

The Allama Iqbal Lecture

**Achieving Sustained, Indigenous and
Inclusive Growth**

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**I. INTRODUCTION
DILEMMA OF STAGNATION AND POLARISATION**

The world economy is now facing paramount problems such as long term stagnation of economic growth and worsening income distributions (or economic polarisation). This is even more embarrassing, because the humans have been seeking more equal society during the post-WWII era by engaging in the revised capitalism or social democracy by the most of capitalist developed economies, the balanced growth strategies under social democracy by most of the developing economies and more dramatically the socialist economic regime by the already collapsed socialist blocs, not to mention the still barely surviving North Korea. “Growth stagnation and economic polarisation” is not the one which has been intended and anticipated by policies but is opposite to intention as well as expectations. Some of the critics on capitalist economy have been arguing that this is the outcome of the fundamental contradiction of the capitalist economy from the Marxian perspective and/or the result of the neoliberal policies since the 1980s [Piketty (2014) and Stiglitz (2012)]. However, if one understands that the neoliberalism had short-lived only during the Thatcher-Reagan era, of course with some lingering effects, this episode can be seen as a typhoon within the tea cup. In this regard, broadly speaking, the common underlying institutions of post-war political-economy regime of the world economy can properly be called as the economic equality-seeking “egalitarian democracy” which includes the revised capitalism and social democracy, not to mention the socialism. Therefore, one can see that the efforts to create more economically equal society or in other words, the shared growth have in fact created more unequal as well as growth-stagnated economies against the intention as well as expectation. This seems to be the fundamental dilemma faced now by the world economies and these are perhaps waiting for the economic as well as any other social science profession to come up with a solution to it. Of course, some naive Marxists or leftist economists would claim that this phenomenon of the worsening income inequality is simply the fact of the capitalist economy, i.e., the fundamental contradiction of the

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capitalism, so that the answer is to strengthen further the redistribution. This has been the main tenet of egalitarian economic policy regimes to support the egalitarian democracy ever since the post-war era.

However, the mainstream camp is often heard to say this may be “a new normal” to sustain for some time, which seems implying they do not know why this is happening and how to deal with this, either [Summers (2013) and Krugman (2013)]? In fact, this confession by the mainstream is partly understandable because the mainstream used to be the architect or supporter of the political economy regime, such as the revised capitalism as well as social democracy all along since the post-WWII.

The theme of this lecture, *how to achieve the sustained, indigenous and inclusive growth* is also related to this issue. The world has been seeking the inclusive growth models during the post war period by adopting revised capitalism, social democracy and even the now debunked socialist economic system. Development economics has also preached a balanced growth as the key goal of economic development. However, the world is now experiencing an even more worsened outcome, “growth stagnation and income polarisation”. Ironically, seeking the inclusive growth ended up with ‘exclusive stagnation’. This raises the question then, what has been wrong with economists’ tool kit for not being able to achieve the desired inclusive growth. While the theme of this lecture is in fact exactly the *raison d’être* for the economics subject, but the economics profession has been failing to deliver the right answers till now.

The order of presentation of this paper is as follows; Section II will briefly but critically review the literature on the institutional approaches for inclusive growth. Section III will briefly present a General Theory of Economic Development (GTED) as the basis for the discussion of inclusive growth. GTED will argue that Economic Discrimination (ED) by markets, corporations and government is a necessary condition for economic development while egalitarianism by any of them will be sufficient condition for economic stagnation. ED means treating the different differently while egalitarianism is an anti-thesis to ED. This approach will also provide an answer to the current economic dilemma faced by the global economies. Section IV will present four different political-economy orders and discuss their implications for inclusive growth together with empirical experiences. It argues that “liberal market democracy” and “developmental state” all incorporating “ED policy paradigm” are development-friendly and also serve well for inclusive growth objective. Section V will dwell on the dramatic experiences of Korea’s best inclusive growth during the developmental state followed by the exclusive stagnation in recent decades. This section will also compare the Korean and Pakistani experiences very briefly over the last 60 years and attempt to explain why they turn out to have once been so different, but to be getting so similar now. Section VI will conclude the paper by mentioning about the fundamental nature of capitalist economic development and about how GTED is compared with the mainstream neoclassical growth accounting approach.

II. BRIEF OVERVIEW OF EXISTING ARGUMENTS

We have developed a general theory of economic development which can deal with this issue more systematically. This paper will try to answer the theme question by applying the new theory referred to as GTED here. Before that, let us quickly go over

some of the attempts reported in the existing literature, which have been trying to encompass the so-called development-friendly institutions.

First, Douglass North (1990) has argued that Private Property Rights (PPR) and Economic Freedom (EF) are the prerequisite for economic development and moreover the new institutional economics (NIE) school of thought has been strongly arguing the importance of economic institutions for economic development. However, their development-friendly institutions are in many cases not well-defined and sometimes became obscure because even PPR and economic freedom have not been enough to generate development in many cases. While they sound persuasive when arguing “Institutions do matter, they have been failing to provide the clear answer to the question, “what institutions do really matter for development?”. However, these arguments are now very well received so that the so-called Washington consensus already accommodated them into the shopping list of consensus for economic development policies.

Second, the Washington Consensus on economic development policy derived from NIE, neo-liberalism and mainstream neoclassical growth theory suggests that the free market supported by the institutions of PPR (private property rights) and economic freedom is the most important instrument for economic development, and therefore, the laissez-faire, free market policy will take care of economic development under the stable macroeconomic environment. Now the Washington consensus list is extended to include PPR, EF, privatisation, deregulation, education, R&D, rule of law, SOC (social overhead capital), free trade, and macroeconomic stability by combining the Neoclassical arguments as well as NIE. This approach rightly emphasises the free market but do not fully appreciate the important roles of government as well as corporation. Such mainstream consensus seems insufficient to explain diverse developmental experiences in the history. I don't think this approach is able to explain the current problems of the world economy, low growth and bipolarisation under the most up to date free market system as well as full-dress democracy.

Third, recently, Acemoglu and Robinson (2012) as one strand of NIE propose the concepts of inclusive institutions as development-friendly institutions while extractive ones as development-unfriendly ones from which now the word, “inclusive” becomes very popular, implying the institutions for a shared growth. They define extractive institutions as nondemocratic and exploitive institutions confirming the common sense understanding while defining the inclusive institutions as democratic institutions together with the PPR and economic freedom as usually argued by new institutional economics. Interestingly they are supporting the now most popular political regime, a plural democracy especially including social democracy seeking economic equalities as the inclusive institutions. This argument, however, is not able to explain why then most of the democratic market economies are facing a non-inclusive stagnation after their long effort for inclusive growth in post war era as mentioned above. Fourth, “egalitarian democracy” seeking economic equality including social democracy as well as welfare state under the revised capitalism has become a dominant political economic system in the world. The most serious weakness of all these approaches turns out to be their vulnerability to economic equality ideology, which is not much different from the now-debunked socialist economic ideology as will be more elaborated in order. They do not mind the danger that equality can cause damage to economic development.

This paper will go beyond the existing NIE perspective by developing a theory of the political economy system to handle the issue of the role of the state in economic development. In principle, there could be two types of states in terms of economic development; one is development-friendly state (DFS) and the other is development-unfriendly state (DUFS). DFS must be able to implement appropriate economic policies for economic development. Pre-requisites for DFS include (1) knowing appropriate theories and policies for economic development; and (2) ability to mobilise political support for necessary economic policies among general public as well as politicians, which in turn requires the state to keep a majority of population embodied with development-friendly ideology consistent with appropriate economic policies. It is because in the 21st century, democracy is developed to the extent that most of economic institutions and policies are determined or strongly influenced by the majority party's ideology. Any state that does not meet those two conditions would be classified as a DUFS.

In sum, DFS should be able to disseminate the right ideology suitable for economic development according to appropriate theories of economic development. This means that ideology, which so far has been treated as an exogenous variable in mainstream economics, becomes indigenised as a choice variable. In addition, the theory of economic development which has been in disarray for several decades should be reformulated to provide correct guides to judge which ideology is development-friendly.

III. A GENERAL THEORY OF ECONOMIC DEVELOPMENT (GTED): A BRIEF OVERVIEW

1. Economic Discrimination(ED) as the Basis of Development

A GTED [Jwa (2015) and forthcoming in (2016)]¹ consolidates the existing debates on the role of the market vs. government and incorporates the role of corporation by going beyond the neoclassical growth accounting approach. GTED accepts the complexity-view of economic development [Beinhocker (2006)] by interpreting the development as a non-linear order transformation process from a wagon-economy to railway, to automobile, to airplane, to spaceship economy, rather than to a more-wagons-economy like in neoclassical growth model, and thereby rightly views the modern corporation as the complex organisation of capitalist economy, the locomotive of order transformation of economic development. It also tries to overcome the weakness of NIE by seeking the answer to the question, what institutions are development-friendly. GTED intends to be "general" by "standing on the shoulders of the giants".

GTED starts with a new interpretation of the function of the markets, and discovers the new role of the modern capitalist corporations as the key feature of capitalist economy which is not in the agrarian economy and the positive role of government, all for economic development. The key organising concept of GTED is "economic discrimination (ED) based on performance" and argues all three players, markets, corporations and government should function as an economic discriminator, which is the key necessary condition for economic development. This ED concept is already well established in the West by the maxim, "the God Help those who help

¹Also see my other works in the references for more details.

themselves”, and in the Orient by the maxim, “Never fail to reward a merit or let a fault go unpunished”, “dispensation of justice” or “信賞必罰 in Chinese (신상필벌 in Korean)”² in 2200 years ago by the Chinese philosophers known as the School of Law or the Legalism. ED has been the fact of life all along with the long history of human evolution. ED means treating economic difference differently but does not imply anything like political or social discrimination. GTED incorporates ED mechanism as the key principle of economic development. A short overview of GTED is in order.

2. Role of Market and Nature of Development

First, the function of markets is redefined here. Markets in the real world, different from the perfectly competitive markets in the textbook, discriminate economic agents according to their economic achievements and direct resources and wealth to the successful agents, which is in fact what we all are doing in everyday life. Markets thereby press to create economic inequalities and motivate them to work harder. In this sense, markets are a motivational discriminator just like a god who helps those who help themselves. This economic discrimination (ED) and motivational function is in fact the essential role of markets that make them an important institution for economic development. In this view, any mechanism strengthening the market’s discrimination function and thereby providing motivation by helping acknowledging differences in economic outcomes will necessarily help promote economic development.

Seen from this perspective, PPR system and economic freedom, in fact, can be a means for creating economic differences and inequalities and as a result motivating economic agents to work harder, and therefore, should be good for economic development. In this regard, the capitalist market economy with unfettered PPR and economic freedom may have more chances to grow. But this is not the end of the story as will be seen in the following.

Second, development is a complex, cultural evolutionary process of free-replication of or free-riding on others’ success knowhow, thereby the mass of people becomes successful, which is the very nature of non-linear order transformation process of development. Markets, however, cannot handle such free-riding problem successfully especially because market transactions are faced with positive transaction costs. Economic leaders that serve as sources of success knowhow therefore tend to disappear from the market. Markets alone are not very good at producing the critical mass of economically successful role models to lead the transformation process. This may be called market failure of ED and motivation, a new kind of market failure which is different from the textbook case. Markets alone are not enough to create developmental process, theoretically as well as historically as vividly exhibited by the long history of economic stagnation during the agrarian economy as well as the modern day catch-up failure by the many underdeveloped market economies.

Here, the introduction of a secure PPR system may help improve the market’s power of discrimination but not enough to solve the free-riding problem since knowhow of success is intrinsically so difficult to be identified that it may become prohibitively costly to fully assign and enforce PPR for it. So, market economy is destined to be trapped in the developmental failure despite the spread of the capitalist market economy.

²“Reward a merit but punish a demerit”. Korean as well as Chinese has the same meaning.

3. Role of Corporation

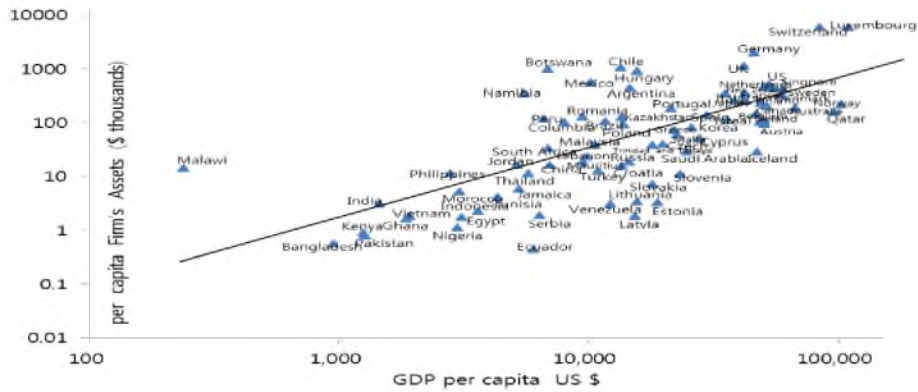
Third, the natural solution to developmental failure is the private firm as an organisation based on the command-control mechanism which can therefore, avoid transaction costs (or save information costs) and solve the market failure by internalising knowhow-free-riding activities. The firm comes into existence to take advantage of the markets' failure of ED and turn itself into an expert in ED. Especially, the modern joint-stock corporation is a new social technology to arise in the capitalist economy as an emergent complex organisation from the individually or family owned black-smith firms in agrarian economy and is able to expand its capital base and capability to take business risk even to the unlimited scale. Theoretically, the market failure of economic development during the long history of agrarian economy had been due to the lack of such complex organisations. Then the natural question should be why many of capitalist economies in the globe are failing in catch-up even with the modern corporate system as well as market economy.

The clue for an answer lies in the very nature of development, free-riding on the shoulders of the giants. In the market places, the successful corporations are destined to be subject to the free-riding on their success-knowledge by the followers and therefore, the market fails to produce such successful corporations on a large scale. In this context, modern developmental-friendly state (DFS) as public organisation has also been the important supplement to the market by promoting the growth of such corporations. Here, we find the positive role for the government as well as corporation for economic development. With the corporate-promotion role of the government, the modern corporations have eventually been the strong supplement to the market in the capitalist economy during and since the industrial revolution. Note that private joint stock company began to appear and burgeon from the mid-17th century, became formally legalised by England in the early 19th century after a century-long dark age under the bubble Act during the 18th century [Micklethwait and Wooldridge (2003)], and has finally played the key locomotive role for the industrial revolution as well as for the development of capitalist economy. The visible hand of modern corporations has begun to supplement the invisible hand of the markets.³ Without the corporate growth, the economy is destined to stay at or move back to the agrarian economy as seen in the case of the very under-developed economies as well as the failed socialist economies. Now the corporate sector in capitalist economy substitutes for the land in agrarian economy as the home of survival of humans as only about less than 5 percent of GDP as well as total jobs in most of developed economies stems from the agriculture.

Now the modern corporations are helping achieve the shared and inclusive growth of capitalist economy as shown by Figure 1 and Figure 2. In this vein, capitalist economy should have been named as "corporate economy", not "market economy". Note that the joint stock company is the unique social technology only in the capitalist economy, while market exchange has been ubiquitous ever since the hunter-gatherer era. Modern corporation shouldn't be regarded any more as an evil monster for creating economic inequalities as argued by Karl Marx or any other critics on Capitalism.

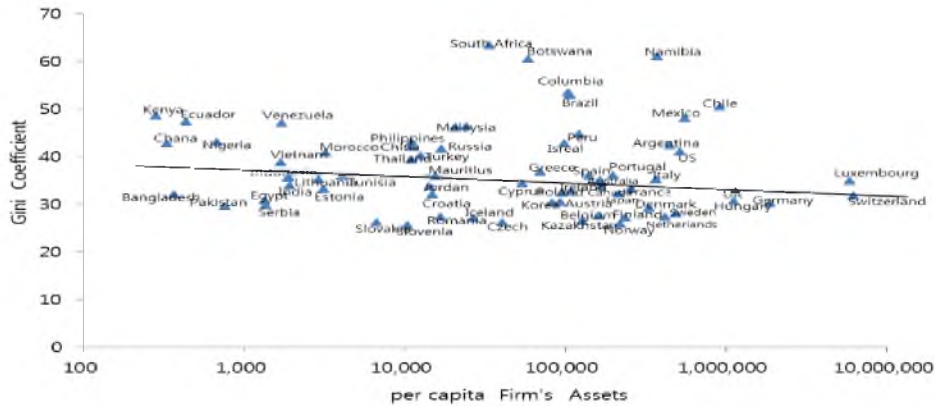
³See Chandler (1977) for a similar argument.

Fig. 1. Corporate-led Growth



Note: GDP per capita and per capita Firm's Assets (77 countries as of 2013). Source: SMP Capital IQ & World Bank.

Fig. 2. Corporate-led Inclusive Growth



Note: Per capita Firm's Assets and Gini coefficient (70 countries for 2008 to 2013). Source: SMP Capital IQ & World Bank.

4. Role of Government

Fourth, GTED reinterprets markets as motivational economic discriminator which can be the logical basis for the role of government for economic development. The government should help correct the market failure of solving free-riding problems by introducing the socio-economic institutions that can help those individuals and corporations who help themselves but are not fully rewarded. The market institutions should be upgraded and reinforced to fully match the rewards to the performances. Market ED-function reinforcement should be the key role of the government for development. This new interpretation of the role of the government is diametrically opposite to the now most popular paradigm of political economy regime seeking economic equalities, as the prime goal of the government policy and different from the main stream economics profession which has been prone to supporting such egalitarian political economy regime.

According to a new interpretation of markets, the market can be interpreted as exercising an industrial policies (IP) everyday by picking better performers and providing more resources to them. In this regards, IP can be re-interpreted as an ED and motivational mechanism. Successful government IP should supplement and reinforce the market's ED function, i.e. the market-led IP by helping those individuals and corporations who help themselves rather than going against or disregarding them. IP should pick the market winners ex post, after the market outcome, rather than pick the winners ex ante, before the market outcome, which can help avoid the difficult question of how to pick the winners in ex ante in the traditional debates.

Seen from this perspective, Japanese and Korean industrial policies were successful precisely because both were implemented in an economically highly discriminatory manner so as to re-enforce the market discrimination and motivational function. That is, IP always helped those corporations that helped themselves, based on their market performances. In this sense, "industrial policy" should be renamed as discriminatory "corporate promotion policy," which could help correct the market and developmental failure. By this corporate-promotional IP, the corporations can become to play the role of the locomotive for inclusive economic development by overcoming the free-riding problem. (see Figure 1 and Figure 2.)

GTED argues that the capitalist economy is a "corporate economy". Then a question may arise as to how promote corporations for inclusive growth in substitution for traditional industrial policy. Governments can select a specific industry for promotion in the name of import substitution policy or new industry promotion policy while the implementation of those policies can be successful only by "corporate promotion policy". Some lessons can be learned from the experience of successful corporate promotion policy like Korea. The corporate promotion policy can be named as "corporate-ED policy" which can be implemented as follows:

- (1) SME policy supported the better performing firms with more financial as well as tax benefits according to their performance, and they were given the choice to take over the poorly performing firms.
- (2) Better performing exporters were given more financial support and tax benefits and were guided to take over the lower performing exporters.⁴
- (3) Privatisation policy will always allow the better performing corporations to take over the SOEs based on the ED paradigm without any political consideration.
- (4) In the process of so-called industrial restructuring, the insolvent firms should always be allowed to be taken over by the solvent, competitive firms.
- (5) Any corporate policy for economic development should keep to the ED principle.

However, there may arise some concern about potential danger of conglomeration and the resulting monopoly power by the adoption of ED principle. This issue has always

⁴Accurate actual market performance evaluation is the key for the success of ED export support policies. If it is necessary to amplify ED-support system further, one can introduce "a nation-wide export contest" which selects and recognises the best and better exporters based on their actual export performances and thereby publicises them to be widely known to banks and financial market which are always looking for them for support.

been on the table for economic policy discussion but without successful solution. Demsetz (1974), and Alchian and Allen (1977) argue that monopoly results either from government protection or efficiency: The same applies to conglomeration. If the source of monopolisation or conglomeration is the efficiency, not the government protection, then the solution can be rationally devised, while otherwise one should remove the protections. In the efficiency-driven case, care should be taken not to confuse “ability” with “incentives” to abuse [Alchian and Allen (1977)]. Ability does not necessarily imply the incentive. Threat of market power can be tackled by stronger competitive pressure of potential as well as actual rivals. It is good to open the market not only for domestic competitors but also for foreign competitors to check the incentives to abuse. Even if the direct regulation as an alternative may have popular political appeal, it is not advised to resort to such direct regulation on the growth of corporations as used to be the case for many economies including Korea now. This policy has a serious danger to kill the very incentive to grow on the part of corporate sector which in turn harms the inclusive growth. The policy should concentrate to minimise the incentive to abuse by bringing actual as well as potential competitive threat as much as possible while the incentive to grow should be maintained as high as possible by allowing freer choice of investment.

The ED feature of successful government policies is not confined only to the cases of successful IP, and is generally applicable to the most cases of economic or public policies. Successful economic policies turn out to be economically discriminatory, while failed policies are egalitarian disregarding difference in performance. This is against the popular egalitarian argument that the government should intervene against market outcomes in order to correct the economic imbalances created by the market economy. In this case, markets will revenge by simply standing still, resulting in stagnation and no-development.

5. Ideology and politics in Development

Fifth, Ideology or mindset is one of the key informal institutions constraining the economic behaviour and performance. In this regard, the most important development-friendly ideology such as “can-do spirit” or “self-help spirit” should be embodied into the peoples’ way of thinking in order to have ‘a sustained and indigenous growth and development’. According to Korean experience, the economic discriminatory policy regime being repeatedly enforced is very important on top of simple education and/or propaganda. Especially, Korea’s “can-do spirit” turns out to have been created by the repeated application of government’s discriminatory economic policies helping only those who help themselves such as Saemaul Undong (new village movement), export-promotion policies and IP for HCI drive. Note that ‘a sustained and indigenous growth can only be achievable if the people’s mindset is changed into a development-friendly one’.

In this regard, politics becomes so important, as the political parties translate the informal institutions such as prevailing political ideology into the formal institutions which constraints economic behaviour and performance as an incentive structure of the society. Therefore, the politics as a framer of economic policy regime in the democratic political system should be ready to accommodate the principle of ED lest the law and regulations go against the ED. Politics as well as government should support ED if they

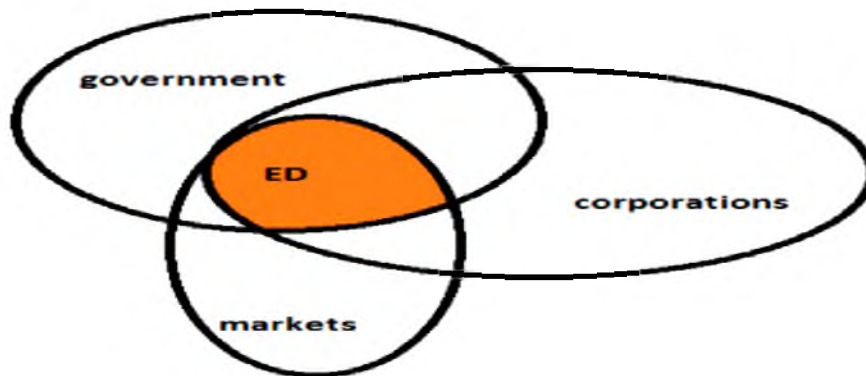
can be development-friendly. They should however make sure to avoid the egalitarian trap, while the equality of opportunity before the law should be fully guaranteed.

6. Holy Trinity of Economic Development, Markets, Corporations and Government

Now, let me consolidate the arguments. Discriminatory economic institutions embodying the principle of treating economic differences differently, i.e. ED paradigm and respecting the ideology of helping those who help themselves are good for development, while egalitarian institutions that treat economic differences equally especially by disregarding economic excellence will hinder economic prosperity. Markets cum PPR system and economic freedom may be good for the survival of the economy, but they need to be supplemented by economic discrimination by the government and private organisations if there could be any chances for real economic take-off and catch-up in the development game. I have been arguing 'that ED is a necessary condition for economic development, while economic egalitarianism is a sufficient condition for economic stagnation'. In fact, "ED and motivation by the market as well as government and corporation is a necessary condition for economic development" is the key message of condensed development experiences of Japan, Korea and China as well as extended western development experiences.

Figure 3 summarise the general theory of economic development in which the holy trinity of economic development, markets, corporations and government should altogether keep to the principle of ED to be development-friendly. It should be remembered that ED paradigm has been the basis not only for the post-war success of Korea under Park Chung-Hee, China under Deng Xiao Ping, Singapore under Lee Kwan Yew, Malaysia under Mahathir and Taiwan in 60s-70s as well as the industrial revolution of the now developed economies but also for all the successful civilisations in history. Furthermore, ED paradigm has always been the key success factor for the corporate management. Now, the ED paradigm which was born even longer than 2000 years ago is being reborn in recent years with the behavioural economics and experimental economics [Gneezy and List (2013)] as well as with management science [Welch (2005)]. Egalitarianism disregarding the excellence in social as well as economic performance can never be useful for the prosperity of any society. Don't forget the memory of the demise of socialist economies which was exactly due to the lack of ED paradigm.

Fig. 3. Holy Trinity of Economic Development [Jwa (2015)]



7. Implications of GTED on Public Policies and Global Economic Dilemma

In general, there can be two different kinds of public policies; one is economic development policy and another is social (empowerment) policy. So far in economic policy discussion, there has not been much concern about the different nature of two policies except for the common-sense understanding that the former is for creating value-added while the latter is just for helping the low income people or the under-privileged to survive or sustain even without new value creation. Along with this line, both policies have been regarded as better to support as many policy objects as possible and as much as possible too. Now it seems the case that economic policies as well as social policies all degenerated to the egalitarian (support) policies without any incentive differentiation depending on the responses, positive or negative, by the recipients, i.e., ED mechanism. As a result, both policies have been unfriendly to growth and development as well as unsustainable as they lack an incentive scheme to create new value-added or growth, which in turn hurts the soundness of public finance.

Now, GTED strongly implies that economic policies should recover their fundamental nature of ED support principle if they can really help develop economy and also the social policies should be reformed to be based on the ED principle if they are to be self-sustainable by creating new value-added. Therefore, public policy in general should adopt ED support principle. In this new framework, not only the economic but also social policies would contribute to growth and development on top of being financially sustainable. Especially, it should be recognised that this new ED social policy framework will greatly help improve its own financial sustainability compared to the traditional incentive-lacking social policy.

Balanced development ideology has been the leading egalitarian policy paradigm. Redistributive welfare policies and social empowerment policies have been egalitarian, lacking the ED principle so that incentive to grow has been discouraged while moral hazard has been encouraged. Thereby the sustainability of the egalitarian policies has been greatly damaged, ending up with financial difficulties for the implementing States. In the midst of low growth and less job creation with the loss of developmental self-help spirit influenced by the egalitarian incentive structure, the size of middle income people is destined to dwindle, thus leading to polarisation.

According to GTED, this scenario seems the most plausible reason for the current global economic problem; egalitarian economic and social policies, killing the incentive to grow and encouraging moral hazard, low growth and no job creation with more social welfare demand, increasing pressure for government expenditures for welfare without corresponding tax revenues, mounting government debts global financial crisis with low growth and income polarisation. Having the social policy as well as the economic policy killing the very incentive to grow, how could we expect the growth and development? One can characterise the current situation as an “egalitarian trap”. GTED implies it is imperative for developed as well as underdeveloped economies to get out of “egalitarian trap” if they want to get over the low growth and bipolarisation dilemma. The solution is to turn to the market democracy keeping to the ED principle as will be argued in the next section.

IV. DEVELOPMENT-FRIENDLY POLITICAL-ECONOMY REGIMES FOR INCLUSIVE GROWTH

This section will apply GTED to discover the development-friendly political-economy order for inclusive growth. The theme of this paper, “sustained, indigenous and inclusive growth” can be achieved if ED principle becomes embodied into the socio-economic institutions so that ED incentive structure is so firmly built into the system and strictly enforced that the members of the society change their behaviour and eventually their mindset consistently with ED principle in the sustained and indigenous manner. Therefore, it is necessary to investigate the role of mindset or ideology as informal institution and politics as framer of formal institutions in development.

1. Ideology of Equality and Development

According to the ED paradigm, the political ideology as well as political institutions allowing economic differences and inequalities as a natural outcome of the development and at least not regarding them as contradiction of capitalist economy as far as the majority becomes improved materially will tend to be development-friendly, while the opposite ideology and political institution favouring economic equalities such as equality of economic outcomes and/or equality of substantive economic opportunity will become development-unfriendly.

Here, some note on the development-friendly concept of equality should be in order. Will equality be a good friend with the economic development under the ED paradigm? Equality before the law can most naturally be a good friend with economic development as it allows the markets to work for ED. Equality of opportunity can be commensurate with development, if it is interpreted as equality of opportunity before the law but cannot be so, if it is interpreted as a substantive opportunity implying the equal capability to achieve as the former interpretation, but the latter will not allow the market to work for ED. Note that an equal capability will naturally lead to an equal outcome except for the case of interruption by difference in luck. Finally, equality of the outcome will obviously kill any incentive to grow as it means a socialist economic system.

From this perspective, one can easily see the potential danger with the ideology of “economic democracy”. Economic democracy seeks substantive democracy by eliminating the economic differences and thereby equalising economic powers among people, organisation, lest unequal economic resources do not unequally and unfairly influence the democratic process [Dahl (1985)]. While it sounds great for an ideal democracy, however, it is destined to go against the function of the market ED and to become development-friendly.

2. Political institutions and Development: The Political Economy Order

The two wheels of the Democracy Cart are liberty and equality. The issue with liberty is that it seems easily subdued by egalitarian ethos especially in modern-day democracies that have emphasised “equal rights.” Central to ideal democracy, for example, is the “*one man one vote*” mechanism, which provides an easy environment for egalitarian ethos to thrive. However, such *egalitarianism* has tended to permeate into all aspects of life, being translated into “equal opportunity” in economic capability rather

than before the law, “equal outcome”, etc. This adversely affects economic development, because economic development is based on ED.

According to the ED paradigm, one can classify political economy regime into 4 different combinations of political order and economic orders as shown in Table 1; A+C=market democracy, A+D=social democracy, B+C=developmental state and B+D=totalitarian regime. Here, it can easily be seen that A+C and B+C are development-friendly because they are adopting ED economic policies while A+D and B+D are development-unfriendly because they are under economically egalitarian regime. Therefore, seen from this perspective, as far as economic development is concerned, political order being democratic or authoritarian is not crucial while choice of economic order becomes very crucial. Even politically authoritarian states can be development-friendly if they are economically discriminatory by adopting ED policies. On the other hand, even liberal democracies can lead to economic stagnation if they become economically egalitarian.

Note that this 4-regime classification is different from the 2-regime classification, inclusive vs. extractive institutions by Acemoglu and Robinson (2012). Our classification is much richer than theirs in that our totalitarian state is exactly same as the extractive institution while our classification amounts to subdividing the inclusive institution into 3 different regimes, developmental state, market democracy and egalitarian democracy. Even inclusive institution can fail to develop if it becomes economically egalitarian. Interestingly they seem to imply the inclusive regime as if egalitarian democracy which is develop-unfriendly according to ED perspective. On the other hand, even authoritarian political regime can become a development state for inclusive growth by implementing ED economic policy regime. In this regard, their two regime classification of inclusive and extractive institutions is not much different from the classification of democratic and nondemocratic order which however is not much helpful in discerning the DFS or DUFS.

Table 1
Political-Economy Matrix of Social Order

Political Order	(A) Liberty (Equal Political Rights)	(B) Authoritarian
Economic Order	(B) Economic Discrimination(ED)	(C) Egalitarianism (Equal Outcome)

Source: Jwa and Yoon (2004a).

3. Historical Experiences of Growth and Development

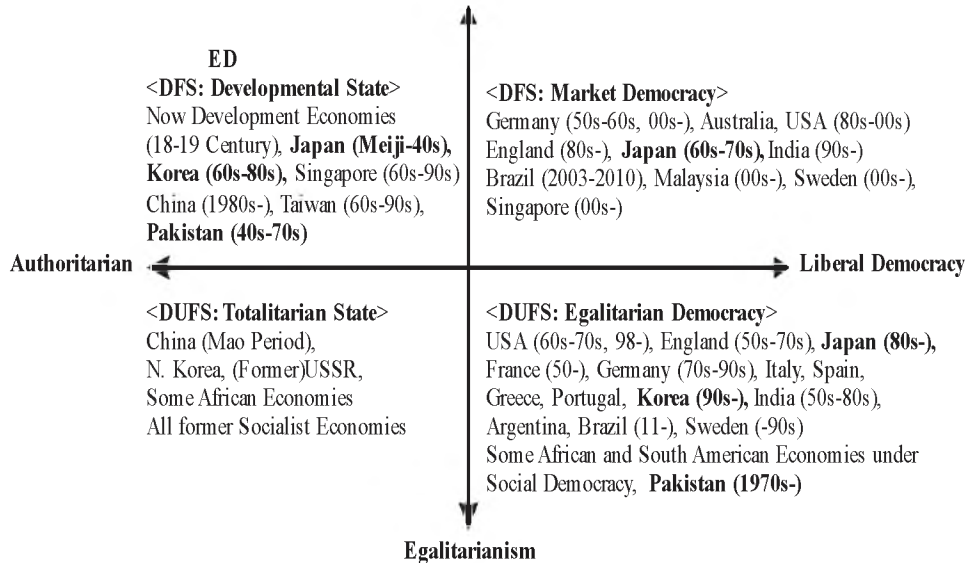
With this framework of political economy regime, one can consistently map out diverse experiences of economic development into 4-different quadrants as shown in Figure 4. This mapping table is from Jwa (2004, 2006 and 2016).

Some interesting observations are in order:

- (1) History seems to reveal the sequential movement of developmental cycles, from totalitarian, to developmental state, to market democracy and to Egalitarian democracy, or from totalitarian state to egalitarian democracy, or back and forth between market and egalitarian democracy.

- (2) Market democracy seems to be not a stable regime and many economies which had once been growing dynamically under market democracy tend to degenerate to the egalitarian democracy. This may be due to the inherent populist nature of democracy which tries to democratise the economy. To avoid this it may be necessary to devise a mechanism to economise the democracy or to minimise the incentive to democratise economy.

Fig. 4. Political-Economy Axis of Social Order



4. How to Create Development-Friendly Ideology and State

Condensed development experiences of Korea, Japan, and China imply that repeated application of economic institutions and policies based on ED principle will help change peoples' ideology toward being development-friendly. Conditions for this are: (1) ED leadership is required who understands ED principle and is determined to introduce and implement the nation's economic institutions which is consistent with ED principle as listed below. (2) Some firewall must be built between economic policy-making and politics in order to minimise the egalitarian populism. The strategy of "economising the politics" may be necessary. Examples of such ED leadership who once succeeded in changing the nation's ideology towards DFS are as follows: leadership in Meiji Japan, Park Chung-Hee in Korea, Lee Kwan-yew in Singapore, Deng Xiao ping in China, Thatcher in England, Lula da Silva in Brazil, Manmohan Singh in India, Mahathir in Malaysia and maybe Reagan in USA, to name a few as can be confirmed in Figure 4.

5. A List of Development-Friendly Institutions for Inclusive Growth

GTED can now provide a rather comprehensive list of development-friendly institutions and policies for sustained, indigenous and inclusive growth from the ED perspective. Institutions could include market democracy, individual and corporate

economic freedom, private property right system, rule of law, and any institution to help reduce transaction or information costs, stable macroeconomic environment, stable political environment, corporate-friendly socio-economic environment, etc. Policies could include economic policies to differentiate incentives in terms of taxes and subsidies and financial supports depending on performances such as SM&E promotion, agricultural support, regional development, R&D support, educational support, etc. Social empowerment policies including various social and welfare policies should also help those who help themselves based on ED if the sustainability is to be improved.

6. Economic Development Needs an Economic Theory of Ideology

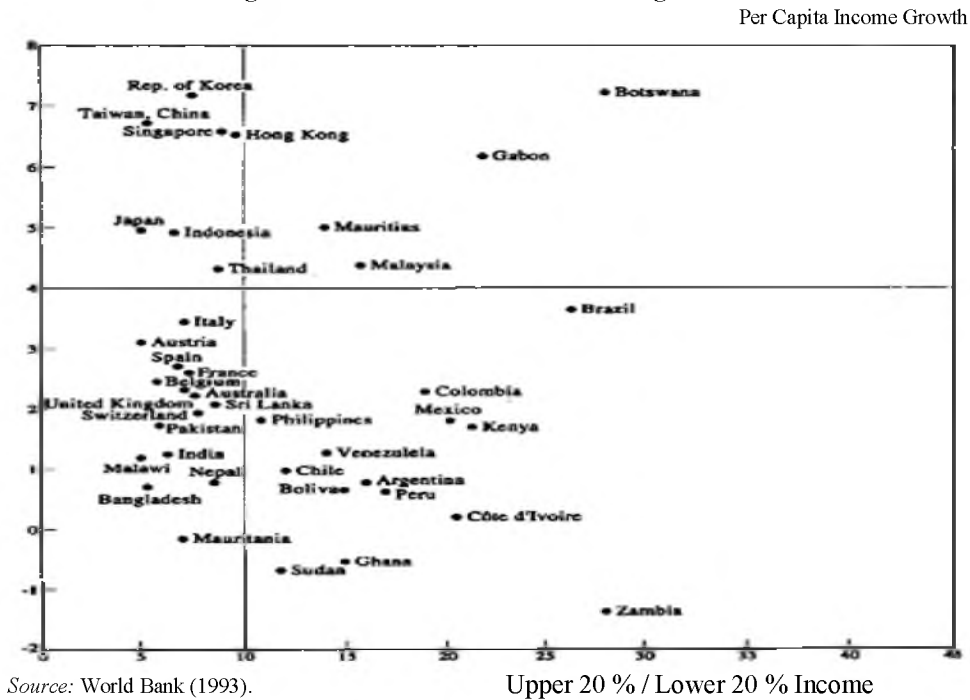
Economic science has so far been lacking an economic theory of ideology and politics and degenerated as providing technical advices to achieve national agenda set by political ideologies. As a result, it became a subsidiary science to political science. This has been the main reason for the egalitarian economic policy regime to widely spread out to the global economies in the name of helping everybody equally regardless of their economic efforts and achievements, and thereby causing most of global economies to degenerate towards stagnation for several decades. Now, it seems most of the globe is covered with the DUFSS while the DFS becomes a dying species. Economic science should provide a theory to discriminate political ideologies based on their economic development implication, and help prevent unfounded political ideologies from producing development-unfriendly institutions and thereby, not only harming the inclusive growth but the dynamism of the global economy. The new GTED based on the ED paradigm is an attempt to contribute to such an effort.

V. KOREA: THE BEST INCLUSIVE GROWTH LED BY ED-LEADERSHIP FOLLOWED BY EXCLUSIVE STAGNATION

1. Korea's Miracle led by Park Chung-hee's ED Leadership

Korea has been praised as one of the best shared or inclusive growth experiences during the developmental era since 1960s-1980s as shown in Figure 5 [World Bank (1993)]. In this era, Park Chung-hee leadership was so critical for inclusive growth. First, he always tried to economise the politics, that is, to prevent the populist democracy from distorting ED principle in economic policy making and implementation by leaning even to rather authoritarian regime, in spite of severe criticism by the domestic opponents as well as foreign allies. Second, he always respected ED-market principle, and applied and implemented ED principle to all economic as well as social policies by helping those who help themselves. Third, he always kept to the ED-corporate promotion policies to help grow the corporations as a means of expanding economic territory, instead of "Colonisation by Strong Army under the imperialism". Finally, he was truly a leader with firm commitment to economic development for people and was clean without corruption. Park's leadership can be dubbed as "ED leadership".

Fig. 5. Korea's Shared Growth During 60s-80s



Economic policies under Korea's era of developmental state all adopted the ED policy which created keen competition among corporations, entrepreneurs, and rural towns;

- (1) Export Promotion policy by helping only those who deliver better export performance.
- (2) Heavy and Chemical Industry Drive (import substitution policy) by allowing only most or more capable exporters to enter the HCI sector.⁵
- (3) Promotion of SME to large corporation by helping only those who perform better in export.
- (4) Saemaul Undong (SU: rural development drive) by helping only those who deliver positive outcome with self-help spirits. With ED incentive structure built into SU by helping only those who help themselves, SU could change the mindset as well as behaviour of rural people in a sustainable and indigenous way.

Note that Park's ED leadership was able to change the peoples' ideology, historical tradition, and culture into being development-friendly by keeping to the dictum of "the God help those who help themselves."

⁵Korean government required the potential entrants to provide the minimum 25 percent of large capital requirements of the HCI and the government loaned the remaining 75 percent. So only the best export performers were able to enter the HCI. If this is to be applied to the Pakistani case, for example, one may probably think of allowing better exporters to take over the SOEs with reasonable prices by requiring a certain minimum own seed-capital to be put in which is not debt-financed.

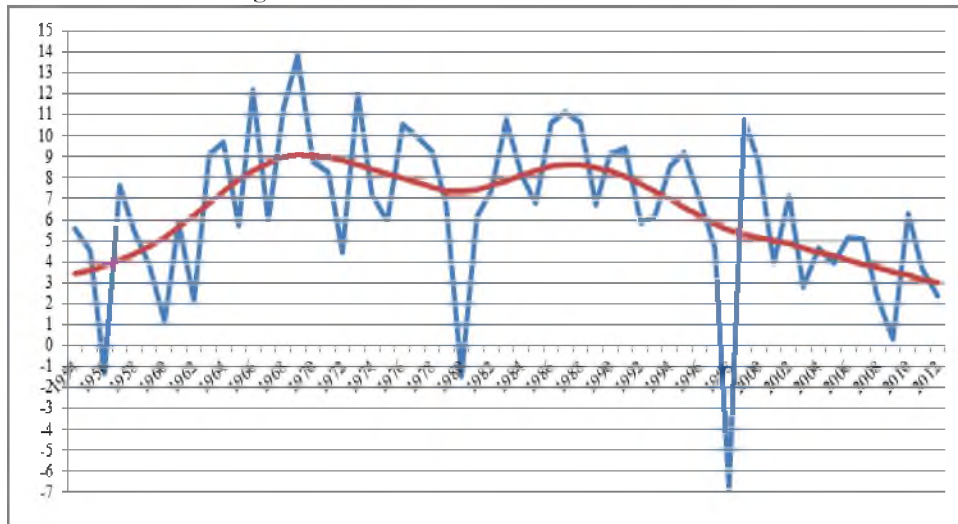
2. Korea's Exclusive Stagnation Led by Egalitarian Democracy

Korea turned away from the Park Chunghee paradigm to egalitarianism under Egalitarian Democracy since the late 1980s. Since then, Slowly first and rapidly later on, Korea has fallen into the “egalitarian trap” to make things even out, disfavouring the large, rich, and growing people, organisations, corporations, schools and regions, etc., over the small, weak, poor and stagnating ones. Specific examples are as follows;

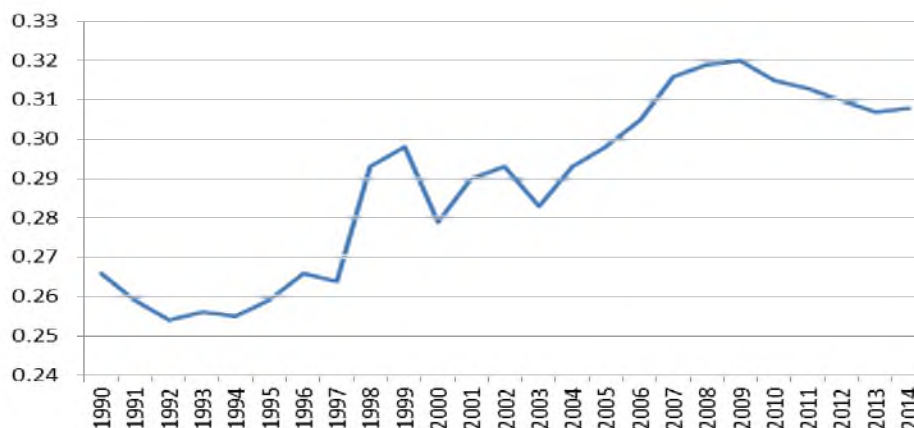
- (1) Regulate the large corporations because they are big, becoming stumbling block to economic democracy.
- (2) Support S&ME because they are small, weak, not because they are doing good.
- (3) Support farmers because they are weak, not because they behave as self-help and are doing good.
- (4) Regulate metropolitan region and support all locals equally to achieve a balanced regional development.
- (5) Disfavour Seoul universities but favour local universities for a balanced growth in university and regions.
- (6) Introduce surtax on the rich.
- (7) Introduce educational system to equalise the students performances across the schools and regions.
- (8) Economic development policy in general and industrial policy specifically turned into egalitarian policies (Ex. Venture promotion, New industry promotion, Green growth initiative, creative industry promotion, etc.).

ED principle has not been at work. The economy has not performed as in the earlier stages of economic development as shown in Figure 6. Is this the end of Korea's economic development? This will be so unless Korea turns into a liberal Market Democracy by getting out of Egalitarian Democracy.

Fig. 6. Korea's Potential Growth Rate Trend



Source: The author's own calculation by applying the Hodrick-Prescott (H-P) filter. Note: Blue; actual GDP growth rate, Red; potential GDP growth rate.

Fig. 7. Korea's Worsening Income Distribution since 1990s

Source: Bureau of Statistics, Korea.

Note: Gini Coefficient (Urban Households).

3. Pakistan Compared with Korea

Now it is time to bring the implications of GTED to explain why Pakistan is lagging behind Korea in terms of growth since 1970s even if Korea learned development knowhow from Pakistan in the early stage of development. What made the difference and similarity between Korean and Pakistani economic performances during the last 70 years?

Korea and Pakistan began their growth game from almost the same starting line in late 1940s. Pakistan took the lead until the end of 50s and Korea even learned about how to write economic development plan from Pakistan. Both had run at the similar pace up to the end of 60s. However, the growth pace began to turn favourable to Korea since 1970s. Since then Korea outpaced Pakistan with unbelievable margin for longer than 40 years. Now in terms of the level, Korea already reached at the level of lower group of developed economies while Pakistan is still working hard to catch up. However, for a decade or so, Korea's growth is rapidly slowing down, converging to and even becoming lower than Pakistan. What makes these differences?

From the GTED perspective, the key factor for the divergence between the two since 70s seems to lie in their different policies toward corporations. In the early 1970s, Pakistan took the radical turn to the policy of nationalising major corporations while Korea amplified her corporate promotion policy by adopting the Heavy and Chemical Industry (HCI) drive even on the top of the strong supportive policies to exporting firms. Pakistan took the nationalisation policy of corporate sector from 1972 to 1976 under the banner of Economic Democracy as follows:⁶

- (1) 1972: 31 large corporations including 22 family-owned and managed corporate groups were nationalised.
- (2) 1973: Constitutional reform to legitimise the nationalisation of large corporations for de-concentration of economic power, and protection of SM&Es and farmers.

⁶Wikipedia

- (3) 1974: 13 commercial banks, over a dozen insurance companies, two petroleum companies and 10 shipping companies were nationalised.
- (4) 1976: More than 2000 traders in agricultural sector were nationalised in order to eliminate the middleman' margin.

On the other hand, Korea continued a journey toward a corporate-led growth strategy up until the late 1980s while she began to deviate from it since then after political democracy. From the 1990s, Korea turned to the egalitarian economic policy regime which is not much different from the Pakistan since 1970s. Pakistan since 1990s has been trying to privatise the SOEs without much success judging from the corporate-ED policy perspective. Now both economies are suffering from the anti-large corporation policies which seem to be the cause for the slow growth in spite of many contemporary innovative policy initiatives by both countries.

VI. CONCLUDING REMARKS

As a few final words, this paper warns against the now-most popular sentiment among the world intellectuals and even economic professions that economic inequality is the “devil monster” while economic equality is the Angel. It should not be forgotten that “economic inequality is a necessary condition for economic development, while economic equality is the sufficient condition for economic stagnation”. Natural inequalities emerging from markets’ as well as government discrimination function based on the actual performances should be most welcomed, while artificial social as well as economic inequalities arising from the government arbitrary intervention to favour special groups with political motivation should be actively driven out of the society. After all, capitalist economic development is the natural process of unequal but shared and inclusive development.

In this regard, it is worthwhile to recall the process of development, free-riding on the others’ success knowhow. This in fact implies that having prosperous neighbour is good for our development as we do exploit them, which becomes the basis for inclusive growth. However, remember that Karl Marx and pro-socialism ideologists have been arguing the other way around that having prosperous neighbour is bad for our development, as they will exploit us. GTED implies Karl Marx is standing on his head.

Finally, it is time to see how GTED is compared with the now most popular neoclassical growth accounting model (NGAM). Unfortunately NGAM is nothing more than an accounting theory or even worse a tautology to describe the endogenous variable by another set of endogenous variables without knowing the exact exogenous explaining variables. This is the reason why NGAM has hard time explaining the current no-development situation or market collapses in certain countries/regions. Note that only the explanation by fundamental causing, exogenous variables can help provide solution, which is what GTED intends to do. Why some countries are but others are not able to develop, given the same international conditions of capital market, labour market, technology market, trade openness and the similar domestic institutions and furthermore, why the world economic growth has now been performing worse than before, even with much more developed levels of the human and physical capital and technology as well as much more refined domestic market institutions, are not readily explained by NGAM.

NGAM as well as Washington consensus tells us tautologically what to do in order to be a developed economy through accounting analysis but never tells us how to achieve what to do for a development. How to achieve a sustained, indigenous and inclusive growth is what GTED intends to answer by trying to discover the fundamental exogenous factors to explain the process of development. GTED approach concludes that ED incentive system is the key and necessary condition to unlock the mystery of economic development as it can help create something even out of nothing. Modern corporations as well as individual farmers, researchers, individual workers and even the public servants motivated under the ED-incentive system can in a concerted manner create physical capital, human capital and technology, thereby economic development, from a lower level and facilitate the objectives of a sustainable, indigenous and inclusive growth.

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