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Ayele, G. M.

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Ayele, G. M.

Assistant Professor, College of Business and Economics, Bahir Dar University, Bahir Dar, Ethiopia

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ABSTRACT

This paper examined the Korean experience of outward looking development strategy in the 1960s to 1980s, and forward some policy lessons to Ethiopia. The analysis generally showed that the Korean successful economic growth strategy can be explained by performance-based incentives for export industries, intensive human capital development, high intervention with huge support for value added private enterprises, committed leadership and outward oriented industrialization with constant policy shifting and upgrading. While the Ethiopian public sector-led growth strategy is inefficient in transforming the economy so that the country's global competitiveness remains at stake due to unsatisfactory export diversification and inefficient production of the traditional export sectors.

Key words: *Outward-looking strategy, export promotion, industrialization, sustainable growth, South Korea, Ethiopia*

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INTRODUCTION

Economic development has become more complex and challenging in all dimensions of government policy, either free market or interventionist. Every nation may adopt its own strategy for sustainable development, given the distinct social, cultural, political, and religious grounds. Hence, a strategy for sustainable economic development would not be mechanically imposed rather it must grow out of the special conditions and the dynamic route of each nation's growth opportunities and barriers including political stability, available resources, strategic location, level of development, and global factors. As (James, Naya, & Meier, 1989) stated, the remarkable economic growth and industrialization of the East Asian countries, Korea in particular, in the 1960s and 1970s was achieved through export-oriented development strategy. The impressive success in those countries challenged the old orthodoxies of export pessimism and import substitution based industrialization though the external shocks of early 1970s questioned the applicability of export-led growth strategies to Least Developed Countries (LDCs).

Korea started industrialization with an import-substitution policy during the reconstruction period in 1950s, like many developing countries did in the post-war period. However, with the implementation of the first five-year plan in 1962, Korea shifted its strategy towards export promotion that was supported by successive major policy reforms in the 1960s (Kim K. S., 1974). Since the adoption of export-led industrialization policy, Korea has shown a remarkable and sustainable economic growth record. Many studies such as (Kim, Shim, & Kim, 1995), (Dornbusch & Park, 1987), (Kim Y.-H. , 1994), and (Grinberg, 2014) stated that the primary reasons for such remarkable economic growth include human capital accumulation, export-oriented development strategy, and close cooperation between the government and entrepreneurs. Besides, the Park regime was highly committed to economic development, and introduced comprehensive policies of trade reforms and export promotion including direct export subsidies, tax exemptions, and preferential export loans. The government also highly encouraged foreign capital inflows to support diminutive domestic savings.

Consequently, according to (International Trade Database, 2019), Korea become the sixth largest merchandise exporter (3.14% of world exports) and the 12th biggest economy with a per capital income of US$ 31,346 in 2018 (World Economic Outlook Database, April 2019). The state-guided outward-looking strategy worked well in overcoming fundamental disequilibrium and poverty alleviation, and transformed the country from hopeless and desolate economy to a well industrialized nation. Hence, Korea's development strategies implemented during the period of state-led export-driven industrialization (1962–80), in which rapid-industrialization was achieved through extensive trade and industry policies, stands as a model for low income countries (Kim K. S., 1991), Ethiopia in particular.

Ethiopia implemented the first and second five-year development strategies, named Growth and Transformation Plan I and II, in 2010 and 2015, respectively. The plans aimed at achieving sustainable, broad-based and equitable economic growth. The country pursued structural transformation through massive investment projects in infrastructures such as roads, hydro-electric generating plants, and sugar factories despite the questionable efficiency. Indeed, Ethiopia has shown a remarkable real economic growth of about 10 percent on average for more than a decade. Such impressive growth was induced through a mix of agricultural modernization, strong global commodity demand (mainly before the global financial crisis), and government-led development investments (WB, 2012). However, the country remained poverty-stricken, aid dependent and an exporter of few agricultural commodities. Despite the expansion of service and agricultural sectors, export diversification and

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industrialization remain the major challenge, and the country's export sector has been highly concentrated in few primary commodities, such as coffee and oilseeds, whose prices are highly volatile and exposed to global price swings.

Therefore, this paper examined the experience of Korea's outward-looking industrialization development strategy and the recent macroeconomic performance of Ethiopia. The second section presents outward-looking strategy of Korea followed by the Korean economic performance at the early stage of development in section three. Section four presents the recent economic performance of Ethiopia, and section five forwards some policy lessons to Ethiopia.

An Outward-Looking Development Strategy of Korea

Korea started its industrialization strategy during postwar reconstruction period in 1950s based on a policy of import substitution in machinery, durable consumer goods and intermediate products. However, the import substitution policy clearly failed to make manufacturing a dominant sector. Thus, Korea shifted from import substitution to export promotion policy in early 1960s with the adoption of the export-oriented industrialization (EOI) strategy that originally promoted growth through labor-intensive manufactured exports in which South Korea could develop a comparative advantage (Ahn & Kim, 1997). This export drive policy was supported by various economic reforms such as budget and tax reform in 1961 and exchange rate and interest rate reforms in 1965 (Chung-yum, 2011).

The goal of the EOI strategy was achieving sustainable economic development through export promotion, industrialization and foreign capital promotion. Despite the Korea's poor natural resource endowment, low domestic saving rate and tiny domestic market, the outward looking industrialization strategy worked well in the process of transforming Korea from poverty-stricken and aid dependent to self-sufficient industrialized nation within a short period of time.

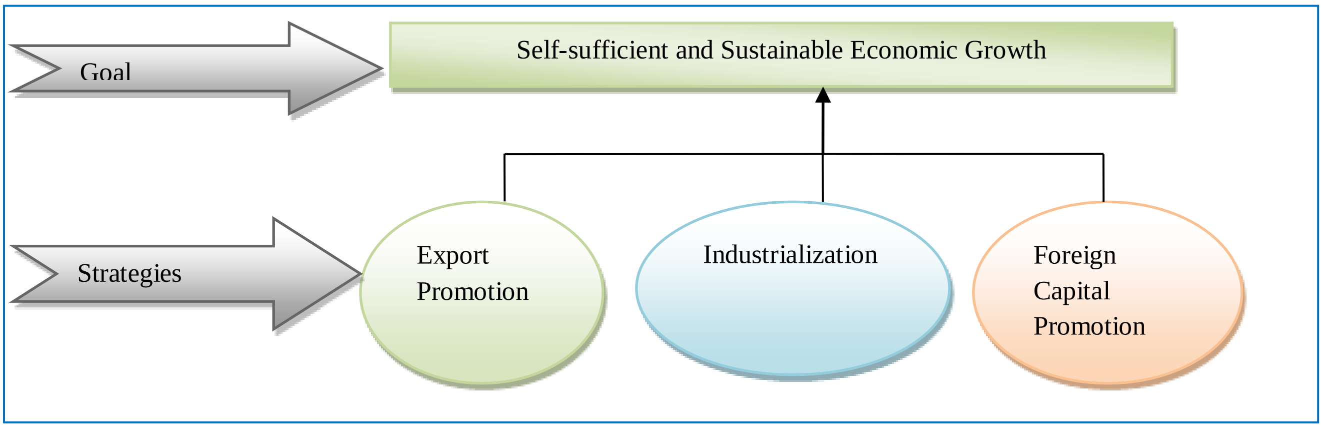

Figure 1: Outward-looking Development Strategy of Korea

The Korean government launched the first five-year economic plan in 1962, which aimed at improving the base of economy before the initiation of export-oriented industrialization strategy in 1964. The plan was focused on providing assistance to basic industries and investing on social and economic infrastructures. However, the domestic saving was not sufficient to satisfy the money demanded for investments. As foreign aid, the main source of capital in 1950s, was drastically reduced in the 1960s, the government also became increasingly concerned about earning sufficient foreign exchange and raising domestic saving. South Korea's foreign exchange holding gradually declined in the early 1960s because of the reduction of USA grant and expansionary policies of the Korean government. Hence, the Korean government was in demand of foreign capital, and took policy measures to encourage the inflow of foreign loans and foreign direct investment. The inflow of foreign capital was highly encouraged to fill the huge gap between domestic savings and investment. The efforts enabled the country to achieve rapid growth in exports and subsequent increases in income (Lee J. , 2013). The country also adopted an export-oriented economic system with extensive export incentive measures in the early 1960s as a means of earning foreign exchange enough to repay the accumulated huge external debt. In fact, as (Yoo, 2008) noted, export promotion measures were used even in the 1950s. Korea adopted 'trade (export) credit system' in 1950 that continued in the 1960s and 1970s, and this system gave exporters priority in allocation of domestic credits and unlimited loans. Exporters were also enjoyed tax favors, tariff exemptions on imports of raw materials, preferential access to foreign exchange loans, and direct subsidies.

In the late 1960s, the government, with the second five-year development plan, intended to foster labor intensive light industries for export expansion as well as for import substitution to support the material supply for export industries. Having limited domestic market size, export was virtually the only way to strongly establish the Korean industries. The government provided comprehensive promotion measures for export industries such as tariff exemptions on imports of raw materials for export production; direct tax reduction on income earned from exports; indirect domestic tax exemption on intermediate inputs used for export production; accelerated depreciation allowances on fixed assets; preferential export credit (policy loan); construction of industrial parks; and technical assistances (Ahn & Kim, 1997; Heo, 2001). Moreover, to support the implementation of the EOI strategy, the government used three direct administrative instruments: annual export targeting system that set by major commodity group and destination; the 'Monthly Trade (Export) Promotion Conference' which essentially served to disseminate the government emphasis on export promotion and to quickly resolve problems encountered by exporters through the direct decision of the president; and the support of KOTRA (Korean Trade Promotion Corporation), established in 1962, to facilitate Korea's rapid export-led economic growth through various trade promotion activities such as overseas market surveys and continuous expansion of global business networks (Kim, Shim, & Kim, 1995; Koh, 2010).

With such intensive support and direct intervention of the Korean government, the EOI strategy was successful in boosting export and economic growth of Korea. The export amount extraordinarily increased to about $US 61.4 billion in 1989, from about $US 55 million in 1962. During the four successive five-year development plan periods, export increased on average at a rate of about 39 percent annually. Besides, the rapid growth of the economy caused a substantial structural transformation. The share of agriculture in GDP declined to 10.8 percent in 1987 from 39.9 percent in 1960 (Harvie & Lee, 2003).

However, Korea's competitiveness was declined in the global market in the early 1970s due to the rise of neo-protectionism for labor intensive industries in the West while the domestic wage rental ratio was rising rapidly. Besides, the USA reduced its forces stationed in South Korea by a third in 1971, and the tension was escalated in the Korean peninsula. Thus, the Korean policy makers found that the heavy and chemical industries (HCI) promotion was an essential and inevitable element of industrialization process in the 1970s to maintain global market competitiveness, improve balance of payment accounts, and enhance the nation's self-defense capability. Accordingly, the HCI drive policy was introduced to promote six HCIs: shipbuilding, steel and iron, electronics, petrochemicals, machinery, and nonferrous metals. The HCIs were provided with various incentives such as corporate income tax exemption, duty-free import of capital goods, and preferential long-term financing through National Investment Fund. With the launch of HCI drive in 1972, the government took policy measures including support of engineering and technical schools to secure engineers and skilled workers, establishment of new research institutes, and construction of industrial complexes for HCI plants (Lee S.-C. , 1991).

Indeed, the massive investment in HCI plan brought about vast excess capacity, and the financial sectors continued to accumulate nonperforming loans from lending to those industries. The negative effects of HCI promotion policy became more apparent in the late 1970s and early 1980s. Albeit Korea reaped the fruits of the HCI drive policy in the long-run since 1980s, the HCI plan is criticized as a failure of extensive government interventionist policies.

Consequently, various trade and industry policy reform measures relying on market forces were undertaken in the early 1980s. Favorable financial support including preferential interest rate for HCIs was abolished in 1982, and National Investment Fund was substantially reduced. Korea shifted to trade liberalization and technology-oriented industrial policy, and incentives for technology and manpower development were strengthened. Korea continued liberalization process in 1990s to rapidly integrate into the world economy (Ahn & Kim, 1997). While liberalizing the economy, the government began to promote the information technology industry as a new driving force of economic growth.

Korean Economic Performance in the 1960s – 1980s

Korean economic miracle started in the early 1960s when the government policy shifted from import substitution towards export promotion. The implementation of an outward-looking strategy in 1964, supported with exchange rate reform in the same year, is considered as the most momentous factor for rapid industrialization and miracle economic growth of Korea in the 1960s and 1970s. Korea was ranked 101st out of 125 countries in terms of per capita income in 1961, but become 62nd in 1980. Further, due to a massive and well-planned export promotion discipline with persistent policy shifting and upgrading (Heo, 2001), after five decades, the country became the 12th biggest economy in the world in 2018.

With the adoption of EOI development strategy, an impressive average economic growth was recorded in the 1960s to 1980s, and continued in 1990s until the Asian crisis of 1997/1998. Korea managed to attain a relatively high (about 8 percent) growth even during the 1974-75 worldwide economic recessions following the first oil shock in 1973. Exports of goods and services also grow spectacularly from about 3.87% of GDP in 1962 to 30 % of GDP in 1981, and further increased to about 56% of GDP in 2012. In fact, the economic performance deteriorated and export growth slowed down in late 1970s as the economy was seriously thumped by increase in prices of oil and raw materials. Besides, the heavy reliance of the government on foreign borrowing for its large scale investment projects caused persistent current account deficit. The external debt grew rapidly throughout the 1970s and reached $US 25 billion (45% of GDP) in 1980.

Consequently, after two decades of spectacular economic record, Korea experienced the first negative GDP growth (of -1.9 percent) in 1980. This was (Kim & Park, 1985), mainly due to agricultural failure caused by unusual weather conditions; sudden decline in the intensity of demand; political instability following President Park's assassination; and a sudden policy shift from growth maximization to price stabilization motivated by the second world oil shock in 1979. Despite the severe crisis in 1980, the economy rebound shortly with a GDP growth rate of about 7.4 percent and 8.2 percent in 1981 and 1982, respectively, partly due to improved production and stabilization policy introduced by the new government.

Table 1: Macroeconomic and Structural Patterns of Korea since 1960s

Measures	*1962*	*1963-1973*	*1974-1980*	*1981-1989*	*1990-2000*	*2001-2016*
GDP growth (annual %)	3.84	10.64	8.63	9.95	7.29	3.89
GDP per capita growth (%)	0.91	8.14	6.91	8.64	6.30	3.34
Annual Inflation (%)	6.62	13.94	19.49	6.15	5.42	2.64
Annual Exports (% growth)	15.70	34.17	16.39	12.61	13.97	7.91
As % of GDP:						
Gross domestic savings	3.30	13.67	26.00	34.16	37.72	34.17
Gross capital formation	14.08	22.65	32.40	33.28	36.66	31.13
Export of goods & service	3.87	10.82	24.77	30.03	28.33	43.66
Merchandise trade	16.99	29.56	56.04	59.10	49.54	70.37
Current account balance				-0.83	0.39	2.95

Source: The World Bank and World Economic Outlook Databases (2019)

The persistent growth spurt was led by manufacturing sector, whose output grew annually by 17 percent and 16 percent in the 1960s and 1970s, respectively. The share of manufacturing in gross value added rose from 12 percent in 1953-1960 to 23 percent in 1971-1980. The share of services increased continuously, while that of agriculture declined. Within manufacturing, HCIs have increased their share at the expense of light industries.

Table 2: Share in gross value added by sector (in %)

Year	1953-60	1961-70	1971-80	1981-90	1991-00	2001-09
Agriculture, forestry and fishing	41.9	35.5	24.6	12.4	6.0	3.4
Mining and Manufacturing	13.4	19.1	24.0	28.4	26.9	27.3
Mining	1.4	1.8	1.3	1.1	0.5	0.2
Manufacturing	12.0	17.3	22.7	27.3	26.5	27.1
Light industries	9.5	11.5	11.3	9.8	6.5	4.5
HCIs	2.5	5.8	11.4	17.5	20.0	22.6
Public utilities and construction	3.7	5.2	6.8	10.0	11.9	9.6
Service	41.1	40.2	44.5	49.2	55.2	59.6
Gross value-added	100.0	100.0	100.0	100.0	100.0	100.0

Source: Bank of Korea (Overview of Korea's Development Experience webpage)

The rapid changes in industrial structure with constant policy shifting and upgrading helped Korea to maintain its global competitiveness. The country's merchandise exports that had been stagnant in the 1950s skyrocketed since early 1960s, and it reached $US 21,268 million in 1981 from about $US 32 million in 1960. The export growth was accompanied by a significant progress in export diversification. The export structure changed dramatically from raw and light industry products in 1960s and 1970s to almost HCI products in 2000s. The proportion of primary products to the total exports decreased rapidly from 72.3 percent in 1962 to 11.1 percent in 1972, and further decreased to 7.7 percent in 1980. But, the proportion of manufacturing products to the total exports increased from 27.7 percent in 1962 to 88.9 percent in 1972 and further increased to 92.3 percent in 1980. Moreover, the proportion of products from light industries to the total exports decreased from 67.4 percent in 1972 to 48.4 percent in 1980, while the proportion of products from heavy industries to the total exports increased from 21.5 percent in 1972 to 43.9 percent in 1980 (Lee J. , 2013).

Table 3: Share of top ten export items in total exports (in %), Korea

Rank	*1961*		*1970*		*1980*		*2018*	
1	Iron ore	13.0	Textile	40.8	Garments	16.0	Electronic goods	30.5
2	Tungsten	12.6	Plywood	11.0	Steel-plate-rolled products	5.4	General Machinery	12.8
3	Raw yarn	6.7	Wigs	10.8	Footwear	5.2	Vehicles	11.1
4	Coal	5.8	Iron ore	5.9	Ships	3.6	Minerals	7.9
5	Cuttlefish	5.6	Electronic goods	3.5	Audio equipment	3.4	Plastics	5.8
6	Live fish	4.5	Confectionary	2.3	Man-made filament fabrics	3.2	Display devices	4.6
7	Graphite	4.2	Footwear	2.1	Rubber products	2.9	Chemicals	4.2
8	Plywood	3.3	Tobaccos	1.6	Woods & wood items	2.8	Iron and steel	4.1
9	Rice	3.3	Iron product	1.5	Video equipment	2.6	Ships	3.4
10	Swine bristle	3.0	Metal products	1.5	Semiconductor	2.5	Iron products	1.7
	Sum	*62.0*		*81.1*		*47.6*		*86.1*

Source: Ministry of Trade, Industry and Energy of Korea, and International Trade Center Database

The Recent Macroeconomic Performance of Ethiopia

Ethiopia has shown a robust economic growth record for more than a decade averaging 10.6 percent from 2004 -2017, placing the country among the best performing economies in Sub-Sahara Africa. After decades of pitiable growth, the remarkable economic rebound in year 2004 (11%) came mainly from increase in agricultural output due to favorable weather conditions, better supply of agricultural inputs, and the increase in cultivated land from the resettlement program. Despite the unpleasant export performance and persistent political tensions, the real GDP growth continued remarkable with 7.7% in 2018. The growth remains robust supported by heavy investment in infrastructure and expansion of services activities such as hotel and restaurants, transport and communications.

With the adoption of the first five-year Growth and Transformation Plan (GTP) in 2010, the country place more emphasis on capital investments that would lead to an increasing share of value-added exports to boost economic growth, especially manufactured products based on agro-processing industries. The first five-year plan (2010/11 – 2014/15) aimed at sustaining rapid and equitable economic growth, ensuring agriculture as a major source of economic growth, inducing the industry to play a key role in the economy, enhancing expansion and quality of infrastructure and social development, building capacity and deepening good governance, and promoting women and youth empowerment. The structural transformation pursued through scaled-up public investments in roads, railroads, hydroelectric generation plants, sugar factories, housing as well as high fiscal spending for human capital development through education, technical and vocational trainings.

Table 4: Macroeconomic Performance of Ethiopia since 1991

Measures	*1991*	*1991-2000*	*2001-2005*	*2006-2010*	*2011-2015*	*2016-2017*
GDP (% growth)	-7.14	3.00	6.61	10.89	10.21	8.90
GDP per capita (% growth)	-10.37	-0.29	3.62	7.96	7.38	6.23
Annual Inflation (%)	35.72	7.08	3.88	18.11	16.59	8.56
Exports of G & S (% growth)	-32.13	16.44	11.68	9.33	2.60	-0.24
External debt (% of GNI)	68.21	106.35	70.91	15.84	28.19	32.94
Merchandise exports (Mill. US$)	189	387	603	1574	3167	3041
As % of GDP:						
Gross domestic savings	5.96	9.85	11.06	5.87	13.64	14.17
Total investment	11.52	14.98	22.56	23.23	36.14	38.50
Current account balance	0.74	-0.80	-5.42	-6.16	-6.52	-8.96
Exports of good & service	4.06	8.72	13.71	12.60	12.89	7.84
Merchandise Exports	1.80	4.76	5.53	5.53	5.76	3.56

Source: The World Bank and World Economic Outlook databases (2019)

However, the efficacy of the public sector led development strategy became questionable as most projects failed to be completed within the projected time period, including sugar projects. The country faced major structural weaknesses, and the economy left highly vulnerable to exogenous shocks by virtue of its dependence on primary commodities and rain-fed agriculture. Agriculture remains the cornerstone of the Ethiopian economy and the most important source of growth, household income, and foreign exchange. It accounts about 37 percent of GDP, while industry accounts for only 21 percent of GDP in 2016. Agriculture also accounts for more than 80 percent of export earnings with coffee, oilseeds, vegetables and fruits, cut flower, and live animals. But, in recent years, the share of industry and service sector in GDP has been improving while that of agriculture slightly declining. The growth in services was driven by the rapid expansion in financial intermediation, wholesale and retail trade, hotel and tourism, transport and communications. The industry sector has also recently grown in value terms, and its contribution to GDP has been rising, which is from 12.2 percent in 2000 to 21.3 percent in 2016.

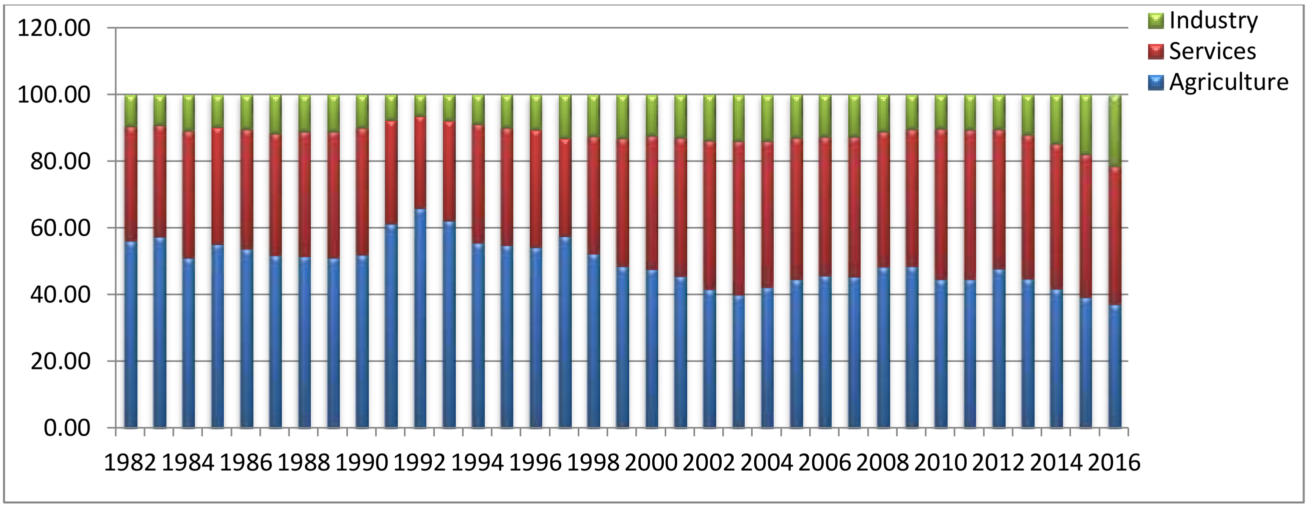

Figure 2: Structural Change and Sectoral Share in real GDP of Ethiopia

Source: National Bank of Ethiopia and World Bank Database (2019)

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Further, Ethiopian exports have been persistently increased in volume over the last two decades despite the disproportionate increase in imports that could be an exposure to the country's unsustainable economic growth. Indeed, the Ethiopian government has various export promotion instruments including duty drawback scheme under "export trade duty incentive scheme proclamation no. 768/2012, export subsidies, tariff or duty exemptions for capital imports and tax holidays for exporting industries. Merchandise trade as a percentage of GDP has continuously increased and peaked in year 2005 (41% of GDP) partly due to high agricultural productivity and the increase in the global commodity price emanated from the overheated global economy before the global financial crisis. However, the merchandise export as a percentage of GDP has been sharply deteriorating and exhibited the worst performance in 2017 with 3.5% of GDP from 7.2% of GDP in 2010. According to (WB, 2014) report, merchandise exports declined by 2.5 percent in 2013, and further decreased by 7.6 percent in 2014 exceeding even the drop observed in 2009 during the global financial crisis.

Consequently, the current account and trade balance have been incessantly in deficit for more than three decades though the values of merchandise exports increased from US$ 486 million in 2000 to US$ 3,163 million in 2017. The recent poor performance of external sector is mainly due to an overvalued exchange rate, limited access to finance, poor infrastructure, decrease in foreign demands for Ethiopian commodity exports, and high trade costs associated with poor logistics. According to World Bank logistics performance index data, for instance, Ethiopia ranked 133rd with a quality of trade and transport related infrastructure index of 1.87 in 2007 and 2.11 in 2016, while the neighboring Kenya has an index of 3.21 in 2016. Such poor logistics performance index would raise trade costs for local industries and hampers the country's competitiveness in the global market.

Regarding export structure, Ethiopia continued to be highly dependent on few primary agricultural commodities indicating that export diversification is still unsatisfactorily low, and the export earnings remain unstable mainly due to high price fluctuations. Five primary products including coffee, oilseeds, vegetables, cut flowers and live animals constitutes more than 80 percent of total export earnings. Coffee remained the leading export item accounting for 34 percent, followed by oilseeds (20%) and live trees (11.4%) in 2018. Secondary sector exports, manufacturing products in particular, remained very low, and even their share to total export has been deteriorating since 2012.

Although the dependency of Ethiopian exports on coffee decreased over the last decade, the export sector has not yet diversified into value added products. The reduction in coffee share is noticeably replaced by other primary commodities mainly oilseeds and vegetables. The excessive dependence on few primary commodities left the country highly exposed to volatile global commodity prices and strong competition that leads to declining share in global trade.

Table 5: Share of top five export items in total exports (in %), Ethiopia

	1995		2000		2010		2018	
	Item	%	Item	%	Item	%	Item	%
1	Coffee	65.4	Coffee	53.7	Coffee	31.2	Coffee	34.0
2	Raw skins	13.6	Vegetables	14.4	Vegetables	17.5	Oilseeds	20.0
3	Vegetables	6.6	Raw skins	9.9	Oilseeds	14.8	Live trees	11.4
4	Cotton	3.3	Oilseeds	6.1	Pearls, stones	7.9	Vegetables	5.1
5	Minerals	2.9	Pearls, stones	5.7	Live trees	7.1	Apparel	4.8
	Sum	91.8		89.8		78.5		75.3

Source: UN Comtrade and International Trade Center Databases (2019)

Policy Lessons to Ethiopia

Ethiopia has adopted an interventionist policy that caused private sector inefficiency, what most South East Asian countries experienced in the 1960s and 1970s. The public sector-led growth strategy resulted inefficient production of both capital and human resources and impeded the promising structural transformation. Despite the implementation of GTPs and the existing export promotion instruments, the country's global competitiveness is at stake due to unsatisfactory export diversification and inefficient production by the traditional export sectors. The manufacturing sector remains petite both in terms of output production and employment. Indeed, Korea achieved incredible economic record through performance-based incentives for exporting industries, committed leadership, high intervention with huge support for value added private enterprises, the creation of institutions to improve technological import capabilities, intensive human capital development, and constant policy shifting and upgrading.

Thus, Ethiopia should shift and allocate its limited resources including human capital selectively to highly productive sectors. Any means of support including export promotion and investment incentives should be transparent and performance-based with a target production or export level. Besides, structural change from agricultural commodity based export to value-added sectors is vital for strengthening global competitiveness and sustainable economic growth. As such structural transformation requires the friendly participation of the government and private investors, the Ethiopian government should open up the economy to broaden the business opportunities to private entrepreneurs and then promote innovation. Given the growing public investment in infrastructure, it is crucial to improve trade logistics and diversify exports towards the industrial sector with more private investment in export-oriented economic activities to sustain high economic growth and strengthen the long-run global competitiveness. The government should also increase public spending for investment in technologies and skills as well as promote FDIs aiming at technology and knowledge transfer.

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