The Economics of Converging Theoretical Paradigms:
Evidences from Indo-Korean Bilateral Economic Cooperation

By

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Abstract

This paper aims to assess economic consequences of converging theoretical paradigms (CTPs) affecting regimes of economic cooperation (RECs). In the past, theoretical paradigms such as Capitalism vs. Socialism or more recent Keynesianism vs. Monetarism clearly diverged on structural, organizational and operational levels, however in the recent times there are ample evidences showing greater theoretical convergence leading towards the "Post-Washington Consensus". This visible paradigmatic convergence is affecting the fundamentals of bilateral, multilateral economic cooperation. There are successful cases of regional or bilateral cooperation regimes - NAFTA, EC, ASEAN or Japan-Malaysia, USA-UK - driven by the convergence of economic paradigms among and between national economies.

Literature that deals with the economic cooperation regimes tends to focus on the changing geo-economic and geo-political dimensions but it ignores the deeper theoretical realignments causing fundamental shift in the nature and scope of economic cooperation. Korea and India are such cases where bilateral economic cooperation got substantial boost from the converging perceptions about economic thinking. This paper argues that differing economic paradigms are converging into one widely accepted perception that market-determined outcomes are crucial for the efficiency of the economic systems, though increasingly with clear human development agenda in mind.

Hypothesis is that the paradigmatic convergence has positive impact on the bilateral or multilateral economic cooperation; 1) because it reduces mismatch in the regulatory regimes emanating from the structurally differing paradigms; 2) because regulatory harmonization creates greater economic opportunities for trade, investment and market between and among economies.

Theoretically, "Post-Washington Consensus" provides a bridge between sharply diverging Keynesian and Monetarist arguments that leads to the softening of the dislocating effects from the market-outcomes. Asian financial crisis of 1997 gave the grim reminder that unfettered cross-border capital flows, though based on the market principles, can cause havoc. Questions arising from the Asian crisis pushed "Washington Consensus" towards the "Post-Washington Consensus".

Empirically, sharply increased bilateral economic cooperation between Korea and India demonstrates the positive impact of converging economic paradigms. It shows that the two distinct phases - market-seeking phase (1970s~80s) and production-seeking phase (1990s~2000s) - in the bilateral economic cooperation between Korea and India are closely related to the phases of diverging and converging paradigms.

The main findings of this research suggest that a growing convergence centered on the primacy of market has galvanized economic cooperation regimes, though often in the regional economic frameworks. In the Cold War period, India and Korea adopted differing economic paradigms: India vigorously fallowed market distorting socialist system whereas Korea aligned itself with the market-conforming capitalist system. This divergence in the economic thinking led to the near-stagnation in bilateral economic cooperation between two economies. During this period, Korean companies exclusively concentrated only on the marketing of their products in India. However, in the post-Cold War period, bilateral economic cooperation between India and Korea changed dramatically due to the convergence in the economic paradigms. In this phase,

Korean corporations moved from the short-term ‘market-seeking approach’ to the long-term ‘production-seeking approach’.

On the policy level, this study notes that enhanced bilateral or multilateral cooperation needs a greater paradigmatic convergence. In the post-Cold War era, economies are moving fast to reorient towards the market-based economic regimes. Korea's post-war experiment with the 'market-conforming' economic logic provides an opportunity to become a role model for many developing economies pursuing structural economic reforms. India is such an economy experimenting with the liberal economic philosophy and finds wider convergence with Korea's decade's old market-conforming economic paradigm.

Key Words: Paradigm, Economic cooperation, Trade, India and Korea.
JEL Classification: F15, F14, B2

Introduction

Liberal international economic order (LIEO) 1820-1913, the first significant example of converging theoretical paradigms (CTPs) marked the beginning of an unprecedented era of bilateral/ multilateral economic cooperation.[1] In this phase, international trade and investment took a quantum leap.[2] The extent of economic change between 1820 and 1913 was both unprecedented and impressive: per capita income in the average OECD country more than tripled; the share of industry rose dramatically; the share of employment in agriculture declined by two thirds; the volume of world exports grew more than thirty fold; a global economy and a global financial system were created; substantial intercontinental capital and population movements took place, connecting the overseas territories to the European economy; and international patterns of specialization in production and trade emerged (Adelman, 1995). Nonetheless, the first LIEO could

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[1] The concept of a paradigm, whose originator, T.S. Kuhn was inspired by the history of the national sciences, is applied to the context of the social sciences. Here the new paradigm does not necessarily replace the old; several paradigms may function effectively side-by-side. Scholars can be said to use the same paradigm in their research and teaching if they show the following common attributes: 1). They work to solve the same or closely related ‘puzzles’. They view social reality from the same, or almost the same angle. They set out to illuminate the same, or almost the same range of phenomena, and are content to abstract away the same phenomena or leave them obscure. Those who work within a common paradigm have the same, or a closely related outlook, viewpoint and approach. 2). They use conceptual frameworks that are the same or closely akin. (Alternatively, it is relatively easy to compile a word list that translates the conceptual apparatus of one author into that of another.) 3). They use the same or a similar methodology for observing, processing experience and drawing conclusions; they support their statements by the same or similar methods. Unlike many other paradigms in the natural or social sciences, here we refer to the system paradigm, which cannot be linked with a single great name, a great innovative figure who fomented a scientific revolution. It developed in a series of works, over a long period. For details, see T.S. Kuhn, *The Structure of Scientific Revolutions*. Chicago: The University of Chicago Press, [1962] 1970.

[2] The period 1820-1913 was one of very free international trade, with no quantitative restrictions and with mostly low or no tariffs on raw material and food imports, varying degrees of industrial protection, extremely free international movements of labor and capital, and a fixed nominal exchange rate under a gold-sterling-standard. For details, see Irma Adelman, "The Long Term Impact of Economic Development in Developed Countries on Developing Countries since 1820" *Journal of Evolutionary Economics,* Vol. 5, No. 3 (1995), pp. 189-208.

not sustain the momentum due to its direct linkages with the colonial political economy and thus fell apart under the multiple pressures originating from the imperial rivalry. Finally, the disrupting impact form WWI, Great Depression and WWII put to an effective end to the first experiment of LIEO. The prevailing political sentiments that emerged out of interwar period favored the new economic rationale that economic welfare would be best promoted through limiting free trade and capital mobility and generally using the power of government to strongly regulate and guide economic activity. A central lesson drawn from the experience of the decades between world wars was that the economic and political fate of the world could not be safely entrusted to the unregulated free market forces. History warned that this was a path to economic instability, global depression and political chaos.

The outbreak of Cold War, based on the capitalist-socialist ideological confrontation, led to the primacy of politics over economics. Soviet Union's resilience to face great depression attracted many developing economies towards state-led planned development. Many newly independent countries created a plan-rational 'developmental state' to augment economic growth.[3] 'Keynesian revolution' swept across the globe justifying activist role of state in the market place. Big governments and Keynesian macro-economic management in the North and the rise of 'developmental state' in the South characterized the early Post-WWII period. Thus, the economic instability that erupted in the 1970s created a powerful movement, led by business and, especially, financial interests to roll back the economic regulatory power of state, replacing conscious societal control with the 'invisible hand' of unregulated markets.

A new economic dynamics begins with the end of Cold War era capitalist-socialist dichotomy when mainstream economic thinking started to converge around 'Washington Consensus' and its mentor the neo-liberal theoretical paradigm.[4] Keynesian economics given way to the monetarist thought. This paradigm shift signals the second coming of LIEO, which is once again initiating a paradigmatic convergence. The dynamic impact of paradigm convergence is virtually creating a borderless global economy where regimes of economic cooperation (RECs)[5] are witnessing a fundamental transformation. In Europe, Latin America, and Asia, regional economic agreements are becoming a dominant expression of relations among states, giving regional structures a geopolitical personality. Clearly, national economies are submerging

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[3] For details about the developmental state, see A. Leftwich, "Bringing Politics Back In: Towards a Model of the Developmental State", *Journal of Development Studies Vol.* 31, No. 3 (1995), pp. 400-27.

[4] J. Aziz, and R. F. Wescott, "Policy Complementarities and the Washington Consensus", IMF Working Paper 97/118. Washington, D.C., 1997.

[5] Apart from the various structures of bilateral economic interaction, RECs includes; regional trade agreements (RTAs), Free Trade Agreement (FTAs), Custom Union, Common Markets, Economic Unions. RTAs are agreements whereby members accord preferential treatment to one another in respect of trade barriers. RTAs vary in terms of the level of integration. At the base is the FTA where trade barriers (usually tariffs) between partner countries are abolished. However, each member determines its own external trade barrier with non-FTA members independently. A prominent example of an FTA is the North America Free Trade Agreement (NAFTA). The next level of integration is the Custom Union where a common external trade policy (e.g. common external tariff regime) is adopted by member countries. MERCOSUR represents such an arrangement. Common Markets like the European Community adopt further provisions to facilitate the free movement of factors of production like labor and capital, and the harmonization of trading and technical standards across member countries. Finally, Economic Unions such as the European Union, extend the harmonization to fiscal and monetary policies, as well as social and legal policies.

into regional economies. NAFTA, EC, ASEAN and MERCOSUR are already in operation. These regional cooperation regimes are linked with the globally integrated economic regime.

This new global economy powered by CTPs provides a great impetus to the RECs. The globalization and regionalization processes emanating from the CTPs are virtually forcing national economies to extend hands of cooperation globally. India and Korea are two such cases where growing convergence in their economic thinking reflects a crucial turn around in their bilateral economic interactions. The power of CTPs is cutting across many of the rules set by traditional geo-economic or geo-political arrangements and creating a set of incentives for the economies to enter into bilateral/or multilateral cooperation regimes such as free trade agreements (FTAs), Custom Unions, Common Markets and Monetary Unions, etc.

Arguments in this paper are organized in the following way. Section II revisits historical legacy by assessing the impact of diverging paradigms – capitalism vs. socialism and Keynesianism vs. monetarism – on the RECs. It argues that differing economic paradigms create distinct regulatory structures to provide governing framework for areas of finance, trade and market. These differing frameworks effectively hinder the process of bilateral economic interaction. It notes that this regulatory mismatch was further complicated by the superpower ideological rivalry played out on the politico-military turf. The Cold War period symbolizes the power of paradigm clash, which clearly fragmented earlier era cooperative economic structures created by the first LIEO.

Section III takes note of growing paradigm convergence in the post-Cold War era when capitalist-socialist dichotomy dramatically given way to the primacy of market logic and assesses its impact on the RECs. It argues that the end of communism unchained powerful forces of market creating a truly global space in terms of finance, trade & investment, production, and market. This market revolution powered by 'Washington Consensus' clearly integrates traditionally segmented national economies into a single world economy. It notes that this phase can be termed as the second LIEO.

Section IV provides the evidence from the bilateral economic interaction between India and Korea where two distinct phases – paradigm divergence and paradigm convergence – are clearly visible. The bilateral Indo-Korea trade data consist of export and import variables validates the basic assumptions of this paper that paradigm divergence prominent during the Cold War years reduces bilateral economic interaction and paradigm convergence of 1990s~2000s increases bilateral economic cooperation.

Section V derives policy lessons from the convergence paradigms deeply affecting RECs. It outlines an institutional cooperation framework that can facilitate qualitative up gradation in the bilateral economic cooperation and create vital linkages to the future multilateral cooperation efforts. It also highlights the point that Indo-Korean bilateral economic cooperation can become the backbone for future regional economic cooperation framework that can move in steps from bilateral free trade agreement to multilateral Custom Union, Common Market and finally Monetary Union of Asian economies.

Section VI concludes that the economics of paradigm convergence positively affects the RECs. It has activated the dormant Indo-Korean bilateral economic cooperation. It shows that during the Cold War period, Indo-Korean economic cooperation was marred by the paradigmatic divergence when Korea experimented capitalist accumulation logic based on the export-promotion, private sector-led economic regime and India adopted socialist distributive logic based on import-substitution, public sector-led economic regime. In the post-1990s, both India and Korea are increasingly witnessing a paradigm convergence leading toward the construction of liberal economic regime. This liberal economic regime is the prime mover of rapidly increasing bilateral economic cooperation.

II. Economics of Diverging Theoretical Paradigms

Cold War Era Capitalist-Socialist Dichotomy and the Fragmentation of RECs

The end of the first LIEO marks the beginning a confrontational era when economic paradigms diverged sharply. In this period, the growing dichotomy between capitalism and socialism led to the unprecedented paradigm clash, which resulted in the fragmentation of the earlier era RECs.[6] This paradigmatic divergence created by conflicting capitalist and socialist arguments got further complicated by politico-military rivalry between the United States and Soviet Union. First time in the world, economic ideas created their political domains bitterly contested in the global scale. These competing ideological frameworks divided countries and continents into antagonistic ideological blocs with almost negligible economic interaction. The power of paradigm clash raised the 'iron curtain' dividing Europe in to two distinct system paradigms: capitalism in the West and socialism in the East. The 'Berlin Wall' not only symbolized the division of Germany but the power of economic ideas to divide and fragment RECs. By effectively blocking the movements of goods, people, and capital, paradigmatic divergence put East-West European economic cooperation to stand still.

In the capitalist bloc, Keynesian and monetarist paradigms, which gave differing emphasis to the role of state in the market place, considerably affected the scope and depth of economic cooperation.[7] The management of 'market aggregates' led to the friction in bilateral trade and investment affecting RECs. Trade and investment frictions of 1980s between East Asia and USA and recurrently trans-Atlantic trade rifts remind the differences in the Keynesian-Monetarist perspectives.

Thus, the paradigmatic divergence between capitalism-socialism /or Keynesianism-Monetarism deeply affected economic linkages between regions and countries. Twentieth century's great clash in economic paradigms destroyed the foundations of international economic cooperation. During the Cold War period, capitalist and communist economies chose not to interact. Apart from politico-military considerations, disruption in trade and investment between

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[6] Socialist relations refer to the trends toward making political, associational, and contractual activity a balance against, or an adversarial alternative to, or a means of redefining, property ownership, in such ways especially as to make the market socially accountable and socially responsible. It has involved political, social, and economic reordering in the direction of regulating, modifying, remedying, or displacing, market behavior and market outcomes by social policy. Socialism, therefore, has corresponded with social relations, law, public policy, standards, and values asserting a broadening conception of human rights reshaping and redefining property rights and market behavior. In capitalist relations, principles of liberty and efficiency (often referred to as "bourgeois") tend in some decisive ways to broaden the sphere of individual initiative and authority as well as equalitarian values and behavior, but they tend at the same time, on behalf of concurrent principles of property rights and economic development, to range themselves against emergent, ever broader standards of liberty, equality, social justice, and development. Also, see Niklas Luhmann, *Social Systems* (Writing Science). Stanford, CA: Stanford University Press, 1995.

[7] S.C. Dow and J. Hillard, eds., *Keynes, Uncertainty and the Global Economy*, Vol.2, Elgar, Cheltenham, 2002.

rival blocs was caused due to the mismatching regulatory structures governing financial, managerial and trade related issues. A closer scrutiny of these regulatory structures confirms that trade and investment flows generally follow well-established channels and networks based on the similar economic ideologies:

Financial Regulatory Structures

The RECs largely derive their functional efficiency and long-term sustainability from the regulatory structures of finance. Sophisticated financial regulations are needed to support cross border capital flows. Market-determined exchange rate regimes, well functioning stock markets, large banking sector, and an efficient international capital market – all are important for the long-term viability of trade and investment flows across borders. On the other hand, financial regulations based on the repressed exchange rate regimes, state controlled banking sector, and large public sector are key deterrent to the growth of RECs. In the march towards European economic union various agreements to streamline financial regulatory structures were been concluded. Maastricht Treaty (1992) lays down the detailed criteria in this effect.[8] In other words, matching financial regulations based on the market logic enhance economic cooperation and mismatching financial regulations based on the political logic hinders the process of economic cooperation. Thus, expansion of international production, distribution and marketing requires market-based matching financial regulatory structures.

Managerial Regulatory Structures

The regulatory structures of management and ownership of a firm falls under the clearly defined two spheres: management and finance. The rise of professional managerial class has fundamentally changed the functioning of a firm towards the greater efficiency and profitability. Market determined decision-making system became the core of capitalist management system. However, the managerial revolution that swept the corporate sector in the capitalist economies left untouched socialist economies. In the socialist economies, the management of a firm has continued to be an administrative work based on the political and social requirements. In this management system prices has always been determined by the political compulsions rather than market signals. These two differing managerial structures prevented firms to form cooperative alliances and ventures.

Trade & Investment Related Regulatory Structures

The policy structures regulating trade and investment flows either conform or distort market signals. Various tariff and non-tariff barriers, anti-dumping duties, import quota system are the potential policy instruments under the governments that can distort free flow of commodities and goods. In the past when economies agreed to have free trade regimes, economic interaction among and between countries increased substantially. Under the GATT and WTO supervision, relatively free flow of goods, commodities and services has been ensured. This has led to the substantial 'trade creation' and subsequent enhanced economic cooperation among trading partners. On the contrary, in the socialist economies, internal and external trade

[8] For the further details about the 1992 treaty, see http://www.essex.ac.uk/info/Maastricht.html

came under the monopoly of state and state-run enterprises hence limiting the potential to trade. Movement of goods and services was restricted by the non-market structures and manned by extensive army of bureaucrats. Thus, sharp variation in the regulatory regimes acted as the constraining factor in the RECs.

Theses diverging regulatory structures created a regime of constraints hindering economic cooperation. Areas under the socialist influence zone traded under the elaborate system of political considerations and hopelessly failed to realize the potential, whereas in the market-based system goods and services moved following the price differentials and realized almost optimal potential. Thus, economic cooperation in the Cold War era strictly followed the matching regulatory spheres and virtually leaving the economies under the mismatching regulatory practices under the sphere of non-cooperation. Cold War ideological confrontation penetrated deep in the RECs and successfully fragmented the regimes of integration realized in the era of first LIEO.

III. Economics of Conversing Theoretical Paradigms

Market Revolution, Washington Consensus, and the Rise of Borderless Global Economy

With the end of the Cold War, the structures created by WWI, Great Depression, and WWII lost their rationale and gave way to the second coming of the LIEO. Following the collapse of Soviet Union and the subsequent end of the paradigmatic clash between capitalism and socialism, a powerful market revolution swept across the globe. From East Europe to China and from Vietnam to newly independent Baltic nations economies started a far-reaching transition to market.[9] These historic events clearly demonstrated that the activist role of state in the economic management is rather damaging. 'Keynesian consensus' lost its supporters and hence replaced by the resurgent 'Washington consensus'.[10] However, in rush to markets, neo-liberal economic reforms in Russia and East Asia also brought misery to millions and raised a question mark before the rigid market orthodoxy. It led 'Washington consensus' to move towards the 'post-Washington consensus'.[11] Thus, the events of the last decade of 20th century proved the inevitability of market system. This powerful market wave created a broad-based paradigmatic convergence, which is increasingly pushing national economies into a borderless single world economy. Globalization of production, distribution, market and investment is creating immense possibilities for the RECs. The economic cooperation in this era is clearly visible in the rising intra-regional trade & investment flows, intra-firm trade, and the hectic cross-border merger and acquisition activities.

Intra-Regional Trade and Investment

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[9] Michael Ellman, "The Political Economy of Transformation", *Oxford Review of Economic Policy*, Vol. 13, No. 2 (1997), pp. 23-32; and Grzegorz Ekiert, "Democratization Processes in East Central Europe: A Theoretical Reconsideration", British Journal of Political Science Vol. 21 (1991), pp. 285-313.

[10] Robert Skidelsky, ed. *End of the Keynesian Era: Essays on the Disintegration of the Keynesian Political Economy*, London: Macmillan, 1977.

[11] Moises Naim, "Washington Consensus or Washington Confusion?" *Foreign Policy*, 118 (Spring 2000), pp. 87-101; Dani Rodrik, *Has Globalization Gone Too Far?* Washington: Institute for International Economics, 1997; and Joseph E. Stiglitz. *Globalization and its Discontents*. New York: Norton, 2002.

The economics of paradigmatic convergence led to the rise of geo-economic considerations. Notion of regional competitiveness started to acquire bigger space in the policy debates than the traditional concept of national competitiveness. This trend created intra-regional trade and investment boom and greatly enhanced economic cooperation between and among the region's economies. European Union, NAFTA, and ASEAN - all are witnessing sharply increased intra-regional trade and investment flows. The European Union is the most highly integrated regional trade area. As shown in the Table 1, in 1980, 57 percent of the total merchandise trade (exports plus imports) of the European Union stayed in the region. This share increased to 66 percent in 1990 but has declined somewhat since then (partly as a result of increased trade with the former Soviet bloc countries).

Following the trend, in 1988, Canada and the United States formed a free trade area that became the North American free trade area (NAFTA) with the inclusion of Mexico in 1994. As the table 1 indicates, trade among the NAFTA countries as a share of their total trade has risen steadily over the last two decades. Similarly, in 1991, Argentina, Brazil, Paraguay, and Uruguay formed the free trade area MERCOSUR, which was later joined by Bolivia and Chile. Around the same time, the Andean group incorporating Bolivia, Columbia, Ecuador, Peru, and Venezuela began a concerted effort to eliminate trade barriers among its member countries. In both areas, the share of regional trade rose sharply in the 1990s after showing little increase during the 1980s.

The association of Southeast Asian nations (ASEAN) (Brunei, Indonesia, Malaysia, Singapore, Thailand, and the Philippines) formed a free trade area in 1992. There was no change in the share of regional trade for the ASEAN countries during the 1980s; however, following the creation of the free trade area, the share of regional trade rose—from 14 percent in 1990 to 18 percent in 1999.

The change in the pattern of Korea's trade also indicates that factors other than free trade agreements are important for increasing regional trade. Korea is not a member of a regional free trade area, yet the share of its trade involving other emerging East Asian countries increased from 10 percent in 1990 to 23 percent in 1999. As with Latin America, this increase in intra-regional trade may have been spurred by an overall reduction in the level of trade barriers, as well as rising income levels in the region.

Table 1: Intra-regional trade as a percent of a region's world trade

	1980	1990	1999
European Union	57	66	61
NAFTA	33	37	47
MERCOSUR	13	14	22
Andean	4	5	10
ASEAN	14	14	18

Source: International Monetary Fund, *Direction of Trade Statistic*s, various years

There has been a proliferation of regional trade agreements (RTAs) worldwide in the 1990s. Within the last 6 years, about 90 agreements covering trade in goods or services, or both, were notified to the WTO. This is a sharp increase compared with the 124 RTA notifications received by GATT (predecessor of WTO) over the 46 years from 1948-1994. As a result of this increase in the number of RTAs, preferential trade increased from 40% of total world trade in the period 1988-1992 to 42% in the period 1993-1997. Western Europe (EU-15) had the highest proportion of preferential trade (70%), but the increase between 1988-1992 and 1993-1997 was small.

The Western Hemisphere (NAFTA and MERCOSUR), on the other hand, experienced significant growth in the proportion of preferential trade, from 19% in 1988-1992 to 27% in 1993-1997. In contrast, only a small proportion of the trade in the Asia Pacific region was preferential trade, and the share had in fact declined from 4% in 1988-1992 to 3% in 1993-1997. This was despite the strong growth of intra- regional trade in Asia Pacific, which rose from 34% in 1985 to 48% in 1995.

In fact, a 1995 study by the WTO Secretariat concluded that regional and multilateral integration initiatives are complements rather than alternatives in the pursuit of more open trade. Regionalism can help to build domestic confidence by first confining market liberalization to member RTA countries. Economies may be more amiable to multilateral trade liberalization after observing the trade creation and investments that regionalism induces. Regionalism would also allow groups of countries to negotiate rules and commitments that go beyond what is possible multilaterally due to the lower bargaining complexities. Thus, this growth in intra-regional trade and investment is not exclusively inward looking but also linked with the global flows of goods, commodities, services and capital.

Intra-Firm Trade and Investment

Intra-regional trade and investment flows have received vigorous support by the growing intra-firm trade. Venables (1999) argues that international fragmentation of production is one aspect of globalization of world economy.[12] This vertical disintegration can be associated to the development of outsourcing through inter-firm relations, leading to an increased share of trade in intermediate goods as described empirically by Feenstra (1998)[13] and explained theoretically by Grossman and Helpman (2002)[14] among others. It can also be associated to a spatial fragmentation with activities remaining within a single firm involving multinationality as described by Venables (1999). The later aspect of fragmentation leads necessarily to the development of intra-firm trade.

Nevertheless, even if it is difficult to measure intra-firm trade due to its nature and the lack of data, some studies assess it's importance regarding total international trade. According to UNCTAD (1996), one third of all international trade occurs within MNCs. In 1993, the share of intra-firm exports by parent firms based in the country and affiliates of foreign firms located in the country in total exports of the country ranges from 38 percent in the case of Sweden to 24 percent in the case of Japan. The corresponding share of intra-firm imports in total country imports ranges from 14 percent in Japan to 43 percent in the United States.[15] Describing French data, Mathieu and Quelennec (1997) found that trade within multinational firms networks

[12] A. J. Venables, "Fragmentation and Multinational Production", *European Economic Review*, Vol. 43, No. 4-6, (1999), pp. 935-945.
[13] R. C. Feenstra, "Integration of Trade and Disintegration of Production in the Global Economy", *Journal of Economic Perspectives*, Vol. 12, No. 4, pp. 31-50.
[14] G.M. Grossman and E. Helpman, Outsourcing in a Global Economy. Mimeo. Harvard University, 2002.
[15] For details, see UNCTAD, *World Investment Report: Investment, Trade and International Policy Arrangements*, United Nations: New York, 1996.

represents more than 35 percent of overall French trade. More than 23 percent of the intra-firm exports of French firms are for use in production.[16]

In reality, broader paradigm convergence leaves crucial areas of policy mismatches in terms of financial structure, trade structure and managerial structure. Thus, a powerful trend among MNCs has been to trade with sister firms or subsidiaries. This way firm doesn't have to deal with certain unknowns in the business. Hence, intra-firm trade accounts for the large part of the international trade.

Cross-border Mergers and Acquisitions

The pressures originating from the globalization and regionaliztion processes are pushing corporations to look beyond the traditional sources of comparative advantage. To achieve the critical economies of scale, to penetrate in crucial markets, and to acquire critical technologies, firms are getting involved in the cross-border M&A activities. M&A activities testify growing closer economic cooperation among and between the involved enterprises, regions, and economies. In the year 2000, Asia alone accounted for US $ 231.9 billion M&A transactions. Table 2 lists the Asian M&A transaction that shows the growing cross-border corporate integration.

Table 2: Cross-border merger and acquisition purchases: Asia Pacific, 1990-1996

Number of deals and value of deals in US$ millions

	Total 1990-1996	
	Deals	Value
Japan	3,178	93,813.371
Hong Kong	650	30,907.742
Australia	584	23,683.622
Malaysia	356	15,439.766
Republic of Korea	337	15,200.842
Singapore	518	11,912.602
China	187	11,810.122
Thailand	128	7,290.200
Taiwan	163	6,976.457
New Zealand	117	4,145.969
Indonesia	76	2,307.838
India	52	1,512.147
Philippines	21	515.190
Brunei	8	470.663
Pakistan	2	107.206

[16] E. Mathieu and M. Quelennec, Industrial Establishment Abroad and Exports, DSTI/EAS/IND/SWP (97) 18, OECD: Paris, 1997.

Vietnam	9	27.060
Bangladesh	1	11.867
Macau	2	10.000
Cambodia	2	7.650
Nepal	1	3.400
Myanmar	2	1.020
Mongolia	1	0.76
Papua New Guinea	2	0
Total	6,392	226,153.71

Source: International Labor Organization

There are diverse explanations pinpointing determinants of M&A transactions.[17] One clear potential determinant is inefficient management in the acquired firm, management, which is not maximizing shareholders' returns and is thus open to a hostile takeover designed to replace the managers. This move is called the market for "corporate control". Another management story explaining M&As is the notion that it is the managers of the acquiring firm (rather than of the acquired firm) who are inefficient, using their power to acquire assets. These acquisition bound managers receive enjoyment from driving their firms larger even when such acquisitions are not to the benefit of the owner shareholders. Many observers suggest that the conglomerate merger wave of the 1970s, a wave that eventually saw most such mergers re-divided, was driven by ambitions of acquiring firms' managers.

Other explanations for M&As exist. One plausible story is that acquirers take advantage of under priced assets in the acquired firm. This story could explain merger waves, since assets could become undervalued across a broad spectrum of companies. A more recent hypothesis is that some M&As occurs in order for management to break contracts (explicit or implicit) with labor, this ability being unavailable to incumbent managers. Apart from these explanations, M&A transactions suggest the cross-border firm level integration, which is one of the indicators of economic cooperation.

The above-mentioned areas of intense economic interaction suggest that paradigmatic convergence can provided sufficient stimulus to broaden the scope, depth and nature of economic cooperation, however with one clear difference; the opportunities of economic cooperation created during the era of first LIEO were enforced by the colonial interests but the economic cooperation during the second LIEO is by choice signaled by the market forces. This difference in the nature of forces that are pushing regimes of economic cooperation can explain the sustainability of present RECs.

IV. The Economics of Converging-Diverging Paradigms
Evidences from Indo-Korean Bilateral Economic Cooperation

Trends in the Indo-Korean bilateral economic cooperation are clearly linked with the economics of converging paradigms. The trade data reveals the fact that economic relations between India and Korea have been primarily shaped by the changes in the contemporary

[17] For details, see L. Waverman, ed., *Corporate Globalization Through Mergers and Acquisitions*, Canada: University of Calgary Press, 1991.

economic thinking, which has witnessed the phase of paradigm divergence as well as convergence. In the history of India-Korea bilateral economic relations, which formally began with the establishment of diplomatic relations in 1973, economic thinking has witnessed a sea change.[18] In the past, theoretical paradigms such as Capitalism vs. Socialism or more recent Keynesianism vs. Monetarism clearly diverged on structural, organizational and operational levels, however in the recent times there are ample evidences showing greater theoretical convergence leading towards the "Post-Washington Consensus" (Stiglitz, 1998, 2002). This changed economic thinking has actively restructured the overall framework of bilateral economic relations, which moved from the lows of 1970s to the highs of 1990s.

It is important to note that the fundamental transformation in the economic thinking came with the three major disjunctions: one, the collapse of centrally-planned economies of communist block; two, end of antagonistic politics of Cold War; and three, the crisis of Fordist model. These developments have raised doubts before the arguments supporting the activist role of state in the market place. Moreover, the stunning advances in the technological front, particularly in the area of information & communication technologies, have accelerated the pace of change. The cumulative impact of forces unleashed by the wider convergence on freer markets paved the way for an unprecedented level of economic integration in the world economy. A new era of globalization and liberalization started to fundamentally alter the established frameworks of production, market and finance. With the rest of other economies, both Indian and Korean economies started to adjust with the changed rules of the global political economy and initiated their own liberalization & deregulation programs.

Furthermore, the removal of dividing wall in Europe, erected by the Cold War superpower rivalry, led to a major realignment in the geo-economic sphere. Regional trade alliances came into fore with Europe leading the charge. Following this general geo-economic trend, Asia too witnessed substantial rise in the intra-Asian trade and investment flows. This explicit rise in the geo-economic considerations affected broader parameters, arguments and policies under which bilateral relations between Korea-India were operating in the past.

Accompanying these broader trends, on the micro level, the loss of India's traditional trade partners following the collapse of Soviet Union made it imperative for India to reorient its external trade. Meanwhile, Korea too witnessed growing trade frictions with the important trading partners such as the US and EC and felt the compelling need to diversify its export market. Hence, with the easing of Cold War super power rivalry, Korea initiated a well-thought policy, popularly known as "nordpolitic", to improve relations with the former communist countries and India articulated "Look East" policy to strike a new balance in its dealing with the regions of East and West.

In the new framework, top Indian policy makers, including the Prime Minister Indira Gandhi, started to admire East Asia's economic success. Rapidly increasing economic weight of East Asia led to the talk of "Asian Century". India favorably responded to these changes by initiating its activist policy to engage nations of East Asia. Korea coming out of colonization, war and national division got particular focus among the Indian policy makers. This fundamental change in the perception of policy planners in both countries provided the basis to construct regimes of substantially increased bilateral economic interaction.

Thus, beginning from the early-1990s, changed economic thinking started to affect economic policies and corporate sector's long-term investment decisions. Reflecting the new

[18] After 11 years of consular relations, India and Korea formally established diplomatic relations in December 1973.

regional calculus, Indo-Korean economic relations moved away from the short-term 'market-seeking approach' followed during the 1960s and 1970s to the long-term 'production-seeking approach' initiated during the 1990s. Korea started to view India not only as long-term market destination but an important base for overseas production that can infuse new blood in the declining combativeness of its fledgling export industries. Korea's big business, namely chaebols, started building large production points in India to produce automobiles, refrigerators, washing machines, air conditioners, TVs and computers sets etc.

To fully understand the economics of converging paradigms, it is also important to briefly review the phase of diverging paradigms, which created structures of constraints under which economic interaction between Korea and India almost stagnated. Thus, the first part of this section discusses the period - 1973 to 1993 - largely dominated by the political logic. During this period, both Korea and India were ideologically aligned with the competing superpower blocs where political calculations dominated over the hard economic realities. This left only a narrow space for the bilateral economic cooperation between India and Korea to flourish. As a close ally of a rival superpower, Korea half-heartedly sought market access in India with largely symbolic investment. This low-key economic interaction has been termed as "constrained cooperation".

The second part of this section closely analyzes post-Cold War period after 1993 when state "roll back" was already engineered with market forces actively shaping the economic outcomes. This was the time when economies of former communist countries, termed as transition economies, initiated experimenting "shock therapy" and "gradualist approach" to adopt market-based systems. By acknowledging this general trend towards market-based systems, India too initiated a far-reaching economic liberalization program aimed at integrating Indian economy with the global economy. Keeping track of Indian developments, Korea in this phase targeted India as one of the destinations to establish production bases to carter domestic as well as overseas market demand. This new approach resulted in the sudden jump of Korea's FDI to India. The economic cooperation under this phase has been termed as "unconstrained cooperation".

Part One
Dominance of Political Logic:
Constrained Cooperation under the Market-seeking Approach

In this phase bilateral economic relations between Korea and India were mostly constrained by the primacy of political logic emanating from the Cold War ideological rivalry. Both India and Korea were aligned with the rival super power camps with distinctly different economic focus: re-distribution under the socialist, public sector dominated economy in case of India and accumulation under the capitalist, private sector dominated economy in case of Korea. These two distinct approaches to development created new type of economic actors that aspired for the differing goals. India's dominant public sector units, operating under the strict import-substitution industrial strategy, were concerned only with the protected domestic market but Korea's diversified business conglomerates, often known as Chaebols, has to perform in the framework of export promotion industrial strategy, and have to face the challenges of global market place. Moreover, the political economy of Cold War created pull and push dynamics that provided Korea a clear advantages in the US and European markets. On the other hand, India's overt import-substitution strategy led economy near to the stagnation level. These developments resulted in the low-key bilateral economic relations between India and Korea.

In the mid-1960s, Korean economy started to feel the dynamic impact of export-led industrialization strategy, whereas Indian economy started to feel the burden of import substitution industrial policies. This divergence in the policy dynamics of both economies resulted in the symbolism than substance in the bilateral economic interaction. In the year 1964 India and Korea signed their first trade agreement, though it did help in initiating the two-way trade but could not lead to any substantial increase in the bilateral trade. Thus, even seven years after the agreement in 1971, the two-way trade was merely US $ 12.4 million. Table 3 confirms nominal economic interaction between the two countries in the most part of the 1970s.

Table 3: Korea's Export-Import to India, 1973~1980

Year	Export	Inc. Rate	Import	Inc. Rate
1973	3	-72.3	12	173.1
1974	5	79.1	22	88.2
1975	7	43.7	39	76.6
1976	11	73.1	34	-13.0
1977	21	79.3	23	-31.8
1978	78	227.8	39	69.9
1979	87	11.9	83	111.4
1980	173	99.0	54	-35.5

Source: Korea International Trade Association (KITA), 2003

The establishment of diplomatic relations between India and Korea in 1973 marks the watershed in the history of bilateral economic cooperation. Just a year after the formal diplomatic relations, both governments agreed to accord each other the Most Favored Nations (MFN) status, which became the guiding framework for bilateral economic relations. With the established set of rules defined by the 1974 Agreement,[19] bilateral trade between India and Korea witnesses a relative increase. It increased to US $ 170 million in 1979. One of the reasons for this increase was probably the renewed agreement of 1974 that replaced the 1964 Agreement (Bhaumik, 1989: 64).

Korea has probably made better use of this Agreement compared to India, because whereas during the first half of the 1970s India enjoyed favorable trade balance vis-à-vis Korea, by 1978 terms of trade became adverse and trade surplus swing to deficit. It turned from US $ 32.4 million in India's favor in 1975 to US$ 38.3 million in Korea's favor in 1978 and two years' later in 1980 India's trade deficit with Korea increased to US $ 119.3 million. In fact, it may be said that increased trade between the two countries during the 1970s was primarily on account of Korea's endeavor.[20] This was the time when Korea's successful export-oriented industrial strategy pushed nation's corporate sector to look for India as the probable market. Between 1971-

[19] In this agreement items available for export and imports were identified and it was sought to maximize trade between the two countries in these items. It was also specified that the goods and commodities exchanged between the two countries should be given the Most Favored Nation (MFN) treatment with respect to taxes and duties to be levied. Similarly, the agreement also sought to encourage technical cooperation between the two countries on the basis of exchange of technical know-how, skilled personnel etc.

[20] T.K Bhaumik, "Indo-Korean Economic Linkages: A Critical Overview," in R.C Sharma, ed., *Korea, India and the Third World*, Rajesh Publications: New Delhi, 1989, pp. 62.

80 while India's exports to Korea increased at the annual rate of 20.8 percent whereas Korea's exports to India increased at the rate of 60.1 percent. Further in 1980s India's exports to Korea declined by 35.6 percent to US $ 53.7 million, but Korea's exports to India increased by 99 percent to US $ 172.9 million. Thus, by the end of 1970s the basic bilateral trade framework between Korea and India was established but the paradigm divergence remained a stumbling bloc.

In the 1980s, India initiated half-hearted, poorly conceptualize economic liberalization program under the Rajiv Gandhi administration, which led to the balance of payment crisis in 1989. In the mean time, Korea witnessed rapid economic expansion and was famously termed as the "Miracle on the Han River." Korean economy grew at the phenomenal pace and started to diversify from the labor-intensive industries to heavy and chemical industries. Korea's rapid industrialization gave birth to a capitalist firm popularly known as 'Chaebol' sitting at the center of diversified, family-owned business conglomeration strategy. During this period, bilateral trade sees many fluctuations. It began to weaken even before it could take any significant shape. The two way trade reached to its peak in 1984, when it reached US $ 1.4 billion or 2.3 percent of Korea's two way trade, but then it began to decline and in 1987 it was only US $ 606 million or about 0.7 percent of Korea's total trade. In the mean time, between 1982 and 1985 Korea succeeded in entering into a few joint ventures programs in India. Between 1982 and 1987 a total of 39 Indo-Korean collaborations were approved, of which 30 were technical collaborations, 5 were financial and 4 were for drawing and designs (Bhaumik, 1989: 77).[21] Table 4 shows the trend in the bilateral trade between Korea and India during the 1980s.

Table 4: Bilateral Trade between India and Korea

(in million US $)

Year	Total Trade	Export	Imports
1981	310	225	85
1982	499	350	149
1983	858	577	301
1984	1,429	1,049	380
1985	683	467	216
1986	639	512	127
1987	606	404	202
1988	635	465	170
1989	932	675	258
1990	718	435	283

Source: Office of Customs Administration, Republic of Korea.

To support, sustain and enhance trade, investment and joint-ventures both countries agreed to establish institutional mechanism. Apart from the Joint Trade Committee (JTC)[22] at the official level, there are two separate forums for brining about greater coordination and interaction between the business communities of the two countries, namely the Korea-India Economic

[21] Ibid, p.77

[22] The third meeting of the JTC was held in New Delhi, India on 9 May 2000. The Indian delegation was led by Murasoli Maran, Minister of Commerce & Industry and the Korean delegation by Dr. Han Duk Soo, Minister of Trade. The Ministers reviewed bilateral economic relations, agreed to expand trade, accelerate Korean investment and strengthen relations in information technology and other areas.

cooperation Committee with the Confederation of Indian Engineering Industries (CEI) as the nodal agency of the Indian side and the Indo-Korean Joint Business Council (JBC) with the Federation of Indian Chambers of Commerce and Industry (FICCI) at the nodal agency from the Indian side. Discussions at business level are held annually in both these forums. In addition, there has always been an interaction between commercial entities of India and Korea such as ITPO & KOTRA, FIEO-AFTAK, EPCS, etc.

The unfolding of 1990s brought the end of Cold War that tilted the balance of economic debate in favor of market-based systems with neo-liberal economic paradigm at the forefront. India initiated a comprehensive structural reform program in 1991 and Korean government launched massive globalization campaign '*segaewha*' and initiated ambitious financial liberalization program. Both economies moved towards a convergence in terms of guiding economic paradigm, which required deeper links with the global economy. This new convergence in economic thinking has thrown open numerous possibilities for investment, trade, market and production.

With the end of the Cold War paradigmatic divergence an important impediment to improve India-Korea relations had been removed. More to the point, that in the 1990s India and Korea had discovered that they had a shared perspective on a wide range of international economic and strategic issues. In the economic sphere, India and Korea could work more closely in organizations such as the IMF, the World Bank and, more importantly, the WTO. At the strategic level, India and Korea ought to have a shared view on the emerging balance of power in Asia. Both countries would like to see a larger role for themselves in the assurance of Asian security, co-operating with the United States, China, Russia, Japan and the ASEAN member countries. India and Korea would jointly propose reforms in the global financial architecture to enable the IMF to deal more effectively with global financial crises. Equally, they had a common stake in ensuring a more transparent functioning of the WTO. A unified Korea would be a major power in Asia with which India could co-operate to ensure peace, security and economic development in Asia.

These mutually beneficial perceptions were highlighted by high-level exchanges between the two countries.[23] In less than two years after being elected to the office of prime minister and in the immediate wake of announcement of major economic reforms P.V. Narasimha Rao paid an official visit to Korea in September 1993; in fact, the first-ever visit of an Indian prime minister to Korea. Hailed by the media in both countries as a significant milestone in the evolution of Korea's deepening of relations with India, the logic and timing of Prime Minister Rao's visit to Seoul underscored the recognition by the both sides of the imperativeness and inevitability of fostering purposive economic relations. The loss of its trade partner following the collapse of Soviet Union made it urgent for India to reorient its external trade, whereas at the same time Korea's dependence on the US market and subsequent trade frictions created the need to diversify export market.

[23] As far back as 1983, P.V. Narasimha Rao visited Seoul as India's Minister of External Affairs. In the same year, Korea's president Chun Doo Hwan was scheduled to visit New Delhi, which subsequently was shelved due to terrorist attack in Myanmar. In March 1986, Korean Prime Minister Lho Shinyong visited India. In the beginning of 1990s, high-level interaction intensified. Korea's Foreign Minister Choi Ho Joong visited in 1990 followed by the speaker of national assembly Park Hyun-Kyu in 1991. In 1992, India's Foreign Minister Madhav Singh Solanki paid an official visit to Seoul. In the same year both countries set up a policy coordinating committee to hold periodic consultations on bilateral and regional issues.

What is more, the evolving political climate in Korea also augured well. It was exactly two years before Rao's official visit to Seoul, Korea became a member of the United Nations.[24] And in the following year, Korea held free and fair elections and returned for the first time in the three decades a civilian president to head the state. Against these new realities in the Korean peninsula, together with far-reaching transformative changes taking in the entire Asia-Pacific region, Rao's journey to Korea was as much politically significant as it was an investment in the future with India's avowed interest in seeking a foothold in the APEC.

While media report suggested that Prime Minister Rao's visit made a significant impression on the Korean government and the business community, admittedly, it signaled the ushering in an era of developing a wide ranging cooperative relationship between the two countries. Although his visit consummated in the signing of three protocols - one on tourism; the second, a cultural exchange protocol and the third, a memorandum of understanding for cooperation in science and technology - the Prime Minister in unequivocal terms underlined the prime objective of his visit: "The Common elements in our positions and approaches to the changing international situation, particularly in Asia, provide many opportunities …to work together for our mutual benefit. A strong and diversified bilateral relationship between us is also an important and positive factor in the Asia-Pacific region".[25]

Prime Minister Rao's appeal to the Korean government and the business community produced the desired results. It appeared as though they were waiting for such an open invitation. For, the very following year, two high-powered technical delegations visited India - one, sponsored by official Korea and the other, a chaebol sponsored delegation represented by the Samsung group. The other, led by Tae Hyuk Hahm, a high-placed economist of the Korean Institute of Foreign Affairs and National Security (IFANS) under the ministry of foreign affairs, an eleven-member delegation comprising of senior officials of the government visited New Delhi in May 1995 and exchanged views with several members of the Union Council of Ministers, officials of the different ministries and the Prime Minister. The range of this discussion was at the same wide and in-depth, including aspects of cooperation in science and technology, utilization of Economic Development Cooperation Fund (EDCF), and trilateral cooperation among Korea, India and other countries of the South and South East Asian region. Echoing the suggestion made by Prime Minister Rao in Seoul the previous year, Hahm pointed out that low labor costs together with the large reservoir of technically qualified people in India could be combined with the sophisticated and labor-intensive technologies from Korea. In respect of the tie-ups between the two countries, he identified particularly such complementary sectors as software development and textile to carter to global markets.[26]

In less than three months, the Samsung sponsored delegation visited India to survey and assess the Indian market for investment opportunities. In its report Samsung delegation pointed

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[24] In 1981, India pioneered its support for the admission of both Koreas - North and South - to the United Nations thereby creating a favorable climate both in G-77 and NAM for other members to join. And, at the UN General Assembly in 1991, India initiated the proposal seeking admission of both Koreas. Recently, India supported South Korea's candidacy for the post of deputy director general of the World Trade Organization (WTO). Also, India voted in favor of South Korea in its bid to become a non-permanent member of the UN Security Council.

[25] Yasmin Javeri Krishan, "Korea-India Economic Relations", *Asia Prashant* (Varanasi), Vol. 2, No. 2 (1995), p. 87.

[26] "Korean Economic Delegation Visits India", *Korean News* (New Delhi), Vol. 22, No. 3, May-June 1994, pp. 8-9.

out importantly the built-in advantages for Korean direct investments such as; 1) large reserve of skilled and easily trainable human resource; 2) low labor cost and cost-effective production process; 3) an increasing large market for industrial products with an estimated consumer base of 250 million people; 4) rapid pace of development requiring capital investment for facilities and equipment; 5) the geographic location of India proximate other South Asian markets; and 6) Korean investments in India could distribute investors' risk by diversifying the sourcing between Indonesia, China, Philippines, Malaysia and India. Also, Samsung report identified the problem areas in respect of Korean investment in India. Among others, it identified factors such as lack of dependable and adequate infrastructural facilities, poor quality of raw materials; bureaucratic hurdles, high levels of local taxes and custom duties together with high interest rates and above all, the rigidity and complexity of the investment and corporate laws governing the private sector.[27]

The finding of theses delegations were revealing for the prospective Korean investors, and in process triggered further discussions between the two countries. No wonder therefore when the President of Korea Kim Young Sam paid an official visit to India in February 1996, among others, he gave priority to two vital agreements with India. One was the Investment Promotion and Protection Agreement between the two countries and the other was the setting up of a joint commission led by the respective foreign ministers of Korea and India to meet once a year.[28] While no protocol was signed, the meeting between two ministers of India and Korea in charge of trade and commerce - Park Jae-yoon and P. Chidambaram discussed issues relating to the lowering of the tariffs and customs on the import of Korea made consumer manufactures. In an effort to bridge the ever-widening trade balance between the two countries the ministers also explored the potentials of enhancing India's export basket to include Indian farm products particularly tropical fruits.[29]

Admittedly, President Kim Young Sam's visit to India not only heralded a new phase in the evolving relations between Korea and India but, more than that, underscored the vital significance of the Indian market for the critical needs of the Korean economy. In fact over the last two decades, especially since Korea adopted the export promotion strategy for its economic development, there has been a discernable shift in Korea's overseas investment which has been concentrating more on Southeast Asia following its earlier focus on US, European Community and Japan. Of late, given the rising labor costs in the ASEAN countries together with region's economic resurgence, Korean overseas investments has bee seeking fresh and fertile new pastures. The obvious and immediate choice was proximate China. Korea invested quite heavily in China but there remains a political concern to concentrate too much on the Chinese market. It is against this background one should assess Korea's surging interest in the Indian sub-continent. As one Indian national news paper in its editorial aptly commented: "Even as the Japanese kept studying Indian economic reforms and the European worried about the political uncertainty, South Korean business [have] decided, with their characteristic risk-preference, to first plunge and then learn to swim in the Indian market."[30]

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[27] Yasmin Javeri Krishan, "Korea-India Economic Relations", *Asia Prashant* (Varanasi), Vol. 2, No. 2, 1995, p.79.

[28] "India and the Republic of Korea: Strengthening the Bonds of Cooperation and Friendship through Economic Reforms and Globalization", Facts for You (New Delhi), Vol. 17, No. 9, March 1996, p. 34.

[29] "Korea-India Agree to Boost Ties, Trade", *Korea News Review* (Seoul), Vol. 25, No. 9 (March 1996), p. 7.

[30] Times of India (New Delhi), 24 February 1996.

Mutual economic gains apart, Korea's meteoric accent in the international stature - having assumed the second high office in the newly set-up WTO, achieving the coveted OECD status, and above all, the diplomatic edge it has secured in the unification process of the divided Korea following the end of Cold War together with decisive economic clout in the Asia-Pacific region - all of which have apparently persuaded India to forge close relations with Korea, more so with its well articulated aspirations to seek a place in the UN Security Council as well as in the APEC.

It should be noted that initially Korea's FDI was driven by a strategy for stable procurement of essential raw materials including crude oil, wood and coal during the early 1980s. Then Korean investors began venturing into foreign countries to sharpen their competitive edge that was softened by an appreciating domestic wage rates as well as by the increasing trade friction with the industrially advanced countries of the European Community and the US. Emerging regional trade blocs too added difficulties to the flow of Korean overseas investment. It is in these circumstances, Korea's FDI shifted to ASEAN and China especially in the labor-intensive manufacturing sectors. Against the huge flow of Korean capital investment overseas, India's share by all reckoning was only marginal during the most of 1990s. According to Bank of Korea, total actual investment in India as of mid-1994 stood at US $ 9,496,000 distributed into about 30 projects. Table 5-A and 5-B show the actual size of investment done by Korean enterprises in India during the 1982-94.

Table 5-A: Korean Investment in India, 1983-1992

Name of J/V Company	Date of Permission	Item	As on June 30, 1994 Unit: US $ 1,000 Approved Equity Amount	
LVT. & Dong In Pvt.	27.05.83	Stone Good	40	120
Daeshin Denken (India)	22.12.87	Elec. Part	25	60
Chanamama Toytronyx	11.02.88	Elec. Toy	30	24
Disco Stone Indo Ltd.	31.05.89	Grave Stone	100	3600
Hyundai Indo Stone	16.11.89	Minerals	-	667
Jark Needle Mfg. Co.	22.12.89	Needle	25	156
Indo-Korea Granite	26.03.90	Stone	60	210
Samwoo-Vasavi Swabs	31.12.90	Needle	30	50
Cheil Indoa Wool Text	07.04.91	Textile	-	1250
Fishing Falcons Ltd.	11.01.91	Fishery	40	1029
Mijura Stone (P)	31.01.91	Stone Process	50	42
Shin-A Chemical (Ind)	04.05.91	Resin	21	288
Gujrat Themis Biosyn	02.03.92	Petrochemical	34.2	1000

Source: Bank of Korea quoted in Krishan (1995) Continued………

Table 5-B: Korean Investment in India, 1992-94

Name of J/V Company	Date of Permission	Item	As on June 30, 1994 Unit: US $ 1,000 Approved Equity Amount

Hanil Era Textiles	03.04.92	Textile	15	1900
Karan Woo Sin Ltd.	22.10.92	Socks	20.4	351
Mardia Samyoung Capital	11.11.92	Antena & Elec.	25	710
Buoy Dae Fishery	16.12.92	Fishery	51	15
Montana Intl Ltd.	31.12.92	Nonmetal Goods	7	200
Shin-A Chemical Pvt.	16.03.93	Petrochemical	-	91
Korin Hair Processing	19.05.93	Human Hair	100	200
Advanced Lightening	18.06.93	Halogen Lamp	50	250
Chang Yun India Ltd.	23.11.93	Auto Parts	49	147
TDT Copper Ltd.	27.12.93	Copper	36	1940
DCM Hyundai Ltd.	29.12.93	Container	37.5	1500
Tai Chonbang Textile	27.01.94	Textile	28	994
Samcor Glass Ltd.	31.01.94	Nonmetal	5	1350
Daeyu Continental Ltd.	01.02.94	Textile	20	161.29
Ellyoung Metal Prdts.	22.02.94	Assy, Nonmetal	50	320
Gujrat Themis Biosyn	01.02.94	Textile	398	469
Indocount Choongnam	27.05.94	Textile	50	3500

Source: Bank of Korea quoted in Krishan (1995)

Of this, investments that were made in the period preceding India's economic liberalization were fractional and were largely confined to trading activities. However, since liberalization Korean approvals of investments increased both in value and volume of projects. Majority of these approvals were in labor-intensive sector. Apart from labor-intensive production, Korean companies have since recently ventured into areas opened up after liberalization including electronics, textile, automobiles, telecommunications, financial services, shipbuilding etc. Although in the past several small and medium-sized Korean companies were setting up joint ventures in such manufactures as halogen lamps, cordless phones, pharmaceuticals, textiles and granite processing, since 1993 major Korean companies (Cheabol) are competing to invest in sectors such as infrastructure including power generation, highway construction, telecommunications, port development and other industrial sectors like cement and fertilizer and heavy and chemical industry, sectors hitherto reserved for India's public sector.

Second part of this section delves into the period (1993-2003) when economics of paradigm convergence becomes operative and starts to shape economic relations. This leads to a new era of ‘unconstrained cooperation’ between Korea and India.

Part Two
Dominance of Economic Logic:
Unconstrained Cooperation Under the Production-seeking Phase

With the arrival of early-1990s, the pendulum of economic thinking swings away from the primacy of 'political logic' to 'economic logic'. The failure of communism as a viable economic ideology provided momentum to the market-based economic regimes around the world. Keeping pace with the trend, the Government of India (GOI) in 1991, initiated a comprehensive structural economic reform program aimed at installing a liberal economic regime.[31] The GOI has placed before the Parliament on July 24, 1991 a Statement on Industrial Policy with the major objectives of removing the bottlenecks in obtaining various approvals by entrepreneurs in making foreign investment policy more attractive and in doing away with the detailed examination by various agencies. A major component of these changes consist of a much greater degree of openness to foreign investment and foreign technology agreements, compared to the past.

By acknowledging the fundamental realignment in economic thinking, the Government of Korea (GOK) also framed a new economic agenda centered on financial system's deregulation and liberalization. In the early 1990s, GOK embarked on a program of financial liberalization, however without simultaneously strengthening prudential standards. In a financial system, where big business was facing very high debt to equity ratios and sharply falling profitability rates, fast-track liberalization came as a destabilizing factor.[32] According to some experts, this led to a full-scale financial crisis in 1997.[33]

Nevertheless, forces unleashed by the liberal economic thought provided a stable ground for paradigm convergence and resultant enhanced bilateral economic cooperation. In the deregulated financial regime corporate Korea was much freer to borrow and invest. First time, many Korean companies started to consider India as a production hub to carter the growing demand for their expanding export industries. These include Daewoo, Hyundai, Samsung, LG, Ssangyong, Hanil, Exim Bank of Korea, Korea Telecom, Daelim, Dongbu, Korea Development Bank, Hyosung, Daecom, Hanwha, TDT, etc. India's national body for small-scale industries, NSIC signed an agreement in July 1995 with the Korean Small and Medium Industries Promotion Corporation (SMIPC) for encouraging cooperation at the SME (Small and Medium Enterprises) level. Under the aegis of the agreement, an SME Investment Seminar was held in Seoul in September 1995. A South Korean SME delegation visited India in March 1996. In line with these interactions, approval of Korean investment in India has risen from US $ 70 million in 1995 to over US $ 860 million in 1999. Table 6: shows year-wise approval of Korean investment.

Table 6: Foreign Direct Investment Approved

Year (Jan-Dec)	Amount in Million Dollars		Percentage of ROK with total investment
	With ROK	With all countries	
1991	2.5	218.3	1.16
1992	15.1	1485.5	0.10
1993	9.6	2890.5	0.33
1994	34.1	4522.5	0.75
1995	100.1	10213.9	0.98
1996	936.6	10510.9	8.91
1997	543.3	15302.9	3.56

[31] For the latest details about Indian economic reforms, see Anne O. Krueger. ed., *Economic Policy Reforms and the Indian Economy*, New Delhi: Oxford University Press, 2002.
[32] In 1996, 20 of the largest 30 chaebols showed a rate of return below the cost of capital.
[33] There are sharp opinion differences to view the 1997 financial crisis. However, one school accepts uncoordinated, rapid financial liberalization as the prime cause of crisis.

1998	93.3	7800.9	1.20
1999	859.6	5665.6	15.17
Total	2,596.2	58,611.0	4.70

Source: Indian Embassy Seoul

Since 1995, Korean investment increased remarkably and Korea's total cumulative investment in India as per FDI approvals rose from a mere US$ 2.5 millions in 1991 to US$ 2.63 billions in 2002 making it the fifth largest investor in India after the U.S., Mauritius, U.K., and Japan, which is about 4% of its total FDI. Daewoo Group was the first to initiate a major investment in India by acquiring dominant equity stakes in the Daewoo-DCM facility in Uttar Pradesh, India. Confirming Korea commitment to the Indian market, Daewoo motors invested more than a billion dollars to expand production facility. Korean commitment to strengthen Indo-Korean ties is further reflected in Hyundai Motor's decision to set up a 100% subsidiary with integrated manufacturing facilities, unlike the CKD (completely knocked down) Assembly Operations by most other manufacturers. This subsidiary has brought in manufacturing and engineering expertise of world-class standards. Hyundai has achieved 80% indigenization level.

Among the numerous Korean investors, LG Electronics and Chemicals has invested US$ 100 million while the Samsung group has made an investment of over US$ 50 million in production facilities of white and brown consumer goods for the Indian market. Hyundai Construction & Engineering Corporation is in the middle of constructing a huge Techno Park in Chennai city. Its big power plant project in the Mangalore and Goa area is also progressing well. In Andhra Pradesh Korea Heavy Industries Ltd is constructing the Kondapally Thermal Power Plant and LG Polymer India Ltd. is operating a chemical plant in the port of Vishakapatnam. LG Telecommunications Ltd is currently trying to make inroads in the Indian telecom industry with attention to the Hyderabad area. It has contract with the mobile handsets with the Reliance Infocom. The Indian Silicon Valley housed in the state of Karnataka is definitely being a fertile place for 'hybrid' sharing of technology, information and expertise with Korea. In Bangalore, the foundation for such a partnership has already been laid by the establishment of research centers by both LG Soft India and Samsung Soft India

With the cutting edge in the field of construction, some of the Korean companies are involved in development projects such as highways, power plants, chemicals, petrochemicals and metro rail projects in India. Furthermore, Korea and India have also close relationship in the field of shipbuilding and energy exploitation. Korean companies like Hyundai Heavy Industry, Daewoo Shipbuilding Marine & Engineering, and Samsung Heavy Industry have contributed to the development of offshore plant project and supplied various vessels such as oil tanker carriers, cargo-ships and LNG carriers. Korea's long-term commitment to India signals Korea's move away from the past market-seeking short-term approach to the production-seeking approach.

Annual two-way trade also reflects this transformed economic relationship. The annual two-way trade volume between the two countries was recorded 2.6 billion dollars in the year 2002. Korea's trade volume with India recorded 0.84% of its total trade in the year 2002, whereas India's trade with Korea posted 2.2% of its total trade in the fiscal year 2001-02. Korean companies like LG, Samsung and Hyundai are now household names in India. Table 7-A, 7-B and 7-C show recent spurt in trade between India and Korea.

Table 7-A: India-ROK Trade

Exports by India (All figures in US $ million)

HS Code	Major Items	Jan-June 2001	Jan-June 2002	Growth (%)
27	Mineral fuels/oil and distillation	123.475	161.573	30.85
23	Oil cake	76.077	118.417	55.65
52	Cotton	106.281	109.595	3.02
26	Iron Ore	56.348	52.611	-6.63
29	Organic Chemical	44.675	48.739	9.10
10	Cereals	34.478	21.919	-36.43
72	Iron and Steel	28.141	17.932	-36.28
84	Machinery & Mechanical Appliances	11.983	17.199	43.53
	Others	115.649	676.092	13.23

Source: Indian Export Bulletin, 2002
Korean Statistics (Imported FOB basis, Exports on CIF basis).

Table 7-B: India-ROK Trade

Export-Import by India (All figures in US $ million)

Year/Months	2000	2001	Jan-Jun 2001	Jan-Jun 2002	Growth (%)
Export	984.705	1105.631	597.107	676.092	13.23
Import	1,326.165	1,407.728	783.832	621.614	-20.70
Total	2,310.870	2513.359	1,380.939	1,297.706	-6.03
Trade Deficit	-341.460	-302.097	-186.725	54.478	129.18

Source: Indian Export Bulletin, 2002
Korean Statistics (Imported FOB basis, Exports on CIF basis).

Table 7-C: India-ROK Trade

Imports by India (All figures in US $ million)

HS Code	Major Items	Jan-June 2001	Jan-June 2002	Growth (%)
84	Machinery & Mechanical Appliances	120.692	122.982	1.90
85	Electrical Machinery & Equipment	170.665	106.147	-37.80
87	Vehicles, Railway or Tramway	46.137	60.513	31.16
39	Plastics/Rubber and Articles thereof	33.605	37.860	12.66
89	Ships, boats and floating structures	146.569	37.253	-74.58
72	Iron & Steel	36.372	28.370	-22.00
29	Organic Chemicals	36.372	26.461	-27.25
54	Man-made Filaments	29.980	26.287	-12.32
	Others	163.440	175.742	7.53
	Total	783.832	621.614	-20.70

Source: Indian Export Bulletin, 2002; Korean Statistics (Imported FOB basis, Exports on CIF basis).

However, a lot has to be done to accomplish a trade expansion of US$ 5 billion within the next few years, the target which was set by an Agreement at the Summit Meeting in 1996. The following projects of different business groups are illustrative of the depth of Korea-India economic interaction.[34]

Daewoo:[35] The Group has signed an Agreement with the Madhya Pradesh Government for a 2 x 500 MW Coal Fired Power Station in Korba. They have also reached an Agreement with M/s Anchor for manufacture of electrical appliances in Goa. Their automobile plant is already in operation and they are planning a collaborative venture in auto components so as to indigenize the manufacture of the car and also to make the Indian operations a center for export of auto components to their operations elsewhere in the world. A tie-up between Daewoo Precision and Ricco Auto Industries for production of shock absorbers, oil pumps and air conditioner switches in NOIDA has been finalized. Daewoo Securities is already a participant in a joint venture for non-banking financial services. Daewoo Corporation also has the proposals to extend operations to the areas of petroleum, aluminum and other non-ferrous metals.

Hyundai: The Group has set up a plant in Tamil Nadu for manufacturing of automobiles. Hyundai Engineering and Construction is engaged in a dialogue for participation in a power project in West Bengal and have also announced interest in construction of a hydel project and the Kanyamkulam Thermal Project in Kerala. The Group has already set up a unit in Madras with DCM for manufacture and export of containers.

Samsung: This Group, which is leader in the area of electronics, has already collaborated with Korea Telecom to provide radio-paging services in a number of cities in India. They are establishing a holding company to engage in a diverse range of activities including electronics, telecom, computers, software, etc., They have also tied up with a Delhi based computer company for manufacturing of color televisions in which they have a 51% equity holding. For telecom equipment production, a JV with L & T has been established.

LG: LG Electronics have established a joint venture with Bestavision for manufacture of color TVs, audio and video equipments in Haryana. They also have an existing collaboration in Madhya Pradesh for manufacture of picture tubes. They have set up a software research centre in Bangalore and a Home Appliance Complex with the Birla Group.

SsanYong: The Group has an existing investment for manufacturing of PTA with the AEC Group. They are having discussions with Indian companies for investments in the power and aluminum sectors and entry in the four wheel drive automobile segment.

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[34] The details in this section are primarily based on the details provided by the Indian Ministry of Foreign Affairs website. Plans, strategies and partners in the area of joint-ventures are constantly changing.

[35] The parent company of the Daewoo subsidiaries in India, Daewoo Group has been declared bankrupt. Daewoo Motors has been sold to the General Motors of USA. Many of Daewoo subsidiaries have been taken over by the creditors. This unprecedented situation may change, alter or scrap many of Daewoo plans in India.

The above list is only indicative of the interest that Korean companies are now showing in India and represents activities of the major Groups. Other groups are also taking up projects in India such as KOHAP (Polyester fiber), Kia (automobiles), Hanjung (Petroleum Refinery), Korea Heavy Industries (Power), Dooray (Aluminum Wheels), etc. Small and medium Korean companies are also very active and inflow of investments can be expected to increase substantially in the 21st century. Interest in economic cooperation with India is also reflected in sectors for which Agreements/MoUs have been finalized.

Textiles: Considerable interest is being shown by the Korean textile industry for investment in India. At a fair in Seoul in November 1995, India was identified as a target destination for investment in Yarn, Fabrics and garments. The Korean Federation of Textiles Industry (KOFOTI) has proposed signing of a MoU for cooperation with Indian industry.

Electronics: The National Association of Software and Service Companies (NASSCOM) have signed a Protocol with the Federation of Korean Information Industries (FKII) for cooperation between the IT industries of the two counties. The Protocol envisages Cooperation through exchange of trade missions, joint surveys, research projects and seminars. The two Associations would also exchange their own periodicals, research & survey reports and establish a Joint Council for Promoting the Cooperation which would be composed of the representatives of not only IT companies but also related research institutes and academic organizations.

Power: The Korean Utility Organization, Korea Electric Power Corporation (KEPCO) is interested both in investing in a power project as well as to take over the management of existing utilities in India. President of KEPCO visited India in this connection and discussed the possibility of taking on a Greenfield thermal project and management of DVC. A technical team has also visited to follow this up.

Finance: The Korea EXIM Bank already has a representative office in India and Cho Hung Bank has begun its operations in Bombay in May 1996. In addition, the Hanil Bank, Korea First Bank, Bank of Seoul and commercial Bank of Korea have been accorded permission by the Korean Government to set up their branch offices in India. The increasing thrust of Korean Banks wishing to enter the Indian market is based on their assessment of increased volume of trade and more particularly Korean investment in India. They hope to corner the major share of the business on the basis of their on-going association with the leading Korean chaebols. Korea Development Bank, a term lending institution, has inaugurated its Representative Office in Delhi in 1996.

V. Policy Lessons

By taking the advantage of existing wider paradigmatic convergence, India and Korea have the historic opportunity to construct the RECs that can transcendent remnants of Cold War era structural barriers. Analysis in this paper points to the fact that there should be a proactive policy framework, which can enhance institutional infrastructure with clear policy targets. Following policy lessons can be implemented in the bilateral/ or multilaterally framework:

- To realize the full potential between the two economies, there is need to evolve a pragmatic policy that can conclude India-Korea Free Trade Agreement. India's edge in the service sector and Korea's comparative edge in the manufacturing sector makes both economies a fit case to sign FTA. This will result in a win-win situation for both economies.

- Both countries should cooperate to go for structured dialogue for the creation of a <u>Custom Union</u>. Other regional economies can also take part in this framework.
- It is important to note that already there are Asia-wide move to create Asian Economic Community. Indo-Korean regime of economic cooperation can positively contribute in the evolving Asian economic order. Both economies can also work towards the eventual <u>Asian Economic Union.</u>

To achieve these stated goals, governments in both countries should formulate the policy to have creative vision that can facilitate higher level of economic cooperation. Before global political economic and strategic interests start to alter paradigmatic convergence, India and Korea must create facilitating institutional structure that can bring visionaries, regional experts and policy makers at one platform.

VI. Concluding Remarks

The analysis in this paper confirms the basic assumption that the economics of CTPs deeply affects the RECs. This paper concludes that the script of economic interaction has always been played on agreed economic frameworks. It highlights that the diverging economic paradigms create dissimilar regulatory structure and pushes economic cooperation to takes a back seat. During the Cold War period, diverging system paradigms based on the capitalist-socialist dichotomy led to the fragmentation of RECs.

It argues that a new economic dynamics begins with the end of Cold War era capitalist-socialist dichotomy when mainstream economic thinking started to converge around 'Washington Consensus'. This led to an unprecedented market revolution transforming the economies of former communist bloc. Not only transition economies adopted market-based system but also many other economies started to rethink the role of state in the market place. Termed as second LIEO, the neo-liberal revolution paved the way for a single world economy and with it new economic order transformed the regimes of economic cooperation.

Indo-Korea trade data supports the basic assumption of this paper that paradigmatic convergence positively affects bilateral/ or multilateral economic cooperation. Bilateral economic cooperation between India and Korea before 1990s confirms that dissimilar regulatory structures based on the paradigm divergence adversely affected bilateral economic interaction. On the other hand, converging economic paradigms create matching regulatory structures conducive for increased bilateral economic cooperation. Indo-Korean bilateral economic cooperation after 1990s confirms this assumption.

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