

Part II: Northeast Asian Economies: The Social, Economic, and Political Environment for Regional Cooperation

1 The Socio-Economic Environment in Northeast Asian Countries for Regional Cooperation

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THE OPPORTUNITY FOR NORTHEAST ASIA¹ IN THE 1990S

After centuries of stagnation, the transformation of the Asia—Pacific region into dynamic economies in the 1950s and 1960s was triggered by the rapid growth of the Western industrialized economies whose GDP grew at rates of about 5 percent. Their markets absorbed large quantities of textiles, garments, toys, and other labor-intensive exports from Japan and Hong Kong in the 1950s, and when wages and prices in these countries rose in the 1960s, the Western countries shifted their purchases of labor-intensive products to Taiwan and Korea, whose growth began to accelerate from the mid-1960s. In the 1960s Western buyers and engineers from the large department stores came to Hong Kong to teach the firms to make radios, TVs, and other durables, with most of the parts and components imported from Japan. Growth rates of aggregate GDP rose to 9 percent levels in Japan and Hong Kong in the 1950s

and 1960s, and in Taiwan and South Korea from the mid-1960s. When Western growth slowed down after 1973 to 2 percent levels and in Japan to 4 percent, sustained high growth of the NIEs (Hong Kong, Taiwan, Singapore, and South Korea) helped to maintain the dynamism of the Asia—Pacific economies in the 1970s and 1980s.²

The NIEs have been growing at high rates (of about 8 to 9 percent) over the past two and a half decades as they were able to readily import technologies from Japan and the West and apply them to their rapidly expanding industries. But soon, probably by the mid-1990s, the NIEs are likely to slow down to moderate levels of growth (of about 5 percent), as Japan did after two or three decades of high growth. The GDP growth rates have fallen to 5 percent during 1989—1991 in Hong Kong, 6.5 percent in Taiwan, 7.5 percent in South Korea, and 8 percent in Singapore. Structural patterns are approaching those of Japan in the mid-1990s. With the maturing of industrialization, the shift to the services has begun in the NIEs. In 1991, the workforce in the service sector exceeded the workforce in manufacturing in all the NIEs.³

Most significantly the NIEs and Japan have begun to generate savings in excess of domestic investment. In Taiwan by the late 1980s, the excess amounted to 43 percent of gross savings, 18 percent in Hong Kong, 12 percent in South Korea, and 11 percent in Singapore. When total savings exceeds domestic savings, they must be sent abroad, either as financial investment and grants or direct foreign investment. And when sent abroad, the excess savings contribute much more to the growth of the GDP of receiving countries than of the home countries.⁴

The major industries in the NIEs are approaching the technology frontier, and they are able increasingly to export machinery. Taiwan and South Korea with a large machinery sector have become net exporters of machinery like Japan.

The NIEs have completed the demographic transition with fertility levels falling below 2.0, and the labor force growing slowly. Unemployment rates have declined to 2 percent or less, and wages are rising rapidly.⁵

In the late 1980s, direct foreign investments from Japan and the NIEs had been flowing into Thailand, Malaysia, and Indonesia in large quantities. And in the early 1990s, Thailand and Malaysia have become fully employed, and Indonesia has begun to witness the rise of prices as it approaches full employment. As wages and costs begin to rise, excess savings in Japan and the NIEs may begin to look for places to go to, with the choice in South Asia or Northeast Asia.

All this means that opportunities are emerging for Northeast Asia to become the next dynamic region in the Asian—Pacific region. Unlike its chief rival, South Asia, it is rich in natural resources, possesses a better educated workforce, and is located closer to the source of dynamism, East Asia. But like South Asia with institutions of obsolete religions and caste, it is saddled with the inhibiting institutions of Communism. (Institutions are defined to be patterned or customary ways of doing and thinking, comprising more than formal organizations.)

If underlying economic growth is the interplay of technology and institutions, as Kuznets noted, institutions are more strategic than technology; the latter can be readily imported into countries which are not yet at the technological frontier. Then attention must be paid to institutions of central planning, "iron rice bowls," nationalized trading, banking, industrialization, and collectivized agriculture. Fortunately

China, the Soviet Union, Mongolia, and even North Korea have taken the first steps toward dismantling Communist institutions. But more must be done. By successfully transforming institutions, the Northeast can become attractive for experienced entrepreneurs with excess savings and advanced technologies from Japan, South Korea and other NIEs. Indeed the crisis caused by the collapse of the Soviet Union, whose trade and aid had previously sustained other Socialist Northeastern economies, may turn out to be a blessing in disguise.

Despite the wealth of natural resources, per capita dollar incomes are low, with US \$522 in Mongolia, US \$300 in China, and US \$987 in North Korea, compared to US \$5,500 in South Korea, US \$7,300 in Taiwan, US \$11,000 in Singapore, US \$12,000 in Hong Kong, US \$2,300 in Malaysia, US \$1,400 in Thailand, and US \$25,000 in Japan.⁶ Even if we take these figures of per capita income at their face value, they are indicative of relatively poor performance over the postwar era. For the market economies during the four decades from the 1950s, South Korea grew at 7.5 percent per year, Taiwan at 8.5 percent, Hong Kong at 9 percent, Singapore at 8 percent, Malaysia at 6 percent, Thailand at 7 percent, and Japan at 7 percent. Data, available for China only from 1952, suggest growth of about 6 percent GDP. This may overstate growth because the low prices fixed for the output of the slow-growing agricultural sector up to the 1980s tend to understate agriculture's weight in the total. That is, if the higher 1980 prices are used to weigh the agricultural sector, the growth rates may fall to levels below 5 percent. The Chinese economy performed well in the 1980s after a series of institutional reforms which are noted below.⁷

Data from the 1950s for North Korea, USSR, and Mongolia are not available. The previously reported official data for all three countries have been questioned and discarded by the new regimes in the USSR and Mongolia. The most unreliable may be those of North Korea.⁸ Perhaps the earliest figures, e.g., in the 1950s, may not be as unreliable as the later ones. Planned economies are able to generate high growth rates in the early period as they are constructing new factories and buildings and equipping them with new machines. But in later periods, growth slows down and stagnates because of inefficiencies and the difficulties of operating at full capacity. The poor quality of goods produced over the decades, especially capital goods such as machines, contributes to lower growth in the later period, while the poor quality of consumer goods and services results in lower incentives to work and decline in consumer satisfaction.

Underlying the slow growth of per capita income is the slow growth of productivity per worker. While in Japan and South Korea productivity per worker grew at 4 percent and 8 percent, respectively, between 1986—1990, the growth was -2 percent in North Korea and about 2 percent in the Russian Far East. Although official figures indicate 7.8 percent for China and 5.5 percent for Mongolia, these are probably overstatements, as noted above.⁹

But more important in the poor growth performance was the strategy of development adopted from the 1950s. Following Soviet practices and believing in the growth theory of Feldman, North Korea and China opted for a strategy of heavy industrialization, rejecting the need for focussing on agriculture and small industries in the initial stages of development.¹⁰ Heavy industries are costly to establish and

difficult to operate efficiently. In poor countries such as China and North Korea, the swift implementation of a heavy industry strategy will necessitate a drastic shift of resources of men and materials from other sectors of the economy: small industry, services, and especially the predominant sector, agriculture. The implementation of this strategy calls for the creation of an entire set of new institutions, the central one being a system of central and local planning with extensive powers to command resources from the other sectors. But it was not easy to persuade the large class of subsistence peasants to give up a large share of their products to feed the workers drafted into the heavy industries. The only solution was the collectivization of agriculture. Foreign trading and banking were taken over to conserve foreign exchange and mobilize savings for the financing of heavy industrialization. All these institutions became an integral part of socialism and met the demands of its anti-capitalistic ideology.

It is encouraging to note that all of the socialist countries have begun to realize the need to transform their institutions. And this is true even in the most orthodox Communist regime, North Korea, which has established free trade zones in its three northern cities (Rajin, Sonbong, and Chongjin), and it is reported that foreign companies will be able to set up wholly owned companies.

RESOURCE ALLOCATION: PLANNING VS. THE MARKET

We examine the institutions of the Northeast Asian countries, comparing the socialist institutions with the capitalist institutions of South Korea and Japan in an effort to understand their role in promoting or inhibiting growth. Taken up first are the planning mechanism and the market, then collectivized and family agriculture, nationalized industries, and nationalized services, and income distribution. The paper concludes with a plea for privatization.

The misallocation and waste of resources have been extensive in planned economies. It is now recognized that it is impossible for planners to foresee all the needs of the economy and to specify the vast variety of outputs and inputs. The data needed far exceeds the capability of statistical agencies to compile the information while the ability of the planners to detect and respond to the frequent changes in demand and supply conditions is limited. In the Soviet Union, planners have had to cope with more than 20 million types, varieties, and sizes of products turned out by 45,000 industrial, 60,000 agricultural, and 33,000 construction enterprises. To deal with the complexities, over 100 planning organizations had to be established just on the national level.¹¹

After experiencing difficulties, various changes in planning procedures were made throughout the postwar period; each time the role of the central planners and ministries was reduced with some of the functions delegated to provincial and county organizations. The changes were most extensive in China where often planning activities by collectives and individuals were encouraged, replacing direct controls by planners with indirect guidance. Changes were also made in Mongolia and the Soviet Union, but there was widespread disappointment as unemployment mounted and

prices rose as corruption, hoarding, monopolizing, rigging, and cheating became rampant. Disillusionment with democratic institutions has now set in.¹²

It takes time to develop the market as an efficient mechanism for allocating resources. For the market to function properly, the forces participating in market operations must be developed. And it took some time in the West to develop and nurture these market forces.¹³ For countries emerging out of decades of nationalized industries under the command of planners, the numerous entrepreneurs (buyers and sellers) able to compete and bargain rationally under a system of market rules and organization do not exist. It is reported that, in Russia, laws and regulations are changing too frequently and that there are uncertainties about who the owners are of various resources, and so on.

It may be necessary to shift to a type of planning under which Japan, South Korea, Taiwan, and other market economies thrived for the most part of the postwar era. In this type of planning (often designated as indicative planning), most activities are undertaken on a private basis with only a small part (such as public utilities) operated on a nationalized basis. The government indicates targets, guidelines, and goals for the private sector to take into account and toward which the government intends to concentrate fiscal, financial, industrial, and foreign trade policies. Important in the guidelines is the strategy of development outlining the sectors of the economy to be targeted. For example, in Japan the plans aimed to develop agriculture in the 1950s to attain rice self-sufficiency and labor-intensive industries (such as textiles) for employment creation and export; to reconstruct and modernize electric power, steel and other basic industries in the 1960s; and to promote the development of the automobile, electronic, and other technologically sophisticated industries in the 1970s.

This type of planning is more flexible and less demanding of the private sector and the mistakes made are less damaging. The Japanese automobile industry, not considered by the planners to have comparative advantage, did not get any support in the 1960s but was permitted to exist and develop on its own and eventually grew to be exportable. Under command planning it would be permitted to exist.

Although China, Mongolia, and Russia have been decentralizing their planning and delegating more powers to local authorities to establish targets and quotas, this may not be enough. They should begin to shift to overall indicative planning and allow state enterprises and collectives to set up their own production goals in accordance with the indicative plans instead of commanding them to meet the goals of the central plans. They should adopt a strategy of transitional development whereby employment will be generated through the expansion of agriculture and labor-intensive industrialization for jobs and export. The industries to be promoted may be food and woodprocessing, textiles, garments, and so on. Privatization should be speeded up to improve the working of the markets. The emerging markets should not be completely free but should be regulated at first to prevent monopolization, cheating, hoarding, and corruption.

As sectors are privatized, the surplus workers may lose their jobs, but fortunately for the Northeast, the extensive infrastructure needed for the development of the region should be a major source of jobs. With the end of the Cold War, military

expenditures should be drastically reduced, and funds should be transferred for *infrastructure construction which has been neglected in rural areas and small towns.*

COLLECTIVIZED AGRICULTURE

Unlike the private farms of South Korea and Japan, the agriculture of the socialist countries is dominated by collective farms owned and managed by the state, ministries, and cooperatives. The latter determine the crops to be produced and the time to be spent on the collective farms by farm families are who contracted to deliver the crops to the governments and collectives. Farmers are allowed to keep small private plots from which subsistence needs are met and the excess sold in the open markets.

The least successful were the Soviet farms, all of whose output had to be sold to the state at fixed prices. The most successful were Chinese collectives where, after the reforms of the 1980s, farmers were permitted to decide on the crops to be grown and sell any excess on the open market. Also farm families were allowed to get together to establish small factories and other businesses which could buy raw materials, borrow funds, and recruit skilled workers. These, together with the sale from private plots, enabled rural markets to flourish. China's agriculture did well in the 1980s, growing at an unprecedented rate of 6.1 percent compared to 2.8 percent in previous decades.

The main problems faced were inefficiencies in the management and operation by the state, collectives, and cooperatives, compared to the small private plots which were able to outproduce the former. Even in China, the growth of agriculture slowed down, falling to 4 percent during the years 1988—1992. This may be due to the beneficial effects of marketization wearing off. In Mongolia, yields on collectives have been reported to be stagnant for some time.

The family contract responsibility system was a more productive form of collectivized agriculture than the previous system in which work teams of unrelated members were paid by the time put into farm work. The incentive to work improved when earnings were to be received by closely related members who pooled their earnings and consumed together, in contrast to unrelated members who did not. Nevertheless, it was inferior to a system of private farming where farmers marketed the total output and kept the entire proceeds. Nor did the system promote investment in farm improvement schemes such as irrigation, drainage, soil improvement, water conservation, and reclamation. When urged by the state to put in more improvements, the farmers replied that they must be paid for the work as the land was not theirs. Under private ownership of farm lands, farmers in Japan, Taiwan, and South Korea saved large amounts of money to invest in equipment and infrastructure.

It should be pointed out that the agriculture of Northeast Asia is quite different from that of most of China, North Korea, and other monsoon areas. Manchuria, Mongolia, northern parts of North Korea, and the Russian Far East lie beyond the reach of the Southwest monsoon rains which water the rice paddies of East and Southeast Asia. Rainfall is about one-half or less than in South Korea and Japan and is insufficient for paddy rice cultivation and other cereal crops such as wheat, barley,

and millet must be grown.¹⁴ This is so even for Northeast China where 90 percent of the farmland is planted in dry-field crops.¹⁵ The yields are higher for rice than for other cereal crops, and together with the longer cold season (which prohibits multiple-cropping), the food per unit of land produced is much greater in South Korea and Japan.¹⁶

Hence, the non-monsoon regions of the Northeast can only support a much smaller population than the monsoon regions. Less than 50 persons per square kilometer live in the Russian Far East and in the northern parts of North Korea. And even in Manchuria, population densities average only about one-half that of South Korea and Japan.¹⁷ Nevertheless, because of the longer and more severe winters, idleness in the winter months is more extensive than in the monsoon regions where multiple cropping and off-farm jobs provide work in the winter months.¹⁸ But lower densities imply that in the future the Northeast can support a larger population as long as it can import food with the foreign exchange earned from the export of natural resources. Furthermore, idleness on the farms can be reduced with the building of roads and other infrastructure which will enable commuting to nearby industries for off-farm employment in the winter months, as in South Korea and Japan.

The system of landlord-tenant farming which previously dominated the agriculture of Japan, South Korea, and Taiwan was swept aside by the comprehensive land reform in the first decade after World War II. Incentives to produce heightened as peasants no longer had to turn over half of the crops to the landlords as in the prewar system. Peasants were encouraged to organize their own cooperatives and associations which pressured governments to construct irrigation and drainage for multiple-cropping and provide loans to mechanize their operations. When industries moved to the rural towns, members of peasant families were able to commute to off-farm work during the slack season. Rising yields per hectare using higher-yielding varieties, together with multiple crops and off-farm jobs, enabled peasant families to improve productivity and earn incomes comparable to those of worker's families in the urban sector.¹⁹ Rice self-sufficiency was attained in Japan and Taiwan early in the postwar era, and later in South Korea.

In the 1990s, the system of small family farming is becoming obsolete, especially in Japan as rural youth leave for better-paying urban jobs and their parents become too old to do much farming. A shift to larger-scale private farming using larger, more efficient mechanical and other technologies is taking place, first in Japan where the labor shortage is most acute, followed by Taiwan and then South Korea. This suggests that, instead of going through the route of small family farms, the socialist countries can privatize and marketize large state and collective farms and, as labor shortages occur, improve productivity by more efficient mechanization.

NATIONALIZED INDUSTRIALIZATION AND THE "IRON RICE BOWL"

All four of the Northeast Asian socialist countries concentrated on industrialization, especially heavy industries, from the early decades of the postwar era. This emphasis on industrialization produced an economic structure heavily weighted in

industries, as the figures in Table 1.1 show.

Notice that the Russian Far East with much lower per capita income has a much higher share of industrial labor force than in Japan, similarly with South Korea and Taiwan over North Korea despite the fact that North Korea's 39 percent is only for manufacturing. Yet Malaysia with more than double the per capita income of Mongolia and China has a lower industrial labor force share than Mongolia and about the same as China—all this despite the capital-intensive industries in the socialist countries and despite the larger share of manufacturing exports in the capitalistic countries.

Table 1.1 The share of total labor force, 1991 (%)

Socialist countries	In agriculture	In industry	In services	Total
Russian Far East	8	51	41	100
North Korea	43	39	18	100
Mongolia	19	28	43	100
China	60	25	15	100
Capitalist countries				
Japan	7	36	57	100
South Korea	17	34	49	100
Taiwan	13	40	47	100
Malaysia	28	26	46	100

Notes: Agriculture includes fishing, forestry, and animal husbandry; industry includes manufacturing, mining, construction, and public utilities; services include transportation, communications, commerce and public, and personal services. North Korea's industry includes only manufacturing.

Sources: *Asia 1984 Yearbook*, *Far Eastern Economic Review*, Hong Kong, 1992. Russian Far East data from tables supplied by Vladimir Ivanov.

These nationalized enterprises were inherently inefficient. They were basically monopolies without effective competition from other enterprises and consumers, whether domestic or foreign. There was no effective mechanism to promote innovation and reduce costs; nor were there adequate incentives for workers, technicians, and managers to improve productivity. Because of the "iron rice bowl," they could not be fired for inefficiencies, so the factories became overstaffed with redundant workers. Whether they were profitable or not, the enterprises continued to operate since losses were made up by subsidies from government budgets. There was no need to measure up to competitors, even if they existed, as there was no threat of bankruptcy.

The choice of heavy industries in the early stage of development was unfortunate because they were highly complex industries, requiring managerial and technical expertise far beyond the capacity of underdeveloped countries to supply, particularly

when such countries undertook to establish at once the entire range of capital-intensive industries, ranging from iron and steel, aluminum, cement, heavy machinery, automobiles, heavy chemicals, to paper and pulp and so on. In China between 1953—1957, 156 major constructions of heavy industries were launched. But because of the lack of design capabilities, improvements were slow and the technologies soon became obsolete. Together with poor quality and input shortages due to inadequate transport facilities, regional imbalances, and planning shortcomings, most of the heavy industries were rarely operated on a full capacity basis.²⁰ Since the machinery industry was included in the heavy industry complex, downstream industries were compelled to purchase the machines produced. The latter were usually of poor quality and of outdated design, so that high costs were imposed on the downstream industries which made it difficult to export.²¹

Japanese industrialization started early in the present century, and a great deal of experience and expertise was accumulated by the start of World War II. Despite the destruction during the war, the labor-intensive industries recovered quickly and were able to export to the West, and, as noted above, heavy industries were reconstructed and modernized in the 1960s and 1970s. In the success of postwar Japanese industrialization, professional managers, who replaced the old *Zaibatsu* families in the control of major enterprises, played a major role. They were able to establish a unique system of labor—management relations in which the labor unions in consultation with workers participated in consensus decisionmaking, skills were developed through extensive in-service and off-service training, incentives were raised through profit-sharing bonuses over and above seniority wage payments, and new technologies from abroad were quickly introduced.

In addition to the above institutions an old institution originating in the prewar decades was brought in which was not unlike the “iron rice bowl.” This was the system of lifetime employment which committed not only the firm to provide work until retirement but also obligated the workers to the firm permanently. The system worked in Japan because employers could afford to invest in extensive training since workers could not leave for other jobs after the training. The firm could also invest in new technologies, especially laborsaving machines, without objection from the workers who did not fear the loss of their jobs and were inclined to favor the introduction of new technologies since profits would increase and more bonuses could be paid.

Unlike the socialist countries, small and medium industries in Japan were not neglected, and policies to improve their management, technology, and finances were implemented, eventually evolving into efficient subcontractors of parts and components to the larger industries.²²

South Korean industrialization started in the 1950s with labor-intensive industries which were able to export from the mid-1960s. With the foreign exchange earned (and loans from the Middle East), heavy and chemical industries were developed in the 1970s. Technology and expertise were brought in from Japan, and they began to export as these industries in Japan lost comparative advantage in the 1980s. The government played a major role in supporting and pushing hard the big industries to improve efficiency and to export. Nevertheless, the contribution of the labor-

intensive industries in earning foreign exchange and as subcontractors in Korean industrialization should not be overlooked.

Recently, with the discovery of the "socialist market economy," government enterprises in China were granted more autonomy to use the market and be responsible for profits and losses. Eighteen deficit enterprises in 1991 and 66 in the first half of 1992 were closed down (of which 9 were heavy industries in Liaoning).²³ It was reported that one-third of state-owned enterprises were in deficit and another one-third had huge "hidden" losses.²⁴ Instead of "bailing out" such firms, they were to be pushed out to fend for themselves in the marketplace.²⁵ Despite the attention paid to heavy industries, the most rapidly growing sector from the 1980s was not the big state enterprises but small township enterprises in which rural workers found jobs, especially during slack seasons. This was a type of off-farm employment which played a major role in Japan and Taiwan throughout the postwar decades.²⁶

NATIONALIZED SERVICES

The labor shares of the service sectors of Japan, Taiwan, South Korea, and Malaysia are considerably larger than in the socialist Northeastern countries, especially in North Korea with only 18 percent and China with 15 percent, as Table 1.1 shows. There is a tendency in socialist planning to neglect the service sector on the grounds that it is largely an "unproductive" sector. But this view appears to be changing, and in China plans are underway to raise the value added in the service sector from 27 percent to 35 percent of GNP,²⁷ and there are similar plans in Mongolia.²⁸ The service sector becomes strategically important with the maturing of industrialization, and demand elasticities rise with the increase in per capita income.²⁹ In the United States and other leading capitalist countries of the West, more than two-thirds of the labor force are working in the services with nearly 60 percent in Japan. Even in the NIEs, it is the fastest-growing sector with a labor force already larger than in manufacturing.³⁰

In the public services, a well-trained bureaucracy in the ministries of industry and trade played an important role in the development of the large businesses of Japan and South Korea.³¹ The trading companies (*sogo shosha*), together with the small industry ministries which found markets, and improved management and technologies of small businesses. A large part of the costs of food, clothing, furnishings, and the like is due to distribution, and without large-scale department stores and supermarkets, these costs would be high. Personal services, such as health care, education, recreation, and personal care (e.g., barber shops) become necessities in the modern urban civilization.

Unlike industries and agriculture, the production of services generates only a limited amount of scale economies as they cannot be mechanized extensively. Nor can they be standardized as much as commodities are. So far, robots can be programmed to do regular, uniform activities, but attempts to construct intelligent robots have not been successful. Under these circumstances, it is difficult to see why restaurants, hotels, department stores, and food and other retail stores should be nationalized, since the modest capital needed for them can be supplied by individuals,

unlike heavy industries.

Anyone visiting cities like Beijing can attest to the poor services of government-operated service enterprises. The problem is partially due to low pay and understaffing since the services are given low priorities in planning, but it may also be the lack of incentives for government-employed cooks to prepare good meals, waiters to be polite, household workers to clean the hotel rooms well, store clerks to maximize sales, and so on, especially as they cannot be fired under the "iron rice bowl" permanent tenure.³²

In China, recent changes have made it possible for peasants to sell part of their output in rural markets and for urban families to open food stalls and craft shops. But it is reported that they run into difficulties because state-owned grain shops have monopolized the trade and have sold at subsidized prices. It is reported that hotels will be given the power to set prices for rooms, food and other goods, including wages for their employees, but if the labor unions continue to control the work schedules of clerks, accountants, maintenance workers, and other employees, rather than the hotel managers, it is hard to see how efficiently the government hotels can be run.³³ In Japan and South Korea, as elsewhere in the capitalist world, commercial and personal services are privately owned and operated and are highly competitive, although prices of some services are regulated by the government.

It is evident that even more than in industries, the key to the service sector is the privatization of the state enterprises, perhaps in the beginning as joint ventures. They should be independently operated with the power to set prices.³⁴

THE DISTRIBUTION OF FAMILY INCOMES

One area where the socialist countries perform better is in the distribution of family incomes. The inequality index, measured by the Gini, of China's distribution was 0.30, which was lower than that of Japan's 0.35 and South Korea's 0.46 and, indeed, lower than those of all other Asian countries (although about the same as in Taiwan).³⁵ Data for Mongolia, North Korea, and the Soviet Union are not available, but it can be surmised that their distributions are probably more like that of China because under socialism the highly variable property and entrepreneurial incomes are minimal, while the differences between salaried and wage incomes and variations in wage rates are much smaller than in capitalistic economies. Recently, Ginis for the Soviet Union have been published, and they show the level to be very low—0.25 in 1980, 0.26 in 1985, and 0.27 in 1988 (which is also the level of Gini in Hungary).³⁶

Indeed, economists from the socialist countries complain that, even though a lower income distribution is desirable from the point of view of welfare, the evenness of wages and salaries is a deterrent to increased productivity in socialist countries where there are insufficient work incentives.³⁷ Lecturing in Beijing a few years ago at the Social Science Academy, I was told that intellectuals receive lower incomes than laborers because intellectual workers are not paid for overtime work. It is reported that, in the 1980s, "the average health providers, educators and others engaged in cultural pursuits were below the national average."³⁸

CONCLUDING NOTES: THE NEED FOR PRIVATIZATION

Chinese economists have advanced the concept of a "socialist market system," similar to a concept Oscar Lange propounded several decades ago. This system may be necessary as a temporary system for the transitional period, but questions emerge when it is considered as a system for the long run. How efficient is the socialist market system in comparison with the privatized, capitalist market system? We have seen above that markets do not work well when government enterprises are too powerful and overwhelm private enterprises, as in the monopolized grain markets; also noted above was the tendency of farmers to resist building irrigation, drainage, and soil improvements because the farms did not belong to them. Nor were they interested in careful maintenance of machines and equipment which belonged to the state.³⁹

Privatization has recently been actively pursued in the capitalist world, with the advanced economies privatizing even public utilities such as telephone and telegraph, postal systems, and railways. In Japan, the Nippon Telegraph and Telephone, the Japan National Railways, and Japan Tobacco and Salt Corporations were privatized in the latter half of the 1980s on the basis that private operations would be more efficient and that labor relations would be more harmonious as the unions would be less demanding of higher wages if company deficits could not be covered by the state budget.⁴⁰ Italy recently passed a privatization bill because many political appointees were being forced upon the staffs of public corporations, in one case as many as 40 executives. Turkey also had to take action as public corporations became overstaffed with politicians. In Thailand, the military rulers made their generals corporate heads.

In contrast to state entities, private enterprises must make profit maximization the central concern of their operation if they are to survive, and this compels them to maximize efficiency. But since state enterprises can count on governments to bail them out, the urge to make profits is likely to be weaker. They are more likely to give in to the demands for higher wages and shorter hours while the capitalists can grant wage increases only on condition that productivity improves. Under capitalism, wages are increased for efficient workers and not for poor workers, with the result of improved incentives for workers to perform better, while greater profits enable the private firms to buy more and better equipment, thereby improving future productivity. In general, because subsidies are not available, private firms must be highly cost-sensitive.⁴¹

Without the countervailing pressure of private owners of enterprises, managers "are unable to resist the demand for wage increases," and this forces planning authorities to step in to regulate wages to keep them from rising too high. This, together with the egalitarian philosophy of socialism, keeps wages evenly distributed since "there was no effective mechanism to allow wage differentials to be developed on the basis of performance," according to Erdos.⁴² The private entrepreneur is more demanding of his workers than the state, and this promotes productivity. It is understandable that the workers tend to oppose denationalization.

In summary, it may be necessary to convert socialist market systems into private market systems, if productivity is to rise in the future. But this may not be an easy task for a socialist society because not only the management of state enterprises but also

the working class will oppose such a step, and since it means the conversion of socialism into capitalism, the "hardliners" in the political system will not like it. It may be interesting to try marketization with privatization in the Tumen free trade zone.

NOTES

1. Northeast Asia countries comprise South Korea, Japan, North Korea, Russia, Mongolia, and China.
2. For details, cf. my *Economic Growth in Monsoon Asia*, Tokyo University Press, 1987; and also my *Strategic Processes in Monsoon Asia's Economic Development*, forthcoming, Johns Hopkins University Press, early 1993. Cf. Angus Maddison, "Growth and Slowdown in the Advanced Capitalist Countries," *Journal of Economic Literature*, Vol. XXV, June 1987, for other data cited.
3. Cf. data in *Asia Yearbook 1992*, published by the *Far Eastern Economic Review*, Hong Kong. Average per capita incomes in U.S. dollars of the NIEs are also about those of Japan in the mid-1970s when Japan's GDP growth rates fell to moderate levels.
4. For a more detailed discussion of excess savings, see my forthcoming volume on *Strategic Processes*. Direct foreign investments from Singapore are going to Batam in Indonesia, from Hong Kong to Canton, and from Taiwan to Fujian. Savings tend to be excessive when domestic capital formation slows down with profit rates tapering off and with the maturation of industrialization.
5. Cf. data in ADB's *Key Indicators*, 1990, on exports, labor force, and wages. Unemployment figures from *Strategic Processes*.
6. Per capita U.S. dollar income in the Russian Far East is about US \$6,000 when rubles are converted to U.S. dollars by the official exchange rate. But the latter overstates the value of the ruble considerably, so per capita income may be substantially lower. Cf. Area Handbook Series, *Soviet Union, a Country Study*. Our paper will depend heavily on the Area Handbook Series which is published for all six countries of this study. The Series covers all countries of Asia, and recent volumes are published by the Federal Research Division, Library of Congress, Washington, D.C. Other sources of data on per capita income from *Asia Yearbook 1992*, *Far Eastern Economic Review*, 1992.
7. GDP data for 1965—1980 from *World Development Report 1992*, and for the previous years, estimated on the basis of national income index from *China Statistical Yearbook, 1992*. Other data from my books cited below.
8. For Mongolia, cf. Area Handbook Series, *Mongolia, a Country Study*: "In late 1989, the new openness about economic conditions occasioned an admission by a deputy minister of foreign relations and supply that many official statistics had been falsified during Tsedenbal years to bolster claims of economic progress", p.xxxv. And Nicholas Eberstadt reports that the economic data for North Korea are "rubber statistics," except for population data. On Soviet statistics, cf. Area Handbook Series, *Soviet Union, a Country Study*, 1991, pp. 451—452.
9. The relation between per capita income and per worker productivity can be expressed in the identity: $o/tp = wp/tp \times o/wp$ where wp (working population) cancels out on the right hand side, leaving o (output) over tp (total population) or per capita income. This is a slight variation of Kuznets' formulation discussed by Robert Fogel in his Afterword to Kuznets' *Economic Development, the Family, and Income Distribution*, Harvard University Press, 1991, p. 427. The growth of productivity is obtained by adjusting growth rate of labor force from the growth rate of real GDP. The former was computed from *Asia Yearbook 1992*, *Far Eastern Economic Review*, and the latter from Won Bae Kim, "Population and Labor in Northeast Asia," paper for this Conference.
10. Feldman argued that it was necessary to develop the heavy industries first, and later machines and materials for the mechanization of smaller industries and agriculture could be easily produced. For detailed discussion of the difficulties encountered by China, cf. my *Economic Growth in Monsoon Asia*, Chap. 9.

11. Cf. Area Handbook Series, *Soviet Union, a Country Study*, Washington, D.C.: Federal Research Division, Library of Congress, ed., R.E. Zickel, 1991, p. 453.
12. Cf. for Russia, *International Herald Tribune*, 3 August 1992, and for Mongolia, *The New York Times International*, 8 July 1992. On China, cf. *Japan Times*, Tokyo, 6 August 1992.
13. Recall the "robber barons" of the 19th century.
14. Cf. data in the Area Handbook Series for the respective countries.
15. *China Statistical Yearbook, 1990*, State Statistical Bureau, Beijing, 1991, p. 315.
16. Cf. V.D. Wickizer and M.K. Bennett, *The Rice Economy of Monsoon Asia*, Stanford University Press, 1941.
17. Area Handbook Series for various countries.
18. Cf. *Strategic Processes in Monsoon Asia's Economic Development*.
19. For data, cf. *ibid.*, and *Economic Growth in Monsoon Asia*, Chapters 4 and 5.
20. Cf. details in *Economic Growth in Monsoon Asia*, Chap. 9. The iron and steel industry in the socialist countries, even in the mid-1980s was using obsolete methods such as open-hearth furnaces and ingot castings at a time when the Japanese industry was shifting to continuous casting which required no more than 6 minutes for slabs to be hot-rolled into flat plates and the use of energy of less than 50 percent of the old methods.
21. E.g., Chinese textile industries had to junk most of the machines bought in China and demanded the right to import machines from abroad in order to export. Cf. *China Daily*, 20 July 1992.
22. Cf. details from *Economic Growth in Monsoon Asia*, Chap. 4.
23. *Japan Times*, Tokyo, 16 August 1992.
24. *China Daily*, Beijing, 16 July 1992.
25. *Japan Times*, Tokyo, 10 August 1992.
26. Cf. *Strategic Processes*, Chap. 7.
27. *China Daily*, Beijing, 20 July 1992.
28. Cf. Area Handbook Series for Mongolia.
29. During the infancy of industrialization, services may be of small value with most services catering to the whims of the leisure class, as during the time of the Physiocrats in France.
30. Data from my unpublished paper, "Long-Term Prospects in the Asia/Pacific Region and Japan's Role," presented at a Tokyo seminar, July 1992. For the Western countries, data based on Angus Maddison, "Growth and Slowdown in Advanced Capitalist Economies."
31. Cf. Area Handbook Series for Japan, pp. 204—207, and the Area Handbook Series for South Korea, pp. 115—122, on the role of government.
32. Food cooked by government cooks in Chinese restaurants falls below the standards of Hong Kong, Taipei, and Singapore.
33. Cf. *China Daily*, Beijing, 16, 18, 20 July 1992.
34. In order to reduce losses, state-owned enterprises have been leased out to private services. Cf. *ibid.*
35. Data from my paper "Kuznets' Curve and Asia's Income Distribution Trends," *Hitotsubashi Economic Journal*, June 1992.
36. Cf. T. Mizoguchi, et al., eds., *Making Economies More Efficient and More Equitable: Factors Determining Income Distribution*. Institute of Economic Research, Hitotsubashi, 1991. The higher income inequality in Japan is offset by systems of public health, pension, and social security, much more comprehensive than in the socialist countries, although this cannot be said about South Korea.
37. Although Taiwan's Gini is about the same as China's, it contains a great deal of inter-wage variations with very little inter-regional wage variations compared to China's, which contained a great deal of regional variations and very few inter-wage variations.

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38. From Tibor Erdos, "Income Distribution and Economic Efficiency in Hungary," in T. Mizoguchi, et al., cited above.
 39. State ownership of the means of production was thought by Marxists to be conducive to efficiency because the workers would believe that they were working for themselves and not for the capitalists "but in actuality no single individual considers himself or herself to be the owner." Erdos, *ibid.*, p. 223.
 40. Cf. *Area Handbook Series on Japan*, p. 213.
 41. Erdos, "Income Distribution," p. 225, notes that in Hungary, 70 to 30 percent of the profits of state enterprises comprise subsidies. Despite the threat to cast off deficit-ridden firms, "bankruptcies take place infrequently, once or twice a decade."
 42. *Ibid.*, pp. 224 and 227.