
Shuangyang District	185.0	12.5	133.0	98.4	8820
Sulan City	183.4	5.5	133.5	58.8	8794
Jiaohe City	194.9	6.3	154.5	57.3	9175
Panshi City	285.1	10.9	190.7	66.9	9186
Huadian City	271.6	12.8	174.7	66.6	9251
Yongji County	121.7	6.6	107.4	34.0	8424
Gongzhuling City	344.4	14.7	237.9	125.9	9197
Shuangliao City	180.8	4.7	75.2	44.1	8391
Lishu County	325.5	6.4	57.3	62.9	8884
Yitong County	142.6	4.5	50.4	37.5	8351
Dongliao County	120.5	4.0	96.2	15.2	8405
Dongfeng County	136.9	6.5	162.3	36.2	8693
Meihekou City	247.8	15.6	167.8	105.2	9540
Jian City	83.0	7.4	104.0	33.3	8711
Huinan County	80.6	6.6	106.9	40.4	9220
Liuhe County	86.7	7.6	96.0	38.7	8393
Tonghua County	115.7	8.7	117.1	28.2	8653
Linjiang City	83.5	5.4	73.4	26.0	8982
Fusong County	151.2	10.2	117.2	35.6	9332
Jingyu County	56.3	3.7	48.7	15.2	4947

	GDP	Fiscal Revenue	Investment in Fixed Assets	Total Retail Sales of Consumer Goods	Per Capital Net Income of Farmers (Yuan)
Changbai County	34.3	2.9	40.5	7.5	7849
Jiangyuan District	139.4	1.7	121.9	23.5	8588
Yanji City	282.7	20.2	184.5	172.4	10040
Tumen City	38.8	2.6	3.0	13	8219
Dunhua City	156.9	10.6	107.4	74.1	9431
Hunchun City	125.2	10.8	102.4	38.1	8578
Longjing City	35.1	2.7	32.3	10.3	5036
Helong City	53.7	3.6	40.4	13.2	5133
Wangqing County	58.1	4.8	54.4	16.7	5031
Antu County	58.5	3.8	51.1	13.6	5241
Fuyu City	336.1	3.6	140.2	86.0	8755
Qianguo County	476.3	11.3	187.7	130.2	9189
Changling County	245.5	3.5	153.4	75.0	7930
Qianan County	185.5	7.3	131.8	40.3	8268
Zhenlai County	112.5	4.8	86.7	21.1	5120
Tongyu County	102.0	4.6	75.8	25.9	5314
Daan City	121.4	7.7	82.7	23.9	4780
Taonan City	110.5	4.1	90.6	26.9	7760

6

Industrial Policies: A Comparison between Korea and Turkey

Murat A. Yülek[1)]

I. Introduction

Korea and Turkey are among the fastest growing economies since 1960s globally. However, Korean economic and developmental progress has been more impressive than that of Turkey. It is arguable that the differences in design and implementation of their industrial polices may have led to different industrialization paths, patterns and end points.

Moreover, their current industrial policies together with science, technology and innovation (STI) policies will no doubt determine the path of their future development under more severe global competitive pressures than in previous decades. A comparative analysis of industrial policies along with STI policies may consequently prove useful for the decision makers in both countries as well as other developing countries.

This paper looks at the key features of industrial and STI policies in the two countries on a comparative basis covering past as well as current records.

1) Professor, Department of Economics, Istanbul Commerce University.

In the second section, Turkey's current industrial policies are reviewed in a historical perspective. In the third Section, Korea's industrial development and current industrial policies are reviewed. The fourth Section undertakes a comparative assessment of policies in the two countries. The last section concludes the paper.

II. Turkey's Industrial Strategy in Historical Perspective

2.1. A Brief History an Assessment of Turkey's Industrialization before 2002

Turkey can be considered as a ‘late-late industrializer’ in Vogel's (1991) terms. Early industrialization efforts started mostly in the second half of the 19th century during the reign of Sultan Abdulhamid, coinciding with rapid development period of another late-developer, Japan. Ottoman industrialization efforts consisted of state-led establishment of various industrial premises and a parallel reform of the educational sector which involved sending students to western countries. However, compared to Meiji Japan, policies were less focused and less export oriented and the country also lacked the economic and reform elites seen in Japan at the time. Consequently, the results were not as successful as the Meiji industrialization, partly also due to continued domestic and international political pressures.

Turkish industrialization picked up immediately after the establishment of the Turkish Republic. Atatürk, the founder and the first President of the republic attached a great importance to economic independence and industrialization. During the early years of the Republic, a set of distinct–though ad hoc–industrial policies were implemented to establish industrial facilities in four main targeted industries: textiles, steel, chemical and metallurgical sectors.

As private sectors' capital accumulation and entrepreneurial skills were inadequate in war-torn Turkey, industrial policy was to be implemented by the leadership of the Government. As a result, most of the major industries, heavy or light, were established by the Government with a view towards subsequent transfer to the private sector. The state-owned large conglomerates (such as Sumerbank and Etibank) also had banking windows. A novelty in those years, it meant direct financing and financial intermediation into the state-led industrialization.

Following the Second World War, a democratically elected government came into power in 1950. During the ten years until 1960, an ad hoc liberalization together with continued but slowing industrialization drive followed. Some private sector businesses have already grown by that time. But they were mostly interested in commercial rather than industrial activities. While liberal in nature, the Government failed to put in place proper incentive mechanisms for a private sector led-industrialization. As the government's attention turned towards road infrastructure and agricultural self-sufficiency, state-led industrialization also slowed down.

The process of democratization was derailed in 1960 following a military coup and the military courts' ruling of capital punishment for the Prime Minister and two other Ministers. The coup also brought some structural changes in policy making. Particularly, developmental planning has been introduced. Though there was an effort towards industrial planning in Turkey during the 1920s and 1930s, the new planning tools were more comprehensive, covering all sectors of the economy. The plan was based on the macroeconomic model of the Turkish economy and had some qualitative and/or quantitative targets for a wide range of individual sectors and sub-sectors.

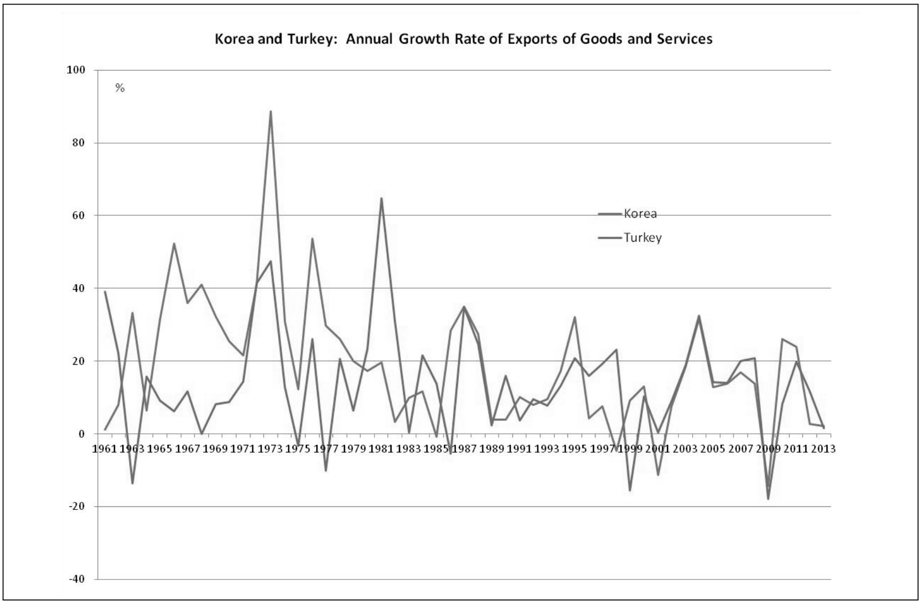
The so called “planned-period”[2] that lasted until the start of liberalization in the 1980s also exhibited strong tendencies of import substitution based on licensing requirements and duties on all imports. The capital account was closed. Heavy price controls were in place. State investments in manufacturing along with infrastructure continued but the private sector, driven by entrepreneurship and tax

2) Development planning is still conducted in Turkey. The phrase ‘planned period’ generally refers to 1960-1980 when planning went hand in hand with import substitution and protective policies.

incentives, took an increasingly important role in the economy. With the objective of boosting private investments (mainly in the industrial sector), financial markets were repressed to direct low cost bank lending to mainly industrial sub-sectors covered by the annual_industrial incentives programs. Banks received low-cost credits from the Central Bank if they lent to firms in those subsectors, thus further reducing the lending costs.

During this period, Turkey rapidly industrialized (Table 1) but were missing a number of important factors. Firstly, export orientation was almost entirely neglected. The ensuing introverted industrialization has provided almost no incentives to Turkish businesses (state or private) to be internationally competitive both in terms of cost and quality/technology. Figure 1 shows the growth rates of Turkey's exports in dollar terms together with Korea's. During the 1960s and 1970s Turkish export growth was subdued significantly whereas Korea's exports exploded. Table 1 shows

Figure 1. Export Growth: Turkey and Korea



that once the economy opened up to international markets in 1980, manufacturing rapidly became the driver of exports.

Secondly, while there was an effort to target certain sectors, decoupling from the international markets and market information led to a strong focus on the needs of the domestic market. So, the ensuing sectoral specialization was not did not follow global market conditions and evolution. For example while Japanese and Korean policies favored electronics and shipbuilding in around the same years, these sectors were not among the priorities in Turkey.

Thirdly, the policies were also not comprehensive in considering upstream and downstream industry linkages and their future evolution. For example while textiles were targeted and succeeded in making Turkey a large producer, manufacturing of textile machinery were not among the priorities.

Fourthly, technology aspects were overlooked; Turkish industrialization was basically a drive to accumulate capital goods imported from abroad. That explains the resilience of import dependence even now. As Table 1 shows, exports-to-import ratio fell considerably during the 1960s and 1970s, and could not go beyond a

Table 1. Turkey's Manufacturing Exports

	Total Exports (Million USD)	Per Capita Exports (USD)	Share of Manufacturing in Total Exports (%)	Exports/ Imports
1950	263	13	1.4	92
1960	321	12	17.9	69
1970	589	17	18.4	62
1980	2,910	65	36.0	37
1990	12,959	235	79.9	58
2000	27,775	432	91.9	51
2010	113,883	1,560	92.6	61

Source: Ministry of Development.

resilient threshold of 60 percent since the 1980s. Lack of an effort to develop homegrown technologies and intermediate goods industries led to the growth of imports in tandem with exports. One result is continued trade deficits.

Lack of export orientation coupled with a continued need to import energy, raw materials and capital goods, led to a current account crisis in the late 1970s. The new government would start a liberalization drive in January 1980 and the liberalization move was further strengthened with another military coup in September 1980 and the renewed process of democratization that followed. Subsequently, the following decade witnessed a comprehensive but also hasty liberalization of the economy covering international trade, the financial sector, capital account and a reduction in the government's role in the economy through privatizations and removal of price controls.

Industrial incentive programs continued during this period and the private sector was encouraged to take the lead in industrial investments. However, the incentives lacked a background of well-designed industrialization policies and incentives. In the 1990s and early 2000s, there were some negative repercussions of hasty liberalization of the 1980s; political instability and bad fiscal balances brought about two major crises in 1994 and 2001 with some fall back of Asian and Russian financial crises in 1997 and 1998. This period also lacked any well designed industrial or industrialization policies.

Turkey's economy recovered strongly after 2002 with macroeconomic balances restored and a number of structural reforms undertaken. Political stability, reduced inflation rates, strengthened banking sector, removal of fiscal dominance over financial markets and monetary policy created a conducive environment for private sector players to flourish. There has also been a new interest in developing the real side of the economy in terms of physical infrastructure, education and R&D. Consequently, the Turkish growth rates recovered since 2002 and total and per capita GDP rose significantly.

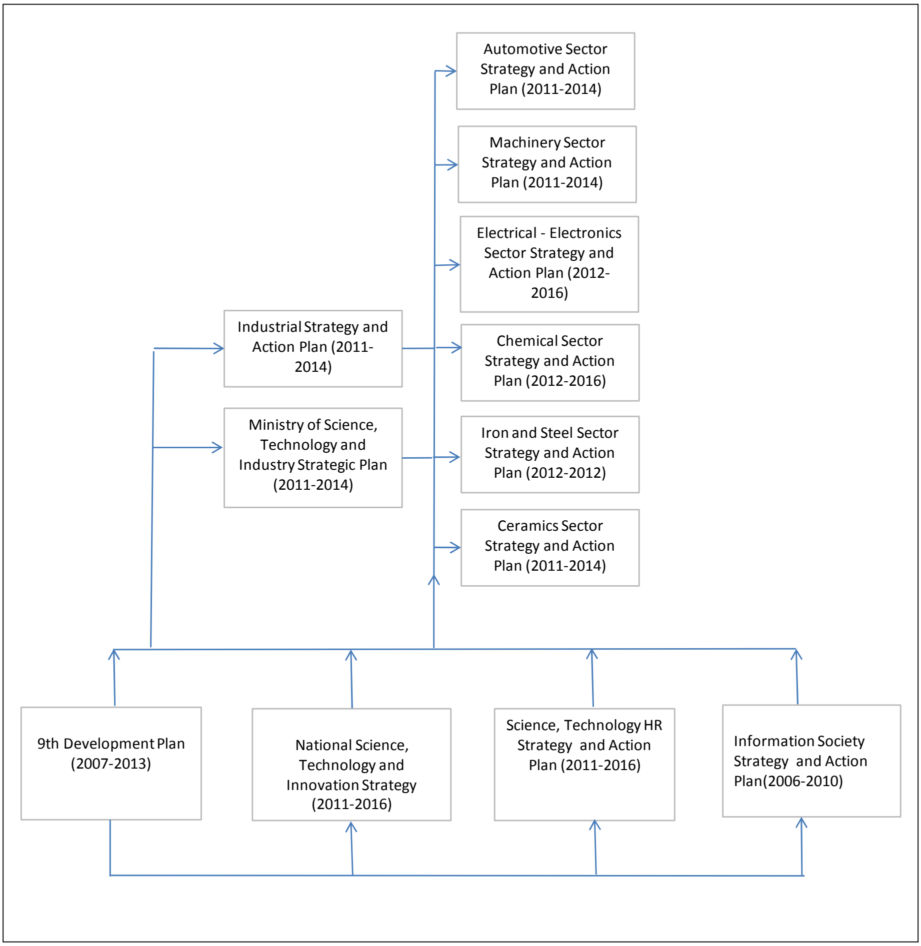
2.2. Turkey's Industrial Strategy since 2002

Turkey's current industrial strategy is mostly based on STI policies and some strategies in the manufacturing sector resembling a type of targeting. STI aspects are administered by TUBITAK, Turkey's scientific research agency which reports to the Ministry of Science, Industry and Technology (BSTB) and also to High Council of Science and Technology (BTYK) chaired by the Prime Minister. The industrial strategy on the other hand is administered by the BSTB. In the defense sector, the Defense Sector Undersecretariat manages offset policies with a view to increasing domestic capabilities.

Turkey's industrial strategy is revealed in a number of official strategy documents (Figure 2). Namely, Turkey's *Industrial Strategy Document and Action Plan (2011-2014)*, six sectoral strategy documents and action plans and the *Strategic Plan of the Ministry of Science*, *Industry and Technology*. These documents were also based on or coordinated with other strategy documents; most importantly the *9th Economic Development Plan (2007-2013)* and *National Science, Technology and Innovation Strategy Document (2011-2016)*, *Science and Technology Human Resources Strategy and Action Plan (2011-2016)* and *Information Society Strategy and Action Plan (2011-2016)*. The more recent 10th Economic Development Plan (2014-2018) updated some aspects of the industrial strategy such as regarding public procurement.

Appendix I presents summaries of two documents on strategy and action plans (automobile and machinery). Review of the strategy documents reveal that they are the reflection of a relatively general and less pointed version of an industrial policy. While they relate to their specific sectors, showing evidence of some kind of targeting, they lack further specificity on what sub-sectors they are really targeting for development and what measurable targets they are proposing. In other words, they are sector specific but not adequately sub-sector specific and not well targeting. For example, regarding the machinery sector, the strategy document does not prioritize any subsector. The strategy documents do not also specify any growth / market

Figure 2. Taxonomy of Turkey's Industrial Strategy



share targets for individual sectors or subsectors. The action plans are full of rather general and non-measurable targets. As such, while they provide a general direction for public policy, they lack an adequate amount of specific and measurable performance targets. The strategy documents are science, technology and innovation oriented rather than traditional industrial policy oriented. TUBITAK has some programs that border on industrial strategy, such as the recent electrical vehicle project whereby it supported private sector development of electrical vehicles. TUBITAK also supports industrial R&D in selected sectors.

Industrial incentives are designed and implemented by the “General Directorate of Incentives and Implementation.” The latest incentives regime introduced the concept of ‘strategy’ in prioritization of investments to elicit benefits from incentives. Turkish industrial incentive regimes feature three key aspects. Firstly, they are predominantly a regional development tool. Incentives tend to be more ‘rewarding’ in regions that are less developed and they do not exist for developed regions. Secondly, they are almost entirely made up of tax rewards (corporate taxes or taxes on energy and employment). Thirdly, in the currently prevailing regime, ‘strategic’ sectors are defined mostly as those that incur a large trade deficit rather than other possible definitions considering other possible benefits emanating from linkages, spillovers, technology etc.

III. Korean Industrial Strategy in Historical Perspective

3.1. Korean Development Policies (1962-1997)

The development literature has extensively discussed Korean development after 1962, some observers labeling it as miraculous, given the country's weak initial conditions marked by war-related destruction, along with weak infrastructure an lack of significant natural resources and capacities.[3)]

Korean industrialization and development during since 1960s can perhaps best be divided into 4 periods: 1962-1973, 1973-1980, 1980-1997 and 1997 onwards. This section first reviews the first three episodes providing a background to the

3) Kwon (2003:30).

account of post-1997 period followed by an overview of the lessons learned.

3.1.1. A Review of Policies during 1962-1997

During the planned economy period, Korea pursued ambitious and focused policies. The implementation of plans generally led to actual growth rates above the plan targets (Figure 1).

3.1.1.1. 1962-1973: Launching Industrial Policy

Korea launched its first five year development plan in 1962.[4] It had clearly specified two key sectors for development: mining and manufacturing. The plan was revised in 1964 which stated as its aims gaining international competitiveness in key industries (including cement, fertilizer, industrial machinery, petrochemicals, electricity, synthetic fibers). The orientation during this period was geared more towards import substitution than exports although the need for external earnings have increased since 1950s. Protective measures to hinder imports and FDI were adopted in sectors that the government deemed strategic.[5] Nevertheless, through a number of devaluations, exports were also promoted during this period as the country faced the continued risk of depletion of reserves.[6] Financial markets were repressed with a view to direct low cost financing to strategic sectors and the banks were kept under close control of the government.[7] The second Plan (1967-1971) continued the main features of the first Plan but broadened it with an emphasis on heavy and chemical industries (HCI) as well as a number of laws to support

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4) Some well-known references providing accounts of Korean development are Amsden (1989), The Federation of Korean Industries (1987), SaKong & Koh (2010), World Bank (1993) and Westphal (1990).

5) Some well-known references providing accounts of Korean development are Amsden (1989), The Federation of Korean Industries (1987), SaKong & Koh (2010), World Bank (1993) and Westphal (1990).

6) SaKong & Koh (2010:17-18).

7) Kwon (2003; 31).

electronics, textiles, machinery and non-ferrous metal industries under which different fiscal measures (such as tax credits) were adopted to support these industries during the late sixties and early seventies. During this period, construction of a government-owned petrochemical factory and a steel mill began. They have ultimately become the largest of their kind in the world.

3.1.1.2. 1973-1980: The HCI Drive

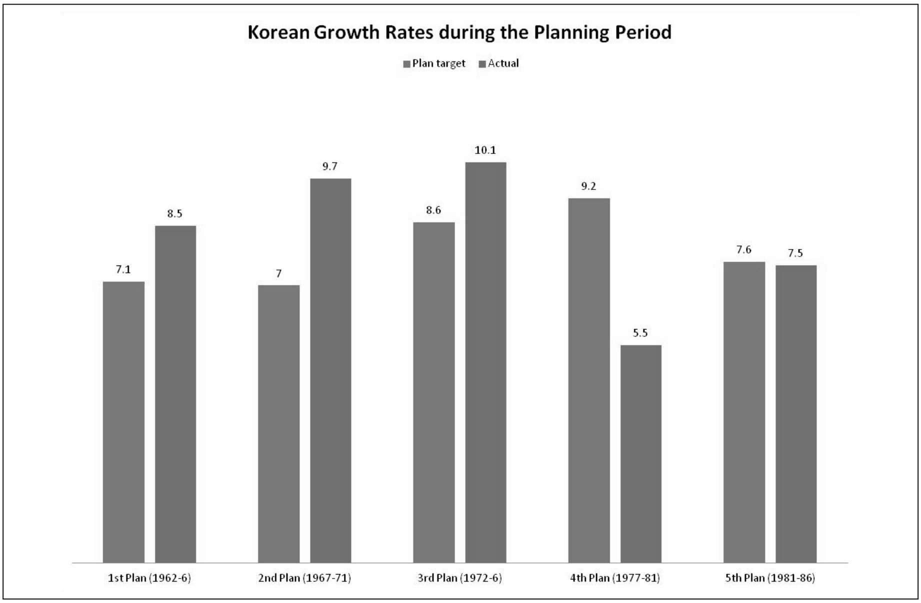
In 1973, when the first oil crises erupted and Japan's high growth period ended, the more comprehensive and ambitious set of HCI industries were re-launched in full scale with President Park's January 1973 Declaration on HCI.[8] The declaration targeted six strategic industries: including steel, petrochemicals, (non-ferrous) metals, shipbuilding, electronics and machinery. The first three were selected "with a view to enhancing self-sufficiency in industrial raw materials" and the other because "they are going to be developed into 'technology-intensive industries'."[9]

Meanwhile, policy direction clearly turned towards exports with ambitious overall and HCI export targets. Korea's exports would increase to USD 10 billion in 1980, half of which would comprise of HCI products. Government support intensified including financial (low interest and directed funding) and fiscal (tax advantages for heavy industries rather than light industries) tools, vocational training and government sponsored R&D through public R&D centers[10] to assist private firms. The government actively worked on chaebols to help them gain scale economies and thus to lower unit labor costs. The picking the winner type industrial policy and export orientation were accompanied by import restrictions as well as financial repression in the form of low interest directed credits to businesses in priority sectors.

As a result, during the third Plan period (1972-1976) growth accelerated and

8) SaKong & Koh (2010: 21), Kim and Leipziger (1993: 18).
9) Kim and Leipziger (1993: 18).
10) Kim (1994: 347).

Figure 3. Korean Growth Rates during the Planning Period



exports increased significantly in terms of value, geography and type of goods. However, domestic inflation also rose correspondingly due to increasing oil prices and trade deficit worsened significantly beyond stated limits. During the fourth (1977-1981) as well as the fifth (1982-1986) plan periods, priorities were broadened to[11] improvements in life and working conditions, education and health.

However, despite high growth rates and good performance in general, exports collapsed in 1979 after a five year period of continued overvaluation of won due to fixed nominal parity with the US dollar when Korea suffered high inflation. Overcapacity followed by overinvestment in some HCI businesses worsened the situation. That was an apparent result of overruling the market forces during planning. President Park's assassination compounded other problems such as the bad harvest in 1980.

11) Federation of Korean Industries (1987: 6-7).

3.1.1.3. 1980-1997: Consolidation, Liberalization and Financial Crises

At the end of the 1970s, international pressures from the second oil crises and slowing world economy intensified on the Korean economy, coupled with other domestic, social and economic issues. Many chaebols inherited a debt overhang and low capacity utilization, while inflation rate increased. The country also faced high current account and budget deficits. Foreign debt rose, income distribution problems became more visible, labor disputes and social unrest increased. Problems between small and large businesses and between manufacturing and agricultural sectors surfaced.

As a result of the problems in the late 1970s, the Comprehensive Economic Stabilization Plan was launched in 1979 introducing a new episode for the Korean economy as the emphasis on direct industrial policy waned. In parallel, Korea started to liberalize import tariffs in 1984. In 1990s the government started to open domestic market to foreign investments. The New Economy Five Year (1993) plan emphasized a liberal and open economy competing on higher-value added products and services.[12] While the previous two periods (1963-1973, and especially 1973-1980) are recognized as 'government-led' development periods, the period 1980-1997 would become a painful transition to a liberalized and private sector-led economy, which was more or less realized in the 2000s.

The priority of the Fifth and Sixth Five Year Plans (1982-1986 and 1986-1990) shifted to macroeconomic stabilization (lowering the inflation rate, reducing the budget deficit) followed by the government's active involvement in first restructuring the HCIs (such as automobiles, heavy electrical and copper industries, construction machinery) and then a forced rationalization (including in footwear, power generation, coal mining, and non-HCI sectors such as shipbuilding and textiles). These policies involved creation of monopolies, arranging mergers between players, capacity reduction and erecting entry barriers as well as large government-sponsored financial arrangements and tax support schemes to companies.[13] Efforts were also made

12) SaKong & Koh (2010:137-139).

by the government to enhance the transparency and accountability of chaebols and their management, improve their capital structure, and revamp their corporate strategies with a view to concentrating on core competences.14) Nevertheless, the reform efforts prior to 1997 seem not to have been adequately designed and implemented, as the crises of 1997 would eventually prove.

Financial liberalization came in various steps in the early 1990s. Various new non-bank financial institutions emerged during 1980-1985 but the interest rate liberalization came only after August 1991 and was completed by 1997, with interest subsidies being abolished.15) The banking sector changed following a number of consolidations, mergers and privatization, which increased international activities of domestic banks as well domestic operations of foreign banks.

3.1.2. General Characteristics of Korean Policies during 1992-1997: Some Lessons Learned

Korea recorded some of the fastest growth rates in the world and a drastic change in economic structure during the three decades prior to 1997, which was based on industrialization rather than on natural resources. During the process, Korea's export pattern changed drastically from labor intensive goods (textiles, apparels, plywoods etc) to capital intensive (ships, Steel, automobiles) and further to early technology oriented industries (semiconductors and memory chips, audio-video instruments). Thus policies must have played a significant role in Korean development as many observers argue. It could be argued that successful Korean development prior to 1997 were driven by the following key factors:

- Macroeconomic stability has been accorded a top priority even amidst aims for high GDP growth. While was not the case that macroeconomic balances were perfect during nearly forty years of growth; but when the problems

13) Leipziger (1988).
14) SaKong & Koh (2010:24).
15) Cho (2003).

arose there was a concerted effort to restore an acceptable balance. Perhaps most importantly, fiscal balances have been taken very seriously throughout but even during the HCI drive.[16] Probably, that was instrumental in not causing fiscal dominance over monetary policy and thus helped to keep inflation rates low. Trade balance,[17] and thus the current account balance, were monitored closely and remained mostly in balance or surplus.

- Korea's industrial policy was not based on a general drive for 'industrialization'. Industrial policies were narrowly focused and were closely monitored; and resource allocation process was clearly planned out. Moreover, industrial policy went hand in hand with disciplined development planning. This was the key to Korea securing a comparative dynamic advantage and becoming an industrial nation with all the benefits as well as costs. However, in targeting industries, market forces were in fact respected to the maximum extent possible.[18]The industrial policy was also comprehensively designed respecting backward, forward and horizontal linkages. STEPI (1995: 5) underlines that "it was expected that the governmental support of selected industries would bring prosperity not only to the industries but also to other industries related with them."
- Export orientation cum import substitution helped rapid industrialization. Korea adopted an export-orientated approach as early as the 1960s although main export orientation came with the HCI drive in the 1970s. Competitive devaluations led to quick rise in export revenues which were badly needed. Until the liberalizations starting in the 1980s, export orientation went hand

16) SaKong & Koh (2010:24).
17) STEPI (1995: 5).
18) Sakong & Koh (2010) notes, with reference to Park (2005) that to maximize capacity utilization, the HCI drive plan specified funding requirements for each project and care was taken not to exceed the budget ceiling.Even during the HCI drive, priority was accorded to finished products rather than intermediate and raw materials, to increase capacity utilization and ensure cash inflow. Even in the case of defense industry, 80 percent of the capacity was allocated to civilian products.

in hand with a falling degree of import substitution. That combination must have led to the formation of an industrial ability and a 'class' of industrial managers that manufactured internationally competitive products. Obviously, in those earlier years, competitiveness was based on low costs. It is thus no surprise that Korea was careful in keeping the exchange rate competitive and tried to raise production scales.

1975 HCI manual quoted by Kim and Leipziger (1993) states:

"In the development of HCI, economy of scale, efficient operation, and competitive prices are prerequisite, since these are the industries which have vast inter-industry effects. The competitiveness of HCI is, therefore, fundamental to the whole economy. Economy of scale is especially required when we consider that domestic markets are so limited that HCI should be developed as export industries. In other words, economy of scale should be supported by an expansion of markets through export promotion.

Most projects of the HCI, in this regard, are now under construction to have their unit production capacity running to an international level so that they may secure competitiveness on the world market, and enhance internal economy effect as well."

- A well-structured and managed homegrown technology development and commercialization policy along with manpower policies: even as early as the 1960s, Korea was deliberate in eyeing technological catch up. Korean plans encouraged development technology that was up-to-date[19]and homegrown.[20] In the absence of adequate private resources, starting with the initiatives of General Park in 1960s, the government established and generously funded ambitious research centers in order to develop critical

19) Kim and Leipziger (1993).
20) Pai, Park & Chang (2003: 224).

technologies domestically in key sectors with public R&D accounting for up to 80 percent of total R&D expenditures.[21] Activities of these centers accelerated in the 1980s and continued in the following decades.

In the 1980s, with the 'Economic Recession and the Industrial Development Act', policies readjusted their focus on industrial R&D and development of industrial technologies. It also liberalized government intervention in the firm's R&D activities in terms of permission, approval and administrative directives. In other words, industrial policy became more favorable to individual technology development project rather than sectoral development."[22] But efforts at technology development were also quite focused and were sector or product specific. For example, in the 1980s, the government announced a plan for indigenous technology development for intermediate goods. The plan eventually succeeded in domestic production of more than 2,000 items out of the original list containing more than 4,000 imported goods.[23]

As a result, R&D intensity reached 1.7 percent of GDP in 1990 and 2.4 percent in 1997, then among the highest in the world as the OECD average was 2.1 percent. In 2013 this ratio rose to 4.3 percent, the highest among OECD countries.

- Manpower policies accompanied technology policies. The government had been providing scholarships to a select group of undergraduate and graduate students to study in the USA and Europe since the 1960s. Upon their return, most were employed with attractive packages in research centers, the government or in the Korean Institute of Science and Technology which was established in 1966 as a center of excellence.[24] These policies also helped increase the quality of bureaucrats and private sector managers. Positive externalities were augmented by 'managing' private sector activity in

21) SaKong & Koh (2010:21); STEPI (1995).
22) STEPI (1995: 19-21).
23) STEPI (1995: 22).
24) Yoon (1992).

Box 1. MOST and the Precursors of Industrial R&D Activities in Korea

In 1966 Korea has become the first country in the world to establish a Ministry of Science and Technology (MOST), a ministry-level government office for science and technology.In 1968, MOST conducted a survey of research centers and researchers in Korea revealing that there were 6,698 researchers and 223 research institutes in the country. The total R&D expenditure in the country was 5,357 million won or 0.43 percent of the GDP. The study also revealed that 80 percent of the R&D expenditure was made by the public sector. Moreover, only about one fourth of the research institutes were really active and a significant part of the R&D expenditure was made in agricultural field. R&D expenditures of private firms were at the level of 0.65 percent of their sales on the average.

Against this background, MOST increased R&D expenditures. Its R&D funding reached a total of 818 million won in 536 research projects between 1967 and 1972 yielding 27 patent applications and 6 patents. However the actual result of the program was an increasing awareness of R&D among researchers and universities.

During the Third and Fourth Plan periods, MOST emphasized reinforcing the science and technology infrastructure and development of industrial technologies with the objective of not only adoption and transfer of foreign technology but also indigenous improvements of technologies in the fields of machinery, steel chemical engineering, ship building and electronics. With 'Specific Research Institute Supporting Act (1973) the government also established new research institutes such as the Korea Ship Research Institute, Korea Electronic Research Institute, Korea Machinery and Metal Research Institute, Korea Institute of Chemistry and Ocean Development Research Institute. In 1976, Korea Atomic Fuel Corporation, the Korea Electric Device Test Institute and the Korea Telecommunication Technology Institute were established.

Source: STEPI (1995: 10-17).

commercialization of technology developed in these centers. Meanwhile, government procurement policies provided much needed market access to newly home-developed products.

- In parallel with the government's manpower strategies mentioned above, a key characteristic of Korean development was the creation of a class of ‘industrial entrepreneurs’ as different from the typical ‘merchant entrepreneur.’ The latter has been present in many countries throughout the history and has played an important role in well-being of their societies. An ‘industrial entrepreneur’ such as August Thyssen or Friedrich Krupp of 19^{th} century Germany is a different player. He has a different time frame for decision making, is aware of technology aspects and competes on developing and manufacturing new industrial products, and is aware of the competitive importance of scale economies. The industrial entrepreneur is important as he is at the receiving end of the industrial policies. Without a class of industrial entrepreneur with adequate ‘quality,’ it is very difficult for industrial policies to be implemented effectively. Korea's early industrial development featured such industrial entrepreneurs.
- Industrial policy were supported by financial and tax instruments. Korean financial markets have been deliberately repressed in order to provide low cost financing to targeted industries through special governmental institutions and banks. Though financial repression in developing countries may lead to a fall in supply of total financial savings,[25] Korean authorities were careful to implement policies to encourage savings, perhaps offsetting–at least partially — the negative effects of financial repression.[26]

3.2. Korean Industrial Policies after 1997

Following the restructurings of 1980-1997 and the 1997 crises, Korea has been placed among the economically most developed and internationally integrated countries in the world. Many of its tradable industries have proven themselves

25) Yülek (1998a and 1998b).
26) Japan followed more or less a similar combination of financial policies. See Yülek (1997).

under international competition both technologically[27] and in terms of scale and unit cost.

Having reached its current level of economic development, Korea is now faced with a different international and domestic environment. It is thus natural that its development policy framework is now significantly different compared to pre-1997 period. This section discusses Korea's current development policy framework.

3.2.1. What Kind of Industrial Policy is Appropriate for Korea now: A Brief Discussion

Together with Japan, Korea can be considered the co-inventors of 'traditional' or 'classical' industrial policies; i.e., a focused policy targeting and nurturing selected winners to raise them into strong global competitors as described.[28] Traditional industrial policies can be considered as policies to generate a class of industrial professionals, companies and abilities at world level. This is exactly what Korea has achieved in the last five decades. Therefore in addition to new 'initial conditions' in this era, it faces a very different competitive environment. In this new era, Korean policy makers appear to follow technology and innovation policies rather than typical industrial policies of the bygone era.

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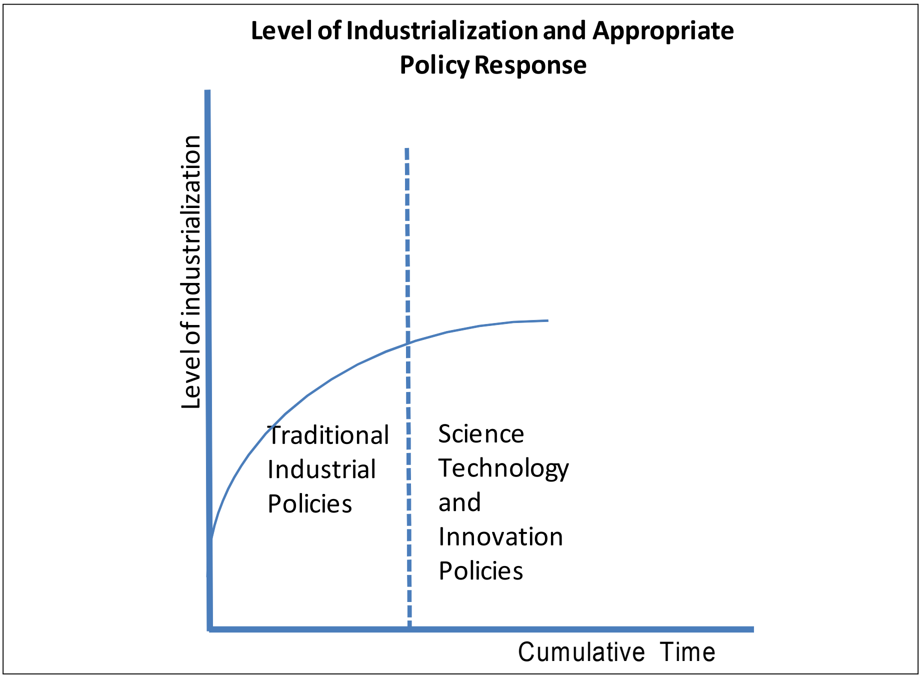
27) Young-Seok (2010) reports that the average unit value of exports of Korean IT products increased rapidly from USD 40 per kg in 2000 to USD 77 in 2007 (although the figures were still significantly behind USA and Japan) and terms of trade of Korean IT products increased substantially from 0.63 to 1.36. His calculations for the year 2007 suggest that in the home appliance and information/communication instruments sectors, Korea has gained international comparative advantage in technological ability; meaning that despite high export prices Korean products sold well due to better technology. In the electronic components sector, Korea's comparative advantage was based on the price, not technology; and in the biotechnology sector, its faced comparative disadvantage, meaning despite lower prices its products trailed relative to its competitors because of low technological level. The positive developments in Korea's IT sector since 2007 are likely to have led to further comparative progress for Korea.

28) More precisely, Japan's industrial policies go back to the Meiji Period in the late 19th century. But the second incarnation of Japanese industrial policies following the Second World War started slightly earlier than those of Korea.

Figure 4. Level of Industrialization and Appropriate Policy Response



Continued overriding of the market forces as in the case of traditional industrial policies for a country like Korea may bring more economic costs than benefits, as the country is now at the threshold of becoming state-of-the art in some of the fastest growing sectors globally. A more appropriate policy to follow for a country like Korea which has attained a high level of internationally competitive industrial abilities and educated manpower, may be to switch to science, technology and innovation policies (Figure 4).

3.2.2. An Overview of Korea's Industrial Policies now: Predominance of Science, Technology and Innovation Policies

There is a consensus among Korean and foreign economists that growth

Table 2. Sources of Korean National Income Growth (%)

	1970-1980	1980-1990	1990-2000	2000-2010	1970-2000
Total	7.8	9.3	5.8	4.6	7.6
Inputs	5.0	5,1	3.0	1.7	4.3
Labor	3.1	3.4	1.8	1.0	2.7
Capital	1.9	1.7	1.1	0.8	1.6
TFP	2.8	4.2	2.8	2.9	3.3

Source: Kim *et al* (2012); OECD (2014a).

accounting exercises reveal that spectacular Korean growth since 1960s have been mostly based on rapid factor accumulation (Table 2).[29] That, however, should not hide two important facts. Firstly, reorganizing its economy in achieving the growth rates among the highest in the world for four decades since 1960s is a policy success with very similar examples among the remaining world economies. Secondly, the TFP growth in Korea, while less than input-based growth, is still impressive.

What is more important however, is that the natural consequence of diminishing returns to factors after four decades of continuous growth and input intensification has been more and more since late 1990s as Korean growth rates fall. KDI estimates in Table 2 reveals that input contribution to growth has gone down from 5.0 percentage points in 1970-1980 to 1.7 in 2000-2010 reducing the total growth along with it. Meanwhile TFP contribution remained slightly below 3 percent and became the primary driver of total growth.

Under these new conditions, Korean policies need to be revised. Seemingly taking note of this, the Korean authorities have been shifting to policies that enhance TFP growth and are looking for 'new growth engines' and R&D. Regarding the latter, Ha (2004) argues that "it is R&D intensity, not the growth rate of R&D

29) See for example Krugman (1994), Kim *et al* (2012), Kim and Koh (2010: 92), OECD (2014a: 20).

Box 2. The Goals and Strategies of President Park's Creative Economy Plan

The Creative Economy Plan includes three goals, six strategies and 3 to 5 tasks attached to each strategy. The goals are set as:

- Create new jobs and markets through creativity and innovation,
- Strengthen Korea's global leadership through a creative economy
- Creating a society where creativity is respected and manifested

The strategies of the Plan are:

- Properly compensate for creativity and create an ecosystem that promotes the creation of startups
- Strengthen the role of venture businesses and small and medium-sized enterprises (SMEs) in the creative economy and strengthen their ability to enter global markets
- Create growth engines to pioneer new markets and new industries
- Foster global creative talent that has the spirit to rise to challenges and pursue dreams
- Strengthen the innovative capacity of science, technology and ICT, which form the foundation for the creative economy
- Promote a creative economic culture together with the Korean people

workers, that explains TFP growth best. This implies that R&D policies that affect economic agents' incentive to do R&D activities can surely change the long-run growth of the economy."

President Kim (1998-2002) supported the ICT sector and formation of new startups financed by venture capital. President Roh (2003-2007) emphasized across-the-board innovation policies and designated selected ten industries as 'new growth engines' for Korea. He also devised spatial[30] policies under the Five Year Balanced National Development Plan for 2004-2008. President Lee (2007-2012) emphasized knowledge-based economy and green growth concepts and targeted 17 technologies and sectors including green technology, intelligent robots and food industry.[31]

30) Japanese Ministry of Land, Infrastructure and Transport (undated).
31) OECD (2014b: 35).

President Park's government which was inaugurated in 2013 launched, in the same year, the ‘Creative Economy Plan’ which essentially includes a number of sets of science, technology and innovation policies. The plan is a continuation of efforts of earlier Presidents and it places a high emphasis on innovation, creativeness and small businesses.

Korea's new science, technology and innovation policies are being implemented by a number of different ministries and institutions, under different programs. The main actors are: Ministry of Strategy and Finance (MOSF), Ministry of Trade, Industry and Energy (MOTIE), and Ministry of Science, ICT and Future Planning (MSIP). National Economic Advisory Council (NEAC) is responsible for providing advice on policy development. A number of institutions responsible for public research and development, program and project evaluation compliment the picture. OECD (2014b) provides an in-depth review and assessment of science, technology and innovation structure and policies.

A broad strategy of development has recently been announced in 2014 by the Ministry of Strategy and Finance under the name Three-year Plan for Economic Innovation. The Plan tackles three main ‘directions’:

- strengthening the economic fundamentals: reform public institutions in addition to fiscal and tax systems; reduce the size of the unregistered economy; improve labor-business relations),
- promoting a creative economy: a set of measures to increase the use of ICT technology in industry and agriculture, to support new ventures and new industries including through M&A; to continue expansion of exports of goods, services and contracting businesses; to expand outbound FDI, measures to prepare for an aging population, address energy security issues and green technologies,
- Boost domestic demand: deregulation with a view to increasing FDI in five key service sectors (healthcare, education, tourism, finance and SW).

Implementation and monitoring of the 3-year plan is to be governed by Ministerial Meetings on Economy through a task force jointly participated by private and public sectors. The activities included in the Plan seem, in general, focused and specific in terms of detail and time schedules.

New Korean policies also aim at

- Sustaining high levels of private R&D expenditures which are almost entirely undertaken by large companies. Private R&D now comprises about 80 percent of the total.[32)]
- Development of new technologies where Korea has not been able to establish itself firmly, such as biotechnology or medical devices.
- Enhancing the internationalization of the domestic R&D effort with a view to increasing returns on R&D investment.
- Enhancing Korean companies performance in commercialization of R&D and innovation.

3.2.3. Has Korea Abandoned Planning?

Korea is still very much engaged in economic planning. Officially, Korea's Fifth Plan (1992-1997) represented its last development plan. A number of Korean officials consider that the level of development that Korea attained meant that Korea has finally ‘graduated’ from developmental planning. However, the current policy framework includes extensive use of certain planning methods and even their titles carry the word ‘plan’, though they are no longer called ‘developmental plans.’

32) Increasing private R&D activity in Korea is till being complemented by public R&D. Shapiro (2007: 111) underlines that “For Korea to remain at the forefront of the global innovation standard policymakers have deemed it necessary to implement science and technology policies to support public-private R&D collaboration as a counter to market failure in R&D efforts. Inthis (?) was, Korea is continuing to move away from the precedent of duplication of foreign-based technologies and generate innovations in a cross- sector collaborative context.”

In fact, many nations have been and are still engaged in planning, though unofficially. Malinvaud (1992:22) identifies three key functions for economic planning: "It must look into the future and announce its likely features; it must define strategies; it must evaluate public projects and control their realization."

Yulek (2014) argues that planning can be considered a type of dynamic government intervention as opposed to the textbook case of 'static intervention' justified by classical economic theory in case of market failures. Planning is thus an effort to intervene in the economy, overruling market forces with the justification that it could "correct" market failures to achieve second bests. Under this perspective, economic planning could be seen as a "dynamic", forward-looking policy framework to address various levels of market failures.[33]

3.2.4. Has Korea Totally Abandoned 'Traditional' Industrial Policy?

Korea still maintains major features of its earlier industrial policies which are based on 'targeting' sectors. As mentioned above, targeting of specific technologies as well as new industries during tenures of the last four President, Korea has not developed internationally competitive businesses. For example, President Roh (2003-2007) targeted ten industries including digital TV/broadcasting, displays, future automobiles, next generation semiconductors, next generation batteries, next generation automobiles, digital content/software, biomedicine, intelligent home networking and intelligent robots.[34] Likewise, as mentioned above, President Lee (2008-2012) targeted 17 technologies and sectors including green technology, intelligent robots and food industry.[35] Under President Park (2013-2017), the Korean government is targeting innovative technologies along with sectoral targets including medical devices.[36]

33) Yulek (2014).
34) Moon and Yoon (2011: 238); OECD (2014b:34).
35) OECD (2014b: 35).
36) MoSF (2014).

This continued Korean policy approach that focuses on specifics rather than general policies may increase the returns on Korean R&D investment both public and private.

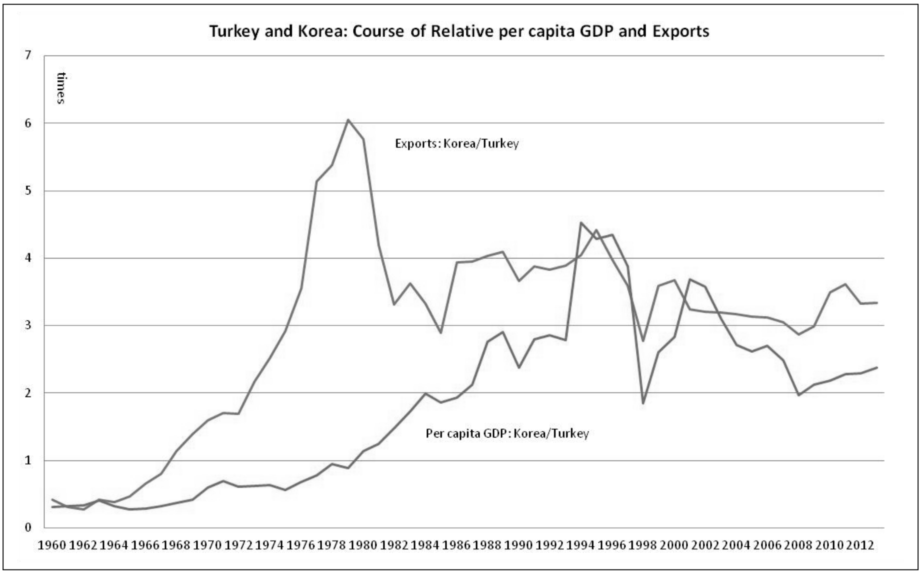
IV. Assessment of Industrial Policies in Turkey and Korea in Historical Perspective

Perhaps a good summary of where policies have taken Korea and Turkey on a comparative basis can be observed through their relative per capita GDP which can also serve as a crude measure of relative development of productivity. Figure 5 shows that Korea's per capita GDP relative to Turkey has risen sharply between 1960s and 1993, pointing to the relative success of Korea. During 1993-2001 rather than development policies, financial crises in both countries (1997 for Korea, 1994, 1998 and 2001 for Turkey) dominated the figures. After 2002, Turkey's per capita GDP increased faster than Korea's until the global crises. While both countries weathered that storm without much damage, more recently, Korea's per capita GDP has been growing faster than Turkey's.

Figure 5 also displays integration with world markets in terms of exports which can be taken as a measure of international competitiveness of each country. From the 1960s until the end of the 1970s, Korean policies led to a rapid accumulation of international competitiveness of Korea relative to Turkey. After Turkey's internationalization since 1980, relative nominal export magnitudes of the two countries became stable. What the figure hides though is the increasing complexity of Korean exports compared to Turkey. ICT products' share in Korea's exports increased significantly during the last decade while in Turkey a major part of the exports is constituted by medium to low technology products.[37]

37) World Bank (2014: 14-15).

Figure 5. A Comparison of Turkey and Korea (Per Capita Income and Exports)



Source: World Bank.

At the point, it would be prudent to ask questions about the factors leading to the difference between the industrial policies conducted in the two countries that in turn led the respective countries to different end points in the level of industrialziation. The review of Korea and Turkey's industrialization process in a historical perspective as well as their current policies yield the following observations:

1. Lack of export orientation has played a key role in Turkey's lag during the period 1960-1980 by withholding incentives on businesses to make them become internationally competitive. Export orientation from the earlier days have benefited Korea in developing an internationally competitive industry. Turkey's starting point came almost two decades later losing valuable learning effects.

Table 3. A General Comparison of Korean and Turkish Macroeconomic Figures

	Korea		Turkey	
Population (Million)	50.2	1	74.9	1
Per Capita GDP (PPP; USD)	33,140	1	18,975	1
GDP Growth (%)	2.9	2	3.5	3
Annual Inflation (%)	3.2	4	8.1	5
Government Balance (% of GDP)	1.9	6	-2.6	6
Goods Trade Balance (Billion USD)	24.8	5	-69.8	5
Goods Trade Balance (% of GDP)	2.4	7	-12.2	1
Current Account Balance (% of GDP)	0.6	8	-6.0	8
Exports of Goods (Billion USD)	547.9	7	151.8	1
Exports of Goods (% of GDP)	47.0	1	18.5	1
Gross Domestic Expenditure on R&D (Million USD)	29,448	9	7,664	9
Researchers: Full-time Equivalent	11.1	9	2.9	9

Sources: OECD, World Bank and authors calculations.

1. 2013
2. Compound growth for 2008-2012
3. Compound growth for 2009-2013
4. Simple average for 2007-2012
5. Simple average for 2007-2011
6. Simple average for 2006-2010
7. 2012
8. Simple average for 2008-2012
9. 2010

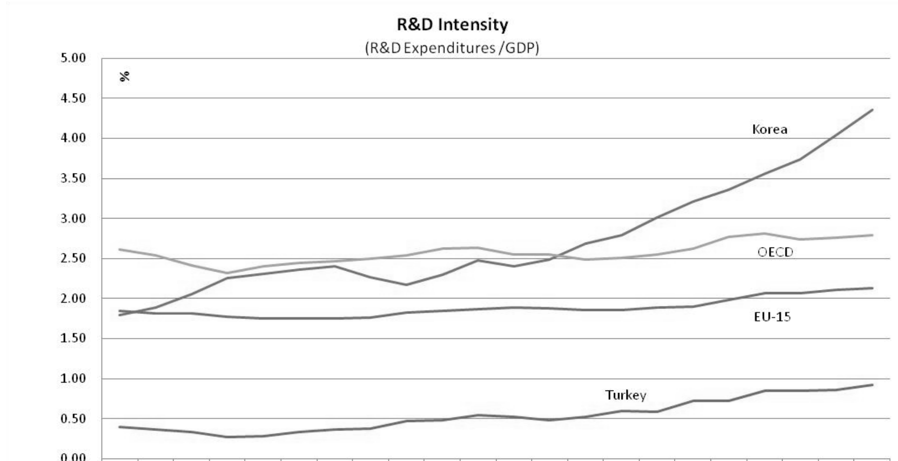
2. Focused industrial targeting that account for linkages: Korea has closely focused in industrial policies into specific sectors since 1962. Turkey's policies lacked such focus and consideration of linkages. Korea respected backward, forward and horizontal linkages in developing industrial policies. As an example, steel, automotive and shipbuilding industries were developed more or less in tandem. On the other hand, development of automotive, rolling stock and defence industries also were coordinated. Anectodal evidence

suggests that on the day of inauguration of the Kyongbu (Seoul-Pusan) Expressway in 1971, General Park asked the contractor Chung Ju Yung, the founder of the *chaebol* Hyundai Group, 'if he could build cars;' which led to the founding of Hyundai Motors.[38)]

3. Korean policy industrial policy emphasized not only transfer of technology but also development of local technological capabilities during industrialization. The latter was largely lacking in the Turkish policies. Turkish policy relied more on passive importing and utilization of technology rather than mastering, adopting and developing it. Korea established state R&D institutes staffed with foreign-educated researchers. These institutions served as developers of "public" good. They conveyed basic technologies to Korean industrial companies that lacked R&D capabilities. As mentioned earlier, Korea smartly established specific technological research institutes in the 1960s (Box 1). Korea also introduced R&D incentives as early as 1970s with the 'Technology Development Reserve System' with continued programs in the 1980s including 'Specific R&D Program' and 'Specific National R&D Program.[39)] For the most part, Turkey lacked state R&D institutions active in the industrial sector. The R&D incentives came only in mid-1990s and were not as effective.
4. Currently Korea is a leader in R&D intensity and Turkey still lags behind (Figure 6). Having went through major industrialization stages in light as well as heavy industries, Korea has shifted to a new stage of industrial polices that concentrates on science, technology and innovation. On the developed Korean industrial structure, such policies are likely to be effective in furthering Korea's industrial abilities and international competitiveness. Turkey's current industrial policies are still general and not adequately focused, linkages are not well considered or well-integrated into policies, and lack

38) Kim and Jaffe (2010).
39) STEPI (1995: 19-20).

Figure 6. R&D Intensity in Korea and Turkey



	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
Korea	1.80	1.89	2.06	2.26	2.30	2.36	2.41	2.26	2.17	2.30	2.47	2.40	2.49	2.68	2.79	3.01	3.21	3.36	3.56	3.74	4.04	4.36
Turkey	0.39	0.36	0.33	0.27	0.28	0.34	0.37	0.37	0.47	0.48	0.54	0.53	0.48	0.52	0.59	0.58	0.72	0.73	0.85	0.84	0.86	0.92
OECD	2.61	2.54	2.42	2.32	2.40	2.44	2.47	2.50	2.54	2.62	2.64	2.55	2.55	2.49	2.51	2.55	2.63	2.77	2.82	2.74	2.76	2.79
EU-15	1.85	1.82	1.82	1.77	1.75	1.75	1.76	1.77	1.83	1.85	1.87	1.89	1.88	1.85	1.86	1.89	1.90	1.98	2.07	2.07	2.10	2.13

Source: World Bank.

well defined and consistent targets. Without having established an adequately industrialized economy, jumping to science, technology and innovation policies may be ineffective in reaching desired results and inefficient in terms of support costs.

5. Experience and abilities with respect to program and policy monitoring, along with evaluation, are adequately developed in Korea.[40] Turkey has not developed adequate skills in these areas. As a result, quality policy design is likely to be low in Turkey.

40) OECD (2014b).

V. Conclusion

Differing features of industrial policy seem to have contributed to a different path of industrialization and development in Korea and Turkey.

During the main industrialization periods (1960-1980 for Turkey and 1962-1997 for Korea) the two countries followed sets of industrial policy including some common but yet other differentiated aspects. Korean industrial policies were more focused; targeting specific industries and complementing this with manpower and technology policies. Also, during this period while import substitution was prevalent in both countries, Korea has emphasized exports while Turkey has not. Macroeconomic management in Korea was more prudent than in Turkey. Restrictive financial policy together with instruments to direct funds was common in both. Also were tax incentives favoring industrial investments in Turkey and specific sub-sector based investments in Korea. Both countries recorded rapid growth rates but Korea's development was much more impressive, seemingly by virtue of more focused industrial policies and export orientation.

More recent industrial policies in both countries emphasize science, technology and innovation. While Korea's current level of industrial abilities and international competitiveness justify transition to such policies, Turkey has yet to complete its industrialization through nurturing of stronger and more internationally competitive industrial sector. Thus it seems early for Turkey to forego focused industrial policies.

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Appendix. Turkey's Industrial Strategy Documents

1.1. Automotive Sector Strategy and Action Plan (ASSAP-2011-2014)

This strategy document specifies a vision, a high level objective, objectives and actions. The vision of ASSAP is set as ‘to become a regional manufacturing and R&D center.’ The high level objective of ASSAP is to increase and sustain the international competitiveness of the Turkish automotive sector, and use it as a basis for a creating a structure with heavy use of advanced technology and high value added. The objectives are to increase R&D, develop the domestic and export markets; develop domestic administrative, regulatory and physical infrastructure, increase the manufacturers' capabilities in design, manufacturing and branding.

The document then specifies actions in line with the objectives above. Most of these actions are general in nature such as: development of test centers; development of laboratory infrastructures in selected university and vocational high schools; review and enhancement of R&D and pre-competitive R&D supports to the sector; development of new incentives for improvement of manufacturing based on original technology and design; support for 'activities (such as clustering) that enhances businesses along the supply chain, development of supporting ‘national focus projects,’ raising skilled human resources; conducting activities to enlarge the domestic market and export markets; raising awareness among citizens to use environmentally friendly vehicles; capacity development within the ministry; enhancement of market monitoring and audit activities; and assistance in production of raw material inputs.

Some actions are more specific in nature such as: support for manufacturing of electrical batteries and alternative fuels in line with Turkey's national vision regarding climate change; directing public procurement to domestically manufactured and environmentally friendly vehicles and vehicles made up of recyclable components; activities aimed at phasing out of older vehicles; provision of cheaper land and infrastructure for investments in industrial zones; enhancement of ports and surrounding transportation infrastructure for automotive products.

The ASSAP specifies a monitoring and assessment framework. However, as most of the actions are general in nature, and because measurable outcomes are not actually specified even for relatively specific actions, it is difficult to monitor and assess performance of ASSAP objectives.

1.2. Machinery Sector Strategy and Action Plan (MSSAP-2011-2014)

The MSSAP has been prepared in line with the 9th Development Plan, Medium Term Macroeconomic Program, and the Strategic Plan of the Ministry of Science, Industry and Technology (2010-2014). MSSAP specifies a vision, a high level objective, objectives and actions. The vision of the MSSAP is set as ‘to become a technology production center’. The high level objective of MSSAP is to develop the sector with a view to manufacture high technology products. The targets are to implement regulatory and structural measures to transform the sector into a high-value-added and branded one; develop healthy financial solutions to benefit from economies of scale and a sustainable domestic and international growth; enhance human resources; enhance promotion of Turkish machinery products in domestic and international markets; enhance R&D and innovation in the sector.

The MSSAP displays less number of actions that are general than the ASSAP: development of buyer-supplier relationships and cooperation; continuation of rural development supports; allowing trainers to become involved in industrial projects; provision of incentives to industrialists supporting vocational training; implementation of exchange programs with developed countries in the sector; development of a macro-plan for applied university training and internships; developing a brand new training program for the machinery and automation sector; opening promotion offices in target markets; establishment of a firm level database; raising awareness among firms on the national financial support products; development of new support mechanisms for SMEs; enhancing quality certifications among firms; support for exhibition participation; development of new markets; establish joint R&D centers and technology transfer centers; developing and conducting national focus projects.

The specific actions include: accelerating the VAT rebate process; reintroducing tax regulations to increase leasing financing and introduce regulatory changes to allow buy-and-lease-back operations; introduction of registration of construction machinery and machine park inventory; limiting imports of second- hand machinery until full EU membership; enhancing patent regulations to increase competitiveness of manufacturers; public procurement; increasing market monitoring mechanisms and import controls to protect registered manufacturers from unregistered actors; assist removal of tractors older than 25 years from the market; introduce industrial zone specifically for the machinery manufacturers with a view to reducing investment costs for development and support of clusters; increase Eximbank financing and insurance to exporters; support and promote IPOs of smaller companies; ensure that firm machinery is accepted as collateral in bank financing; support vocational training; launch professional standards and certification in the sector; establish a machine technology institute; develop supports for companies that develop R&D and innovation based on new products.

As in the case of ASSAP, the MSSAP also specifies a monitoring and assessment framework. However, as most of the actions are general in nature and as even for the more specific actions measurable outcomes are not specified, it is difficult to monitor and assess performance of MSSAP objectives as in the case of ASSAP.

7

The Arab Spring: Facts and Illusions

***Moaness Tahoun*[1]**

I. Abstract

Late 2010 and early 2011 a series of uprisings swept the Arab World from Morocco in the west to Bahrain in the east and from Syria in the north to Yemen in the south, with the spark occurring in Tunisia and culminating in Egypt. Though the uprising was due to several political, economic and social factors, nevertheless in each country that witnessed the Arab Spring, people or demonstrators were chanting the same slogan: "Freedom, Dignity and Social Justice."

This humble paper is not in any sort of an attempt trying to explain what happened, but rather an illustration of how the future of the Arab Spring presents us with both enormous potential and disastrous perils. There are many fears the

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1) First Secretary, Egyptian Commercial Service Statutory Declaration: I hereby declare that I have written this paper myself without any external unauthorized help, that it has been neither presented to any institution for evaluation nor previously published in its entirety or in parts. Any parts, words or ideas, of the thesis, however limited, and including tables, graphs, maps etc., which are quoted from or based on other sources, have been acknowledged as such without exception.
Moreover, I have also taken note and accepted the rules and guidelines of the Korean Institute of International Economics.

uprising predisposed in favour of many forces that genuinely work against the Arab Spring. It cannot be simply dismissed that there were deliberate efforts that seek to sabotage the movement in its infancy and to steer the uprising toward an authoritarian and totalitarian path, while absolutely crushing freedom and democracy.

The Arab Spring needs a strong voice and encouragement to again shift gears to the right direction. Anarchy, violence and conflicts were the norm after the first wave of the revolution failed to safeguard the initial success in thwarting and ousting tyrant regimes in Tunisia, Egypt, Libya and Yemen; where strongmen had remained in power for decades and most Arab Spring countries fell in the quagmire of internal conflict and even to the verge of a civil war. Different stakeholders have underlying interests in returning the clock back to pre-empt the movement of change.

The great momentum crowned by toppling of several brutal regimes in the Arab World could be lost if forces trying to subvert the democracy and spread chaos and violence instead succeed in destabilizing the democratic foundations. The counter-revolution strategy hinges on pushing the public anger through economic deterioration and abetting public disorder, taking advantage of chronic problems that still hurt the people, namely high unemployment and inflating prices.

However, there is still a strong chance that the Arab Spring may succeed and forces of freedom would overcome the existing hurdles, following other democracies in helping the region transition to a success model of democracy. The situation in the Arab countries is far from being settled and although things seem to be getting worse, all stakes are still on the table and the sunshine will unveil the gloomy horizon to reveal facts, while unravelling myths and the illusions.

List of Abbreviations

EU	European Union
FDI	Foreign Direct Investment

GDP	Gross Domestic Product
IMF	International Monetary Fund
MB	The Muslim Brotherhood
NGO	Non-Government Organizations
NSF	National Salvation Front
SMEs	Small and Medium Scale Enterprises
WB	World Bank

II. Introduction

"Rarely has revolution been more universally predicted, though not necessarily for the right countries or for the right dates" were the words of historian Eric Hobsbawm on the eve of the 1848 mass rebellions in Europe. The case was not much different in the period prior to the Arab Spring in December 2010. True, the Arab World was due for a change, but no one could predict how it would happen, when it would take place and how things would develop.

The sparks of the Arab Spring with waves of freedom that hit different Arab countries in different extents range from toppling a regime to riots and demonstrations that resulted in minor reform. The uprising represents a serious attempt to change the status quo in different, stagnant Arab countries and to address the vague interrelationship paradigm between the people, the regime and the institutions.

Events are taking place rapidly on the ground with new, emerging forces taking the lead, while other organized political forces are dwindling. Questions concerning the role of democracy and social justice in the region still persist and remain current, and have recently been strengthened with increasing suspicions associated with stability and democratic transition, and the possibility of bringing the totalitarian rule to a complete end. Therefore, it was necessary to attain greater understanding of the dynamics and the parameters of the Arab Spring, and its impending political, economic and civic implications.

It is still too early for full evaluation–especially amidst ongoing radical transformations–of such a dynamic process. Yet however stunning, critical differences have emerged on how things developed and unfolded, in patterns particular to the country. While the Tunisian case offered more outspoken dialogue about the role of the majority and opposition, and a fierce debate between religious parties and advocates for a secular state, the Egyptian case appears more subtle–where democracy was established quickly but without proper democratic institutions to embody the new order, for the moment at least, due to fierce resistance by loyalists of the old regime. The Libyan and Syrian scenarios were worse, where the uprising turned to armed conflict with thousands of casualties from battles between militia, with shadows of long and brutal civil war now lingering in the background.

This paper focuses more on the Egyptian case, because in addition to the fact that Egypt has its own specificity, Egypt is the most populous country in the region and is often considered the heart of the Arab world. The Egyptian case is full of struggle, aspirations, suffering, success and failure and the country will act as the proverbial beacon that will guide the region towards a new order. Nasser's eighteen years in power had not witnessed a single election, while Bourgiba's more than thirty years in power in Tunisia were not any different. Bourgiba even officially declared himself “President for life”. When freedoms are routinely suppressed, political life deliberately paralyzed, ideologies and opposition stigmatized, authoritarianism and totalitarianism glorified, then the people will have either to pretend that things were just right or to smell the smoke burning from every side.

The shift from one type of regime to the other is not a simple matter, because many have stakes aligned with a certain order and with a specific sort of regime. The political transition for example is very different from a small country such as Estonia or Slovenia than in comparable country such as Bahrain, and things are also different from Poland and in Egypt although both countries had similar authoritarian experiences. The internal politics and equally important, and regional and international contexts are very crucial in determining the shape of future events.

The battle for freedoms, rights and dignity is not completed by merely toppling a certain regime. The ability to build functioning institutions and to enforce bills of rights that clearly define the roles of religion, state and politics is the milestone that must be crossed successfully in a transition period.

Authoritarianism will prevail in the short run as a reflection of public anger with democratic politics that did not offer much progress quickly. However, over a period of 7–13 years different countries will shift to democratic governance once the model succeeds in any Arab country and can be replicated (Domino Effect).

The influence of the old regimes and the affiliated business cronies cannot be simply eliminated in a short time. The success in managing post–revolutionary periods hinges upon concerted efforts to build consensus and to avoid conflict between the political rivals that joined the uprising, in addition to reversing the economic downturn, advocating labor and social rights to get as many people on board as possible and lastly, preventing friction and divisions.

The process of democratic transition is typically troublesome and perilous. Many believe that they can manipulate transition times and periods of anarchy for their own interests more easily than at any other time when set rules prevail. Although solidarity is a must to avoid the very serious risks of return to authoritarianism; many players have different stakes and their own calculations. Under public pressure, the long term and the chronic socio-economic problems need to find a magic wand to absorb public anger. Nevertheless, decades of economic stagnation and “run to fail policy” has caused degradation of infrastructure; thus things cannot be simply improved by just overthrowing a regime and reinstating another. Unless people can bear the cost of change, then it is pointless to think of a revolution or an era of freedom, prosperity and rights when no one is willing to bear or to share the cost.

The path to freedom usually is subject to the old guard beneficiaries' resistance to free elections, genuine democracy or rule of law. The Turkish model is just one example where democracy was reinstated after four coups. In fact, the Algerian model seems worse where election results were annulled and the military took control, started a so called “war on terrorism” and never allowed elections again. The conflicting interests of different groups that joined together to start the uprising will need to be properly addressed to reflect the new power game among competing political players. As a rule of thumb, the longer military-affiliated regimes remain in power the more likely issues pertaining to democratic transition and human rights will be shelved for decades.

Although, we do not know the future, we can look ahead to the future by way of similar experiences that took place in the past. For example, we have two neighboring countries, North Korea and South Korea, at the end of the Korean War in the fifties with comparable populations, income, economic level, and education, etc. After only thirty years from the Korean War, we can see one model of successful progress, with industrial development, high per capita income and gradual democratic transition in the south; compared with high poverty, military regime, tyrannical authoritarianism and absence of basic human rights in North Korea.

In short, there is no path that leads directly from military dictatorship to democracy and prosperity, the facts from the ground notwithstanding, at least from what we learned from political history. The nature of the political synergies in provisional regimes will be certainly be critical towards determining the new facts on the ground. The greatest peril lies in truncated and aborted superficial changes where genuine democratic and human rights principles will be offered a back seat and lag behind superstitious and illusionary goals of national security, fighting terrorism or other rhetoric slogans.

2.1. Methodology

Investigating this range of objectives requires a qualitative approach that not only describes the relationships between different variables and precedents among different countries, but also the interrelationships between the socio-economic problems of the desperate middle/ working classes on the one hand and hopes of bringing an end to the endemic dictatorship, corruption, economic stagnation and social injustice.

A qualitative approach of data gathering and analysis will be used, including an analysis of official documents that investigate the perspectives of different stakeholders in the Arab countries along with an elaborative approach of the model applied elsewhere of countries that proceeded from dictatorship and authoritarianism to democracy/freedom and eventually to economic prosperity and social justice.

A particular emphasis is on assessing the increased instances of violence during the transition period, especially in the Arab countries, to understand how certain counter-revolutionary forces try hard to prevent changes or to manipulate the course of expected outcomes. An extensive analysis will then be carried out to determine preliminary assumptions that will emerge from content examination. Then this study will focus on whether there are clearly articulated phases of transition that require specific courses of action or positive regulations during the initial and critical periods of transition. This will be verified or rejected during the review of the applicability and validity of the analysis. The relevance of this methodology will be alternately scrutinized depending on the future direction of events that can validate or nullify the argument.

2.2. Issues to be Analyzed

This paper attempts to explore possible answers for the following perils and challenges that are shaping the face of the Arab Spring at present:

i. Can regime change alone absorb the public anger following decades of dictatorship, corruption and socio-economic marginalization?
ii. Can the Economy become the driving engine to jumpstart the process,

by creating more jobs, improving living standards and building a strong middle class before jumping to a genuine Democracy?

iii. Can the Arab Spring prevent further turbulence and resist forces of military loyalists to the old regime, violence and crimes, religious divisions and multi-ethnic issues, and plots to spread chaos, anarchy and disorder?

iv. Can the deteriorating economic conditions and social injustice be justified as a pretext to delay political and democratic reforms needed to ensure accountability and rule of law till a sound economy is functioning?

v. Why were economic development and democracy successful in some countries and failed in others, and which model is more applicable to the Arab scenario?

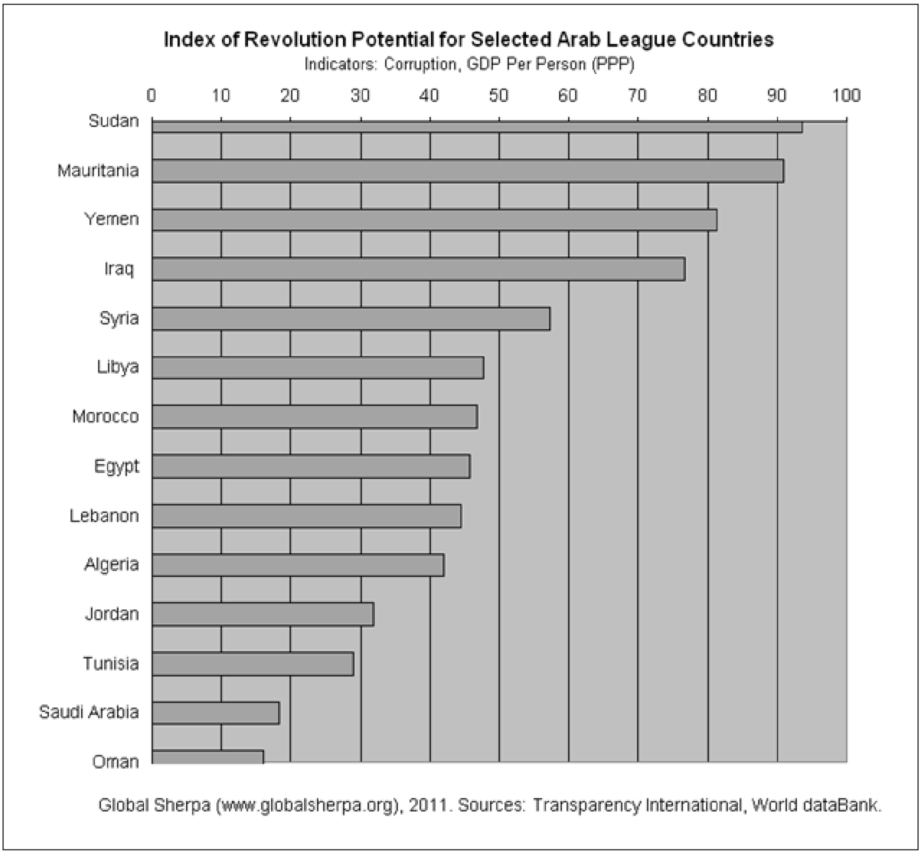
vi. What are the best means of promoting values of Pluralism and Diversity in societies suffering from rifts caused by political and religious divisions?

vii. Are the monarchies in the Gulf and the rich oil-and-gas-producing countries in the Arab world resistant to the waves of the Arab Spring and democratic transition?

2.3. Historical Background

Different regimes with military background ruled different Arab countries such as Naguib, Nasser, Sadat and Mubarak in Egypt; Gadhafi in Libya; Boutaflika in Algeria; Hafez Al-Assad and later Bashar Al-Assad in Syria, Bourgiba in Tunisia, Saddam Hussein in Iraq and Aly Saleh in Yemen; and all tried to reinterpret democracy to secure their interests in terms of state involvement and monopoly of political, economic and religious spheres.

Thus, any interrelationships between the secular military regimes that has ruled the different Arab countries, especially countries that have witnessed the Arab Spring (i.e. Tunisia, Egypt, Libya, Syria, Bahrain, and Yemen) needs to be understood in the framework of relatively oppressed communities and people ruled by elites



typically from the military trying to sustain power by suppressing opposition and political activists on the one hand, and by a progressive degradation of ideology and culture on the other hand that ended up with violent confrontations and popular uprising that re-shaped the face of several Arab states.

"Political development means not just bureaucratization and institutionalization but the eventual incorporation of all citizens into a single constitutional structure. The proponents of civil society have argued that this occurs once there is an associational life outside the state, which can then be incorporated into the body politic."[2] For decades, stagnant political life in the Arab World without the state willingness or desire to tolerate relatively autonomous organizations including political parties, bloggers, opposition, minorities, sarcastic media, religious groups and non–government organizations (NGOs) was a source of despair and anguish for many, especially the youth.

In different undemocratic states, deep–seated elites who fear the loss of their power and privileges under democracy and rule of law would rather opt to postpone or to entirely abandon democratization, liberalization and reform–arguing with claims that populists, once democratically elected, would not behave democratically. It is a trivial argument that, of course, does not sufficiently explain the political, economic and social turmoil in different Arab countries. The changes taking place in the Arab World now are very significant, although it might disappoint people who were looking for a fast and comprehensive transformation.

Many Arab countries–much of which do not enjoy the wealth or the abundant oil and gas resources of the Gulf countries, are not rich enough to resist the waves of reform and democratization over a long period. Eventually, the state has to submit to the will of people and the civil society and introduce constitutional, social and democratic measures to curb the increasing public anger of failed economic policies, social injustice and educational collapse along with alarming indicators such as absence of a vibrant political life or even a genuine will to fight corruption, nepotism and elite interests.

The desire of many Arab states to postpone reform indefinitely has led to either a further isolation or retreat of the state from its own people in addressing day-to-day problems, and to offset those perils by simply pumping its natural resources wealth to postpone reform, which is happening in the case of the Gulf States, and Algeria. Alternatively, other Arab states proceeded into a catastrophic path that is equally irrational. However, since those non–rich states cannot afford the

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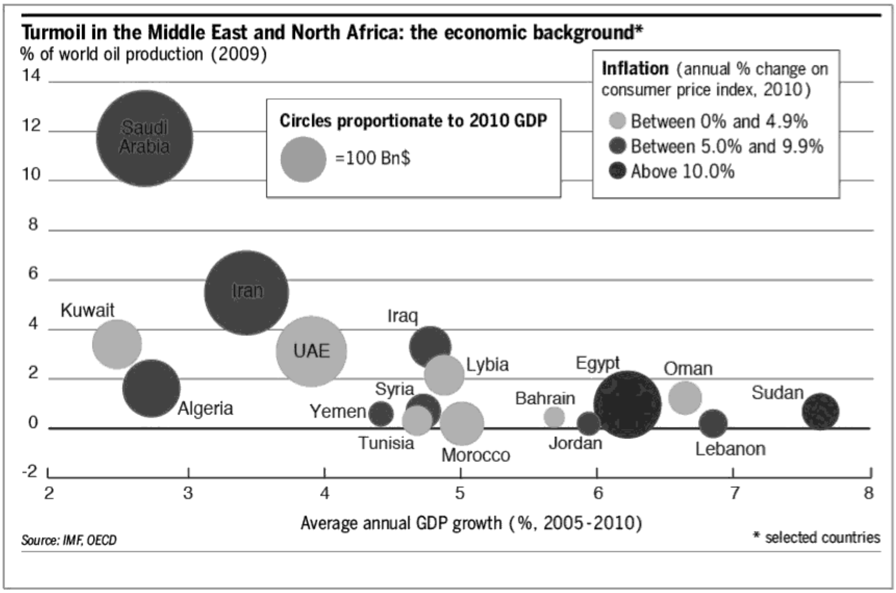
2) Robert D. Lee "Religion and Politics in the Middle East" Identity, Ideology, Institutions and Attitudes" Westview Press 2010.

luxury of the Gulf States–that can absorb the fees of deferred reform; they ended with a series of revolts, riots and uprising in what is known as “The Arab Spring.”



Deaths in the Arab awakening

Recorded deaths during protests/clashes between civilians and government security forces

To July 12th 2011 (Libyan figures unavailable)

Country	Status	Population, m*	Number killed, minimum	Deaths per m population	Period of unrest
Syria	Ongoing revolution	20.4	1,300†	63.7	Mar 2011 - present
Egypt	Regime toppled	81.8	846	10.4	Jan - Feb 2011
Tunisia	Regime toppled	10.5	219‡	20.9	Dec 2010 - Jan 2011
Yemen	Ongoing revolution	24.1	200§	8.3	Feb 2011 - present
Bahrain	Uprising crushed	1.3	29**	23.0	Feb - Jun 2011

*2010 estimates †Excluding security force members
‡Of which 72 reported linked to the unrest or in custody
§Excluding deaths resulting from clashes between security forces and other armed groups
**Of which 16 reported linked to the unrest or in custody

Sources: Amnesty International; Egyptian Ministry of Health; OHCHR; UN Population Division; press reports

III. Political Stagnation as Causal Force

3.1. Traces of Failure

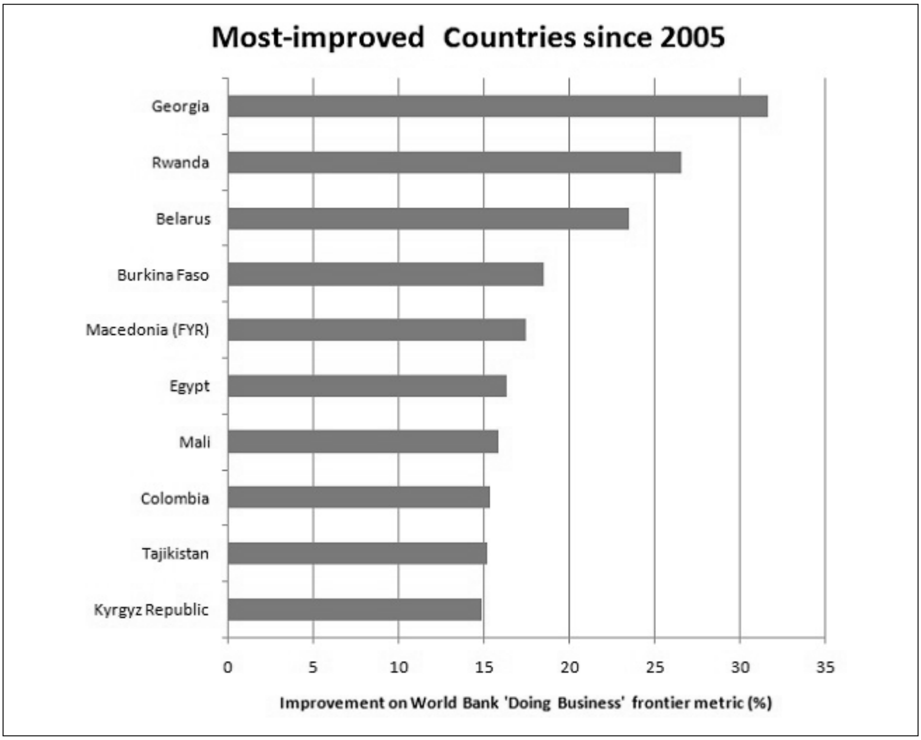
A successful state needs a good degree of trust and partnership between the state and its own citizens. The state needs the support of its people to secure legitimacy, to enhance its own capacities and to mobilize momentum for development. Thus, the issue here is about having such a degree of partnership and collaboration that would include a degree of autonomy in return for a measure of support.

It is equally important to spread values of tolerance and peaceful coexistence between the different group of people living together (Muslims, Christians, Sunni, Shias, Religious, Seculars, Socialists, Liberals, etc.).

Accordingly, the problem is not economic stagnation or living standards per se, but rather in building synergies between the state and people until the state has voluntary cooperation of the relatively autonomous non–state actors. It is remarkable that Egypt recorded an impressive 7.2% growth rate in 2008 before the economic crisis, while Tunisia was praised by the International Monetary Fund as an economic miracle, where growth rates reached 4.5% in 2010 and where the World Economic Forum had Tunisia as the 32nd most competitive country in 2010/2011 Global Competitiveness Report ahead of countries like Italy or Spain.

In Europe, the literature is abundant that such collaboration between the state and the people resulted mainly from political bargaining and not from any sort of good will from the state, delegation of authority, idealism of political elites or from any sort of forbearance of religious institutions. Most western European countries such as France, Italy, Britain, Netherlands, etc. had their own path that was peculiar, and they had tried their best to avoid violence and disorder, which unfortunately was the occurred with frequency during the Arab Spring.

The norm now in the European Union for example, is freedom of political and personal expressions and governments' neutrality toward religion and politics. Whereas, the role of political Islam has been rising significantly in the last three



Source: World Bank, Doing Business Report.

decades to demonstrate the success of non-governmental groups, mainly Islamic, in providing public services where the government has been absent or ineffective in responding to substandard living conditions, which rendered the argument that the Arab Spring was all about economic problems a mere illusion; the reality being an intermingling of complex problems with different political, economic, social and labor façades.

For example, the Muslim Brotherhood (MB) in Egypt has transferred itself from the religious to the political sphere underpinned by values of democracy, diversity and political pragmatism. Thus, the old French model of secularism of the state or laïcité was totally irrelevant in the Arab World and the Arab constituency

Confidence in Democracy Ebbs

	2013	2014	Change
Views of democracy	%	%	
Democracy is preferable	66	59	-7
Non-democratic gov't can be preferable	21	25	+4
Does not matter	11	14	+3
Democracy vs. stability			
Democracy is priority	51	44	-7
Stability is priority	43	54	+11

Source: Spring 2014 Global Attitudes survey. Q19 & Q106.

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gave the MB much credit when they won numerous elections following the revolution.

The result is thus a balance, with concordance of interests, to be reinstated through a political bargaining process and not through blocking some groups or associations from joining the political life; or barring other NGOs from registering their institutions; which area all meant to maintain political, the economic and the social sphere under tight state control.

3.2. Political Domain

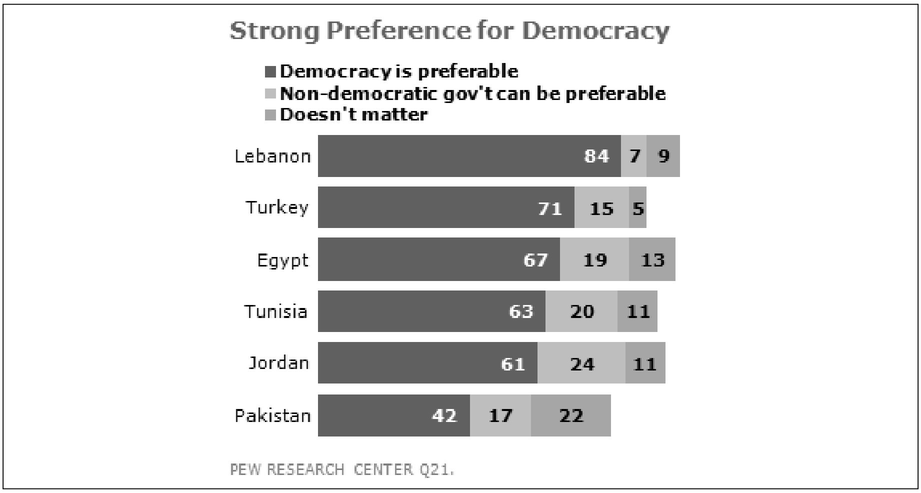
Active political and economic spheres require a normative approach. Many Arab leaders crafted their notion of the ideal “Head of State” on the basis of a conviction that a strong regime capable of maintaining stability and order, no matter how suppressive or brutal and by whatever means, is better than a ‘soft’ regime; regardless of whether that soft regime was democratically elected or even accountable to its own people. The argument is buttressed by allegations that a democratic and soft regime simply cannot offer public goods such as securing borders, protecting people's lives and properties, etc. Although there is a grain of truth in such argument, and true public order is a prerequisite and a foundation for a civil life, nevertheless such a malicious strategy often times end up with catastrophic outcomes

Thomas Ertman defines "political development to include two components, the institutionalization i.e. bureaucratization of the state and the expansion of inclusiveness through the implementation of constitutionalism".[3] A state that is overwhelmingly staffed by professionals, selected on the basis of their merit, will be better qualified to offer high quality services–regulation, defense, infrastructure, health, education and to respond effectively to public needs in general in a timely manner, while making efficient use of the available resources. As mentioned earlier, a state needs a strong partnership and coordination to succeed in gaining public confidence and mobilizing the resources needed to provide such public services.

In the case of the Arab Spring that were part of the uprising, we can clearly see institutional failure where counter–revolutionary forces of the old regime that concentrated in critical position at the executive and the judiciary branches of the state collectively mobilized their forces to reach a failed state scenario, so as to prepare the public to demand authoritarianism. What some may call "The Deep State" is a strong barrier to building a cluster of healthy institutions and protecting democracy as Ertman argued. When the national institutions have their loyalty only to specific figures affiliated to one regime or another and not to the state to where it belongs, then anything can happen, allowing a new regime to totter and sway.

However, this is not only the case of the Arab Spring countries alone; Romania, Bulgaria and ex. Soviet states had similar experiences where change was met with resilient confrontations. Any state will come up short in competition with another that is regulated by functioning institutions and constitutionalism, in providing public goods or to develop national agenda to enhance progress and development. As Ertman mentioned in the case of Europe, neither façades of political development

3) Thomas Ertman, Birth of the Leviathan: Building Sates and Regimes in Medieval and Early Modern Europe (Cambridge, UK: Cambridge University Press, 1997).

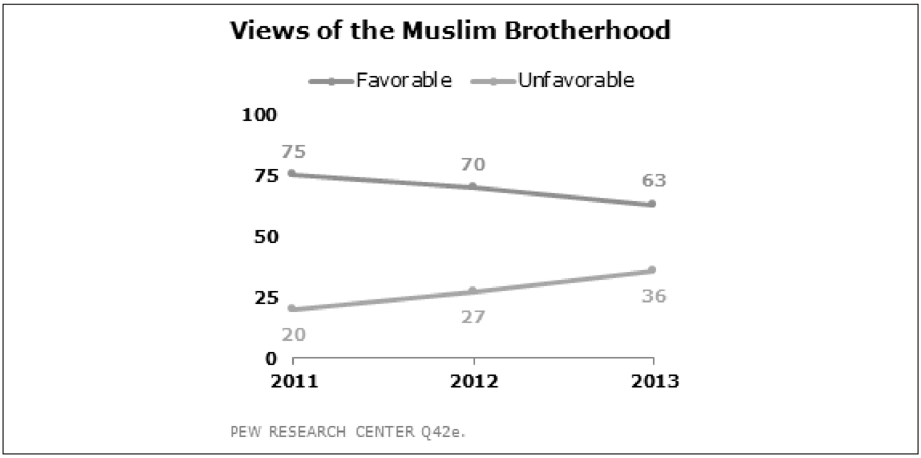


is sufficient without the other.

The European history, along with the recent events in the Arab World suggest that political development may become an active agent in spurring change, thus disrupting the task of the state in maintaining order. Latecomers to European political development such as Germany learned from the French mistakes and proceeded to build bureaucracies before they came under serious challenge.[4] Latecomers to economic development such as Arab and African states were dependent on flawed models of foreign aid, investment or selling natural resources, without strong institutions or bureaucracies that can act as buffers during turbulent times.

In Egypt, the state attempted to repress any opposition to the regime, and so did the "progressive" regimes in Libya, Syria and Algeria–all countries where the military played a heavy role in politics after gaining independence. Islamic parties and organizations–on the footsteps of the Muslim Brotherhood–whatever their mission is, found wide popular support and came to threaten the stability of the illegitimate (by concept) military regimes.

4) Ertman, Birth of the Leviathan, 34.



Vaclav Havel has been significant in reviving the theory of civil society. For him, the civil society came as a response to a state that tries to manipulate and dominate the different aspects of society so that they can act independently from the state, supply much of their needs, and from this experience can learn that the state is one of their means and absolutely not the only determinant.

The different Islamic organization such as the MB in Egypt and in other Arab countries have established or revived number of community associations and organizations that enriched the civil society. The Muslim Brotherhood had its start in the remote city of Ismailia on the brink of the Suez Canal and then spread to other cities and towns across Egypt. It created elements of a civil society that eventually became a major political force in Egypt.

The state nevertheless has regulated, controlled, abstained, cracked down or in many instances, stood against the civil society. A year in power left MB with fading popularity and lot of criticism from all spectrums that affected the group's image. The charity and philanthropic activities which usually adds to the popularity of charitable organizations can be easily offset by defamation campaigns and political challenges especially after revolutions.

3.3. The Democratic Deficit

The Arab people were usually presented with a false choice between anarchy and chaos on the one hand and dictatorship and authoritarianism on the other by unelected regimes who tended to underscore the failure of Arab democracy to validate their existence. It is perhaps ironic to find several Arab regimes that declared their intent to democratize under western pressure or popular demands but eventually retracted from such promises or simply dressed their totalitarian regimes and rules in ceremonial robes of democracy.

The contradictions between what different western states, mainly America and the EU preached about democracy and what it exercised is gigantic, flawed and ridiculous. America and Europe have pledged to support democracy, empower democratic transition in the Arab World, as well as offering other rhetoric pledges. Nevertheless, the American, the European and the other democratic states offered nothing more than lip service when Egypt and Tunisia were struggling to survive in the aftermath of revolutions, and amidst crackdowns by its closest Arab allies on civil activists and human rights, while retracting from the democratic path.

When in 1991/1992 the National Salvation Front (NSF) won the municipal elections in Algeria and even demonstrated stronger results in the first round of the legislative elections, the state–provoked by the military, annulled the second round and sought to suppress the NSF. The consequence was a decade of civil war. In defending themselves against such retraction from the track of democracy, the regime provoked fears that Islamic parties would take full power and subvert any possibility for future democracy. Such trivial argument by the Algerian state and by other Arab states has continuously reduced the inclusive capacities and legitimacy of their regimes to mediocre levels.

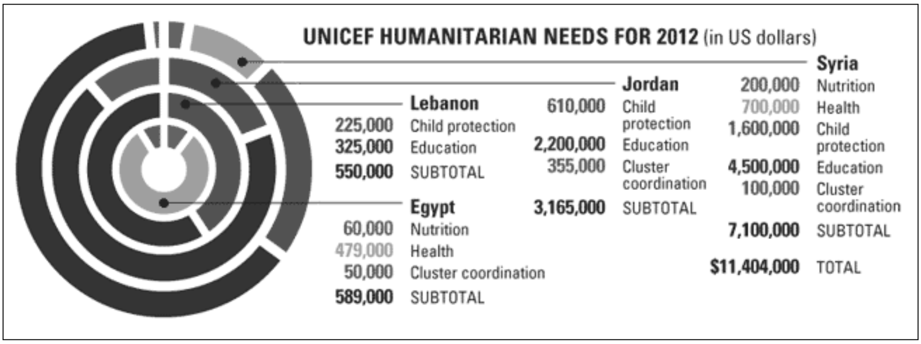
The fundamental illegitimacy of many Arab states, committed to democratic principles that it never honors has caused a democratic deficit. The democratic process may conceivably open the gate for progress, but democracy requires a regime with sufficient strength and an enough dose of confidence to permit such step. The general lack of strong will, along with the political elite's skepticism concerning genuine democracy and shifts in the political power, have produced a rhetoric tone trying to back-up the state by emphasizing national identity (us versus them, war against terrorism, national security, anarchy versus stability, national mega projects, patriotism and honor, etc.).

By one line of thinking, opening the doors to full democracy in different Arab countries and permitting different forces including MB and NSF to be fairly represented would lead to a more stable balance between the political and the religious spheres on the one hand and between the state and the civil society on the other. However, authoritarian regimes in different Arab countries exercise absolute powers, with fundamental absence of debate on questions of authority, accountability or legitimacy. Ted Gurr argued in his inspiring book, <Why Men Rebel>, “the gap between what the people have and what they believe they are entitled to lie at the heart of the revolution”.[5]

The different political spheres in the Arab Spring countries have not yet fully agreed upon a common ideological foundation for a modern state, but it seems there has been some narrowing of ideological differences and sooner than later among people in the Arab World as well as different ruling regimes, they will have to agree on democracy at the basic level, while statements such as “People are not ready for democracy” as stated by Omar Sueliman, Vice–President Mubarak before getting overthrown will become nothing more than vestiges of a rotten past.

A Pew survey of Egyptian public opinion released in May found out that a solid 66 percent of Egyptians preferred democracy to any other form of government, and 51 percent were willing to live under a democratic government even if they risk instability. There is not much evidence that the aspirations of the Egyptians or the other Arab countries differ much from those in other countries seeking peace, security, prosperity and good governance. There were numerous literatures on “The Arab Exception” to explain the resilience of many Arab dictatorships

5) Gurr, Ted, “Why Men Rebel”, Princeton University Press, Princeton, NJ, 1971.



Source: UNICEF.

that survived domestic pressure and external shocks.

The same survey highlighted Egyptians' growing economic pains and worries. Only 29 percent of those surveyed stated they expect the economic situation to improve next year, a result down from 50 percent in 2002. Some 42 percent thought their economic situation would worsen next year, up from 20 percent in the previous year. And, a strong 76 percent majority believed the economic situation was “bad” in general.[6]

The path toward stability in Egypt is long and painful. It is hard to imagine a modern Egypt that is not democratic and plural, and it is even more difficult to imagine an Egyptian state seeking legitimacy without working hand in hand with its own people to collectively tackle the serious economic and social problems.

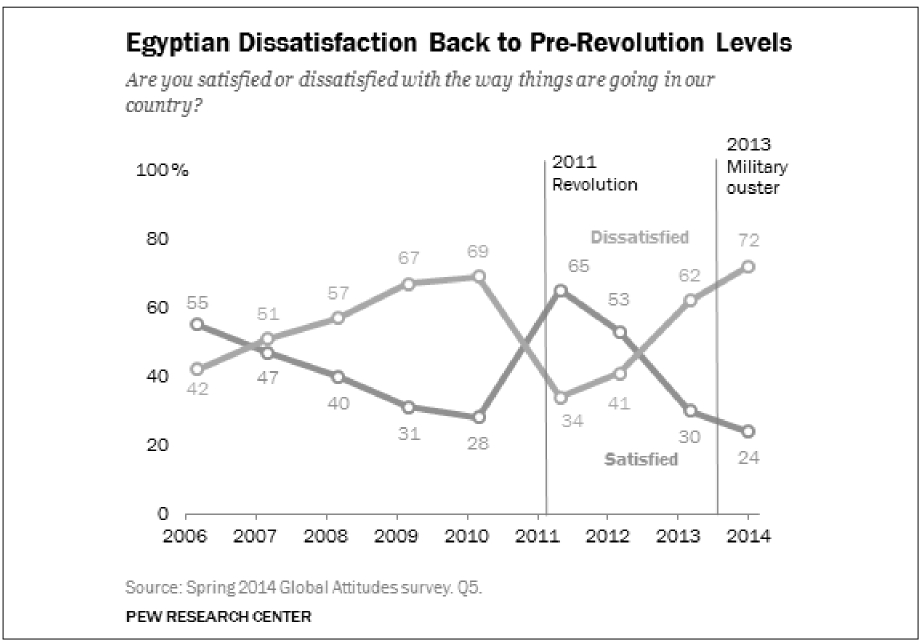
The lesson learnt from the European experience would imply that the answer will come from a close cooperation and may become a struggle that will lead to everlasting harmony and positive and peaceful interaction between the political, civil and religious spheres.

Several years has passed now since the turbulence of the Arab Spring was triggered, and the interaction between the state, civil society and the religious sphere seemed to have produced an iron grip that actually strengthened the regime's

6) Spring 2014 Global Attitudes Survey, Q5.

authoritarianism. The peaceful rotation of power that is conductive to a healthy democratic society is missing, and the synergies tended to increase authoritarianism in different Arab states. "Different Arab regimes were happy with rhetoric such as the “war on terror” as a handy excuse to round up domestic opponents on the flimsiest evidence. Now, even the most moderate of Islamists could be jailed on charges of supporting terrorism, adding to increasing domestic repression".[7]

The development of the Egyptian national state was conductive to the development of political Islam in Egypt, where the MB took control for only one year before being ousted from the political scene. Ennahda in Tunisia agreed to give up power in favor of a conciliatory path to avoid political division and to postpone democracy until there were more consensuses on the government and the first minister.



7) Lin Noueihed and Allex Warren, The Battle for the Arab Spring, Yale University Press, New Haven and London, 2013.

However, such development poses more question marks than answers of how the future in Egypt and Tunisia would be for example? How can pluralism and diversity fit within such frameworks? How can the authority of the nation-state b in front of the legitimacy from the ballot boxes? The progress of the nation state created such questions and will eventually require clear and straight answers.

The Economic Conundrum

3.4. Economic Downfall following the Arab Spring

Since the first wave of the Arab Spring in Egypt was initiated in January 2011, the country has witnessed one of its worst economic crises in modern history. The escalation of events culminated in political crisis, social unrest, and strong polarization between the groups of revolutionaries and political groups who lit the sparks of the Egyptian revolution just a few years earlier.

3.5. Reform Measures

At a quick glance, fiscal austerity is a must and subsidies need to be rationalized at a time when the current regime in Egypt is attempting to retain order, secure power and spur economic growth. The one indicator critical to understanding the Egyptian turmoil is the growth rate. Annual growth rates have declined sharply from 7.2% in 2008 to a mere 2% at the moment. Consequently, the budget deficit has been inflated, the balance of payment is worse than before and the foreign reserves are declining. The Egyptian state is very dependent on the direct funding it receives from the rich monarchies in the Gulf notably Saudi Arabia, United Arab Emirates and Kuwait, who have strategic interests in extracting Egypt from its current quagmire.

Economy Souring Since Crisis

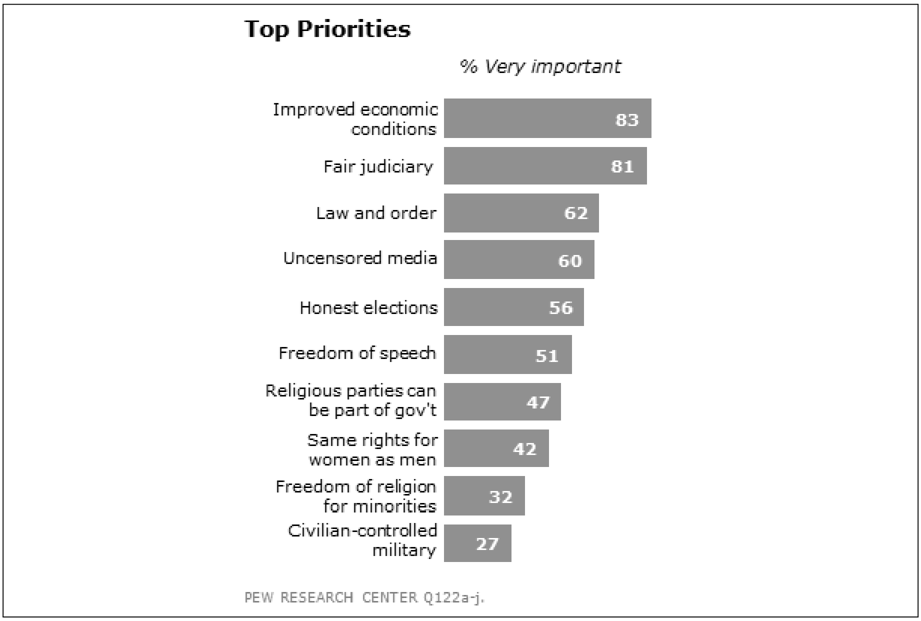
	% Economy is good		
	2007	**2013**	***Change***
Advanced economies	%	%	
Spain	65	4	*-61*
Britain	69	15	*-54*
Italy	25	3	*-22*
Czech Rep.	41	20	*-21*
France	30	9	*-21*
U.S.	50	33	*-17*
Canada	80	67	*-13*
Poland	36	27	*-9*
Israel	46	43	*-3*
Japan	28	27	*-1*
Germany	63	75	*+12*
S. Korea	8	20	*+12*
Australia	--	67	--
Greece	--	1	--
MEDIAN*	**44**	**24**	***-20***
Emerging markets			
Mexico	51	38	*-13*
Argentina	45	39	*-6*
Russia	38	33	*-5*
China	82	88	*+6*
Turkey	46	53	*+7*
Malaysia	76	85	*+9*
Chile	49	58	*+9*
Indonesia	23	37	*+14*
Brazil	--	59	--
S. Africa	--	53	--
Venezuela	--	44	--
MEDIAN*	**48**	**46**	***-2***
Developing economies			
Pakistan	59	17	*-42*
Egypt	53	23	*-30*
Ghana	57	37	*-20*
Jordan	45	27	*-18*
Kenya	60	52	*-8*
Lebanon	9	10	*+1*
Uganda	40	44	*+4*
Palest. ter.	10	22	*+12*
Philippines	--	68	--
Bolivia	--	54	--
Senegal	--	48	--
El Salvador	--	33	--
Nigeria	--	32	--
Tunisia	--	11	--
MEDIAN*	**49**	**25**	***-24***

* Medians based on only those countries surveyed in both 2007 and 2013.

PEW RESEARCH CENTER Q4.

In Tunisia, Tunisian economist Murad Ben Turkiye stipulated that his state needs to grow by 7% annually to create 60,000 new jobs annually to absorb the new young labor force entering the labor market annually to absorb public anger. However, under Ben Ali, the state was growing at approximately 4.5% creating around 250,000–300,000 that were not enough to halt the revolt. Nevertheless, the economy shrank 1.8% in 2011 following the Arab Spring and was not yet able to sustain growth or create the needed jobs to utilize the labor force.

Theoretically, the solution seems to lie with FDI to create more jobs, and to improve the balance of payment in Egypt and in Tunisia. However, it is very unlikely that foreign investors would risk their portfolios in countries with high political risk that is reviving and stumbling from revolutions. Egypt and Tunisia has no means at the moment except to depend on its Gulf allies to secure resources needed to jumpstart the economy, in order to boost growth and to appeal to foreign investors. Some surmise that a trickle–down effect is possible with billions of dollars

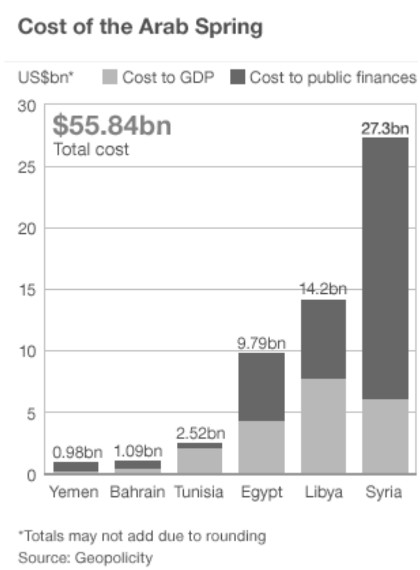


injected from the Gulf States. However, the economic problems are more than merely a trickle–down process. A complete restructuring and reform is needed to ensure that the economy is back on the right track.

Egyptian and Tunisian governments have no alternative but to use austerity measures and to cut public spending to ensure sound finance. However, without political stability, any talks about high growth rates, increasing investments or balanced budget is simply unrealistic.

The Arab Spring came at a time when Europe is fighting its own sovereign debt crisis, having to bail out Greece and to offer significant assistance to countries such as Portugal, Ireland or Italy. It is very unlikely that the EU, which is the main trading partner for both Tunisia and Egypt, can secure any serious sums needed to support the Arab countries in Transition. Egypt and Tunisia should not expect much other than eloquent lip service from the European or the Americans about the importance to democratize or to liberalize their economies.

The pledges made during the Deauville summit between the Western and the

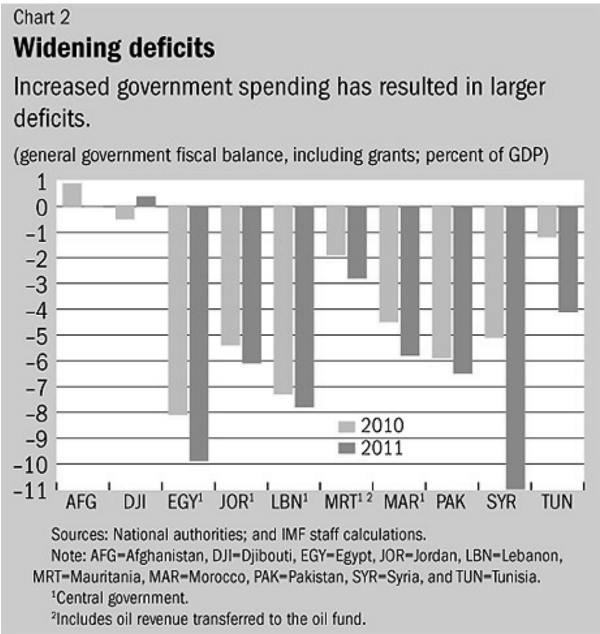


Arab states with billions of dollars to be poured in support of the democratic transition in the Arab World, something similar to the Marshall plan after World War II, was not realized and offered nothing more than selected technical assistance. Nevertheless, few attempts were made to support the transition process in the Arab countries, but those steps were not nearly enough to match the needed change. Tunisia for example, was offered US guarantees to help the government borrow at favorable rates. The European Bank for Reconstruction and Development changed its mandate to support the private sector in the Arab Spring countries with $1.3 billion of allocation available.

The state fiscal revenues–as a percentage of Gross Domestic Product (GDP)–declined sharply from around 30% of Egypt in the 1980's to roughly 20% in the second millennium. During Mubarak's and Ben Ali's eras, the largest business tycoons and their cronies along with the industrial magnates could find different ways to evade taxes through corruption and nepotism. The situation was about civil marriage between business and politics and the people had to, in figurative terms, pay the dowry for that marriage from their own pockets.

About one thirds of the Egyptian budget is spent on interest to the enormous public debit–more than 100% of the GDP, along with a foreign debt that is at alarming levels. Another tranche of the budget is allocated to wages and salaries which are out of touch as well. The commodity subsidies, mainly to fuel hydrocarbons are a third big chunk with increasing crazy allocation annually that serves the poor but ultimately to no avail. The subsidies are supposedly target the low-income households, but it rarely reaches their target groups.

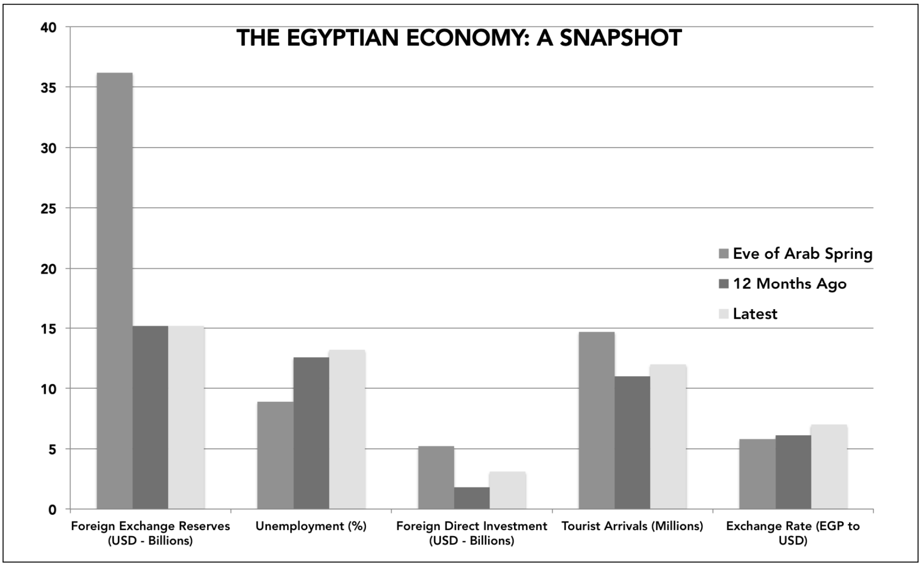
The different chronic economic problems in Egypt were barely tackled effectively during the Mubarak era, who tried as best as possible to avoid public anger, public unrest and riots resulting from comprehensive economic reform that would decrease subsidies, increase taxes and raise prices. The result was increased use of sedatives that deferred reform from one generation to the other, at a price that was more expensive than tackling the economic problems promptly and seriously. Mubarak had in mind the 1977 riots that erupted when late president Sadat decided to liberalize



the economy and to remove subsidies that were provided to a big pool of goods from bread to cigarettes. Sadat had to withhold his economic reforms and Mubarak followed suit and was very skeptical about reforms that would raise prices, increase unemployment in the short run even, or to overhaul different economic sectors and challenge the status–quo.

The typical revenues from the export of oil and natural gas were dwindling and Egypt became a net importer of oil since 2006 and a net importer of energy since 2012. The budget deficit now surpasses 13% in the 2013/2014 budget, while exports, industry and even households are paying a hefty price for delayed planning and reform.

Economic reform and privatization now has negative meaning with the old regimes in Tunisia, Egypt and other Arab countries that followed the IMF/WB recipes. The gigantic corruption and the hazy boundaries between the regimes and



Source: CAPMAS.

its affiliated inner circles of business cronies on the one side and manipulating business opportunities on the other gave a sinister reputation to reform, economic liberalization or to privatization.

Most Value Democracy Over Strong Leader, but Not Over Strong Economy

	We should rely on...		*Which is more important?*	
	Dem. gov't	**Strong leader**	**Good democracy**	**Strong economy**
	%	%	%	%
Lebanon	80	19	53	46
Turkey	68	26	58	37
Egypt	61	33	48	49
Tunisia	61	37	40	59
Jordan	49	42	33	61
Pakistan	31	61	34	58

PEW RESEARCH CENTER Q71 & Q72.

The Egyptian foreign reserve declined steadily from about thirty five billion USD by the end of 2010 before the Arab Spring to virtually sixteen billion USD by mid-2014. It is not yet understandable how Egypt and Tunisia will be able to economically survive in the absence of clear economic plans to support the private sector, secure energy and tighten the budget deficit simultaneously.

IV. Corruption and Rule of Law

4.1. Absolute Powers and Absence of Accountability

The Arab Spring was not about freedoms only, but a shout of anger over regimes and elite corruption, economic disparities, social injustice and business cronies and security bodies that were out of touch. As Leila Bouazizi, the sister of Mohamed Bouazizi who put himself into fire and might had been one of the reasons of the Tunisian revolt described things in Sidi Bouzid, the remote town in central Tunisia as follows “In Sidi Bouzid, those with no connection and no money for bribes are humiliated and insulted and not allowed to live.”

The dilemma that the roots of the Arab Spring uprising is still prevalent represent one of the key impediment to understand how glamorous goals of freedom, dignity and social justice can be reached. Different Arab regimes have crushed opposition and persecuted political and civil activists and brutally dispersed members of different political, civil and religious groups with agendas of change. When prison, exile or hiding was the possible outcome from opposing the repressive regimes, the lilies of the Arab Spring smelled fragrant.

Presidents for life in different Arab states along with aging monarchs were equally depressing and intimidating to many people. Many Arab leaders had reiterated statements and warnings that their heavy–handed ruling is the only shield to avert anarchy and disorder, which seemed to accentuate the desperate hopes of change to come from the regimes or even from a mild bargaining with those in power. The opponents were kept with no refuge to gather and to congregate except in the mosques, feeling strength and rightfulness with different Islamic groups that will ultimately defeat the debilitated seculars after toppling the regimes in numerous rounds of free elections and referendums.

The Arab long legacy of oppression, along with systematic foreign intervention in the region will be critical in the post–revolutionary transition periods that will create deep divides and mistrusts between the revolutionary forces themselves. The old regimes made transition very difficult to any force that would take over in the future, since a culture of benefaction, bribes and nepotism was flourishing and state institutions weakened by regimes' inner circles of interest group and cronies and drove normal people or investors to seek bribes or connections to get their business done.

Different Arab regimes had undermined the civil society in general and the NGOs in particular by attempting to make life very hard for them. Different laws were introduced banning NGOs from operation till they attain permission and a verbal approval from the state, usually from the state security apparatus, where the process was just overwhelming.

NGOs were underscored with heavy burdens not only to register and to operate

Few Things Seem to Be Getting Better

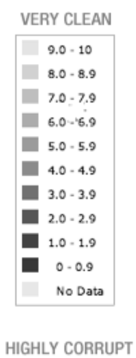
	Compared to the past, __ is ...			
	Getting better	**Getting worse**	**Staying the same**	**DK**
	%	%	%	%
Fairness of judicial system	35	35	23	8
Personal freedoms	33	36	28	3
Law and order	26	44	27	3
Morality	23	39	34	5
Standard of living	12	56	30	2

PEW RESEARCH CENTER Q43EGYa-e.

but also to attain funding from foreign or international resources. Different regimes suppressed the civil society NGOs, labor unions, political parties and syndicates to ensure they are under–resourced and unqualified to mobilize masses of people to challenge the state legitimacy or even to oppose failed policies and deteriorating living standards.

Authoritarian rulers build strong coalitions with business cronies, intelligentsia, and society elites to reinforce their ruling. The absence of a termed called "the rule of law" from daily life meant that everything was possible and no one exactly know what is permitted and what is not. In 2009 just a couple of years before the uprising, "an average 4.6 percent of the Arab GDP went on military spending, compared to a global average of less than 2 percent".[8)]

2010 Transparency Index of Corruption: 0-9: rankings out of (Best 1→178 Worst)
-Transparency International



Country	Iraq	Iran	Sau. Arab.	Yemen	Syria	Egypt
Index	1.5	2.2	4.7	2.2	2.5	3.1
Ranking	175	146	50	146	127	98

Employment Rates 2009-2010 (only consistent data offered) Ranking 1-199 countries (best→worst)
-CIA World Fact Book ☹

Country	Iraq	Iran	Saudi Arabia	Yemen	Syria	Egypt
Rate	15.3%	14.6	10.8	35	8.3	9.0
Ranking	150	145	116	181	94	101

Source: Transparency International and CIA World Fact Book.

8) Stockholm International Peace Research Institute (September 2011).

High level corruption was no secret. From Tunis to Tripoli to Cairo to Damascus to Riyadh scandals of high level officials or monarchs who had allegedly been siphoning off millions and sometimes billions of dollars in the form of illegal commissions or bribes were surfacing quite occasionally.

However, some benefits from the economic liberalization and the FDI was trickling down to the people creating more jobs, but the bigger beneficiaries were privileged circles to the regime who had increasing wealth and power at the expense of an increasing frustration from the masses.

4.2. Cost of Corruption

The economic corruption was just as worse as political corruption. Increasing public deficit, skyrocketing public debt, high inflation and recent rise in unemployment levels are all indicators of the deteriorating economic environment in the Arab World particularly in Syria, Yemen, Egypt, Algeria, Libya and Tunisia.

In 2011, over 25% of the Egyptian population lived in poverty, more than 17% did not have access to food and over 31% of Egyptian children were suffering from malnutrition. The gulf continues to widen between the social services needed and the real funds allocated to target the socially and economically marginalized.

Economic Outlook Bad in Arab World

	Standard of living worse than parents at same age	Worse off financially compared to five years ago	Bad national econ. situation	Bad personal econ. situation	Economy will worsen over next 12 months	*Very* difficult to get a better job/become wealthier than parents	Hard work no guarantee of success	Not better off in free market economy
	%	%	%	%	%	%	%	%
Egypt	35	42	71	76	20	44	42	45
Jordan	29	31	70	64	34	40	37	54
Lebanon	50	51	88	73	45	48	64	34
Christian	*43*	*33*	*83*	*61*	*31*	*33*	*56*	*38*
Sunni	*70*	*76*	*92*	*83*	*65*	*54*	*65*	*36*
Shia	*42*	*53*	*94*	*82*	*47*	*64*	*70*	*29*
Tunisia	22	36	83	43	12	41	24	37
MEDIAN	**32**	**39**	**77**	**69**	**27**	**43**	**40**	**41**

PEW RESEARCH CENTER Q4, Q14, Q15, Q18, Q20, Q26, Q64b & Q84.

The corruption in East Asia in the 1960s described in a manuscript by the Nobel Prize Laureate Gunner Myrdal, could be easily emulated and even surpassed by the Arab counterparts. Myrdal's manuscript explains this in term of soft states. Such countries are “dominated by powerful interests that exploit the power of the state or government to serve their own interests rather than the interests of their own citizens.”[9] Myrdal also advocated “It is a system that easily leads people to think that anybody in a position of power is likely to exploit this in the interest of himself, his family, or other social groups to which he feels loyal”. In an environment where corruption becomes the norm and rule of law is the exception, when public resentment becomes rife due to opportunists who can make easy money by manipulating corrupt institutions, an uprising would not be too far away.

Many things in different Arab countries went wrong. Procedures for obtaining a construction permit can be expedited with a bribe and some good connections, income taxes can be halved or more if you make ‘compromises’ with the tax officer and reward him with generously; no aspect of life including police fines, room in public hospital, free public medical care, and was left untouched by nepotism and corruption. The size of the cash economy and at the same time the informal or the black economy was growing and the rule of law was absent and some civil servants had to supplement their meager income from other sources.

Many people felt that such things as merits and qualifications were meaningless. People had to depend on their personal connections to attain employment or business opportunities. The public was especially discontent with elite corruption and this created hated figures in different Arab countries. Ahmed Ezz, the Egyptian steel magnate and business tycoon was one of the most hated figures in Egypt. Similarly, Leila Trabelsi, spouse of the Tunisian president Ben Ali, was perceived as a greedy opportunist, a modern Marie Antoinette, who was keen on keeping many businesses and investments within her family, as well as to having a stake in any profitable private business.

9) Gunnar Myrdal, Asian Corruption, Asian Drama, 1968.

Will 2011 Popular Uprisings Lead to More Democracy?

	Yes %	No %	DK %
Egypt	76	23	2
Tunisia	69	18	14
Jordan	65	20	16
Lebanon	65	26	9
Turkey	34	37	29
Pakistan	21	20	59

PEW RESEARCH CENTER Q114.

By the time different Arab leaders understood the public frustrations and the popular resentment, it was too late to change or to accommodate masses of people with a mere change of cabinet or economic reform. The inefficient national institutions along with greedy and corrupted business environment left the masses, especially the youth, unable to access the job market in an economy that was in a conundrum, compounded by an environment full of corruption. The punishment then came to many regimes, who underestimated their own people.

At the start of the Arab Spring, protestors were not demanding the removal of geriatric rulers that stayed in power for decades, but rather a stronger rule of law, greater economic equality and political accountability, and a credible mechanism to realize such goals through democratic process through elected parliamentarians and representatives, who truly represented the legitimate interests of the people and not the regime.

V. Conclusion

The Arab region now faces greater instability than ever as the wave of tensions and internal conflicts boil under the surface. However, only by allowing such tensions to come to the surface to be absorbed rather than suppressing them, can they be handled properly. One lesson learnt about the Arab Spring is that the will of the people will be the key determinant in shaping the future of the region. The rulers and the different regimes in the Arab World will no longer enjoy their monopoly over decision-making or exercise absolute and unrestricted powers.

The political transformations have affected all of the four domains where politics and state typically interact: identity, authority, morality and organization. However, the dynamic nature of such changes makes it difficult to predict the direction or the path of future events. Nevertheless, it is certainly clear that Tunisia, Egypt and other Arab countries will never be the same as before; it will be difficult to go back to pre-Arab spring era, establishing absolute and undisputed authority by crushing freedoms.

The growing evidence from the Arab Spring, not limited to Egypt, puts in jeopardy the democratic transition theory, with its assumptions about the secularization of politics and society, as it does not interpret what transpired in Egypt, Tunisia and in other Arab countries and why the uprising was independent of religion, in many instances,.

Modernization does not require secularization. It requires only that people find means of accommodating modernization within religious ideas and adapting religious practice to fit their exigencies. The issues that matter to the Egyptians and to other Arabs are not much different from those in other parts of the world. When asked with an array of different questions, 69 percent chose economy as their utmost priority–reflecting deteriorating living standards, a slightly higher percentage in Egypt than in neighboring countries.

Under the Mubarak regime, only authorized political parties were permitted to contest elections and only authorized candidates were permitted to run. The arena is now open, but typically those who were in opposition or operating underneath are the ones that will lead the field. Some rulers would still follow suit with Mubarak, in being "civilized, corrupted conservative" that Ibn Khaldun[10] predicted would ultimately make every dynasty subject to overthrow.

The rise religious groups such as MB and Ennahda could be a step back in the perspective of liberal western democracies. However, there was never a democracy in Egypt and in Tunisia prior to the Arab Spring and free elections was a bold step forward toward establishing a functioning democracy, rule of law and fairly representing the interest of different constituents. It is unrealistic to conduct comparative studies with prominent democracies that had long established rules and institutions. In addition, religion still play an important role in many western countries such as the United States where the puritanical Christian teachings have influenced voters in different issues, and the Christian right continues to be a dominant player.

Democracy does not function in a vacuum, apart from the historical and political developments as well as the identity of the people. It is much easier to install a new constitution and a new political order, than to enforce such norms and practices that need generations to understand, apply and to successfully exercise. Religion, culture, customs and ethos are all factors affecting the political development and the legitimacy of the state.

Keeping Islamists and genuine opposition under the ground will not do anyone any good. States will face growing skepticism of their legitimacy, from the opposition themselves who will not be denied governance and from the western allies of the Arab regimes who will become a target for militant groups.

The success of the first revolutionary wave with MB and Ennahda in power–at least for some time–proved the fallacy of prominent Islamic militant groups such as Al-Qaeda, the Islamic State and others who have their own limited vision for

10) Ibn Khaldun, The Muqaddimah, World Press.

the Islamic World that can only be achieved by resorting to violence to oust tyrannical rulers and regimes. MB and Ennahda strengthened the argument that Islam and democracy are compatible and boosted the credibility of Islamic parties and groups to contest more elections. It is also true that anarchy and power void in the post–uprising era gave opportunity for some terrorists groups to fill that void in Yemen, Syria and Libya in particular.

The expectation from the Arab Spring is exceptionally high especially for democracy and freedoms. However, the challenge or the problem is that no other group ever exercised governance and regulation other than the old authoritarian regimes that were toppled in the uprising. Developing new leaders and political parties that can effectively overhaul corrupted administrative institutions is not a simple matter and require top notch politicians who can integrate the economic, political, legal, regulatory, cultural, and institutional realities under the countless frictions and conflicts that emerge at the interface between global business decisions and national political practices.

For some time, voters will choose their candidates based on their religious zeal, since politicians were in general corrupted insiders or business cronies allied with the old authoritarian regimes. Once in power, religious parties will lose part of their appeal, especially when tackling chronic economic and social problems, and in bargaining with a constituency frustrated from deteriorating infrastructure and substandard living conditions.

In the present revolutionary context, many segments of the population strive to maximize their benefits and force governments through protests to offer substantial measures such as employing more people in the public sector; provision of additional subsidies and social benefits; raise salaries or to stop privatizing public enterprises. If a government yields to such sectorial demands, they would be faced with worsening public finances, increased demonstrations and riots, tendencies towards greater protectionism as well as burdening the private sector.

The Arab world had been always been presented with an artificial choice between anarchy and dictatorship by illegitimate rulers who attempted to accentuate failures in the Arab democracy as a scapegoat to justify their own existence. The battle for the Arab Spring has revealed economic malaise, institutional failure, social injustice and political fallacy. Armed militants, illegal immigration, ethnic divisions and foreign meddling in the region are all symptoms of the chronic multifaceted problems that paved the way to the Arab Spring.

Many Arab states are now locked in life-or-death struggle with counter-revolutionary forces. However, the seeds of change have been sown and in the near future the grain will be reaped. The breeze of the Arab Spring has carried new uncertainties to replace old certainties. In this new era, everything seems possible.

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Korea Institute for International Economic Policy

370 Sicheong-daero, Sejong-Si 339-705, Korea
Tel: (8244) 414-1042 / Fax: (8244) 414-1043
URL: http://www.**kiep**.go.kr